WACHOVIA
ECONOMICS GROUP

Weekly Economic & Financial Commentary

June 26, 2009

U.S. Review

Clawing Our Way Back

We have often noted the road to recovery would be long and arduous. The most recent batch of economic data supports that notion. Better news in one area continues to be tempered by setbacks elsewhere. This week's pleasant surprise was durable goods orders, which showed more strength and breadth than expected. That gain was offset by mixed data on home sales and a rebound in unemployment claims.

We still expect the recession will end this summer. Second quarter real GDP likely declined at close to a 3 percent annual rate, with most of that drop coming from a plunge in inventories. Third quarter real GDP is expected to rise solidly, with a rebound in motor vehicle production and slight improvement in consumer spending providing much of the boost to output. The largest boost to third quarter GDP, however, will come from a reduced pace of inventory liquidations.

Sales of existing homes rose 2.4 percent, while sales of new homes fell 0.6 percent in May. Sales have stabilized recently and look as though they have bottomed. Even the hardest hit areas of the country are noting some improvement.

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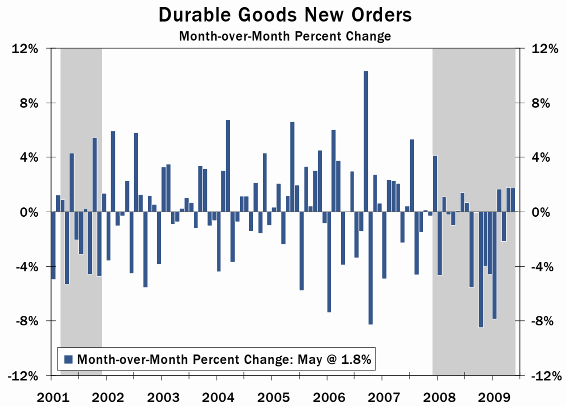

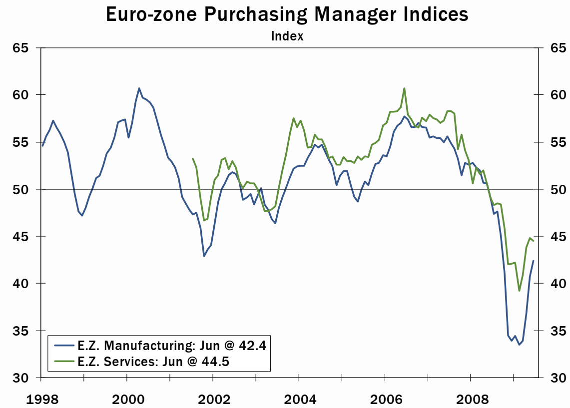

Global Review

Signs of Global Stabilization

Over the last several weeks, economic developments around the world have shown that the freefall in activity that followed the financial crisis last fall is showing signs of moderation. This week was no exception and purchasing managers in the Euro-zone are beginning to take heart that the worst of this global recession may finally be in the rearview mirror. While the early "flash" readings of Euro-zone Purchasing Manager Indices (PMIs) for June showed a small down-tick for the services component, it also registered a substantial improvement for manufacturing. The composite index for all industries rose to 44.4 from 44.0. This is still below the key "50" level which means the current conditions are still reflective of a period of contraction. It is the highest reading, however, since last September (before the Lehman bankruptcy) and suggests that the

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Recent Special Commentary

Date	Title	Authors
June-25	Recession Probability Drops Again—This Time to 37 Percent	Silvia & Iqbal
June-19	Labor Market Evolution: Realities and Romantics	Silvia, York & Whelan
June-18	What Drives Consumer Delinquency Rates?	Vitner & Iqbal
June-18	Personal Income Fell Accross Much of the Country	Vitner

U.S. Forecast

	Actual				Forecast				Actual				Forecast	
	2008				2009				2005	2006	2007	2008	2009	2010
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q						
Real Gross Domestic Product [1]	0.9	2.8	-0.5	-6.3	-5.7	-3.4	2.9	2.1	2.9	2.8	2.0	1.1	-2.7	2.1
Personal Consumption	0.9	1.2	-3.8	-4.3	1.5	-1.0	1.7	1.9	3.0	3.0	2.8	0.2	-0.7	1.4
Inflation Indicators [2]														
"Core" PCE Deflator	2.2	2.3	2.3	1.9	1.8	1.7	1.2	1.0	2.1	2.3	2.2	2.2	1.4	0.9
Consumer Price Index	4.2	4.3	5.2	1.5	-0.2	-1.3	-2.6	-0.3	3.4	3.2	2.9	3.8	-1.1	1.1
Industrial Production [1]	0.2	-4.6	-9.0	-12.9	-19.2	-15.5	2.0	2.9	3.3	2.3	1.5	-2.2	-11.4	1.1
Corporate Profits Before Taxes [2]	-1.5	-8.3	-9.2	-21.5	-18.0	-16.0	-12.0	-8.0	17.6	15.2	-1.6	-10.1	-13.8	5.8
Trade Weighted Dollar Index [3]	70.3	71.0	76.1	79.4	82.5	80.0	82.6	85.0	86.0	81.5	73.3	79.4	85.0	85.0
Unemployment Rate	4.9	5.4	6.1	6.9	8.1	9.3	9.9	10.3	5.1	4.6	4.6	5.8	9.4	10.6
Housing Starts [4]	1.06	1.02	0.87	0.66	0.53	0.47	0.51	0.55	2.07	1.81	1.34	0.90	0.51	0.74
Quarter-End Interest Rates														
Federal Funds Target Rate	2.25	2.00	2.00	0.25	0.25	0.25	0.25	0.25	4.25	5.25	4.25	0.25	0.25	0.50
10 Year Note	3.45	3.99	3.85	2.25	2.71	3.80	3.80	3.80	4.39	4.71	4.04	2.25	3.80	4.20

Data As of: June 10, 2009
[1] Compound Annual Growth Rate Quarter-over-Quarter
[2] Year-over-Year Percentage Change
[3] Federal Reserve Major Currency Index, 1973=100 - Quarter End
[4] Millions of Units

Inside

U.S. Review

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Excesses are Gradually Being Eliminated

Even though new homes sales declined 0.6 percent, excesses are being cleared out of the market. Construction has pulled back even more than sales, which has led to a steady decline in inventories. Inventories of unsold homes have fallen by 161,000 over the past year and are now back near the lows seen in the late 1990s, which was before the housing boom began. Of course, there are still plenty of nearly new homes in existing home inventories. Many of these homes have never been lived in and are giving builders stiff competition for the few buyers that are in the market right now.

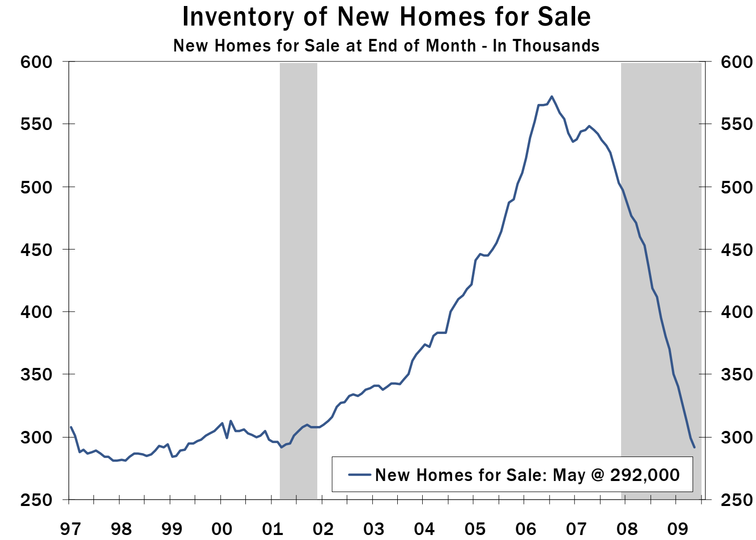
Personal income jumped 1.4 percent and after-tax income rose 1.6 percent. Disposable income was boosted significantly by the American Recovery and Reinvestment Act. Consumer spending rose 0.3 percent in May. The gain was slightly less after adjusting for higher inflation, with real personal consumption expenditures rising 0.2 percent. That gain follows declines during the previous two months. Real personal consumption outlays are currently running at a 0.5 percent annual rate below its first quarter pace. Even if spending rises by another 0.2 percent in June, the second quarter will still see a slight decline in real consumer outlays. Another gain, however, would set the third quarter up for a solid increase and bolster our forecast for third quarter real GDP growth.

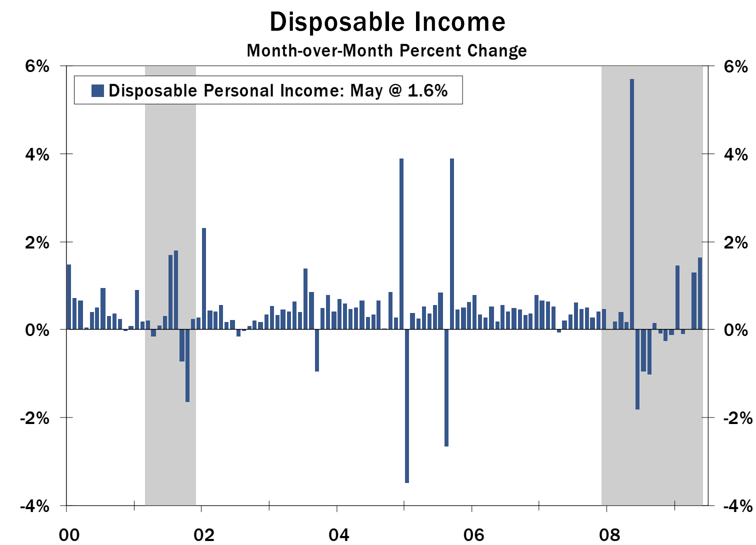
The weekly first-time unemployment claims data continue to be the most important real-time information we get on the economy. This past week saw initial claims rise a surprising 15,000 to 627,000 and the previous week's number was revised up by 4,000. The closely watched four-week moving average and continuing claims also increased. In addition, several states noted that education services accounted for a large portion of recent claims. That last note caused many folks to downplay the increase. The layoffs, however, reflect serious financial strains at private schools, colleges and universities and public schools. These layoffs are real and present a growing threat to the recovery.

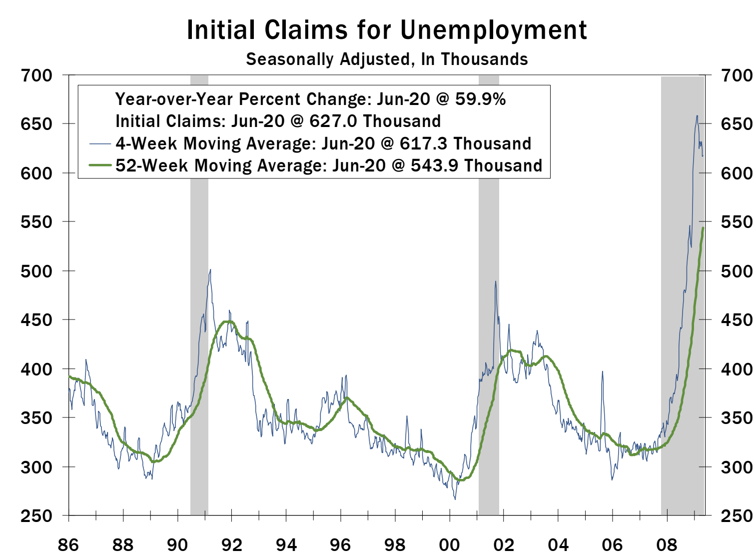
The jobless claims data provide us with much of the information needed to estimate nonfarm employment and the unemployment rate. We expect nonfarm payrolls declined by around 420,000 jobs in June, while the unemployment rate likely rose to 9.6 percent. Labor force growth will have more influence on the unemployment rate over the next few months, as recent college graduates join the workforce and teenagers and college students search for summertime jobs. The annual influx often leads to wide swings in the employment and unemployment data, particularly when we are around key turning points in the business cycle.

Selected Current Data

Gross Domestic Product - CAGR	Q1 - 2009	-5.5%
GDP Year-over-Year	Q1 - 2009	-2.5%
Personal Consumption	Q1 - 2009	1.4%
Business Fixed Investment	Q1 - 2009	-37.3%
Consumer Price Index	May - 2009	-1.3%
"Core" CPI	May - 2009	1.8%
"Core" PCE Deflator	April - 2009	1.9%
Industrial Production	May - 2009	-13.4%
Unemployment	May - 2009	9.4%
Federal Funds Target Rate	Jun - 26	0.25%







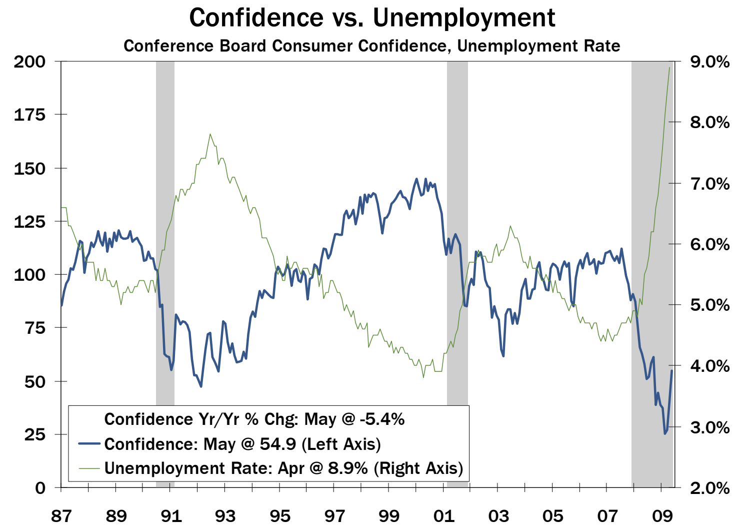
Consumer Confidence • Tuesday

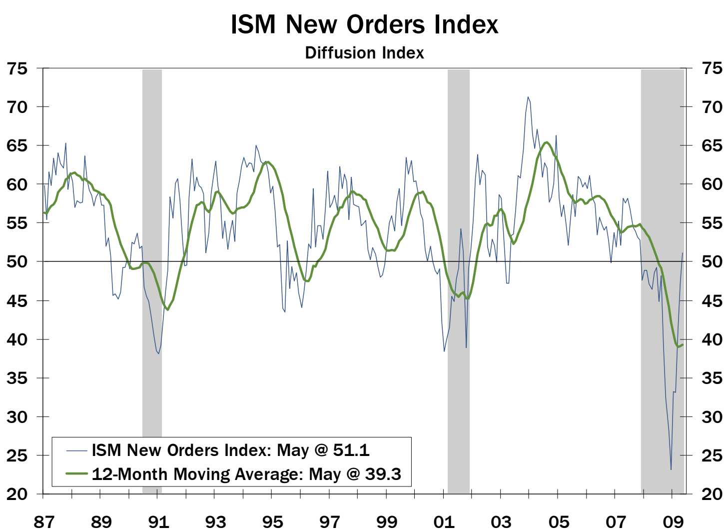
Primarily lifted by increasing expectations that the end of the recession is likely coming to an end sometime in the second half of this year, consumer confidence has more than doubled from the record low set in February.

While we are calling for economic growth, and thus an end to the recession, to resume in the third quarter, we believe there will be a slight pullback in consumer confidence for the month of June. Stock prices are slightly higher, on average, when compared to May but have cleared slowed. Gasoline prices, while well below last year's level, continue to climb as we enter the summer driving season. Lastly, the unemployment rate continues to rise towards double-digit levels as job creation in many industries remains scarce.

Previous: 54.9 **Wachovia: 49.5**

Consensus: 55.2





ISM Manufacturing Index • Wednesday

The Institute for Supply Management's headline manufacturing index rose to an 8-month high in May signaling that the prolonged contraction in the factory sector could be coming to an end in the not too distant future. Much of that optimism comes from the forward-looking new orders index which jumped above the expansion/contraction line to 51.1 in May – marking the first time it has crossed into expansionary territory since November 2007.

We believe the recent upward momentum in the headline index should continue in June as several regional purchasing managers' indices, notably the Philadelphia and Richmond indices, have shown significant improvement. As always, the employment index will be closely watched and should register a modest gain with manufacturing activity beginning to bounce off recessionary lows.

Previous: 42.8 **Wachovia: 43.5**

Consensus: 44.0

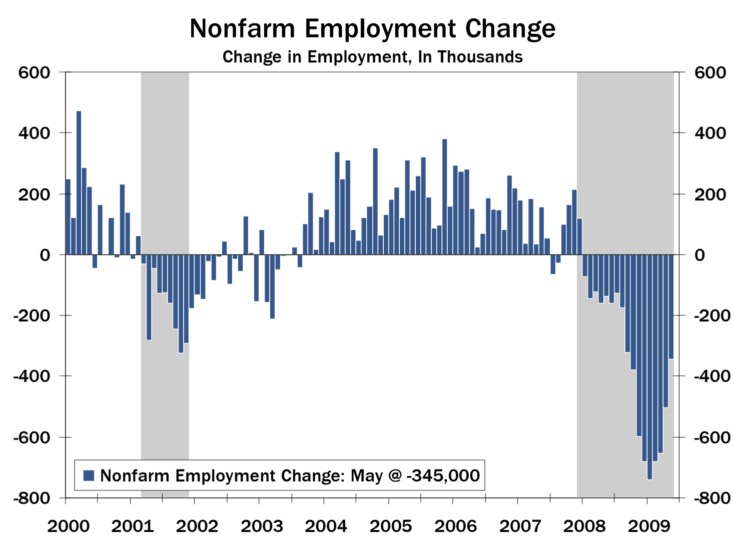
Employment Report • Friday

Despite the decreasing nonfarm job losses over the past few months, firms are still cutting workers at an uncomfortably elevated pace. We expect to see a modest pullback in June with nonfarm payrolls declining around 400K. If realized, job losses in the second quarter (at a -416K average) would be significantly lower than the first quarter (-691K average) confirming recent signs of stabilization we have seen in the broader economy. Reflecting that optimism is the recent improvement in temporary help. Temporary help employment, which has historically been a leading indicator of improvement in the labor market, fell only 7K in May versus an average decline of 62K over the past three months.

The unemployment rate should continue to drift higher, albeit at a slower pace than we have seen over the past 6 months. Our call is for a two-tenths percentage point increase to 9.6 percent. Unfortunately double-digit unemployment is not too far away.

Previous: -345K **Wachovia: -400K**

Consensus: -370K



Global Review

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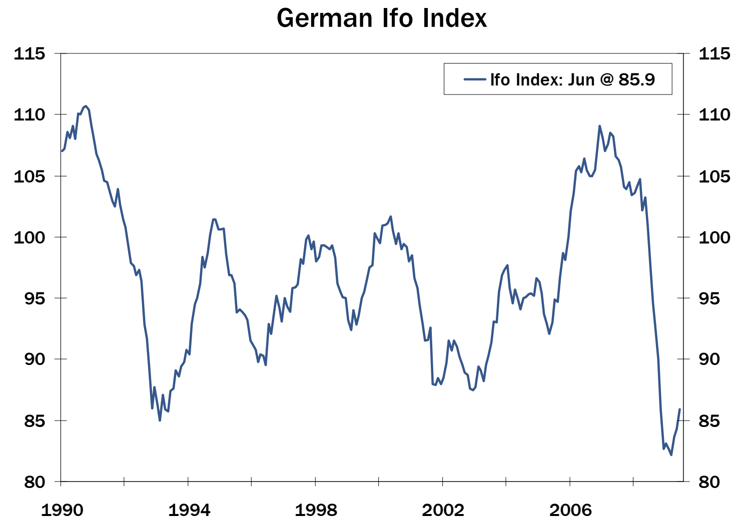
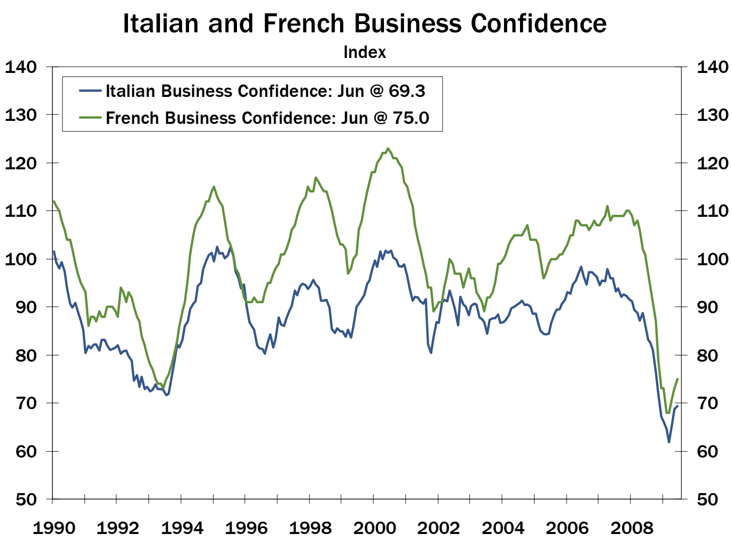
Sentiment is Improving as Global Recession Loses Steam

Euro-zone is now contracting at slower pace and the economy is stabilizing. We estimate that real GDP in the Euro-zone contracted at roughly a four percent annualized rate in the second quarter, which is not quite as bad as the 9.5 percent drop registered in the first quarter. While growth may remain slightly negative in the third quarter, real GDP should start to grow again, albeit at a sluggish pace later this year. Other measures of business sentiment corroborate the story of improvement in the economic picture. In Germany, the Ifo index—a key yardstick for business confidence—improved for the third straight month. While German businesses did not note any improvement in their current assessment, expectations for business performance in the next six months jumped to 89.6, the highest reading since last summer.

French business confidence also increased for the third-straight month in June. President Sarkozy recently announced a roughly €30B stimulus package which includes tax cuts and spending projects to help lift France out of recession. Businesses are not the only ones feeling encouraged; French consumer sentiment also increased in June, marking the fourth consecutive month of improvement for that series. Consumer sentiment is now the highest it has been since March of last year. There is a growing outlook that this global recession is losing steam. Italian business sentiment is also improving, but a recent report suggests that rising unemployment is keeping a lid on wage growth.

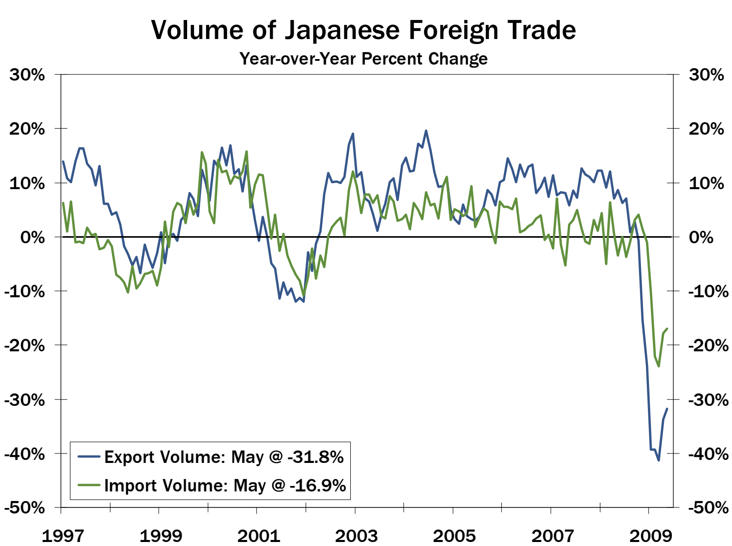
Domestic demand is also weak in Japan, where data released this week showed further contraction in imports. May imports fell 3.6 percent. The trade balance showed a ¥222B surplus in May, the second monthly increase. Exports to the U.S. market and Europe continued to decline as did exports to the rest of Asia. While Japan's May exports fell in nominal terms on a seasonally adjusted basis, on a volume basis they actually showed growth. Real export volumes rose a seasonally adjusted 1.8 percent for the month of May after a 1.0 percent gain in April. The current global recession has been as challenging in Japan as it has been anywhere in the world. These recent improvements in export volumes are welcome developments for Japan, where foreign trade is critically important to the health of the overall economy.





Selected Global Data

Japan	GDP Year-over-Year	Q1 - 2009	-8.8%
	CPI	May - 2009	-1.1%
	Unemployment	April - 2009	5.0%
	BoJ Target Rate	Jun - 26	0.10%
Euro-Zone	GDP Year-over-Year	Q1 - 2009	-4.8%
	CPI	May - 2009	0.0%
	Unemployment	April - 2009	9.2%
	ECB Target Rate	Jun - 26	1.00%
UK	GDP Year-over-Year	Q1 - 2009	-4.1%
	CPI	May - 2009	2.2%
	Unemployment	May - 2009	4.8%
	BoE Target Rate	Jun - 26	0.50%
Canada	GDP Year-over-Year	March - 2009	0.0%
	CPI	May - 2009	0.1%
	Unemployment	May - 2009	8.4%
	BoC Target Rate	Jun - 26	0.25%

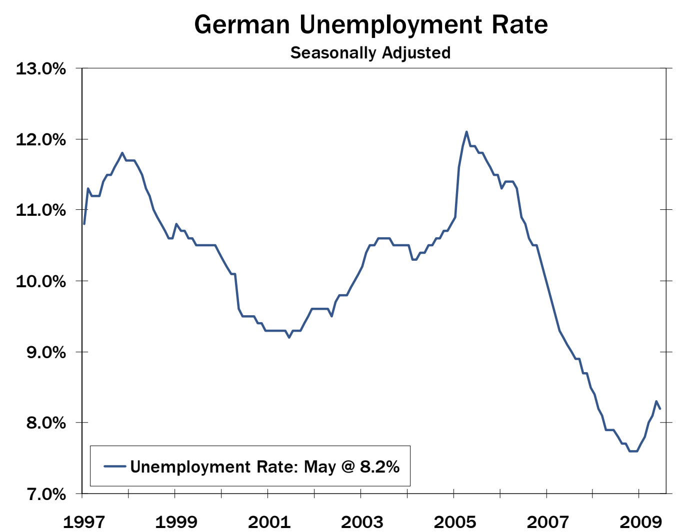


German Unemployment Rate • Tuesday

Economic growth in the Euro-zone's largest economy contracted at a 14.4 percent annualized rate in the first quarter of this year as Germany weathered the slowdown in global demand that followed the financial crisis late last year. Industrial production data are still declining at a double digit pace, suggesting the economy still faced headwinds in the second quarter. That said, recent improvement in business sentiment and early signs of recovery in global trade have offered some hope that the pace of decline is slowing. German employers have had to scale back production and let go of workers in recent months. However, fewer people lost their jobs in May than any other month since last October, suggesting a welcome slowing in the rate of job losses. Still, with industrial production falling so swiftly German employers will have more cuts to make before this recession has fully run its course. The consensus expectation is that the unemployment rate climbed slightly in June.

Previous: 8.2%

Consensus: 8.3%



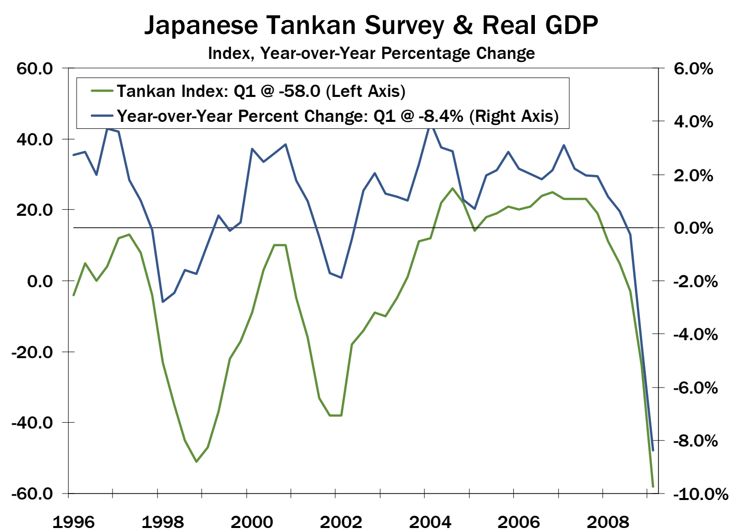
Japanese Tankan Survey • Wednesday

Some market watchers have used the word "depression" to describe the economic situation in Japan. With real GDP contracting at more than a thirteen percent annualized rate in each of the last two quarters, one can understand why. The collapse in global trade, made worse by last fall's credit crunch, rocked the Japanese economy. Indeed, real exports of goods and services crashed at an annualized rate of 70 percent in the first quarter.

In the global review section of this report, we discussed the recent improvement in exports. That improvement has fueled hopes for a turnaround in the Japanese economy. The Tankan index of Japanese business sentiment plunged from a reading of -24 in the fourth quarter of last year to -58 in the first quarter, edging out the all-time low set in the deep recession of 1975. As the nearby chart shows, the Tankan tracks closely with GDP. The consensus is expecting a relative improvement in the second quarter when this number prints on Wednesday.

Previous: -58

Consensus: -34



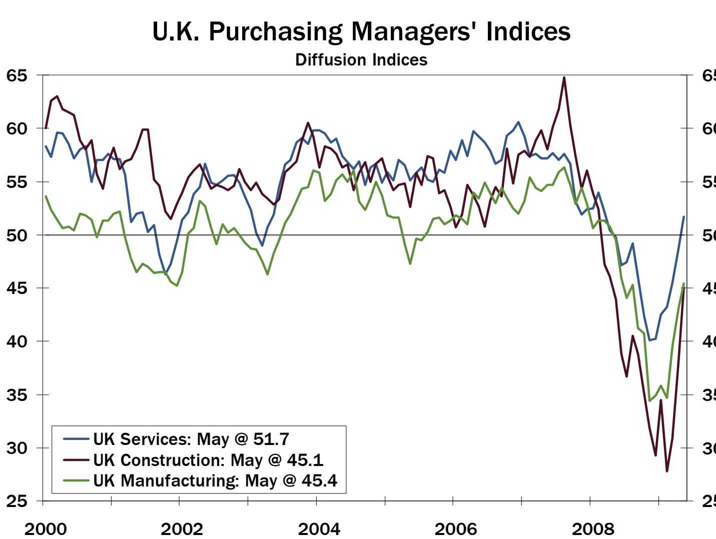
U.K. Purchasing Manager Indices (Wed.-Fri.)

Real GDP in the United Kingdom contracted at an annualized rate of 7.3 percent in the first quarter, the sharpest rate of contraction since the third quarter of 1979. But purchasing managers' indices (PMIs) have recovered in recent months. In fact, the services PMI is above 50 for the first time since April 2008. The manufacturing and construction PMIs are moving in the right direction but still remain firmly in contraction territory.

In the second half of next week the PMI reports will be gradually rolling in. On Wednesday, manufacturing PMI is expected to show modest improvement, but will likely remain below 50. Construction PMI is reported on Thursday; little change is likely for this series as homebuilders in the U.K. try to gauge whether or not the real estate market has bottomed. Finally on Friday the services PMI prints, and markets will watch to see if the series remains over 50.

Previous: Mfg. 45.4, Construction 45.1, Services 51.7

Consensus: Mfg. 46.4, Construction 46.0, Services 51.5



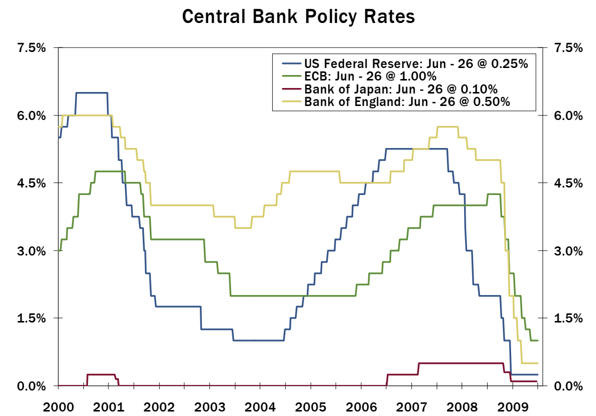
Interest Rate Watch

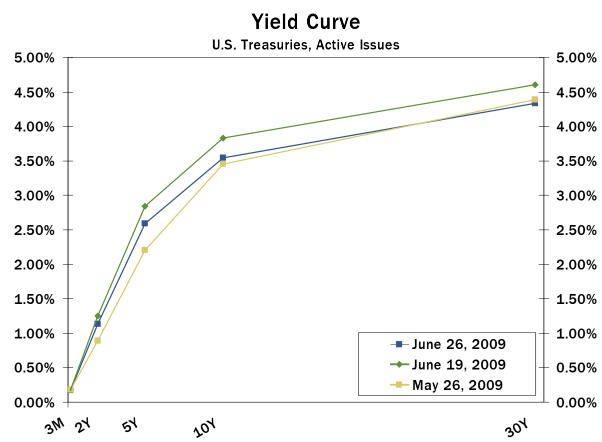
Economy Dictates Steady Fed Policy

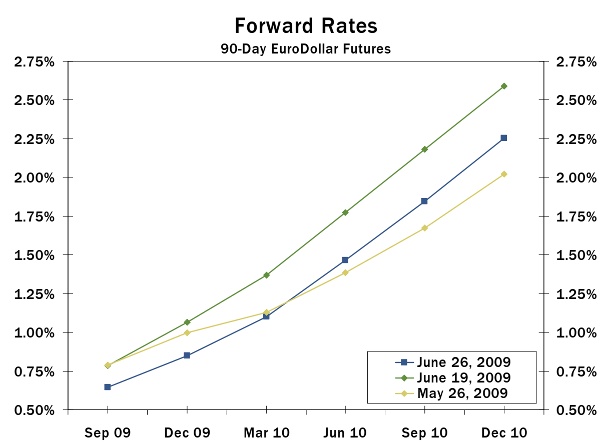
This week's statement from the Federal Open Market Committee focused on two fundamentals. First, the FOMC stated that "information received suggests that the pace of economic contraction is slowing." We concur. Second, the FOMC stated "the Committee expects that inflation will remain subdued for some time." We concur again. Thus, our outlook remains unchanged—the range for the Federal funds rate will remain steady for the rest of this year.

Our view that the funds rate would remain unchanged received additional support from the Fed's announcement on its liquidity programs. This announcement follows up on the comments of Bill Dudley, President of the New York Fed, which suggest there will be no rapid drop-off in the Fed's support. The Federal Reserve extended commercial paper and primary dealer facilities suggesting the Fed wants to keep these just in case the expected recovery runs into problems and/or some unexpected end-of-year complications develop. Extending these programs until February allows the Committee to review all programs at their semi-annual outlook session.

The limits on the asset-backed commercial paper and term securities programs were lowered but appear generous relative to recent usage. As for the Term Auction Facility (TAF) the Fed argued that bid amounts at recent auctions had fallen below the auction amounts. This suggests that interest right now is limited and this allows the Fed to reduce the amounts going forward. We view the lowering of these limits as a sign of policy success and not a restraint on the marketplace. To the extent private investors, not the Fed can maintain an orderly market the better off the economy becomes.







Topic of the Week

Recession Probability Still Declining

Economic recovery prospects have improved. The probability of recession two quarters from now has downshifted sharply over the previous three months. The latest probability calculation from our quarterly recession model is consistent with prior economic recoveries. The second quarter reading currently stands at 37 percent, down significantly from the 80 percent readings registered earlier this year. Our model takes a look at a very broad set of variables, and the results suggest economic recovery is likely within the next six months.

Economic improvement began to show up in our model in recent months in the regional Chicago manufacturing survey. While the official recovery call will come from the National Bureau of Economic Research, our outlook is that the recovery will begin in the third quarter of this year with economic growth increasing around a three percent annualized pace.

While we do expect recovery in the pace of economic growth, employment remains an issue for both cyclical and structural reasons. Job declines have been widespread with major losses in manufacturing and construction. The only bright spot recently has been healthcare and education. Aggregate hours worked in the U.S. economy have declined in recent months suggesting continued weakness in both employment and hours worked.

Moreover, the structural trend of declining employment in blue-collar manufacturing continues as it has since the early 1970s. These declines reflect the high cost of labor relative to capital that has prompted the increased use of technology and capital to substitute for labor, as well as the evolution of consumer demand from "goods" to "services."

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Market Data ♦ Mid-Day Friday

U.S. Interest Rates

	Friday 6/26/2009	1 Week Ago	1 Year Ago
3-Month T-Bill	0.18	0.17	1.71
3-Month LIBOR	0.60	0.61	2.80
1-Year Treasury	0.18	0.34	2.37
2-Year Treasury	1.09	1.20	2.66
5-Year Treasury	2.53	2.80	3.39
10-Year Treasury	3.50	3.78	4.03
30-Year Treasury	4.30	4.50	4.60
Bond Buyer Index	4.79	4.86	4.83

Foreign Exchange Rates

	Friday 6/26/2009	1 Week Ago	1 Year Ago
Euro ($/€)	1.407	1.394	1.576
British Pound ($/£)	1.652	1.649	1.989
British Pound (£/€)	0.852	0.845	0.792
Japanese Yen (¥/$)	95.090	96.270	106.810
Canadian Dollar (C$/$)	1.152	1.135	1.014
Swiss Franc (CHF/$)	1.083	1.081	1.024
Australian Dollar (US$/A$)	0.806	0.806	0.956
Mexican Peso (MXN/$)	13.231	13.360	10.297
Chinese Yuan (CNY/$)	6.834	6.836	6.866
Indian Rupee (INR/$)	48.115	48.085	42.685
Brazilian Real (BRL/$)	1.946	1.975	1.604
U.S. Dollar Index	79.831	80.264	72.487

Foreign Interest Rates

	Friday 6/26/2009	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	1.12	1.23	4.95
3-Month Sterling LIBOR	1.20	1.24	5.95
3-Month Canadian LIBOR	0.60	0.61	3.45
3-Month Yen LIBOR	0.46	0.49	0.93
2-Year German	1.32	1.45	4.46
2-Year U.K.	1.17	1.32	5.13
2-Year Canadian	1.21	1.29	3.16
2-Year Japanese	0.32	0.36	0.83
10-Year German	3.38	3.50	4.52
10-Year U.K.	3.69	3.81	5.01
10-Year Canadian	3.39	3.52	3.71
10-Year Japanese	1.40	1.45	1.66

Commodity Prices

	Friday 6/26/2009	1 Week Ago	1 Year Ago
W. Texas Crude ($/Barrel)	69.06	69.55	139.64
Gold ($/Ounce)	939.30	934.05	917.30
Hot-Rolled Steel ($/S.Ton)	335.00	335.00	1125.00
Copper (¢/Pound)	229.20	224.55	382.35
Soybeans ($/Bushel)	12.03	12.11	15.29
Natural Gas ($/MMBTU)	3.84	4.03	13.10
Nickel ($/Metric Ton)	15,588	14,919	21,538
CRB Spot Inds.	400.77	400.28	501.58

Next Week's Economic Calendar

	Monday	Tuesday	Wednesday	Thursday	Friday
	29	**30**	**1**	**2**	**3**
U.S. Data		**Consumer Confidence** May 54.9 June 49.5 (W)	**ISM Manufacturing** May 42.8 June 43.5 (W) **Total Vehicle Sales** May 9.9M June 9.8M (W) **Construction Spending** April 0.8% May -0.5% (W)	**Nonfarm Payrolls** May -345K June -400K (W) **Unemployment Rate** May 9.4% June 9.6% (W) **Factory Orders** April 0.7% May 0.8% (W)	**Independence Day (Obs)** U.S. Markets Closed
Global Data	**Euro-zone** **Economic Confidence** Previous (May) 69.3	**Germany** **Unemployment Rate** Previous (May) 8.2% **UK** **GDP (QoQ)** Previous (1Q) -1.9% (P)	**Japan** **Tanken Lge Mfg Index** Previous (1Q) -58 **UK** **PMI Manufacturing** Previous (May) 45.4	**UK** **PMI Construction** Previous (May) 45.9	**UK** **PMI Services** Previous (May) 51.7

Note: (W) = Wachovia Estimate (c) = Consensus Estimate

Wachovia Economics Group

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