March 11, 2011

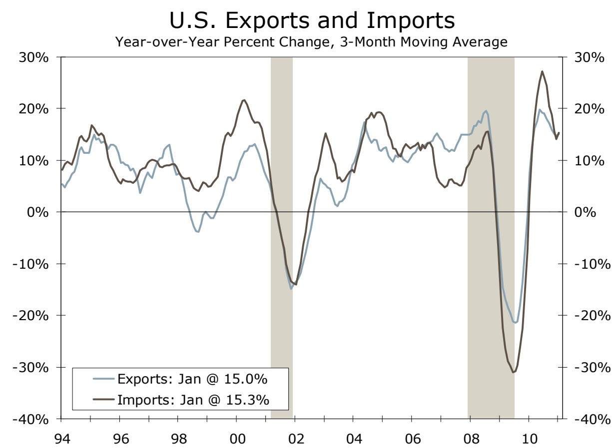
Economics Group

Weekly Economic & Financial Commentary

U.S. Review

Indicators Point To Moderate Growth

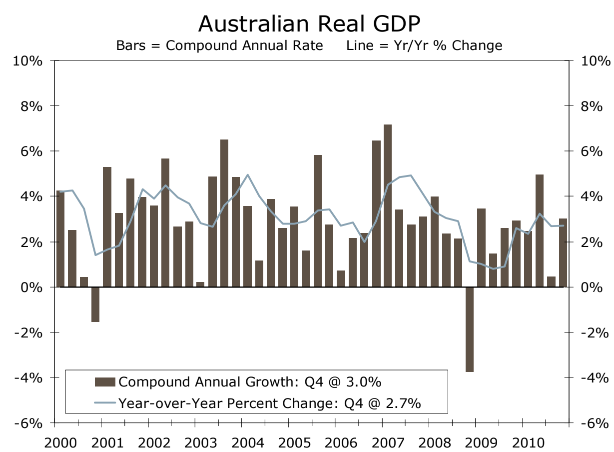
- Retail sales in February, which rose 1.0 percent, provided a good sign that consumer spending remained strong in the first quarter.
- The trade deficit grew wider than expected in January, as imports grew twice as fast as exports. The stronger imports number was driven by real non-oil imports rather than the rising costs of oil imports.
- The slight increase in jobless claims this week may be tied to the timing of the President's Day holiday and does not reflect a reversal of the underlying trend.



Global Review

If You Must Go Through Flood Waters, Hit the Gas

- After a lackluster third quarter, the Australian economy picked up speed in the fourth, expanding at a 3.0 percent annualized rate. While the flooding and typhoons that ravaged Queensland are only partially captured in the fourth-quarter data, it will surely weigh on growth in the first quarter of 2011.
- The jobs report in Australia this week was a miss on the headline, with payrolls falling for the first time in 18 months. The details were more encouraging; a drop-off in part-time employment hid the largest jump in full-time employment since November.



Wells Fargo U.S. Economic Forecast

	Actual 2010				Forecast 2011				Actual			Forecast	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	2008	2009	2010	2011	2012
Real Gross Domestic Product [1]	3.7	1.7	2.6	2.8	2.9	2.6	2.8	3.0	0.0	-2.6	2.8	2.7	3.0
Personal Consumption	1.9	2.2	2.4	4.1	2.4	2.5	2.5	3.0	-0.3	-1.2	1.8	2.8	2.6
Inflation Indicators [2]													
"Core" PCE Deflator	1.8	1.5	1.2	0.8	0.8	0.9	1.0	1.3	2.3	1.5	1.3	1.0	1.4
Consumer Price Index	2.4	1.8	1.2	1.2	1.9	2.9	3.0	2.9	3.8	-0.3	1.6	2.7	2.6
Industrial Production [1]	7.1	7.2	6.2	3.2	4.8	4.4	4.1	3.9	-3.3	-9.3	5.7	4.6	4.0
Corporate Profits Before Taxes [2]	37.6	37.0	26.4	12.5	8.2	6.2	6.2	6.7	-16.4	-0.4	27.5	6.8	7.0
Trade Weighted Dollar Index [3]	76.1	78.8	73.6	73.2	72.5	73.0	74.0	75.0	74.3	77.7	75.6	73.6	78.0
Unemployment Rate	9.7	9.6	9.6	9.6	8.9	8.7	8.5	8.4	5.8	9.3	9.6	8.6	8.2
Housing Starts [4]	0.62	0.60	0.59	0.53	0.59	0.61	0.65	0.71	0.90	0.55	0.59	0.64	0.83
Quarter-End Interest Rates [5]													
Federal Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	1.88	0.25	0.25	0.25	0.75
Conventional Mortgage Rate	4.97	4.74	4.35	4.71	4.90	5.15	5.15	5.20	6.04	5.04	4.69	5.10	5.63
10 Year Note	3.84	2.97	2.53	3.30	3.60	3.75	3.75	3.80	3.66	3.26	3.22	3.73	4.13

Forecast as of: March 11, 2011
[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
[5] Annual Numbers Represent Averages

Inside

U.S. Review

Theme of Sustainable Economic Growth Continues

This week's economic indicators continue to signal that the economy is experiencing a moderate pace of growth in the first quarter of this year. Data this week indicated that sales among both retailers and wholesalers improved in January while the trade deficit widened further than expected.

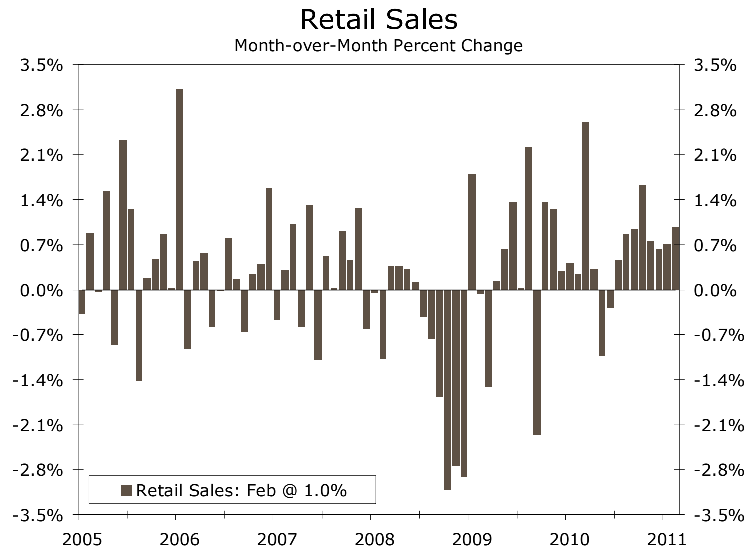
Retail sales for February rose in line with expectations, increasing 1.0 percent led by gains in motor vehicles and parts sales. In addition, January's retail sales were revised upward to 0.7 percent from the originally reported 0.3 percent. This report is consistent with our expectations of a gradually strengthening consumer sector adding to growth this year.

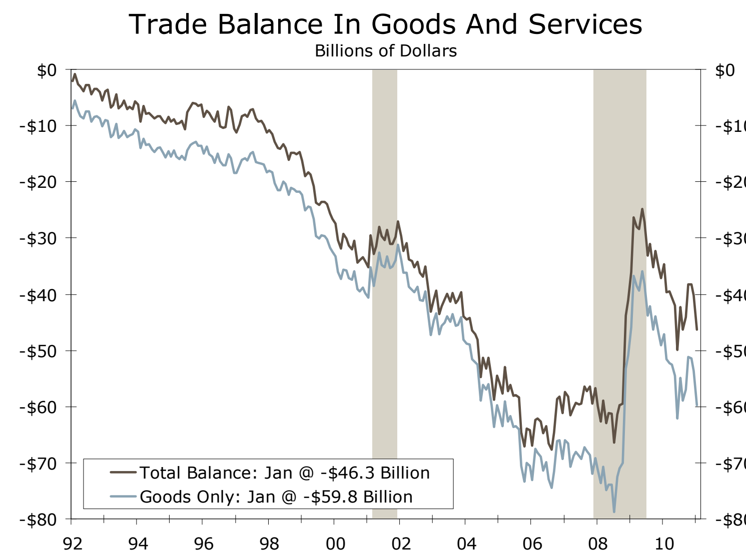
Wholesale inventories for January edged upward by 1.1 percent led by increases in durable and non-durable goods. The inventory-to-sales ratio continued its downward trajectory. A 1.13 inventory-to-sales ratio is now below the historical average of 1.15, implying that firms will likely begin to rebuild inventory levels. This would be good news for manufacturing output and employment over the next few months. Firms also turn to global sources to replenish inventory levels and, in fact, this week's trade data showed a marked increase in imports.

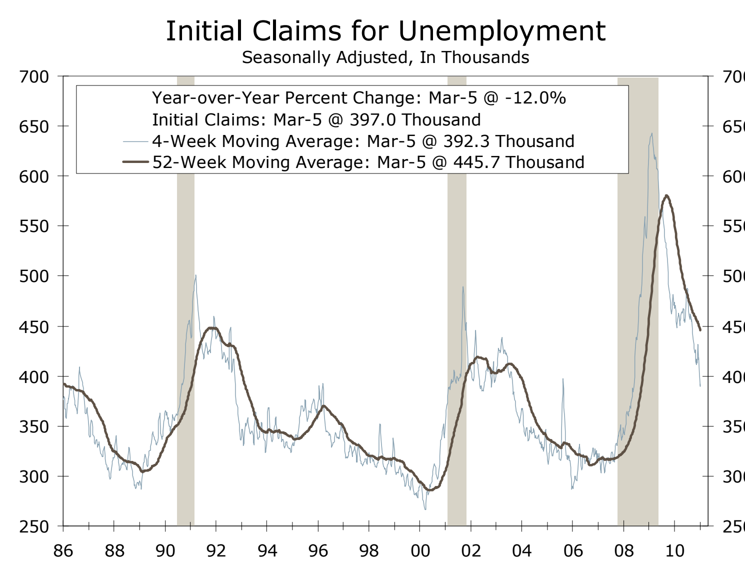
January trade data indicated that the trade deficit widened more than expected as import growth rose twice as fast as exports. The pick-up was driven up by real non-oil imports such as vehicles and parts and industrial supplies rather than the rising costs of oil imports. Exports for the month rose 2.7 percent led by a $1.3 billion rise in vehicles and parts exports. The increase in demand and higher prices helped to boost commodity exports. While the news of a wider trade deficit typically subtracts from growth, if the additional imports show up in the inventories numbers, the detraction from GDP would mostly be offset.

On the small business front, the NFIB small business index continued to signal a turnaround in the small business sector, but not without some challenges. The headline index posted its eighth straight month of increases with the index for February reaching 94.5, the highest reading since the onset of the recession in December 2007. While the trend in the index was welcome news, the details of the release pointed to some possible difficulties for this sector. Credit conditions for small businesses remained relatively unchanged for the month and higher commodity and import prices have led small businesses to pass along higher costs to their consumers, a move that may harm their competiveness with larger firms. These factors will likely play a role over the next few months in tempering the pace of employment growth within this sector.

Initial jobless claims rose slightly this week to 397,000 from last week's upwardly revised 371,000. While the increase is a bit of a surprise, the four-week moving average remains below the important 400,000 level that historically has signaled stronger job growth. In addition, the Labor Department citied some seasonal issues due to the President's Day holiday as a potential factor affecting the data.





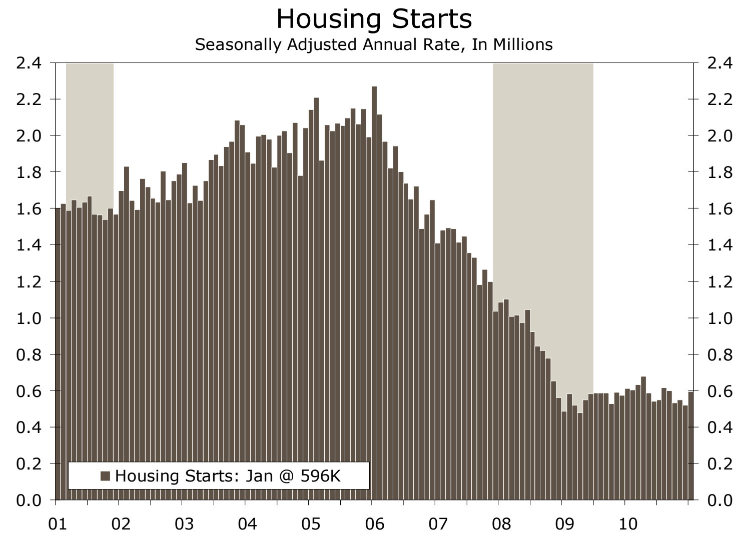


Housing Starts • Wednesday

Housing starts jumped 14.6 percent in January to a 596,000 annual rate. However, the entire increase came from a 78 percent surge in multifamily starts following the rush of multifamily permits in December ahead of building code changes. Meanwhile, single-family starts, which comprise 70 percent of the market, fell 1.0 percent to a 413,000 annual rate, the lowest since May 2009, as weak demand and bad weather both played a role. Building permits fell 10.4 percent in January as multifamily permits fell after the year-end surge. Single-family permits fell as well, but the three-month moving average has trended up over the past few months. Housing completions took a big dive in January due primarily to bad weather, so we could see a bounce in this number for February. Although new home inventories are at all-time lows, we do not expect a significant pickup in building activity anytime soon as unemployment remains high and mortgage standards remain tight.

Previous: 596K **Wells Fargo: 600K**

Consensus: 575K

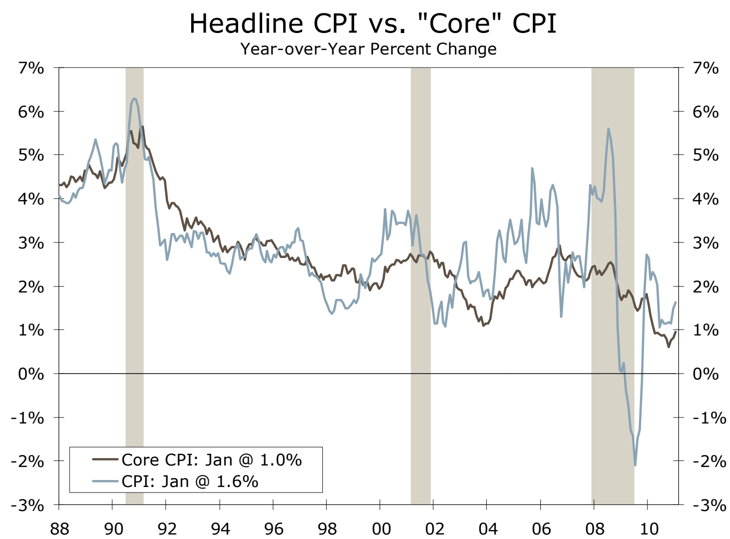


Consumer Price Index • Thursday

The CPI rose 0.4 percent in January, exceeding the 0.3 percent expected increase. Prices were 1.6 percent higher than a year ago. The increase was largely due to a 3.5 percent increase in gasoline prices, which came on the heels of a 6.7 percent jump in December. Food prices rose 0.5 percent, the biggest increase since September 2008, as poor growing conditions restrained supplies amid growing demand. Core prices rose 0.2 percent, the biggest increase since October 2009, which brought the year-ago rate to 1.0 percent, the highest since March 2010 and the fourth straight monthly increase. Rising cotton prices stoked a 1.0 percent jump in apparel prices, the biggest since February 2009. This, along with rising airfares, helped to drive core prices higher. Still, high unemployment is containing wage increases, which continue to slow on trend. If February inflation comes in above 1.7 percent year-over-year, it will be the first month of negative real wage growth since April 2010.

Previous: 0.4% **Wells Fargo: 0.4%**

Consensus: 0.4% (Month-over-Month)

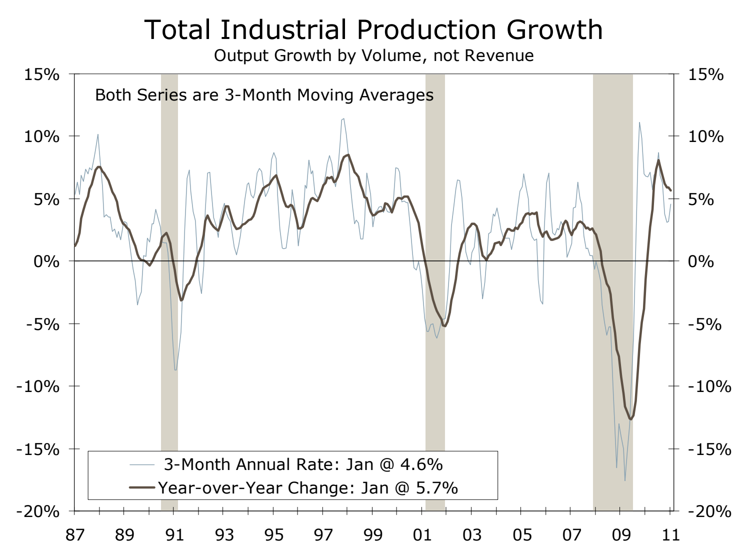


Industrial Production • Thursday

Industrial production fell 0.1 percent in January. Mining output fell 0.7 percent and milder temperatures in some areas of the country led to a 1.6 percent drop in utilities output. In contrast, manufacturing output rose 0.3 percent, fueled by a 3.2 percent increase in production of motor vehicles and parts as vehicle demand continues to improve. Outside of motor vehicles and parts, production rose just 0.1 percent, the weakest showing since September. Production of home electronics fell for the fourth straight month, while production of construction and business supplies also fell. Meanwhile, production of business equipment remained strong as companies continued to upgrade technology to improve productivity. Capacity utilization dipped slightly to 76.1 percent from 76.2 percent and remains well below the levels seen prior to the recession. Recent manufacturing reports suggest that industrial production probably accelerated in February.

Previous: -0.1% **Wells Fargo: 0.6%**

Consensus: 0.6%



Global Review

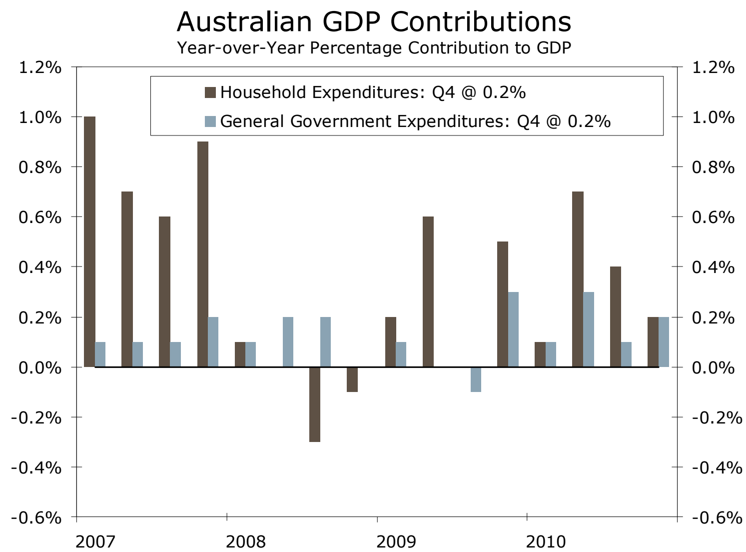
Aussie Economy Has Momentum Heading into Floods

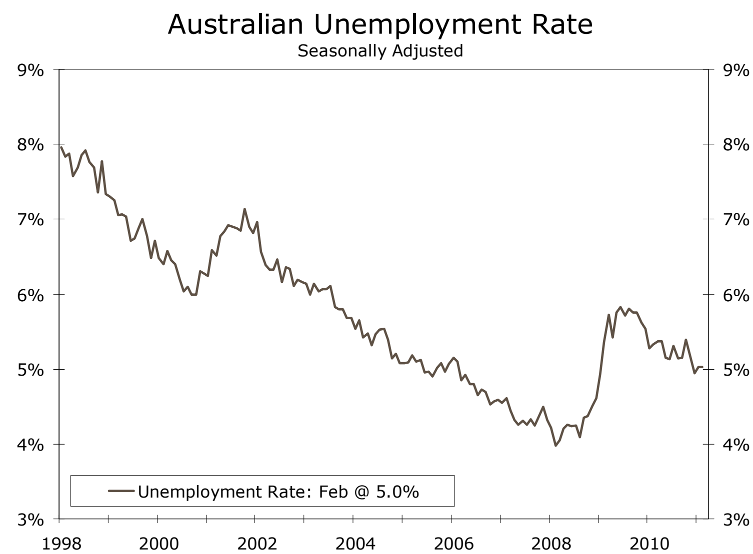
The Australian economy sidestepped the recession during 2008 and 2009 as emerging-market demand for Australian raw materials and commodities helped fuel growth even as other developed economies succumbed to the global slowdown. More recently, we learned that growth picked up steam in the final quarter of last year as GDP expanded at a 3.0 percent annualized rate. The largest positive contribution to fourth-quarter growth came from a modest rebuilding in inventories. A pickup in consumer spending and government spending was more than enough to offset a slight decline in business spending.

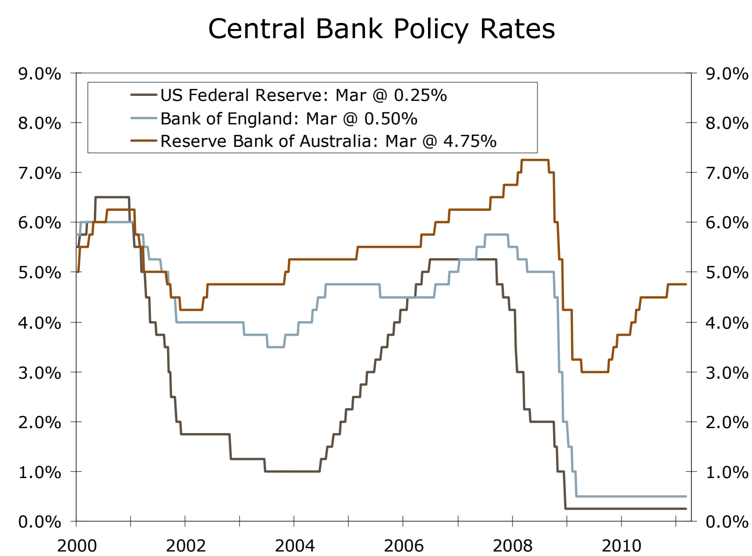
While it may have had some impact in the fourth quarter, this is the last report on Australian economic growth before the full effect of massive flooding and cyclones that ravaged the country's Northeast took a significant toll on growth. The impact of the damage of these natural disasters is tough to gauge at this point, but one Reserve Bank of Australia (RBA) board member suggested the flooding could cut GDP by 1 percent, or A$13 billion.

A more contemporary bellwether of economic activity in Australia is the monthly employment report. February employment data for Australia printed this week and presented a somewhat mixed picture for the job market. For the first time in a year-and-a-half, employers cut workers as the total number of employees on payrolls dropped 10,100. Expectations were running high prior to the release with the consensus looking for an increase of 20,000 jobs, which would have marked the 19th consecutive increase. So, the dip in February was a bit jarring, but the underlying details offered a somewhat more optimistic take on the employment picture. The decline was all part-time job cuts. Full-time employment actually jumped by 47,600 jobs, the highest monthly full-time payrolls gain since November.

In its ahead-of-the-curve execution of monetary policy tightening, the Reserve Bank of Australia (RBA) has raised its cash rate 175 bps at a time when many other central banks have been keeping rates on hold. While some market watchers feared the tightening could dampen growth during an uncertain time for global markets, it is hard to find fault with the outcome thus far. Economic growth has been steady and inflation remains in check. CPI inflation came in at 2.7 percent year over year through the fourth quarter. Another outcome has been a significant strengthening in the local currency. The Aussie dollar has been trading roughly at parity with the U.S. dollar since the start of the year, though at points it has touched levels of strength not seen since the early 1980s. Earlier this month, the RBA left rates on hold for a third straight meeting; but language out of the Bank has been growing increasingly hawkish, lifting the likelihood of another rate hike by midyear. The next look at CPI inflation will be on April 26th when first-quarter price data become available. Should that report show a jump in inflation north of 3 percent and the economy is still in expansion, we would expect the RBA to resume its tightening campaign with a 25-bp increase in the cash rate at its May 3rd meeting the following week.







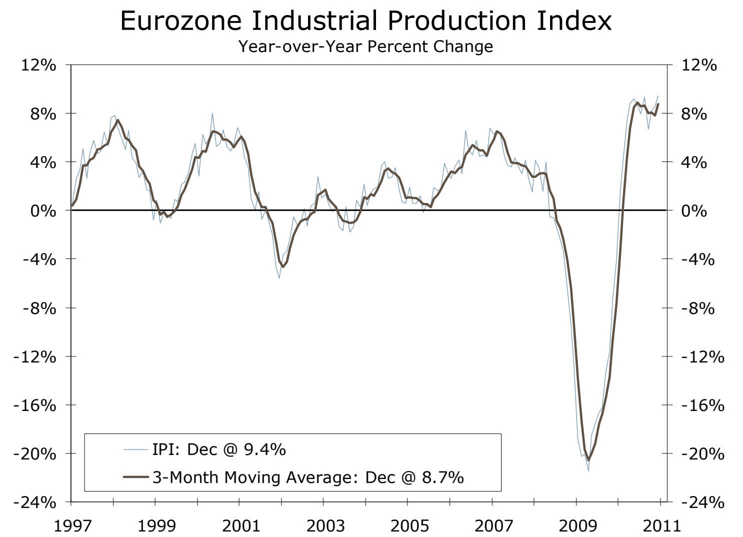
Eurozone Industrial Production • Monday

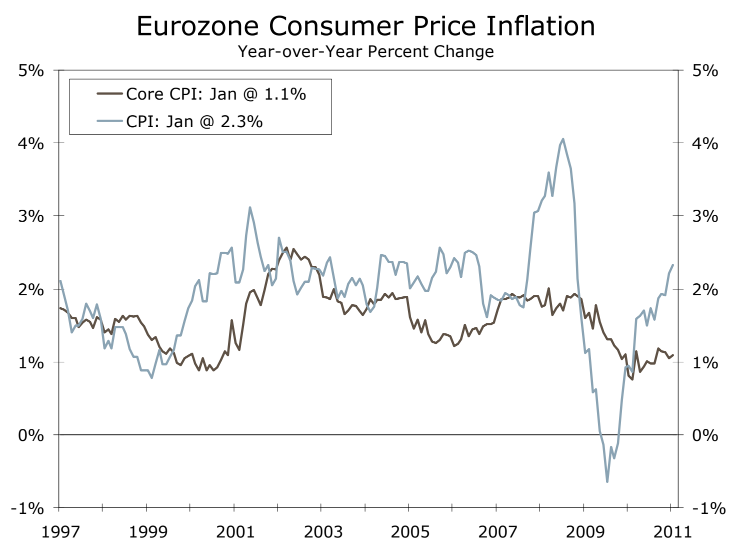
Eurozone industrial production for January should give a good clue to the strength of the region's economy entering 2011. Since the last month of last year, the index has shown a negative 0.1 percent month-on-month performance. A positive print by industrial production in January could help minimize the importance of the previous month's negative number, especially if the January number comes in on the strong side.

While the month-over-month index dropped in December, the year-over-year index still remained at a strong 8.8 percent, which means that the industrial sector will probably remain as one of the leading sectors within the region. Of course, a big reason for this increase in industrial production is probably due to the stellar performance of the German economy, which will continue to point to the zone's strong dependency on Germany's industrial might.

Previous: 8.8% (Year-over-Year)

Consensus: 6.4%





Eurozone Core CPI • Wednesday

ECB officials have been all over the airwaves in recent weeks making a case for increasing interest rates at the bank's next monetary policy meeting on April 7, 2011. The markets, especially foreign currency markets, have been acting accordingly, sending the U.S. dollar down again against the euro.

Thus, the release of the core consumer price index this Wednesday may give ECB policymakers more ammunition to continue to preach the gospel of higher interest rates. We do not expect much of a reaction from the markets regarding whether the ECB will move or not, but we could see some impact if the core CPI comes in higher than what markets are expecting. Even though the overall CPI recorded a 0.7 month-on month decline in January, the year-over-year rate stood at 2.4 percent, which is already higher than the ECB's comfort zone.

Previous: 1.1% (Year-over-Year)

Consensus: 1.1%

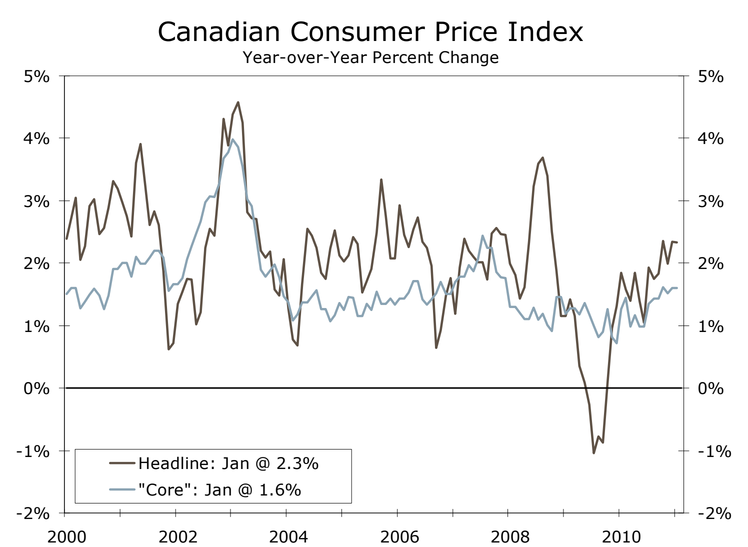
Canada CPI • Friday

The Canadian consumer price index for February will be released on Friday and this could reinforce our view that the Canadian central bank is poised to move interest rates higher. We expect the first move by the central bank to be for a 25-bp tightening at the May 31st meeting.

Stronger GDP growth in the last quarter of the year has changed the view of analysts regarding the direction of the Canadian economy, and the central bank has taken note. While the rate of inflation, at 2.3 percent year on year remains within the range targeted by the central bank, the institution will try to prevent any inflation surprise by preempting any potential resetting of inflationary expectations. The only way to do this is to start tightening monetary policy today to get ahead of the curve; otherwise the Bank may fall behind, which is a risk if the economy continues to accelerate.

Previous: 2.3% (Year-over-Year)

Consensus: N/A



Interest Rate Watch

Fundamentals for the Outlook

Since January, we have expected that long-term Treasury benchmark rates were going to rise and that remains our expectation in our latest monthly outlook. We expect sustained economic growth, even at the modest pace of 2.7 percent in 2011 and 3.0 percent in 2012, to be associated with rising credit demands and a shift in investor preferences toward equities and corporate debt and away from U.S. Treasury debt. Inflation is expected to run slightly higher, with the overall CPI rising 2.7 percent this year and core CPI rising 1.3 percent.

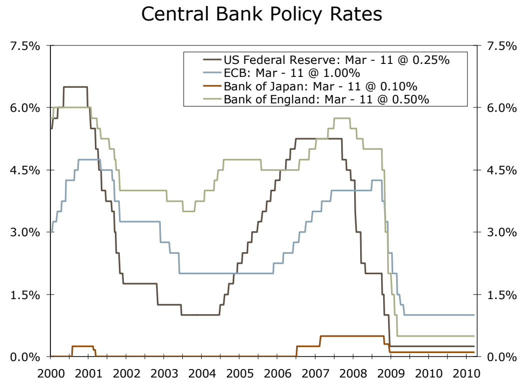
At the short-end of the curve, rates will still reflect the Fed's focus on completing its second round of quantitative easing by June. However, we do not expect another large asset purchase program to follow. Moreover, we expect the first Fed funds rate hike to occur in early spring 2012 as inflation will be rising and the recovery firmly evident to even the most diehard pessimist.

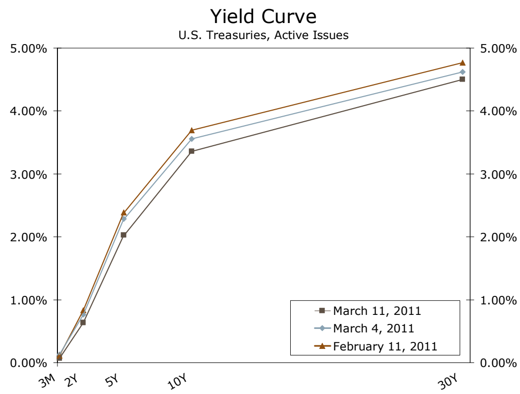
Deflationary Shocks and Sovereign Risk

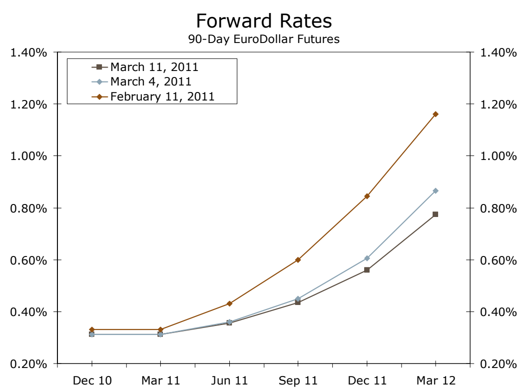
Increases in benchmark Treasury rates have been muted over the past year due to the impact of the deflationary concerns on unrest in the Middle East and its impact on oil prices/consumer income and the still unsettled European sovereign debt crisis.

For now, the U.S. Treasury market remains a refuge for many investors in a time of perceived uncertainty. Yet, for investors, these interludes of flights to safety cannot hide the underlying trend of rising inflation and interest rates since November.

Recent comments from members of the Federal Reserve suggest that a further large-scale asset purchase program is increasingly unlikely. For investors, this would suggest that the pressure will be toward higher benchmark interest rates this spring as the Federal Reserve drops out of the bid side of the bond market. Our expectation is that rates will rise even sooner as the evidence of rising inflation becomes more pervasive and the Federal Reserve will be heard making more comments about an exit.







Credit Market Insights

Debt in the Economy Expands

The Federal Reserve's Flow of Funds report released this week showed that nonfinancial-sector debt in the economy increased at an annualized rate of 5.1 percent in the fourth quarter. Public debt increased at a faster clip than private debt. State & local and federal government debt rose at an annualized rate of 7.9 percent and 14.9 percent, respectively, compared to an increase of 3.6 percent in business debt. Cash and other liquid assets on the balance sheets of nonfinancial corporate businesses remain at a 30-year high of 10.8 percent of financial assets, reducing many firms' needs to borrow. Nonfinancial corporate business debt outstanding ended 2010 at $7.3 trillion compared to $11.9 trillion of government debt outstanding.

On the household side, borrowing fell as consumers continued to deleverage on an aggregate basis. Household borrowing fell for the eleventh consecutive quarter on the heels of a 1.3 percent drop in mortgage borrowing. Household mortgage debt outstanding has fallen 5 percent since peaking in the first quarter of 2008 amid bank write-downs and fewer home sales. Consumer credit borrowing, on the other hand, increased for the first time in more than two years, rising at an annualized rate of $48.5 billion, or 2.0 percent. Total debt as a percentage of disposable income continues to trend downward, but the increase in consumer credit this past quarter signals that the bulk of consumer deleveraging may be behind us.

Mortgage Data

	Current	Week Ago	4 Weeks Ago	Year Ago
Mortgage Rates				
30-Yr Fixed	4.88%	4.87%	5.05%	4.95%
15-Yr Fixed	4.15%	4.15%	4.29%	4.32%
5/1 ARM	3.73%	3.72%	3.92%	4.05%
1-Yr ARM	3.21%	3.23%	3.35%	4.22%
MBA Applications				
Composite	514.2	445.1	464.7	633.1
Purchase	194.4	172.8	186.1	226.8
Refinance	2,383.7	2,034.7	2,086.4	3,007.2

Source: Freddie Mac, Mortgage Bankers Association and Wells Fargo Securities, LLC

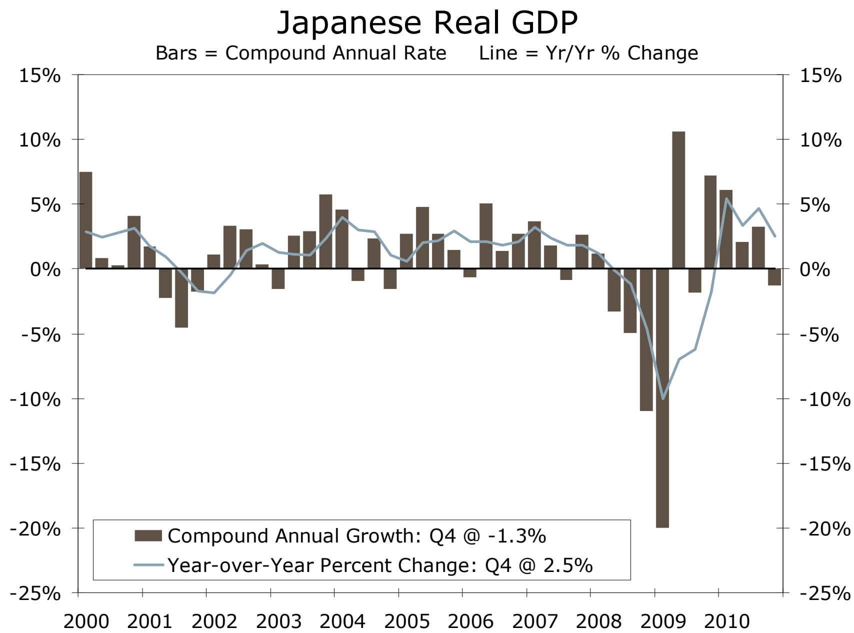
Topic of the Week

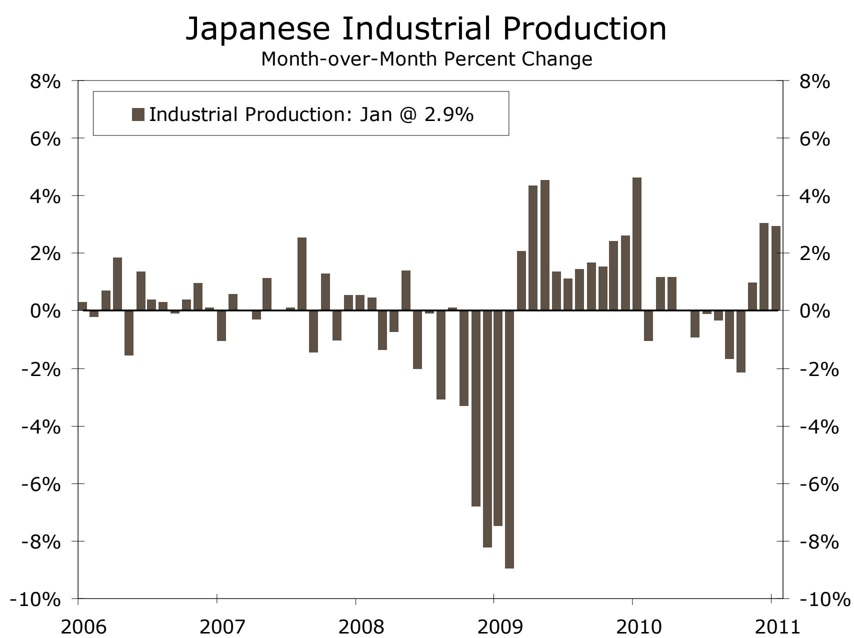
Economic Impact of the Earthquake in Japan

Earlier today, the largest earthquake in Japan's recorded history spawned a devastating tsunami that slammed portions of Japan's eastern coast. The economic consequences resulting from this earthquake will likely be noticeable, coming at a time when Japan's economy already appears to be in the midst of a slowdown—the latest reading for real GDP in Japan turned negative, showing that the Japanese economy contracted 1.3 percent (annualized) in the fourth quarter of last year.

The last time a major earthquake damaged Japan's economy was in 1995 when the Great Hanshin Awaji earthquake struck the city of Kobe. Total damage and destruction associated with that earthquake was estimated to be worth more than $100 billion, or about 2 percent of total Japanese GNP at that time. The economic impact of today's earthquake in Japan may not be as large, though, as following the Great Hanshin Awaji earthquake, Japan greatly improved its disaster response systems, and many firms there have made significant steps toward diversifying supply chains to deal with such disasters. Moreover, the bulk of Japan's industrial sector appears not to have been directly affected by today's earthquake as most of the hardest hit areas are tied to Japan's agricultural sector.

When evaluating economic impacts tied to natural disasters, it is important to make the distinction between impacts to an economy's wealth and national income. On the one hand, the hit to wealth in Japan will likely be large, representing the lost value tied to the many homes, farmland and industrial facilities destroyed by this earthquake. On the other hand, Japan's GDP will be less affected as GDP measures the flow of activity in an economy, not the stock. Economists call this effect the broken window fallacy: While today's earthquake will affect Japanese GDP by interrupting domestic business and industrial production, these effects will be offset by future rebuilding activity, giving the appearance of stronger growth.





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Market Data ♦ Mid-Day Friday

U.S. Interest Rates

	Friday 3/11/2011	1 Week Ago	1 Year Ago
3-Month T-Bill	0.07	0.11	0.15
3-Month LIBOR	0.31	0.31	0.26
1-Year Treasury	0.23	0.31	0.41
2-Year Treasury	0.63	0.68	0.95
5-Year Treasury	2.05	2.18	2.42
10-Year Treasury	3.39	3.49	3.73
30-Year Treasury	4.54	4.60	4.67
Bond Buyer Index	4.91	4.90	4.33

Foreign Exchange Rates

	Friday 3/11/2011	1 Week Ago	1 Year Ago
Euro ($/€)	1.383	1.399	1.368
British Pound ($/£)	1.604	1.627	1.506
British Pound (£/€)	0.862	0.860	0.908
Japanese Yen (¥/$)	82.050	82.320	90.510
Canadian Dollar (C$/$)	0.977	0.973	1.024
Swiss Franc (CHF/$)	0.929	0.925	1.068
Australian Dollar (US$/A$)	1.007	1.014	0.915
Mexican Peso (MXN/$)	11.979	12.008	12.565
Chinese Yuan (CNY/$)	6.575	6.568	6.827
Indian Rupee (INR/$)	45.243	44.988	45.611
Brazilian Real (BRL/$)	1.664	1.655	1.764
U.S. Dollar Index	77.047	76.400	80.323

Foreign Interest Rates

	Friday 3/11/2011	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	1.13	1.12	0.59
3-Month Sterling LIBOR	0.81	0.81	0.64
3-Month Canadian LIBOR	1.22	1.22	0.40
3-Month Yen LIBOR	0.19	0.19	0.25
2-Year German	1.66	1.76	1.04
2-Year U.K.	1.30	1.39	1.25
2-Year Canadian	1.74	1.85	1.53
2-Year Japanese	0.22	0.24	0.15
10-Year German	3.21	3.27	3.18
10-Year U.K.	3.56	3.63	4.15
10-Year Canadian	3.27	3.33	3.51
10-Year Japanese	1.26	1.31	1.33

Commodity Prices

	Friday 3/11/2011	1 Week Ago	1 Year Ago
WTI Crude ($/Barrel)	100.73	104.42	82.11
Gold ($/Ounce)	1413.83	1430.90	1109.50
Hot-Rolled Steel ($/S.Ton)	870.00	870.00	635.00
Copper (¢/Pound)	415.25	447.20	336.60
Soybeans ($/Bushel)	13.30	13.89	9.41
Natural Gas ($/MMBTU)	3.90	3.81	4.44
Nickel ($/Metric Ton)	26,020	28,834	21,445
CRB Spot Inds.	613.71	622.38	499.65

Next Week's Economic Calendar

	Monday 14	Tuesday 15	Wednesday 16	Thursday 17	Friday 18
U.S. Data		**FOMC Rate Decision** Previous 0.25% Expected 0.25% (W) **Import Price Index** January 1.5% February 0.4% (W)	**Housing Starts** January 596K February 600K (W) **PPI** January 0.8% February 0.7% (W) **Current Account** 3Q -$127.2B 4Q -$110.0B	**CPI** January 0.4% February 0.4% (W) **Industrial Production** January -0.1% February 0.6% (W) **Leading Indicators** January 0.1% February 1.1% (W)	
Global Data	**Eurozone** **IP (YoY)** Previ0us (Dec) 8.8% **Japan** **Consumer Confidence** Previous (Jan) 41.1	**Brazil** **Retail Sales (YoY)** Previous (Dec) 10.1%	**Eurozone** **Core CPI (YoY)** Previous (Jan) 1.1%		**Canada** **CPI (YoY)** Previous (Jan) 2.3% **Germany** **PPI (YoY)** Previous (Jan) 5.7%

Note: (W) = Wells Fargo Estimate (c) = Consensus Estimate

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