September 17, 2010

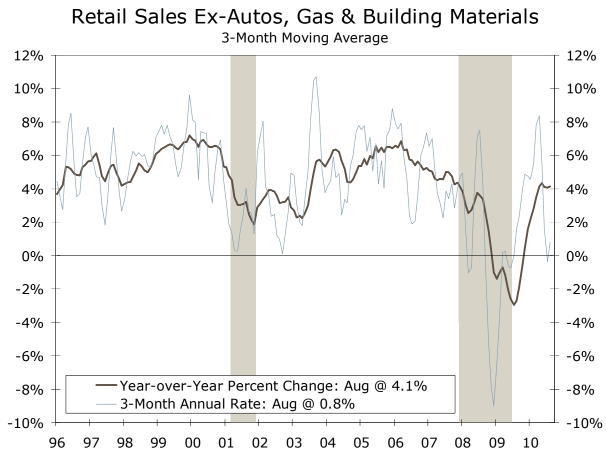
Economics Group

Weekly Economic & Financial Commentary

U.S. Review

Mostly Better News But Sluggishness Still Reigns

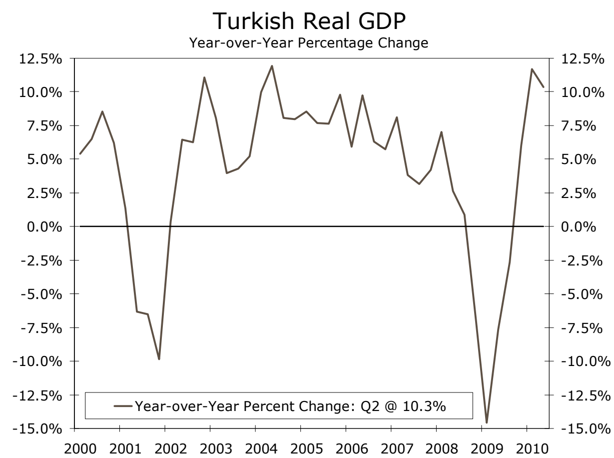
- This week's economic reports mostly came in ahead of expectations or roughly in line with them, which further alleviated fears of double-dip recession.
- Retail sales rose solidly in August, with overall sales rising 0.4 percent and our preferred core measure of retail sales climbing 0.6 percent.
- Weekly first-time unemployment claims declined for the third week in a row but remain relatively high at 450,000. Emergency claims also declined again.



Global Review

Turkish Economy Slows, Recovery Still on Track

- Turkish GDP slowed from 11.7 percent year-on-year to 10.3 percent, but was better than expected. The manufacturing, construction and agriculture sectors posted strong gains. Trade remained a drag on GDP as strong domestic demand and demand for intermediate goods resulted in imports outpacing exports.
- While headline inflation remains low, capacity utilization rates continue to trend higher and are quickly approaching pre-crisis levels. This suggests that Turkish interest rates have likely bottomed, though no hikes are currently planned.



Wells Fargo U.S. Economic Forecast

	Actual						Forecast		Actual				Forecast	
	2009				2010				2006	2007	2008	2009	2010	2011
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q						
Real Gross Domestic Product [1]	-4.9	-0.7	1.6	5.0	3.7	1.6	1.6	2.3	2.7	1.9	0.0	-2.6	2.7	2.2
Personal Consumption	-0.5	-1.6	2.0	0.9	1.9	2.0	1.7	1.3	2.9	2.4	-0.3	-1.2	1.5	1.6
Inflation Indicators [2]														
"Core" PCE Deflator	1.6	1.5	1.3	1.7	1.8	1.5	1.3	1.0	2.3	2.4	2.3	1.5	1.4	1.1
Consumer Price Index	-0.2	-1.0	-1.6	1.5	2.4	1.8	1.1	0.6	3.2	2.9	3.8	-0.3	1.4	1.0
Industrial Production [1]	-17.6	-10.3	8.3	7.0	7.1	6.7	6.2	2.2	2.2	2.7	-3.3	-9.3	5.5	3.5
Corporate Profits Before Taxes[2]	-17.3	-11.4	-3.9	42.5	37.6	39.2	17.6	12.8	10.5	-6.1	-16.4	-0.4	25.8	6.8
Trade Weighted Dollar Index[3]	83.2	77.7	74.3	74.8	76.1	78.8	76.8	77.3	81.5	73.3	79.4	74.8	77.3	83.0
Unemployment Rate	8.2	9.3	9.6	10.0	9.7	9.7	9.6	9.9	4.6	4.6	5.8	9.3	9.7	9.6
Housing Starts[4]	0.53	0.54	0.59	0.56	0.62	0.60	0.55	0.60	1.81	1.34	0.90	0.55	0.59	0.81
Quarter-End Interest Rates														
Federal Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	5.25	4.25	0.25	0.25	0.25	0.31
Conventional Mortgage Rate	5.00	5.42	5.06	4.93	4.97	4.74	4.10	4.20	6.14	6.10	5.33	4.93	4.50	5.15
10 Year Note	2.71	3.53	3.31	3.85	3.84	2.97	2.50	2.60	4.71	4.04	2.25	3.85	2.98	2.98

Forecast as of: September 8, 2010
[1] Compound Annual Growth Rate Quarter-over-Quarter
[2] Year-over-Year Percentage Change

Inside

Together we'll go far

U.S. Review

Sluggishness Still Reigns

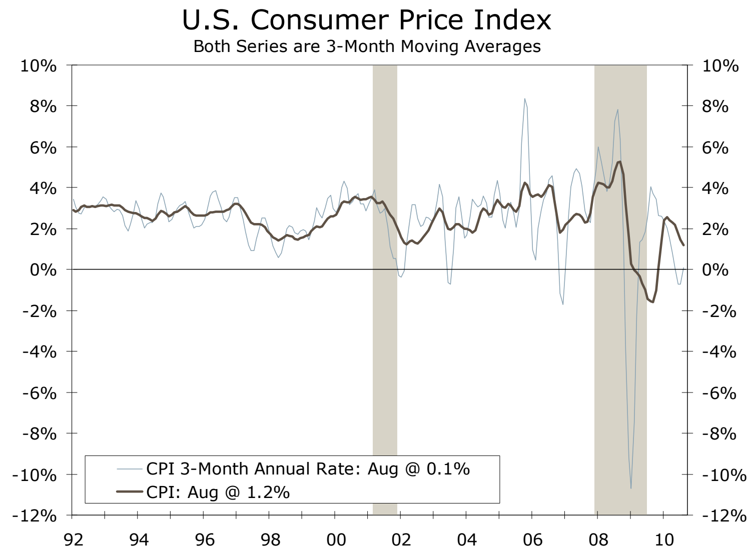
This week's economic reports show consumer spending held up better than expected during August and inventories also built up at a much faster rate. Reports on manufacturing activity were mixed, however, with production holding up relatively well in August, but new orders have slowed. Factories are also awash in excess capacity, which means inflation is unlikely to accelerate in a big way anytime soon. This week's inflation reports were mixed, with higher energy costs and higher prices for some key industrial commodities driving the Producer Price Index up 0.4 percent. Excluding food and energy prices, the PPI rose just 0.1 percent. The Consumer Price Index rose slightly less, with higher fuel prices pushing the overall CPI up 0.2 percent and prices excluding food and energy items rising less than 0.1 percent.

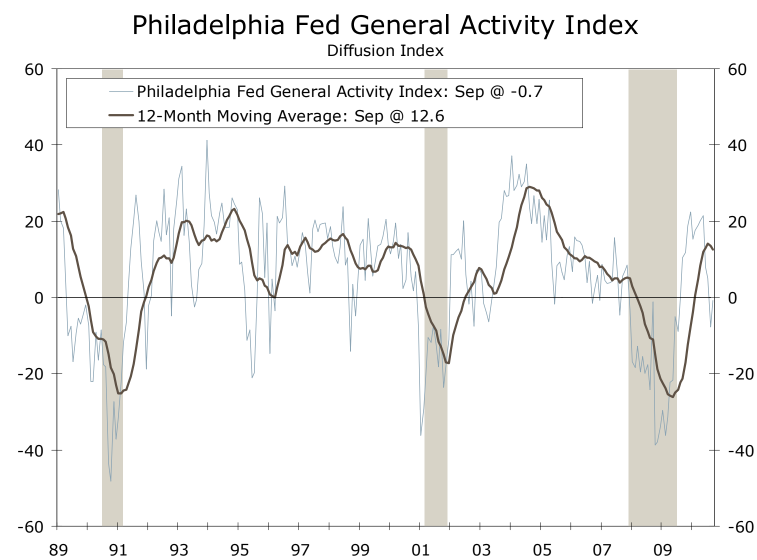
Taken together, this week's economic reports show the economy continuing to grow at a modest pace in the third quarter. Consumer spending appears to be holding up at around a 2 percent pace for the quarter. Core retail sales, which exclude motor vehicles, gasoline and building materials from the overall number, rose 0.6 percent in August and are up at a 0.9 percent pace over the past three months. Sales of clothing and apparel were a bright spot in August, with spending rising 1.2 percent. The increase in sales took place despite aggressive discounting by retailers. The CPI data show apparel prices falling 0.1 percent in August and falling 0.4 percent over the past year.

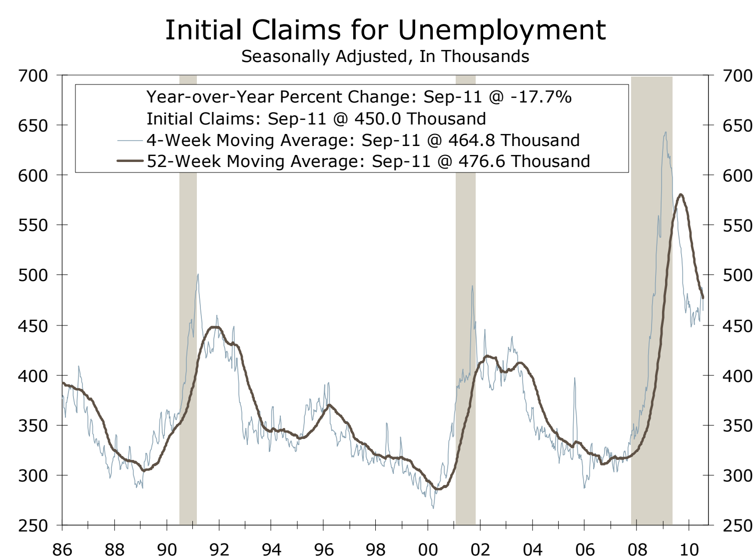
Motor vehicle sales declined in August, with sales at vehicles and parts dealers falling 0.7 percent. The decline may be a harbinger of production cuts or more aggressive sales incentives later this year. Inventories of motor vehicles have increased substantially over the past three months, rising 2.5 percent in July, 3.7 percent in June and 1.0 percent in May. While inventories are not at problematic levels, a sustained slowdown in sales would likely lead manufacturers to scale back output later this year.

Industrial production rose 0.2 percent in August, which was roughly in line with expectations. The more leading data on the factory sector look a bit more worrisome. The September surveys from the Federal Reserve Banks of New York and Philadelphia both point to some slowing in coming months. The New York Fed's Empire Survey fell 3.0 points in September to 4.1. The subcomponents of this series are quite volatile but show a clear slowing in new orders and shipments from earlier this year. The Philadelphia Fed Survey rose 7.0 points in September but remained in negative territory at -0.7. The new orders component fell 1.0 point to -8.1, which was the weakest reading since June 2009.

Weekly first-time unemployment claims fell 3,000 to 450,000. Claims have now dropped for 3 straight weeks and the pullback makes the spike reported in early to mid August look more like an anomaly tied to the timing of motor vehicle assembly plant shutdowns rather than to some new broad based slowdown in economic activity. The level of unemployment claims remains high, however, and is consistent with sluggish job growth.





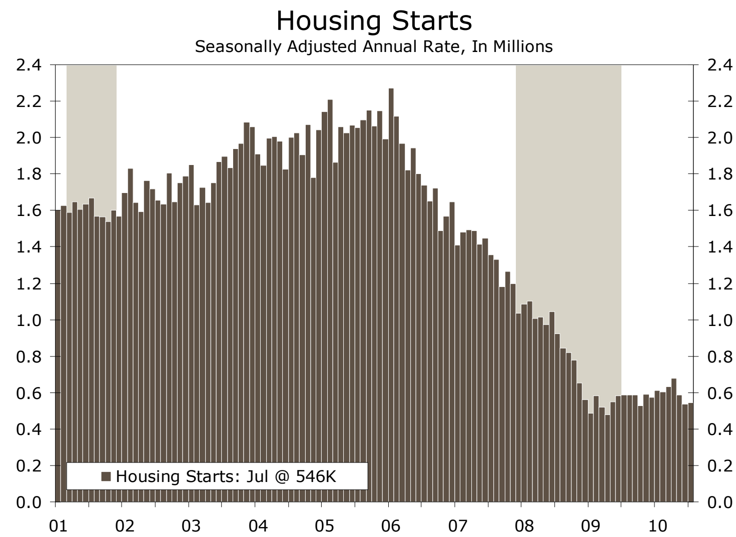


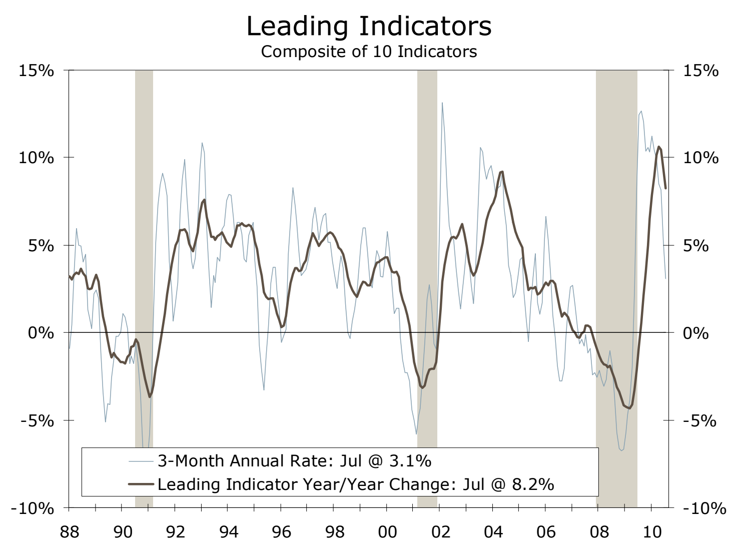
Housing Starts • Tuesday

Homebuilders continue to struggle with the after-effects of the homebuyer tax credit. Single family starts have declined in each of last three months and are now down 23.3 percent since the April contract signing deadline. The collapse in single family starts more than erases the two months of incentive-induced gains. We expect housing starts to linger near their current levels for the next few months. The tax credits likely pulled demand forward into the first half of the year and the recent slide in underlying economic growth will likely restrain demand for new homes. Oversupply also remains a problem, although most of the inventory is in existing homes. Moreover, permits for new single family homes are running slightly below the current pace of construction, suggesting we could see little to no improvement in construction over the next few months.

Previous: 546K **Wells Fargo: 535K**

Consensus: 550K





Leading Economic Indicator • Thursday

The LEI rose just 0.1 percent in July after falling 0.3 percent the prior month. A widening in the interest rate spread, a rise in the average workweek, a small decline in jobless claims and some lengthening in supplier deliveries helped offset declines in consumer expectations, the money supply and building permits. The LEI is probably even weaker than the headline number suggests. The wider interest rate spread boosted the index by 0.3 percent in July and has made a slightly larger contribution to the index for six consecutive months. With the federal funds rate essentially at zero, the value of this component is seriously in question. Excluding the interest rate spread, the LEI would have fallen in three of the past four months and would have shown much less strength earlier this year. The LEI continues to point to sluggish economic growth, however, with no double dip recession.

Previous: 0.1% **Wells Fargo: 0.0%**

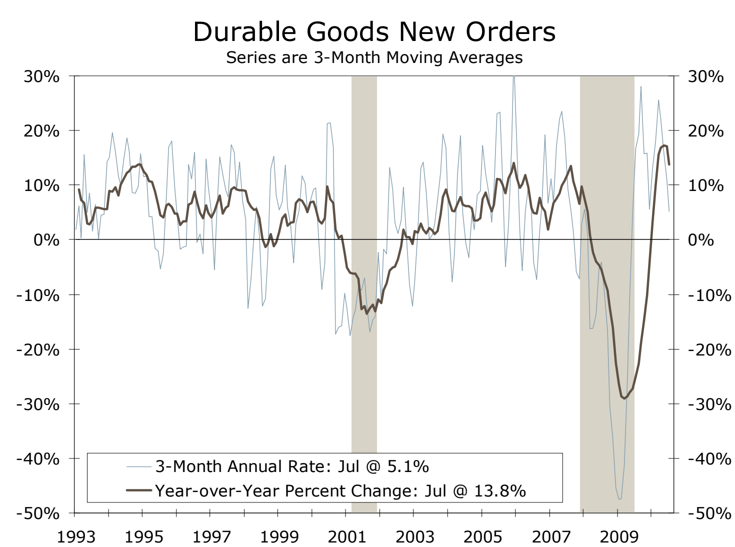
Consensus: 0.1%

Durable Goods • Friday

The manufacturing recovery that fueled economic growth a little more than a year ago is losing steam as global demand slows and the inventory cycle continues to wind down. Advance orders for durable goods rose only 0.3 percent in July, which was less than expected. The modest increase was driven by a 75.9 percent surge in nondefense aircraft orders, which is clearly not sustainable and will likely be retraced in August. We expect durable goods orders will likely fall 1.0 percent in August. The forward-looking series on nondefense capital goods orders (excluding aircraft) dropped 8.0 percent on the month also suggesting further pullback. The trend is more promising, however. On a three-month annualized basis, nondefense capital goods orders (excluding aircraft) were up 19.8 percent, but the pace is slowing.

Previous: 0.3% **Wells Fargo: -1.0%**

Consensus: -0.9%



Global Review

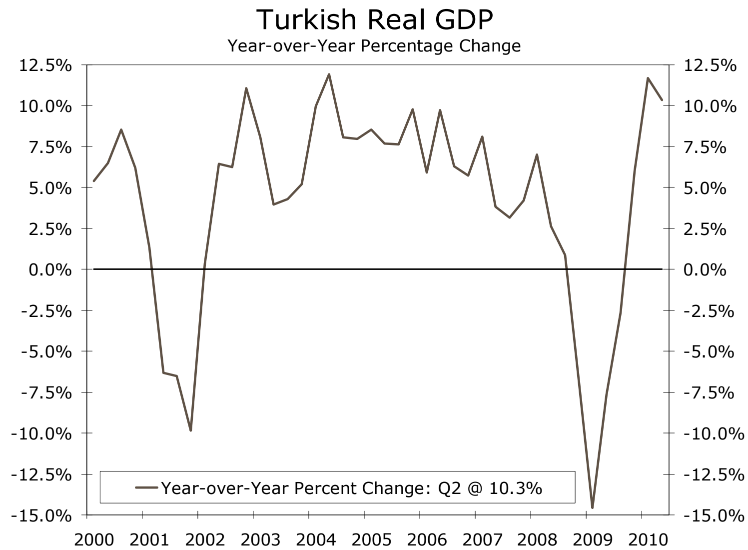
Turkey's Growth Strong; Referendum Passes

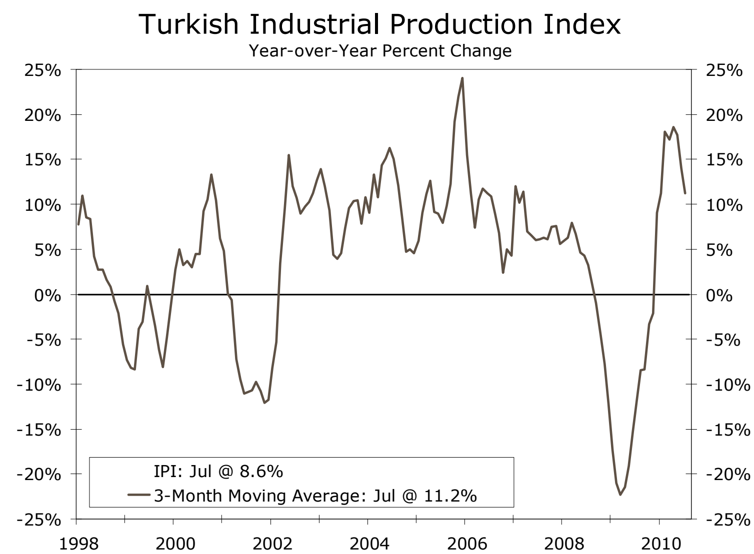
Turkey's real GDP growth softened a bit to 10.3 percent year over year in the second quarter, down slightly from 11.7 percent in the first quarter. Still, growth was better than expected and on par with China's 10.3 percent, which was the strongest among major economies. This is a vast improvement from the depths of the global financial crisis, when real GDP contracted 14.6 percent in Q1 2009. Of course, year-over-year comparisons have been quite favorable of late due to the fact that the economy bottomed during the first half of 2009.

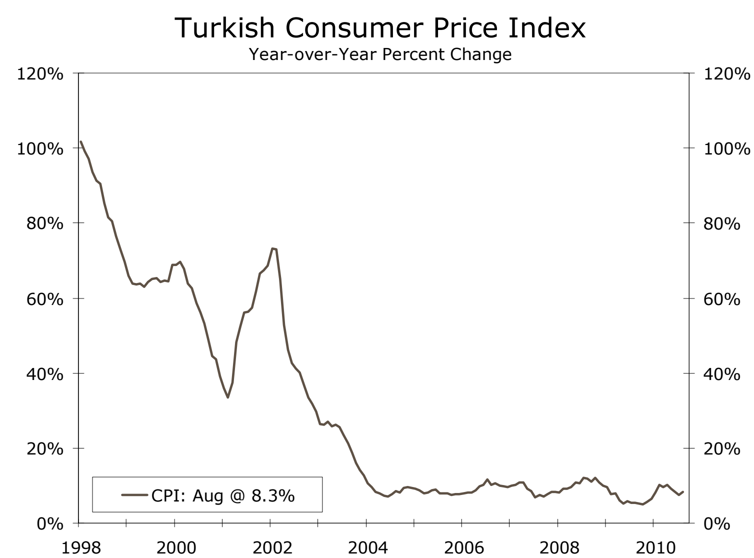
Manufacturing, which accounts for a quarter of GDP, rose 15.4 percent. Construction jumped 21.9 percent while real estate rose 8.2 percent from a year ago. This is in stark contrast to the United States, where the real estate and construction industries continue to struggle in the wake of the housing bust. Transportation and wholesale trade saw strong growth, but slowed a bit from the previous quarter. Mining saw robust growth as demand and prices for commodities have strengthened over the past year as developing nations resumed swallowing up resources. The agricultural industry saw the strongest quarterly second-quarter growth since 2006, and the financial sector continued to improve as the stock market remained strong and bank lending accelerated. Trade was a drag on growth as the resurgent domestic economy and rebound in the lira have fueled a swift turnaround in imports over the past year. Imports have also risen as manufacturers have imported more crude and intermediate goods used in the manufacture of goods for export. While exports were up a strong 24 percent from a year ago in the second quarter, imports were up an even stronger 34 percent.

Despite robust production and domestic demand, inflation has remained relatively contained, coming in at 8.3 percent year over year in August. Like many other foreign currencies, the Turkish lira plunged during the financial crisis. Since March 2009, it has gained back about half of that decline as investor appetite for risky foreign assets has returned. The lira's recent strength has helped to keep inflation low as the rise in imports has increased competition for domestic companies, forcing them to keep a lid on prices. Although there remains some slack in the economy, the capacity utilization rate has trended steadily higher since March 2009 and is near pre-crisis levels. While low inflation has allowed the central bank to keep interest rates extremely low, this rise in utilization, along with a falling unemployment rate and rising consumer confidence, suggests interest rates have likely bottomed. However, there are currently no plans to raise interest rates.

On September 12, the AKP party received a shot in the arm as a referendum increasing the party's powers passed by a wider-than-expected margin. The new amendments would allow the trial of military personnel in civilian courts, give the government more control over judicial appointments, broaden rights for women, children, the elderly and the disabled, and expand the rights of workers to form or join unions. For a more in-depth analysis, please see our report "Turkey Looks Forward" in the "Country Reports" section of our website.





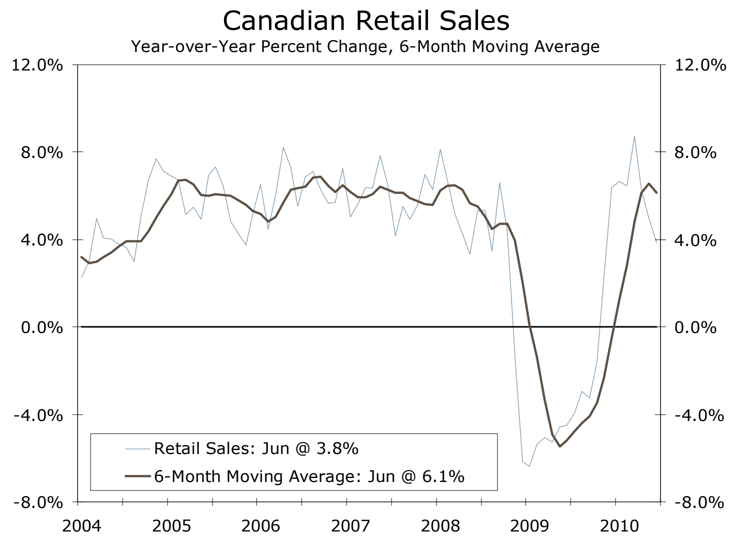


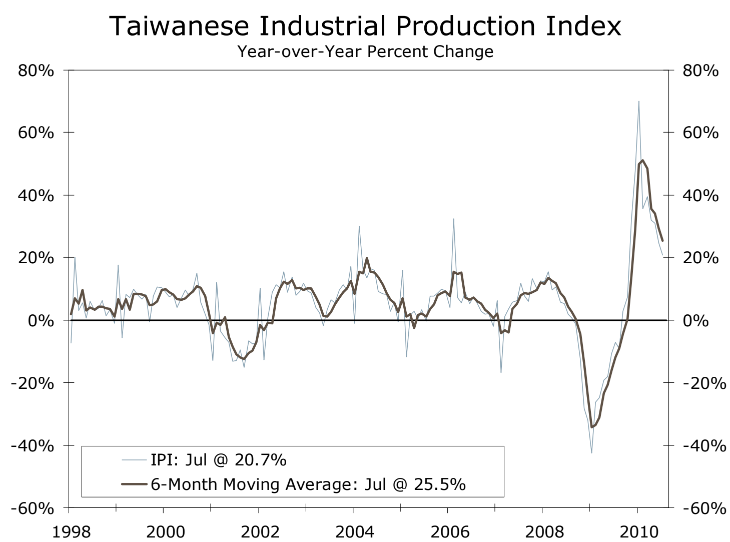
Canadian Retail Sales • Wednesday

Canadian retail sales are expected to rise 0.5 percent in July from the month before. Retail sales rose a modest 0.1 percent in June, which broke a two-month string of sales declines. June sales gains were led by electronics and appliances, furniture stores, and car sales. Retail sales declined in June for general merchandise, clothing, health and personal care, gasoline, and food and beverage. A bright spot in the June data, vehicle sales are expected to rise another 1.0 percent in July. New vehicle sales comprise about 19.0 percent of total sales, so the vehicle market is an important one. The gasoline CPI index also rose 3.5 percent in July, suggesting a significant boost in gasoline station sales. But even excluding autos, Canada's retail sales are expected to rise a solid 0.3 percent. Canada's consumers, unlike their American counterparts, have been aggressively tapping consumer and mortgage credit to help fuel their current spending.

Previous: 0.1% (M-0-M) **Wells Fargo: 0.5% (M-o-M)**

Consensus: 0.5% (M-o-M)





Taiwan Industrial Production • Thursday

Taiwan industrial production for August will help the markets hone their forecasts for global chip demand and the extent of the economic slowdown in China and the rest of Asia. Taiwan's industrial production is clearly slowing down now. Industrial production for July came in slightly below market expectations, rising 20.7 percent from a year ago. Comparisons from a year ago will be more difficult to beat from here on out. There are plenty of economic data that foreshadow another weaker reading from Taiwan's manufacturing in August. The HSBC PMI index for Taiwan fell to 49.2 in August from 50.5 in July, below the 50.0 threshold that signals expansion in manufacturing. Taiwan's export growth narrowed sharply in August slipping to 26.6 percent year-on-year from 38.5 percent in July. Taiwan's leading economic indicators have fallen now for two consecutive months after a 17 month advance.

Previous: 20.7%

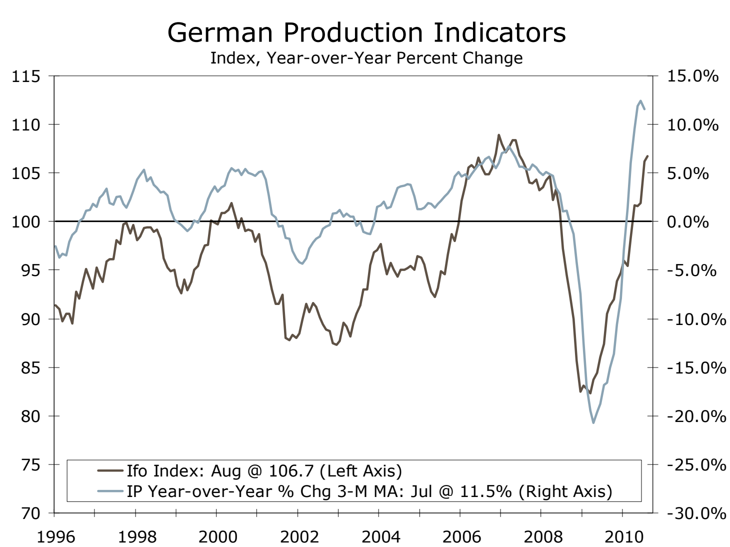
Consensus: 21.98%

German Ifo • Friday

The German Ifo index is a good indicator of current production and GDP growth in Germany. The August Ifo rose more than expected to 106.7. But that is where the good news ends. The forward-looking future expectations component, which tends to lead GDP growth and correlates well with new orders fell in August to 105.2 from 105.6 in July. A marked improvement in manufacturing and retail sentiment paced the gains in sentiment, while confidence in the construction and wholesale sectors waned. Strong readings from German manufacturers point to solid growth in German GDP in 2010. The government recently increased its forecast for German growth this year as economic data imply a stronger-than-expected economic recovery this year. German GDP rose 2.2 percent in the second quarter, the fastest rate since reunification, as companies stepped up investment and exports surged.

Previous: 106.7

Consensus: 106.4



Interest Rate Watch

A Little Chatter But Not Much Else

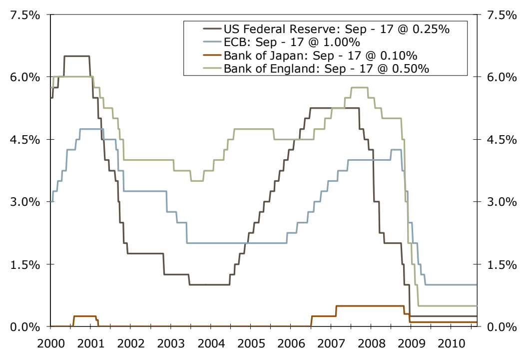
The week began with talk that the yield on the 10-year Treasury was destined to dip below 2 percent, as economic growth slows later this year and the Fed steps up its purchases of Treasuries. Market sentiment appears to have gotten a little ahead of itself and this week's economic reports were certainty not dire enough to justify such a move. Better-than-expected reports on retail sales and weekly first-time unemployment claims helped send yields slightly higher this week, but more moves by the Fed are clearly expected.

The next big test for the Fed will be the September employment report, which will once again likely show an increase in the unemployment rate, possibly to as high as 9.8 percent. The ISM index is also expected to dip down near 50 later this year and a breach of that key breakeven level might be the trigger for more aggressive action by the Fed.

No moves are expected at next week's FOMC meeting. There will likely be plenty of lively discussion on the merits of a second quantitative easing and the minutes that come out two weeks later might provide some interesting clues about what the Fed may do later this year. We continue to believe the Fed will opt for a second round of securities purchases, not so much because it fears the economy is sliding back into recession, but more because it realizes the cost of reversing such a slide is so much greater than what is needed to prevent it.

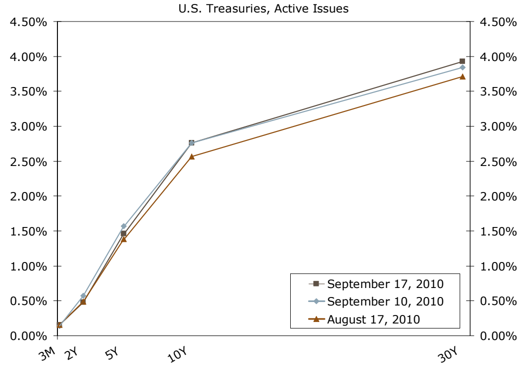
The language in the Fed's policy statement will also likely be changed to indicate a greater level of concern about the current and prospective pace of economic activity. We continue believe it will be very difficult for the Fed to make any major policy changes prior to the November 2 mid-term elections. The next FOMC meeting is not well timed either, with the meeting concluding the day after the election and just before the October employment numbers. At the end of the day, the Fed will do whatever it needs to do. Right now we believe that puts the timing of a second quantitative easing right around Thanksgiving.

Central Bank Policy Rates



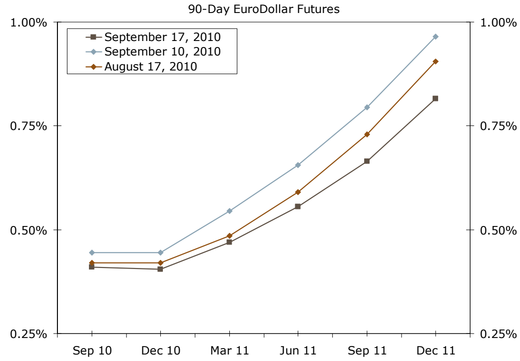
Yield Curve

U.S. Treasuries, Active Issues



Forward Rates

90-Day EuroDollar Futures



Consumer Credit Insights

Is it Much Further?

When going on long trips with children, after awhile they often ask if it's much further. To placate the child one usually answers, "No, it's not much further." Until finally, after getting sick and tired of hearing the same old question, you retort, "Yes, it is!!!" If you're lucky, the children usually don't ask again for quite a while.

Well, here we are, two years after the devastating bankruptcy of Lehman Brothers, and we still have a long ways to go to reach our ultimate destination, which is a return to normal levels of unemployment, delinquency and foreclosure rates, bankruptcies, household debt, bank lending and so on. It seems as though we are traveling through the biggest forest known to man, for we have no idea when we will be "out of the woods." Of course, we have to keep looking for clues, but the search is getting tiresome, and the question is getting old.

Thursday's report on foreclosures from Realty Trac provided little optimism that the end is near. While foreclosure notices were down five percent from a year ago in August, they were up four percent from July. The number of homes repossessed by banks was up a remarkable 25 percent from a year ago and was the most since the start of the mortgage crisis. The number of homes scheduled for auction was also up 9 percent from last August. So on this long journey, it seems that the answer to the question of whether it's much further is, "Yes, it is!!!"

Mortgage Data

	Current	Week Ago	4 Weeks Ago	Year Ago
Mortgage Rates				
30-Yr Fixed	4.37%	4.35%	4.42%	5.04%
15-Yr Fixed	3.82%	3.83%	3.90%	4.47%
5/1 ARM	3.55%	3.56%	3.56%	4.51%
1-Yr ARM	3.40%	3.46%	3.53%	4.58%
MBA Applications				
Composite	801.5	880.0	829.7	592.8
Purchase	183.7	184.5	169.4	272.9
Refinance	4,396.1	4,926.5	4,676.7	2,454.5

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

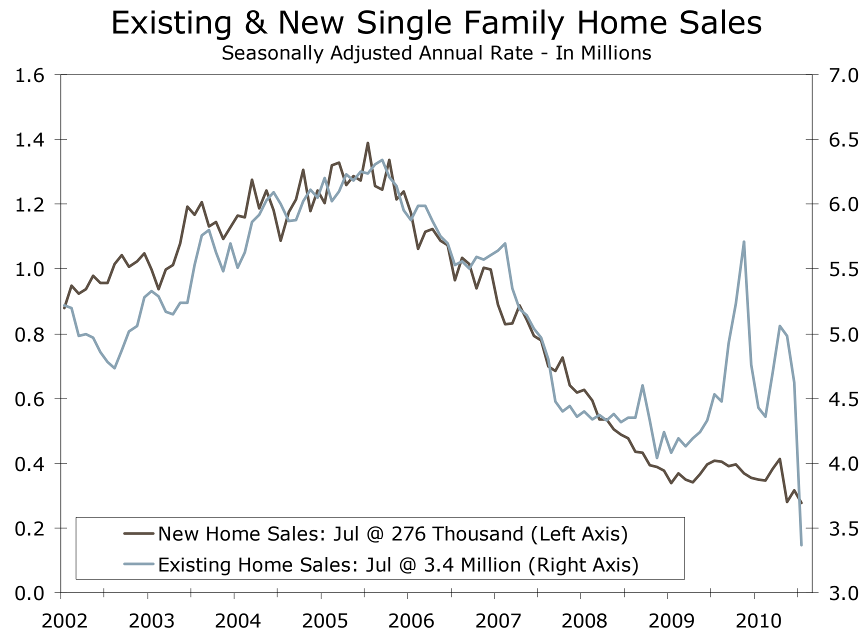
Topic of the Week

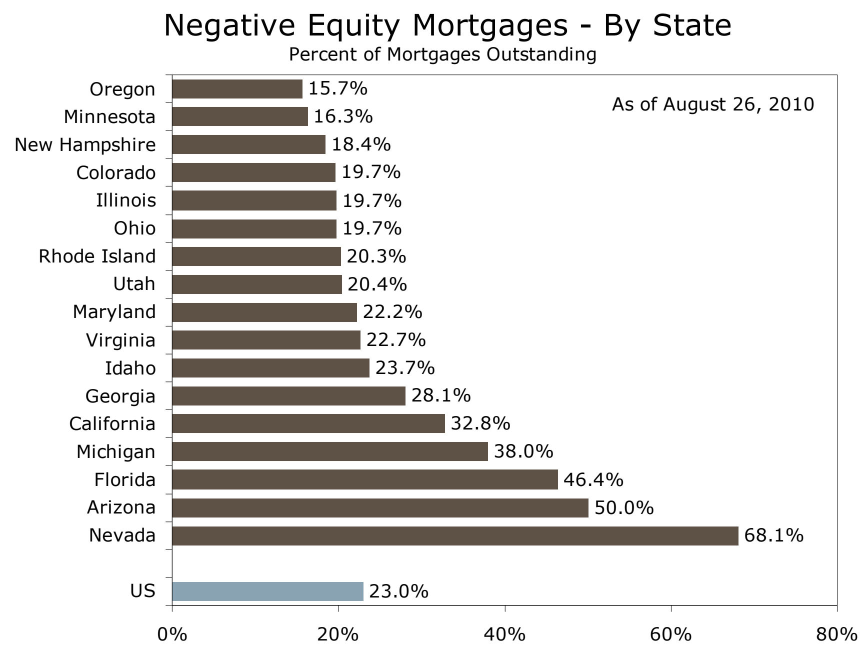
Record Low Mortgage Rates, Still Few Buyers

Record low mortgage rates have not yet produced much of a lift for home sales. Sales of both new and existing homes appear to have risen modestly following their sharp declines in July in the wake of the expiration of the homebuyer tax credits. However, no significant improvement in sales or construction is expected to take place until the spring homebuying season. By then, the economy should have put up a fairly lengthy string of modest private-sector job gains, which should bolster confidence and household formations.

New home construction is being limited by the still-enormous supply of vacant homes for rent and for sale. We continue to believe this measure is the best gauge of the oversupply of housing on the market. The current inventory totals 4.4 million vacant homes for rent and 2.0 vacant homes for sale. The normal inventory would be around 3.2 million vacant for rent and around 1.3 million vacant for sale. As sales recover over the next two or three years, this excess supply will gradually dissipate. During this period, new home construction will likely remain constrained relative to job growth and household formations.

The threat of foreclosures is again taking center stage, with anecdotal reports showing a surge in foreclosures occurring in August. The large number of homes currently in foreclosure and the high percentage of homes with negative equity and/or seriously delinquent mortgages are keeping homebuyers and builders on the sidelines until they better understand the impact of this shadow inventory on prices, appraisals and mortgage underwriting. States like Nevada, Arizona, Florida, Michigan and California, which tend to lead the nation in foreclosures and the share of homes with negative equity, are most at risk for additional price declines during the second half of the year. The prospect of additional price declines is making the appraisal process more perilous and may freeze up the sales process in many challenged markets.





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Market Data ♦ Mid-Day Friday

U.S. Interest Rates

	Friday 9/17/2010	1 Week Ago	1 Year Ago
3-Month T-Bill	0.15	0.13	0.09
3-Month LIBOR	0.29	0.29	0.29
1-Year Treasury	0.28	0.28	0.50
2-Year Treasury	0.46	0.57	0.94
5-Year Treasury	1.43	1.58	2.36
10-Year Treasury	2.73	2.79	3.38
30-Year Treasury	3.91	3.87	4.17
Bond Buyer Index	3.89	3.92	4.20

Foreign Exchange Rates

	Friday 9/17/2010	1 Week Ago	1 Year Ago
Euro ($/€)	1.305	1.268	1.474
British Pound ($/£)	1.564	1.536	1.645
British Pound (£/€)	0.834	0.826	0.896
Japanese Yen (¥/$)	85.770	84.150	91.080
Canadian Dollar (C$/$)	1.033	1.037	1.065
Swiss Franc (CHF/$)	1.009	1.020	1.028
Australian Dollar (US$/A$)	0.938	0.927	0.873
Mexican Peso (MXN/$)	12.797	12.927	13.275
Chinese Yuan (CNY/$)	6.725	6.770	6.827
Indian Rupee (INR/$)	45.840	46.479	48.153
Brazilian Real (BRL/$)	1.716	1.722	1.806
U.S. Dollar Index	81.430	82.698	76.188

Foreign Interest Rates

	Friday 9/17/2010	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	0.83	0.82	0.72
3-Month Sterling LIBOR	0.73	0.72	0.59
3-Month Canadian LIBOR	1.24	1.20	0.50
3-Month Yen LIBOR	0.22	0.23	0.35
2-Year German	0.77	0.74	1.29
2-Year U.K.	0.71	0.74	0.84
2-Year Canadian	1.48	1.47	1.27
2-Year Japanese	0.14	0.15	0.22
10-Year German	2.42	2.40	3.37
10-Year U.K.	3.13	3.13	3.73
10-Year Canadian	2.95	2.98	3.36
10-Year Japanese	1.08	1.16	1.35

Commodity Prices

	Friday 9/17/2010	1 Week Ago	1 Year Ago
WTI Crude ($/Barrel)	73.35	76.45	72.47
Gold ($/Ounce)	1276.30	1246.25	1013.60
Hot-Rolled Steel ($/S.Ton)	545.00	545.00	555.00
Copper (¢/Pound)	350.30	339.70	288.00
Soybeans ($/Bushel)	10.11	10.21	9.43
Natural Gas ($/MMBTU)	4.00	3.88	3.46
Nickel ($/Metric Ton)	23,257	22,744	17,217
CRB Spot Inds.	517.27	511.90	438.12

Next Week's Economic Calendar

	Monday 20	Tuesday 21	Wednesday 22	Thursday 23	Friday 24
U.S. Data		**Housing Starts** July 546K August 535K (W) **FOMC Rate Decision** Previous 0.25% Expected 0.25% (W)		**Leading Indicators** July 0.1% August 0.0% (W) **Existing Home Sales** July 3.83M August 4.0M (W)	**Durable Goods Orders** July 0.4% August -1.0% (W) **Durables Ex Transp.** July -3.7% August 0.6% (W) **New Home Sales** July 276K August 291K (W)
Global Data		**Canada** **CPI (YoY)** Previous (Jul) 1.8%	**Canada** **Retail Sales (MoM)** Previous (Jun) 0.1%	**Euro-zone** **PMI Manufacturing** Previous (Aug) 55.1 **Euro-zone** **PMI Services** Previous (Aug) 55.9	**Germany** **IFO-Business Climate** Previous (Aug) 106.7

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

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