

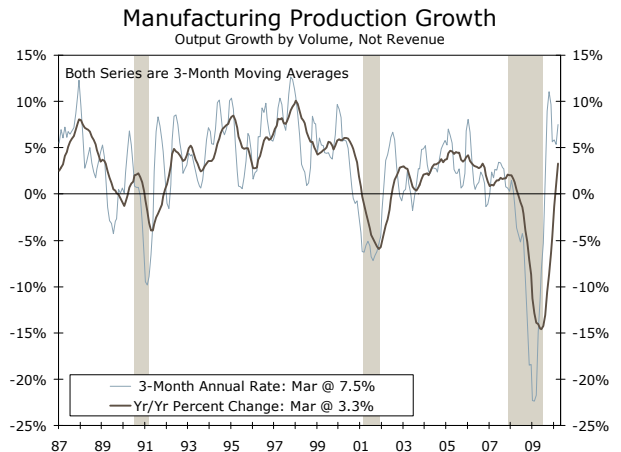
# Economics Group

## Weekly Economic & Financial Commentary

### U.S. Review

#### Good Day, Sunshine

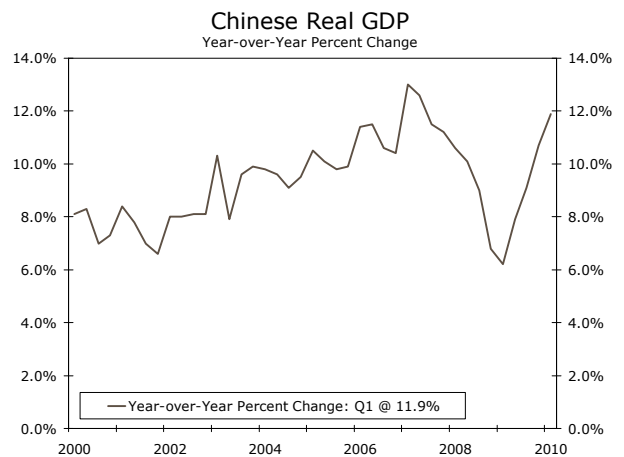
- Continued economic recovery, low inflation and a little help from our friends provide an optimistic tone this week. Retail sales and industrial production, both coincident indicators, suggest that the recovery is in place and there is no double dip.
- This week's data are consistent with our view expressed in the *Annual Outlook*, published December 2009, that the recovery (which we say began in June 2009) will continue but rebalancing in critical areas such as the federal deficit and interest rates will also continue.



### Global Review

#### China Is Booming Again

- Real GDP growth in China shot up to 11.9 percent in the first quarter due to robust growth in domestic demand. Although base effects may account for some of the jump in the year-over-year growth rate, it appears that the economy expanded briskly on a sequential basis.
- The major economic risk in China has shifted over the past year from subpar economic growth to potential overheating. Chinese authorities may soon allow the currency to appreciate again in order to dampen inflationary pressures.



Wells Fargo U.S. Economic Forecast														
	Actual 2009				Forecast 2010				Actual				Forecast	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	2006	2007	2008	2009	2010	2011
Real Gross Domestic Product <sup>1</sup>	-6.4	-0.7	2.2	5.6	3.5	2.2	2.3	2.2	2.7	2.1	0.4	-2.4	3.0	2.5
Personal Consumption	0.6	-0.9	2.8	1.6	2.8	1.5	2.0	2.0	2.9	2.6	-0.2	-0.6	1.9	2.0
Inflation Indicators <sup>2</sup>														
"Core" PCE Deflator	1.7	1.6	1.3	1.5	1.4	1.2	1.2	1.2	2.3	2.4	2.4	1.5	1.2	1.6
Consumer Price Index	-0.2	-1.0	-1.6	1.5	2.5	2.6	2.2	2.1	3.2	2.9	3.8	-0.3	2.3	2.4
Industrial Production <sup>1</sup>	-19.0	-10.4	6.4	6.6	6.5	3.4	3.4	6.5	2.3	1.5	-2.2	-9.7	4.4	5.7
Corporate Profits Before Taxes <sup>2</sup>	-19.0	-12.6	-6.6	30.6	22.0	16.0	10.0	8.5	10.5	-4.1	-11.8	-3.8	13.7	8.0
Trade Weighted Dollar Index <sup>3</sup>	83.2	77.7	74.3	74.8	76.1	75.5	77.5	79.4	81.5	73.3	79.4	74.8	79.4	83.6
Unemployment Rate	8.2	9.3	9.6	10.0	9.7	9.8	10.0	9.9	4.6	4.6	5.8	9.3	9.9	9.5
Housing Starts <sup>4</sup>	0.53	0.54	0.59	0.56	0.60	0.64	0.67	0.71	1.81	1.34	0.90	0.55	0.65	0.82
Quarter-End Interest Rates														
Federal Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	5.25	4.25	0.25	0.25	0.50	3.25
Conventional Mortgage Rate	5.00	5.42	5.06	4.93	4.97	6.10	6.00	6.00	6.14	6.10	5.33	4.93	6.00	6.30
10 Year Note	2.71	3.53	3.31	3.85	3.84	4.20	4.20	4.30	4.71	4.04	2.25	3.85	4.30	4.70

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Forecast as of: April 7, 2010  
<sup>1</sup> Compound Annual Growth Rate Quarter-over-Quarter  
<sup>2</sup> Year-over-Year Percentage Change

Together we'll go far



**U.S. Review**

**Good Day, Sunshine**

It has been a hard day's night, but the signs of sustained economic recovery are in place. Recovery is no longer a forecast. This week we saw solid gains in retail sales and industrial production, while inflation remained low. Yet, financial rebalancing remains a challenge for the federal deficit and financial markets.

**Retail Sales, Industrial Production: Is There Really Love Between New York and Philadelphia?**

Strawberry fields forever seems to be the message from the retail sales and industrial production reports. Retail sales have climbed for the third straight month and are up 10 percent from year ago levels. In March, sales climbed 1.6 percent after a positively revised gain of 0.5 percent for the previous month. 'Core' sales, after stripping out gas, autos and building materials, rose 0.5 percent and are up 7.5 percent at an annualized rate over the first three months of the year. Longer term, consumers will remain reluctant to purchase big-ticket durable items until the labor market improves further. For all of 2010, we expect consumer spending to add to growth but at a pace below historical recovery periods. Industrial production has improved by 7.8 percent over the past three months. While unseasonably warm spring weather has resulted in a decline in utilities output, manufacturing output was strong and has risen more than 7 percent over the past three months.

In separate releases, the New York and Philadelphia Fed came together to suggest the recovery is here. The Empire Manufacturing Index rose to 31.9 with gains in new orders, shipments, number of employees and average work week. The general activity index has been up for the past nine months. Meanwhile, Philadelphia's index came in up for the eighth month with a solid gain in new orders and better credit conditions.

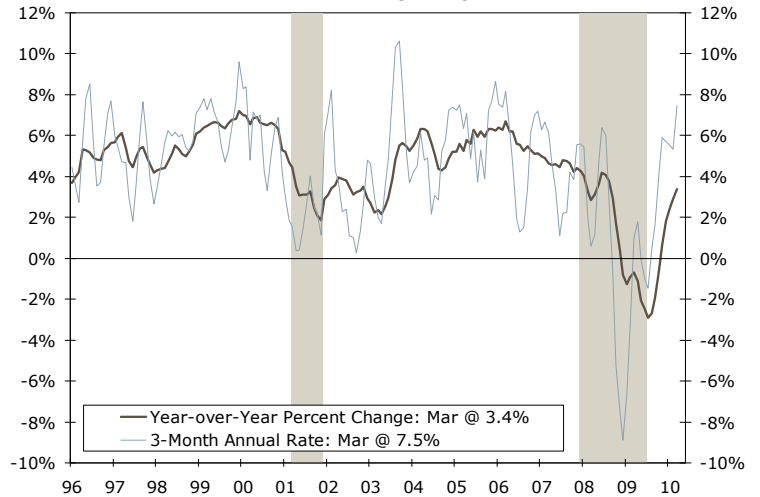
**Inflation: We Used to Worry...**

Headline consumer prices remain well-behaved as overall consumer prices are up just 2.3 percent over the past year, while core CPI is up just 1.1 percent. Medical care remains the long-term challenge, with prices up 3.6 percent over a year ago. Benign consumer price increases should allow the Fed to keep short-term interest rates low.

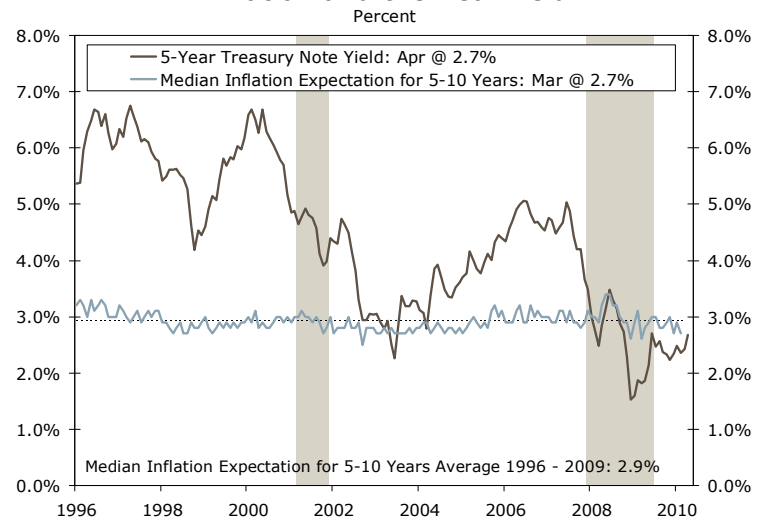
**The Taxman: With Help from Our Friends**

March's budget deficit came in at \$65.4 billion and is anticipated to come in at \$1.4 Trillion for this fiscal year. Meanwhile, the TIC report indicates that foreign investors were big buyers of U.S. Treasuries in February—partly in response to concerns about sovereign debt abroad. Entitlements haunt the longer picture. The consequences of sustained, outsized, deficits are reduced economic growth and decreased financial stability. To avoid this, revenues must increase or outlays must decline. The aging population is a major challenge to reigning in the costs of entitlements. Addressing the tax/spending challenges will help avoid the consequences of prolonged sub-par economic growth and increased instability.

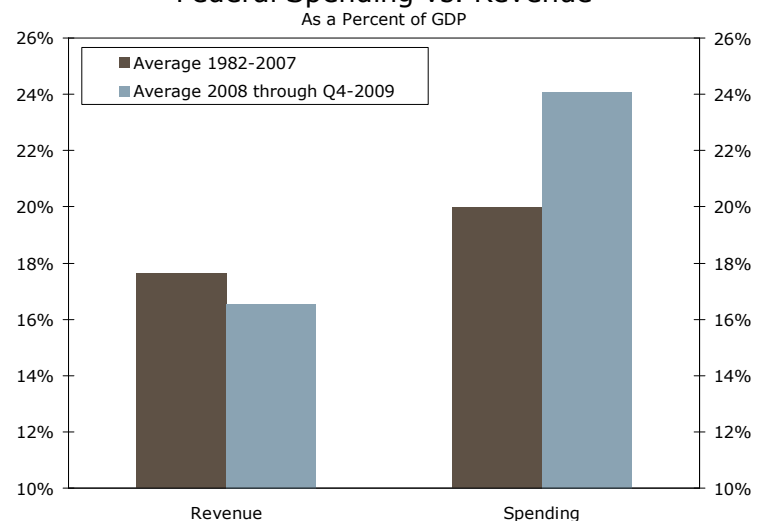
Retail Sales Ex-Autos, Gas & Building Materials  
3-Month Moving Average



Inflation and the Real Yield



Federal Spending vs. Revenue



## Leading Economic Indicators • Monday

Leading indicators will likely post a 1.3 percent gain in March, the largest increase in nine months. The boost will be in stark contrast to the modest 0.1 percent increase posted in February. That less-than-robust February monthly gain was mostly driven by a decline in the average work week. The contraction in the average work week was likely weather-related, which should be reversed in March. Positive contributions will likely be broad-based, and suggest continued economic growth in coming quarters. However, the money supply and consumer sentiment will likely show declines. Orders should be flat. Still, real GDP is expected to grow at a 3.5 percent annual pace during the first quarter and 3.0 percent annual pace for 2010.

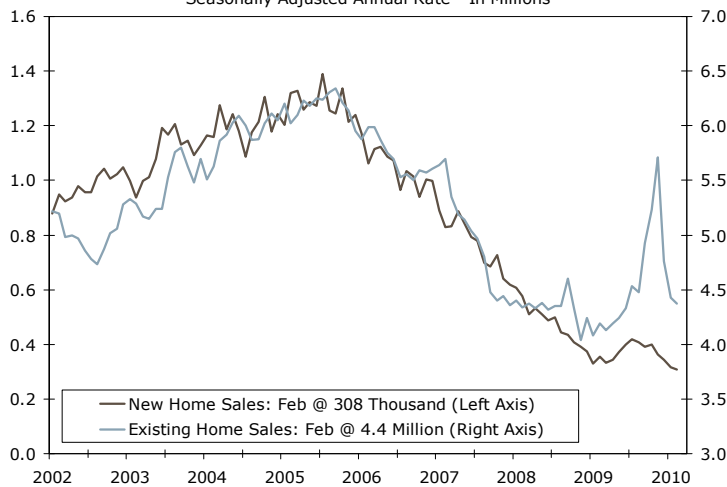
**Previous: 0.1%**

**Wells Fargo: 1.3%**

**Consensus: 1.0%**

## Existing & New Single Family Home Sales

Seasonally Adjusted Annual Rate - In Millions



## Durable Goods Orders • Friday

Advance orders for durable goods rose 0.5 percent in February, the third consecutive monthly increase. The forward-looking series on non-defense capital goods (excluding aircraft) orders is now up 9.3 percent on a three-month annualized basis suggesting further gains in business equipment spending. Most of the gain in February's headline can be attributed to a 4.7 percent monthly increase in machinery bookings. We expect durable goods orders to continue their positive momentum in March increasing 0.3 percent. The headline will likely be held down by a decline in non-defense aircraft due to fewer Boeing orders in March. Shipments of core capital goods suggest capital spending could make another positive contribution to economic growth, but downward revisions like we saw with January's data might cause forecasters to pull back estimates for first quarter economic growth.

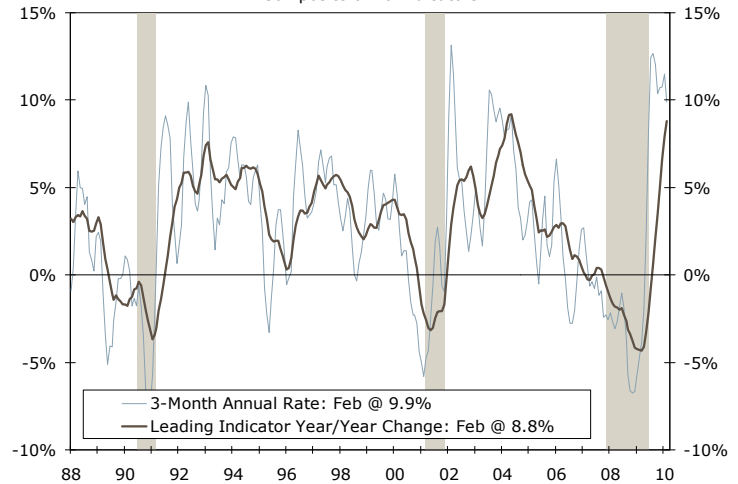
**Previous: 0.5%**

**Wells Fargo: 0.3%**

**Consensus: 0.1%**

## Leading Indicators

Composite of 10 Indicators



## Existing Home Sales • Thursday

Existing home sales have shown signs of weakness in recent months. Sales fell 0.6 percent in February, the third consecutive monthly decline, which boosted the months' supply to 8.6 months. Unseasonably harsh winter weather and the first scheduled expiration of the first-time homebuyer tax credit likely continued to pull existing home sales well below their 6.49 million unit pace in November. We expect sales will remain in the recently established narrow range increasing to a 5.25 million unit pace in March. Sales will likely continue to gain positive momentum in coming months due to the spring home buying season and the second scheduled expiration of the tax incentives in late April. Thereafter, the end of the Fed's mortgage-backed securities purchasing program will likely put upward pressure on mortgage rates making it hard for the housing recovery to regain momentum.

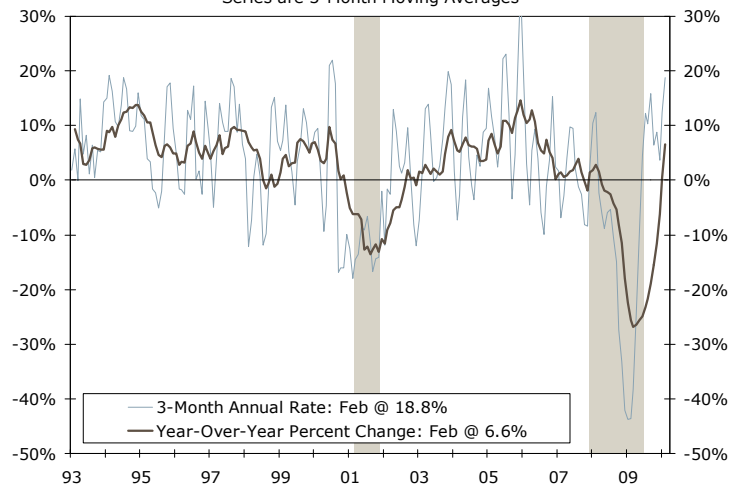
**Previous: 5.02M**

**Wells Fargo: 5.25**

**Consensus: 5.30M**

## Durable Goods New Orders

Series are 3-Month Moving Averages



## Global Review

### Chinese Economy Rockets Higher

Data released this week showed that real GDP in China shot up 11.9 percent in the first quarter of this year relative to the same period in 2009 (see graph on the front page). Yes, some of the strength in the first quarter of 2010 reflects base effects. That is, growth was depressed last year by the sharp global downturn, so the year-over-year comparison today is not very onerous. That said, we reckon that real GDP rose sharply on a seasonally adjusted sequential basis in the first quarter. (Official data are not available on a sequential basis.) In other words, it appears that the Chinese economy is booming again.

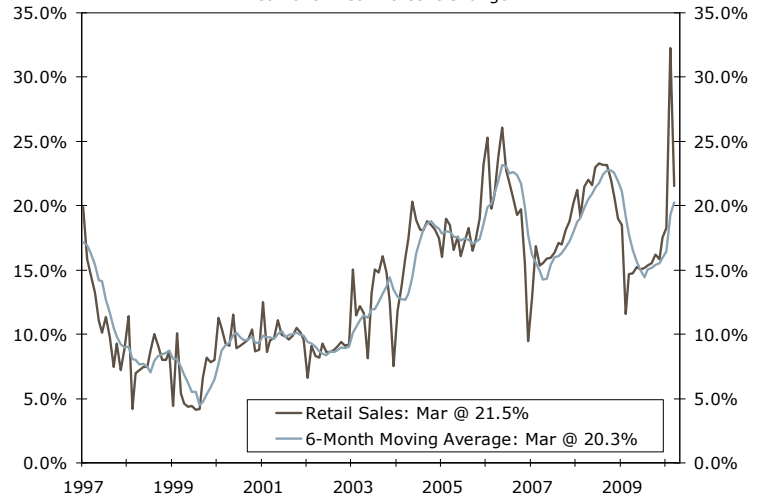
A breakdown of the real GDP data into its underlying demand components is not readily available, but monthly indicators suggest that the acceleration in the economy reflects domestic spending rather than external stimulus. For example, retail spending was very strong, rising 18 percent in the first three months of the year relative to the same period in 2009 (top chart). Fixed investment in urban areas was up 26 percent in the first quarter.

Import growth was also very strong because it is highly correlated with growth in domestic demand. Indeed, China recorded its first trade deficit in six years in March (middle chart). The deficit in March was due in large part to some one-time factors, and surpluses in the trade account will likely return in the months ahead. Nevertheless, net trade appears to have exerted a slight drag on overall GDP growth in the first quarter. That is, real GDP growth would have been even stronger had imports not surged.

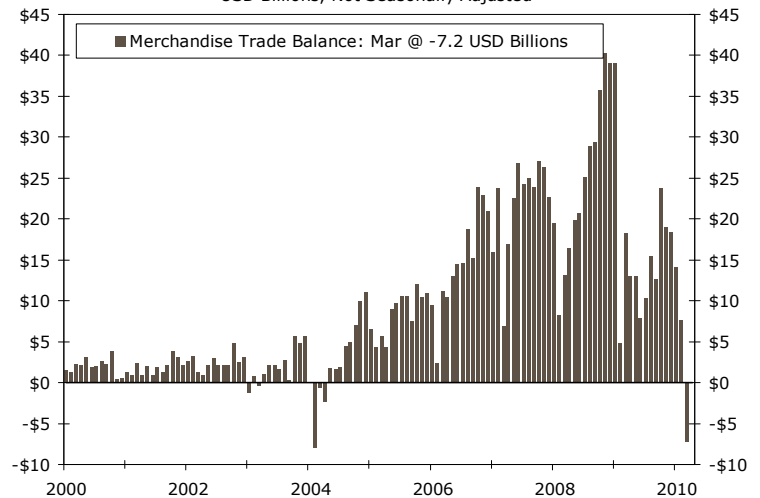
Strong economic growth over the past few quarters has caused CPI inflation to turn positive again (bottom chart). Although some of the rise in inflation recently reflects increases in food prices, which account for one-third of the Chinese CPI, non-food prices have been climbing as well. At only 1.0 percent in March, the rate of CPI inflation excluding food prices is rather benign at present. However, inflationary pressures appear to be building as illustrated by the 5.9 percent increase in the producer price index over the past 12 months. The risks to the Chinese economy have clearly shifted over the past year from subpar economic growth to rising inflationary pressures.

Therefore, Chinese authorities are taking steps to slow economic growth to a more sustainable pace before the economy overheats. A few months ago Chinese officials directed banks to rein in the rampant growth of lending. Voila! Loan growth has slowed sharply to about 20 percent at present from nearly 35 percent at the end of last year. Another way that Chinese officials may try to address budding inflationary pressures in China is via exchange rate appreciation. As we discuss in the Topic of the Week on page 7, exchange rate appreciation helps to dampen inflation directly by reducing import prices and indirectly by slowing down growth in exports. Although a move by Chinese authorities to allow currency strength may not necessarily be imminent, we look for the renminbi to be stronger versus the greenback at the end of the year than it is today.

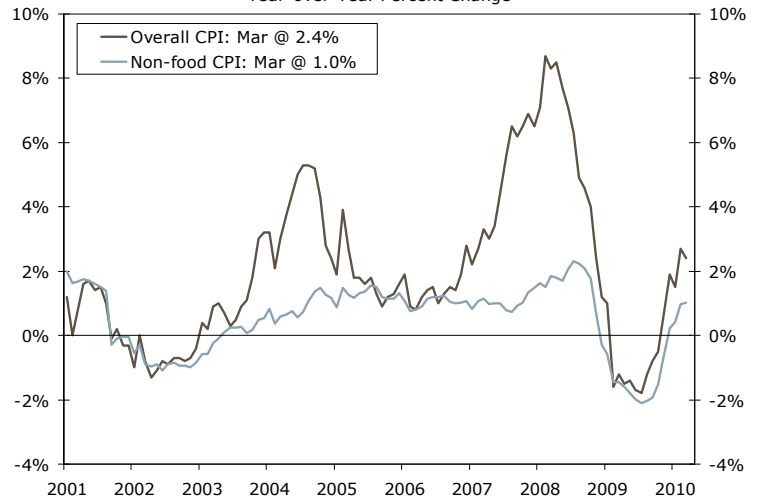
Chinese Retail Sales  
Year-over-Year Percent Change



Chinese Merchandise Trade Balance  
USD Billions, Not Seasonally Adjusted



Chinese CPI Inflation  
Year-over-Year Percent Change



## Bank of Canada Policy Meeting • Tuesday

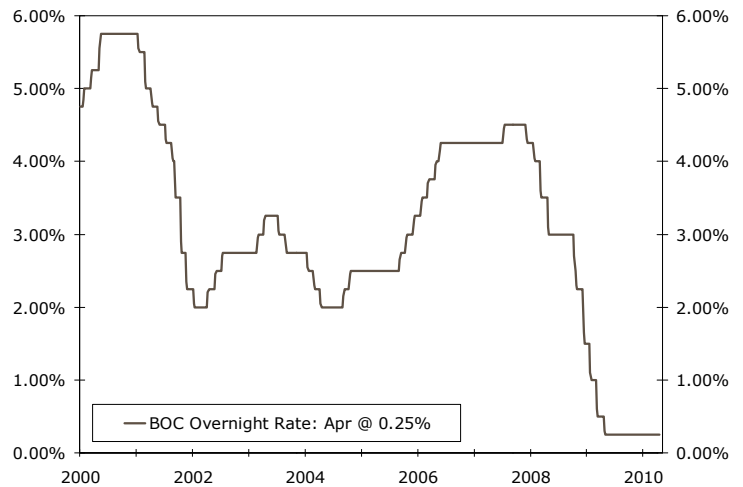
The overnight lending rate in Canada has been 0.25 percent since April 2009. In recent months, the Canadian economy has shown signs of a recovery that has bested most analysts' expectations. While the Bank of Canada (BoC) has maintained an official position of leaving rates unchanged until the end of the second quarter of 2010, BoC Governor Mark Carney made headlines in March when he stated that commitment is "expressly conditional on the outlook for inflation." On Tuesday, April 20, we will get a rate decision from the BoC. While we do not expect a change in the overnight rate yet, market-watchers will look for further comments in the statement about the inflation outlook.

On Friday, April 23, CPI inflation data for March will be released. Given their importance in monetary policy, inflation data will be watched even more closely in months ahead.

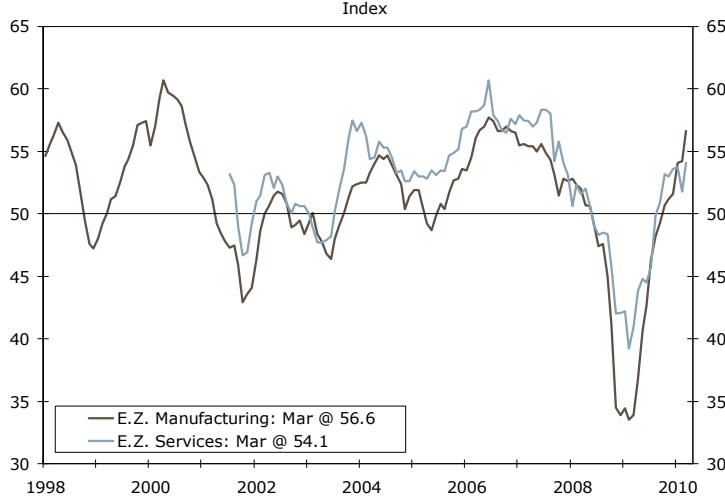
**Current Policy Rate: 0.25% Wells Fargo: 0.25%**

**Consensus: 0.25%**

### Bank of Canada Overnight Lending Rate



### Euro-zone Purchasing Manager Indices



## Euro-zone PMIs • Thursday

Although the purchasing managers' indices have been in expansion territory since last summer, economic activity in the Eurozone has been very weak. To wit, real GDP was flat in the fourth quarter relative to the previous quarter. That said, "hard" data have shown some signs of life recently. For example, industrial production in the Eurozone rose 0.9 percent in February, which follows on the heels of the 1.6 percent increase registered in January. And the sharp increase in the manufacturing PMI in March suggests that industrial production rose further last month. Therefore, investors will be interested to see what the "flash" estimate indicates about the state of the economy in April.

Some individual countries within the Eurozone have data releases on the docket. The business confidence index in France is slated for release as are industrial sales and orders data in Italy.

**Previous Manufacturing PMI: 56.6 Consensus: 56.7**

**Previous Services PMI: 54.1 Consensus: 54.4**

## U.K. Real GDP • Friday

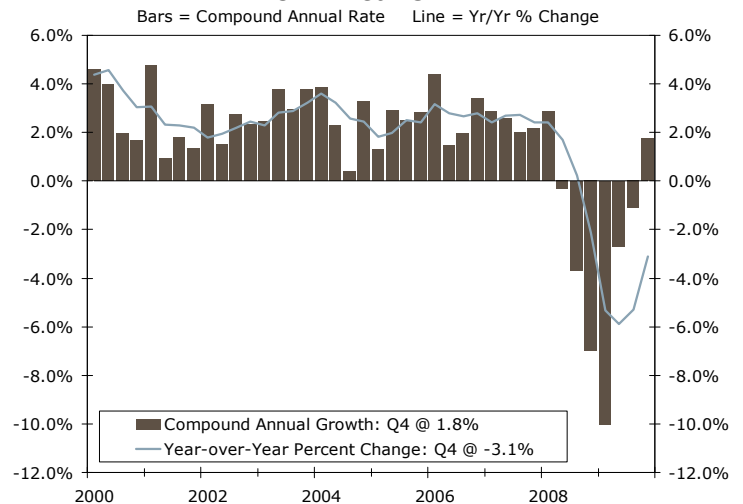
Following the deep recession in 2008-09, the British economy is growing again. On a sequential basis real GDP rose 0.4 percent (not annualized) in the fourth quarter, and the economy looks to have expanded at roughly the same rate in the first quarter. The initial estimate of Q1 GDP growth will print on Friday.

Earlier in the week, we get some more insights into the current drivers of economic growth. For example, retail sales data for March will show how consumers are holding up at present. The employment report will offer insights into the current state of the labor market, and CPI data will tell investors if there are any inflationary pressures in the economy. Finally, the minutes of the Bank of England's policy meeting on April 8 will give some glimpses into the current thinking among monetary policymakers.

**Previous: 0.4% (not annualized) Wells Fargo: 0.4%**

**Consensus: 0.3%**

### U.K. Real GDP



**Interest Rate Watch**

**Rates Evolve as Recovery Matures**

As the news of an emerging economic recovery comes in, the issue for financial markets remains the “normalization” of interest rates and asset prices in a world with limited government intervention. In the search for a new equilibrium, for example, we start with a TED spread that remains remarkably low given the Fed’s generous provision of liquidity. Yet, such low short-term rates are unlikely to persist as the Fed withdraws itself from the market and begins the process of normalization of short-term policy rates such as raising the interest rate on excess reserves.

**Long Rates and Cost of Credit**

Meanwhile, 10-year Treasury rates have risen in recent weeks despite very benign inflation data. This has given way to a very steep 10-year/two-year Treasury spread that appears out of line with expectations of continued economic growth consistent with the patterns of earlier cycles. For spread products, AAA CMBS spreads have come down from their peak but remain well above ‘normal’ ranges. This pattern may, in fact, be the true normalization, as today’s rates are below the Lehman peak and yet above the speculative fury of 2005-2007 period.

**Interdependence: Global Capital Flows and Domestic Fiscal Policy**

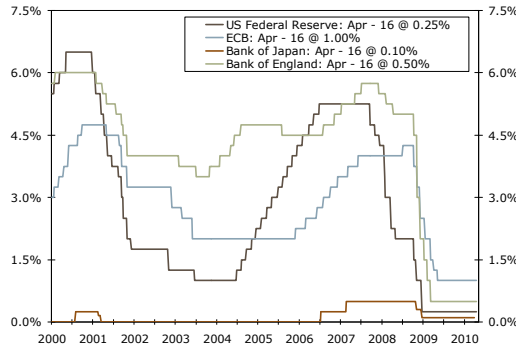
Looking ahead, change will continue particularly in two areas—global capital flows and fiscal policy. At present, global capital flows, reflected in this week’s TIC data and its impact on exchange rates, do not appear consistent with the imperative of rebalancing the global capital markets. Moreover, these flows are interrelated with interest rates and exchange rates in a complex, simultaneously determined, financial system such that a change in one area, such as the Yuan/dollar exchange rate, would lead to changes in global capital flows. Meanwhile, changes in fiscal policy in developed markets, such as the United States, United Kingdom and Greece, for example, dictate further changes in global capital flows and therefore, rates. Interest rates continue to evolve and equilibrium remains a distant dream.

**Consumer Credit Insights**

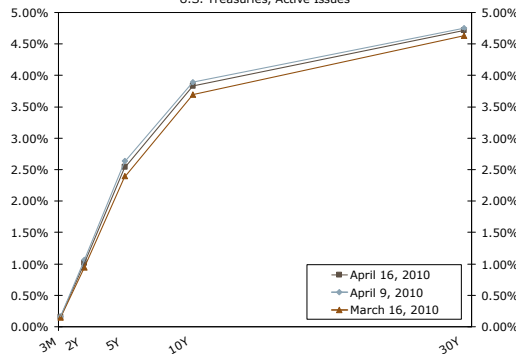
**Housing Starts: The Credit Cap.**

This week’s housing starts report suggest continued improvement in the housing market, yet at a pace that is distinctly below the pace of traditional economic cycles. Year-to-date housing starts are running at a 610,000 pace, and we expect starts to average 650,000 this year. While the improvement in recent months is reassuring the issues of foreclosures, tight credit, a weak labor market and the uncertainty of home price values remain a cap on housing improvement. Foreclosures and tight credit reflect the ongoing revaluation of homes as collateral for banks and as an investment/lifestyle choice for households. Foreclosures continue to rise as these usually lag the business cycle. Yet, the hidden inventory of homes in distress remains a concern. A large portion of the mortgage modifications that have been made in recent years have become delinquent in a relatively short period of time. The likely culprit is the unusually large number of people out of work for six months or more and the large number working fewer hours and receiving less pay. Meanwhile, lending remains tight as many lenders are rebuilding capital, while credit committees remain very wary of the market values assigned to real estate in a highly volatile and uncertain marketplace. With the economic recovery, credit standards will ease as expected income growth rises and job security improves. Yet, housing values remain a challenge particularly in severely overbuilt markets.

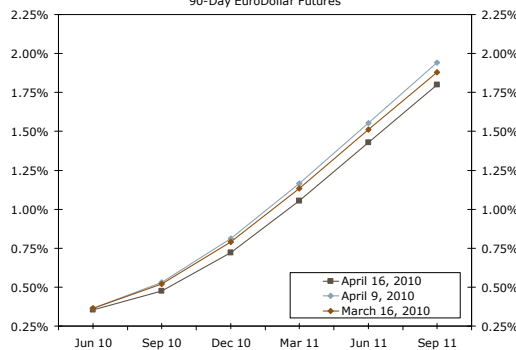
Central Bank Policy Rates



Yield Curve  
U.S. Treasuries, Active Issues



Forward Rates  
90-Day EuroDollar Futures



**Mortgage Data**

	Current	Week Ago	4 Weeks Ago	Year Ago
<b>Mortgage Rates</b>				
30-Yr Fixed	5.07%	5.21%	4.96%	4.82%
15-Yr Fixed	4.40%	4.52%	4.33%	4.48%
5/1 ARM	4.08%	4.25%	4.09%	4.88%
1-Yr ARM	4.13%	4.14%	4.12%	4.91%
<b>MBA Applications</b>				
Composite	484.6	536.3	620.9	1,113.2
Purchase	218.0	243.6	221.5	264.1
Refinance	2,047.1	2,250.6	2,955.9	6,071.7

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

## Topic of the Week

### Is Singapore a Harbinger?

Because Singapore is such a small open economy, net exports play a crucial role in determining economic performance in the city-state. Therefore, the exchange value of the Singapore dollar is the primary policy variable of the Monetary Authority of Singapore (MAS). This week, the MAS announced that it was effectively revaluing its currency, and that it would allow the Singapore dollar to appreciate further going forward. Although the Singapore dollar has now strengthened about 4 percent versus the greenback since early February, further gains in the months ahead seem likely.

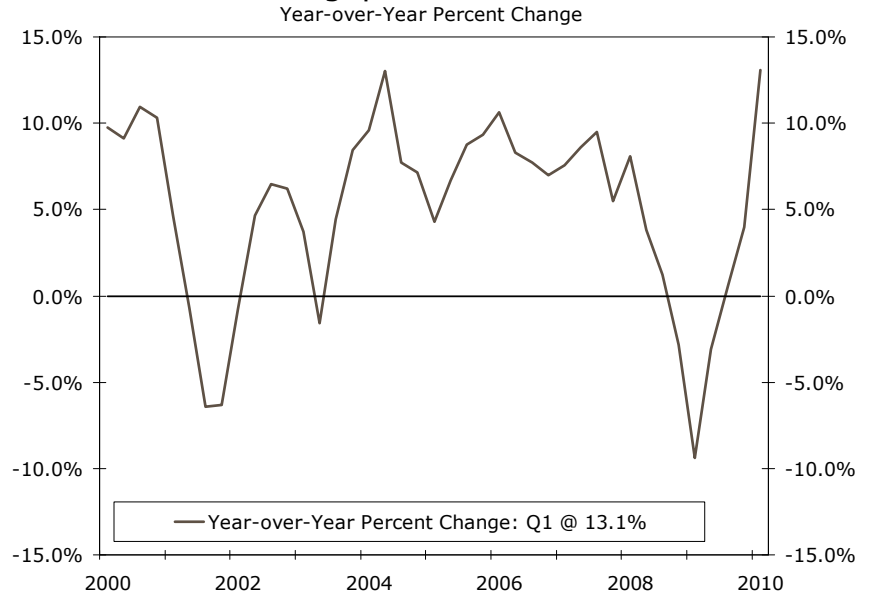
The MAS announced its decision in conjunction with the very strong GDP figures that were released this week. On a year-ago basis, real GDP shot up 13.1 percent in the first quarter of this year. Although CPI inflation is generally benign at present (1.0 percent in February), authorities are beginning to worry that supercharged growth could eventually lead to rising inflationary pressures. Exchange rate appreciation helps to dampen inflation directly by reducing import prices and indirectly by slowing down growth in exports.

Does the decision of the MAS have relevance for other central banks in the region, especially for the People's Bank of China (PBoC)? We seriously doubt that the MAS and the PBoC explicitly coordinate policies. This week's decision by the MAS does not necessarily mean that a similar announcement is imminent from Beijing. That said, the circumstances that led to the MAS's decision to allow its currency to appreciate are similar in China. As discussed in this report, economic growth in China is currently very robust and inflationary pressures may soon become apparent. Therefore, currency appreciation makes macroeconomic sense for China at present. Moreover, Chinese authorities allowed the renminbi to strengthen about 12 percent between mid-2007 and mid-2008 when inflation was an issue. Therefore, it seems very likely that the renminbi will be stronger against the dollar by the end of the year than it is today.

### Singapore Exchange Rate



### Singapore Real GDP



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## Market Data ♦ Mid-Day Friday

## U.S. Interest Rates

	Friday 4/16/2010	1 Week Ago	1 Year Ago
3-Month T-Bill	0.15	0.15	0.12
3-Month LIBOR	0.31	0.30	1.11
1-Year Treasury	0.37	0.42	0.38
2-Year Treasury	0.99	1.06	0.90
5-Year Treasury	2.52	2.62	1.77
10-Year Treasury	3.81	3.88	2.83
30-Year Treasury	4.70	4.74	3.71
Bond Buyer Index	4.43	4.45	4.78

## Foreign Exchange Rates

	Friday 4/16/2010	1 Week Ago	1 Year Ago
Euro (\$/€)	1.353	1.350	1.319
British Pound (\$/£)	1.543	1.537	1.493
British Pound (£/€)	0.877	0.878	0.883
Japanese Yen (¥/\$)	92.530	93.180	99.270
Canadian Dollar (C\$/¥)	1.004	1.003	1.207
Swiss Franc (CHF/\$)	1.060	1.066	1.147
Australian Dollar (US\$/A\$)	0.932	0.933	0.721
Mexican Peso (MXN/\$)	12.174	12.187	13.089
Chinese Yuan (CNY/\$)	6.826	6.824	6.833
Indian Rupee (INR/\$)	44.330	44.294	49.761
Brazilian Real (BRL/\$)	1.750	1.764	2.174
U.S. Dollar Index	80.777	81.093	85.227

## Foreign Interest Rates

	Friday 4/16/2010	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	0.58	0.58	1.41
3-Month Sterling LIBOR	0.65	0.65	1.52
3-Month Canadian LIBOR	0.43	0.42	1.00
3-Month Yen LIBOR	0.24	0.24	0.56
2-Year German	0.90	0.97	1.37
2-Year U.K.	1.15	1.17	1.32
2-Year Canadian	1.93	1.84	1.12
2-Year Japanese	0.17	0.17	0.43
10-Year German	3.11	3.17	3.18
10-Year U.K.	4.01	4.05	3.24
10-Year Canadian	3.70	3.65	2.95
10-Year Japanese	1.35	1.39	1.46

## Commodity Prices

	Friday 4/16/2010	1 Week Ago	1 Year Ago
WTI Crude (\$/Barrel)	83.86	84.92	49.98
Gold (\$/Ounce)	1151.75	1162.00	875.70
Hot-Rolled Steel (\$/S.Ton)	615.00	615.00	410.00
Copper (¢/Pound)	356.20	358.45	218.35
Soybeans (\$/Bushel)	9.69	9.32	10.28
Natural Gas (\$/MMBTU)	4.02	4.07	3.60
Nickel (\$/Metric Ton)	27,165	24,668	12,399
CRB Spot Inds.	512.90	507.27	354.61

## Next Week's Economic Calendar

	Monday 19	Tuesday 20	Wednesday 21	Thursday 22	Friday 23
U.S. Data	<b>Leading Indicators</b>			<b>PPI</b>	<b>Durable Goods Orders</b>
	February 0.1%			February -0.6%	February 0.9%
	March 1.3% (W)			March 0.6% (W)	March 0.3% (W)
				<b>Core PPI</b>	<b>Durables Ex Transp.</b>
				February 0.1%	February 1.4%
				March 0.1% (W)	March 0.5% (W)
Global Data				<b>Existing Home Sales</b>	<b>New Home Sales</b>
				February 5.02M	February 308K
				March 5.25M (W)	March 335K (W)
	<b>UK</b>		<b>UK</b>	<b>UK</b>	<b>Canada</b>
	<b>CPI (YoY)</b>		<b>Unemployment Rate</b>	<b>Retail Sales Ex Auto</b>	<b>CPI (YoY)</b>
	Previous (Feb) 3.0%		Previous (Jan) 7.8%	Previous (Feb) 1.6%	Previous (Feb) 1.6%
			<b>Euro-zone</b>	<b>UK</b>	
			<b>PMI Manufacturing</b>	<b>GDP (QoQ)</b>	
			Previous (Mar) 56.6	Previous (4Q) 0.4%	

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

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