THE FRIDAY BRIEF
A weekly discussion of events and their impact on your investments
BEACON INVESTMENT MANAGEMENT

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# Traction Despite the 'Greece'

Recovery remains firmly on track as revealed by the government's first of three estimates on the growth of US Gross Domestic Product for the first quarter of this year. While a little below expectations, the 3.2% gain is solid and continues on the heels of a 5.6% pace set in the fourth quarter. The six months together comprise the strongest advance since 2003.

Perhaps the biggest news is that consumer spending grew by the most in three years on improving job prospects. Consumer spending, which amounts to more than two thirds of the economy, rose at a 3.6% annual pace last quarter compared to a 1.6% gain in the fourth and the largest since the first quarter of 2007. Spending added 2.55 percentage points to GDP.

On Wednesday the Fed in a 9 to 1 vote held the fed funds target range from zero to 0.25%. Kansas City Fed President Thomas Hoenig dissented against maintaining the "extended period" language for keeping interest rates low fearing the Fed will be hamstrung if it needs to tighten to restrain inflation pressures. However the official statement read "with substantial resource slack continuing to restrain cost pressures and longer-term inflation expectations stable, inflation is likely to be subdued for some time."

Today's GDP report mildly contradicted inflation trends as employment expenses rose 0.6% in the first quarter with benefit costs rising the most since 2007. The rise in the employment cost index followed a 0.4% gain in the final three months of 2009. But for now, the Fed is holding the line on their view that low interest rates are appropriate for an extended period of time due to "low rates of resource utilization, subdued inflation trends, and stable inflation expectations."

The central bank's preferred price gauge, which is tied to consumer spending and strips out food and energy costs, rose at only a 0.6% annual pace, the lowest level since records began in 1959. It was down from a 1.8% increase in the prior quarter.

Home prices show few if any signs of improving soon as indicated by the Case-Shiller unadjusted home price index. It reveals continued weakness as its Composite 10 Index declined 0.6% in February to 156.82 (157.89 first reported). The unadjusted Composite 20 Index fell 0.9%. This report and last week's new home sales data for March point to additional declines. As the major asset for many Americans, declining prices from new foreclosures and distressed sales will dampen confidence.

While recent confidence surveys have suggested weakness, the Conference Board's report this week announced a second straight month of strong advances, up 5-1/2 points in April to 57.9. The gain centered on expectations which jumped 7 points to 77.4, reflecting rising optimism over the outlook for business conditions and easing pessimism on the outlook for employment and income as reported by Bloomberg.

Improvement on the jobs front continues, but at a painfully slow pace. Initial jobless claims fell in the April 24 week to 448,000 vs. 459,000 in the prior week. The four-week average is up 1,500 to 462,500. Continuing claims are down 18,000 to 4.645 million in data for the April 17 week. Early expectations for April suggest a solid improvement.

While much of the economy remains sluggish, the business side is firing on all cylinders. The Institute for Supply Management-Chicago Inc. said today that its business barometer rose to 63.8 this month, the highest level since April 2005, from 58.8 in March (greater than 50 signals expansion).

First quarter earnings continue to surprise analysts. With 305 of S&P 500 companies reporting, 78.4% have been higher than expected, compared to 67.5% for the same period last year. Alternatively, negative surprises are half of what they were last year; 12.5% vs. 24.5%. The share weighted total growth in earnings is 50.2% compared to a decline of 27.1% last year.

The US equity market continues to slough off the bad news particularly that of Greece's and Portugal's credit downgrades and the potential for major economic impact on southern states from a massive oil spill in the Gulf. The MSCI Total Market Index is up 2.75% for the month and 10.5% YTD. The S&P 500 is up 3.3% and 8.25% respectively. Bonds have performed well too. Intermediate Treasuries are up 1.1% MTD and 2.7% YTD, while long term Treasuries are up 2.2% and 2.4% accordingly.

Have a nice weekend



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