



Weekly Economic Commentary

December 1, 2008



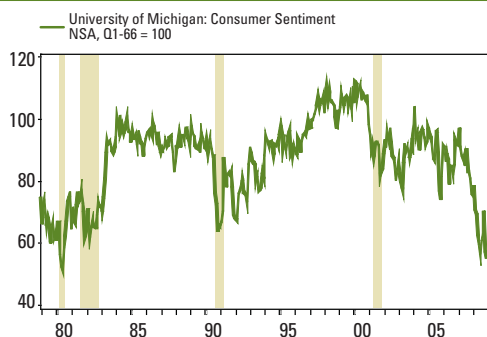
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ECONOMIC CALENDAR

Monday, Dec 1	Chain Store Sales <i>November</i>
Construction Spending <i>October</i>	Factory Orders <i>October</i>
ISM Mfg <i>November</i>	Friday, Dec 5
Tuesday, Dec 2	Private Workweek <i>November</i>
Domestic Car/Light Vehicle Sales <i>November</i>	Average Hourly Earnings <i>November</i>
Wednesday, Dec 3	Mfg Payrolls <i>November</i>
Productivity <i>Q3</i>	Unemployment Rate <i>November</i>
Unit Labor Costs <i>Q3</i>	Nonfarm Payrolls <i>November</i>
ISM NMI <i>November</i>	Consumer Credit <i>October</i>
Thursday, Dec 4	
Initial Claims <i>wk 11/29</i>	

1 Consumer Sentiment Remains Pinned at 27 Year Lows as Consumers Continue to Face Stiff Headwinds



Source: University of Michigan / Haver Analytics 12/01/08

Executive Summary:

Before It Gets Better, It Has to Stop Getting Worse

We “borrowed” the title of this week’s “Weekly Economic Commentary” after seeing a similar phrase used to describe the early reports of the holiday shopping season that kicked off last Friday, November 28. We think the phrase is a good way to characterize what is going on in the overall economy right now, and in particular to describe last week’s batch of economic data.

Financial markets once again headed into last week (November 24-28) with an eye toward trying to gauge the depth and breadth of this recession. Market participants are now comparing this downturn to the severe recessions of 1973-75 and 1981-82, and in some cases to the Great Depression of the 1930s. Right now, our view is that while we are not in a repeat of the Great Depression, this recession could end up being as severe as the 1974-75 downturn, which was second only to the 1981-82 recession in terms of duration and severity.

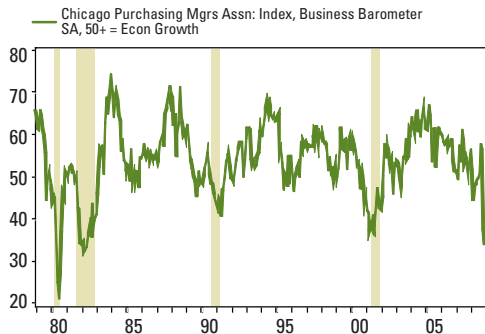
For the second consecutive week, the market was bracing for horrible data for October, but was hoping for some signs of improvement in the data between October and November. The market once again got the horrible data it expected for October, but there were few, if any, signs in the November data that the economy has stabilized. If anything, the data released for November suggests that the economy was even worse in November than it was in October. **Almost across the board, the data released last week was either weaker or worse than expected, and helped to solidify the view that the U.S. economy contracted sharply in the current (fourth) quarter.** In short, the data released last week provided little, if any, hope that the month of November was “better” than October, which led us to choose the title *Before It Gets Better, It Has to Stop Getting Worse*.

The good news is that even though the economy did not “stop getting worse” in November—as evidenced by last week’s data releases—that didn’t stop the U.S. stock market, as measured by the S&P 500, from:

- Posting five consecutive daily gains last week for the first time since July 2007
- Turning in its best weekly percentage gain since 1974
- Achieving the largest percentage gain over five consecutive sessions since 1932!! (Based on the performance of the Dow Jones Industrial Average)



2 Manufacturing Activity in the Midwest Plunged in November to Near 27-Year Lows



Source: PMAC / Haver Analytics 12/01/08

Thus, last week, despite the steady diet of horrible news on the economy in October and November, it seems that market participants may be coming around to our view that the unprecedented amount of fiscal and monetary policy stimulus already in place (and in the pipeline) may indeed be enough to prevent the U.S. economy from sliding into a 1930s' magnitude Great Depression. **On the other hand, last week's equity market rally in the face of another dose of horrible economic data may have just been a coincidence, a rally in a deeply oversold market. It's probably too soon to tell for sure, although this week's batch of economic data will be another huge test for the market.**

The following reports from last week's economic data fit solidly into the "didn't stop getting worse in November" category:

- November consumer sentiment report from the University of Michigan
- November Chicago Area Purchasing Managers Index
- Weekly jobless claims report for the week ending November 22
- November reading on the Richmond Fed's manufacturing index

The October data released last week—all of which was worse than already lowered expectations—included:

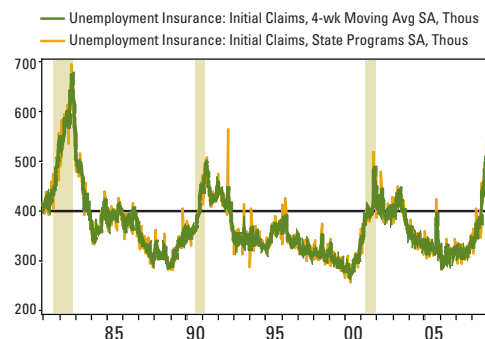
- The dreadful October durable goods orders report
- The abysmal personal spending report for October
- The disappointingly weak new and existing home sales reports for October

Based on the lack of signs of stability (between October and November) in last week's economic reports and the consensus forecasts for this week's key reports (more details below), we are probably still a bit too optimistic in our forecast for real gross domestic product growth for the current quarter. As a reminder, in early November, we wrote that the U.S. economy probably contracted by between 3.0% and 4.0% (on an annualized basis) in the current (fourth) quarter of 2008, as measured by real gross domestic product (GDP). However, last week, in the November 24 Weekly Economic Commentary, we lowered that forecast for Q4 GDP to a drop at the rate of 4.0% or more, in the wake of a slate of spectacularly bad economic reports released in mid November. The Q4 2008 GDP data won't be released until January 30, 2009.

While we continue to remain hopeful that the economy will "stop getting worse" in November, that view is likely to be severely tested this week with the release of many reports on economic activity in November, including:

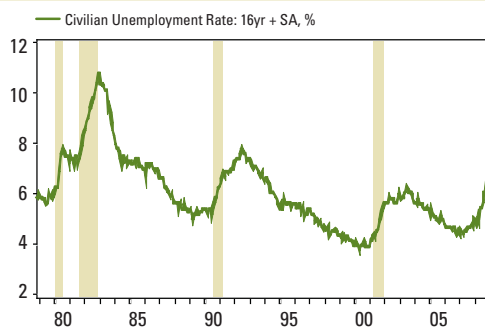
- The November vehicle sales reports
- The Institute of Supply Management's reports on manufacturing and service sector activity in November
- The weekly jobless claims report for the week ending November 22
- The November employment report, which will provide the market with the unemployment rate and nonfarm payroll count in the month of November

3 Jobless Claims Continue to Suggest that the Labor Market is Deteriorating Quickly



Source: Department of Labor / Haver Analytics 12/01/08

4 The November Employment Report Will be a Key Test for Financial Markets



Source: Bureau of Labor Statistics / Haver Analytics 12/01/08



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