

## BCA Market Perspective © January 2011

### The Progress of the Economic Recovery

A year ago, the BCA Market Perspective declared that a U.S. economic recovery had begun. In fact, the domestic stock market achieved double digit returns, outpacing bonds more than two fold during 2010. The spread between corporate and treasury bonds narrowed, signaling more confidence and less risk in the credit markets. These events underscore that stock markets are good predictors of economic growth and recessions.

With 15 million people out of work here at home or nearly 10% of the work force, it appears that a recovery has not really occurred. However, a closer look at the data reveals that private sector hiring increased each month in 2010. GM and Ford are reopening plants and hiring. While the real estate and construction sectors remain depressed, investment and job growth is occurring in manufacturing, healthcare, technology, telecom, agriculture, onshore energy exploration, mining, aerospace, and transportation to name a few. While the unemployment rate has shown little change, it has reached a steady level that will likely improve through private sector job creation. The negative factors include the ongoing government sector layoffs and the steady influx of young people seeking employment.



Source: US Bureau of Labor Statistics

Confidence in the economic recovery is growing among consumers. Domestic retail sales grew in the second half of 2010; e-commerce retail sales in 3Q were +3.9% above 2Q. Seasonally adjusted domestic truck and car sales have increased year-over-year each month since August 2010, driven by improving consumer confidence and newly available credit. The GM initial public offering was over-subscribed, a strong indication of improving sales and profitability. Both Ford and GM are paying down debt faster than anticipated 12 months ago.

The Federal Reserve's \$600 billion quantitative easing (phase two) program is designed to keep the recovery on course in 2011. As more positive economic data is reported and investors move from bonds to equities, the expectation is that bond and mortgage rates will rise. The Fed's backstop approach is to intervene in the bond market, as a buyer, to manage or slow down the speed at which borrowing rates rise.

While inflation expectations receive much media attention, the Fed's priority is to positively influence the recovery. The result of this policy will be job creation and improving aggregate demand; a byproduct being a healthy dose of inflation. In fact, rising commercial and residential real estate valuations would have a profoundly positive impact on the economy resulting in increased tax receipts to municipalities and a slowing of the rate of mortgage foreclosures.

Finally, the U.S. economy is on a steady recovery. Private sector job growth will continue, along with increased manufacturing output and consumer spending. State and local governments will see rising tax receipts and budget pressure relief in 2011 and 2012.



