

WEEKLY MARKET REVIEW

Week ended June 26th

Stocks Mixed Amid Further Signs of Stabilization

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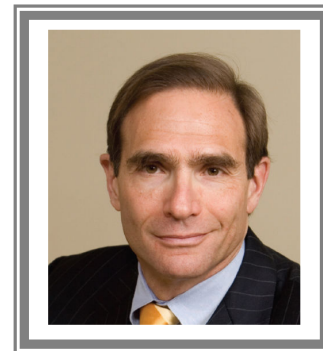
The broad S&P 500 Index ended the week essentially flat and the yield on the 10-year Treasury fell, as the Federal Reserve (the Fed) signaled that it has no plans to raise interest rates any time soon. In the minutes from the latest Federal Open Market Committee meeting, the Fed explained that while the pace of economic contraction appears to be slowing, “economic conditions are likely to warrant exceptionally low levels of the Federal Funds rate for an extended period.” The statement also made clear that the Fed would continue its purchases of agency mortgage-backed securities, agency debt and Treasury securities to help keep rates low and to facilitate borrowing.

The Fed’s statement is consistent with our economic outlook. Despite plenty of reasons for measured optimism about the prospects for a recovery, there is no rush to unwind the stimulus plan or other measures adopted to spur growth. Various inflation indicators, including 5- and 10-year TIPS breakeven rates, show that the market is still pricing in very mild inflation expectations. In addition, as last week’s consumer spending, durable goods orders and existing home sales reports suggest, the stimulus program and low interest rates appear to be having the desired effect of helping stabilize the economy and lay the groundwork for an eventual return to growth.

Personal income and spending rise with stimulus help

Personal income rose 1.4% in May, thanks almost entirely to a one-time Social Security payment of \$162 billion, which was part of the federal stimulus package. Wages and salaries actually fell for the month. **Consumer spending**, by far the largest contributor to Gross Domestic Product, rose a mild 0.3%.

The disparity between income and spending growth pushed the **savings rate** up to 6.9%—far above pre-recession levels. Consumers, nervous about job losses and saddled with high debt, have quickly become more frugal; whether they will stay that way remains to be seen. However, soft consumer demand continues to keep inflation in check. **Core Personal**



Dr. Jerry Webman is Chief Economist for OppenheimerFunds, Inc. In this capacity, Dr. Webman provides strategic viewpoints on the overall financial and economic markets to investment management and the financial advisor and investor communities.

For over 20 years, Dr. Webman has been involved in the investment and economic markets—as a researcher, a financial advisor and a portfolio manager.

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Consumption Expenditures (PCE) inflation was just 0.1% in May, versus 0.3% in April.

As the recession has begun to ease, consumers have adopted a steadily more positive outlook on economic conditions. The Reuters/University of Michigan **Consumer Sentiment Index** rose 1.9 points to 70.8 since its month-end May reading, following a series of strong improvements throughout April and May. The index's expectations component was flat, while the reading on current conditions improved.

Jobless claims move higher amid leveling trend

Initial claims for unemployment benefits rose 15,000 to 627,000 in the week ended June 20, while the prior week's results were revised higher by 4,000. Continuing claims also rose. While the economy continues to shed jobs (and despite the latest rise in claims), the overall rate of job losses appears to be leveling off after having peaked in March.

Durable goods orders rise

In a positive sign for manufacturing, **durable goods orders** grew 1.8% in May after improving by about the same amount in April. Orders for non-defense capital goods rose a whopping 10.0%, and orders for such goods excluding aircraft (a proxy for equipment spending in the calculation of Gross Domestic Product) rose a solid 4.8%. Durable goods orders remain well below pre-recession levels, but the recent improvement is encouraging. I'd caution, however, that while the improvement points to stabilization, it's not necessarily indicative of a return to strong economic growth.

Home sales improve

Existing home sales grew a solid 2.4% in May, but the improvement comes off a low base; the actual number of sales remains relatively low. The supply of unsold homes on the market is still elevated, though it declined somewhat in May. Interestingly, distressed sales made up a lower share of total sales than in recent months—another potential sign of stabilization.

New home sales, which make up only a small fraction of overall home sales, dropped -0.6% in May, with the South responsible for most of the decline. Elsewhere, new home sales generally rose. Sale prices for new homes jumped by over 4% in May but are still down 7% over the past 12 months.



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Oppenheimer funds are distributed by OppenheimerFunds Distributor, Inc.
Two World Financial Center, 225 Liberty Street, New York, NY 10281-1008
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JGK-1-6-29-09 June 29, 2009



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