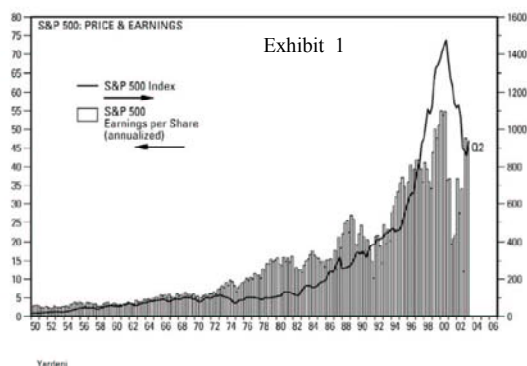


## Help Wanted

A combination of fresh economic data suggesting that the economy is on the move has impacted the markets as one might expect. The stock market, still clawing its way back from the lows hit in 2002, moved higher on a combination of positive economic data and perceived global stability, and approached levels of about two years ago. Interest rates moved sharply higher off the lows reached in June 2003 as deflation concerns faded, pushing bond prices lower through the end of August, and approached levels of about 18 months ago. From the end of June to the end of August, the price of the 10-year U.S. Treasury bond dropped by about seven percent, and the S&P 500 index rose by about 2.5 percent. These moves took a few steps back in September, as some of the new orders data came in mixed, and helped push both interest rates and the stock market lower. For the quarter, the S&P 500 finished up 2.20 percent, and the 10-year U.S. Treasury finished down 1.87 percent.

We have seen the underlying economic data improve over the last 12 months and, as expected, have seen the headline data improve over the last three to four months as well. As a result, the directions of the move in both the S&P 500 stock index and longer-term interest rates have been consistent with our views. The reason for the sharp move upward in interest rates is rather complicated because there was a combination of factors at work. The safety premium built into U.S. Treasuries unwound as the perception that the world is a safer place, both economically and geopolitically, increased. Expectations of economic growth and increased deficit spending fueled future inflation fears, and mortgage-backed investment pools sold long-term bonds to keep their expected maturities in-line as mortgage refinancing activities are expected to slow. These factors combined to push interest rates higher and, of course, bond prices lower in rather short order.

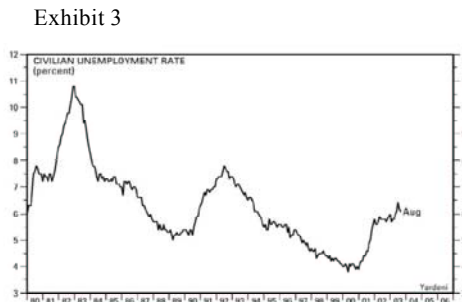
We are generally happy with the economic data being reported, as they support our view that the economy is on the rebound. There are bound to be some hiccups in both the economy and markets along the way, but we are moving in the right direction.



Some interesting data caught our eye when we compared the price of the S&P 500 index with the earnings per share of the S&P 500 index. Exhibit 1 indicates that the price of the market (depicted by the line) was a little ahead of itself in the late nineties, and when earnings (depicted by the bars) failed to materialize, the price index fell. We have recently experienced an earnings recovery, and if trends continue to improve, we could be seeing the early stages of a longer-lasting recovery for corporate America. If so, earnings would ultimately push the stock market higher over time.

While we have previously stated that the building blocks are in place to support economic growth, a few more pieces of the economic puzzle need to fall into place to give our economy firmer footing.

One of those basic pieces, still missing in action, is employment. New and continuing claims for unemployment are at rather high levels for a lasting economic recovery. Exhibit 2 shows the number of people receiving unemployment benefits skyrocketed at the end of 2000, and is currently at higher levels than the during the last recession. The good news is, while the percentage of people unemployed



(Exhibit 3) is high, it is still lower than levels of the last recession. Other data show that job creation is moving at a much slower pace than our last two economic recoveries. If the good times are to continue, we need to create more jobs, which will give additional confidence to those with jobs, and new income to those without. Granted, employment data is a lagging indicator, but we would like to see some confirmation at the employer level that businesses have the confidence to add to their payrolls.

We have previously discussed the other pieces of the puzzle that are important to this recovery: new orders and capital spending from businesses. With the exception of August reports on durable goods orders and Chicago Purchasing Managers Index auto-sector related decline in orders, new orders data has been improving. The Philadelphia Federal Reserve indicated that new orders in that region hit a 45-month high last month, and the September National Institute for Supply Management data on new orders hit a nine-month high as well. Durable equipment spending has turned up (while only modestly) as well this last quarter.

These two pieces of economic data are important, as these are key components for quality economic growth in the future. Others are also watching this data, and the markets will likely continue to trade on economic data for some time, as economic activity contributes to the earnings capability of most businesses and individuals.

**Stephen J. Taddie**  
**October 3, 2003**