

U.S. Economic Trends

October 2012



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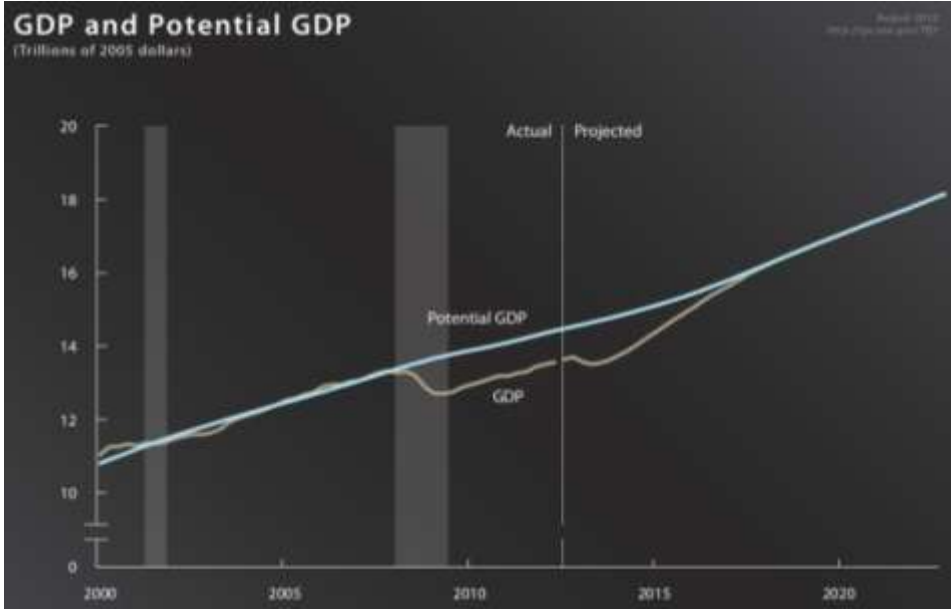
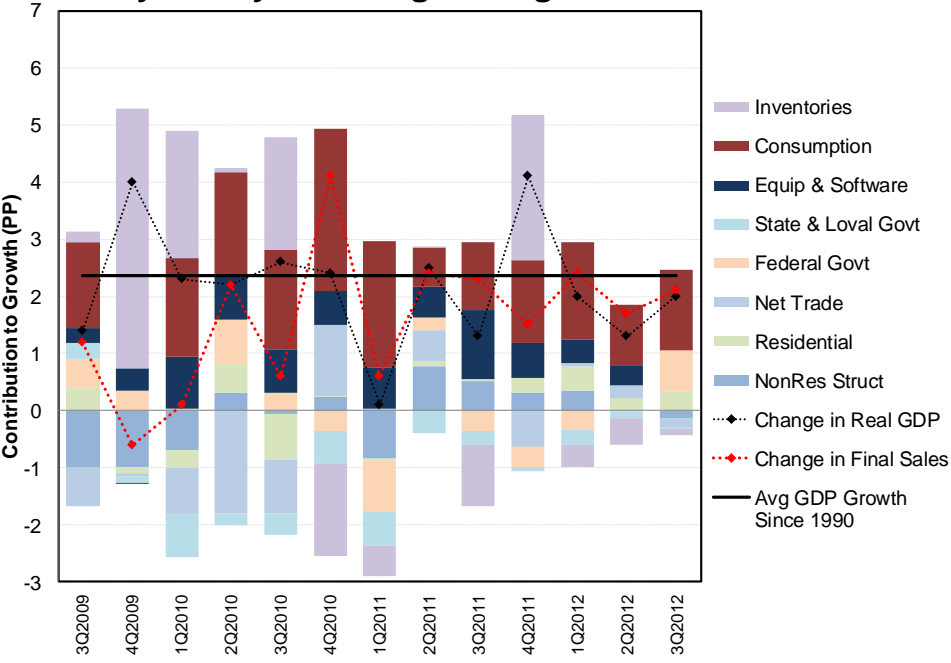
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 - Signs Of Recovery Abound In Builder Sentiment, Permits/Starts, & Home Prices**
 - Still Some Impediments From Weak Labor Market, Tight Credit, & Shadow Inventory**

U.S. Economy

U.S. Economy Continues Slow Growth

Recovery Barely Matching Average GDP Growth

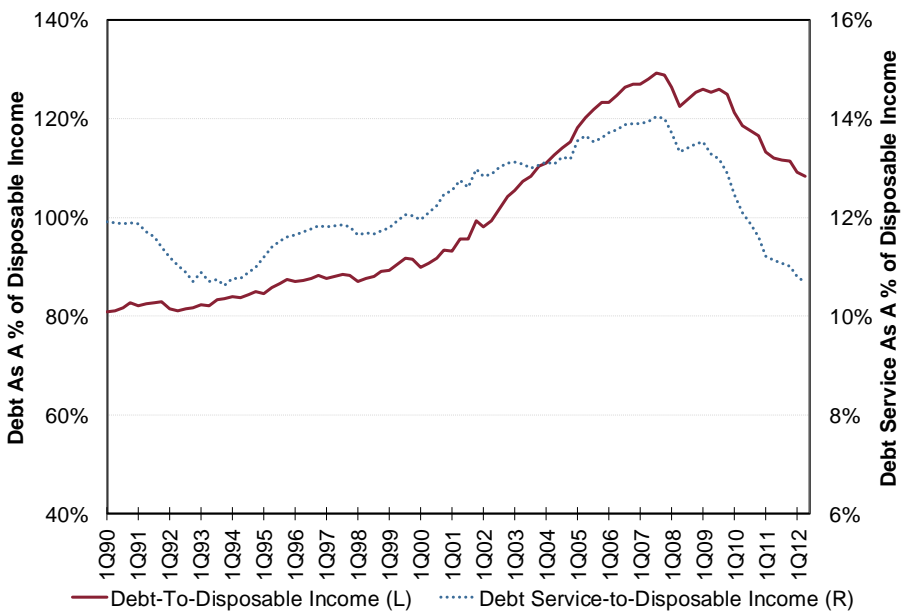


Economic Growth Failing To Return U.S. To Previous Potential GDP Path; Efforts To Restore Long-Term U.S. Fiscal Health Assume Rosy GDP

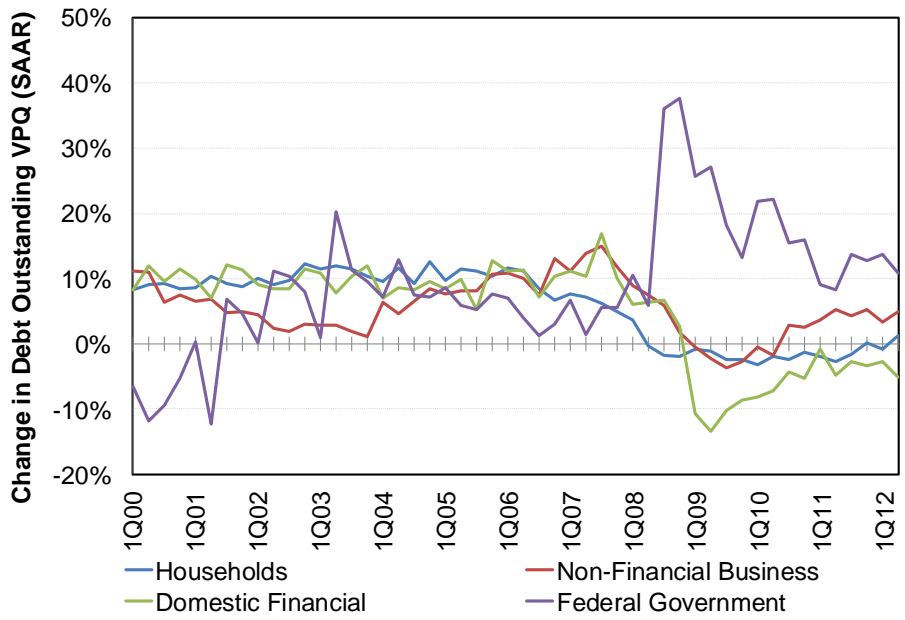
Source: BEA, CBO

Recovery Impediment: Leverage Lacking

Household Debt Stabilizing As FOMC Lowers Payments



Households Nearly Through Slow Deleveraging



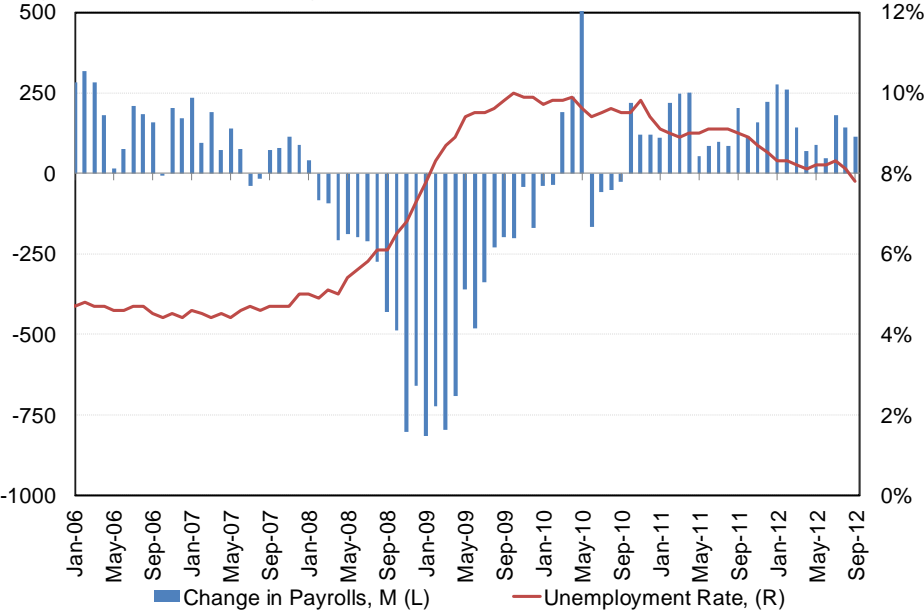
Without Leverage It Is More Difficult To Initiate A Virtuous Cycle Within The Economy

Source: BEA, Federal Reserve Flow of Funds

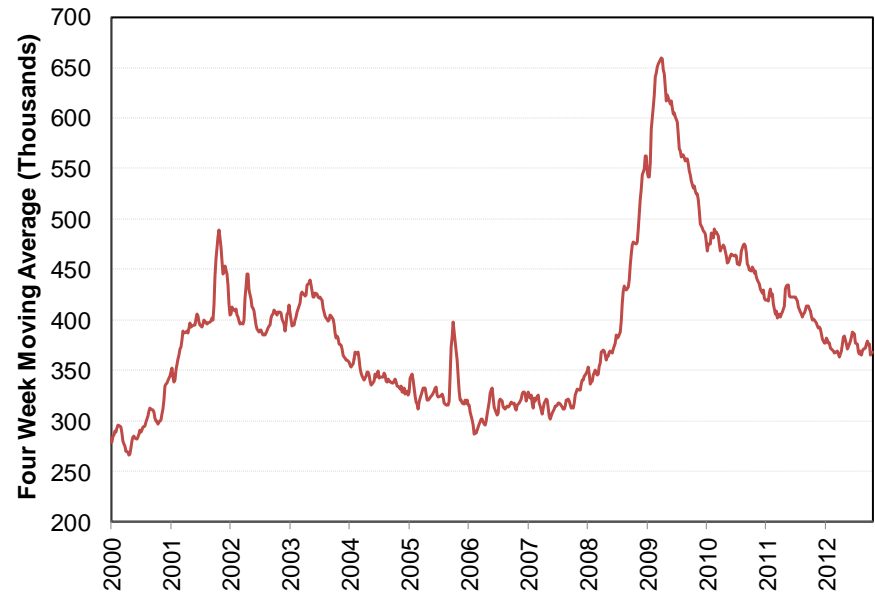


Labor Market Recovers From Spring Swoon

Payrolls & Unemployment



Initial Claims



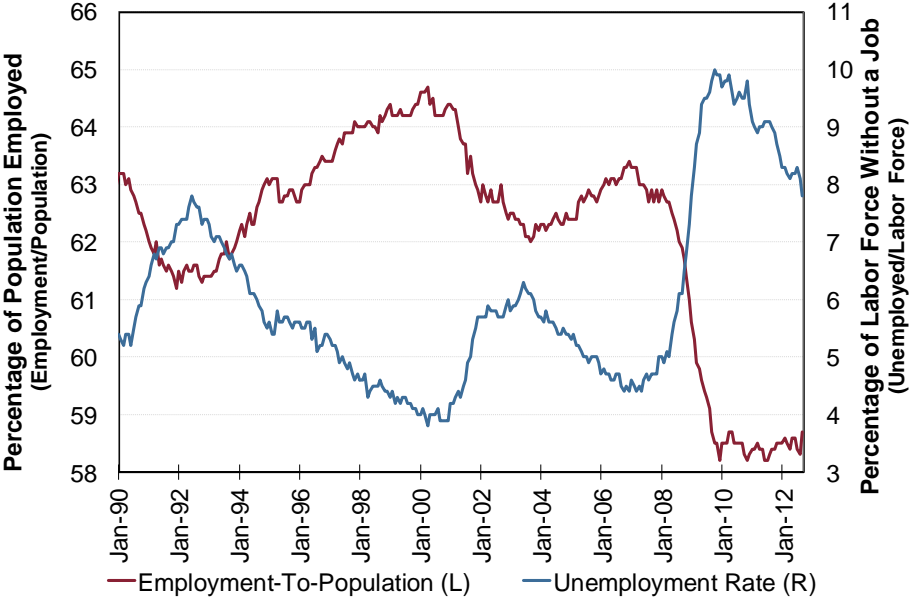
**Payrolls Growth Averaged 146K in 3Q After Dipping Below 100K In 2Q
Initial Claims Have Levelled Off In 2012**

Source: BLS

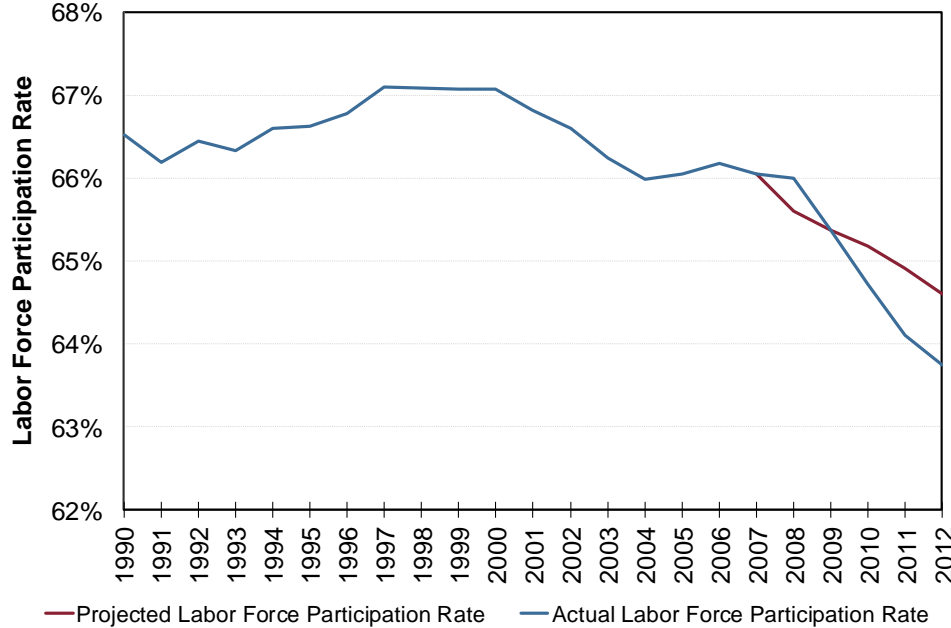


Unemployment Rate Masks Scale Of Problem

Employment-To-Population Has Barely Budged



Decline In Labor Force Is Beyond Demographic Trends



**Employment Growth Is Still At A Weak Level
Expect Fed Accommodation To Continue & Potentially Expand**

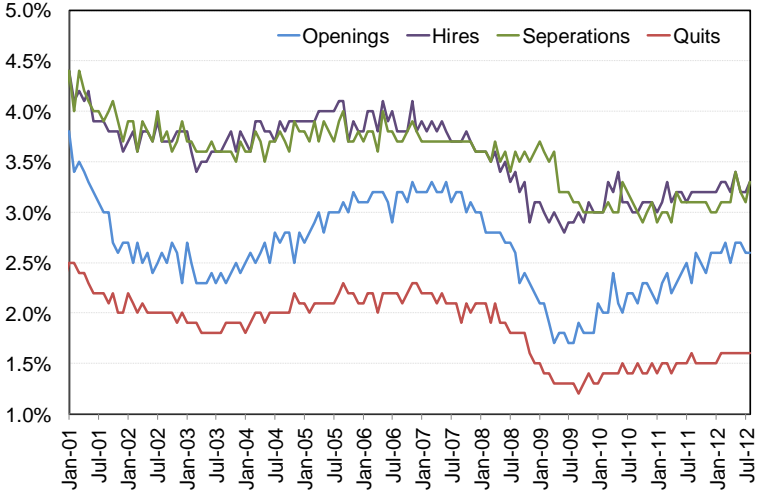
Source: BLS



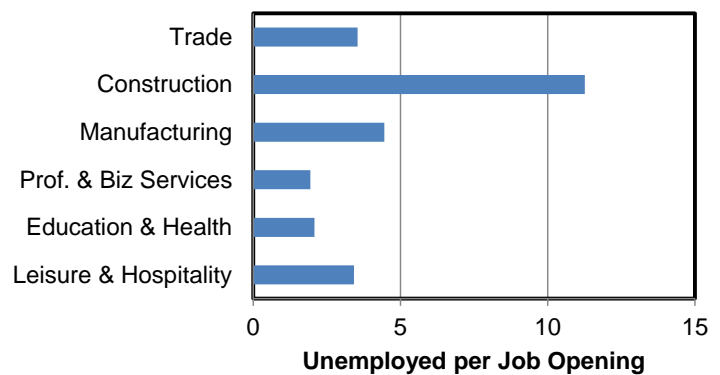
Skills Mismatch Hinders Economy

Job Openings Still Trending Up

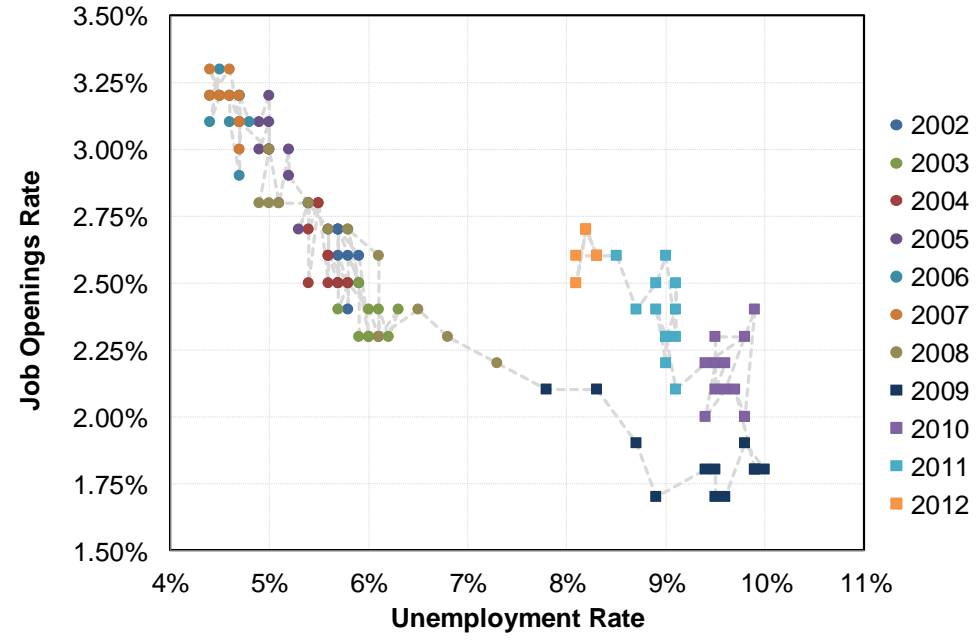
But Hiring Remains Weak



August 2012 Breakdown



Poor Matching Of Openings and Skills Persists

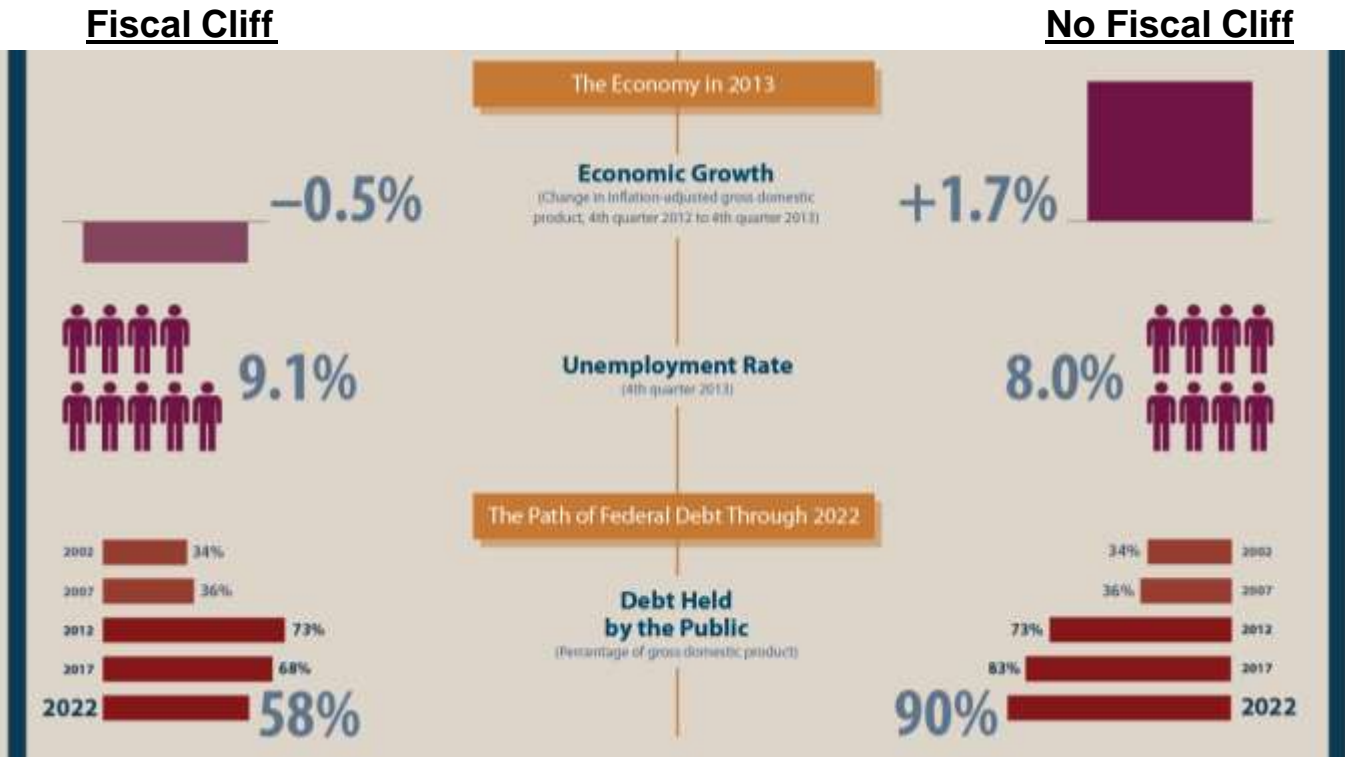


**Economy Held Back By Mismatch Of Skills And Opportunities
Housing Boom Skewed Incentives In Developing Skills**

Source: BLS

Challenges Ahead

Uncertainty 1: Fiscal Cliff



Fiscal Cliff Composed of Bush Tax Cuts (\$280B), Payroll Tax Cut (\$125B), Automatic Budget Cuts (\$98B), & Extended Unemployment Benefits (\$40B)

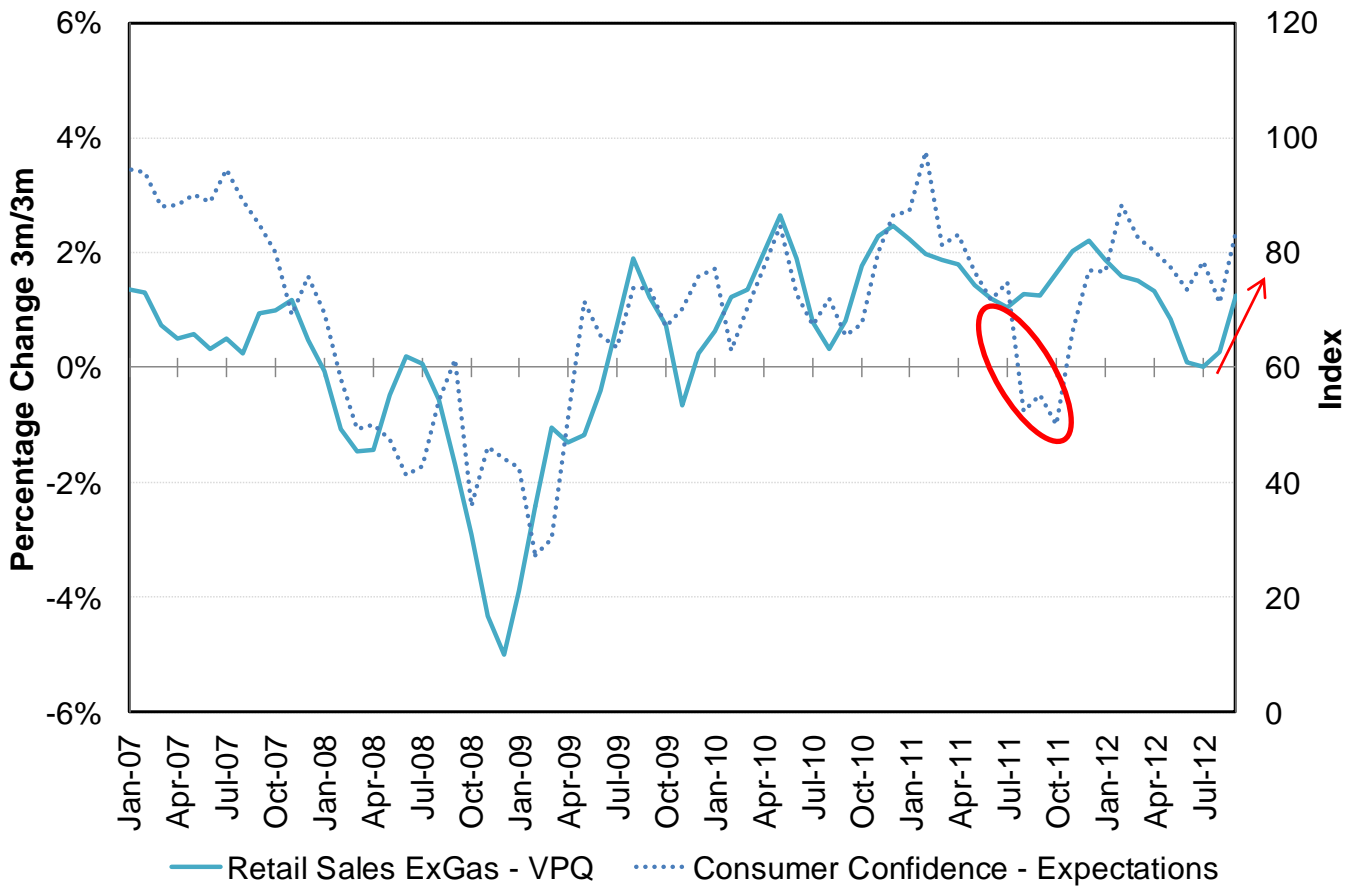
Tax Hike for Middle Income About \$755, Impact More Severe on Lower & Upper Income Households

Fiscal Cliff = Recession

Source: CBO, JPMorgan, Tax Policy Center

Consumption Continues Unabated For Now

Retail Sales vs Consumer Confidence



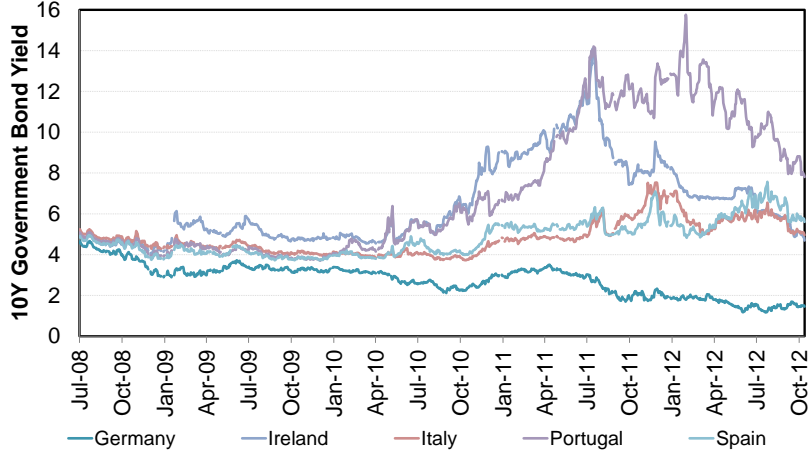
**Despite Looming Tax Increase, Consumers Have Remained Optimistic
Bickering By Congress After The Election Could Harm Spending**

Source: Federal Reserve, Census, Conference Board

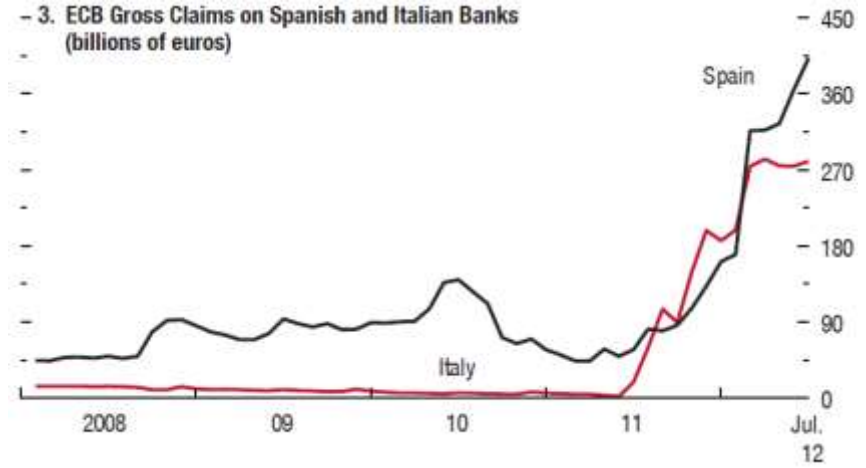
Uncertainty 2: Global Growth/Europe

While Reduced, Yields Remain Elevated For Spain & Italy

European Government Bond Yields



Banks in Spain and Italy Leaning On ECB

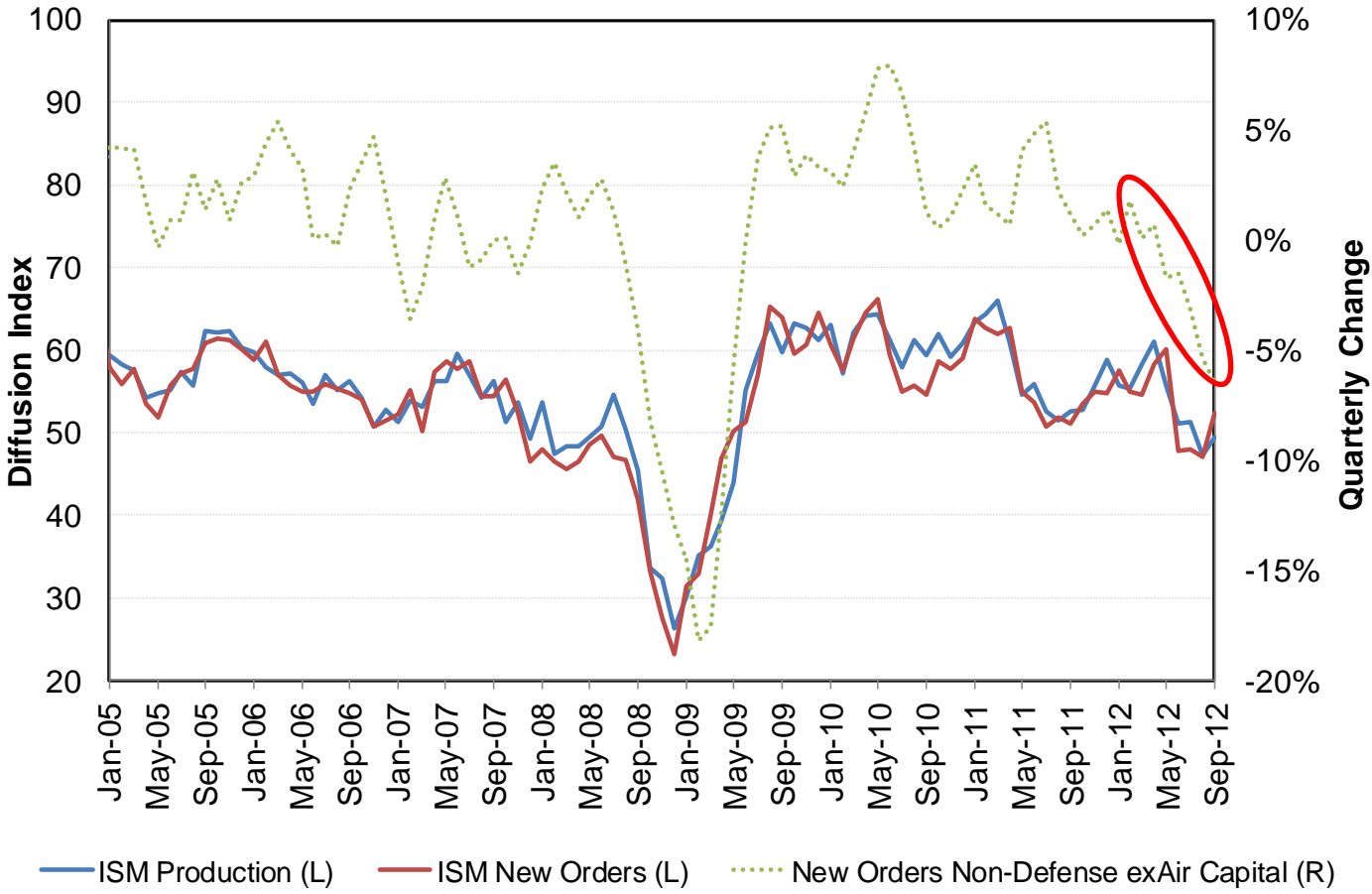


European Financial Crisis And Slowing Global Growth = Fewer Export Oriented Jobs + Concerns About U.S. Banks' Exposure

Source: IMF/World Bank, JPMorgan

Businesses Slow Investment

Uncertainty Saps Business Investment



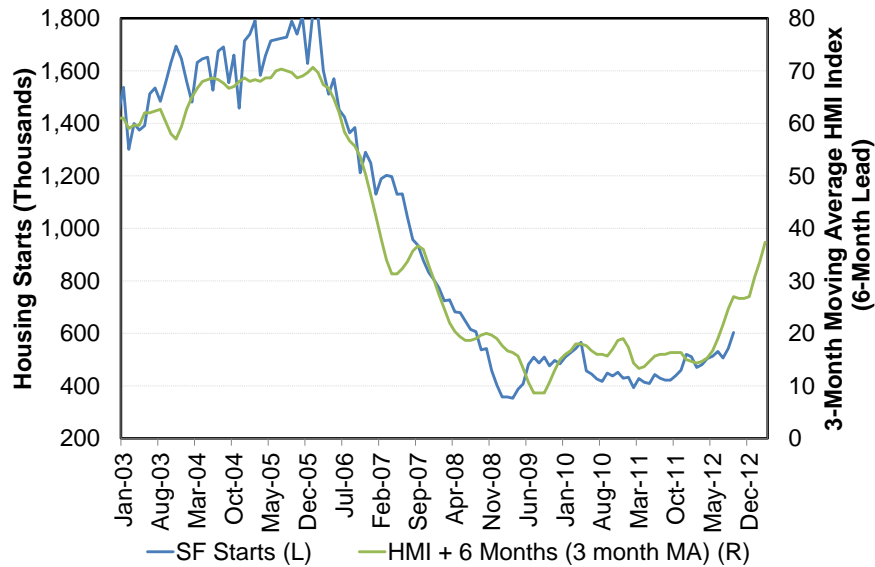
Uncertainty Has Slowed Business Investment and Hiring Especially Prevalent in Export Oriented Manufacturing

Source: Federal Reserve, Census, Conference Board

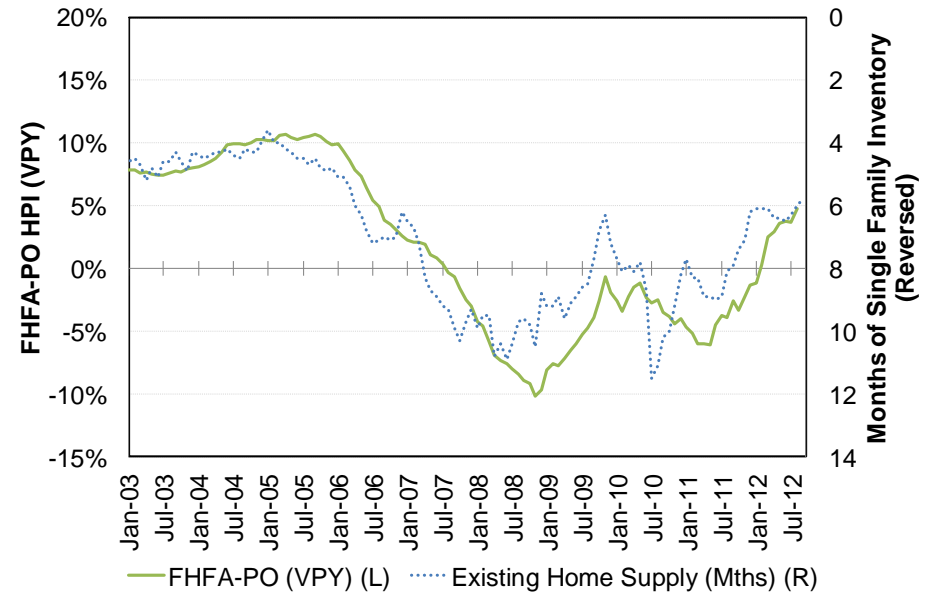
Housing

Housing Trends Positive

Home Builder Survey Indicates Surge In Starts



Prices Improve As Supply & Demand Balance



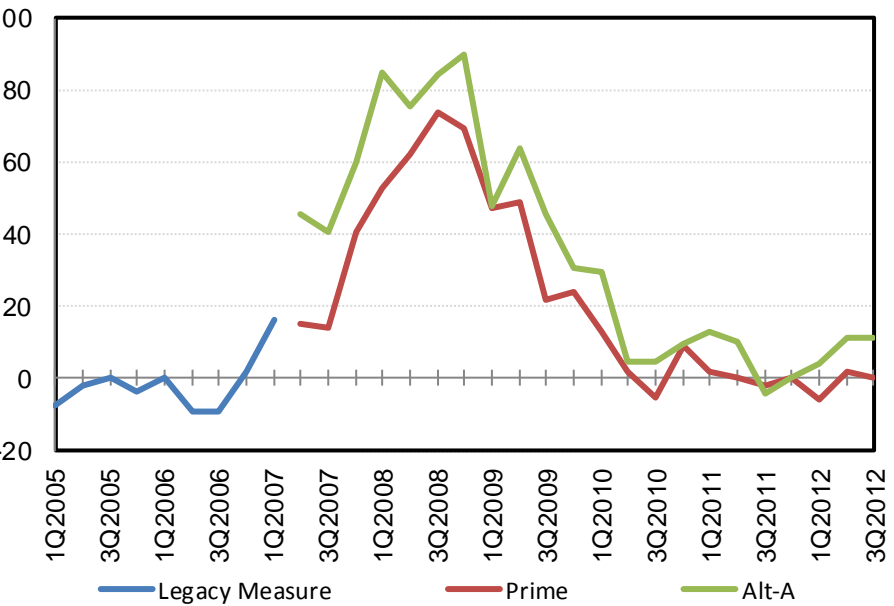
**Leading Indicators Point To Increased Demand
Starts And Permits Beginning Slow Upward Trek Following Sentiment
Prices Improve As Supply And Demand Balances**

Source: NAHB, BLS, Census, NAR

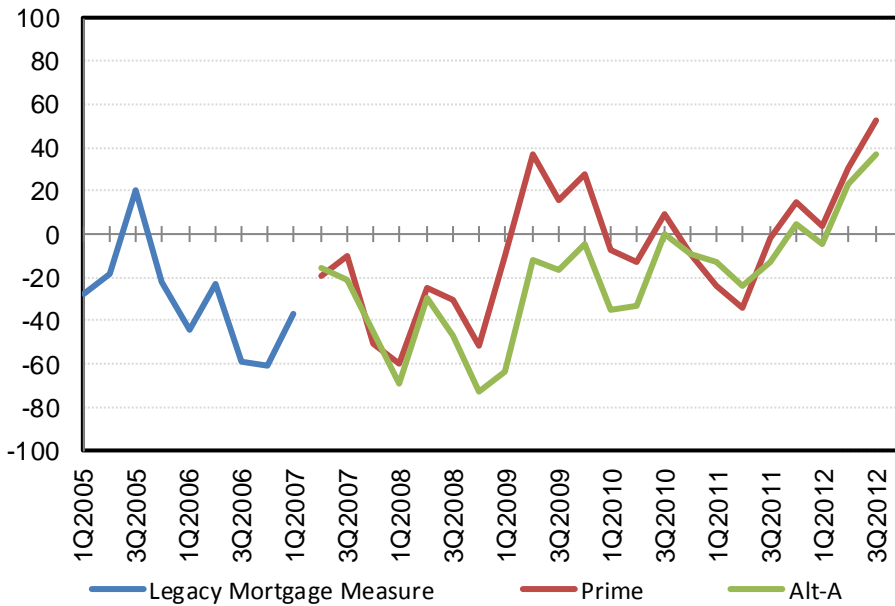
Increase In Demand Despite Tight Standards

- Home Affordability And Increased Rents Spur Demand
- MBA Purchase Apps, However, Remain At Late 1990s Level

Net Percentage of Banks Tightening Lending Standards: Mortgages



Net Percentage of Banks Reporting Stronger Demand: Mortgages



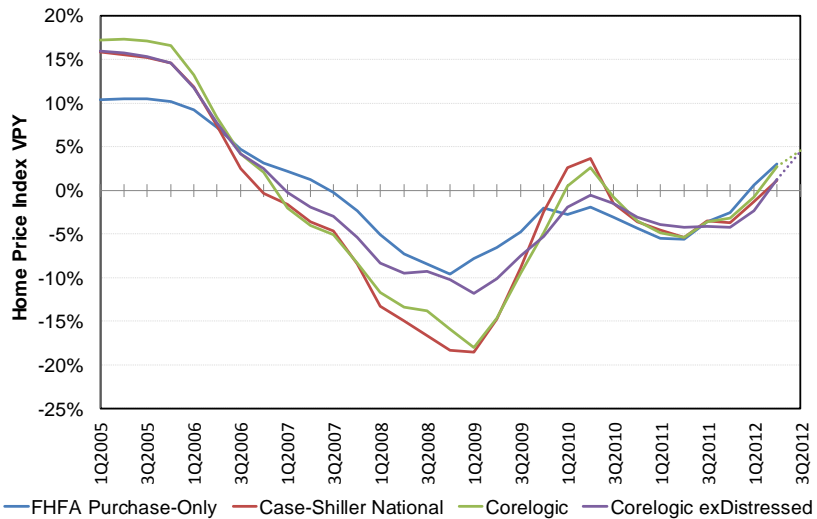
Banks Standards Remain Tight As Borrower Interest Begins To Rebound

Source: Federal Reserve

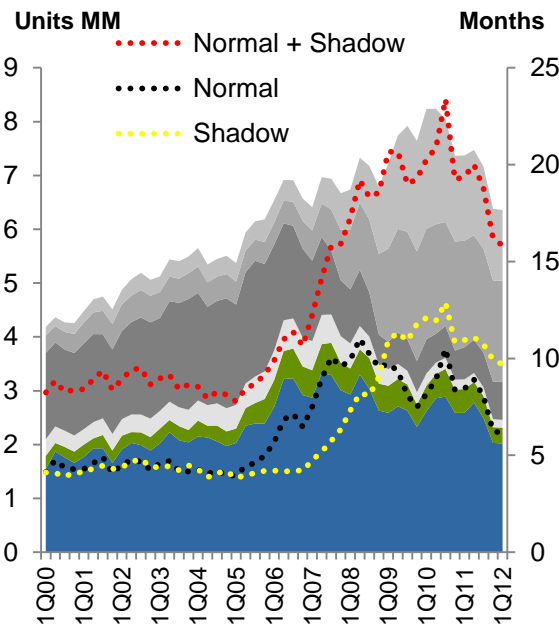


Housing Prices And Shadow Inventory

Home Prices Recovering



Normal Inventory Nearing Stability



2Q12 Supply (MM units)

“Shadow Inventory”

1.3 90-day Delqs

1.9 Foreclosure Inventory

0.7 Housing Starts

0.1 New, For Sale

0.3 Condos/Townhomes

2.0 Existing Single Family

2.5 MM 6Mos

5.0 MM 11Mos

6.4 MM 16Mos

Source: Census, NAR, MBA

Nascent Home Price Momentum Forming

- Corelogic HPI Positive VPY/VPM 6 Straight Months
- Case-Shiller & FHFA Positive VPY/VPQ In 2Q12

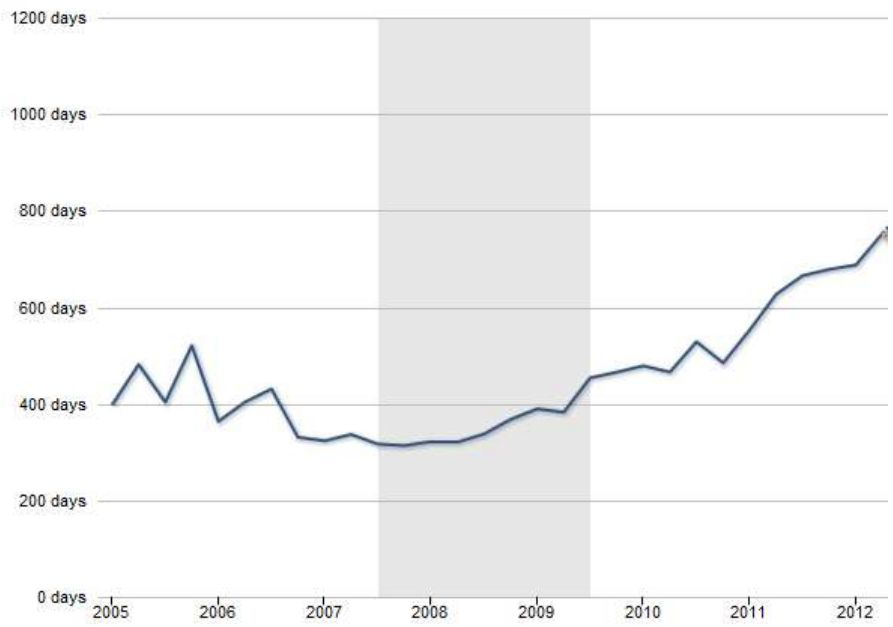
Shadow + Normal Inventory Remains 16 months For 3rd Straight Qtr

- Foreclosure Processing Time Critical
- Quicker Disposition Could Pressure Home Prices In Near-Term
- Slower Processing Threaten To Drag Out Crisis With Uncertainty

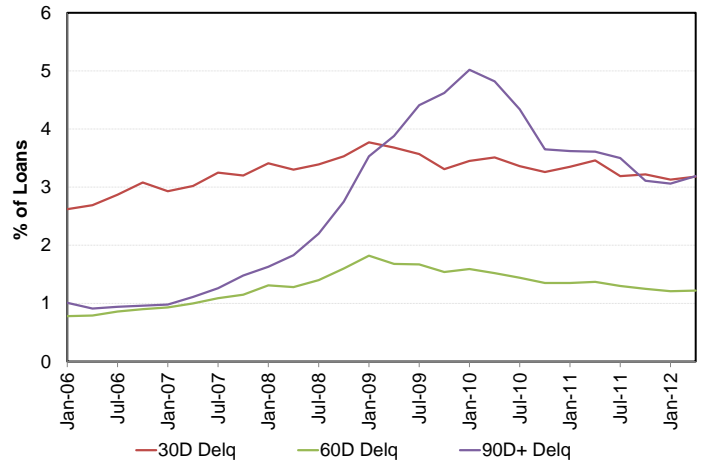
Shadow Inventory Continues To Weigh On Home Prices
Home Prices, However, Have Stabilized And Begun To Increase
Labor Market Recovery Key To Both Going Forward

Loans Stuck In Shadow Inventory

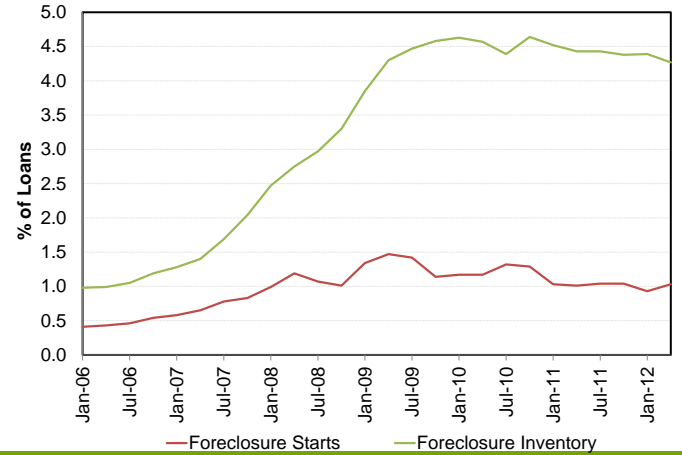
Average Days To REO From Serious Delq



Delinquency Rates



Foreclosure Inventory Remains High

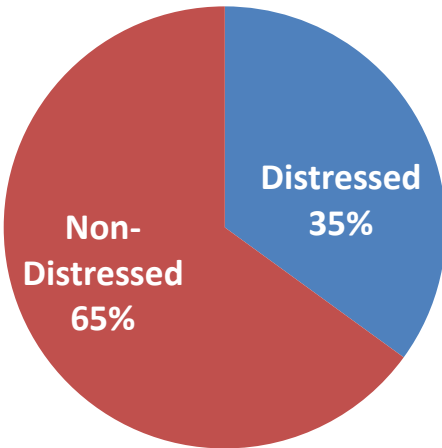


**Despite Decline In 90+ Delq Loans,
Slowing Foreclosure Process Leaves Overhang Of Shadow Inventory**

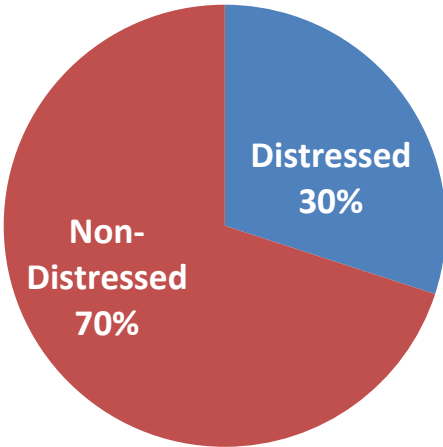
Source: Federal Reserve Bank of New York; MBA National Delinquency Survey

Distressed Sales Decline As Pipeline Slows

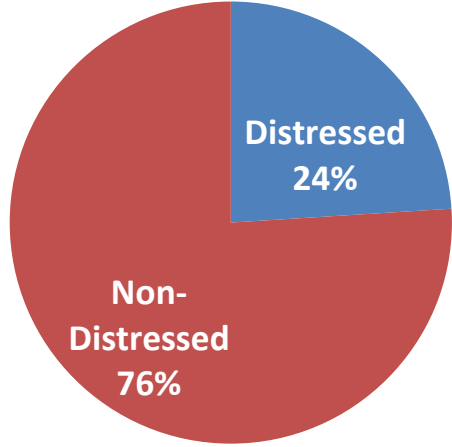
September 2010



September 2011



September 2012

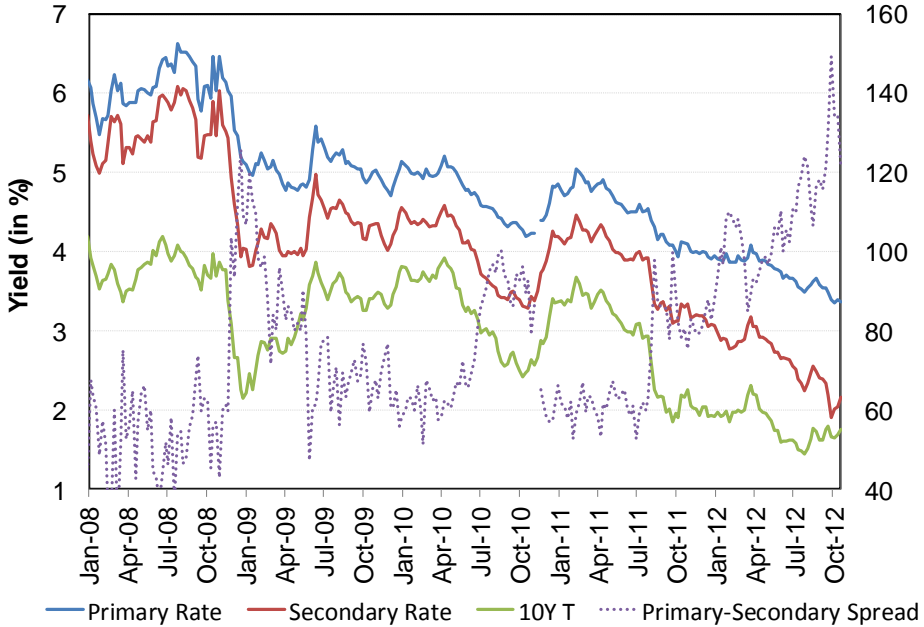


**Distressed Share Of Sales Continues To Decline
VPY Sales Are Up 10%, Non-distressed Sales Are Up 20%**

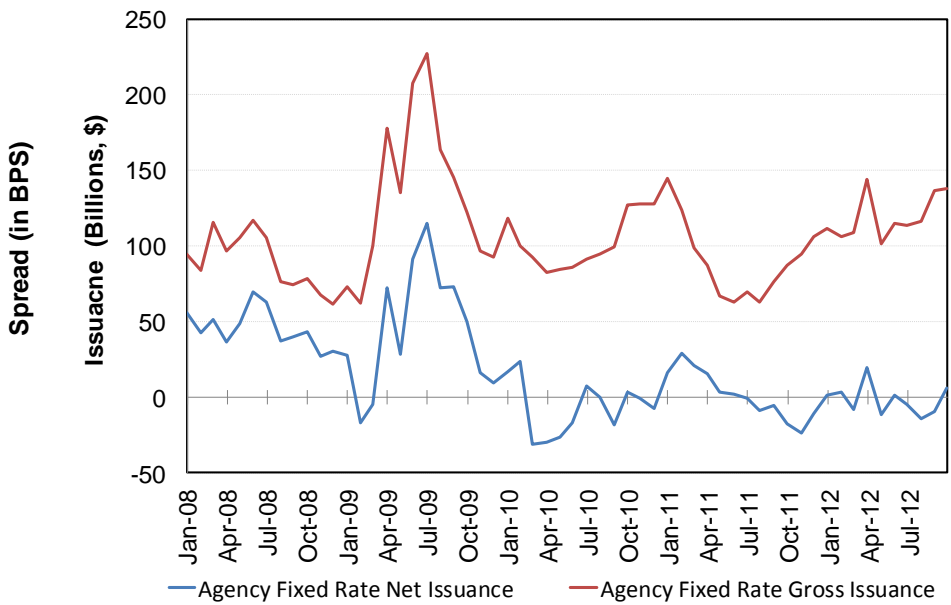
Source: NAR

FOMC Actions

Lenders Profit From Excess Spread



Not Much For The Fed To Buy



**Fed Purchases Push Normal Market Participants From Agency MBS
Secondary Rates Drop But Capacity Issues Limit How Much Borrowers Feel**

Source: JPMorgan

Data Source Statement

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