MACRO PULSE™

February 2011 A Delphi Advisors Publication Volume 2, No. 2

"Sixteen Tons"

Thanks to a lack of shocks in January, the U.S. economy managed to stay "on the tracks." The 4Q2010 real GDP growth rate picked up to 3.2 percent (from 3Q's 2.6 percent), but that growth appears to have been as much the result of unrealistically optimistic statistical assumptions as genuine activity. When the dust settled at the end of the month, we just felt ("borrowing" from the song that graces our title) "another month older and deeper in debt."

Not that we individually are necessarily deeper in dept, but rather we collectively – as a nation. Moreover, several of the countries that have typically been the most willing to buy U.S. debt have either become net sellers of Treasury securities (especially China) or purchased new debt at a much slower pace than usual (Japan). The Federal Reserve has responded to the funding shortfall by ramping up its purchases of those securities. Unfortunately, if history is any guide, continuing to "monetize" the debt in that way could ultimately result in higher interest rates and a depreciated dollar.

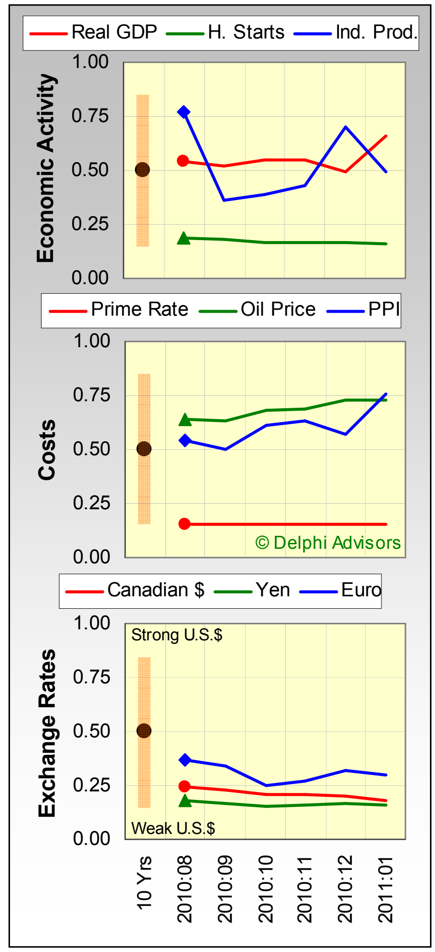

***Figure 1.* Previous six month's behavior of macroeconomic variables indexed relative to their historical 10-year min, max and average (lower and upper ends of the orange bars, and black dots, respectively)**

On the employment front, an abysmal 36,000 non-farm jobs were created in January. Although the number of full-time employees rose and part-timers fell, we were particularly dismayed to see that the civilian labor force participation rate (the share of the population 16 years and older either working or seeking work) fell to a fresh 27-year low of 64.2 percent; also, individuals not counted as being in the labor force but who would like a job jumped to a record-high 6.64 million.

Manufacturing was the bright spot again. The rate of inventory accumulation dropped, and new orders (especially *sans* transportation) nudged higher. Also, surveys by the Institute for Supply Management showed activity in both the manufacturing and service sectors jumped by healthy margins. The cloud associated with that silver lining, however, is that input prices have been rising noticeably in past months. Should that trend continue, more marginal production capacity will be forced to curtail.

Residential construction activity appears to have found a fairly firm base, but has yet to muster the energy to launch off the bottom. On a positive note, total housing vacancies have begun to decline, although the "off-market" component (including foreclosed units held by lenders) keeps expanding. On the negative side, signs seem to be proliferating that a price-induced housing double dip is unfolding.

The most critical economic "wild card" involves the social unrest currently unfolding in the Middle East and elsewhere. The United States is already in a phase in which expenditures for energy are rising but the amount of energy used is flat or falling. A reduction in Middle East oil supplies would exacerbate that relationship.

This report is a compilation of articles posted on our website (http://delphiadvisorsmacropulse.blogspot.com/); those articles relate recent economic developments to the U.S. forest products sector in much greater detail. They also provide context for our complete, 24-month forecast, which is contained in the *Economic Outlook* newsletter available through Forest2Market (http://www.forest2market.com/f2m/us/products/outlook). ■