



**ABOUT
BILL SULLIVAN**

William V. Sullivan, Jr. serves as Chief Economist at JVB Financial Group, working closely with the firm's trading desk, providing analysis and commentary on the U.S. economy and the financial markets. Among his duties are authoring a weekly report on credit market trends and maintaining a regular schedule of conference calls that focus on interest rate developments. He appears frequently on Bloomberg TV and is often quoted in Barron's.

Mr. Sullivan is the familiar voice that JVB features on our weekly conference call, where he discusses the economy and the events that affect the marketplace.

He was previously associated with Morgan Stanley in New York City for more than twenty years, where he was an Executive Director and a Senior Economist in the firm's Retail Fixed Income Division. Bill published a widely quoted weekly letter on the financial markets and was a frequent guest commentator on several business networks, including Bloomberg TV, CNBC, and Fox News.

Mr. Sullivan received his Bachelor of Arts Degree in Economics from Fairfield University.

JVB FINANCIAL

Weekly Commentary by Bill Sullivan, JVB Chief Economist

August 10, 2009

Jobs, clunkers, and the Fed

The employment situation report for the month of July was interpreted by many observers as a turning point for U.S. labor market activity. Indeed, the moderate pace of job losses in relative terms was viewed as a firm indication that the longstanding recession was over and that the domestic economy was poised for a significant recovery. While there is no doubt the data weren't as grim as earlier in the year, there appeared to be several distortions that suggest a genuine improvement in the employment picture is still well in the future. Against that backdrop, the Federal Open Market Committee (FOMC) at this week's meeting is apt to confirm once again that policy is on hold for an extensive period, suggesting that the current target on Federal funds could be maintained until at least early next year.

Perhaps the most significant quirk in the July employment report was the number of individuals that moved to the sidelines of the labor market during the survey period. According to the Bureau of Labor Statistics, the total number of people not considered in the labor force last month increased by 637,000. Since 1980, there have been only five other months that had labor market withdrawals that exceeded the July, 2009, tally, underscoring the unusual nature of that adjustment. There is little doubt that the huge gain in this category contributed to the unanticipated drop in the nationwide unemployment rate, the first decline in fifteen months. Clearly, some of these "dropouts" chose to withdraw from the labor force, having been unable to find a job and, in turn, became a "discouraged" worker. Eventually, these individuals will reenter the labor market setting which will likely set the stage for a renewed climb in the nationwide unemployment rate to a new cycle high later

this year. As a result, a double digit jobless rate before too long is distinctly possible, a development that will resonate in both the political and monetary policy arenas.

In view of the potential for a further rise in the unemployment rate, the FOMC is still likely to take a cautious approach regarding the economy's overall prospects. No doubt, in the statement that will be issued at the conclusion of the August policy convocation on Wednesday afternoon, the Committee will call attention to the ongoing improvement in financial market conditions, especially the rise in equity evaluations since the last meeting in late June. Additionally, the membership will probably judge the latest pattern of household spending as encouraging, particularly in the context of the strong response to the Federal Government's rebate program for the purchase of new vehicles. Nevertheless, the Fed must acknowledge that business firms are continuing to cut staffing, as reflected in the contraction in July non-farm payrolls and will probably view those reductions as a source of weakness for some time. Given this outlook for labor market activity, the Committee should reinforce its preference for maintaining a historically low Federal funds rate for an extended period. Moreover, considering the level of support that has been provided the banking and automotive sectors of the economy, it would be "politically untenable" for the central bank to withdraw liquidity from the financial system before the pace of new job creation is restored to a level that reduces the nationwide unemployment rate on a sustained basis.

The Committee at this week's meeting will of course have to render a judgment as to whether the "Cash for Clunkers" program

(Continued on page 2)

(Continued from page 1)

is a tipping point for consumer spending or whether the stimulus will prove short-lived and actually create some downside risks for the economy in the autumn and winter months. Clearly, the Government's largess is being embraced by the car buying public and as many as 750,000 new vehicles may ultimately be acquired by American families, with most of the outlays transpiring in July and August. The concentrated upturn in durable-goods related expenditures sets the stage for a strong performance in personal consumption that should translate to a positive reading for real Gross Domestic Product for the third quarter. Whether the projected jump in aggregate economic activity represents the beginning of a genuine recovery process remains open to debate, particularly if the job and income environments remain weak for several more quarters. Although the success of the Government's program is undeniable, there are several downside risks, in our judgment, that need to be considered. As an example, as these older vehicles are scrapped, there will be a reduction in earnings capability for many repair facilities and auto part suppliers. Additionally, the acquisition of a new car is almost always a credit sensitive purchase for consumers. The program is thus essentially encouraging households to take on a larger debt load, with many families already having extreme difficulty in managing their finances. Conceivably, the rebates for new cars could divert spending away from other discretionary items, which could offset some anticipated increase in auto-related expenditures. The biggest challenge forthcoming from this program, however, is whether the support is effectively borrowing from future sales. Many households that may have been considering replacing their vehicles in the next year or so may have

chosen to take advantage of the support that is being provided by U.S. taxpayers. Once this influence is removed, spending on new cars could weaken considerably for at least several months, as underlying sales trends will be dominated by the prevailing changes in employment and income growth. Unless households begin to experience a stronger pattern of take-home pay, the net result of the "Cash for Clunkers" program may be to shift prospective sales from later this year and the opening months of 2010, to the third quarter. This adjustment will undoubtedly buoy current economic growth, but could be laying the groundwork for renewed weakness in durables-related consumption and the general economy, just as the key holiday season draws near. ■

*William V. Sullivan, Jr.
Chief Economist
JVB Financial Group
August 10, 2009*

JVB Financial Group, LLC, member FINRA, SIPC
2700 N. Military Trail, Suite 200 / Boca Raton, FL 33431
(561) 416-5876 • www.jvbfinancial.com

For Broker Dealer, Institutional, and Advisor Use Only
Not to be distributed to individual investors

This document has been furnished to you solely for your information and may not be reproduced in any manner or provided to any other person. The information contained herein is based on sources that we believe to be reliable, but we do not represent that it is accurate or complete. Nothing contained herein should be considered as an offer to sell or a solicitation of an offer to buy any financial instruments discussed herein. All references to prices and yields are subject to change without notice. Any opinions expressed herein are solely those of the author. As such, they may differ in material respects from those of, or expressed or published by or on behalf of JVB Financial Group, LLC or its officers, directors, employees or affiliates.