Northwestern Mutual Wealth Management Company®

Weekly Market Commentary by Emmett Wright

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The fireworks began early as investors, heartened by progress in Greece and some better-than-expected news about U.S. manufacturing, drove the Dow up 5.4%, its best week in two years and the best since November 2008 if measured by points, having gained 648.19. And the S&P 500 and NASDAQ were even more torrid, gaining 5.6% and 6.1% respectively. The surge was not enough to salvage the month, with the Dow off for the seventh straight June, but it was enough for investors to eke out a gain for the second quarter, with the index improving 0.8% (though the S&P and NASDAQ were slightly down).

	Key Market Data		
	Week ending…		
	7/1/11	6/24/11	Change
Dow Jones Industrial Average Index	12,582.77	11,934.58	+5.43%
S&P 500 Index	1,339.67	1,268.45	+5.61%
NASDAQ Composite Index	2,816.03	2,652.89	+6.15%
10-Year Treasury Note Rate	3.1999%	2.869%	+0.330 pct. pts.
NYMEX Crude Future (Barrel)	$94.94	$91.16	+4.15%
Euro/U.S. Dollar	$1.4526	$1.4189	+$0.0300

Greece continues to be front and center in the minds and hearts – and stomachs – of the world's investors, both because of the inability of European leaders to take decisive action and the growing fears about contagion. But last week all was well – for the moment, anyway – as Greece's Parliament approved the latest round of austerity measures that the European Central Bank and the International Monetary Fund (IMF) insisted on if the country was to get its next round of bailout money and stay solvent through the summer. The package includes spending cuts, tax increases and the sale of state assets, all of which will hamper economic growth, the opposition party claims. However, the meeting of Europe's financial leaders that was scheduled for this weekend to discuss the second bailout was postponed as they felt there were too many details to be worked out yet and a meeting that fell short would only raise concerns anew. With the latest payout, Greece – and its lenders – have until the end of August before Greece will run short on cash again. Meanwhile, both France and Germany, the two largest holders of Greek debt, seem to have agreed to some form of voluntary debt restructuring by banks (which the debt agencies have warned they would see as tantamount to bankruptcy), with Nicolas Sarkozy, France's president, saying, "We're committed to going from a principle – the voluntary participation of the private sector – to concrete reality."

As for that contagion, one of the candidates, Portugal, said its budget deficit for the first quarter was higher than expected, representing 8.7% of GDP; Portugal must get down to 5.9% by the end of the year to meet the terms of its €78 billion ($112.1 billion) bailout. In Great Britain, austerity plans led to a long-scheduled general strike which included school teachers and civil servants. And Italy is pushing forward with its own plan to reduce its budget deficit and calm investors with the goal of eliminating its deficit by 2014.

Back at home, there was little progress on our own burning issue, raising the debt ceiling, but plenty of drama. As the Treasury Department affirmed Aug. 2 as the drop-dead date, the President said Congress would have to work out a deal no later than July 22 if it expected to get the paperwork done in time to meet that deadline. At a news conference, President Obama said that lawmakers "need to do their job" to avoid default which, in his estimation, means accepting that higher taxes are unavoidable, particularly for the rich, not to mention tax breaks for businesses. "You'll still be able to ride on your corporate jet," the President said. "You'll just have to pay a little more." He said the Democrats had accepted curtailing programs they had long championed and the GOP needed to follow suit: "Everybody else has been willing to move off their maximalist position – they need to do the same." He also said that the federal government could do more to address unemployment and a weak economy with such programs as reduced payroll taxes, public works projects and trade pacts. The GOP response was as expected with Speaker of the House John Boehner (R - Ohio) saying the President's remarks "ignore economic and legislative reality."

In fact, word had it that the two sides in Congress were closer to a deal than one might think given the rhetoric, and early last week Treasury Secretary Timothy Geithner told *The Wall Street Journal*, "It's a political town in a political moment, but there's a very pragmatic, a very realistic, a very constructive spirit. And we hope that results in some compromises, the kind you need to make a broad deal work." There was also a rumor, which Mr. Geithner denied, that he would step down as soon as the debt deal was done, unsettling news given his central role in policy making during the recovery.

Lastly, Minnesota provided an example in miniature of what can happen when consensus isn't reached, with the state shutting down after the governor, a Democrat, rejected the budget bill sent to his desk by the GOP-controlled Legislature. The issue was whether needed revenues would come from cost cutting or higher taxes – sound familiar? Photos of Boy Scouts being thrown out of jamborees over the holiday weekend because state parks were closed should be enough to give any politician pause – and incentive to get a deal done, whether in St. Paul or in Washington D.C. The IMF also weighed in on the debt ceiling issue in its annual report which urged the United States to act to raise its debt level, saying that any delay could raise interest rates and hurt both the U.S. and global economies. The IMF also warned us about the need for a long-term plan to address our deficit.

As noted, the market got a boost as the week went along because of some surprisingly upbeat news about manufacturing, which had seemingly settled into the doldrums after having long been at the heart of the recovery. The Institute for Supply Management's (ISM) index for manufacturing in Chicago rose more than expected in June, up to 61.1 from 56.6 where a drop to 54.0 was forecast. Investors were also heartened later in the week when the ISM announced that its manufacturing index for June was up for the first time in four months, rising to 55.3 from 53.5.

In even more surprising news, the S&P/Case-Shiller home price index for April improved for the first time in eight months, up 0.7%, with increases in 13 of the 20 cities the index tracks. In March it had fallen 0.8% to a new low as prices were down in 18 cities. Even so, the index was 4% lower than it was a year ago.

The Census Bureau said that state and local tax collections climbed 4.7% in the first quarter to $321.6 billion, though it was really about the states, up 9.3%, not local governments, down 0.6%. It was the sixth consecutive quarter of year-over-year gains, but the totals remain below pre-recession levels.

And car sales bounced back, for Detroit anyway, as sales for Japanese cars were hurt by low inventories. Overall sales were up 7.1% from last June, though the seasonally adjusted annual rate fell from 11.8 million in May to 11.5 million – it had been over 13 million earlier this year. Sales at Toyota and Honda both fell 21%, while Chrysler was up 30%, GM 11% and Ford 10%. In news that was less happy for the auto industry, the President has been meeting with industry leaders to discuss a plan for roughly doubling the efficiency of American vehicles to 56.2 miles per gallon by 2025, putting us on par with Europe and Japan. The proposal is technically feasible and would dramatically reduce our dependence on foreign oil while reducing pollution, but it would also, according to automakers, result in lighter, smaller and more expensive cars that might not suit the taste of Americans.

Other economic news was less stellar. For instance, the Commerce Department said that consumer spending was flat in May and hit its lowest point since September 2009. Adjusted for inflation, spending fell 0.1% (as it did in revised numbers for April), the first decline since January 2010, with high gas prices a key factor. Incomes did rise 0.3%, but only 0.1% after being adjusted for inflation. And construction spending fell to a 10-year low in May, the Census Bureau reported, down 0.6% from April to $753.5 billion.

In other news, the Fed cut the fees that retailers pay banks, about $20 billion a year, in half with a cap mandated by the Dodd-Frank financial overhaul bill. The average fee was 44¢ per transaction and will now be 21-to-24¢; some had expected the Fed to cut it down as far as 12¢. Consumers, who pay the money indirectly, are unlikely to feel the change other than through fewer price increases from retailers.

There was also some news about the leaders of the IMF, past and present. As expected, the French finance minister Christine Lagarde did get the job as the new president, the first woman to hold the position, with the United States clinching the deal by casting its vote her way. A few days later her predecessor, Dominique Strauss-Kahn, who'd stepped down after being charged with sexual assault, was released from house arrest after the credibility of his accuser collapsed; the charges against him may well be dismissed this week.

Lastly, there was evidence that the issues that triggered the Great Recession are still very much in the news after reports that Bank of America will pay $8.5 billion to settle the lawsuit brought by investors who lost money on mortgage-backed securities before the housing market collapsed, the largest such settlement to date. Not only would that wipe out the bank's earnings for the first half of the year but it would also set a precedent for other cases against banks still on the docket.

A look ahead

In a holiday-shortened week, there will be releases about factory orders and wholesale inventories which will give investors a read on whether or not the recent good news about manufacturing will hold up. There will also be updates on consumer spending, chain-store sales and the ISM's nonmanufacturing index. The big test for investor confidence will come when the latest unemployment rate is announced on Friday. Estimates have the economy adding about 90,000 jobs after gaining only 54,000 in May with the jobless rate expected to remain at 9.1%.

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All index references and performance calculations are based on information provided through Bloomberg. Bloomberg is a provider of real-time and archived financial and market data, pricing, trading, analytics, and news.

The Dow Jones Industrial Average Index® is a price-weighted average of 30 blue-chip stocks that are generally the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

Standard and Poor's 500 Index® (S&P 500®) is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Standard & Poor's offers sector indices on the S&P 500 based upon the Global Industry Classification Standard (GICS®). This standard is jointly maintained by Standard & Poor's and MSCI. Each stock is classified into one of 10 sectors, 24 industry groups, 67 industries and 147 sub-industries according to their largest source of revenue. Standard & Poor's and MSCI jointly determine all classifications. The 10 sectors are Consumer Discretionary, Consumer Staples, Energy, Financials, Health Care, Industrials, Information Technology, Materials, Telecommunication Services and Utilities.

The NASDAQ Composite Index® Stocks traded on the NASDAQ stock market are usually the smaller, more volatile corporations and include many start-up companies.

NASDAQ - National Association of Security Dealers Automated Quotations. The NASDAQ is a computer-operated system owned by the NASD that provides dealers with price quotations for over the counter stocks.

Bear market calculations and interpretations are derived from data supplied by Ned Davis Research, Inc.

The International Monetary Fund (IMF) is the intergovernmental organization that oversees the global financial system by following the macroeconomic policies of its member countries, in particular those with an impact on exchange rate and the balance of payments.

The gross domestic product (GDP) is the amount of goods and services produced in a year, in a country.

The ISM Index, released monthly by the Institute for Supply Management, tracks the amount of manufacturing activity that occurred in the previous month.

The S&P/Case-Shiller Home Price Indices are designed to be a reliable and consistent benchmark of housing prices in the United States. Their purpose is to measure the average change in home prices in a particular geographic market. They are calculated monthly and cover 20 major metropolitan areas.

The Dodd–Frank Wall Street Reform and Consumer Protection Act is a federal statute in the United States that was signed into law by President Barack Obama on July 21, 2010. The Act is a product of the financial regulatory reform agenda of the Democratically-controlled 111th United States Congress and the Obama administration.