



May 10, 2010

Investors suffered through the kind of week that became all too familiar when the recent recession was in full swing, with indexes both major and minor getting battered. However, there was a big difference between then and now: With the exception of the grim news from Greece and the yet-to-be-explained trading issues that sent the stock market into a freefall on Thursday, there was almost nothing but good news about the economy last week, with upbeat reports about jobs, earnings, industrial production, consumer spending, and even housing. Still, in a sign that a correction may be at hand (and the NASDAQ has already endured one, having fallen 10.2% from its 2010 peak), the major indexes recorded their worst week in over a year and they're now in the red for 2010 after the Dow fell 5.71% (off 0.46% for 2010), the S&P 500 dropped 6.39% (down 0.38% for the year), and the NASDAQ tumbled 7.95% (off 0.15%).

But first the good news – and there was plenty of it. In a sign that consumers are starting to open their wallets, the Commerce Department said that spending was up 0.6% in March and personal income rose 0.3%. Thomson Reuters backed up that report, reporting that same-store sales improved 0.5% in April, and auto sales in April jumped 19.8% year-to-year (though they were slightly down from March when Toyota spiked an industry wide surge with sales incentives in the wake of its recall). The Institute for Supply Management (ISM) said that its index of manufacturing activity rose to 60.4 in April, its highest point since June of 2004, with 17 of the 18 industries surveyed reporting growth. The ISM's index

	Key Market Data		
	Week ending		
	5/7/10	4/30/10	Change
Dow Jones Industrial Average Index	10,380.43	11,008.61	-5.71%
S&P 500 Index	1,110.88	1,186.69	-6.39%
NASDAQ Composite Index	2,265.64	2,461.19	-7.95%
10-Year Treasury Note Rate	3.431%	3.663%	-0.232 pct. pts.
NYMEX Crude Future (Barrel)	\$75.11	\$86.15	-12.81%
Euro/U.S. Dollar	\$1.2731	\$1.3314	-\$0.0583

for new orders rose 4.2 points to 65.7, indicating that the growth was not just a matter of restocked inventories, and its employment index climbed 3.4 points to 58.5, the fifth straight uptick. The Commerce Department also reported that factory orders were up 1.3% in March, the eleventh increase in the last twelve months, and, excluding the volatile transportation sector, they rose 3.1%, the largest upswing since August of 2005. Further, the Labor Department said that productivity climbed 3.6% in the first quarter. On the housing front, the National Association of Realtors reported that sales agreements for previously owned homes rose 5.3% in March, largely because of the homebuyers' tax credit, and construction spending improved 0.2% in March. Though the numbers are still coming in, first quarter profits for S&P 500 companies are expected to be up 87% year-to-year, which would obliterate the previous record of 35% set in the second quarter of 1993. (The forecast for the current quarter, though rising, is 16%.) Finally, on Friday, the Labor Department said that 290,000 new jobs were added in April, the largest gain in

four years, though the jobless rate actually rose from 9.7% to 9.9% because of new entrants into the workforce. There was job growth almost across the board, including 44,000 new manufacturing positions, the largest such increase since 1998. Even so, the number of people out of work for six months or more is now 6.7 million, 45.9% of the jobless, and the underemployment rate, which includes those with part-time work who want a full-time job as well as those who have given up looking, reached 17.1%.

And then there was that 16-minute interlude on Thursday afternoon that *The New York Times*, in a page-one headline, adjudged to be “one of the most terrifying moments in Wall Street history.” Though the market rebounded and the Dow “only” fell 347.80 points for the day, investors will be rightly edgy until the Securities and Exchange Commission (SEC) pins down what happened. Human error was the initial suspect, but it now it appears as though the SEC is focused on structural challenges created by the growing number of high-frequency trading networks that lack the liquidity replenishment rules in place at more traditional exchanges such as the New York Stock Exchange.

The Senate continued to try and hammer out the details of the financial overhaul bill and even made some bipartisan progress last week when it voted 93-5 to give the government broad new powers to break up failing companies without using taxpayer money, the idea being to dispel the idea that any one company is “too big to fail.” The Senate also moved to reject an amendment favored by liberal Democrats that would have limited the size of banks and financial services firms based on their total deposits and assets. And after some horse trading with the administration, it appears that the Senate will also drop from the proposed bill the provision that would have resulted in increased Congressional oversight of the Federal Reserve’s policy-making which Fed

Chairman Benjamin Bernanke had said would “politicize” the Fed, settling instead for some one-time audits and reviews of the Fed’s books.

The broader view

Though Greece has been front-page news for months now, the story took the worst possible turn last week when the headlines were about death rather than debt after three people were killed in a bank fire caused by protestors. The protests, which are expected to continue to test the government’s will, are driven by the fact that Greece is trying to reform a country where an astounding one out of every three people has a civil service position which, until recently, was guaranteed for life, and also clamp down on the nation’s legions of tax evaders.

Later in the week, the European Union (EU) and the International Monetary Fund (IMF) finally acted on the long-discussed and debated loan for Greece, approving a package totaling €10 (\$145 billion) with the first installment coming in time for Greece to meet its next big debt payment on May 19th. Nonetheless, based on the still-rising yield Greece must offer to sell its debt and the plunging euro, it’s clear that the market continues to have its doubts both about Greece and the EU’s ability to act decisively. The doubts arise from the fact that, even if the Greek government can convince the nation to swallow the dose of castor oil it has pledged to take in the form of additional austerity measures, it will be hard-pressed to not only pay down its back-breaking debt, but simultaneously lower its double-digit deficit and grow its feeble economy, a tall order for any country. If Greece cannot do so, the contagion may well spread to one of the other countries that is in similar economic straits, such as Portugal or Spain, the latter a far greater concern given the fact that it’s Europe’s fourth largest economy. Spain’s unemployment rate is now 20%, double what it was when the recession began, and last week our

government put the projected cost of bailing out Spain at \$600 billion.

In Germany, which will contribute €2.4 billion (\$30 billion) to the bailout, Chancellor Angela Merkel has done her best to refocus the debate on the euro, not the profligate Greeks, who two-thirds of Germans believe should not be bailed out, saying the loan was about “nothing less than the future of Europe.” Even so, she’s now in a precarious position politically, as her party, the Christian Democratic Union (CDU), lost an election on Sunday in Germany’s most populous state that came to be seen as a referendum on her decision to help Greece. As a result, the CDU no longer holds a majority in the Bundesrat, Germany’s upper house in Parliament, and will now have to negotiate with parties on the left to pass any new legislation.

Meanwhile the leaders of the EU continue to point fingers at speculators and rating agencies for exacerbating Greece’s woes, rather than the culprit many perceive to be responsible for the continuing crisis, the EU itself. However, all 27, EU finance ministers held a special session in Brussels over the past weekend to try and come up with what they dubbed a “stabilization mechanism” to address debt downgrades and market perceptions, and the result was a \$957 billion rescue package for struggling EU members, including \$560 billion in new loans, \$76 billion as part of an existing loan program, and another \$321 billion from the IMF. As Olli Rehn, the European commissioner for monetary policy said when announcing the fund, “We shall defend the euro, whatever it takes.” The plan will also feature the establishment of “swap



Emmett Wright, CFA
Chief Investment Officer
Northwestern Mutual Wealth Management Company

lines” from other central banks, including the Federal Reserve, that will, in essence, print new money in their own currency and swap them for euros to help create liquidity.

A look ahead

This coming week there will be updates on wholesale inventories, mortgage applications, retail sales, the trade gap, and industrial production and capacity utilization. However, with anxiety and volatility on the rise, the market-watchers will be far more focused on whether or not stocks will rebound or continue to fall. The glitch that sent the Dow plummeting almost 1,000 points will be addressed as the SEC looks to institute new rules to prevent a repeat performance (as soon as it determines the cause). Hopefully, a series of checks and balances will lead to market uniformity across the various exchanges. That said, while the crisis in Greece could create economic ripples across the globe, most analysts had been expecting a correction at some point this year given the bullish returns in 2009. Furthermore, as noted, the recent economic news has been profoundly upbeat, so there’s no reason to expect an extended stock market slump. In sum, a potential correction, however painful, is far from unexpected and presents a good opportunity for investors to review and rebalance their assets to keep their portfolios in line with their goals.

61-1200

material does not constitute investment advice and is not intended as an endorsement of any specific investment or security. Information and opinions are derived from proprietary and non-proprietary sources.

Northwestern Mutual Wealth Management Company, Milwaukee, WI, is a subsidiary of The Northwestern Mutual Life Insurance Company, Milwaukee, WI (NM) and a limited purpose federal savings bank authorized to offer a range of financial planning, trust, fiduciary, investment advisory and investment management products and services. Securities are offered through **Northwestern Mutual Investment Services, LLC**, subsidiary of NM, broker-dealer, registered investment adviser, member FINRA and SIPC.

Please remember that all investments carry some level of risk, including the potential loss of principal invested. Indexes and/or benchmarks are unmanaged and cannot be invested in directly. Returns represent past performance, are not a guarantee of future performance, and are not indicative of any specific investment. Diversification and strategic asset allocation do not assure profit or protect against loss. Although stocks have historically outperformed bonds, they also have historically been more volatile. Investors should carefully consider their ability to invest during volatile periods in the market. The securities of small capitalization companies are subject to higher volatility than larger, more established companies and may be less liquid. Bond investors should carefully consider risks such as interest rate risk, credit risk, securities lending, repurchase and reverse repurchase transaction risk. Greater risk is inherent in investing primarily in high yield bonds. They are subject to additional risks, such as limited liquidity and increased volatility. There is an inverse relationship between interest rates and bond prices. Investing in foreign securities is subject to certain risks not associated with domestic investing such as currency fluctuations and changes in political and economic conditions.

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 FINRA 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.

ISM Index is a monthly index released by the Institute of Supply Management which tracks the amount of manufacturing activity that occurred in the previous month.

International Monetary Fund (IMF) is an organization set up in 1944 to lower trade barriers between countries and to stabilize currencies by monitoring the foreign exchange systems of member countries, and lending money to developing nations.