

WEEKLY MARKET COMMENTARY

Cheered by better-than-expected news about manufacturing – maybe there wasn't

going to be that much of a slowdown after all – the Dow closed at a four-year high on Tuesday. But then job jitters took hold, and after they were confirmed by the Labor Department on Friday, the Dow was not only down for the week - the S&P 500 and NASDAQ also posted their worst weekly performances of 2012.

That downward trend may pick up some steam this week as the governments in both France and Greece were overturned by voters disgruntled about austerity programs and high unemployment, hardly cheering news for President Obama and his prospects for a second term. The incoming leaders rode into office with pledges to push back against Germany and its demands, and there's genuine fear that contagion may reach a new level in the ensuing squabble.

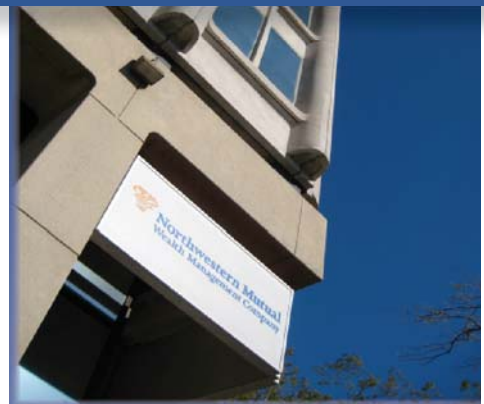
But first, jobs.

Heading into Friday, there had been conflicting news about jobs that kept investors off balance. On Wednesday, ADP, the payroll processor, announced that only 119,000 new positions had been created in April, the worst showing in seven months. But on Thursday the Labor Department said that first-time jobless claims had fallen 27,000 to 365,000, the biggest drop since last May. Then came reality: On Friday, the Labor Department said that only 115,000 jobs had been created in April, well below forecasts that had ranged as high as 170,000. The private sector added 130,000, but that was offset by a loss of 15,000 federal positions. The unemployment rate actually ticked down from 8.2% to 8.1%, but that was only because an estimated 342,000 Americans had given up looking, partly because the average period of time they've been out of work was a dispiriting 39.1 weeks.

The GOP wasted no time in taking aim at President Obama and his policies, with Mitt Romney describing the report as “terrible and very disappointing,” while adding that the economy was “slowing down, not speeding up.” The president tried to accentuate the positive – jobs were still being created – but also admitted, “We've got to do more.”

Looking beyond the politics – no easy task right now – what does this latest report tell us about the state of job creation in America, which is crucial to both consumer confidence and consumer spending?

We think that the April job numbers may well be the last time that an unemployment report will be significantly influenced by the “pull forward” of economic activity from a mild winter. Weather appeared to be a modest weight upon April's jobs report, as was the case in March, and construction employment fell for a third consecutive month. That's in part because, thanks to the unusually warm winter, some 100,000 construction jobs were added from December to February that normally would have been added



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Key Market Data

week ending...	4/27/12	5/4/12	Change
Dow Jones Industrial Average Index	13,228.31	13,038.27	-1.44%
S&P 500 Index	1,403.36	1,369.10	-2.44%
NASDAQ Composite Index	3,069.20	2,956.34	-3.68%
10-Year Treasury Note Rate	1.931%	1.880%	-0.051 pct. pts.
NYMEX Crude Future (Barrel)	\$104.93	\$98.49	-6.14%
Euro/U.S. Dollar	\$1.3253	\$1.3084	-\$0.0169
MSCI EAFE Index	1,521.38	1,483.87	-2.46%

in March and April. After all is said and done, the employment reports in March and April were not that different from each other, and employment reports for May and beyond should be on firmer fundamentals.

The birth/death rate adjustment probably accounted for much of the overestimation of job growth between early 2008 and early 2010. However, at this point in the business cycle, it probably underestimates “true” job growth. That would account for much of the disparity between healthy gains in retail sales, poor income growth and a declining rate of savings – more job growth should lead to more income growth and a higher savings rate. Off this report, for example, we estimate that personal income likely rose just 0.2% in April and industrial production only advanced 0.5%.

But there are some other positive signs. Temp services, a good leading indicator for job growth, rebounded in April. In fact, professional business services excluding temp services were solid. Furthermore, the length of the workweek was unchanged as were average hourly earnings, and those earnings are up 1.8% from a year ago. Lastly, the broadest measure of unemployment, the underemployment rate, which includes those who have given up looking as well as people who are working part time who would prefer full-time jobs, was unchanged at 14.5%; the recession peak was 17%.

In sum, while the report was disappointing, we don’t see it as the start of a bad run. In fact, job growth may well pick up from here on in.

If there was any consolation for Americans, the news was even worse in the eurozone where the jobless rate hit a new euro-era high of 10.9% in March from 10.8% in February; in March of last year the rate was 9.9% and it was the 11th month in a row with an increase.

But the big stories in Europe were in France and Greece where the general elections that were held on Sunday could result in very different economic agendas for those two nations.

As expected, Franoise Hollande defeated Nicolas Sarkozy in France, giving Sarkozy the dubious distinction of being the first president since 1981 to not be reelected. Hollande has said he will try to renegotiate the fiscal compact that sets debt and deficit limits, pushing economic growth over austerity. “If I am elected president,” Hollande said before the votes were tallied, “there will be a change in Europe’s construction.”

In Greece, the two main parties, the New Democrats and the Socialist Pasok – tarred because of what’s seen as their complicity in punishing austerity plans – were walloped at the polls with the Coalition of the Radical Left winning more seats than the socialists while radical parties such as the Golden Dawn party, whose members perform Nazi salutes, won seats in Parliament for the first time. The incoming government may renege on the terms that secured Greece its most recent bailout deal and it may even, some say, abandon the euro for the drachma. In addition, if the many parties now represented in Parliament can’t form a government, there may be yet another round of elections.

As a sign of growing instability, tens of thousands of people took to the streets on May Day, Europe’s Labor Day, to protest austerity programs that more and more governments are coming to see as impediments to growth and job creation. There were large-scale protests in Spain, Greece, Great Britain, France – where marchers waved “Down With Merkozy” signs – and even in Germany, where Chancellor Angela Merkel continues to maintain that austerity is the only way to save the euro.

At the European Central Bank's meeting on Thursday, its president Mario Draghi warned European governments against raising taxes as a way to pay debt. He also said "several governments need to be more ambitious" in attacking their fiscal and structural problems. The bank left its benchmark rate unchanged at 1%.

And in a further sign of dysfunction, European Union finance ministers met in Brussels to discuss tougher laws on capital requirements for banks (the deal will be voted on at the next meeting on May 15). The session ended with George Osborne, Britain's Chancellor of the Exchequer accusing his fellow ministers of making him look like "an idiot" because he wanted to tighten up the rules even further.

Meanwhile Spain, as expected, reported that its economy contracted in the first quarter.

In other economic news, the Institute for Supply Management's manufacturing reading for April hit 54.8, its highest point in 10 months, as 16 of the 18 industries reported gains. For stat mavens, the index's recession low was 33.1 and the long-term average is 52.8, while the all-time high is 61.4, posted before the recession. Later in the week the ISM said that its services sector index fell from 56 in March to 53.5 in April.

The auto industry had its best month in four years in April, driven by Toyota which has finally bounced back from last year's earthquake and tsunami in Japan. Sales were up 2.3% overall from a year earlier to 1.18 million vehicles, and the annualized rate hit a healthy 14.4 million vehicles. But American automakers did not fare as well, with Ford down 5.1% from a year earlier and GM off 8.2%. Sales for the other big American automaker, Chrysler, jumped 20.4%, but even that lofty figure was actually a slowdown from its recent showings.

The Commerce Department said that personal spending rose 0.3% in March after a revised gain of 0.9% in February; personal income was up 0.4% after increasing 0.3% in February. The price index for personal consumption expenditures (PCE), excluding food and energy, climbed 0.2% and is up 2.1% over the last 12 months, pretty much in line with the Federal Reserve's target of 2% inflation.

Construction spending improved 0.1% in March following a 1.4% decline in February; economists had forecast a 0.5% increase.

Same store sales were up 2.9% in April, and chain store sales rose 2.2%, the lowest reading in a year and a half.

In a good sign for drivers who are grimacing as they pump gas, the price of crude oil fell below \$100 for the first time since February.

First-quarter earnings reports are still coming in, but as of Friday Thomson Reuters reported that 67% of S&P 500 companies had beat expectations.

Finally, Hillary Clinton was in Beijing to discuss a long list of economic and political topics with China's leaders, but it remains to be seen if the talks can recover from the drama involving the fate of the blind activist Chen Guangcheng, who took refuge in the U.S. Embassy and then was turned over to the Chinese under circumstances that no one seems to agree on.

A Look Ahead

This week there will be only a handful of economic updates – the latest on

wholesale inventories, the trade balance and the producer price index – but investors will have plenty to mull over, especially as the new governments in France and Greece settle in and decide if they can make good on their campaign pledges without throwing the eurozone into a state of turmoil.



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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.

The 10-year Treasury Note Rate is the yield on U.S. Government issued 10-year debt.

NYMEX Crude Future is the futures price on a barrel of oil on the New York Mercantile Exchange.

Euro/U.S. Dollar is the currency exchange rate between the Euro and the U.S. Dollar.

The MSCI EAFE Index measure international equity performance. It comprises the MSCI country indices that represent developed markets outside of North America: Europe, Australasia and the Far East.

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

The European Central Bank (ECB) is the institution of the European Union (EU) which administers the monetary policy of the 17 EU eurozone member states.

The European Union (EU) is an economic and political union of 27 member states which are located primarily in Europe.

The Institute for Supply Management is a not-for-profit U.S. association for the benefit of the purchasing and supply management profession, particularly in the areas of education and research.

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