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FIRST Trust ADVISORS L.P.

Dec, 4 2006

Monday Morning Outlook

Date/Time (CDT)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
12-5 / 7:30 am	Q3 Non-Farm Productivity	+0.4%	**+0.5%**		+0.0%
7:30 am	Q3 Unit Labor Costs	+3.4%	**+3.3%**		+3.8%
9:00 am	Oct Factory Orders	-4.0%	**-6.2%**		+2.1%
9:00 am	Nov ISM Non-Manufacturing	56.0	**58.0**		57.1
12-7 / 7:30 am	Initial Claims	320K	**330K**		357K
12-8 / 7:30 am	Nov Non-Farm Payrolls	105K	**110K**		92K
7:30 am	Nov Manufacturing Payrolls	-15K	**-8K**		-39K
7:30 am	Nov Unemployment Rate	+4.5%	**+4.5%**		+4.4%
7:30 am	Nov Average Hourly Earnings	+0.3%	**+0.3%**		+0.4
7:30 am	Average Weekly Hours	33.9	**33.9**		33.9

The Shrinking Dollar

Falling oil prices pulled the trade deficit in September 2006 ($64.3 billion) below its level of September 2005 ($64.97 billion). The October deficit should be smaller still. But the shrinking trade deficit has not helped the US dollar.

In the past seven weeks, the dollar has fallen 6.6% against the Euro (down 12.7% this year) and 3.5% against the Japanese yen (down 2.1% for the year). The Chinese yuan has reached a new high (5.7% higher than in July 2005) and the British pound is at a 14-year high against the dollar.

For many, this decline in the dollar is long overdue. For at least the past 20 years, conventional wisdom has argued that a large US trade deficit would force the dollar to decline. In the past three years, fears of a slowdown in US growth have caused many analysts to become permanent dollars bears.

But focusing on the trade deficit, the amount of Treasury bonds held by foreign investors, the budget deficit, or the savings rate, is a mistake. Like any commodity, the value of the dollar is a function of supply and demand. And because the Federal Reserve has sole control over the supply of dollars, any analysis that does not discuss the Fed would be wrong.

When the Fed is easy; look for a weak dollar. When the Fed is tight; the dollar will be strong. Of course, other central banks could also be tight or easy, and it is the relative policy stances of the central banks that matter. But, in the end, if the Fed wants to stabilize the dollar it can do so easily.

The Euro first began trading in January 1999. Its initial exchange rate against the dollar was $1.18/€. From its inception it tanked, falling to a low of $0.83/€ in October 2000. After bouncing around for the next nine months, it traded again below 85 cents in July 2001, but then immediately started to move higher – peaking at $1.36/€ in December 2004. The dollar strengthened in the first nine months of 2005, but has been very weak again lately.

Interestingly, Fed policy was very tight in 1999 and 2000 – eventually causing fears of deflation. The dollar soared. The Fed reacted to deflation by making monetary policy excessively loose and the dollar fell. Now, with the Fed on pause and policy not yet tight enough to drain the excess liquidity added the last several years, it should not be a surprise that the dollar has weakened again. Add to this the fact that fiscal policy appears to be shifting as a result of the recent change in Congressional leadership. Tax hikes and protectionism, regulation and growth of government, when combined with easy money are a perfect recipe for inflation and dollar weakness. Until these policy stances of loose money and activist government change, a shrinking dollar is highly likely.

Week of December 11, 2006

Date/Time (CDT)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
12-12 / 7:30 am	Oct International Trade Balance	-$63.5B	**-$61.2B**		-$64.3B
12-13 / 7:30 am	Nov Retail Sales	+0.4%	**+0.5%**		-0.2%
7:30 am	Nov “Core” Retail Sales	+0.3%	**+0.4%**		-0.4%
12-14 / 7:30 am	Nov Import Prices	-0.4%	**+0.4%**		-2.0%
7:30 am	Nov Export Prices	-0.1%	**+0.3%**		-0.4%
12-15 / 7:30 am	Nov Consumer Price Index	+0.2%	**+0.2%**		-0.5%
7:30 am	“Core” CPI	+0.2%	**+0.3%**		+0.1%
8:15 am	Nov Industrial Production	+0.2%	**+0.3%**		+0.2%
8:15 am	Nov Capacity Utilization	+82.3%	**82.4%**		+82.2%

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