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FIRST Trust ADVISORS L.P.

Apr 24, 2006

# Monday Morning Outlook

| Date/Time (CST) | U.S. Economic Data | Consensus | First Trust | Actual | Previous |
|---|---|---|---|---|---|
| 4-25 / 9:00 am | Mar Existing Home Sales | 6.65M | 6.80M | | 6.91M |
| 4-26 / 7:30 am | Mar Durable Goods Orders | +1.6% | +4.0% | | +2.7% |
| 9:00 am | Mar New Home Sales | 1.10M | 1.15M | | 1.08M |
| 1:00 pm | Fed Beige Book | | | | |
| 4-27 / 7:30 am | Initial Unemployment Claims | 305K | 297K | | 303K |
| 4-28 / 7:30 am | Q1 Real GDP: Advance | +5.0% | +5.0% | | +1.7% |
| | Q1 GDP Price Index: Advance | +2.8% | +2.8% | | +3.5% |
| 9:00 am | Apr Chicago PMI | 58.0 | 61.0 | | 60.4 |

## Oil, the Economy and Inflation

During the seventeen years between 1986 and 2002, the price of West Texas Intermediate crude oil averaged $20.53/bbl. In 2003, the average price for oil reached $31.14/bbl., in 2004 it was $41.44/bbl., in 2005 it was $56.47/bbl., and during the first three months of 2006 the price has averaged $63.35/bbl. On Friday, the price rose above $75/bbl., an all-time high in nominal terms.

Most commentary about these price increases have focused on specific issues of supply and demand in the energy markets. In fact, most commentary about any commodity price movements focuses on specific, market-oriented issues, such as Chinese demand, production problems, or weather.

This focus on microeconomic issues misses the impact of monetary policy. In the 1970s, oil and other commodity prices moved up as Fed policy was inflationary. During the 1980s and most of the 1990s, monetary policy was focused on bringing inflation down. It became a widely followed maxim during that period that investors should shy away from “stuff” and focus on value-creating “ideas.” This trend accelerated in 1997 when Fed policy became deflationary.

With prices low, investment in commodity production was deterred. As a result, once the Fed started fighting deflation, commodity prices, including gold, silver, copper, and energy products started rising again. Yes, other factors, such geopolitical instability and capacity issues, have played a role. But, the underlying monetary policy environment is still the fundamental driving force beneath these movements.

After adjusting for inflation, the price of oil is still below its peak of $85/bbl. in the second quarter of 1980. Yes, energy prices are rising rapidly, and consumers are spending $244 billion more on energy per year today than they did in 2001. However, total after-tax incomes are running $1.7 trillion higher. In other words, consumers have $1.48 trillion more to spend today – *even after subtracting energy costs* – than they did in 2001.

When we jump in a bathtub the water level rises significantly. The ocean is another story. The more liquidity in an economy, the easier it is to absorb rising prices. This is why record-high energy price have not caused the economic damage that many expected. Inflation is both a cause of rising prices and a cushion against them.

***Week of May 1, 2006***

| Date/Time (CST) | U.S. Economic Data | Consensus | First Trust | Actual | Previous |
|---|---|---|---|---|---|
| 5-1 / 7:30 am | Mar Personal Income | +0.4% | +0.4% | | +0.3% |
| | Mar PCE | +0.4% | +0.4% | | +0.1% |
| 9:00 am | Mar Construction Spending | +0.5% | +0.3% | | +0.8% |
| | Apr ISM Manufacturing Index | 55.0 | 56.5 | | 55.2 |
| Sometime During | Apr Domestic Auto Sales | 5.4M | 5.4M | | 5.3M |
| the Day | Apr Domestic Light Truck Sales | 7.7M | 7.6M | | 7.7M |
| 5-2 / 9:00 am | Mar Factory Orders | +1.0% | +2.2% | | +0.2% |
| | Apr ISM Non-Manu Index | 59.0 | 62.0 | | 60.5 |
| 5-4 / 7:30 am | Q1 Productivity | +3.6% | +4.0% | | -0.5% |
| | Q1 Unit Labor Costs | +1.3% | +1.5% | | +3.3% |
| 5-5 / 7:30 am | Apr Non-Farm Payrolls | +225K | +205K | | +211K |
| | Apr Manufacturing Payrolls | 0K | +5K | | -5K |
| | Apr Unemployment Rate | 4.7% | 4.6% | | 4.7% |
| | Apr Average Hourly Earnings | +0.3% | +0.3% | | +0.2% |
| | Apr Weekly Hours | 33.8 | 33.9 | | 33.8 |

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*Consensus forecasts come from Insight Economics, LLC*