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FIRST Trust ADVISORS L.P.

Jul 3, 2006

# Monday Morning Outlook

| Date/Time (CDT) | U.S. Economic Data | Consensus | First Trust | Actual | Previous |
|---|---|---|---|---|---|
| 7-3 / 7:30 am | May Construction Spending | +0.2% | +0.1% | **-0.4%** | -0.2% - r |
| 9:00 an | Jun ISM Manufacturing Index | 55.0 | 57.0 | **53.8** | 54.4 |
| Sometime During | Domestic Auto Sales | 5.4M | 5.5M | | 5.3M |
| the Day | Domestic Light Truck Sales | 7.2M | 7.1M | | 7.0M |
| 7-5 / 9:00 am | May Factory Orders | +0.1% | 0.3% | | -1.8% |
| 7-6 / 7:30 am | Initial Unemployment Claims | 315K | 305K | | 313K |
| 9:00 am | Jun ISM Non-Man | 59.0 | 61.0 | | 60.1 |
| 7-7 / 7:30 am | Jun Non-Farm Payrolls | 158K | 195K | | +75K |
| | Jun Manufacturing Payrolls | 0K | 5K | | -14K |
| | Jun Unemployment Rate | 4.6% | 4.6% | | 4.6% |
| | Jun Average Hourly Earnings | +0.3% | +0.4% | | +0.1% |
| | Jun Weekly Hours | 33.8 | 33.8 | | 33.8 |

**Hard Money, Low Taxes**

A recent Bloomberg/LA Times poll, taken before last week's Fed rate hike, found that by a 65% to 22% margin Americans opposed another Fed rate increase. The public opposition to rate hikes (or hard money) is a time honored tradition dating back hundreds, if not thousands of years. Most people think low interest rates (and easy money) are good for the economy. Part of this is driven by governments (both elected and unelected) who have historically used monetary policy for political or financial gain.

Before central banks, when gold or sliver standards were widely used, the Romans (and others) clipped coins. By clipping off a bit of each coin as it came through the treasury, and then using those clippings to make new coins, the currency was debased. This was an underhanded form of taxation, which also caused inflation.

In 1896, before the US Federal Reserve System was created, William Jennings Bryan ran for President against William McKinley and famously argued against a gold standard by saying, "you shall not crucify mankind on a cross of gold." This was populist rhetoric designed to appeal to farmers and others who were watching the price of their products fall as productivity improved. They blamed falling prices on hard money and advocated a more inflationary policy.

Following the invention of central banking, governments refined their manipulation. By forcing monetary authorities to print money (hold interest rates low) just before an election, the economy is artificially boosted. While this may help a politician in the short-run, it creates inflation and eventually drives up interest rates. All of this interferes with entrepreneurship and wealth creation.

Realizing this, some governments, after manipulating the money supply have then attempted to use force to alter the results. Around the time of the French Revolution, the guillotine was used to punish those who raised prices. In a more civilized fashion, Richard Nixon instituted wage and price controls in the early 1970s to stop the inflation caused by his monetary mistake of closing the gold window. This did not work. The controls distorted the economy and once they were removed, prices soared.

Ludwig von Mises, our favorite dead economist, said that sound money was just as important for a country as a Bill of Rights or a Constitution. A currency should hold its value over time, just like the length of a foot or yard, or the amount of gasoline in a gallon. If weights and measures were uncertain, chaos would result. Stable currencies are even more important. This is why central bank independence is so important. Politicians will always support short-term manipulation of the economy and ignore long-term problems.

All of this brings us back to the current environment. In recent months, whenever the Fed has indicated that a "pause" in rate hikes may be in the offing, the value of the dollar has fallen, while commodity prices have soared. The markets are clearly saying that if the Fed pauses now it will be too soon and inflation will continue to rise. While the public may not want interest rates to move higher today, it is clearly in the best interest of the economy to have the Fed tighten enough to end inflation. If it does not do so, interest rates will rise even more in the future. As President Reagan and Fed Chairman Paul Volcker showed, hard money and low taxes are the only recipe for prosperity and low interest rates.

***Week of July 10, 2006***

| Date/Time (CDT) | U.S. Economic Data | Consensus | First Trust | Actual | Previous |
|---|---|---|---|---|---|
| 7-12 / 7:30 am | May Trade Balance | -$65.0B | -$65.0B | | -$63.4B |
| 7-14 / 7:30 am | June Retail Sales | +0.5% | +0.6% | | +0.1% |
| | Jen Retail Sales Ex Autos | +0.4% | +0.5% | | +0.5% |
| | Jun Import Prices | +0.5% | +0.4% | | +1.6% |
| | Jun Export Prices | +0.4% | +0.3% | | +0.7% |

**Brian S. Wesbury; Chief Economist** **Bill Mulvihill; Senior Economist**