Wavering consumer confidence and lower revenues from Citi and Bank of America have stocks under water today and slightly down for the week. Earnings season kicked off with a strong report from Alcoa, but there have been some hits and misses since then. For example, Intel reported a recorded a blockbuster quarter, but Google's profits missed estimates. From a bottom line standpoint, Bloomberg reports that of the 23 companies in the S&P 500 that have reported for the quarter, only three haven't exceeded forecasts for earnings-per-share. However, EPS is only one measure and there are many moving parts including today's revenue misses by the banks. The Dow is currently down 40 points compared to last Friday's close, while the Nasdaq is unchanged and the S&P off 6. Yields continue to know no lower boundaries, with the 2-year hitting a record low. Yields are currently 0.59%, 1.68%, 2.94%, and 3.94%, respectively for the 2-, 5-, 10-, and 30-year notes/bond. The key release for the week was Advance Retail Sales, although the disappointment in manufacturing activity that we'll get to later raised a few eyebrows. But first, sales fell 0.5% in June, and were lower than the forecasted 0.3% drop. Auto sales, which were off 2.3%, drove results, although sales less autos were down 0.1% due to price drops at gas stations. The significant ex auto and gas gauge rose 0.1%, but overall, weakness across a variety of areas such as grocery stores (-0.5%), furniture (-1.1%) and sports, books, and music (-1.4%) put a damper on the release. Furthermore, prior month readings were revised lower, and along with June, should serve to push Q2 consumption estimates, and thus GDP, down.

The government auctioned $69 billion in coupon Treasuries this week with decent demand overall. The $35 billion 3-year sale went so-so, selling to yield 1.055%, approximately one basis point higher than pre-auction forecasts. The bid-to-cover at 3.20 was quite good for a 3-year, but was driven mostly by primary dealers. Indeed, dealers were left with 45.1% of the issue, as only 40.6% went to indirect bidders and 14.3% to direct bidders. The $21 billion 10-year reopening didn't go much better than the 3-year. The notes were awarded at 3.119%, about two basis points higher than pre-auction trading. Similar to the 3-year, the bid-to-cover was a solid 3.09, but was driven by dealers. Final investor demand was respectable with 41.7% and 9.8% going to indirect and direct bidders, respectively. Last, the $13 billion 30-year reopening was the best of the bunch. The long bond was sold to yield 4.080%, approximately one basis point below pre-auction levels, with a bid-to-cover of 2.89, the highest since September. Demand from final investors was good, with indirect bidders taking down 34.7% of the issue, while 16.1% went to direct bidders.

In looking at the production part of the economy, signs point to a moderation compared to the last few months. On the positive side, Industrial Production was up 0.1% in June, lower than the 1.3% from May but higher than estimates of -0.1%. Utility output (+2.4%) and a probably better than expected reading (-0.4%) in the manufacturing gauge helped. In addition, mining (+0.4%) didn't experience a significant pullback, considering this section includes oil and gas drilling, which one would think would be badly affected by the spill in the Gulf. Capacity Utilization in June logged in at 74.1%, exactly in line with estimates and May's downwardly revised figure. Moving on to Empire Manufacturing for July, the numbers aren't as solid. The index fell from 19.57 from the month prior to 5.08, with analysts way off in expecting 18.00. Orders (10.13 vs. 17.53), shipments (6.31 vs. 17.53), and employment (7.94 vs. 12.35) all contracted. The Philly Fed index finished at 5.1, below 8.0 from the month before and again off analysts too high forecasts of 10.0. Orders (-4.3 vs. 9.0) slipped into negative territory, while shipments (4.0 vs. 14.2) slowed and employment (4.0 vs. -1.5) ticked higher.

As long as one believes in the validity of the CPI and PPI measures, inflation is benign. First, on the producer end, headline PPI shrank 0.5% in June, driving the YoY down from 5.3% to 2.8%. A large decline in food prices (-2.2%) and moderation in energy prices (-0.5%) were the causes for the plunge in the headline number. Core PPI rose 0.1% (MoM), while the yearly change edged lower from 1.3% to 1.1%. Softness in the motor vehicle components segment put the breaks on core. On the consumer front, the headline number fell for the third straight month, sliding 0.1% to help push the YoY change down from 2.0% to 1.1%, as gasoline prices have decreased. Core CPI, on the other hand, was up 0.2%, ahead of both estimates and May's 0.1% increase. The YoY change stayed at 0.9%. The shelter component was the main driver to core's uptick, as it comprises more than 40% of the index and has turned higher since bottoming in the spring. Other sectors to note that helped push core were used cars (+0.9%), clothing (+0.8%), medical care (+0.3%), and personal care (+0.2%).

The FOMC Minutes for the June meeting were perhaps a bit more hawkish than investors were expecting. The release didn't have much market impact, but there was little talk about what the Fed would do if the economy does not recover as expected, especially considering the most recent economic data and headlines. In fact, the Minutes contained discussion around the exit strategy with a minor nod at the end for a deteriorating economy, stating, "members noted that in addition to continuing to develop and test instruments to exit from the period of unusually accommodative monetary policy, the Committee would need to consider whether further policy stimulus might become appropriate if the outlook were to worsen appreciably." The Fed lowered its GDP forecast for 2010 to 3.3% from 3.5% and for 2011 to 3.9% from 4.0%.

In other news, the Import Price Index fell 1.3% (MoM) in June, pulling the YoY number down from 8.7% to 4.5%. Petroleum prices were down 4.4% and the ex-fuels segment dropped 0.6% due to a retraction in metals, capital goods, and consumer goods. TIC Flows indicate that foreign investors slowed their purchases of U.S. securities from $81.5B in April to $35.4B in May.

The continuation of earnings season will likely hold center stage next week, as the economic calendar will be on the light side. Scheduled for release are the NAHB Housing Market Index, Housing Starts, Building Permits, Existing Home Sales, and Leading Indicators.

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Yield Analysis as of July 15, 2010

Yields

	Yesterday	1 Week from Yesterday	6/30/2010	12/31/2009	12/31/2008
2yr Note	0.61	0.62	0.61	1.14	0.77
5yr Note	1.76	1.81	1.78	2.68	1.55
10yr Note	3.00	3.03	2.93	3.84	2.21
30yr Bond	3.99	4.01	3.89	4.64	2.68

Spread (in basis points)

	Yesterday	1 Week from Yesterday	6/30/2010	12/31/2009	12/31/2008
Invst. Grade Corporate*	198	206	209	190	604
High Yield*	673	698	713	639	1812
Global HY and EM*	565	586	601	551	1456

*Merrill Lynch Corporate, High Yield Master II, and Global High Yield and Emerging Markets

Municipal Yields and Taxable Equivalent Yields

	2 Year	5 Year	10 Year	20 Year	30 Year
AAA G.O.'s	0.48	1.48	2.87	4.09	4.38
% of Treasury	79%	84%	96%	109%	110%
35% Taxable Eq.	0.74	2.28	4.42	6.29	6.74
30% Taxable Eq.	0.69	2.11	4.10	5.84	6.26
25% Taxable Eq.	0.64	1.97	3.83	5.45	5.84

*Municipal yields according to Bloomberg's AAA national general obligation curve as of yesterday's close

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