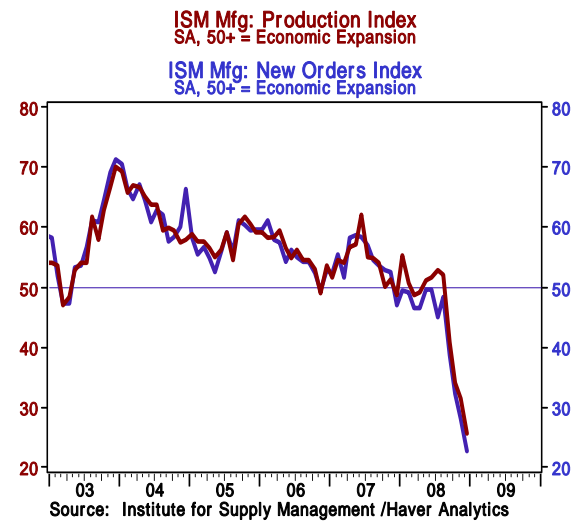
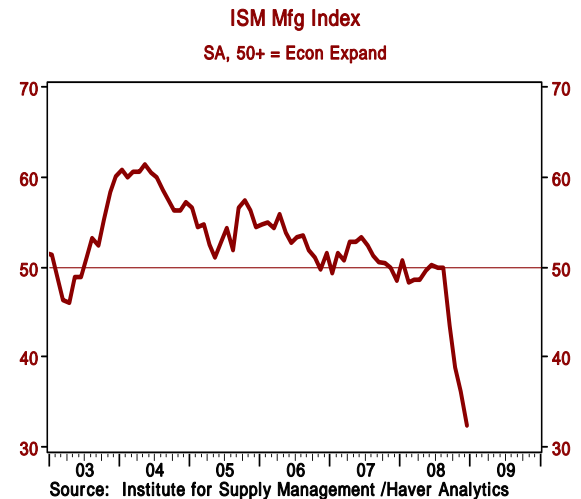


DECEMBER ISM MANUFACTURING INDEX

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- The ISM Manufacturing index fell to 32.4 in December from 36.2 in November. The consensus had expected a decline to 35.4. (Levels higher than 50 signal expansion; levels below 50 signal contraction).
- The output components of the overall index continued to decline. The index for new orders fell to 22.7 from 27.9; the production index fell to 25.5 from 31.5; and the employment index declined to 29.9 from 34.2. The new orders and production indexes are at their lowest levels ever recorded and the employment index is the lowest since 1982.
- The prices paid index declined to 18.0 from 25.5, and is now at the lowest level since 1949.

Implications: The US manufacturing sector contracted rapidly in December, with the ISM Manufacturing index hitting the lowest level since the intense recession of 1980. The sub-indexes for both production and new orders are the lowest on record since 1948, which is when the Institute for Supply Management started these measures. Barring a collapse in US automakers, which is now unlikely given the willingness of the federal government to support the industry, the ISM index is probably at or very close to a bottom. Manufacturing will continue to weaken in the months ahead but not as intensely as in the past few months, which should mean the ISM index starts to move up from here, but stays below 50. We are still forecasting real GDP will drop at about a 6% annual rate in the fourth quarter due to the “risk aversion hysteria” that struck the economy and financial system with the collapse of Lehman Brothers in September. However, with leading indicators of risk aversion starting to ease (such as the gap between 3-month LIBOR and 3-month T-bills plus the 2-year swap spread), we believe a recovery will take hold this Spring. On the inflation front, 2008 was a year of wild swings. In June, the ISM prices paid index was the highest since 1979; now, it’s the lowest since 1949. We expect some broad-based year-to-year price measures, like the CPI, to go negative in the months ahead, but that inflation will start to re-emerge by late 2009. Then, in 2010 and beyond, inflation will again become a problem as a result of the Federal Reserve’s monetary ease.



Institute for Supply Management Index <i>Seasonally Adjusted Unless Noted: 50+ = Econ Growth</i>	Dec-08	Nov-08	Oct-08	3-month moving avg	6-month moving avg	Year-ago level
Business Barometer	32.4	36.2	38.9	35.8	41.8	48.4
New Orders	22.7	27.9	32.2	27.6	35.8	46.9
Production	25.5	31.5	34.1	30.4	39.5	48.6
Inventories	38.8	39.1	44.3	40.7	43.3	45.4
Employment	29.9	34.2	34.6	32.9	40.4	48.7
Supplier Deliveries	44.9	48.4	49.2	47.5	50.1	52.6
Order Backlog (NSA)	23.0	27.0	29.5	26.5	33.5	43.0
Prices Paid (NSA)	18.0	25.5	37.0	26.8	49.9	68.0
New Export Orders	35.5	41.0	41.0	39.2	46.8	52.5

Source: National Association of Purchasing Management

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