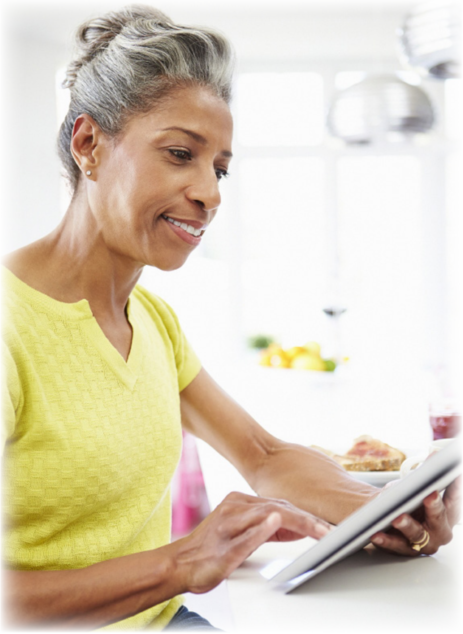
Reach | *September*



A TWO-MINUTE ECONOMICS COURSE

Economics isn't a fun subject in or out of school, but being familiar with some basic facts about the U.S. economy may help you make better investment decisions for your retirement plan account.

GDP — Measuring Overall Growth

Every quarter, the U.S. Commerce Department estimates the total value of the goods and services produced in the United States during the past three months. Focus on the amount the GDP has changed, not the number itself. The change in the GDP measures the rate of overall economic growth. Slow growth can mean companies' profits are shrinking, which means that stock prices may decline, too. A drop in the GDP for two quarters in a row indicates the economy could be in a recession. When the GDP is growing, companies are doing well and, usually, stocks are too.

Interest Rate Changes — Pushing Bond and Stock Values

The number to watch is the 10-year Treasury yield — the interest on newly issued U.S. Treasury bonds with a 10-year maturity. The bond market sets this yield, not the government.

Changes in interest rates affect bond values. Usually, values drop when interest rates rise, and values rise when rates fall. Bonds have a fixed interest rate. So, when newly issued bonds offer a higher rate than existing bonds, it pushes the market value of the previously issued bonds down so that their actual return is in line with the new issues.

Stocks also react to changes in interest rates. Higher rates increase companies' borrowing costs, which lowers the companies' earnings potential. Because stock values generally reflect earnings prospects, rising interest rates are generally bad for stocks, while falling rates are generally good.

CPI — Indicating the Inflation Rate

The U.S. Department of Labor calculates the monthly Consumer Price Index (CPI) by comparing the current prices of a set list of goods and services — housing, food, clothing, transportation, medical care, etc. — with prices during a base period. The change in the CPI is an important indicator of the rate of inflation. Stock prices often rise when inflation is low and fall when inflation increases.

Unemployment Rate — Signaling Future Inflation

The U.S. Department of Labor also tracks the percentage of U.S. workers who are unemployed. The monthly unemployment report can forecast future inflation. A low unemployment rate indicates a possibility that inflation will rise because workers' increased spending power drives prices up. High unemployment means less consumer spending and, therefore, less pressure on prices.

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