

Economics Group

Weekly Economic & Financial Commentary

U.S. Review

Economic Recovery: Different Pace, Different Shape

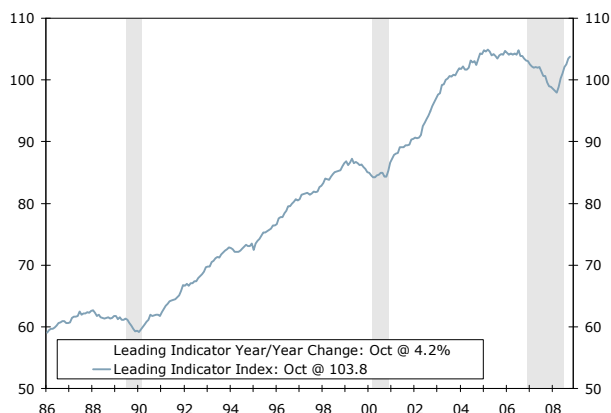
- The leading economic index signals modest growth will continue into next year. Yet, the pace of that growth is consistent with a below-average recovery compared to the first year of prior recoveries as well as a possible longer-term downshift in trend growth.
- Housing starts were clearly disappointing to the “V”-shaped recovery crowd. “Core” retail sales are up modestly compared to the first year of the 2002 recovery, and the outlook for holiday sales is weak. Still, inflation data which may start exceeding the market’s benign expectations suggest that we remain cautious.

Global Review

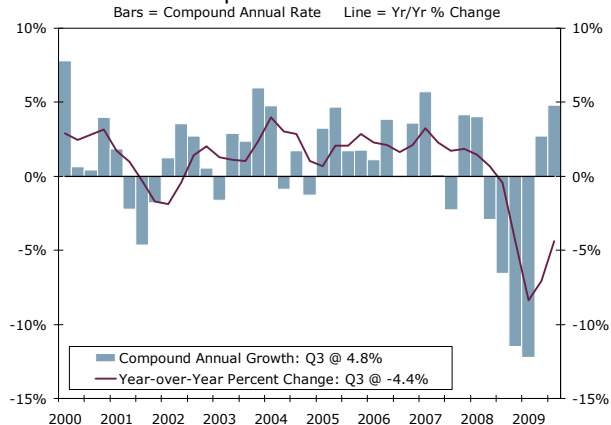
Japanese Economy Continues to Expand

- Real GDP in Japan rose at an annualized rate of 4.8 percent in the third quarter. Inventories and net exports made important contributions to growth, but consumer spending and capital expenditures also rose in the third quarter.
- Japan continues to experience a mild case of deflation. The level of real GDP remains well below the peak that was reached in early 2008, and unemployment has risen to its highest rate in decades. In our view, the Bank of Japan will refrain from raising rates for the foreseeable future.

Leading Indicator Index



Japanese Real GDP



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Wells Fargo U.S. Economic Forecast														
	Actual				Forecast				Actual			Forecast		
	2009				2010				2006	2007	2008	2009	2010	2011
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q						
Real Gross Domestic Product ¹	-6.4	-0.7	3.5	2.0	2.7	2.7	2.5	2.2	2.7	2.1	0.4	-2.5	2.4	2.4
Personal Consumption	0.6	-0.9	3.4	-1.2	0.9	1.2	1.3	1.3	2.9	2.6	-0.2	-0.7	0.8	1.4
Inflation Indicators ²														
“Core” PCE Deflator	1.7	1.6	1.3	1.4	1.4	1.2	1.2	1.3	2.3	2.4	2.4	1.5	1.3	1.6
Consumer Price Index	-0.2	-0.9	-1.6	1.2	2.0	2.0	1.5	1.4	3.2	2.9	3.8	-0.4	1.8	2.0
Industrial Production ¹	-19.0	-10.3	5.2	6.1	2.3	3.1	2.8	4.2	2.3	1.5	-2.2	-9.9	2.8	4.1
Corporate Profits Before Taxes ²	-19.0	-12.6	-10.5	20.0	22.0	16.0	10.0	8.5	10.5	-4.1	-11.8	-7.0	13.9	8.0
Trade Weighted Dollar Index ³	83.2	77.7	74.3	73.5	76.1	78.6	81.0	81.8	81.5	73.3	79.4	73.5	81.8	82.8
Unemployment Rate	8.1	9.3	9.6	10.2	10.3	10.6	10.8	10.8	4.6	4.6	5.8	9.3	10.6	10.6
Housing Starts ⁴	0.53	0.54	0.59	0.60	0.60	0.65	0.68	0.71	1.81	1.34	0.90	0.56	0.66	0.80
Quarter-End Interest Rates														
Federal Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	5.25	4.25	0.25	0.25	0.50	3.25
Conventional Mortgage Rate	5.00	5.42	5.06	5.10	5.20	5.30	5.30	5.40	6.14	6.10	5.33	5.10	5.40	6.00
10 Year Note	2.71	3.53	3.31	3.50	3.60	3.60	3.60	3.70	4.71	4.04	2.25	3.50	3.70	4.40

Forecast as of: November 11, 2009
¹ Compound Annual Growth Rate Quarter-over-Quarter
² Year-over-Year Percentage Change

Together we'll go far



U.S. Review

Doesn't Look Like a Duck...Doesn't Quack Like a Duck

The leading economic index increased 0.3 percent in October and has risen for the past seven months. This implies modest growth will continue into next year. Yet, two elements of the gain don't quite look like the usual recovery. One, the pace of the improvement fell sharply from the one percent average monthly gain over the prior six months. Second, the components of the gains reveal government efforts (money growth, the yield curve) that are more reflective of short-term government efforts than longer-term sustainable private sector recovery. Our outlook for the next two quarters is for sub-par growth of 2.4 percent. In many aspects this recovery does not look like the typical recovery. On the real economy side, housing starts and retail sales do not fit the typical strong pattern of prior recoveries. These indicators are clearly disappointing to the "V"-shaped recovery crowd.

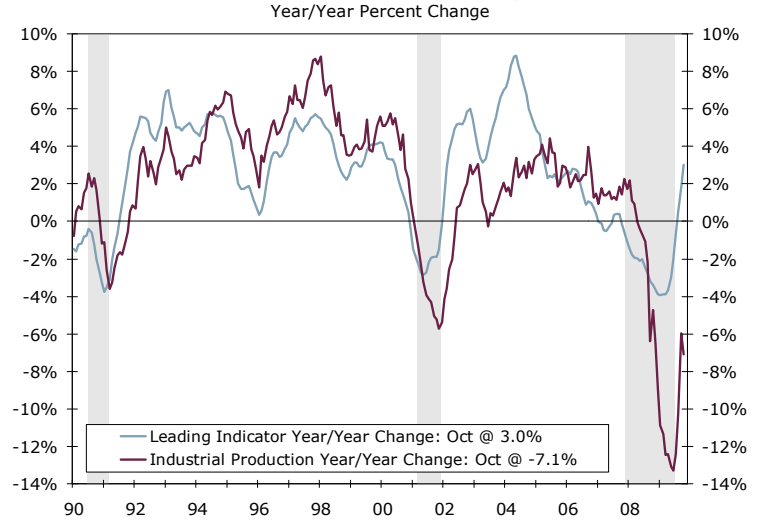
Housing starts fell in October as the first-time home-buyer tax credit came to an end. Housing, traditionally a booming business in a recovery, is flat without federal band-aids. This indicates that the private sector economy, still suffering from credit/wealth problems as well as job losses and low confidence, cannot sustain a rapid housing recovery. Moreover, "core" retail sales are below the pace of the first year of the 2002 recovery. In addition, our outlook for holiday sales is for a second year of declines—the only declines on record since data began in 1993. Fundamentals are not positive for spending. Unemployment is higher while confidence is down. Earned income from wages & salaries has declined while state sales taxes are up. Finally, consumer credit usage is likely to be constrained on both the demand and the supply side. Consumers will demand less credit as they rebalance. Credit cards companies and retailers will limit the supply of credit as they fear reduced credit quality among consumers.

Another odd aspect of this recovery that may be a greater concern than many investors expect is inflation. This is not the roaring inflation of the Jimmy Carter era but rather, with Treasury rates so low, any modest blip for inflation could sharply alter interest rates and therefore the shape of the recovery. Inflation pressures are often characterized as too much money chasing too few goods. Yet the overwhelming sentiment is that it is too much money that drives the process. Perhaps this time it will be a bit too much money in the face of much less than expected goods. As of October, core CPI goods inflation is up 2.3 percent and the overall CPI is up 3.7 percent over the last three months. Headline inflation has probably bottomed for this cycle.

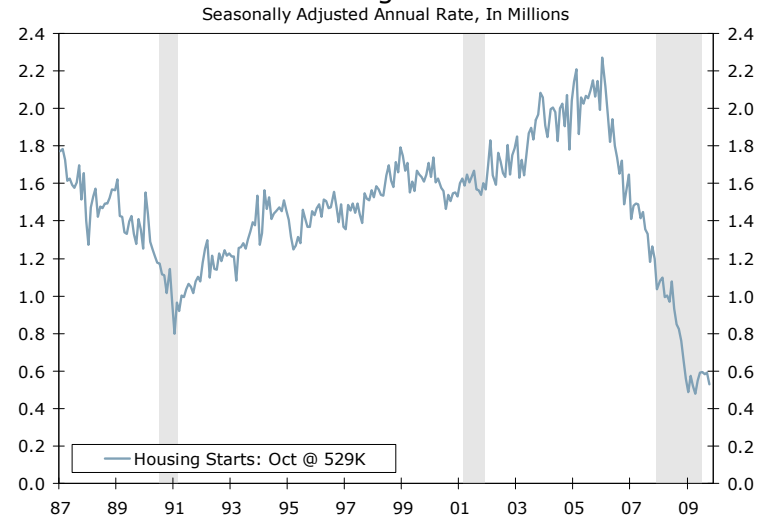
Looking Ahead: Different Duck—Different Strategy

This recovery is not shaping up like prior recoveries. The pace and character of growth is different. The outsized nature of fiscal and monetary stimulus is different. Even the position of the U.S. economy as boxcar, rather than locomotive, differs from the past. Yet, strategic thinking in so many quarters is that while the bird doesn't look like a duck and certainly is not acting like a duck we will treat it like a duck until it becomes a swan—or a vulture.

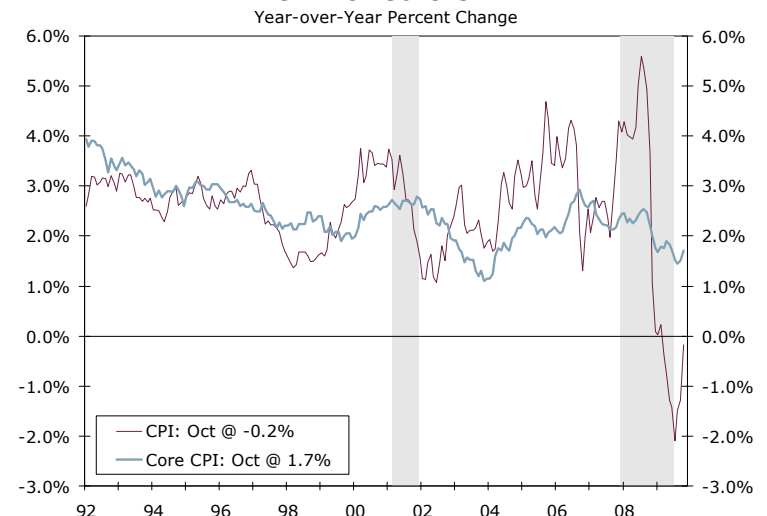
Industrial Production and Leading Indicators



Housing Starts



CPI vs. Core CPI



Consumer Confidence • Tuesday

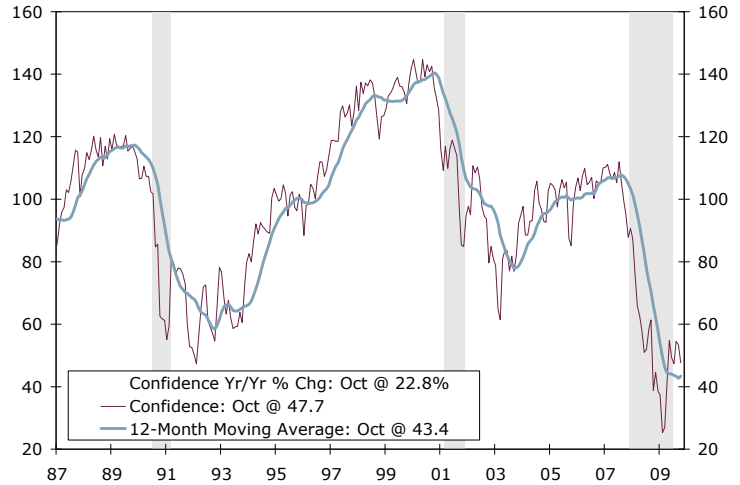
Consumer confidence likely fell for the third consecutive month in November due to its strong correlation with the health of the labor market. While layoffs have clearly decelerated, hiring shows no sign of picking up. The latest data from the Bureau of Labor Statistics show that job openings remained at a record low share of nonfarm employment during the month of September. Consumer confidence will not likely rebound until hiring picks up and that may not be for several more months. Moreover, with the unemployment rate reaching double digits, we expect consumer confidence likely fell slightly to 47.6 in November. Consumer confidence should remain at depressed levels as long as the labor market struggles to gain traction.

Previous: 47.7

Wells Fargo: 47.6

Consensus: 47.0

Consumer Confidence Index
Conference Board



Durable Goods • Wednesday

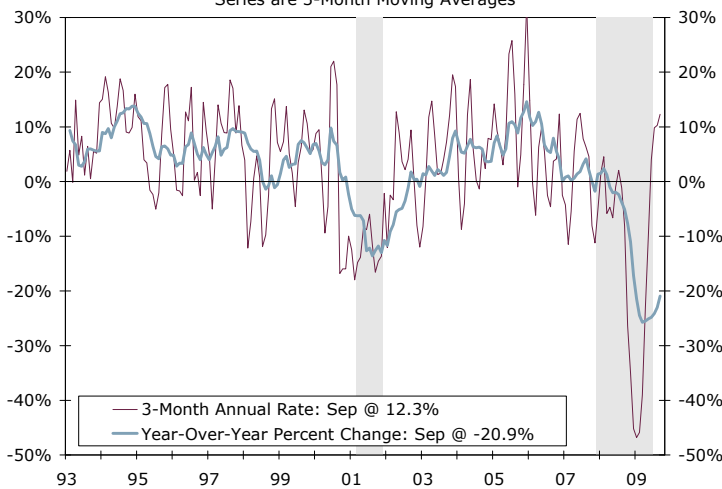
New orders for durable goods rose one percent in September driven by a significant increase in machinery orders, which is an early cycle recovery sector. While orders appear to be moving in the right direction, the “headline” tends to be extremely volatile on a month-to-month basis. The three month annual rate of nondefense capital goods orders excluding aircraft is a better gauge of manufacturing activity, which has risen four consecutive months suggesting future business equipment spending. Moreover, recent consecutive gains in industrial production suggest a similar rise in new durable goods orders in October. Hence, we expect “headline” durable goods orders rose 1.4 percent in October. Further, the continued depletion of inventories and increase in shipments suggest manufacturing activity will continue its positive momentum in coming months.

Previous: 1.0%

Wells Fargo: 1.4%

Consensus: 0.5%

Durable Goods New Orders
Series are 3-Month Moving Averages



New Home Sales • Wednesday

After six consecutive months of increases, sales of new homes retraced part of its gains in September likely due to the scheduled expiration of the first-time home buyers tax credit (new home sales are measured based on contract signings). Uncertainty around the extension likely continued to pressure new home sales lower. We expect new home sales likely fell three percent in October to an annual pace of 390,000. The recent extension and expansion of the tax credit will likely help sales regain its upward momentum in coming months. Inventory levels of unsold homes have continued to improve and have reached levels not seen since the early 1980s with just 251,000 units on the market in September. If sales regain footing, the sustained low levels of inventory suggest a pick up in new construction in coming months.

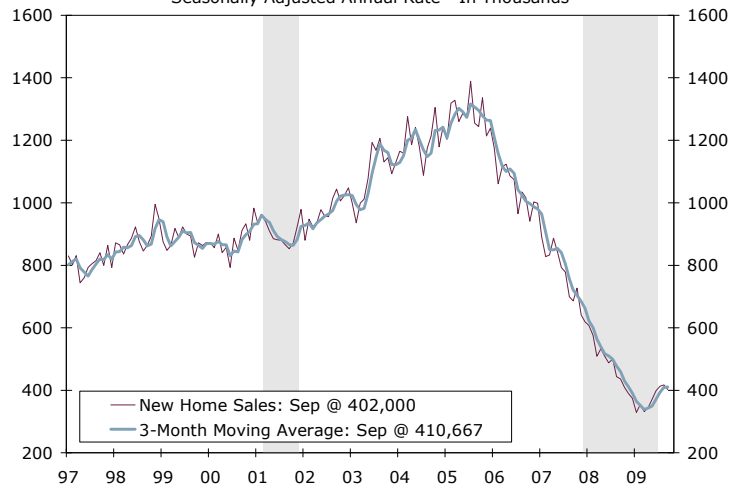
Previous: 402K

Wells Fargo: 390K

Consensus: 410K

New Home Sales

Seasonally Adjusted Annual Rate - In Thousands



Global Review

Japanese Economy Continues to Expand

Recent GDP data show that the expansion in the Japanese economy, which began in the second quarter, continued in the third quarter. To wit, real GDP rose at an annualized rate of 4.8 percent on a sequential basis, which was much stronger than most analysts had expected (see chart on front page). Although the size of the economy is still about seven percent smaller than it was at the peak in the first quarter of 2008, real GDP has risen nearly two percent off of the bottom.

Some of the lift in real GDP was due to inventories. Businesses switched from liquidating stockpiles in the second quarter to building inventories in the third quarter. This inventory swing accounted for 1.4 percentage points of growth. Net exports also boosted growth. Although real imports rose at an annualized rate of 14 percent in the second quarter, real exports grew even faster, shooting up 28 percent. Therefore, economic growth in the rest of the world is helping to lift Japan out of its deepest downturn since the end of the Second World War.

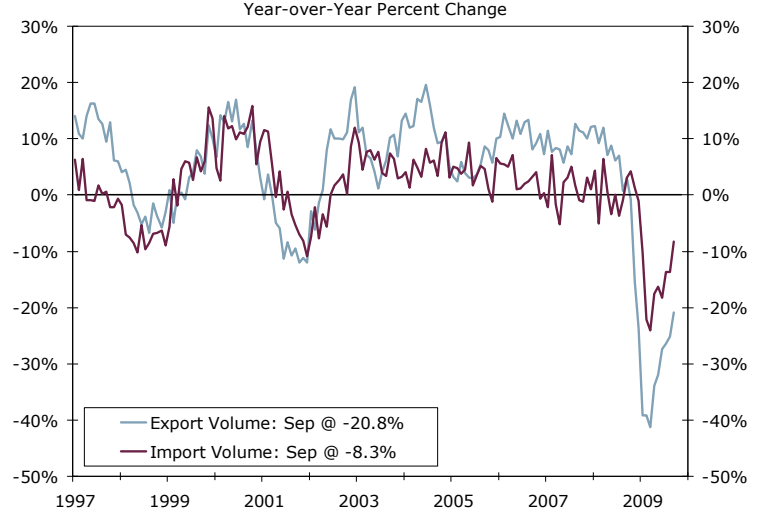
However, it would not be accurate to claim that Japanese growth in the third quarter reflected nothing more than the temporary effects of an inventory cycle and the pull from the rest of the world. For starters, real personal consumption expenditures rose 2.8 percent, the second consecutive quarter in which consumer spending has grown at a strong rate. Employment fell off a cliff last year as the economy tanked (middle chart). However, the labor market is showing tentative signs of stabilizing, and modest employment gains in the months ahead should help to support growth in consumer spending. In that regard, the sharp rise in consumer confidence since the beginning of the year should make consumers a bit more willing to part with some of their hard-earned yen.

In addition, private non-residential investment spending rose nearly seven percent, the first increase in this component in six quarters. In sum, several important components of domestic demand have stabilized and are starting to grow again. Although we do not expect a rapid pace of recovery, we look for growth to remain positive in Japan in the quarters ahead.

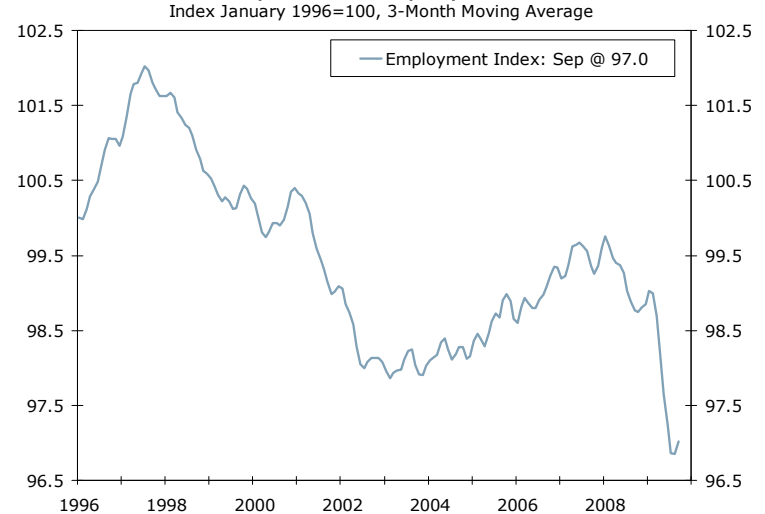
With the economy showing signs of recovery will Japanese policymakers start to tighten economic policy? Hardly. As noted above, the level of economic activity in Japan is still well below its previous peak so we would not characterize the Japanese economy as "strong" at present. Indeed, unemployment has just recently edged down from its highest rate in decades. With the economy still fragile, we do not believe policymakers want to jeopardize the budding recovery by tightening policy.

Moreover, the Japanese economy is experiencing a mild case of deflation as "core" consumer prices have been trending lower for a decade (bottom chart). With no inflationary pressures in the economy, there certainly is no need for the Bank of Japan (BoJ) to raise its main policy rate from only 10 basis points. Indeed, we look for a low interest rate environment in Japan for as far as the eye can see.

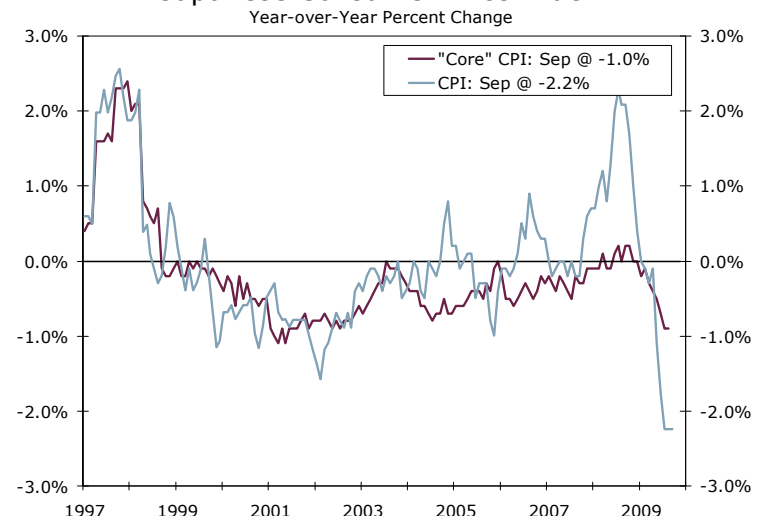
Volume of Japanese Foreign Trade



Japanese Employment



Japanese Consumer Price Index



Euro-zone PMIs • Monday

A number of surveys that measure business sentiment in the Euro-zone will be released next week. The purchasing managers' indices for both the manufacturing and service sectors in the overall euro area have moved above the demarcation line that separates expansion from contraction, and the consensus forecast anticipates that both indices will remain in positive territory when the "flash" estimates for November print on Monday.

The Ifo index of German business sentiment, one of the most widely followed monthly indicators in the Euro-zone, will be released on Tuesday. It too is expected to rise further. Comparable indices for France and Italy are on the docket as well next week. "Hard" data on industrial orders in the euro area in September, which will print on Tuesday, are expected to show their fourth monthly increase.

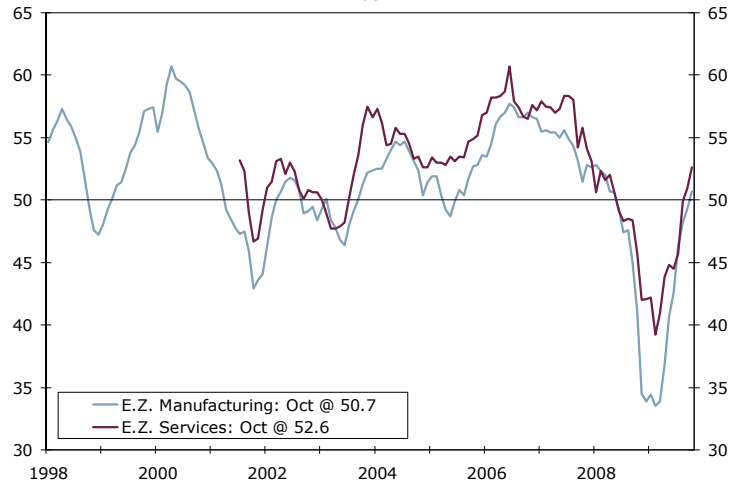
Manufacturing PMI: 50.7

Consensus: 51.3

Service PMI: 52.6

Consensus: 52.6

Euro-zone Purchasing Manager Indices
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Canadian Retail Sales • Monday

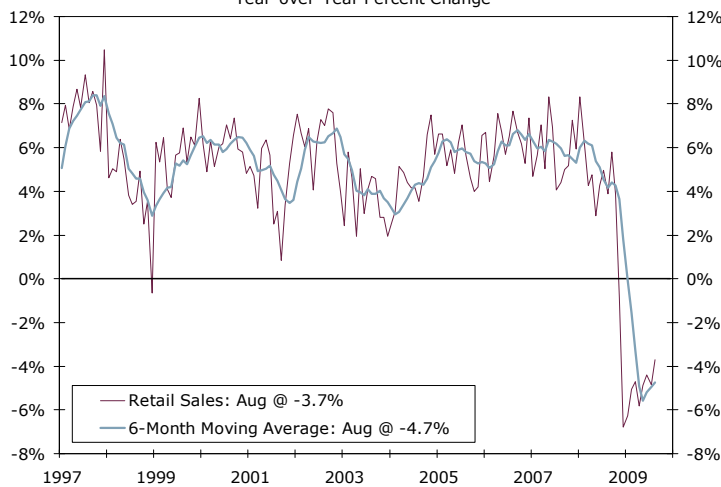
Retail sales in Canada for the month of August came in much better than expected, rising 0.8 percent in the month and signaling strength in Canadian consumer spending.

Total retail sales fell off a cliff at the end of last year as the financial crisis spooked consumers around the world. Between September and December, total retail sales dropped 8.5 percent. But for most of this year, Canadian consumers have been rather resilient. In fact, sales have increased in six out of the eight months reported so far this year and the total level of retail sales are roughly halfway back to their pre-crash levels. Retail sales are expected to increase again in September. The data will print this coming Monday and will give analysts the final month of spending data for the third quarter, which should help hone third quarter GDP forecasts.

Previous: 0.8%

Consensus: 0.6%

Canadian Retail Sales
Year-over-Year Percent Change



Japanese Unemployment • Friday

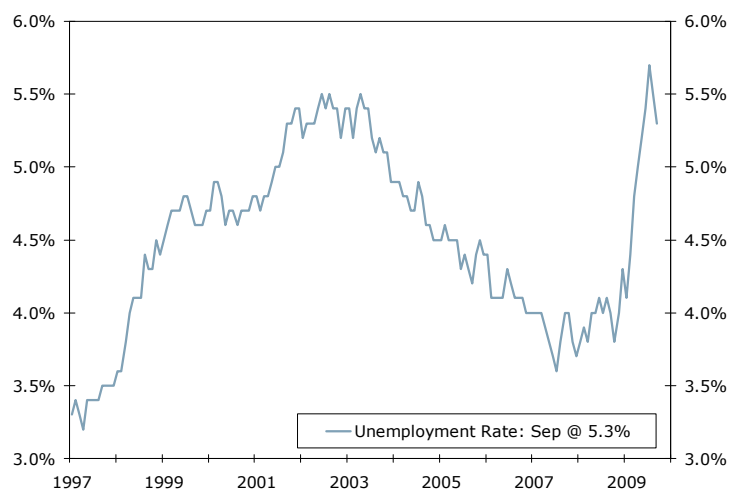
A number of data releases scheduled for next week will give investors some insight into the state of the Japanese economy early in the fourth quarter. For starters, the labor market report for October will show how well employment is holding up. In that regard, the consensus forecast anticipates that the unemployment rate held steady at 5.3 percent in October. Retail sales have risen for three consecutive months. Will that streak continue in October? Investors will find out on Friday.

As noted on page 4, CPI inflation is negative at present. Indeed, the overall CPI was down 2.2 percent in September, and the consensus forecast looks for the rate of deflation to increase to 2.4 percent in October.

Previous: 5.3%

Consensus: 5.3%

Japanese Unemployment Rate



Interest Rate Watch

Policy Conflicts and Exit Strategies

Decision makers face anything but a straightforward outlook for interest rates in the year ahead. Four fundamentals shape the range of possibilities for rates in 2010: growth, inflation, the dollar and fiscal policy.

Economic growth signals are very mixed. This week we noted that leading indicators signaled growth but housing starts were disappointing. Industrial production, a coincident indicator, was disappointing.

Second, inflation, as suggested by this week's consumer price data, indicate that core inflation data has picked up a bit. One bedrock assumption by both the Federal Reserve and the capital markets is that inflation will remain low while unemployment is high. But what about creeping inflation that could undermine such expectations? Today's benign inflation outlook may be just undermining tomorrow's outlook. Once again, the shift in the inflation outlook could be very difficult with long-term Treasury rates in the low three percent range.

Recently, political and economic trends have brought into question the outlook on the dollar and the implications for capital flow and thereby interest rates. With the U.S. fiscal deficit so dependent on foreign buying, a shift in dollar expectations would indicate a change in the outlook for rates rather quickly. Indeed, just rumors in recent years of diminished foreign interest in dollar assets have led to sharp reversals in rates and currency valuations.

Finally, fiscal policy will come to the forefront in early 2010 as President Obama presents his budget outlook for fiscal 2011 and the years ahead. There will be very difficult decisions as investors, both domestic and foreign, expect some suggestion of long-term fiscal discipline. If President Obama fails to deliver on those expectations then the market reaction could be large and destructive as higher rates and a lower dollar would carry negative implications for the economy and further throw the economy off its unstable equilibrium. Interest rate expectations remain unsteady.

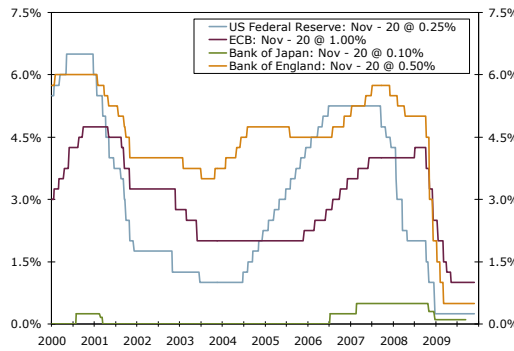
Consumer Credit Insights

Delinquencies and Jobless Claims

Mortgage delinquency rates for both prime and subprime mortgages rose in the third quarter over the second quarter and are significantly above year-ago levels. The delinquency rate for mortgages (number of loans past due by 30 days or more) rose to 9.64 percent in the third quarter from 9.24 percent in the prior quarter. This is not surprising given that delinquencies and foreclosures lag the business cycle. However, the associated high level of jobless claims and the weakness in real disposable income gains suggest that consumer fundamentals do not herald a quick turnaround in delinquencies. Moreover, the increase in delinquencies was entirely concentrated in loans due 90 days or more (4.41 percent vs. 3.88 percent in the second quarter) for both prime and subprime loans. The stress is far beyond that of just subprime mortgages.

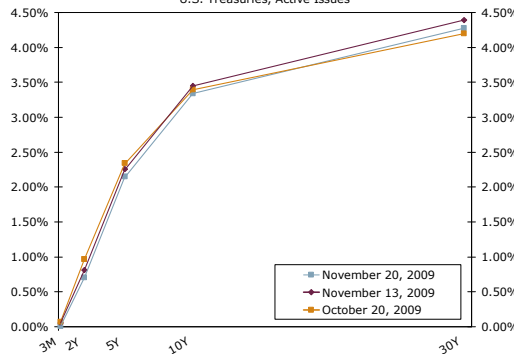
These patterns suggest that delinquencies will continue to put a drag on the economy as it will take time to work through them under conditions of weak job and income gains as well as modest home price gains in distressed real estate markets. High rates of delinquencies and foreclosures will limit the improvement in bank balance sheets and therefore the availability of credit going forward. The workout in housing and the economy will take longer than the traditional "V"-shaped pattern would suggest. Our outlook is for housing starts to remain far below the one million unit pace for both 2010 and 2011.

Central Bank Policy Rates



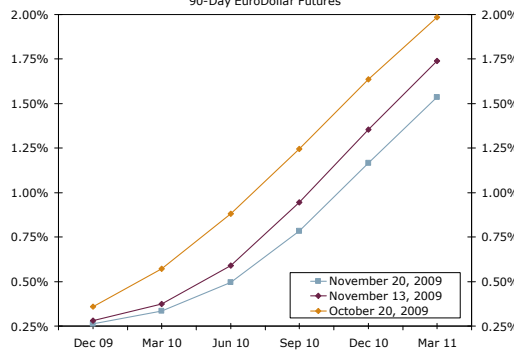
Yield Curve

U.S. Treasuries, Active Issues



Forward Rates

90-Day EuroDollar Futures



Mortgage Data

	Current	Week Ago	4 Weeks Ago	Year Ago
Mortgage Rates				
30-Yr Fixed	4.83%	4.91%	5.00%	6.04%
15-Yr Fixed	4.32%	4.36%	4.43%	5.73%
5/1 ARM	4.25%	4.29%	4.40%	5.87%
1-Yr ARM	4.35%	4.46%	4.54%	5.29%
MBA Applications				
Composite	611.7	627.5	641.0	398.6
Purchase	210.6	220.9	268.8	248.5
Refinance	2,955.4	2,998.2	2,808.0	1,281.2

Source: Freddie Mac, Mortgage Bankers Association and Wells Fargo Securities, LLC

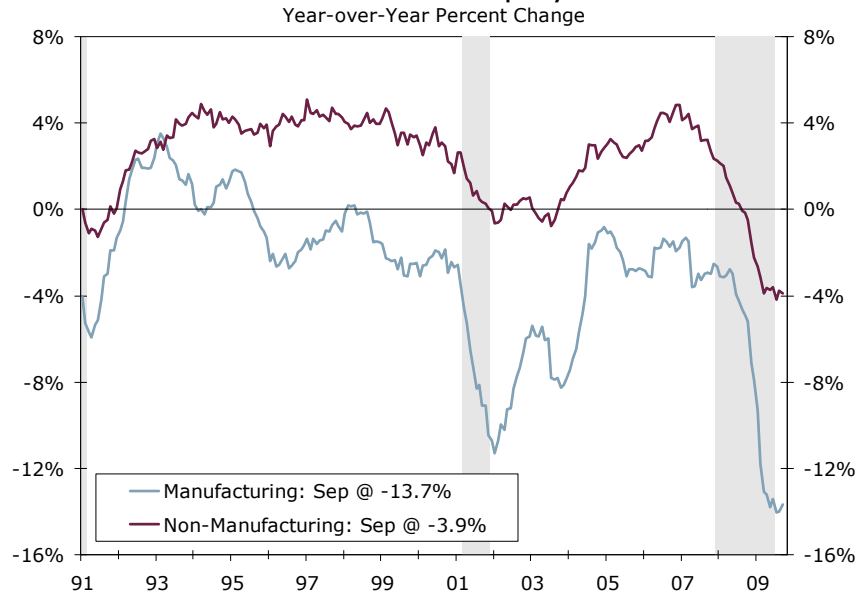
Topic of the Week

North Carolina Faces Difficult Road to Recovery

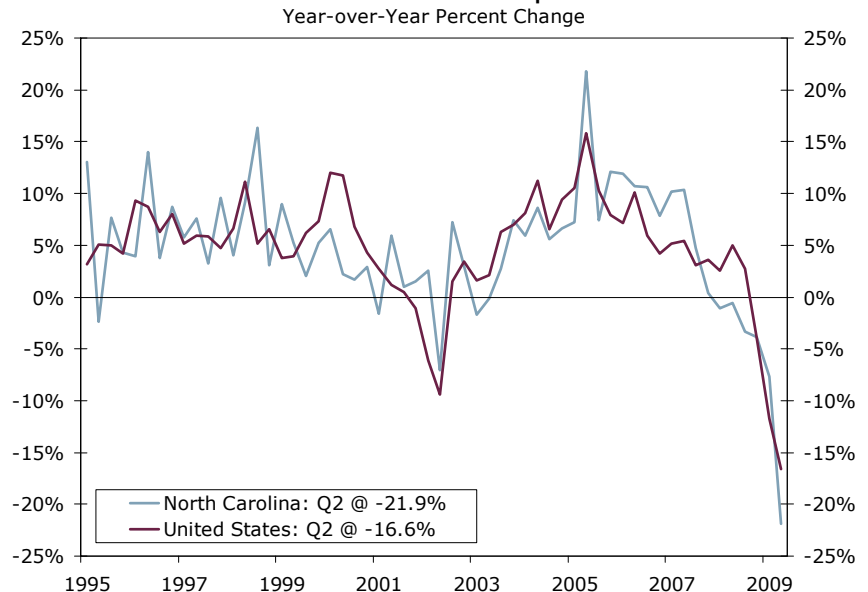
Annually at this time, thoughts of strategic planning become the focus as we all look into next year. For North Carolina, such planning is of paramount focus given the structural economic challenges facing the state. There are no quick fixes. First, on the jobs front, there is a widening gap between the labor force we need and the skills of many of our current workers. This mismatch was noted before but in the past two years the manufacturing base has evolved even more toward higher value-added production that requires ever higher skilled workers. Over the past 20 years, manufacturing job growth has both diminished in quantity of jobs and yet raised the bar in terms of the quality of skills needed. Second, the disparity of economic performance between the rural/small city and large city economies has widened. Rural/small cities that are historically more dependent on a single dominant manufacturing facility increasingly find that the facility is leaving. Meanwhile, growth sectors in the economy such as technology, medicine and financial services continue to favor the major urban areas. Third, the hard reality of educational underachievement continues to pitch a large part of the population into a future of disappointing incomes. North Carolina has long prided itself, with justification, on its elite schools. Yet, the majority of students do not attend these schools. Instead, the need for retraining workers has never been clearer and the continued underperformance in terms of high school graduation rates hobbles the progress of many. Finally, the budget gaps between political promises and our revenue base have never been more evident.

As North Carolina moves forward, the strategic vision cannot be more of the same superficial projections of past performance. Instead, recognizing that future success will require a much broader vision of our goals and the uncertainties of policy initiatives will give the state a chance of success rather than a guarantee of failure as we move into the 21st century. Please see our full report on our website.

North Carolina Employment



State Tax Receipts



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Market Data ♦ Mid-Day Friday

U.S. Interest Rates

	Friday 11/20/2009	1 Week Ago	1 Year Ago
3-Month T-Bill	0.01	0.05	0.02
3-Month LIBOR	0.26	0.27	2.15
1-Year Treasury	0.21	0.32	0.67
2-Year Treasury	0.71	0.81	0.98
5-Year Treasury	2.16	2.25	1.89
10-Year Treasury	3.36	3.42	3.01
30-Year Treasury	4.30	4.35	3.49
Bond Buyer Index	4.35	4.40	5.13

Foreign Exchange Rates

	Friday 11/20/2009	1 Week Ago	1 Year Ago
Euro (\$/€)	1.486	1.490	1.245
British Pound (\$/£)	1.651	1.668	1.473
British Pound (£/€)	0.900	0.894	0.846
Japanese Yen (¥/\$)	89.006	89.657	93.695
Canadian Dollar (C\$/\\$)	1.070	1.052	1.296
Swiss Franc (CHF/\\$)	1.019	1.012	1.225
Australian Dollar (US\$/A\\$)	0.914	0.933	0.611
Mexican Peso (MXN/\\$)	13.085	13.041	13.900
Chinese Yuan (CNY/\\$)	6.828	6.826	6.834
Indian Rupee (INR/\\$)	46.635	46.343	50.150
Brazilian Real (BRL/\\$)	1.733	1.722	2.392
U.S. Dollar Index	75.731	75.334	87.969

Foreign Interest Rates

	Friday 11/20/2009	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	0.67	0.67	4.06
3-Month Sterling LIBOR	0.61	0.61	4.07
3-Month Canadian LIBOR	0.50	0.50	3.00
3-Month Yen LIBOR	0.30	0.31	0.92
2-Year German	1.32	1.20	2.05
2-Year U.K.	1.27	1.34	2.00
2-Year Canadian	1.24	1.39	1.79
2-Year Japanese	0.25	0.26	0.54
10-Year German	3.29	3.38	3.40
10-Year U.K.	3.66	3.80	3.89
10-Year Canadian	3.38	3.48	3.36
10-Year Japanese	1.31	1.35	1.45

Commodity Prices

	Friday 11/20/2009	1 Week Ago	1 Year Ago
WTI Crude (\\$/Barrel)	76.40	76.35	49.62
Gold (\\$/Ounce)	1139.70	1118.70	745.06
Hot-Rolled Steel (\\$/S.Ton)	465.00	485.00	770.00
Copper (\\$/Pound)	308.35	296.85	156.85
Soybeans (\\$/Bushel)	10.12	9.60	8.65
Natural Gas (\\$/MMBTU)	4.31	4.39	6.32
Nickel (\\$/Metric Ton)	16,917	16,130	10,113
CRB Spot Inds.	462.33	450.45	345.61

Next Week's Economic Calendar

	Monday 23	Tuesday 24	Wednesday 25	Thursday 26	Friday 27
U.S. Data	Existing Home Sales September 5.57M October 5.60M (W)	GDP 3Q: Advance 3.5% 3Q:2nd 2.9% (W) Consumer Confidence October 47.7 November 47.6 (W)	Personal Income September 0.0% October 0.3% (W) Durable Goods Orders September 1.4% October 1.4% (W) New Home Sales September 402K October K 390K (W)	Thanksgiving Holiday U.S. Market closed	
Global Data	Canada Retail Sales (MoM) Previous (Aug) 0.8% Euro-zone PMI Manufacturing Previous (Oct) 50.7	Germany GDP (QoQ) Previous (3Q) 0.7% Germany IFO - Business Climate Previous (Oct) 91.9	UK GDP (QoQ) Previous (2Q) -0.4%	Germany CPI (YoY) Previous (Oct) 0.0%	Japan Jobless Rate Previous (Sep) 5.3%
Note: (W) = Wells Fargo Estimate (c) = Consensus Estimate					

Wells Fargo Securities, LLC Economics Group

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