HOW TO KNOW WHEN THE ECONOMY IS TURNING UP

The economy stinks. GDP fell 3.8% last quarter and experts believe the decline this quarter will be even worse. But recessions don't last forever, and we'll be coming out of this one long before official statistics say so. That's just the way it works. Most economic data — like the quarterly GDP reading — are lagging indicators. What you need are leading indicators that will signal when we've made a turn.

So far, there's been little evidence to suggest a bottom is at hand. But with this recession well into its second year it's not too early to start looking for signs of a recovery. The earliest clues will be anecdotal — you have to park farther from the mall entrance; your contractor takes longer to return your calls. Real evidence would follow. Here are 10 indicators to help you know when times are getting better.

ECONOMIC INDICATORS

1. Home Sales
2. Jobs
3. Jobs (again)
4. Car Sales
5. Retail Sales
6. Interest Rate Spreads
7. The Pasta Indicator
8. The Cardboard Indicator
9. Sweet-Talking Bill Collectors
10. Movie Madness

This is where our troubles began and this is where they should end. Any perking up in the housing market would be a signal that we're on the mend. Some pundits like CNBC's James Cramer and the highly regarded researchers at Moody's Economy.com are calling for a bottom the second half of this year. But there isn't a lot more to be optimistic about right now. "There's still a tremendous excess of unsold homes, both new and existing," says Jeoffrey Hall, chief US economist for Thomson Financial. He's watching the National Association of Home Builders House Market Index, which measures recent sales, expected sales, and prospective buyer traffic. The index is at an all-time low: 8 (on a scale of 100, where 50-60 is normal). Further, all three components of the index hit an all-time low in December. He'll start to feel better about a recovery if the index gets back to 20 this year — even if it's only prospective buyer traffic that pushes the index higher. "The faster it rises," says Hall, "the faster I'd say we're emerging from recession."

The employment scene is a disaster. We've shed 3.6 million jobs since the recession began. Private sector average weekly hours worked stuck at a record low 33.3 hours in January, and because companies typically cut hours before cutting heads the slide means more layoffs are coming. Look for this number to stabilize over a period of two or three months and then begin to inch upward for an early indicator that the economy is recovering. We won't hit a normal reading of around 35 hours for a long time. But the key is to just change the direction. You can find private sector average weekly hours worked on the Bureau of Labor Statistics web site.

A recovery in employment is crucial. So here's a second job-related indicator that economists are watching: monthly temporary employment. "Companies can always ask their employees to work a little longer," says Bernard Baumohl, chief global economist at Economic Outlook Group. "But when they start hiring you know something is going on, and temporary hiring typically picks up well before permanent hiring." In 2002, temporary hiring went from net job losses to net job gains almost to the month that the recession ended. At this moment, the monthly change in temporary employment has been negative for 25 months running. When it swings positive you can be sure that better times will follow. This can be tracked on the BLS web site as well.

Automakers had a rough go of it in 2008, when sales of new cars and trucks fell to 13.2 million units after several years of selling 16-million plus. October, November and December registered the worst

annualized rates in 28 years at just 10.5 million, 10.1 million and 10.3 million vehicles, respectively. Cars are one of the first big-ticket items that consumers buy when they start to feel good again. When new vehicle sales stabilize — at any level — and then start to tick higher it will provide a solid read on the mood of consumers, who collectively are two-thirds of the economy. "It's only fear that's holding consumers back," says James Smith, chief economist at Parsec Financial Management. "They have money — $56.5 trillion of net worth — and the products available are attractive and well priced." They just need to start feeling a little better about the economy and their financial future.

For the seventh consecutive month, retail sales fell in January. When that string reverses it will be a positive sign. But more important will be any shift away from discounters like Wal-Mart and Dollar General towards specialty or higher end stores like Nordstrom or Saks. "That would be a sign consumers are starting to feel better about the economy in general and their own prospects in particular," says Richard Moody, chief economist at financial firm Mission Residential in Austin, Texas. You can track retail sales at www.census.gov. But it might be just as useful to pay attention to monthly financial reports, comparing the trend at Wal-Mart with the trend at Nordstrom. Who's doing better or worse than expected? The last year or so has been a Wal-Mart story. Watch for a shift.

Modest signs have begun to emerge suggesting that the credit freeze is thawing. But borrowing rates remain way out of whack. Consider the difference between the 10-year Treasury bond, currently yielding around 3%, and a typical 10-year corporate bond now yielding around 7%. That spread of 4 percentage points has narrowed from 6 percentage points in recent weeks but still is double what's typical. Historically wide credit spreads between securities that tend to track closely suggests that borrowers — other than the U.S. government, anyway — are having great difficulty getting funds. When credit spreads across the spectrum narrow it will signal that money is flowing again, a critical development. But Richard DeKaser, chief economist at National City Corp., says not to get too excited until spreads narrow substantially. Even a 4-percentage point spread in the bond yields just mentioned is a level typical of recessions. He'll exhale when we get back to a 2-point difference. Also, and perhaps easiest to follow, look for jumbo mortgages which are now about 1.5 percentage points above conforming mortgages to close to within half a point.

Pasta is a cheap meal, and sales are shooting through the roof — rising 22% in 2008 after years of tepid growth, according to Nielsen Co. Much of the increase is due to commodities related price hikes. But the trend still means that pasta is claiming a larger portion of the average grocery basket. When pasta sales begin to slow you'll know times are getting better. One way to track the trend is by watching financial results at American Italian Pasta Co. (ticker: AIPC), which is North America's largest pasta producer. The stock has soared from $5 to $26 in the past 12 months while just about everything else got hammered. Revenue surged 43% to $569 million in 2008 — after declining or growing only modestly the previous three years. When this counter cyclical pasta packer hits a rough patch it could signal better times for the rest of us.

Alan Greenspan was fond of tracking liner board prices. The idea is simple: liner board is a main component of cardboard, which is used as packaging to ship just about everything. When liner board prices surge it means that packaging is in demand, which can only be the case if people are buying things, which in turn signals a healthy economy. Demand of a sort is already ticking higher: alleged financial criminals like Bernie Madoff using the stuff to cover their car window on the way to court. But cardboard is in a deadly bear market. Prices for the raw material used to make boxes are in freefall, having hit $25 a ton in January from $115 in September, according to Mark Arzoumanian, Editor-in-Chief at Official Board Markets. When the price turns up it will mean people are shopping again. Liner board isn't easy to track. As a proxy, keep your eye on the stock price of leading cardboard producers Smurfit-Stone Container Corp. (ticker: SSCC) and International Paper (IP). Their shares began falling before the recession started and could turn higher before the recovery begins.

It's hard to imagine a friendly bill collector, especially one that has gotten fat and comfortable by charging annual interest of 18% or more for years. But worried credit card companies have become downright hospitable to struggling debtors. The big card companies are waiving fees, restructuring debt and even accepting payoffs of as little as pennies on the dollar. They're not doing this to be good guys; they are bracing for a continued wave of defaults and want to collect as much as they can right now — before some other bill collector gets to you first and leaves you with empty pockets. You'll

know the economy is righting itself when credit card companies stop negotiating with debtors. To monitor this industry, check out creditcard.com.

Hollywood often produces movies that are a couple steps behind the times, meaning that with the recession now a year old we're almost certain to see a batch of back-to-basics storylines in 2009 — like the just released *New In Town* starring Renee Zellweger, which is the story of a business woman who moves to a rural area and discovers a simple life. But where Hollywood storylines tend to lag the economy, movie goers as a group tend to lead the economy. So it was that the number of tickets sold dropped 4% last year, when film buffs collectively concluded that with money so tight they might as well make better use of their high-def home theater system. Watch for that trend to reverse. If movie ticket sales increase on a sustained basis (they were up a bit in January), it could mean nothing more than that there have been some blockbuster films released — or just maybe that the economy is getting better. You can check for year-to-date movie ticket sales comparisons at ercboxoffice.com.