



Economic Evaluation Group, Inc.
131 Jericho Turnpike
Jericho, NY 11753
(516) 338-2800
Fax: (516) 338-7284
www.eegroup.com

Economic Evaluation Group, Inc. Presents **Monthly Economic Update for March, 2008**

Quote of the month. “The future is here. It’s just not widely distributed yet.” – William Gibson

The month in brief. The economy was most definitely under the weather in February, but how sick was it, and when would it get better? Federal Reserve Chairman Ben Bernanke talked merely of “a period of sluggish growth,”¹ but many economists preferred a nine-letter word to describe what he was talking about. Indicators particularly showed the service sector and housing sector suffering, and the pace of inflation slightly accelerating. Stock markets around the world suffered with the news.

Domestic economic health. February began with a recessionary omen: the economy lost 17,000 jobs in January, the first decrease in payrolls since 2003 and a development unpredicted by 80 polled economists.² On top of that, the Institute for Supply Management’s January service sector index registered 44.6, the first reading below 50 in nearly five years. When the index is under 50, it signals contraction rather than expansion; in January, the ISM found that 3 service sectors expanded while 14 contracted.³ At mid-month, a Bloomberg News survey of noted economists painted a gloomy picture. Their median estimates: 50% odds of recession this year, the benchmark interest rate at 2.5% by June, 0.5% 1Q GDP, 1.0% 2Q GDP and 1.7% total growth for 2008.⁴

With news like this creeping into the headlines, how did the consumer feel? The consumer was spending more and worrying more, according to data from the

Commerce Department, the Labor Department and the Reuters/University of Michigan index. While consumer spending rose 0.4% in January, consumer prices rose 0.4% as well and core inflation rose 0.3%.⁵ Food prices rose the most in 11 months.⁶ The University of Michigan’s final February consumer sentiment index fell down to 70.8, the lowest final reading since February 1992.⁷

There was some very positive news for the consumer. President George W. Bush signed the economic stimulus plan into law, ensuring that most U.S. taxpayers will receive tax rebates this year of up to \$600 (single filers) and \$1,200 (joint filers), plus \$300 per child for families.⁸

The pressure was on the Fed, which had to weigh if, when and how much to cut interest rates with indicators showing mounting inflation. The Fed revised its 2008 forecast in February, estimating joblessness at 5.2-5.3%, inflation of 2.1-2.4%, and 2008 GDP of 1.3%-2%.⁶

Global economic health. As noted last month, many analysts believe the fallout from America’s 2007-08 credit crisis will affect but by no means wreck Asia’s economies and stock markets. Many of these economies have very large foreign exchange reserves, and trade surpluses – so if the U.S. isn’t buying their products, they can tap European markets to sustain growth.⁹ Notably, data did show that India – which does not have a large trade surplus

– actually experienced slower growth in the fourth quarter of 8.4%.¹⁰

Eurozone inflation was flat for February ... but it was still at 3.2%, the highest since euro cash was introduced in 2002. The European Central Bank has left interest rates alone since June, but may have to make a move in March. The ECB wants Eurozone inflation at 2% or less for 2008, given projected growth of 1.8%. But the European Commission thinks inflation will average 2.6% in the Eurozone for the year.¹¹

World financial markets. It was another shaky month overseas. In the Asian markets, Vietnam's VN index got the worst of it – at the end of February, it had fallen 21% for the month and 28.5% on the year.¹² China's CSI Index is now officially in a bear market, having lost 20% of its value since October.¹³ Early February was disconcerting – when the Institute for Supply Management's January service sector index data was released, Hong Kong's Hang Seng fell 5.4% and Japan's Nikkei 225 index fell 4.7% on the day.¹⁴ At the start of March, the Nikkei 225 was down almost 15% for the year.¹⁵ But the MSCI Asia Pacific Index gained 2.8% in February, with help from speculation that U.S. bond insurers would be rescued from credit losses.¹⁶

Mirroring the U.S. markets, European stocks fell for the fourth straight month. England's Dow Jones Stoxx 600 Index was down 13% for the year through the end of February.¹⁷ At the close of the month, the DAX, FTSE 100, CAC 40, Stoxx 50 and Euro Stoxx 50 all fell 1.4-1.7% on recession fears linked to credit losses.¹⁸

Commodities markets. Oil and gold prices set new records. Gold was up to \$948.59 per ounce on the London Bullion Market on February 21,¹⁹ and hit a new record intraday high of \$967.10 per ounce eight days later.²⁰ Silver prices climbed toward the \$20/ounce level by month's end, hitting an intraday high of \$19.93/ounce in Asia trading – a price level not seen since 1981.²¹

While thousand-dollar gold certainly seemed on the horizon, \$100/barrel oil was already evident. Crude oil prices reached \$101.32 per barrel on February 21,¹⁹ and then the \$103 per barrel level on February 29.²² The price of diesel fuel also hit a record in America – \$3.541 per gallon on February 22.²³

Housing & interest rates. The glass was much less than half full. New U.S. Census Bureau data showed that January was a miserable month for new home sales – the worst in almost 13 years. Sales dropped 2.8% from December and 33.9% from January 2007.²⁴ As for residential resales, the picture showed no improvement – in fact, it showed more decline. Existing home sales fell for the sixth month in a row, and the January median resale price was 4.6% below the median a year ago, according to the National Association of Realtors.²⁵ Mortgage rates rose for most of February; at the end of the month, rates on 30-year FRMs were at their highest level since mid-November, at 6.24%.²⁶

Major indexes. The January 30 rate cut did not propel the stock market north for long. In fact, February was the fourth consecutive negative month for stocks. The DJIA ended the month with a 315-point drop. Not since 2002 have the S&P 500 and DJIA endured four losing months in a row.²⁷

% Change	1-Month	Y-T-D
DJIA	-3.13	-7.53
NASDAQ	-5.21	-14.36
S&P 500	-3.60	-9.38

Source: CNNMoney.com, USAToday.com, 2/29/08

March outlook. President Bush maintains we are not in a recession. The Fed has not concluded that we are in a recession. But economists everywhere see a recession, and the indicators of January and February have affirmed some of their suspicions. At the start of the year, many economists felt the first quarter of 2008 would be the hardest for America's economy, and for stocks. In their eyes, recovery from this downturn/recession is not likely to happen until the third quarter. March may bring us another raft of negative indicators, leaving investors looking forward to earnings season. The outlook can be summed up in two simple words: hang on. Many economists see another interest rate cut coming for March, even with recent indicators showing rising inflation; the Fed will have to perform a real high-wire act for the first half of the year.

To conclude, here is the March economic calendar: revised 4Q productivity and January factory orders (3/5), January pending home sales (3/6), February

wages and unemployment (3/7), January wholesale inventories (3/10), February retail sales and business inventories (3/13), February consumer sentiment and CPI (3/14), February industrial production (3/17), February PPI, housing starts and the FOMC policy statement (3/18), February existing home sales data

(3/24), March consumer confidence (3/25), February durable goods orders and new home sales data (3/26), final 4Q 2007 GDP (3/27), and February personal spending, personal income and core PCE inflation (3/28).

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Citations.

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