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Economic Evaluation Group, Inc. Presents **Monthly Economic Update for May, 2007**

Quote of the month. “Never stand begging for that which you have the power to earn.” – Miguel de Cervantes

The month in brief. The Dow surged past 13,000, largely on the strength of earnings reports and foreign economies with rising industrial and manufacturing needs. The S&P 500 approached its 1999 record high, the NASDAQ hit its highest close since 2001, and the Russell 3000 hit an all-time high. The housing market still hurt: while March data released at the end of April showed new home sales rose 2.6%, part of that jump could be attributed to the Commerce Department’s downward revision of previous sales figures. The National Association of Realtors announced the biggest monthly dip in residential resales since 1989 (8.4% in March). Per-barrel crude oil prices climbed from \$64 to nearly \$66 during April.

Domestic economic health. The month ended with a question: could consumer spending continue to hold up a crawling economy? America’s GDP grew only 1.3% in the first quarter of 2007, while the core PCE price index rose 2.2%. Minutes from the Federal Reserve’s March meeting appeared, in which Fed officials cited the possibility of tighter credit due to “uncomfortably high” inflation readings. New Commerce Department data indicated that America’s trade deficit was finally starting to narrow. Meanwhile, the Reuters/University of Michigan

Surveys of Consumers index fell to an 8-month low, with the entire loss of consumer confidence among upper-income households. The Commerce Department reported at the close of the month that consumer spending rose just 0.3% during March, less than the 0.5% analysts had predicted.

Global economic health. At the end of April, the Euro hit an all-time high versus the dollar (\$1.3682). Days earlier, the British pound topped \$2 for the first time since 1992. With the strength of the pound, U.K. manufacturing grew at the slowest place in three months. In Germany, unemployment fell to the lowest level in six years and the government revised its 2007 growth forecast to 2.3% from 1.7%. Manufacturing activity in China grew at the fastest pace in more than two years in April, according to a survey of that nation’s purchasing managers. India’s central bank has let the rupee appreciate 7.2% since March with the goals of controlling inflation and making imports more affordable.

World financial markets. In mid-April, economists at the International Monetary Fund forecast increased risk in global financial markets, citing the troubles in the American housing sector, a surge in private equity buyouts, and a disturbing level of comfort in a situation of superb corporate profits and low market volatility. Yet, world markets did well. London’s FTSE 100 shares index hit its highest level in almost six-and-a-half years in mid-April, and the Australian S&P/ASX 200 also hit a new record high. The Nikkei 225 Stock Average gained half a percentage point in April, but that was lost at the start

of May with news that after consumer spending had slowed in the U.S., easing demand for exports. On April 20, the blue-chip Hang Seng Index, the Toronto S&P/TSX and other global indexes fell 2-3% after the State Council of China announced the possibility of measures to curb that nation's 3.3% first-quarter spike in inflation. Still, it was a strong month.

Commodities markets. Crude oil prices spiked three times on three geopolitical concerns. Oil prices jumped \$1.55 on April 20 to \$63.38 per barrel over fears about the Nigerian presidential election, then topped \$66 per barrel on April 27 after Saudi Arabia arrested 172 Islamic militants, some of whom allegedly planned to attack oil fields. On April 30, after a brief decline, crude prices hit \$65.89 with news that Nigerian militants had kidnapped six Chevron Corp. oil workers. Gasoline inventories in the U.S. had declined for 11 straight weeks by month's end, with the Energy Department estimating inventories at 87.8% of capacity.

Gold and silver prices continued their advance into April, with gold prices approaching \$700 an ounce and gaining \$38 since the start of March against the weakening dollar. But gold and silver stocks dropped quickly in the last week of April from a high of \$698 per ounce on April 20, as the dollar's decline failed to kick-start a precious metals rally.

Housing & interest rates. The real estate market did not appear headed for any kind of rebound. On May 1, the latest data from the National Association of Realtors brought no good news: Pending sales of existing U.S. homes in March fell 4.9% to the lowest level since March 2003. In the prime mortgage market, rates were almost unchanged

from late March: at the end of April, 30-year FRMs were averaging 6.16%, 15-year FRMs 5.87%, and 5-year ARMs 5.88%.

May outlook. The bull market of this earnings season cannot cancel a crawling GDP and continued woes in the housing sector. Yet there is palpable feeling that the stock market has plenty of upside, having gained more than 8% in the last six months in the face of troubling indicators. Most economists do not feel that consumer spending or business investment will pick up in the near future, although orders for durable goods did rise in March Commerce Department data. Inflation also rose 0.4% in March, in line with the Federal Reserve's targets. The Fed's next meeting on interest rates occurs May 9.

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