



RECENT ECONOMIC DEVELOPMENTS

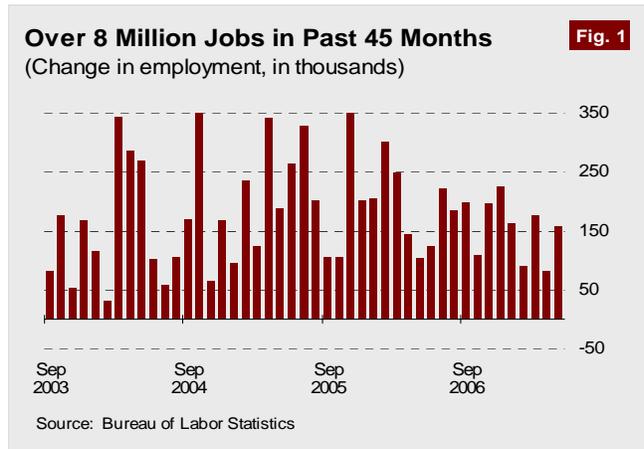
JUNE 12, 2007

INCOMING DATA SUGGEST ECONOMIC RESILIENCE

The economy cooled in the 1st quarter, with annualized growth in the inflation-adjusted (real) gross domestic product (GDP) dipping to 0.6%, the weakest in more than four years. However, recent data on consumer and business investment spending, construction activity, and net exports all suggest improvements in final demand for goods and services. Measures of activity in the manufacturing and services sectors over the past two months also indicate a rebound of production relative to averages in the 1st quarter. Private forecasters expect growth to remain moderate in the near term as adjustments in the housing market continue, but also expect growth to accelerate to a more trend-like rate of close to 3.0% by year's end. Real GDP has grown at a healthy average rate of 2.9% over the past 22 consecutive quarters of expansion. Employment has also continued to expand; over 8 million new payroll jobs have been created in the past 45 months of consecutive job gains.

Highlights

- Job gains continue; 157,000 new payroll jobs were created in May. Payrolls are up by over 8 million new jobs in the past 45 consecutive months with job gains (Fig. 1).
- The unemployment rate remained at 4.5% in May and has ranged between 4.4% and 4.6% since last September (Fig. 2, next page).
- Real GDP growth was revised down to an annualized 0.6 % in the 1st quarter from an earlier estimate of 1.3% (Fig. 3, next page).
- The housing market continues to cool: existing home sales fell by 10.7% in April on a year-over-year basis; new home sales fell by 10.6% (Fig. 4, next page).



Over 8 Million New Jobs in 45 Months; Unemployment Rate at 4.5%

Payroll employment increased by 157,000 new jobs in May – the 45th consecutive month with job gains (Fig. 1). More than 8 million new jobs have been added to payrolls over that period. Over the year ending in May, more than 1.9 million new jobs have been added to payrolls. During the past year, payroll job gains have averaged a healthy 160,000 per month. The *unemployment rate* held at 4.5% in May and has ranged between 4.4% and 4.6% since last September, well below the near-term peak of 6.3% in June 2003 (Fig. 2, next page).

GDP Growth Revised Down to 0.6% in the 1st Quarter

GDP growth was revised down to a 0.6% annualized rate for the 1st quarter from an earlier estimate of 1.3%. Consumer spending remained resilient, growing at a 4.4% annualized rate. Business investment rebounded, increasing 2.9%, in contrast to a decrease of 3.1% in the 4th quarter of last year. That decline was the first downturn in business investment in three-and-a-half years. Residential investment decreased 15.4% in the 1st quarter and has fallen for six consecutive quarters, reflecting the slowdown in housing markets. Despite recent below-trend growth, real GDP has grown for 22 consecutive quarters, averaging a healthy 2.9% annualized rate over that period. The *Blue Chip* consensus of private forecasters sees a gradual acceleration in growth, rising to 2.9% by the end of 2007 (Fig. 3, next page).

Incoming Data Suggest Resilience

Incoming data on *consumer and business investment spending, construction activity and net exports* all point to improved growth in final demand for goods and services. In addition, the *Institute for Supply Management (ISM) survey* of manufacturing activity has risen from a recent low of 49.3 in January, indicating a very mild contraction in manufacturing, to 55.0 in May, indicating expansion (a value of the index above 50 indicates expansion; below 50 indicates contraction). The ISM survey of activity in the services sector, which accounts for the bulk of the Nation's output, has risen from a recent low of 52.4 in March, indicating mild expansion, to 59.7 in May, indicating a vibrant pace of expansion. While lingering effects of the housing downturn and higher gasoline prices will likely keep GDP growth below 3% in the second half of 2007, the *Blue Chip* consensus of forecasters sees growth rising to a more trend-like 3.0% or slightly higher next year.

The Housing Sector Continues to Cool

Existing home sales fell 10.7% in April relative to a year earlier and have not risen for 17 straight months. *New home sales* fell 10.6% on a year-over-year basis and have fallen for 17 straight months. *House-price appreciation* has slowed and *housing starts and permits* have each declined for 13 straight months through April on a year-over-year basis. Home sales have fallen from the rapid pace of the summer of 2005, but levels of sales remain healthy, supported by still-low mortgage rates.

The Fed Remains on Hold

The *Fed* kept its *target overnight interest rate* at 5¼% at its May policymaking meeting, a target that has been in place since June 29 of last year. Between June 2004 and late June 2006, the Fed had raised its target from 1% to 5¼% with 17 consecutive quarter-point increases. Despite those actions, long-term interest rates remain low. In its May policy statement, the Fed notes the economic slowdown in the early part of this year, and believes that "...the economy seems likely to expand at a moderate pace over coming quarters." The Fed also indicates that its "...predominant policy concern remains the risk that inflation will fail to moderate as expected."

Gasoline Prices Remain Elevated

The U.S. *average retail price for regular gasoline* fell to \$3.08 per gallon as of June 11, the 3rd straight weekly decline. Prices are below the near-term high of \$3.22 reported by the Energy Information Administration on May 2, but are 17 cents per gallon higher than this time last year.

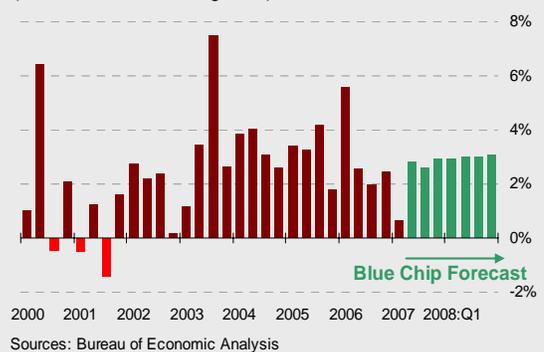
Unemployment Rate at 4.5%

(Civilian unemployment rate, SA)



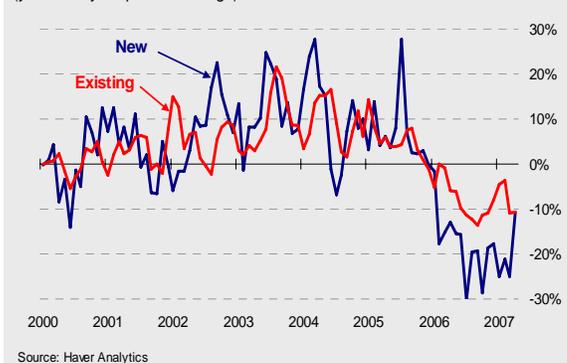
Economic Growth Since 2000

(Real annualized GDP growth)



Existing and New Home Sales Have Fallen

(year-over-year percent change)



Upcoming Indicators

Inflation – The Consumer Price Index for May is scheduled for released on *June 15*.

Federal Reserve – The Fed's next policy meeting is scheduled for *June 27 and 28*.

GDP – The "final" estimate of GDP for the 1st quarter is scheduled for release on *June 28*.

Employment – The Bureau of Labor Statistics reports June's employment situation on *July 6*.