



...weekly since 1976

Your guide to understanding
today's economy and
financial markets

October 31, 2007

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Minus 25

Written by Jeff Thredgold, CSP, President, Thredgold Economic Associates

The Federal Reserve's Open Market Committee (FOMC) delivered what financial markets widely expected today with a 0.25% (25 basis point) reduction in its important federal funds rate to 4.50%. A basis point is 0.01%.

The federal funds rate was chopped by a more aggressive 50 basis points on September 18. Despite comments in the Fed's accompanying statement today, we would suggest greater than 50/50 odds of another 0.25% rate cut on December 11.

The Fed has been concerned about financial markets expecting too much in the way of additional monetary ease following the aggressive September cut. The Fed's accompanying statement noted its continuing concern about inflation pressures by stating, *"Readings on core inflation have improved modestly this year, but recent increases in energy and commodity prices, among other factors, may put renewed upward pressure on inflation."*

Balance

The statement noted that, *"the upside risks to inflation roughly **balance** the downside risks to growth"* (emphasis added). Few on Wall Street or Main Street America agree with that statement. It does, however, serve the Fed in two ways.

The Fed's inflation concern reinforces the idea that the Fed's primary job IS inflation containment, with the statement perhaps pacifying those who think recent actions by the Fed will soon let the

"inflation toothpaste out of the tube."

The statement also provides the Fed with greater flexibility to provide additional assistance in coming months IF financial market anxiety rises again.

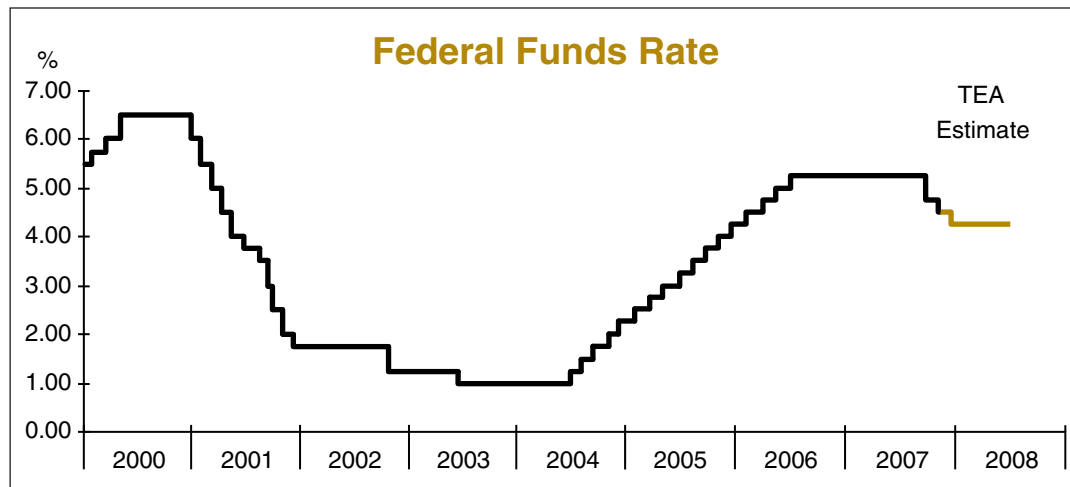
At the same time, the balancing of inflation risk versus economic slowing also provides the Fed with the ability to stay on the monetary sidelines for some time to come. This is clearly the Fed's first choice in coming months.

Even as the Fed moved to the balance position, it left the door open for more rate cuts in coming months by noting, *"The Committee will continue to assess the effects of financial and other developments on economic prospects and **will act as needed** to foster price stability and sustainable economic growth"* (emphasis added).

Offsets

The Fed well recognizes, as do most financial types, that the weakness in housing has yet to reach bottom. The Fed also sees that the current strength in American manufacturing exports, tied to strong global demand and a weaker dollar, is largely offsetting the weakness in housing, especially when looking at the overall U.S. economy from a "macro" viewpoint.

The surprising 3.9% real (inflation adjusted) annual growth rate in 2007's third quarter reported today supports this notion...and reaffirms our view that when all is said and done...the American economy will avoid recession.





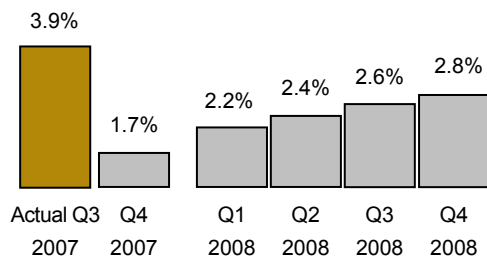
USA TODAY • MONDAY, OCTOBER 29, 2007

Quarterly economic survey

The USA TODAY economic survey of 53 top economists was conducted October 18-24. Median estimates through Q4 2008:

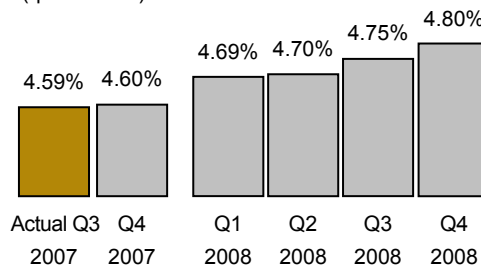
Gross domestic product

(real annual growth rate)



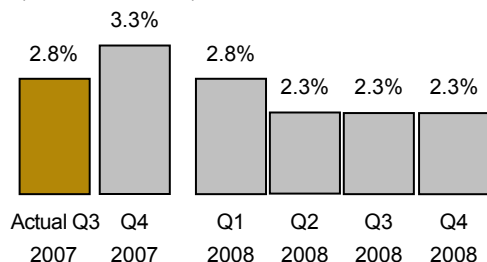
10-year T-note yield

(quarter end)



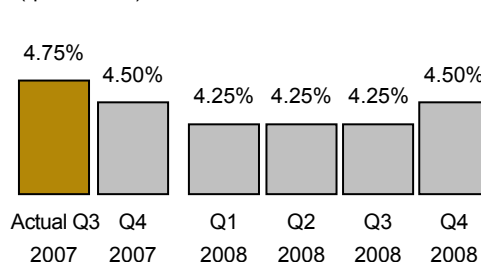
Consumer price index

(12 months ended)



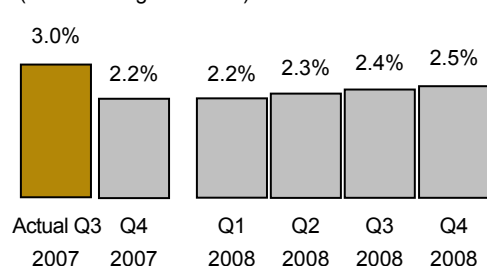
Federal funds rate target

(quarter end)



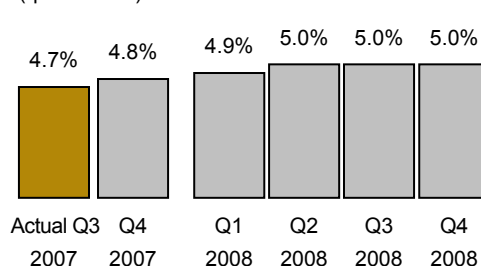
Consumer spending

(real annual growth rate)



Unemployment rate

(quarter end)



Survey participants: Scott Anderson, Wells Fargo; Nariman Behraves, Global Insight; Richard Berner, Morgan Stanley; David Berson, Fannie Mae; J. Dewey Daane, Vanderbilt University; Richard DeKaser, National City; Rajeev Dhawan, Georgia State University; Doug Duncan, Mortgage Bankers Association; Michael Englund, Action Economics; Gail Fosler, The Conference Board; Lyle Gramley, Stanford Washington Research Group; Ethan Harris, Lehman Brothers; Maury Harris, UBS; Tucker Hart Adams, The Adams Group; Stuart Hoffman, PNC Financial Services Group; David Huether, National Association of Manufacturers; William Hummer, Wayne Hummer Investments; Saul Hymans, University of Michigan; Paul Kasriel, Northern Trust; Irwin Kellner, North Fork Bank; David Kelly, Putnam Investments; Timothy Martin, Bank of America; Ken Mayland, ClearView Economics; Dan Meckstroth, Manufacturers Alliance/MAP; Jim Meil, Eaton; Robert Mellman, JPMorgan/Chase; Richard Moody, Mission Residential; Joel Naroff, Naroff Economic Advisors; Frank Nothaft, Freddie Mac; Donald Ratajczak, Morgan Keegan; Martin Regalia, US Chamber of Commerce; David Resler, Nomura Securities International; Timothy Rogers, Briefing.com; David Rosenberg, Merrill Lynch; Chris Rupkey, Bank of Tokyo-Mitsubishi UFJ; John Ryding, Bear Stearns; David Seiders, National Association of Home Builders; Joshua Shapiro, Maria Fiorini Ramirez; Robert Shrouds, DuPont; John Silvia, Wachovia; Allen Sinai, Decision Economics; James Smith, Parsec Financial and Western Carolina University; Sean Snaith, University of Central Florida; Sung Won Sohn, Hanmi Bank; Neal Soss, Credit Suisse; Donald Straszheim, Roth Capital Partners; Diane Swonk, Mesirow Financial; **Jeff Thredgold, Thredgold Economic Associates**; Chris Varvares, Macroeconomic Advisers; Brian Wesbury, First Trust Advisors; Richard Yamarone, Argus Research; Lawrence Yun, National Association of REALTORS; Mark Zandi, Moody's Economy.com

“TEA”sers

Scary thoughts to help you celebrate Halloween!

- Shotgun wedding: a case of wife or death
- If you don't pay your exorcist, you get repossessed
- Local Area Network in Australia: the LAN down under

—Scott Friedman, CSP



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