

# Valance Company, Inc.



Weekly

May 24, 2006

III

## Highlights

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**US** – Housing Market cooling (page 2)

**Euroland** – German consumer spending expands more than expected in Q1 (page 7)

**Japan** – Q1 GDP increased on solid private demand (page 15)

**UK** – Retail Sales were solid while CBI Factory Orders held steady (page 22)

**CA** – BoC hiked interest rates by 25bps (page 28)

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Valance Economic Reports

Valance Co., Inc.

# Valance Economic Report: United States

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May 24, 2006

This week's data addressed two key points of the Fed's macroeconomic forecast- housing slowdown and business investment spending; unfortunately they did not clarify the Fed's path much. New home sales were up in April, but confirmed a weaker tone to the housing market as the Fed expects. Core capex in the durable goods data was weak for the month, but the Y/Y trends in this volatile series remain solid. Bernanke, Fisher, Hoenig, Poole and Lacker all made comments on the economy this past week. They all emphasized the importance of the macro data over the next month, but some Fed officials highlighted the cooling of the housing market and others, the elevated core CPI reading.

## Weekly Highlights

**New Home Sales-** down 5.9% Y/Y with prices up 0.9% Y/Y. (page 2)

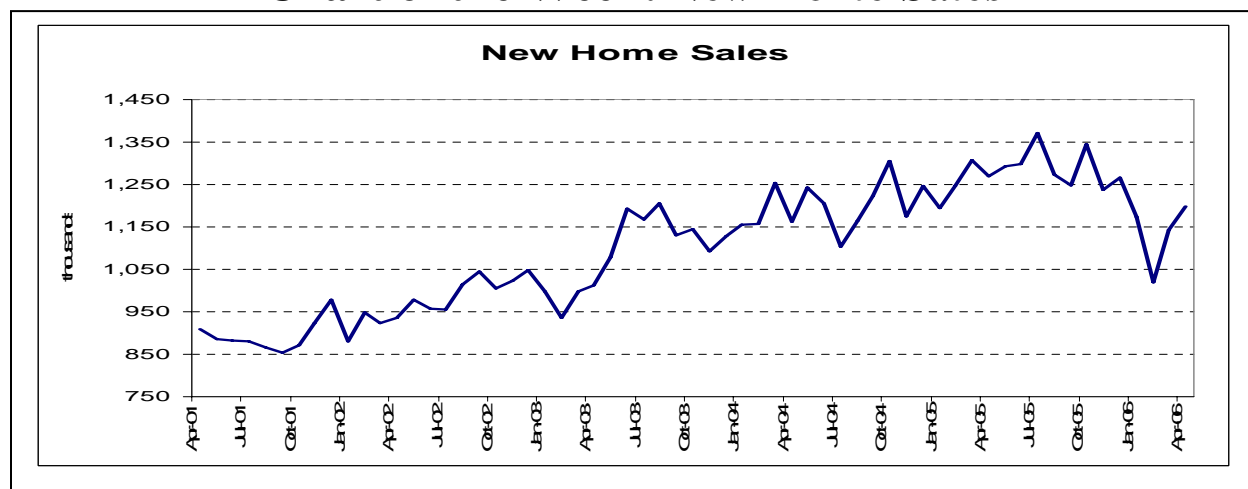
**Durable Goods Orders-** declined 4.8% M/M and increased 11.3% Y/Y (page 4)

**Mortgage Purchase Applications-** down 14.7% Y/Y on a four-week moving average basis. (page 4)

**ABC Consumer Confidence-** continues to trend lower. (page 5)

## Weekly Releases

### Chart of the Week: *New Home Sales*



New Home Sales grew from 1,142k seasonally adjusted annualized units to 1,198k, up 4.9% M/M and down 5.6% Y/Y in April. Median prices gained 2.8% M/M and 0.9% Y/Y. Inventory levels decreased from 6.0 months to 5.8 months. Overall, the new home sales data shows the housing market is cooling off, but not unraveling.

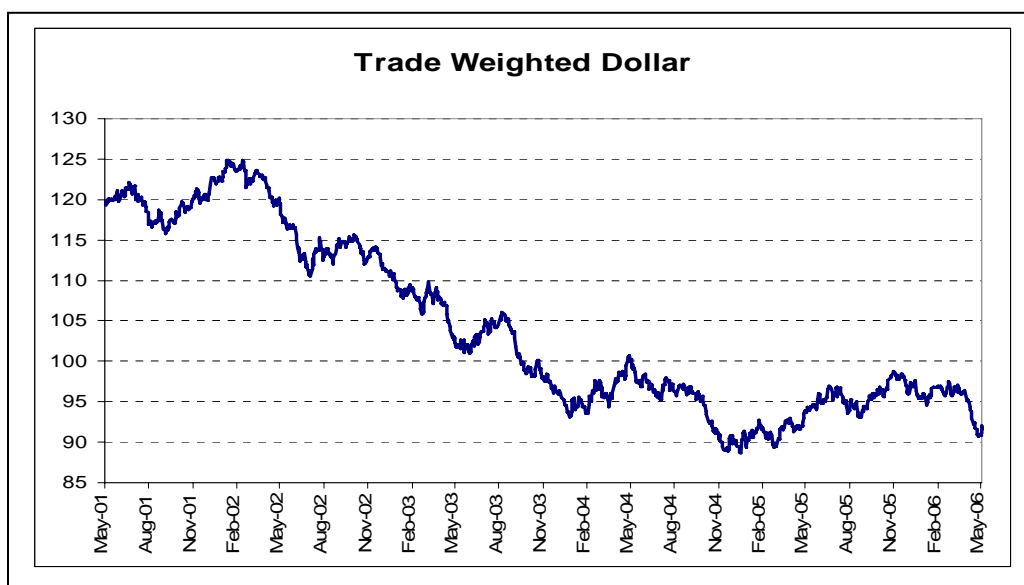
## ***U.S. Financial Balances & Trade Weighted Dollar***

### ***Financial Balances***

<i>U.S.</i>	<i>Latest period (\$blns)</i>	<i>Last 12mth. as a % of GDP</i>
Budget Balance	118.9(April)	-2.0%
Trade Balance	-62.0 (March)	-5.7%
Current Account Balance	-224.4 (Q4)	-6.3%
Private Balance	--	-4.3%

The budget deficit is currently at \$266 bln on a trailing twelve month basis and forecasts see the budget deficit increasing to \$375 bln with Katrina related spending in 2006. The larger budget deficit will stimulate the economy in the short-run, but the trade deficit as of March is still 5.7% of GDP, with no clear signs of narrowing quickly. The budget deficit will remain too small to support a robust and sustained expansion, given the size of the current account deficit. As mortgage equity extraction slows and debt service levels increase, fragility in the economy should become more evident.

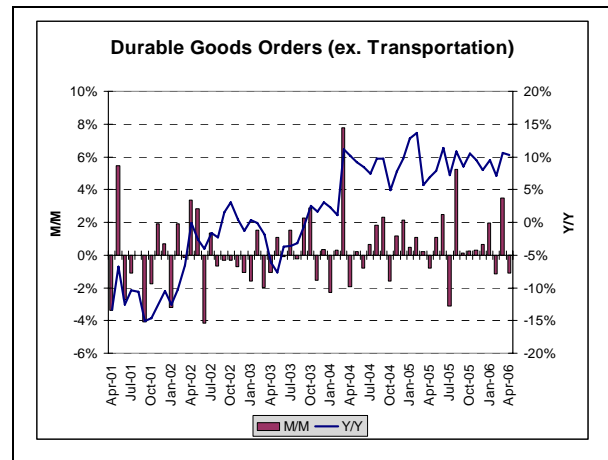
### ***Trade Weighted Dollar***



## Durable Goods, Mort. Apps. & Employment Claims

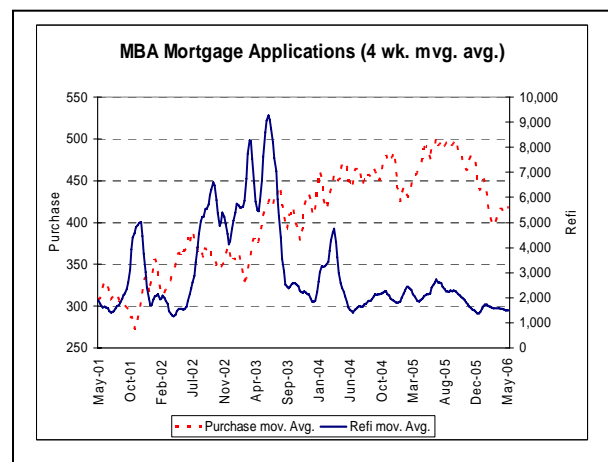
### Durable Goods ex. Trans.

Durable Goods in April, excluding Transportation, fell 1.1% M/M and increased 10.3% Y/Y. Headline Durable Goods Orders dropped 4.8% M/M and increased 11.3% Y/Y. Non-defense capital goods orders, excluding aircraft, declined 1.7% M/M and is up 6.8% Y/Y. The M/M weakness should be taken lightly because this series is notoriously volatile and longer-term trends remain healthy.



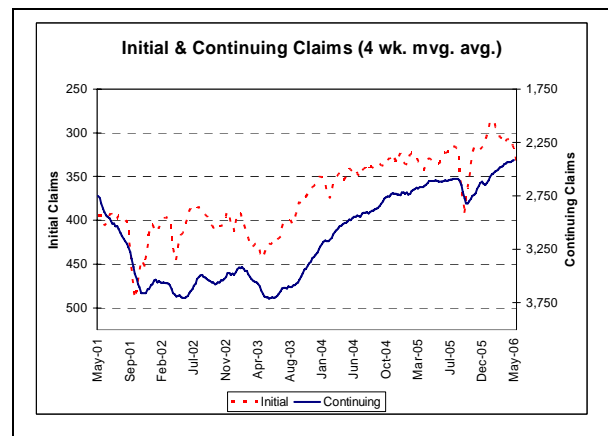
### MBA Mortgage Applications

Purchase mortgage applications decreased 7.1% W/W and refi applications were down 4.3% W/W this week. The four-week moving average of purchase applications is down 14.7% Y/Y and was down 17.8% Y/Y just based on last week's reading. This series continues to confirm a soft housing market.



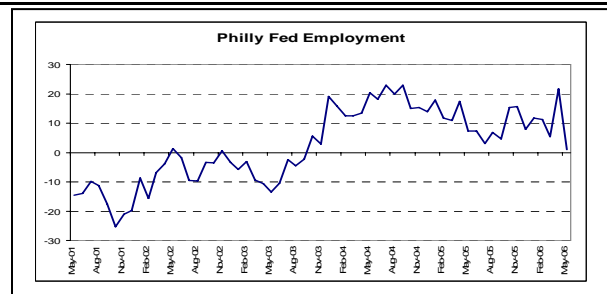
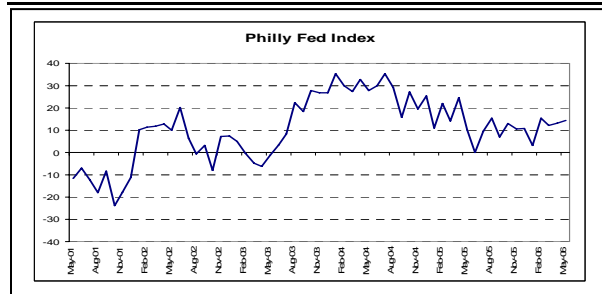
### Initial & Continuing Claims

The four week moving average of initial claims increased by 14k to 332k while continuing claims decreased by 10k to 2,413. Initial claims were distorted by 46k due to the partial government shut-down in Puerto Rico. Initial claims, adjusted for one-time items, and continuing claims continue to suggest solid payroll gains in May.



## Philly Fed, Consumer Confidence & Leading Indicators

### Philly Fed Index

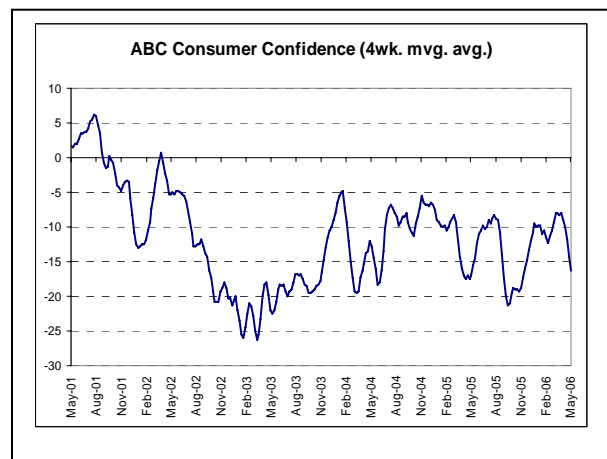


The Philly Fed Index increased slightly from 13.2 to 14.4 in May. The employment and new orders components had significant declines, dropping from 21.7 and 12.2 to 1.1 and 2.7, respectively. The Philly prices paid increased from 29.0 to 55.3 and the prices received declined from 15.4 to 10.3.

### ABC Consumer Confidence

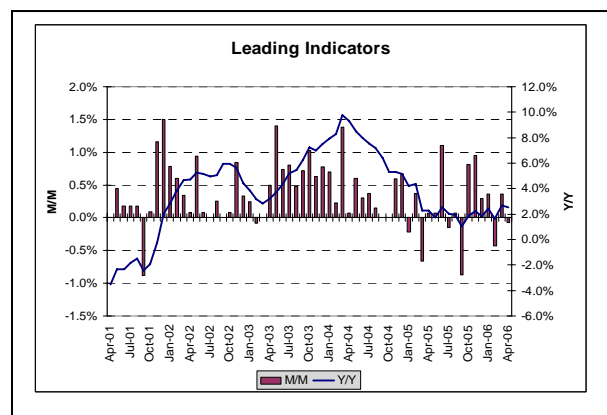
The ABC Consumer Confidence Index decreased from -17 to -19.

The economy component remained flat at -34, but the finance and buying components dropped from 16 and -34 to 12 and -36, respectively. Consumer confidence continues to deteriorate and is now almost at the levels reached post-Katrina.



### Leading Indicators

Leading Indicators decreased 0.1% M/M and increased 2.5% Y/Y in April. The individual components were mixed again, netting out to little change in the overall index.



## ***Fed Comments & Key Dates***

**Bernanke-** “Lapse of judgement” (on the Bartiromo/ CNBC episode)  
 “Fed will watch data very closely”  
 “Orderly and moderate cooling of housing expected”

**Fisher-** “Housing market clearly cooling”  
 “Fed has a lot to learn between now and end of June”  
 “Must stay wary of inflation”

**Hoenig-** “Recent inflation figures higher than expected”  
 “Must guard against overshooting”

**Poole-** “A lot of data between now and June meeting”  
 “Inflation tilted to upside”  
 “Softer economy may not end infaltion risk”  
 “Fed decision will evolve with new data”

**Lacker-** “Inflation data makes pause less likely”

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/25	Initial Jobless Claims (MAY 20)	315K	367K
05/25	Continuing Claims (MAY 13)	2405K	2389K
05/25	Help Wanted Index (APR)	38	38
05/25	Existing Home Sales (APR)	6.75M	6.92M
05/26	Personal Income (APR)	0.7%	0.5%
05/26	Personal Spending (APR)	0.6%	0.6%
05/26	PCE Core (APR) (M/M)	0.2%	0.3%
05/26	U. of Michigan Confidence (MAY)	79.0	79.0
05/30	Consumer Confidence (MAY)	101.0	109.6
05/30	ABC Consumer Confidence (MAY 29)	--	-19
05/31	MBA Mortgage Applications (MAY 26)	--	-6.0%
05/31	Chicago Purchasing Manager (MAY)	56.0	57.2
05/31	Minutes of May 10 <sup>th</sup> FOMC Meeting	--	--

Valance Co., Inc.

# Valance Economic Report: Euro Zone

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May 24, 2006

**Euro Zone domestic economic data showed a few positive signs this week as both German and French Consumer Spending picked up and Italian Confidence increased as new Prime Minister Prodi laid out plans to boost growth. French Spending contracted the month prior however, so sustained improvement has not yet been seen. It is encouraging nonetheless.**

## Weekly Highlights

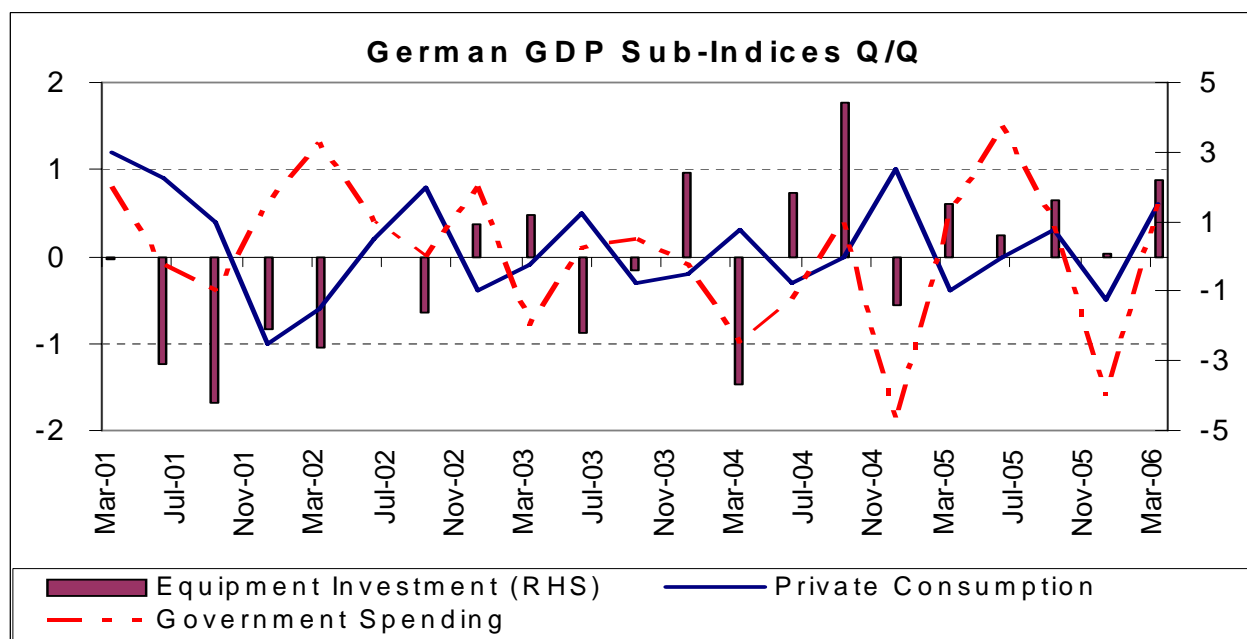
**German Private Consumption**— expanded more than expected in Q1. (page 7)

**French Consumer Spending**— rebounded markedly in April. (page 9)

**German IFO**— business climate and expectations contracted less-than-expected in May. (page 12)

## Weekly Releases & News

### Chart of the Week: *German GDP Components*



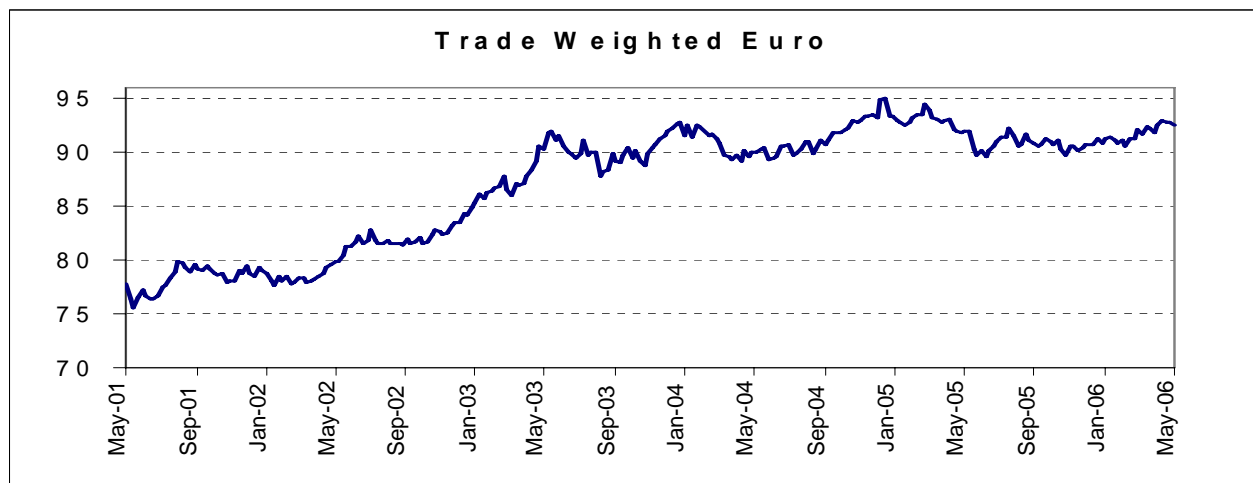
Germany's Q1 expansion was confirmed at 0.4% Q/Q and 1.4% Y/Y. Private Consumption expanded a stronger than expected 0.6% Q/Q, Government Spending expanded 0.6% Q/Q, Domestic Demand expanded 0.1% Q/Q, Exports expanded 4.6% Q/Q, and Imports expanded 4.5% Q/Q.

## ***Euro Zone Financial Balances & Trade Weighted Euro***

### ***Financial Balances***

<i>Germany</i>	<i>Last period (\$blns euros)</i>	<i>Last 12mth. as a % of GDP</i>
Budget Balance	-80.3 (12/04)	-3.6%
Trade Balance	12.1 (May)	7.1%
Current Account Balance	5.2 (May)	3.6%
Private Savings Balance	--	7.2%
<i>France</i>		
Budget Balance	-5.15 (May)	-3.4%
Trade Balance	-1.25 (May)	-1.3%
Current Account Balance	-2.87 (May)	-1.0%
Private Savings Balance	--	2.4%
<i>Italy</i>		
Budget Balance	-3.4 (July)	-3.5%
Trade Balance	-0.36 (May)	0.4%
Current Account Balance	-3.2 (May)	1.2%
Private Savings Balance	--	4.7%

### ***Trade Weighted Euro***

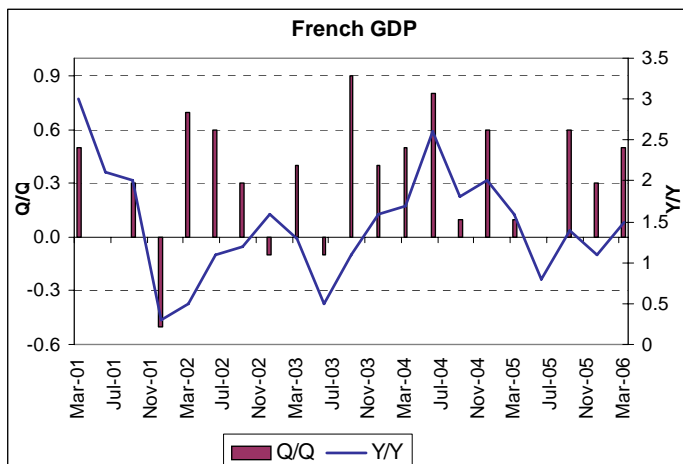




## French GDP, Consumer Spending & Business Confidence

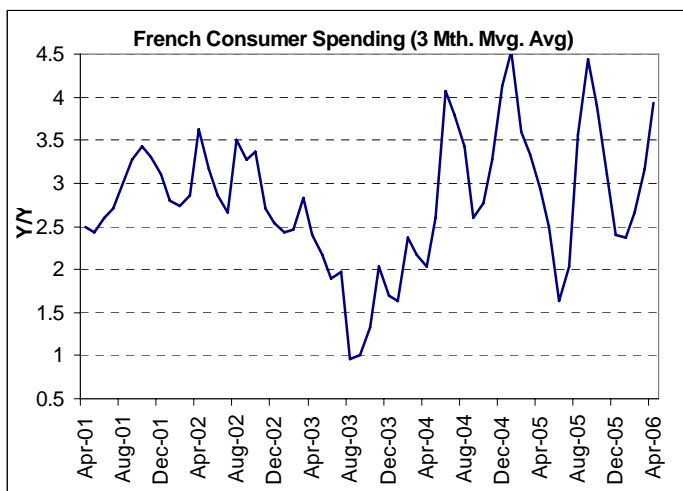
### French GDP

The French economy expanded 0.5% Q/Q and 1.5% Y/Y in Q1, slightly slower than expected. Q4 2005 GDP was revised downward from 0.4% Q/Q to 0.3% Q/Q. According to the Insee Institute, consumer spending expanded 0.9% Q/Q, while exports expanded 3% Q/Q.



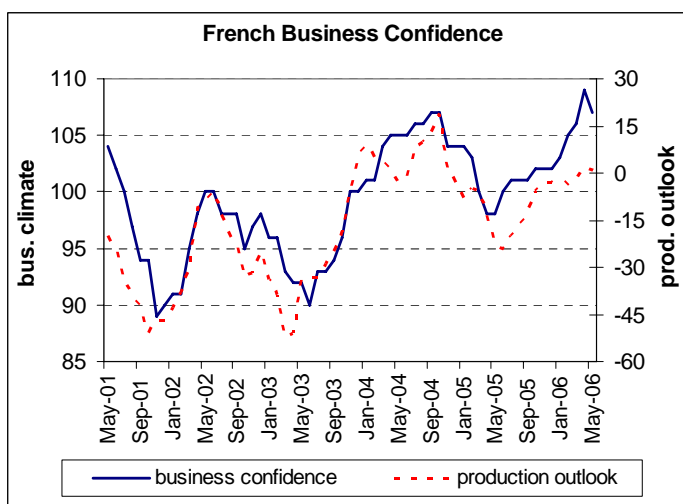
### French Consumer Spending

French Consumer Spending expanded a stronger than expected 0.7% M/M and 4.3% Y/Y in April, after contracting in March.



### French Business Confidence

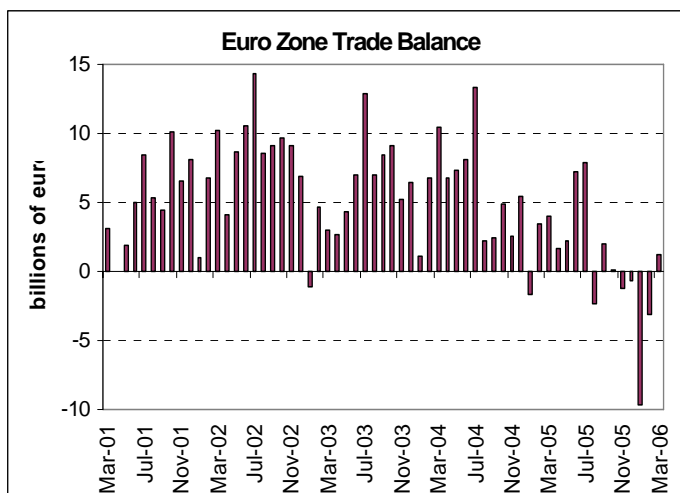
French Business Confidence contracted in May, declining from 109 in April to 107, as expected. The Production Outlook Indicator contracted from 2 to 1.



## Euro Zone & Italian Trade Balances

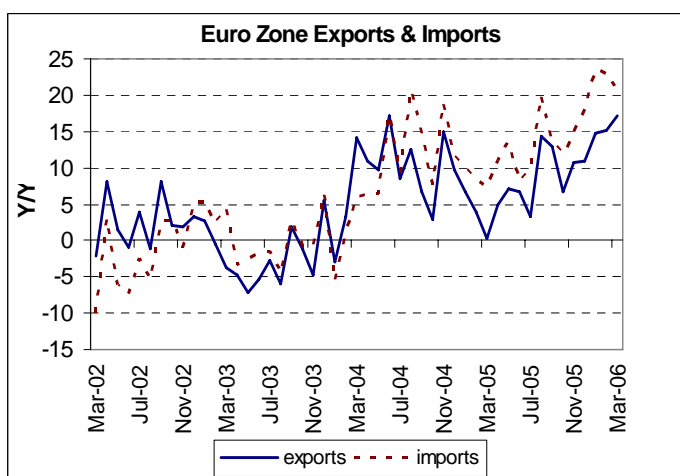
### Euro Zone Trade Balance

*The Euro Zone Trade Balance increased from a deficit of 3.1 bln euros to a surplus of 1.2 bln due to a surge in export growth.*



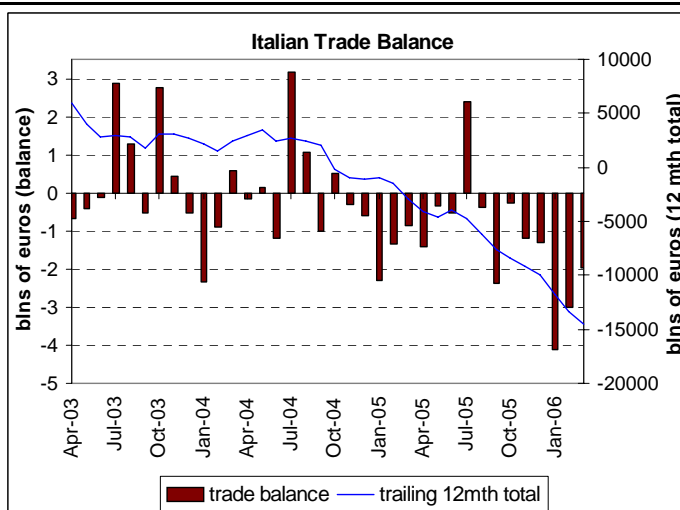
### Euro Zone Exports & Imports

*Euro Zone Exports expanded 15% M/M and 17% Y/Y in March while Imports expanded 11% M/M and 20% Y/Y.*



### Italian Trade Balance

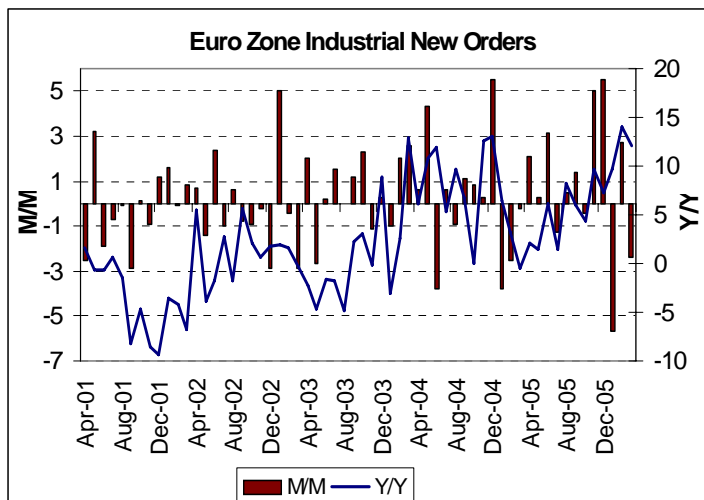
*The Italian Trade deficit narrowed from 2.9 mln euros in February to 2 mln in March as exports expanded 16% M/M.*



## ***Euro Zone Orders, Spanish Factory Orders & Italian Orders***

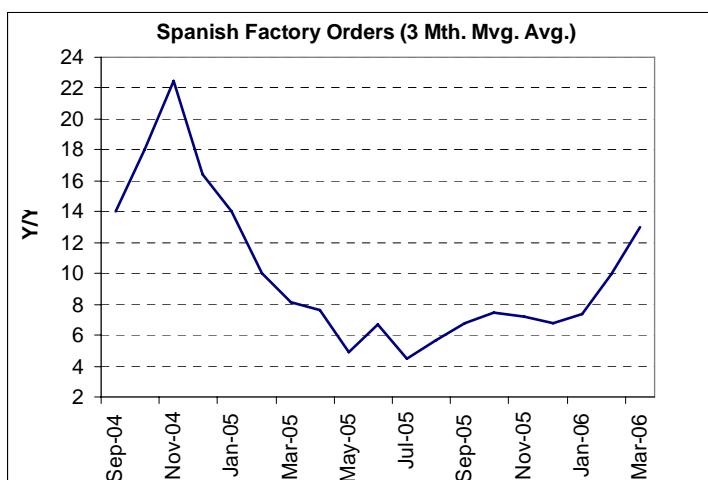
### ***Euro Zone Industrial Orders***

*The Euro Zone's March  
Industrial New Orders contracted  
2.4% M/M while expanding  
12.1% Y/Y in March.*



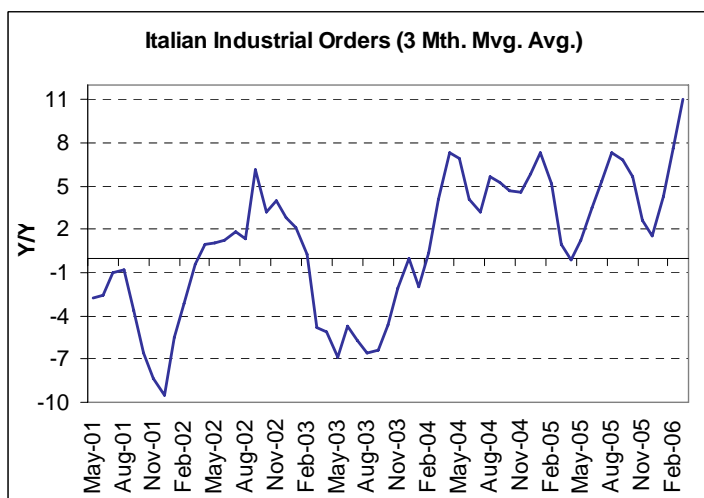
### ***Spanish Factory Orders***

*Spanish Factory Orders expanded  
16.8% Y/Y in March, led by strong  
durable goods sales.*



### ***Italian Industrial Orders***

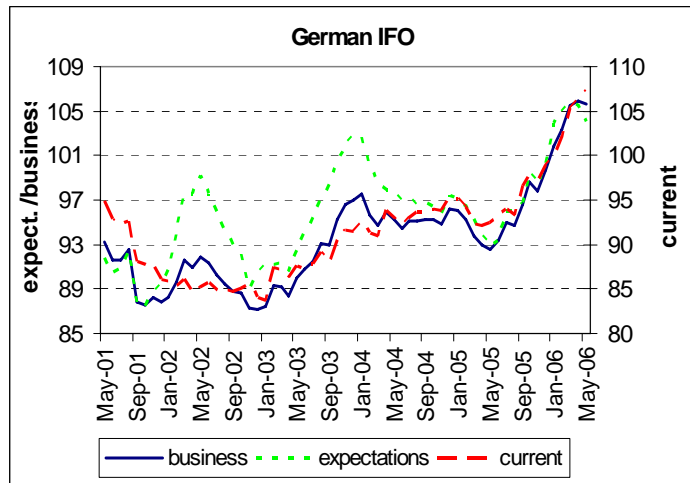
*Italian Industrial Orders contracted  
3.4% M/M while expanding 9.3%  
Y/Y in March. Industrial Sales  
expanded 3.1% M/M and 14.5%  
Y/Y.*



## German IFO, Italian Confidence & French Current Account

### German IFO

German Business Confidence slowed slightly in May, declining from 105.9 in April to 105.6. The Expectations Index contracted from 105.5 to 104 while the Current Assessment Index increased from 105.4 to 107.3. In light of the stronger Euro and higher oil prices, expectations were for a weaker outturn.



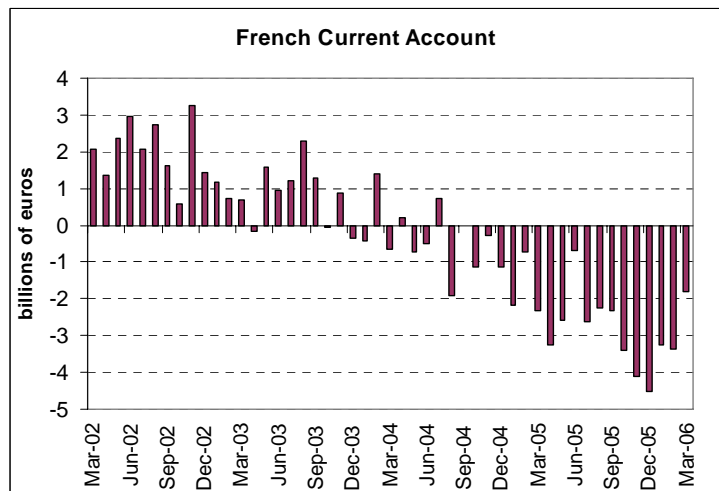
### Italian Consumer Confidence

Italian Consumer Confidence rose from 106 in April to 107.6 in May as the uncertainty surrounding recent elections faded.



### French Current Account

France's March Current Account deficit narrowed from 3.5 bln euros in February to 1.8 bln.



## News

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May 24<sup>th</sup> – **ECB Member Nicholas Garganas** stated that Euro Zone growth may exceed the bank's forecast this year and added that "There is clearly a case for a gradual rebalancing of rates in view of risks to inflation." Garganas also characterized the risks to price stability as "substantial". Members Liebscher and Issing reiterated the views earlier in the week stating, "if developments continue as expected then there's a reason to withdraw accommodation." Liebscher added, "I see a certain increase in risks on price stability, there is no doubt about it."

May 24<sup>th</sup> – **The German cabinet approved law changes that liberalize** doctors' working practices and guaranteed patients medical treatment. The measures also allow doctors to work beyond the age of 68. The German government will also increase welfare benefits for people in eastern Germany, increasing the monthly payments from 331 euros to 345 euros.

May 24<sup>th</sup> – **Germany's preliminary State Consumer Prices** were as follows:  
Baden Wuerttemberg – 0.1% M/M, 1.9% Y/Y    North Rhine West – 0.2% M/M, 1.7% Y/Y  
Brandenburg – 0.1% M/M, 2.3% Y/Y Bavaria – 0.2% M/M, 2.3% Y/Y

May 24<sup>th</sup> – **Ifo member Gebhard Flaig commented on the May Ifo** stating that "the outlook for further economic recovery still remains positive overall." Flaig noted that the business climate has cooled slightly but that exporters continue to assess their export opportunities as excellent.

May 23<sup>rd</sup> – **The OECD cut its 2007 German growth forecast from 1.7% to 1.6%**, stating that the VAT increase will cool consumer spending. In addition, employment is forecasted to improve only gradually and household consumption should gain momentum this year. The German deficit was forecasted to remain slightly above 3% this year and then to decline to 2.25% in 2007.

May 23<sup>rd</sup> – **The OECD forecasts that French growth is accelerating as exports** pick up and unemployment falls. GDP is forecasted to grow 2.1% this year and 2.2% in 2007. Unemployment is forecasted at 9.5% this year and 9.2% in 2007. The OECD also raised its Italian growth forecast from 1.1% to 1.4% in 2006. The 2007 growth forecast was trimmed from 1.5% to 1.3%.

May 23<sup>rd</sup> – **Belgian Business Confidence declined in May** as oil costs weighed on profit margins. The index contracted from 4.3 in April to 2.0 in May.

May 23<sup>rd</sup> – **German non wage labor costs reached** a record in 2005 as manufacturers paid an average of 22,000 euros per employee according to the IW Institute. Costs expanded 0.8% Y/Y in 2005, a "new record".

## Key Dates This Week

May 23<sup>rd</sup> – **Business confidence among German Tradesman** rose to a 5yr high in Q1, increasing from 65.4 in the 4<sup>th</sup> quarter of 2005 to 70.9. Domestic demand, large foreign orders and government measures are credited for the increase.

May 22<sup>nd</sup> – **The Kiel Institute stated that domestic demand in Germany** has failed to stabilize and is likely to underperform once again in 2007. Dennis Snower, head of the institute, stated, “Domestic demand has improved but it doesn’t look like a sustainable improvement.” The comments mirror those made by the German Finance Ministry which stated that increasing tax revenues shouldn’t be interpreted as a “clear upturn in domestic demand”. The Ministry added that “a comparable development of retail sales data isn’t noticeable.”

May 22<sup>nd</sup> – **The Bundesbank stated that accelerating money supply growth**, rising energy costs and higher VAT in Germany pose “serious” threats to inflation in the Euro Zone. The report stated, “There are immediate inflationary risks emerging” and that money supply growth “is a serious warning sign.”

May 22<sup>nd</sup> – **The chief employer’s negotiator stated that he considers wage** talks with the Marburger Bund union for university clinic doctors to be over, and that the wage accord by Ver.di will stand. The Marburger Bund union had rejected the wage accord won by Ver.di, sticking to their demands of a 30% wage increase and better working conditions.

May 18<sup>th</sup> – **Spanish Prime Minister Jose Luis Zapatero stated** that the Spanish economy will exceed government forecasts and accelerate to 3.5% this year.

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/25	Spanish Producer Prices (APR)	0.6% M/M	0.3% M/M
05/25	Italian Business Confidence (MAY)	95.6	96.1
05/25	Italian Retail Sales (MAR)	0.1% M/M	0.1% M/M
05/26	Italian Hourly Wages (APR)	0.2% M/M	0.3% M/M
05/25	German CPI (MAY)	1.9% Y/Y	2.0% Y/Y
05/28	German Retail Sales (APR)	1.5% M/M	-2.7% M/M
05/29	Italian Retailer’s Confidence (APR)	--	103.7
05/30	Spanish Retail Sales (APR)	--	2.0% Y/Y
05/30	Euro Zone M3 (APR)	--	8.6% Y/Y

Valance Co., Inc.

# Valance Economic Report: Japan

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May 24, 2006

Growth in Japan was solid in Q1, albeit not at the pace seen in Q4 2005. Services demand declined, as did the Leading Index. Despite recent softness on the consumer side, we continue to look for the BoJ to end its Zero Interest Rate Policy as early as Q3 2006. Due to recent improvements with consumers becoming optimistic, much of the recent softness may prove to be transitory.

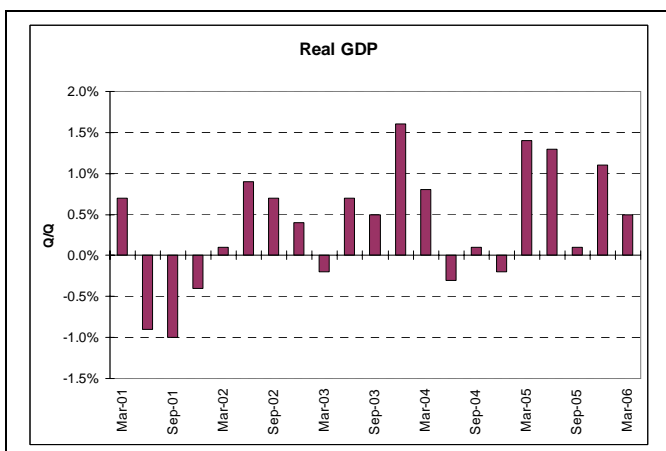
## Weekly Highlights

**Real GDP** – increased 0.5% Q/Q and at an annualized rate of 1.9% in Q1. (page 15)

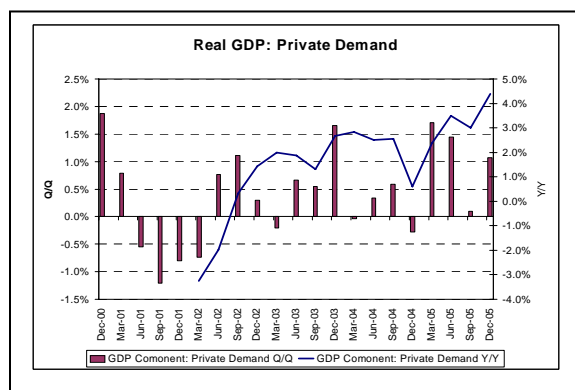
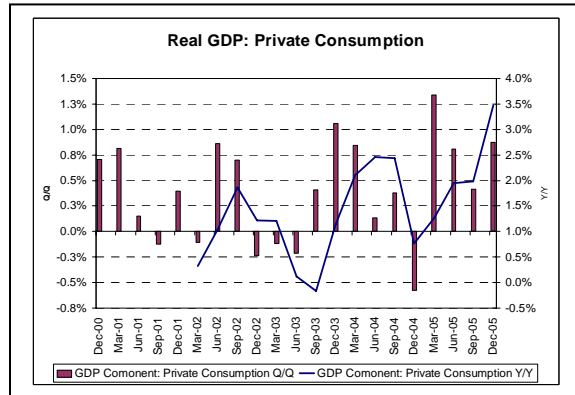
**Tertiary Index**– declined 0.6% M/M in March. (page 18)

**Leading Index**– declined from 60.0% to 54.5% in March. (page 18)

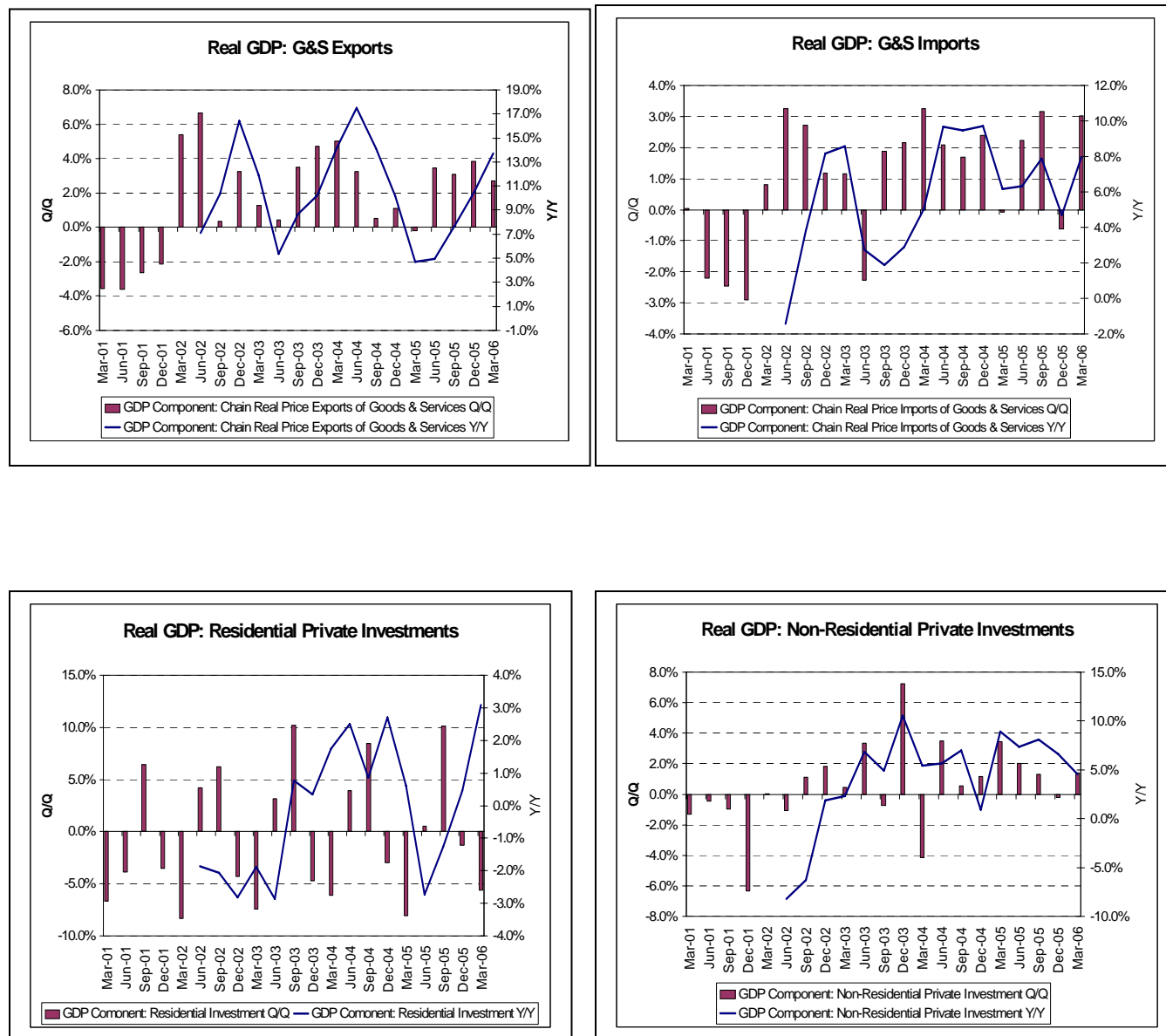
## Chart(s) of the Week: Gross Domestic Product



Preliminary data indicated that Japan's Real GDP increased 0.5% Q/Q in Q1 (from 1.1% in Q4) as the economy grew at an annualized rate of 1.9% (from 4.3% in Q4). The data on Q1 growth was slightly better than the annualized rate of 1.1% that economists expected. Private demand improved 0.8% Q/Q. Residential investment improved 1.1% Q/Q and Capital investments improved 1.4% Q/Q, all contributing to Q1 growth. Net exports increased 2.7% Q/Q while net imports increased 3.0% Q/Q. The GDP deflator met expectations, declining 1.3% after having declined 1.6% in Q4. The Domestic Demand GDP deflator was unchanged Y/Y.



## Gross Domestic Product

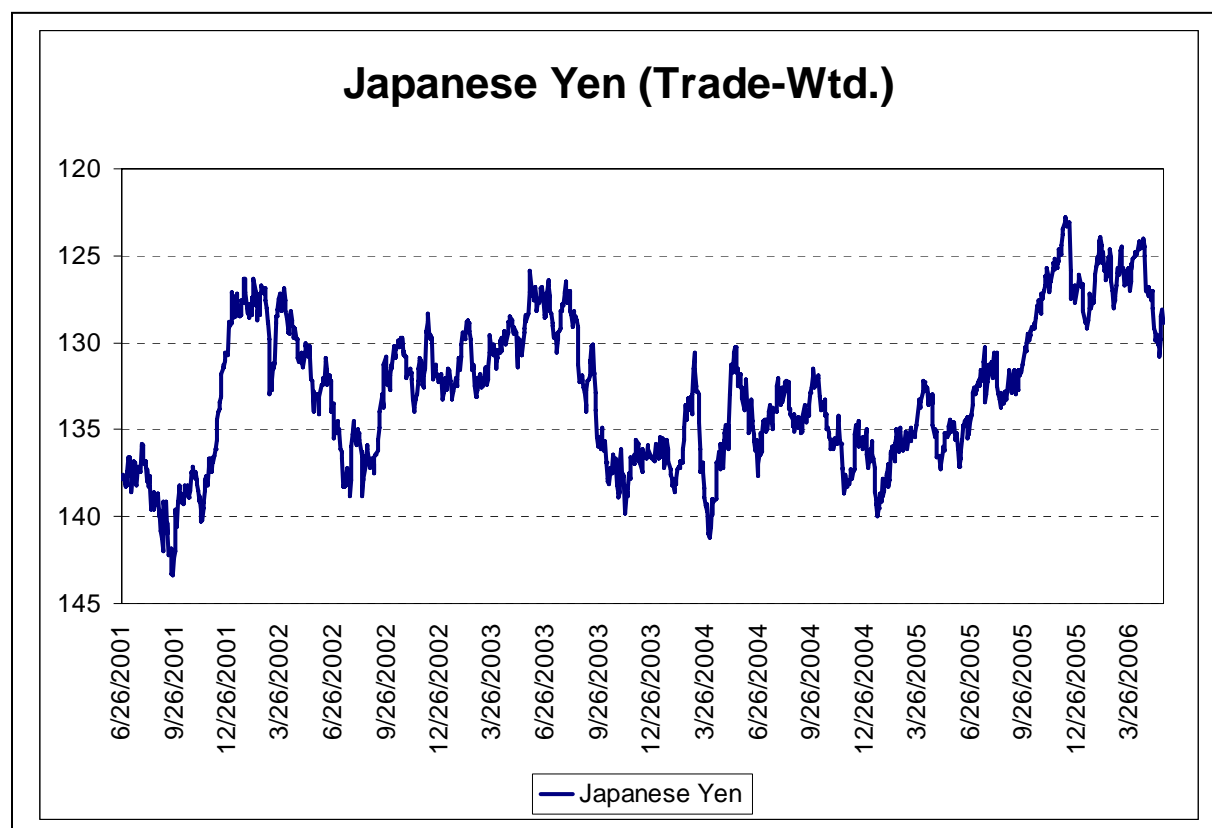




## ***Japan's Financial Balances***

### ***Financial Balances***

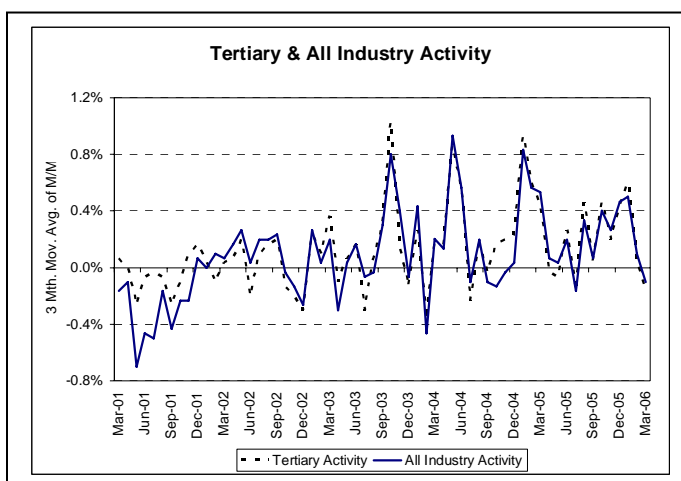
<i><b>Japan</b></i>	<i><b>Last period (¥trln)</b></i>	<i><b>Last 12mth. as a % of GDP</b></i>
Budget Balance	-3.50 (Dec)	-6.9%
Trade Balance	0.58 (Dec)	1.5%
Current Account Balance	1.87 (Dec)	3.5%
Private Balance	--	11.6%



## Tertiary/All Industry Index & Leading/Coincident Indices

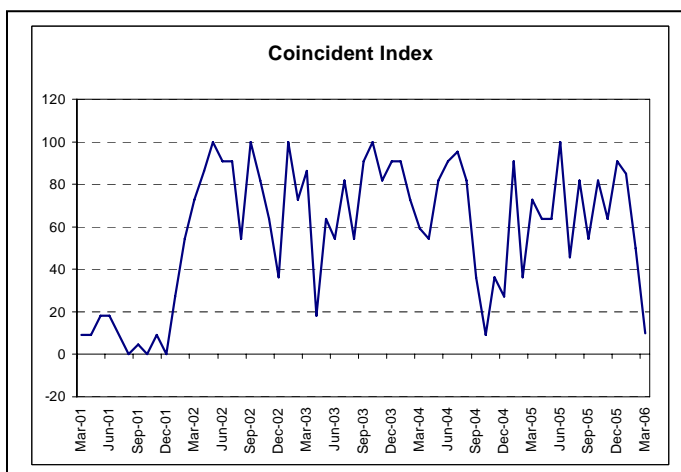
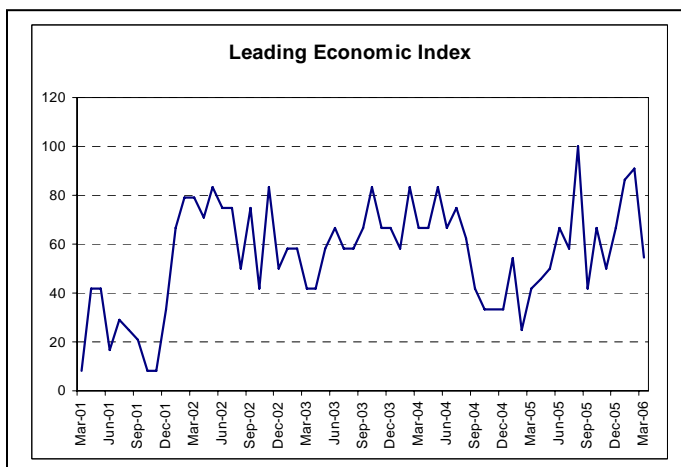
### Tertiary/All Industry Index

The Tertiary Industry Index declined 0.6% M/M while the All Industry Index declined 0.4% M/M in March. Both exceeded the 0.2% M/M and 0.1% M/M declines the market expected, respectively. The decline in the Tertiary Industry index was caused by a decline in services, wholesale/retail, and the finance/insurance sectors.



### Leading/Coincident Indices

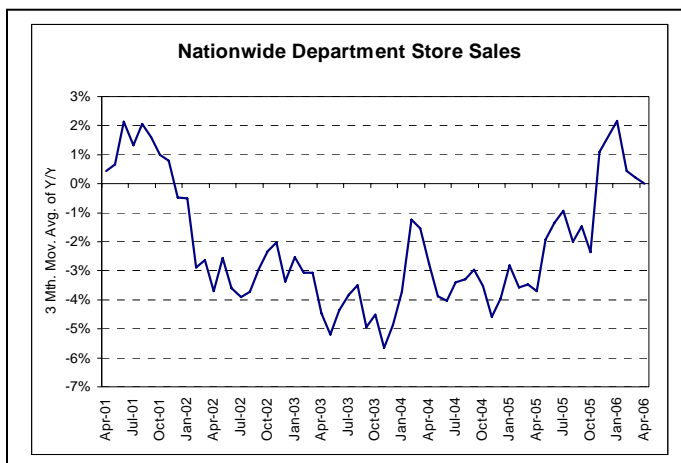
The Leading Economic Index declined from 90.9 in February to 54.5 in March, while the Coincident Index declined from 50.0 in February to 10.0 in March. Declines in the leading index were due to reduced producer final demand, fewer new job offers, and fewer new machinery orders. Within the Coincident Index, most sectors saw declines with the exception of manufacturing overtime.



## ***Nationwide Dept. Store Sales, Tokyo Dept. Store Sales & Convenience Store Sales***

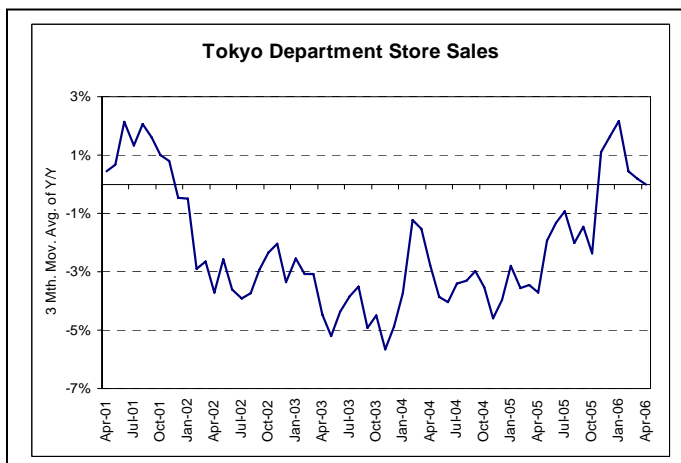
### ***Nationwide Dept. Store Sales***

*Nationwide Dept. Store Sales declined 0.6% Y/Y in April. The decline was largely seen in clothing and household goods declines, while accessories, sundries, and cosmetics improved.*



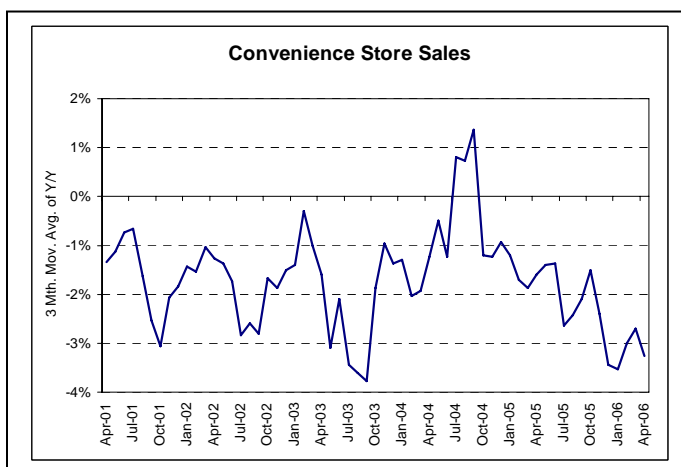
### ***Tokyo Dept. Store Sales***

*Tokyo Dept. Store Sales declined 0.5% Y/Y in April. The decline was centered in household appliances while accessories, sundries and cosmetics improved.*



### ***Convenience Store Sales***

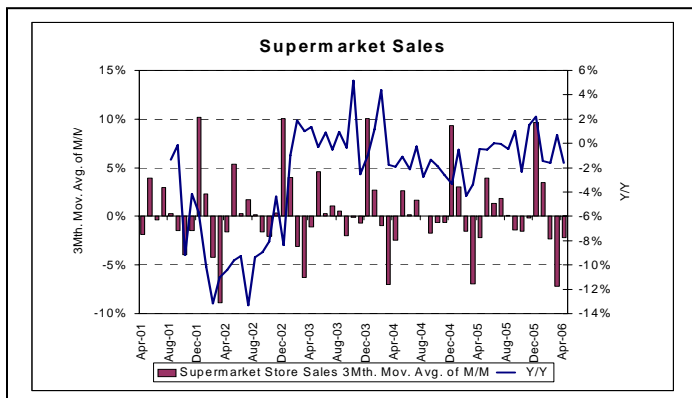
*Convenience Store Sales declined 4.9% Y/Y in April. On a same-store basis, sales declined 4.9% Y/Y while traffic declined 4.8% Y/Y.*



## Supermarket Sales & News

### Supermarket Sales

Supermarket Sales increased 1.7% M/M and declined 3.3% Y/Y in April. Y/Y declines were driven by declines in services and clothing sectors.



### News

**May 24<sup>th</sup>** - IMF Deputy Director Daniel Citrin commented that “Any increase in interest rates would be probably both gradual and would still imply that monetary policy is rather accommodative and remains supportive of growth...I don’t see that they would be tightening unduly.” He also commented that he sees the economy moving forward “quite briskly,” that “corporate profitability is very high and household incomes and employment have started to improve,” and that Japan has exited from the period of deflation. The IMF expects the economy to expand 2.75% this year and 2% in 2007, below its April forecast of 2.8% due to recent revisions made to its GDP numbers.

**May 23<sup>rd</sup>** – BoJ’s Gov. Fukui commented on the upcoming change in rates, stating that, “The economy has emerged from a protracted slump, but some areas are not healthy.” He also commented that, “We can anticipate that the supply-demand gap will close and that inflationary pressures will steadily grow,” but noted that, “We must be mindful of minimizing fluctuations of the economy and prices.”

**May 23<sup>rd</sup>** – The OECD increased its growth estimates for 2006 and 2007 from 2.0% for both years, to 2.8% in 2006 and 2.2% in 2007. They expect Japan’s Unemployment Rate to be reduced to around 3.5% in 2007 based on “the strength and duration of the upturn.” They expect the inflation rate to approach 1% by the end of the 2007.

**May 22<sup>nd</sup>** – Six economists interviewed by the Nihon Keizai Shimbun have projected real economic growth of 2.3%-3.1% through FY06. Three of those economists see the BoJ lifting its ZIRP in July, while two picked August and one picked September.

**May 22<sup>nd</sup>** – The BoJ lifted its outlook for the economy during its monetary policy meeting, keeping ZRIP in place, but noting that “[the] economy is expected to expand moderately.” This comment was an improvement from the April report, which noted that “[the economy] is expected to continue to recovery steadily.” In recently released minutes, it was noted that some BoJ policy members felt that the market misunderstood how quickly the BoJ would end its ZIRP. Also in the minutes, some commented that it would be necessary to closely monitor the effects of changes in service prices at the start of the fiscal year. On the corporate side, it was noted that some companies are starting to reflect higher costs in prices while others, particularly manufacturers, are still having difficult doing so.

**May 22<sup>nd</sup>** – Total assets held by Japanese banks increased 2.3% Y/Y as of Feb 28, reaching their highest level in 4.5 years, according to the BoJ.

## Key Dates This Week

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/24	Merchandise Trade Balance (Apr)	¥800.0 Bln	¥970.4 Bln
05/24	Adj. Merchandise Trade Bal. (Apr)	¥620.0 Bln	¥698.1 Bln
05/25	Tokyo CPI (May M/M)	0.1%	0.2%
05/25	Tokyo Core CPI (May M/M)	0.1%	0.0%
05/25	Tokyo CPI (May Y/Y)	0.3%	0.3%
05/25	Tokyo Core CPI (May Y/Y)	0.3%	0.3%
05/25	Nat'l CPI (Apr M/M)	0.2%	-0.1%
05/25	Nat'l CPI (Apr Y/Y)	0.4%	0.3%
05/25	Nat'l Core CPI (Apr M/M)	0.0%	0.0%
05/25	Nat'l Core CPI (Apr Y/Y)	0.5%	0.5%
05/25	Corp. Service Prices (Apr Y/Y)	0.0%	-0.2%
05/28	Large Retailers' Sales (Apr)	0.0%	-0.3%
05/28	Retail Trade (Apr M/M)	N/A	-0.3%
05/28	Retail Trade (Apr Y/Y)	N/A	1.1%
05/29	Jobless Rate (Apr)	N/A	4.1%
05/29	Job-Applicant Ratio (Apr)	N/A	1.01
05/29	Overall H Hold Spending (Apr Y/Y)	N/A	-2.1%
05/29	Industrial Production (Apr M/M)	N/A	0.2%
05/29	Industrial Production (Apr Y/Y)	N/A	3.1%
05/30	Vehicle Production (Apr Y/Y)	N/A	5.4%
05/30	Small Business Confidence (May)	N/A	50.8
05/30	Labor Cash Earnings (Apr Y/Y)	N/A	0.4%
05/30	Overtime Earnings (Apr Y/Y)	N/A	3.3%
05/31	Housing Starts (Apr Y/Y)	N/A	3.3%
05/31	Annualized Housing Starts (Apr)	N/A	1.217 Mln
05/31	Construction Orders (Apr Y/Y)	N/A	-15.7%
06/01	Vehicle Sales (May Y/Y)	N/A	-7.8%

Valance Co., Inc.

**Valance Economic Report: United Kingdom**

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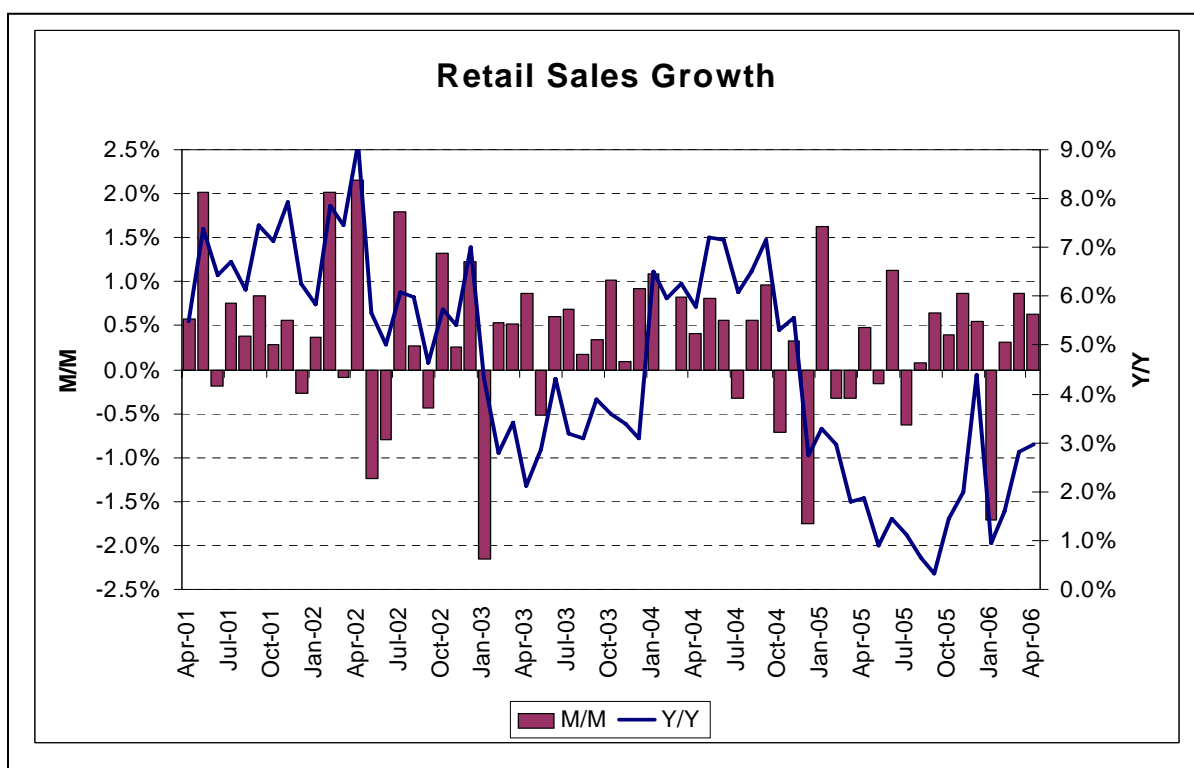
May 24, 2006

This week's data was somewhat positive as Retail Sales were solid while CBI Factory Orders held steady from a large increase in export orders.

**Weekly Highlights**

**Retail Sales-** increased 0.6% M/M and 3.0% Y/Y in April. (page 22)

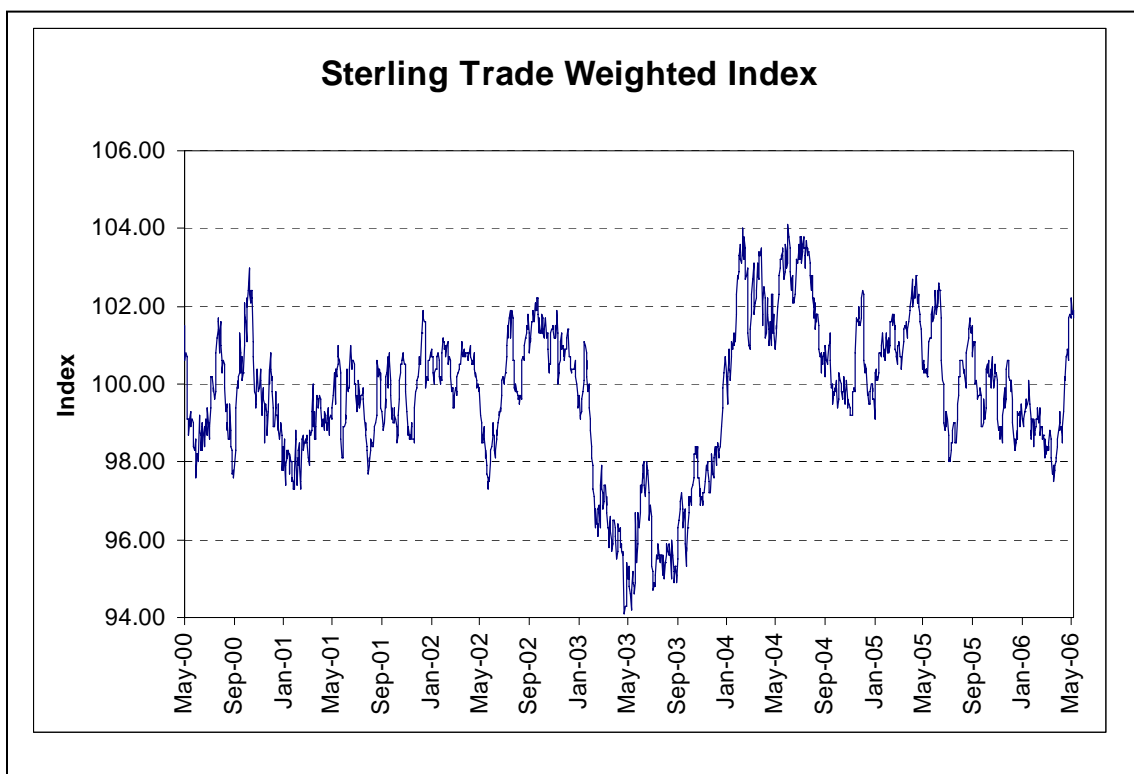
**The Budget Deficit-** increased from £0.40 bln in April 2005 to £1.40 bln in April 2006. (page 24)

**Weekly Releases & News****Chart of the Week: Retail Sales Growth**

Retail Sales increased 0.6% M/M and from 2.8% Y/Y in March to 3.0% Y/Y in April. Non-food stores sales increased 1.4% M/M and 4.2% Y/Y mainly due to the recent surge in housing activity. Sales at household and electrical good stores increased 3.3% M/M and 7.1% Y/Y. Food stores sales decreased 0.3% M/M and increased 2.4% Y/Y.

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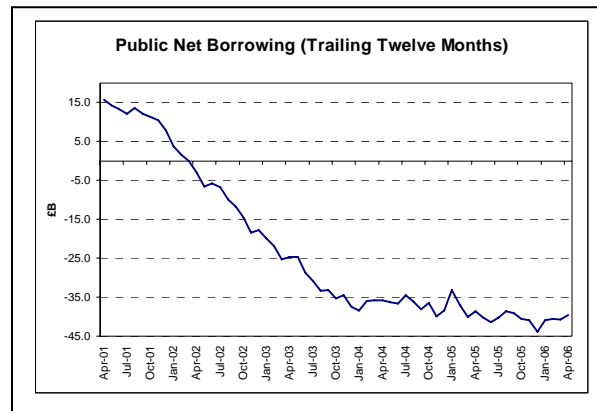
<i>U.K.</i>	<i>Last Period (blns)</i>	<i>Last 12mth. % of GDP</i>
Budget Balance (monthly)	-£1.4 (Apr)	--
Trade Balance (monthly)	-£3.8 (Mar)	-1.3%
Curr. Acct. Balance (quarterly)	-£11.0 (Dec)	-3.9%
Private Balance	--	-3.4%



## Budget Deficit

### Budget Deficit

*The Budget Deficit increased from £0.40 bln in April 2005 to £1.40 bln in April 2006.*





## **Data & Comments**

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### **Data**

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#### **CBI Industrial Trends Survey:**

CBI Factory Orders decreased slightly from -11 to -12 in May, holding up from a surge in export demand. Export orders jumped from -13 to 0, the highest since February 1996. Average Prices decreased from +11 to 0. Finished Stocks increased from +7 to +10.

#### **BBA Mortgage Lending:**

BBA Mortgage Lending decreased 9.0% M/M and decreased 2.0% from its six month average in April.

### **Comments**

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#### **MPC Member Kate Barker comments:**

May 24<sup>th</sup> – MPC Member, Kate Barker commented that changing interest rates wouldn't have “much of an effect” on house prices, which “are a concern to many.”

#### **MPC Nominee David Blanchflower comments:**

May 24<sup>th</sup> – The MPC's newest appointee, David Blanchflower, insists that his new role will be his “primary responsibility” despite acknowledging that he will spend less than half his time in Britain. The news of Professor Blanchflower's new role, an economist who left Britain for the United States 17 years ago who will commute from America at British taxpayers' expense for 12 days a month, has sparked controversy. There have been suggestions that it would be “much more difficult” for him to follow the state of the British economy from his Ivy League college than for a UK resident. Blanchflower went on to discuss several topics including:

On whether he agrees with Stephen Nickell's view that lower rates are needed: *At this moment I'm not persuaded one way or the other. I'm going to wait and see at this moment. There is some evidence in that direction but there is counter evidence as well. It's a time to be cautious, look at the data, be briefed by the bank and try to make an independent decision.*

On unemployment: *It appears that unemployment has actually trended down significantly. Ex-ante I don't think we would have expected that. It's been driven by changes in productivity. We've seen permanent changes in equilibrium level unemployment levels. Inflation has remained relatively constant. It doesn't seem to me that we are very far from the NAIRU or the equivalent rate. It has to do with changes in productivity potentially brought by technology. It's hard until it's finished to see that that's happened. There's lots of ways of calculating it but given that they all come out with the same answer.*

## ***News & Upcoming Dates***

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### ***News***

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**May 21<sup>st</sup> - Hutton warns of looming pension's crisis** - Britain will face a pension's crisis unless the government restores the earnings link to the basic state pension by 2012, John Hutton, the work and pensions secretary, warned. Tony Blair and Gordon Brown have reached a deal to restore the earnings link, one of the central recommendations of Lord Turner's Pensions Commission, from 2012 instead of 2010 to help to meet the Treasury's concerns about affordability. Under the deal, the date could slip to 2015 if the Treasury still deemed it to be too costly. But Mr. Hutton made clear the government could not wait that long. Echoing Lord Turner's recommendation that the state pension should start to rise in line with earnings between 2010 and 2012, Mr. Hutton said. "There isn't a pension's crisis now and I agree with him there isn't, but there will be one if we don't take action within broadly that time frame."

**May 19<sup>th</sup> - BOE Tucker: Pension Uncertainty Explains Low Investment** - Concerns about the viability of company pension schemes and the threat of competition from China and India have been the main factors behind the slower-than-expected pickup in U.K. business investment, Bank of England Executive Director, Paul Tucker said. Despite strong profits and an economy which has grown without interruption for over a decade, that has yet to happen, and the MPC has been looking for an explanation. Tucker said the realization that the scale of shortfalls in the funding of company pension funds and the impact this has had on the way investor's value companies may be part of the reason for the sluggish pickup in investment. "Firms may...have been reviewing their preferences between risk-taking in their core business and risk-taking via pension provision and for a while may have been unusually uncertain about how equity markets value those different sources of uncertainty," Tucker stated. "If so, that may conceivably offer part of the explanation for the measured recovery in U.K. business investment having been weak, relative to the economy's total output, compared with past cycles."

**May 18<sup>th</sup> - Nationwide profits up but lending slumps** - Nationwide posted a 15% rise in annual profits, but said its mortgage business slumped as it scaled back lending in fear of a tough housing market. Its share of new mortgage business fell to 6.7% from its traditional 9% share of the market, but said it planned to return to that level this year. "We were concerned this time last year about what would happen in the housing market so we made a clear decision that we wanted to concentrate on quality," Stuart Bernau, Commercial and Communications Director, told Reuters. "We've had the soft landing and the economy has stayed benign so we'll want to push back to par share." He commented that Nationwide expects house price inflation this year to be similar to 2005 at between 3% and 5%, mainly due to a shortage of houses.

**May 18<sup>th</sup> - Ex-BOE's Julius Would Have Voted for U.K. Rate Cut** - Former MPC Member DeAnne Julius, said she would have voted to reduce the benchmark interest rate this month, siding with outgoing rate-setter Stephen Nickell. "I would have cut. The labor market seems to be getting a little more spare capacity and that's indeed the main generator of what's sometimes called domestically generated inflation. It does seem to me that Steve Nickell has a very good point."

## *Upcoming Dates*

### *Key Dates This Week*

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/25	GDP Q1	0.6% Q/Q 2.2% Y/Y	0.6% Q/Q 1.8% Y/Y
05/26	Nationwide House Prices	--	0.1% Q/Q 4.8% Y/Y
05/26	BBA Mortgage Lending	--	--

Valance Co., Inc.

# Valance Economic Report: *Canada*

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April 24, 2006

**The Bank of Canada (BoC) hiked interest rates 25bps to 4.25%, the highest level since 2001, but signaled a pause to follow. On the data front, Core CPI ticked down while Retail Sales surprised to the upside.**

## Weekly Highlights

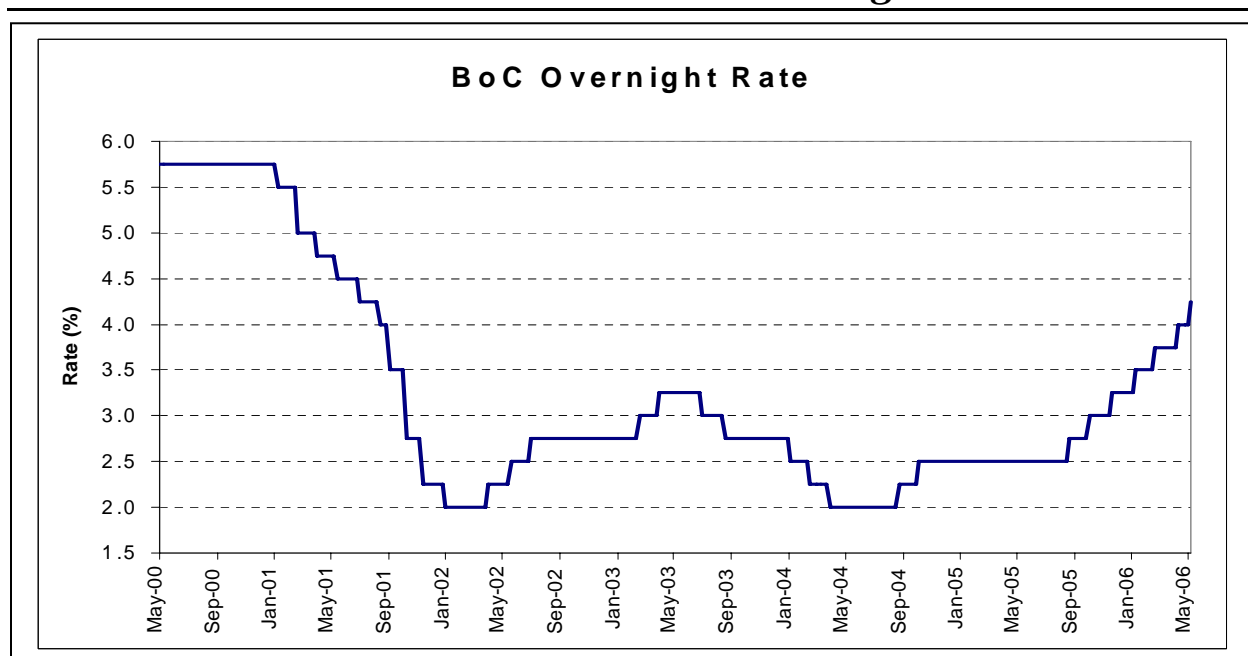
**The Bank of Canada** - raised its overnight rate by 25bps to 4.25%, as expected. (page 28)

**Core CPI** – decreased 0.1% M/M and increased 1.6% Y/Y, in April. (page 30)

**Retail Sales** – increased 1.5% M/M and 5.9% Y/Y in March. (page 30)

## Weekly Releases & News

### Chart of the Week: *BoC Overnight Rate*



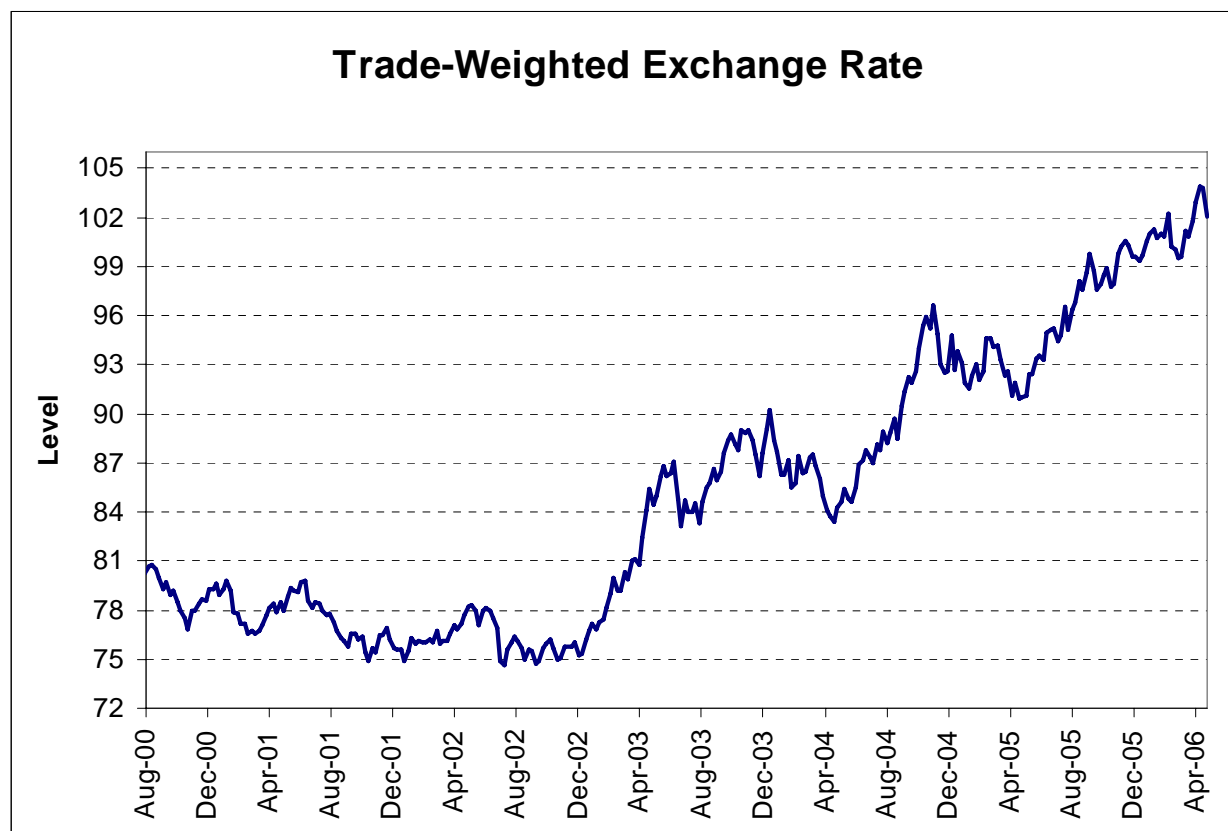
The Bank of Canada (BoC) raised its overnight rate by 25bps to 4.25%, to reach the highest level since August 2001. To support this move, the Bank noted, “Recent Canadian data confirm that domestic demand remains solid, and that both CPI and core inflation are evolving largely in line with the Bank’s expectations.” The Bank, however, in explicit pause language, stated, “With today’s increase, the target for the overnight rate is now at a level that is expected to keep the Canadian economy on the base-case path projected in the April Monetary Policy Report (MPR) and to return inflation to the 2 per cent target.” The Bank of Canada’s next scheduled date for announcing the overnight rate target is July 11<sup>th</sup>, 2006 and the next Monetary Policy Report Update will be published on July 13<sup>th</sup>, 2006.

## ***Financial Balances & Trade Weighted Exchange Rate***

### ***Financial Balances***

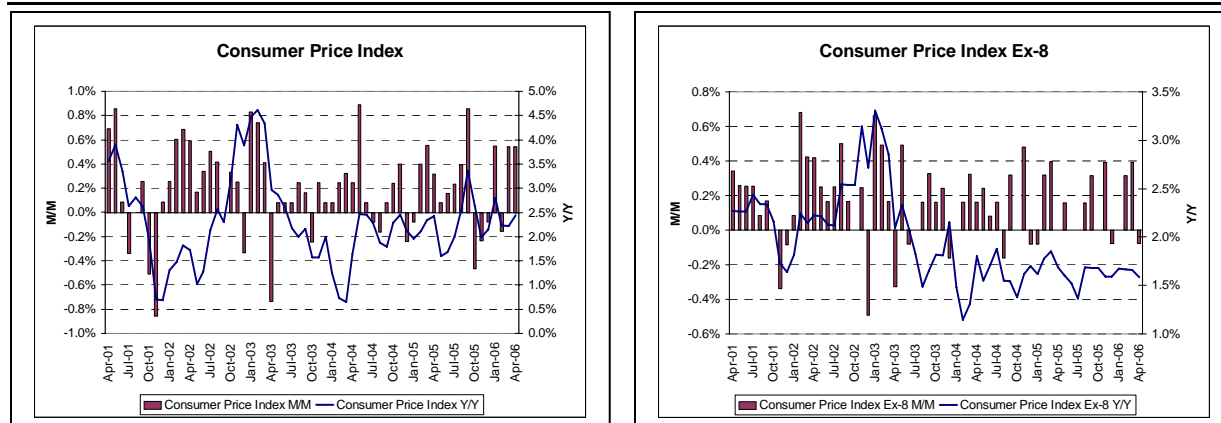
<i>Canada</i>	<i>Latest period (C\$bbln)</i>	<i>Last 12mth. as % of GDP</i>
Budget Balance	4.1 (Feb)	0.4%
Trade Balance	6.3 (Feb)	4.8%
Current Account Balance	13.3 (Q4)	2.2%
Private Balance	--	1.8%

### ***Trade-Weighted Exchange Rate***



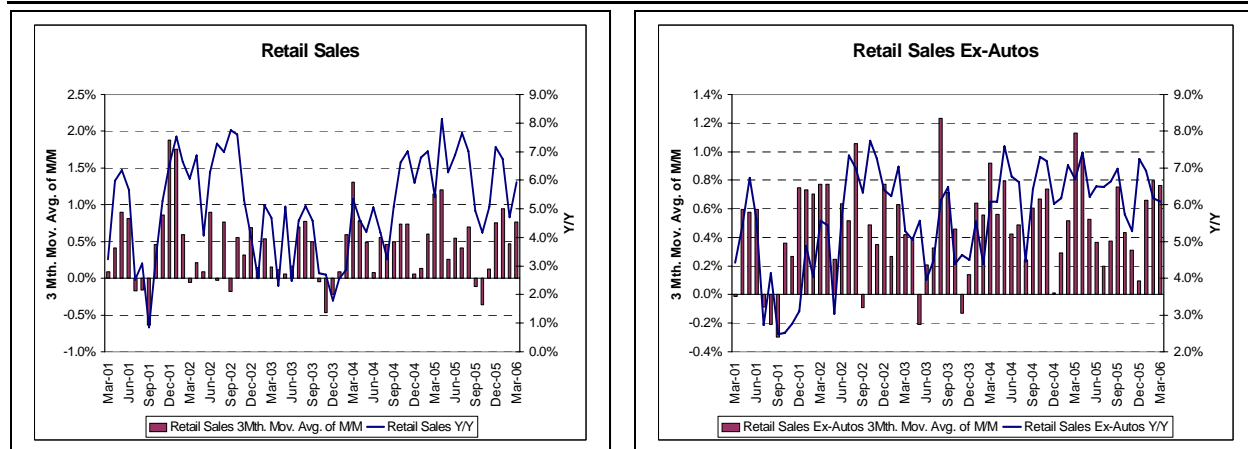
## CPI & Retail Sales

### CPI



Canada's Headline CPI increased 0.5% M/M and 2.4% Y/Y in April, in line with expectations. Transportation (+3.3%), shelter (+0.3%), and alcoholic beverages and tobacco products (+0.3%), all exerted some upward pressure on Headline CPI. On the other hand, Core CPI unexpectedly declined 0.1% M/M, helped by a large decrease in women's clothing prices (-5.8%). The purchase and leasing of automotive vehicles (-0.7%) also exerted some downward pressure.

### Retail Sales

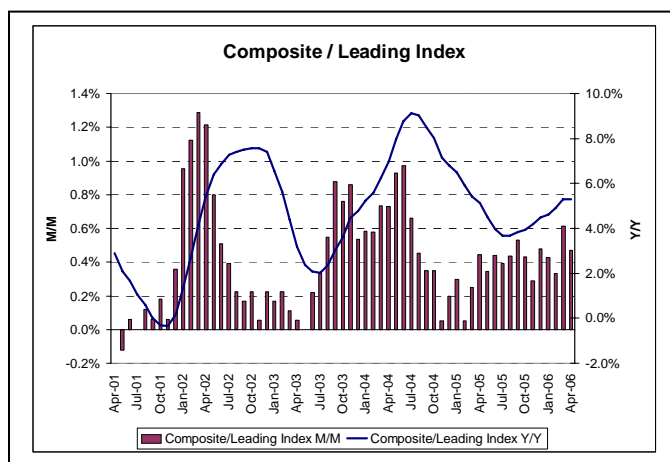


Retail Sales growth increased 1.5% M/M in March, well above expectations for a reading of 0.6% M/M, with all sectors, except food and beverage, posting higher sales. Y/Y growth increased 5.9%. Retail Sales, excluding autos, increased 0.7% M/M, and 6.1% Y/Y.

## Composite/Leading Indicator & News

### Composite/Leading Indicator

The Composite/Leading Indicator increased 0.5% M/M and 5.3% Y/Y in April, above expectations. The M/M increase came as a result of strong sales of durable goods, furniture and appliances sales and gains in the S&P/TSX stock price index.



### News

**May 24th - Rising Canadian Dollar Helps Strengthen Productivity** - The Canadian Finance Minister, Jim Flaherty, commented that the Canadian dollar's appreciation against the U.S. dollar has made the Canadian economy more Productive. "Technology and machinery and equipment are more affordable to Canadian industry when purchased from abroad, and what we're seeing is an increase in our productivity," Flaherty stated.

### **May 23<sup>rd</sup> - Summary of OECD May 2006 Canada Economic Outlook**

	2007	2006	2005	2004	2003
Real GDP	3.3%	3.1%	2.9%	2.9%	2.0%
Private consumption	3.6%	3.3%	4.0%	3.4%	3.1%
Government consumption	2.9%	3.5%	2.8%	2.7%	2.9%
Gross fixed investment	3.7%	6.1%	6.6%	6.6%	5.9%
Total domestic demand	3.4%	4.0%	4.5%	3.9%	4.6%
Net exports	0.0%	-0.7%	-1.5%	-0.9%	-2.4%
Employment	1.6%	1.7%	1.4%	1.8%	2.4%
Unemployment Rate	6.2%	6.4%	6.8%	7.2%	7.6%
Employee compensation	6.3%	6.1%	5.4%	4.2%	4.2%
Unit Labor Cost	3.0%	3.0%	2.4%	1.3%	2.2%
Disposable Income	5.8%	5.3%	4.0%	3.9%	3.7%
GDP Deflator	1.9%	3.1%	3.1%	3.1%	3.3%
Consumer Price Index	2.3%	2.0%	2.2%	1.8%	2.8%
PCE Deflator	1.6%	1.2%	1.6%	1.4%	1.6%
Household saving ratio	1.0%	0.5%	-0.2%	1.4%	2.4%
Gov. financial balance	1.8%	2.2%	1.7%	0.7%	0.0%
Current account balance	3.3%	3.3%	2.2%	2.2%	1.5%
Long-term interest rate	4.6%	4.5%	4.1%	4.6%	4.8%

## *News Releases (Cont'd.) & Upcoming Dates*

### *News Releases (Cont'd.)*

**May 23<sup>rd</sup> – Summary from the COMPAS web-survey** - The COMPAS web-survey of CEO's and leaders of small, medium, and large corporations which was conducted on May 17<sup>th</sup>-19<sup>th</sup>, showed by a three-to-one margin that business panelists were not in favor of the Bank of Canada's increasing interest rates today. Panelists did not want rates to increase due to the strong Canadian dollar. They consider the ideal value of the Canadian dollar to be U.S. \$.86, which is lower than its current value, but higher than the panel's ideal value over the last 2-3 years. Most panelists said that the strong dollar has neither helped nor harmed their business, but a third reported that the rising dollar has done some harm.

Although panelists have opposed to further increase in rates, the Bank of Canada's Governor, David Dodge, was praised for his astute handling of monetary policy. For inflation, he earned a grade of 77%, one of the best performance scores ever seen in the COMPAS databank of performance scores. He also received 71% for managing interest rates and 67% for the exchange rate. The scores are basically unchanged from their December 2004 values.

### *Key Dates This Week*

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/30	Industrial Production (M/M) (APR)		0.8%
05/30	Raw Materials Price Index (M/M)		0.8%
05/31	Gross Domestic Product (M/M)	0.4%	0.2%
05/31	Quarterly GDP Annualized 1Q	3.0%	2.5%



Valance Co., Inc.

# Valance Economic Report: Australia

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May 24, 2006

The Federal Budget continues to receive a positive reaction in terms of its impact on growth and is seen as offsetting the “negative” of the RBA’s rate hike earlier this month. Elsewhere, housing affordability has worsened and according to the RBA, labor shortages may fuel wage growth and pressure inflation upwards.

## Weekly Highlights

**Average Weekly Wages** – rose 0.9% Q/Q and 4.5% Y/Y in Q1. (page 33)

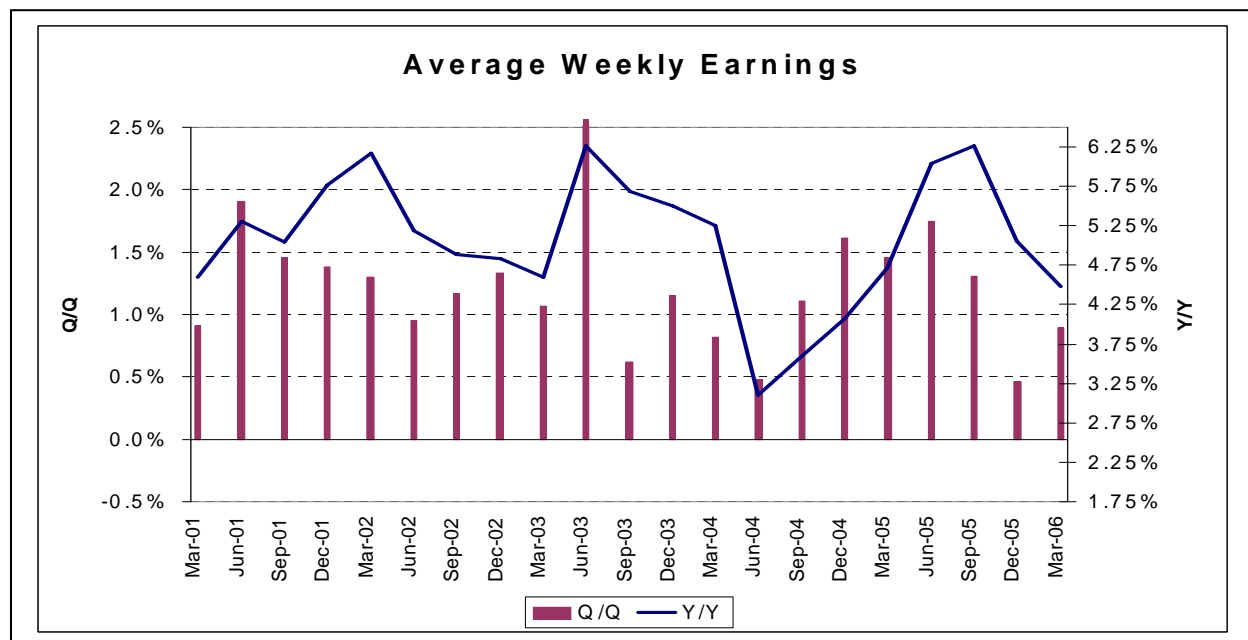
**New Car Sales** - increased 0.5% M/M and declined 4.7% Y/Y in April. (page 34)

**Consumer Confidence** – fell to a 7-month low in April. (page 34)

**Westpac Leading Economic Index** – rose 0.8% M/M and 4.7% Y/Y in March. (page 34)

## Weekly Releases & News

### Chart of the Week: Average Weekly Wages

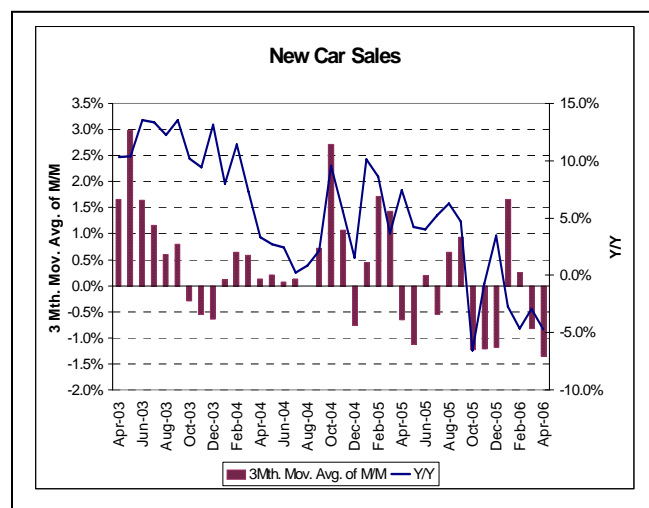


Average Weekly Wages rose 0.9% Q/Q and 4.5% Y/Y in Q1. This gain was less than Expected, spurring speculation the RBA won't increase interest rates again this year.

## New Car Sales, Skilled Vacancies & Housing Affordability

### New Car Sales

New Car Sales increased 0.5% M/M and declined 4.7% Y/Y in April.



### Westpac Consumer Confidence

The Consumer Sentiment Index fell to 104.1 in May from 110.7 in April, according to Westpac Banking Corp. and Melbourne Institute. This was the lowest reading since October last year. The weak confidence was likely partly due to high gasoline prices and higher interest rates, which both outweighed the effect of income tax cuts. A reading above 100 shows that optimists outnumber pessimists. The index gained 5.4% from a year ago.

### Housing Affordability

Australia's housing affordability dropped 0.7% in Q1 due to a continuous rising of regional property prices. In Q1, the median first-house price increased 2.1% to A\$334,000 while the typical monthly loan repayment rose 2.1% to A\$1,941. Prices rose 6.2% in regional Australia and declined 0.1% in the nation's capital cities.

### Westpac Leading Economic Index

The Leading Index, a gauge of growth for the next six to nine months, rose 0.8% in March from February. The Y/Y growth rate of the index was 4.7%, which is above its long-term trend of 3.8%.

## ***DEWR Skilled Vacancies & Comments***

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### ***DEWR Skilled Vacancies Index***

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An index measuring the number of jobs available for skilled workers in Australia rose 1.8% in May from April when it gained a revised 1.9% (previously 1.3%). Total skilled vacancies were 1.9% lower in May than a year earlier.

### ***Comments***

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#### ***Australian Treasurer Peter Costello on Commodity Prices (05/18):***

- “I believe the Chinese process of industrialization has a long way to go, so commodity prices will remain strong for some time.”
- “With the demand that is coming out of China, it means that countries like ours which can export gas, coal iron ore and base metals will do very well because the demand is such that prices are increasing.”

#### ***OECD on Australian Economy (05/23/06):***

According to OECD, the economy will grow 3.7% in 2007 on Mining. That would be the fastest pace in 5 years as primarily Chinese demand for minerals and metals has driven exports and investment.

- “The main driving force of economic activity is the global boom in minerals, of which Australia is a major producer. The recent monetary tightening should be sufficient to counter emerging inflationary pressures.”
- “Any further unexpected windfalls through 2006-07 should be allowed to accumulate in higher surpluses rather than add to demand.”
- “Exports have been held back by tight capacity, such as inadequate infrastructure and insufficient skilled labor. Companies are using profits to expand production and facilities, which should allow higher resource-based exports.”
- “That forecast may change if Chinese demand continues and commodity prices remain high. In that case, Australia's economic rebound may be ‘more vigorous’ and further monetary policy tightening may be needed.”

#### ***Australian Construction Work to Rise 9% in 2006 - Survey (05/21):***

- “Australian construction companies will increase their work by 9% this year as mining companies expand production. Chinese demand for Australian iron ore and coal has prompted mining firms to expand or open new mines. Construction work for miners is expected to increase 20% this year and 10% in 2007.
- “Shortages of skilled labor remain a key problem for the building industry, the survey found, with 80 percent of companies reporting either major or moderate difficulty in recruiting skilled labor.”

## ***Comments Cont. & Upcoming Dates***

- “There are a significant number of projects at the stage of advanced planning in energy, mining and minerals, particularly in the boom states of Queensland and Western Australia.”

### ***RBA's Recent Comments:***

- “Labor shortages may fuel wages growth and accelerate inflation.”
- “Business have been reporting that lack of suitable labor was a bigger constrain on their activities than more traditional concerns about the adequacy of demand or sales.”

### ***Key Dates This Week***

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/24	House Prices Q/Q; Y/Y(Q1)	0.0%/2.7%	2.1%/2.3%
05/29	Retail Sales (APR)	---	0.3%
05/29	Building Approvals M/M; Y/Y (APR)	---	2.2%/1.7%
05/28	Trading Balance (APR)	---	-1545mn
05/30	Construction Work Done (Q1)	---	0.1%
05/30	Private Sector Credit M/M; Y/Y (APR)	---	1.2%/14.3%

Valance Co., Inc.

# Valance Economic Report: New Zealand

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May 24, 2006

**Net migrant flow rebounded, which will not escape the RBNZ given the links between migration and the housing market. Even though OECD predicted very weak growth in New Zealand for 2006 this week, the migration data suggests that home buying and consumer spending may have remained solid enough so as to not allow the RBNZ to ease this year.**

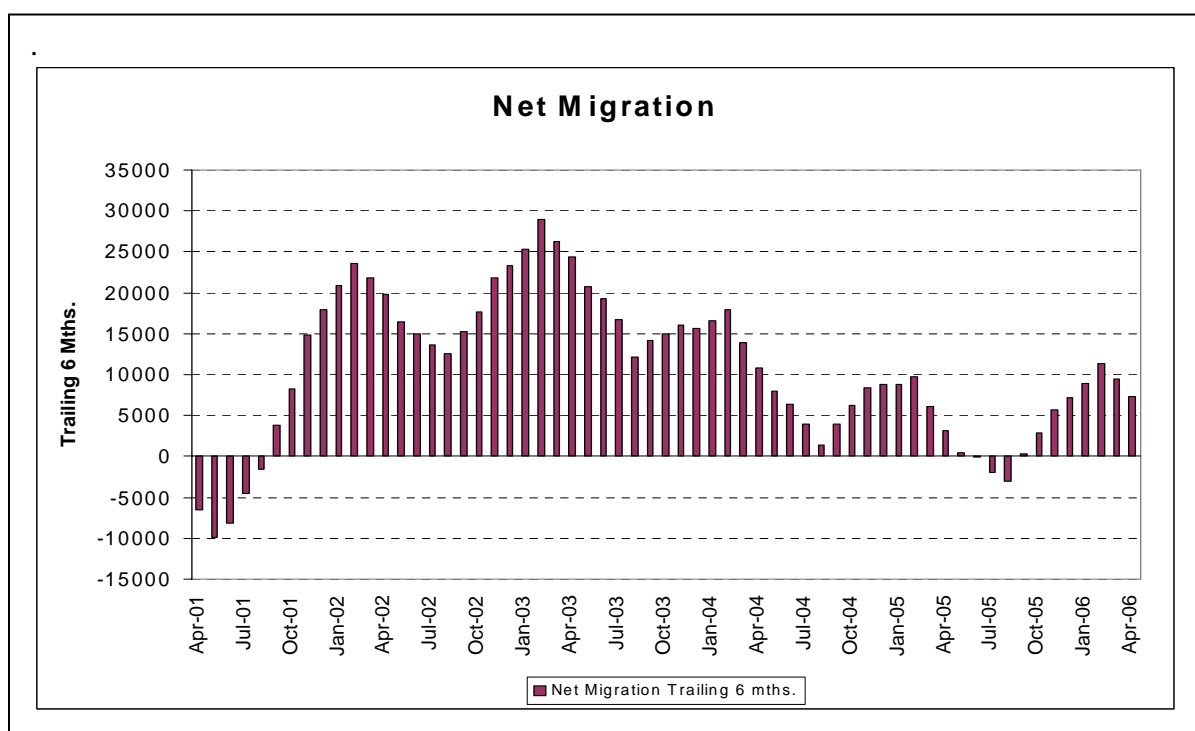
## Weekly Highlights

**Net Migration** – New Zealand gained 7.8% more permanent migrants in the year through April (page 37)

**OECD:** New Zealand Economic Growth May Be Second-Worst in 2006. (page 38)

## Weekly Releases & News

### Chart of the Week: Net Migration



Permanent arrivals exceeded departures by 970 seasonally adjusted in April. New Zealand gained 7.8% more permanent migrants in the year through April.

## Comments

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### Comments

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#### **Finance Minister Michael Cullen on Budget (05/17):**

Cullen Predicts 4 Years of N.Z. Budget Deficits to accumulate to NZ\$7.4 bln.

- “Economic growth is now slowing as part of the normal business cycle”
- “The prudence of the past means we have the flexibility to move through the cycle without having to take evasive action.”
- “Budget is moving back to providing a significant fiscal stimulus to the economy, which I estimate at 1.5% of GDP this year. That makes broad tax cuts impractical.”
- “If I were to be adding further fiscal stimulus that would inevitably see monetary policy tighten.”
- “Our government isn't obsessed with Australia and there is no point in destroying New Zealand to make it like Australia.”
- “The outlook for the deficit is slightly above my comfort range.”

#### **The RBNZ's Governor Alan Bollard on Slowing Economy (05/22):**

New Zealand's slowing economic growth could increase the risk to some borrowers as household debt rises and interest payments increase.

- “A slower-growing economy will bring challenges to some households, in particular lower and middle income households that have large debt-servicing needs. Consumers have been increasingly ready to purchase property for investments, boosting debt so that over time households have raised their financial vulnerability to interest rate changes, unemployment and swings in property capital values.”

#### **New Zealand Economic Growth May Be Second-Worst in OECD in 2006 (05/23):**

Key Points from the OECD report:

- “The economy is currently going through a sharp correction.”
- “Households consumption growth will be relatively modest. Private investment is projected to fall for several quarters.”
- “Easing too early would allow second-round effects to become embedded in inflation expectations, while easing too late could incur unnecessary losses in output and employment.”

## ***RBNZ's Stability Report & Upcoming Dates***

### ***RBNZ's Stability Report***

*The RBNZ's Governor Alan Bollard said in a statement (05/19):*

- “New Zealand's financial system is well placed to weather the slowdown in the economy. With few exceptions, financial institutions are well capitalized and profitable. Foreign exchange markets have facilitated an orderly, albeit sharp, depreciation in the New Zealand dollar.”

*Dr Bollard said the FSR highlighted a wide variation in financial exposure among households and financial institutions.*

- “Household indebtedness has reached a record high, raising households' vulnerability to higher interest rates, unemployment, and a downturn in house prices”
- “Vulnerabilities may be concentrated in those households that have recently invested in residential rental property.”

*Dr Bollard said New Zealand's banking sector was profitable, well capitalized and able to bear increases in impaired assets as economic conditions become more challenging.*

- “In this environment, credit risk management needs to be monitored closely, especially in light of the implementation of the new Basel II regime for bank capital requirements.”
- “A combination of rapid growth and comparatively young institutions, which have limited experience in managing a downturn, makes a significant part of the finance company sector particularly vulnerable to a more challenging economic environment. Isolated and individual failures among these institutions are unlikely to threaten overall financial stability, however.”

*Dr Bollard concluded that some of risks facing the financial system had crystallized since the Bank's last FSR.*

- “Other challenges have increased. Maintaining financial stability will require that risks continue to be adequately identified, priced and allocated to those best able to manage them.”

### ***Key Dates This Week***

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/24	Trade Balance (APR)	-215mln	59.1mln
05/30	Building permits M/M (APR)	---	-14.1%

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## Weekly Economic Report: *China*

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May 24, 2006

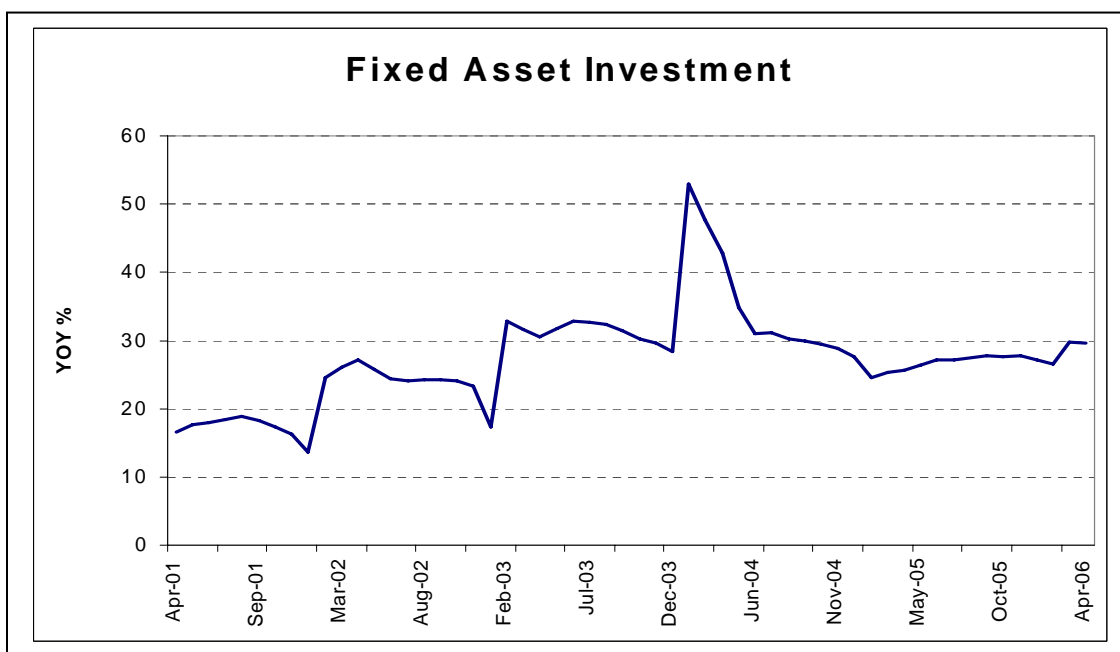
**Fixed Assets Investment, the only economic indicator released this past week, posted solid gains. Elsewhere, the OECD predicts that China's economy will grow 9.7% this year and 9.5% in 2007.**

### Weekly Highlights

### Weekly Releases & News

### Chart of the Week: *Fixed Asset Investments*

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Fixed Asset Investments increased a solid 29.6% Y/Y in April, above expectations for a reading of 29.1% Y/Y. This series is trending well above the government target for gains of 18% Y/Y in 2006, and may pressure the government to take more measures to curtail investment.



## ***News Releases***

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### **May 23<sup>rd</sup> – Excerpts from the OECD's Economic Outlook Report:**

“Greater use should be made of interest rates to stabilize demand and to reduce the reliance on non-market quantitative lending controls, and this will require freer movement of the exchange rate.”

“Rapid monetary growth coupled with lower growth of loans has led to abundant liquidity in the inter-bank market and has pushed down short term interest rates to below the inflation rate, helping reduce the pressure on the exchange rate but moving the authorities yet further from their goal of using market instruments to stabilize the economy.”

“The introduction of new risk management instruments, notably a foreign exchange futures market, suggests that preparations are underway to allow more flexibility in the exchange rate.”

The “neutral” policy environment offered by fiscal and monetary policy “should allow rapid growth of domestic demand to continue during the projection period, with investment continuing to rise relative to output, so further boosting the growth of potential output. The pace of overall growth is likely to remain rapid, with only a slight slackening as the impact of the small appreciation of the effective exchange rate is felt, resulting in only a very modest decline in the current account surplus as a share of GDP despite a further increase in nominal terms.”

Inflationary pressures should also “remain moderate” and will depend primarily on the rate at which regulated oil product prices are allowed to move up to world market levels.

The OECD predicts that China's economy will grow 9.7% this year and 9.5% in 2007.

**May 23<sup>rd</sup> – Q1's GDP Higher Than Reported** – The National Bureau of Statistics reported that China's economy grew “higher than reported” from 10.2% to 10.3% in Q1. The added growth came partly from industries such as farming, fishing, animal husbandry and forestry.

**May 21<sup>st</sup> – China To Be Biggest Economy By 2050** - According to a Price Waterhouse Cooper report, China will be the world's largest economy by 2050, surpassing the U.S., based on purchasing power. The report also indicated that, in the future, China will face a decline in its working age population – those between 16 and 50 years old.

**May 21<sup>st</sup> – PBoC To Slow Growth In Lending** - In its annual report, the PBoC announced that a combination of “monetary tools” will be utilized to reduce lending growth. Lending in the first four months of the year equaled 1.58 trln yuan – two thirds of the Central Bank's 2006 overall target of 2.5 trln yuan. BOA's Strategist, Qing Wang remarked, “Bank lending is rising too quickly and that's driving investment growth. There's too much liquidity in the financial system and that needs to be addressed.”

**May 18<sup>th</sup> – Faster Yuan Gains Shouldn't Be Allowed** - Market News International reported that an official of the National Reform and Development Commission stated that China shouldn't allow the yuan to gain faster. The official was also reported as saying that “concessions” should not be made to trading partners urging greater gains for China's currency.

## ***News Releases (Cont'd.) & Upcoming Dates***

### ***News Releases (Cont'd.)***

#### **May 18<sup>th</sup> – Director of the National Economic Research Institute, Fan Gang, Comments on Currencies, the Economy and Commodities:**

*On currencies:* “I believe the current China exchange-rate regime is the right regime. This makes China do something to pay its own duty to these global imbalances by gradual revaluation.” The “euro is a successful effort to diversify the currency system and Asia now encouraged by the success of the euro tries to think of a regional arrangement.”

*On economy:* “China's national savings ... cannot explain the \$600 billion U.S. deficits. China's wages have been growing slower than the labor productivity.”

*On commodity prices:* Our “import maybe too much so we bid up the commodity prices in the global market in the past years.”

### ***Key Dates This Week***

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/25	Industrial Profits YTD (Y/Y) – Apr	--	21.3%
05/29-31	Government Revenue / Expenditure – Apr	--	289.4B / 250.4B
05/29-31	Leading/Coincident/Lagging Indices – Apr	--	102.9 / 100.8 / 94.0
05/31	PMI Manufacturing – May	--	58.1

Valance Co., Inc.

# Valance Economic Report: Sweden

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May 24, 2006

**PPI rose a more-than-expected 0.6% and the Unemployment Rate held at 5.5% in April. The OECD released its 2006-2007 projections. Riksbank Governor, Stefan Ingves, commented that a further rate increase is “reasonable.”**

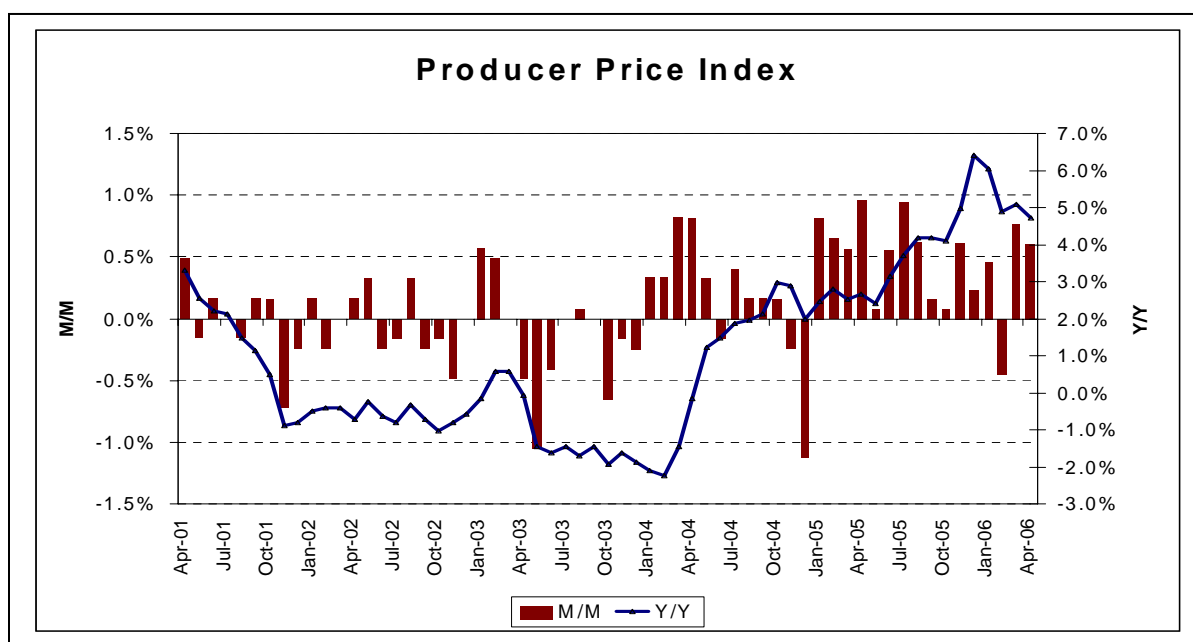
## Weekly Highlights

**PPI** - rose by 0.6% M/M and 4.7% Y/Y in April, above expectations. (page 43)

**Unemployment Rate** – was unchanged at 5.5% in April. (page 44)

## Weekly Releases & News

### Chart(s) of the Week: PPI

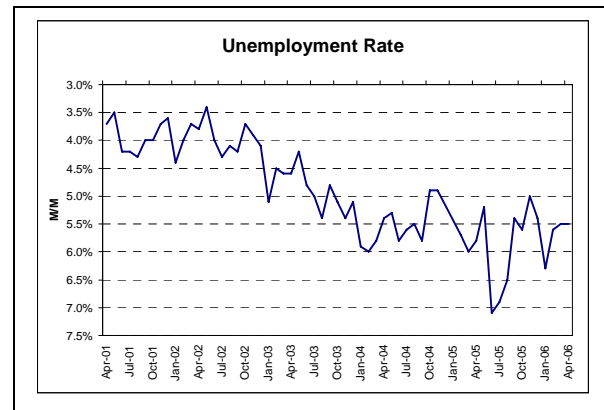


The Producer Price Index rose by 0.6% M/M and 4.7% Y/Y in April, above expectations. The M/M increase was led by higher costs for metals products.

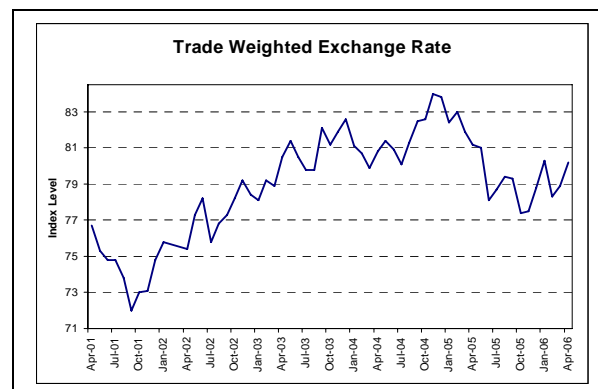
## *Unemployment Rate, Trade Weighted Exchange Rate & News Release(s)*

### *Unemployment Rate*

*The Unemployment Rate held at 5.5% from March to April. The number of unemployed individuals increased to 248K – up 2K from the month before, while the number of employed fell by 15K to 4.238 mln.*



### *Trade Weighted Exchange Rate*



### *News Release(s)*

#### May 23<sup>rd</sup> – OECD Comments on Rates and Spending:

“An expansionary monetary policy is fueling the boom in investment and is also driving increases in property prices. Over the projection period, the central bank should increase policy rates to at least neutral levels and the fiscal stimulus should be withdrawn.”

The OECD also made the following predictions:

	<b>2007</b>	<b>2006</b>
<b>GDP</b>	3.0%	3.5%
<b>CPI</b>	2.1%	n/a
<b>Gross Fixed Capital Formation</b>	n/a	5.8%
<b>Exports</b>	n/a	8.9%
<b>Unemployment</b>	4.2%	4.8%

## ***Riksbank Comments & Upcoming Dates***

### ***Riksbank Comments***

**May 23<sup>rd</sup> – Further Rate Increase ‘Reasonable’** - In a speech posted on the Riksbank’s website, Riksbank Governor, Stefan Ingves stated that, “Market expectations in recent weeks have assumed a continued gradual increase in the interest rate from early summer, which I consider to be reasonable, given the developments we have seen since February.” He added, since the February inflation report, the economy “has developed approximately in line with our assessment.” It’s likely inflation “will be above our earlier forecasts,” Ingves said citing rising oil and energy costs. He further stated, “There is considerable uncertainty regarding, for instance, the direct effects on other macro variables.”

**May 19<sup>th</sup> – Policy Expansionary, Increase In Rates Expected** - Riksbank Deputy Governor, Lars Nyberg stated in a speech on the Bank’s website that “The economic indicators and inflation prospects imply it will soon be time to take the next step towards less expansionary monetary policy. This is also in line with market expectations.” Nyberg’s comments suggest that the Bank will raise rates when they make their next announcement on June 20<sup>th</sup>.

**May 19<sup>th</sup> – Asset Prices ‘Routinely’ Used In Setting Monetary Policy** - The Riksbank stated in a report that it “routinely takes into consideration changes in asset prices and other financial variables.” The Bank also indicated that it is “guided” by the measure of underlying inflation which they feel is the best measure of price growth. “The need to draw attention to an alternative measure of inflation has, however, decreased now that the Riksbank has extended its forecast horizon from two to three years,” the Bank added.

### ***Key Dates This Week***

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/29	Consumer Confidence – May	--	17.5
05/29	Trade Balance – Apr	--	17.5B
05/29	Manufacturing Confidence s.a. – May	--	--
05/30	Retail Sales s.a. (M/M) / n.s.a. (Y/Y) – Apr	--	-0.1% / 5.1%

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# Valance Economic Report: Switzerland

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May 24, 2006

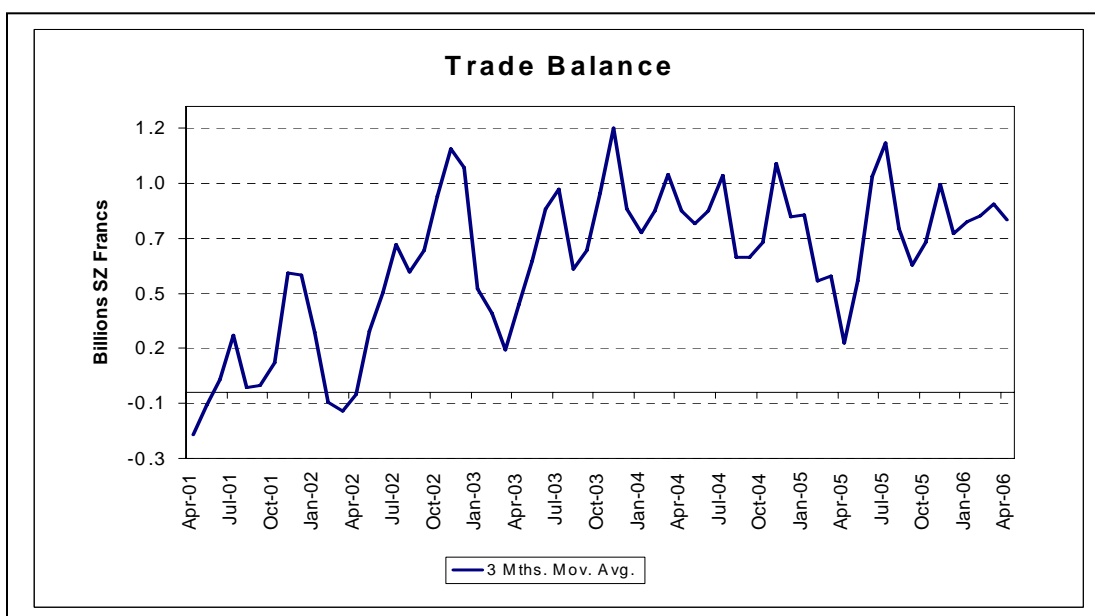
Indicators released this past week were mixed, highlighted by a widening Trade Surplus. The OECD released its May 2006 Economic Projections. SNB policy maker, Philipp Hildebrand commented on markets.

## Weekly Highlights

**Trade Balance** - widened from a surplus of 0.61 bln in March to a surplus of 0.91 bln in April. (page 46)

## Weekly Releases & News

### Chart(s) of the Week: *Trade Balance*

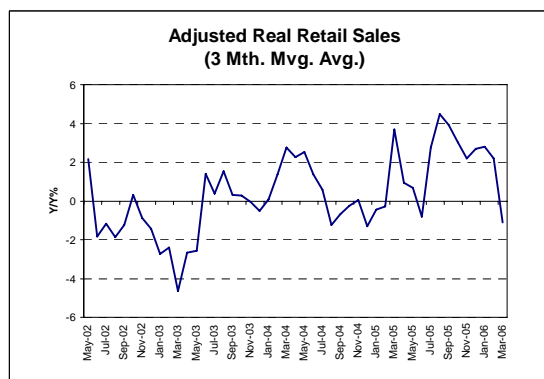


Switzerland's Trade Balance widened from a surplus of 607.8 mln in March to a surplus of 911.3 mln in April. Real exports rose by 8.6% M/M, while real imports declined 3.8% M/M.

## Adjusted Real Retail Sales, Producer and Import Prices & UBS Consumption Indicator

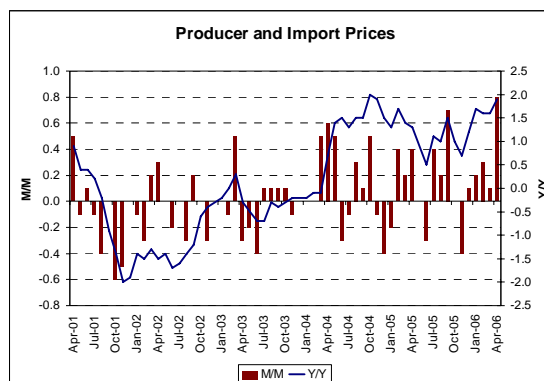
### Adjusted Real Retail Sales

Swiss Retail Sales, when adjusted for inflation, fell for the first time since May 2005 by 6.8% Y/Y, in March. The decrease was led by rising oil prices and the Easter holidays which fell in April this year. This marked the largest decline in three years.



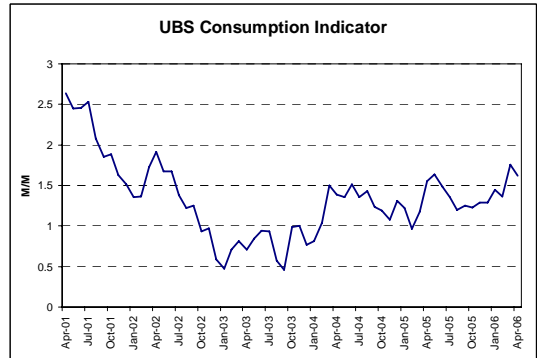
### Producer & Import Prices

Producer & Import Prices, led by rising oil and energy prices, rose 0.8% M/M and 1.9% Y/Y in April – the largest monthly increase in thirteen years.



### UBS Consumption Indicator

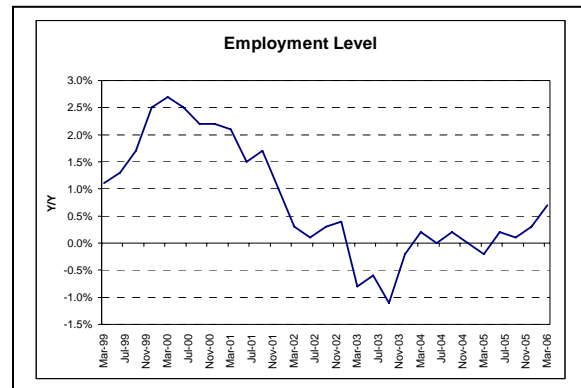
The UBS Consumption Indicator fell from a revised 1.758 in March (up from 1.743) to 1.620 in April, marking the second drop in three months. The decline occurred as shoppers cut back spending on new cars. UBS Economist, Daniel Kalt remarked, "Despite the moderate decline in the consumption indicator, UBS's economists expect private consumption to remain robust."



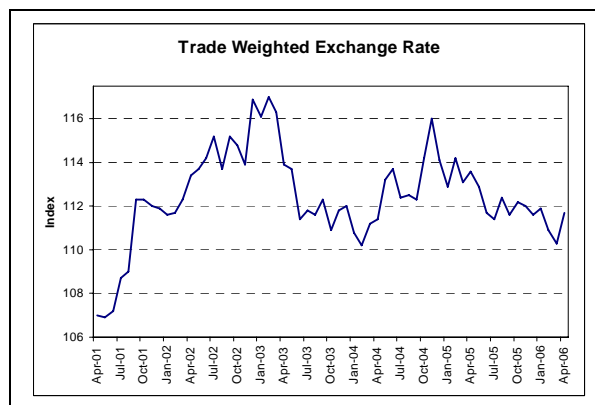
## Employment Level & Trade Weighted Exchange Rate

### Employment Level

Switzerland's Employment Level rose 0.7% Y/Y in Q1 – the largest increase in four years. Expectations were for a gain of 0.6 Y/Y.



### Trade Weighted Exchange Rate





## OECD Projections & Central Bank Comments

### OECD Projections

**May 23<sup>rd</sup> - OECD May 2006 Switzerland Economic Outlook Projections -**

	2007	2006	2005	2004	2003	2002
<b>-% changes, volume (2000 prices)</b>						
<b>Private Consumption</b>	1.6	1.8	1.6	1.4	0.8	259.3
<b>Government Consumption</b>	0.5	0.5	1.3	1.4	2.2	50.4
<b>Gross Fixed Investment</b>	3.1	4.1	3.1	3.3	-1.3	92.8
<b>Final domestic demand</b>	1.8	2.2	1.9	1.8	0.5	402.6
<b>Stockbuilding (a)</b>	0.0	0.0	0.1	-0.8	-0.1	0.5
<b>Total domestic demand</b>	1.7	2.2	2.0	1.0	0.4	403.0
<b>Exports of goods and services</b>	7.1	7.3	4.5	8.9	-0.5	188.0
<b>Imports of goods and services</b>	7.6	7.7	5.3	7.4	1.3	160.5
<b>Net exports (a)</b>	0.1	0.2	-0.1	1.0	-0.7	27.5
<b>GDP at market prices</b>	1.8	2.4	1.9	2.1	-0.3	430.5
<b>GDP deflator</b>	1.3	0.8	0.6	0.5	1.2	n/a
<b>Consumer Price Index</b>	0.8	1.1	1.2	1.0	0.6	n/a
<b>Private consumption deflator</b>	1.2	1.4	1.7	1.1	0.6	n/a
<b>Unemployment rate</b>	3.5	3.9	4.3	4.2	4.1	n/a
<b>General gov't. financial bal. (b)</b>	0.2	-0.2	-0.5	-1.1	-1.5	n/a
<b>Current account balance (b)</b>	14.2	13.3	12.5	14.0	13.4	n/a

### Central Bank Comments

**May 22<sup>nd</sup> - Swiss Central Bank's Hildebrand Comments on Markets:**

*On inflation expectations:* "Don't look at gold by itself. You want to look at the entire movement you see in commodity markets. The question of whether it's an indication of inflation expectations can be answered with a 'no'. We know inflation expectations have evolved to some extent but it's all minimal. Central bankers throughout the world are firmly committed to keeping inflation expectations anchored. If you look carefully at the relationship between some of the price movements in commodity and gold and inflation expectations there's no clear link between any significant deterioration in price expectations and the price of gold."

*On geographical changes to financial markets:* "We are likely still at the beginning of a geographic rearrangement of global capital markets. The four most important financial markets, the U.S., the euro zone, Japan and the U.K., currently account for more than 80 percent of the global financial stock. However, the financial stock of regions with currently much smaller shares like China or Eastern Europe is growing rapidly. Their average annual growth rates for the period from 1993 to 2003 amounted to 14.5 percent and 19.3 percent, respectively, compared to 8.4 percent for the global financial stock. Another indicator for the ongoing geographical shift in global financial markets is the evolution and distribution of Countries' currency reserves. In 1980, the ten largest reserve holders were all developed nations. Today, eight of the ten largest holders are Asian emerging economies. As the currency reserve numbers indicate, change in the geographic make-up of the world's financial markets is under way and may have important repercussions in terms of how the global economy functions as well as in terms of what kind of financial architecture is required to manage it."

## ***Central Bank Comments (Cont'd.)***

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*On the use of equity in housing mortgages:* “While the liquefaction of mortgages and other loans is already highly advanced in the United States, this trend is still in its infancy in continental Europe. In the years to come, I expect further innovation in this area in Europe. Augmented possibilities in the area of equity extraction in Europe's housing market presumably have the potential to boost domestic consumption and thereby contribute to global rebalancing.”

*On the resilience of financial markets to shocks:* “More flexible financial markets have likely made economies more resilient to shocks. The more flexible financial markets are, and the more risks are diversified, the more our financial markets will be able to absorb these shocks, and the less severe will be the impact of such shocks on the real side.”

*On risks posed by financial markets:* “Given the growing significance of global financial markets, the economic consequences of a major financial crisis could obviously be severe. Moreover, the dramatic efficiency gains in financial markets also mean that modern financial markets are potentially capable of transmitting a regional financial crisis rapidly throughout the global financial system. In other words, through contagion effects, modern financial markets could themselves become a potential source of systemic risk. A second concern that preoccupies many central banks is the liquidity risk associated with the fact that market participants assume that financial instruments behave in particular ways with respect to their price and liquidity dynamics. In reality, we know that our genuine understanding of the price and liquidity dynamics of increasingly complex and sophisticated financial instruments can only become more accurate through the effect of time and experience, and to the extent that we are able to monitor the behavior of these instruments under different economic and market conditions. As a result, we face the risk that fat tail events, not sufficiently captured by risk management models, could cause an unexpected drying up of market liquidity. Such sudden shortages of liquidity could have serious repercussions in a heavily securitized market where credit risk is managed on the premise that liquidity is available and securities can be traded readily. There are other risks associated with modern financial markets. They range from infrastructure and settlement risks associated with some of the new instruments to the potential links between new market participants and extreme levels of price fluctuation and market volatility. One thing many of these risks have in common is that they elicit calls for increasingly far-reaching regulation of financial markets. While some regulation may indeed be required to guarantee the integrity of financial markets, the threshold for such regulation should be set high.”

*On regulation of financial markets:* “Once we are able to agree on a clear objective for any new piece of regulation, we should consider actual regulation only if there is overwhelming evidence that market participants lack the incentives or the capability to manage adequately potential new risks associated with financial innovation. By applying this yardstick, I suspect we will find that, in many cases, new regulation will not be an adequate response to innovation in financial markets. Indeed, additional regulation will often risk stifling the kind of innovation that has proven so beneficial in recent years. Rather than seeking regulation, market participants, central banks and regulators should focus on strengthening an already active dialogue with the aim of furthering our understanding of new types of risk associated with modern financial markets.”

## *Key Dates This Week*

<i>Date</i>	<i>Indicator</i>	<i>Expectation</i>	<i>Previous</i>
05/31	KOF Swiss Leading Indicator – May	--	2.03