DAILY GLOBAL COMMENTARY

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New Home Sales – Headline Is Deceptive, Momentum Is Weak

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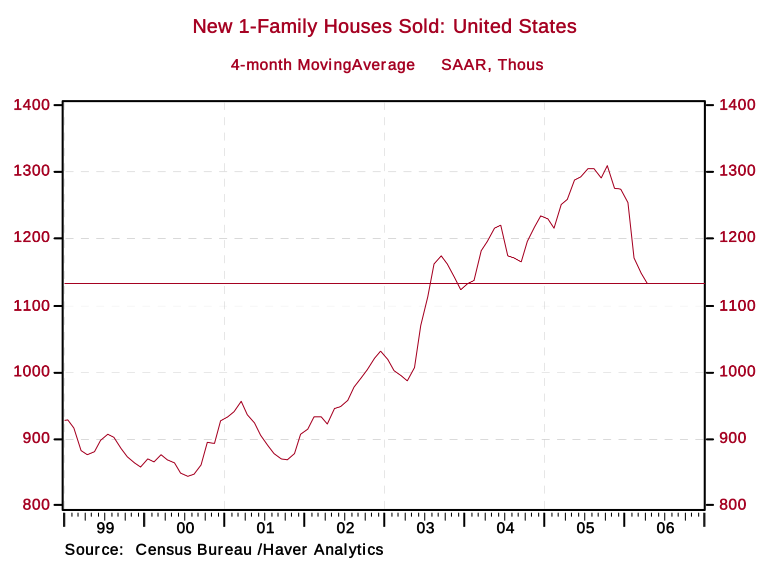
Sales of new homes rose 4.9% in April, which appears stronger than predictions. However, revisions to estimates of prior months indicate this perception is incorrect. The levels of sales of new homes in the January-March period were revised down (see table 1). As a result of this, the declines now reported for January and February are larger than the changes reported in March and the gain reported for March is slightly lower. Forecasts for sales of new homes in March were based on the original estimate of sales in March -- 1.213 million units. The level of sales in April at 1.198 million units is now lower than the original estimate reported for March. The main message is that the momentum in the market for new home is weak

Table 1 New Home Sales – April Sales and Estimates Reported in March

	Level	Change	Level	Change
	New		Old	
January	1,173	-6.83%	1,197	-5.45%
February	1,020	-13.04%	1,066	-10.94%
March	1,142	11.96%	1,213	13.79%
April	1,198	4.90%		

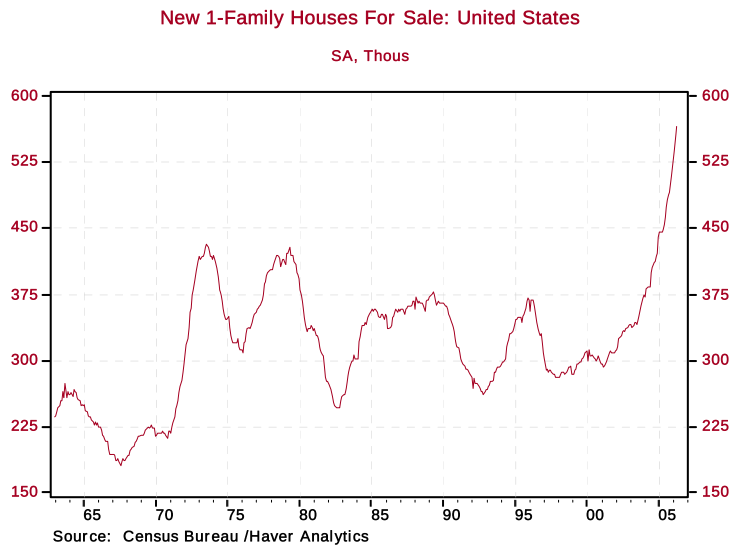
On a regional basis, sales of new homes rose in Northeast (+8.2%), South (+7.8%) and West (+2.0%) but fell in the Midwest (-1.1%). Year-to-date, sales of new homes have averaged 1.133 million units (chart 1), the lowest since December 2003.

Chart 1



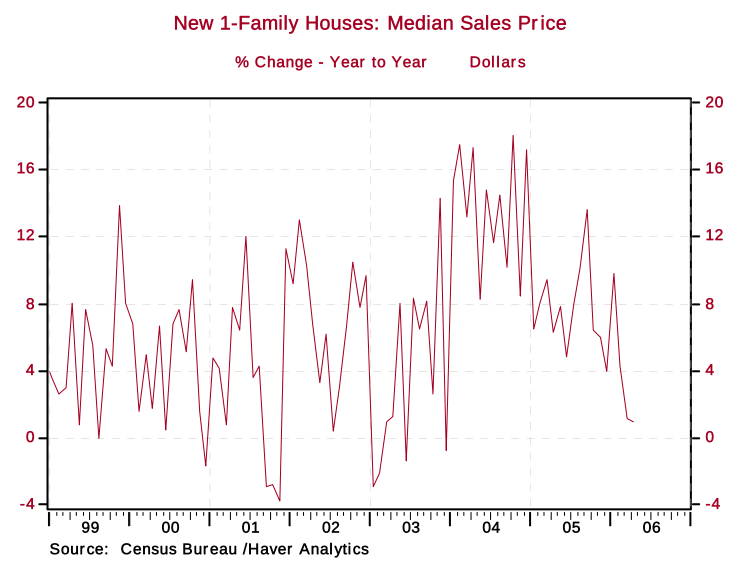
The number for homes for sale in April 2006 is the highest on record (see chart 2), with the completed homes posting a 26.2% year-to-year increase in April. There was a 5.8-month supply of unsold homes at the current sales pace up from a 4.3-month supply a year ago.

Chart 2



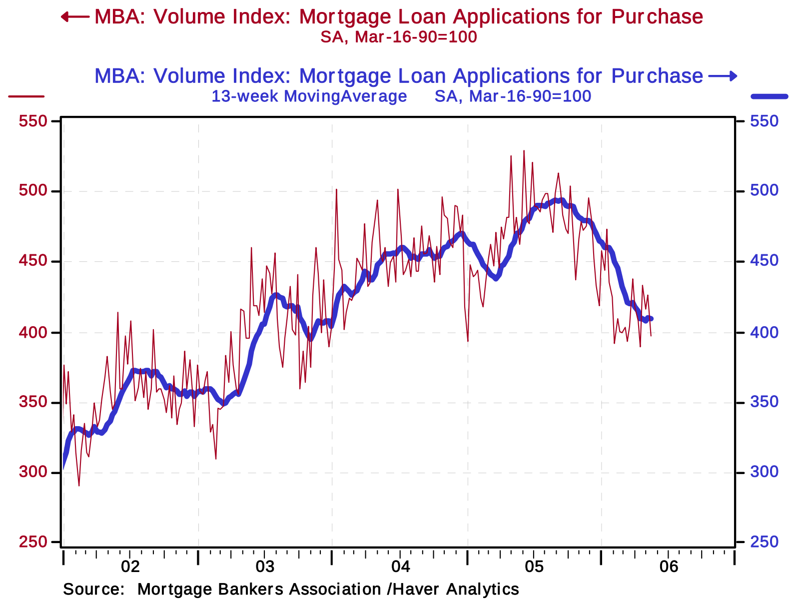
Although the headline number showed an increase in sales of new homes, the median price ($238,500) of a new single-family home moved up only 0.9% from a year ago vs. a 7.5% increase in 2005.

Chart 3



In other housing market news, the Mortgage Bankers Association's Purchase Index dropped 30.3 points to 396.4 during the week ended May 19. On a 13-week moving average basis, the recent readings of the Purchase Index are at lows comparable to early 2004.

Chart 4



Orders of Durable Goods Were Weak As Expected

Orders for durable goods dropped 5.8% in April after 6.6% jump in the prior month. As expected, orders of defense goods (-24.2%) and civilian aircraft (-32.2%) declined during April after strong gains in the prior two months. In addition to the drop in orders of these two categories, bookings of almost all other major categories of durable goods fell in April. The 3.2% increase in orders of the primary metals components probably reflects price gains.

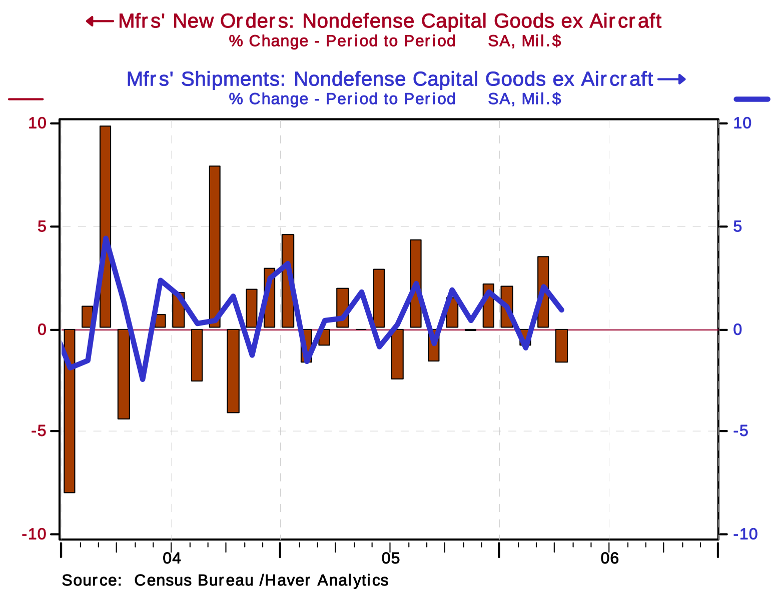
DURABLE GOODS ORDERS - % CHANGE M-M

DATE	TOTAL	DEFENSE	NON-DEFENSE CAPITAL GOODS	NON-DEFENSE CAPITAL GOODS EX-AIRCRAFT	COMPUTERS AND ELECTRONIC PRODUCTS
Oct-05	3.2	40.3	7.4	1.5	-2.1
Nov-05	4.4	-27.1	19.3	-0.2	0.7
Dec-05	0.9	-6.3	-0.6	2.1	0.9
Jan-06	-7.6	-38.6	-17.7	2.1	-1.0
Feb-06	3.6	130.7	4.7	-1.0	6.3
Mar-06	6.6	15.3	11.9	3.6	12.0
Apr-06	-4.8	-24.2	-6.0	-1.7	-10.4

Shipments of durable goods fell 0.9% after two monthly gains. Shipments of non-defense goods excluding aircraft rose 0.9% in April vs. a 2.1% increase in March. Inflation adjusted shipments of non-defense goods excluding aircraft during April suggest that equipment and software spending should add to GDP in the second quarter but a slower pace than the 16.4% increase reported for the first quarter.

DURABLE GOODS SHIPMENTS- % CHANGE M-M

DATE	TOTAL	NON-DEFENSE CAPITAL CAPITAL GOODS	NON-DEFENSE CAPITAL GOODS EX-AIRCRAFT	COMPUTERS AND ELECTRONIC PRODUCTS
Oct-05	1.5	4.9	1.9	1.7
Nov-05	0.4	2.4	0.4	0.2
Dec-05	3.2	4.7	1.9	3.4
Jan-06	-1.3	-4.6	1.1	-0.9
Feb-06	0.3	1.1	-0.9	5.1
Mar-06	0.3	1.3	2.1	-3.4
Apr-06	-0.9	-0.7	0.9	-0.5



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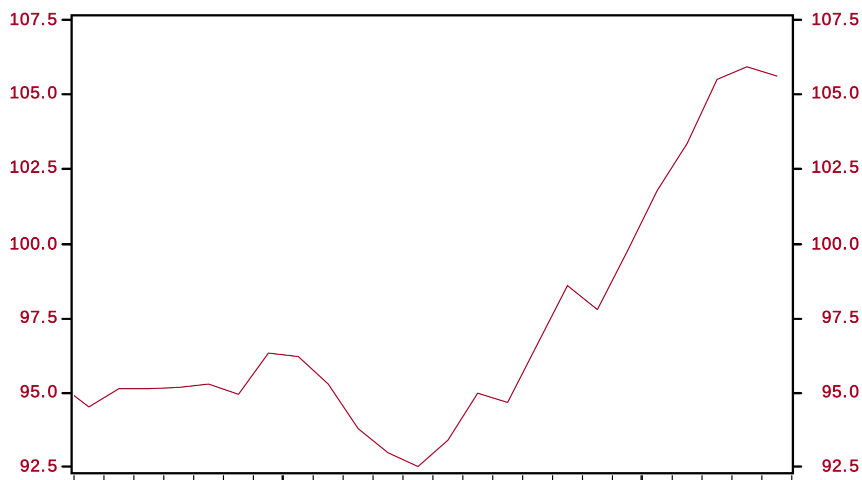
German and Belgian Data Point to Firm Euro-zone Economy in 2006; But Outlook for 2007 Uncertain

Data releases from Germany and Belgium over the past twenty-four hours once again bode well for the strength of the Euro-zone economy heading toward the second half of the year, and confirm expectations of further interest rate hikes from the ECB. Less clear, however, is the outlook for 2007.

The German Ifo business sentiment index eased only a tad from last month's 15-year peak, with the main business climate index reaching a still-high 105.6 (105.9 in April). The expectations sub-index eased back further, however, to 104.0 from 105.5 in April, suggesting expectations for six months from now are turning a little more cautious. The manufacturing component slipped from 20.7 to 19.4 but companies remained bullish about their export prospects. Neither higher oil prices nor a rising euro have dented Germany's robust export machine yet. However, sentiment in the retailing sector remained weak, with the retailing component sliding to -5.7 from -5.2 the month before.

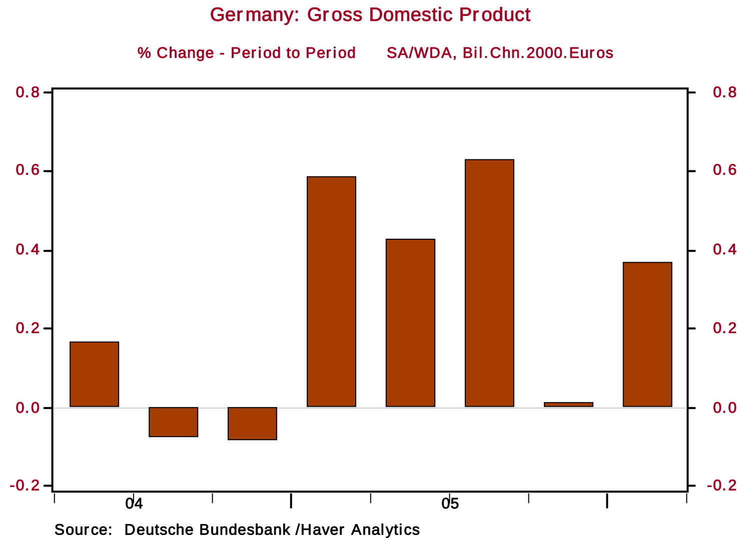
Germany: Ifo Business Climate Index: All Sectors

SA, 2000=100

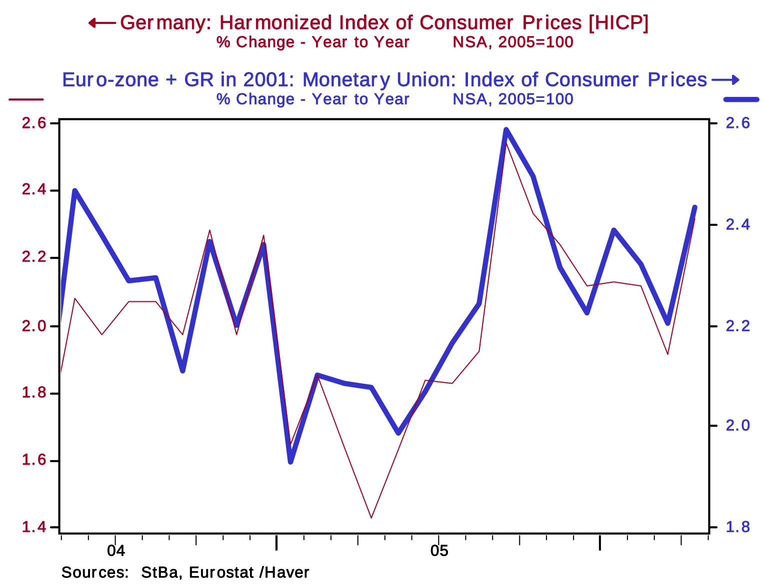


Source: ifo-Institut fr Wirtschaftsforschung /Haver Analytics

Added to yesterday's first quarter GDP data, the Ifo reinforces hopes for a solid economic recovery for Germany this year. The GDP breakdown revealed a surprisingly-strong pick up in private consumption in the first quarter, up 0.6% over Q4 2005 and contributing 0.4 percentage point to overall growth. Net foreign trade added another 0.3 percentage point, while bad weather led to a drop in construction such that Q1 GDP growth came in at 0.37% on the quarter (up from just 0.01% in Q4). With the weather and hence the construction sector improving, odds are that Q2 will see even better growth. Interestingly, French household spending rebounded in April, while Italian consumer confidence rose in May – adding to the view that the Euro-zone recovery is becoming more broad based.

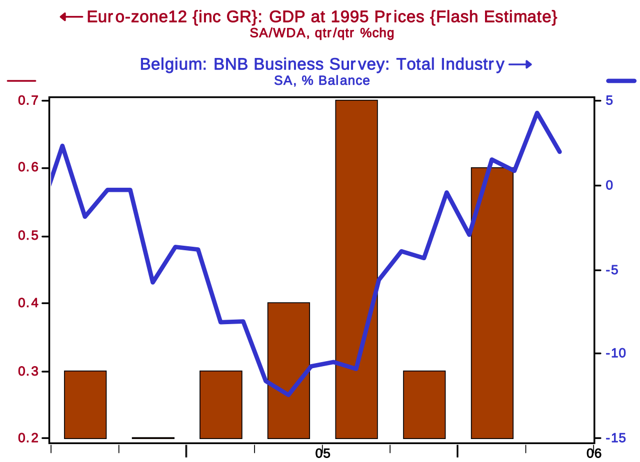


Meanwhile, there appears to be good news on the inflation front in Germany, with today's preliminary data from four of the German states showing consumer price increases between 0.1% and 0.3% on the month, suggesting an annual inflation rate for all of Germany that is lower than last month's 2.3% and some easing in Euro-zone inflation from the 2.4% seen in April.



Upcoming German data include the preliminary all-German CPI data tomorrow, the GfK consumer sentiment survey on Friday 26th, and unemployment data for May on the 31st. Euro-zone flash estimate May CPI also is due May 31.

In Belgium the business confidence index for May fell rather more than expected to 2.0 from last month's near-six-year high of 4.3. (Recall that, thanks to Belgium's strong trade ties with its neighbors, this index is a leading indicator – about six months out – for GDP growth in the Euro-zone as a whole.) The index has climbed fairly steadily since Q2 2005, and jumped into positive territory in Q1. In marked contrast with last month, the retail sub-index shot up to +0.3 (-8.2 in April) while the manufacturing sub-index slid to +1.4 (+6.4 the month before) and construction was more-or-less stable at +6.4 (versus +7.0). Within the manufacturing sub-index the component on the trend in domestic orders dropped from +8 last month to -3 and the component on the export order trend plummeted from +18 to 0. Within the retail trade sub-index, however, the component on the trend in domestic demand improved from -7 to -3, while the trend for foreign orders recovered to +1 (-11 in April). This suggests that the retail sector is becoming more upbeat, even as manufacturers start to feel the pinch of high oil prices and a stronger euro.



Sources: Eurostat, BNB /Haver

So, the German economic recovery is becoming more broad-based, but German companies are possibly starting to get a little more cautious about the outlook – not surprising, given that the planned three percentage point increase in German VAT next year could hit domestic demand. The BNB survey also points to a broadening of the Euro-zone economic recovery over the coming months, but some uncertainty about the outlook heading into 2007.

Meanwhile, it is apparent that the ECB will be hiking interest rates by another 25bp, to 2.75%, on June 8. Trichet has started using the V-word again – i.e., "vigilance" – to describe the central bank's stance regarding inflationary risks, as did the bank's May bulletin. And, with the data pointing to a broader and stronger recovery in Germany and across the Euro-zone this year, further rate hikes can be expected in the second half. This will help to underpin the euro, which has already risen more than 7% in nominal terms against the US$ since the start of the year.

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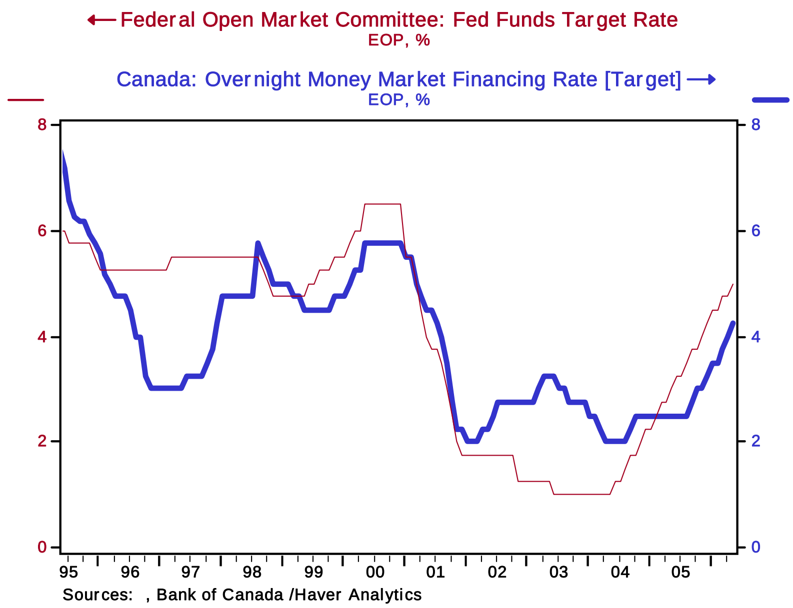
Canada: Interest Rates Have Peaked, But Manufacturer's Will Still Suffer

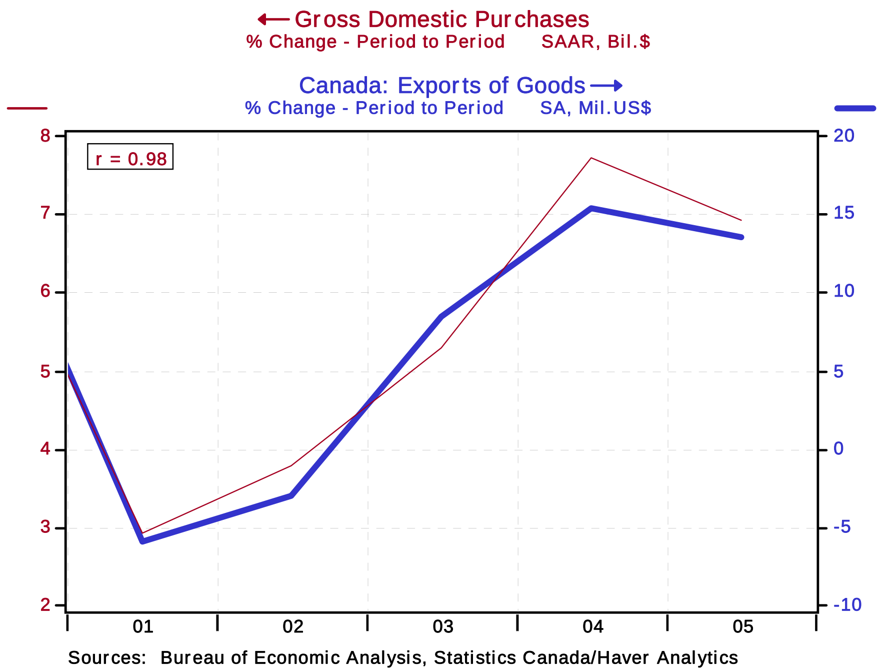
The Bank of Canada (BOC) raised its main interest rate 25bps at today's policy meeting. This was the seventh consecutive rate hike and brought the target rate for overnight loans between commercial banks to 4.25%, its highest rate since August 2001. The official statement dropped language that stated additional increases "may be required", signaling a pause in the tightening cycle heading into the summer months.



Today's announcement delivered yet another blow to Canadian manufacturing exporters, who were pushing for a pause to help stem pressures from the rising loonie and an expected slowdown in US economic growth. The Canadian dollar has appreciated 3.5% against the greenback this year and is trading over 20% stronger than its 2001 low point. The strong currency makes it difficult for Canadian manufacturers to remain competitive by driving up not only the price of export goods but also the cost of domestic labor and inputs. Manufacturers have laid off 165,000 workers over the past three years, but the employment surge in the resource-rich Western provinces has offset this decline in factory payrolls. (The national unemployment rate reached a 31-year low of 6.3% in March.)

On a national level the Canadian labor market appears strong, a fact that supports the robust outlook for domestic demand. The trade account continues to benefit from the West's abundant natural resources and inflationary pressures are kept in check both by the strength of the loonie and the biggest cumulative interest rate increase since 1997-98. This balanced-path of stable growth and inflation set the stage for the Bank of Canada's pause signal, but does little to comfort the struggling manufacturers in the central and eastern provinces.

Even if the BOC holds rates steady at 4.25% for the remainder of the year and the US Fed raises rates to 5.25%, which would imply some greenback appreciation versus the loonie, this wouldn't solve Canada's exporting woes. As Canada's largest trading partner, US domestic purchases set the pace of Canadian exports. So even if the US: CAD exchange rate improves, without a subsequent improvement in US demand, Canadian manufacturers will continue to falter.



In conclusion, global demand for Canadian commodities and a stable domestic consumer will support growth throughout the remainder of 2006, but there is little hope for a manufacturing rebound. The strong currency and past rate hikes will mitigate inflationary pressures, allowing the central bank to maintain rates at 4.25% until year-end, assuming no major global market disruptions.