RB

Brounes & Associates

2319A WORDSWORTH ▪ HOUSTON, TEXAS 77030 ▪ 713.962.9986 ▪ ron@ronbrounes.com

AND THAT'S THE QUARTER THAT WAS…
For the Quarter Ended March 31, 2007

Market Matters…

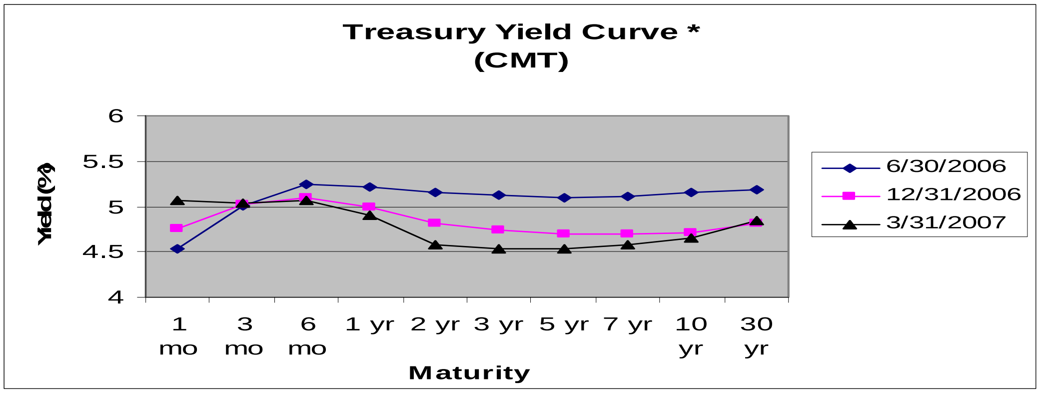
Market/Index	Year Close (2006)	1st Qtr Close (03/31/07)	Qtr Change
Dow Jones Industrial	12,463.15	**12,354.35**	**-0.87%**
NASDAQ	2,415.29	**2,421.64**	**0.26%**
S&P 500	1,418.30	**1,420.86**	**0.18%**
Russell 2000	787.66	**800.71**	**1.66%**
Fed Funds	5.25%	**5.25%**	**0 bps**
10 yr Treasury (Yield)	4.71%	**4.65%**	**-6 bps**

SUBPRIME: Heading into the year, most investors had barely heard of subprime loans (unless they had poor credit). Today, hardly a day passes without another defunct lender moving toward bankruptcy, more "misled" borrowers crying foul, panicked investors unloading mortgage-related stocks, and tough talking regulators and politicos threatening harsh actions. With companies like ***New Century***, ***Novastar***, ***Fremont***, and ***Accredited*** becoming household names (and that's not a good thing for them), the subprime fiasco undoubtedly contributed to negativity in the overall markets, while hindering any potential rebound in housing. Stay tuned…this one may not be ending any time soon. **HOUSING:** On a related note, many analysts expected the housing sector to pull itself out of its recent doldrums. After all, several top homebuilders watched their market values plunge by over 40% during the past two years. In recent weeks, however, ***Toll Brothers***, ***KB Homes***, and ***Lennar*** each reported a decline in profits of over 65%, while ***Beazer Homes*** is facing new shareholder lawsuits. As for the future of the industry, perhaps Tom Tomlitz, the ***DR Horton*** CEO, said it best…"*2007 is going to suck.*"

OIL: Volatility was the name of the game in the energy sector this quarter, as the unseasonably warm winter contributed to an early pullback in oil prices from the elevated highs of last summer. In January, prices briefly moved below $50/barrel and economists began reducing their expectations for inflation. Enter Iran (again). In February, the UN Security Council expressed concerns about its uranium enrichment program. A month later, the detainment of British soldiers by Iranian officials threatened an international incident (that even lead to rumors about Iran's firing on a US vessel). By quarter-end, prices has surged back into the mid-$60's, gasoline was averaging over $2.60/gallon, and those inflationary concerns were back in full force. **TRANSACTIONS**: Despite the housing and energy concerns, business execs seemed confident about the current investment climate. ***KKR*** continued its buying spree (***Dollar General*** for $6.8 billion), ***Blackstone*** announced plans for an $4 billion IPO to fund future acquisitions, and ***ABM Amro*** and ***Barclays*** announced merger plans to form a global financial superpower.

MARKETS: Equities began the year on a strong note with global markets (particularly in Asia) reaching record levels. The major domestic indexes roared into February with the Dow Jones and Russell 2000 (small-cap) hitting new highs and the S&P 500 reaching its best level in six years. Suddenly…the Shanghai Composite plummeted by nine percent one day in late February and the rest of the world followed suit. The Dow experienced its worst performing day (down 416 points) since the aftermath of 9-11 and the general bearish tone remains today. Subprime and oil woes certainly have not helped. All in all, the major indexes (including fixed income) ended the quarter at levels not that far off from where they began, though the mood seems vastly different today. Steel and mining companies were among the top sector performers (with ***Alcoa*** leading Dow stocks), while builders and mortgage lenders lagged (no surprise). Bonds benefited from a "flight-to-quality," though inflation talk (and an occasional ill-timed comment by Bernanke) ruined the optimism about a near-term rate cut. And can someone please shut up Mr. Greenspan?

Economically Speaking…



**** Reflects changes in interest rates over various time frames.***

FEDSPEAK: "…*invariably forces build up for the next recession, and indeed we are beginning to see that sign*…" (Isn't it time for Alan Greenspan to find a new hobby.) The talking heads were out again this past quarter with the former Fed Chair attempting to stay in the limelight. While very few economists had been uttering the dreaded R-word in quite some time, Greenspan reopened the debate and prompted other current Fed officials to refute his comments. (Thanks Mr. Poole.) Even Treasury Secretary Paulson joined the act by announcing that the domestic economy remains "*quite healthy*" despite the challenges in housing. Just when Bernanke thought he had nipped the recessionary concerns in the bud, he reopened the I-word discussion with his "*recent readings (of core inflation) remain uncomfortably high*" quote. The Fed left interest rates unchanged (at 5.25%) for the sixth straight time and even removed the "*additional firming may be needed*" line from the recent policy statement. While most economists expect the next move in rates to be lower, the jury is still out about the exact timing of such an action.

HOUSING: Those eternal optimists expecting a rebound in housing may have to wait just a bit longer (like maybe another few years). In January, new home sales experienced its sharpest decline in 13 years and then fell another 3.9% in February. Building permits, long considered a leading predictor of future construction activity, dropped to its lowest level in nine years. In fact, within the unemployment data, 62,000 construction jobs were eliminated in February. **LABOR:** The job market continued to be the saving grace for the economy; the unemployment rate fell to 4.5% in February. Bear in mind, a strong labor sector contributes to enhanced retail activity and other consumer-driven markets. The downside to (near) full employment is the pressure it places on wages. This year, Congress passed its first minimum wage increase in 10-years so buyers beware as employers attempt to pass along their higher compensation costs to consumers.

INFLATION: Bernanke's concerning comments may turn out to be somewhat prophetic as some recent pricing trends could mean additional inflationary pressures. On the wholesale level, food costs skyrocketed in February and experienced their largest monthly gains since October 2003. Energy prices soared as well and seem primed to continue; as such, gasoline costs may be on the rise at the most inopportune time (the upcoming vacation season). On the retail front, winter freezes in certain agricultural regions have affected seasonal citrus crops which will translate into higher prices at the grocery store. As for the higher wages…(see above). **OVERALL:** The economy as measured by GDP grew by 2.5% in the 4th quarter and by 3.3% for all of 2006. While hardly recessionary numbers, many economists expect a slowdown in the quarters to come as a sluggish housing market and rising oil prices ultimately impact other sectors of the economy as well. **TRADE:** Oh, and the US trade deficit set a record for the fifth straight year. By the way, does anyone have an opening in their golf foursome for Greenspan?