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February 7, 2008

**MFR's U.S. Economic Forecast 3rd Most Accurate  
in 2007 Wall Street Journal Survey**

We are pleased to announce that our economic forecast was judged to be the third most accurate out of 60 participants in the Wall Street Journal's 2007 survey process.

The text from the article in the February 7, 2008 issue of The Wall Street Journal is appended below:

**By JUSTIN LAHART**

**February 7, 2008**

With its twists and turns, the economy last year was tough to predict. Lehman Brothers economist Ethan Harris came closest to the mark, taking top honors in The Wall Street Journal's economic-forecasting rankings.

While most economists expected the economy to shake off the housing slump and gain strength through 2007, Mr. Harris thought housing would continue to weigh on the economy. Despite sluggish growth, he predicted that price gains would accelerate through the year. That inflation forecast set him apart from the other 59 participants in the forecasting survey.

**FEBRUARY SURVEY: LEADERS OF THE PACK**

*Here are the top five economists:*

1. Ethan Harris -- Lehman Brothers
2. Dean Maki -- Barclays Capital
3. Maria Fiorini Ramirez / Joshua Shapiro -- MFR Inc.
4. Robert McGee --U.S. Trust Bank of America Private Wealth Management
5. Neal Soss -- Credit Suisse

Mr. Harris, who was at the Federal Reserve Bank of New York before joining Lehman Brothers in 1996, says that heading into 2007, he consciously tried to avoid a "sun-will-come-out-tomorrow forecast." Even so, he didn't foresee how sharply the economy would slow at the end of the year. And his projection that an inflation-fighting Federal Reserve would leave the target for its benchmark federal-funds rate, at which banks loan each



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other money overnight, at 5.25% through the end of the year was a full percentage point too high.

Barclays Capital economist Dean Maki, saw the economy losing steam in a way that Mr. Harris didn't, and saw inflation running nearly as hot, but his expectation that the federal-funds rate would hit 6% knocked him down to the No. 2 spot.

Rounding out the top five spots were Maria Fiorini Ramirez & Joshua Shapiro, of MFR Inc.; Robert McGee, of U.S. Trust, Bank of America Private Wealth Management; and Neal Soss of Credit Suisse. Mr. McGee took the top honors in the previous two rankings.

Forecasters were ranked on four criteria -- their estimates of quarterly gross-domestic-product growth for 2007, their inflation and unemployment estimates for November 2007 and their year-end forecast for the federal-funds rate. They submitted those estimates to The Wall Street Journal in December 2006.

The methodology for the latest rankings, which The Wall Street Journal is using for the first time, was created by Federal Reserve Bank of Atlanta economists Robert Eisenbeis, Daniel Waggoner and Tao Zha and spelled out in a 2002 paper. Unlike the approach used in previous rankings, it compensates for distortions that arise when the numbers get smaller. It also makes adjustments for the difficulty of forecasting more volatile measures, such as GDP, and the tendency of some measures, such as inflation and interest rates, to move in sync.

In the paper, the Atlanta Fed economists noted that forecasters' accuracy was lowest at "turning points," such as when the economy was heading into the 1990 and 2001 recessions and during the economy's "soft landing" in 1995, when it slowed markedly but avoided recession. One sign that the economy now is at a turning point: Mr. Harris's score was just 41 out of a possible 100. The average score was just 18.

The economist with the lowest score was also the most bearish: James Smith, chief economist for Parsec Financial Management. Mr. Smith thought that when the yield on 10-year Treasury note dipped below the yield on the three-month Treasury bill in July 2006, and stayed below it -- a phenomenon that always augured for a recession in the past, he says -- it meant a downturn was coming. As a result, he forecast that the economy would contract in the second and third quarters of 2007, when it was actually at its strongest. And he thought that the slump would cause a collapse in oil prices, leading to a substantial cooling of inflation.

What happened to Treasury yields "either had an unusually long lead time as an indicator, or things are different this time," says Mr. Smith. He reckons it is the latter, and that the economy will skirt recession this year.

For his part, Lehman Brothers' Mr. Harris puts the odds of a recession this year at 40%, below economists' average forecast of 49%. The Fed's rate cuts, coupled with an



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economic-stimulus package that is making its way through Congress should help keep the economy afloat, he says. But growth will be sluggish this year and next.

"The big problem in the economy right now is that you have way too much inventory of homes for sale, and that will continue into 2009," he says. "It's hard to imagine the consumer picking up in that kind of environment."

That will leave the economy vulnerable to recession for some time, he thinks. It should also help cool inflation, but perhaps not as much as past experiences suggest, as demand from China and other rapidly developing economies keep commodity prices from falling sharply.