

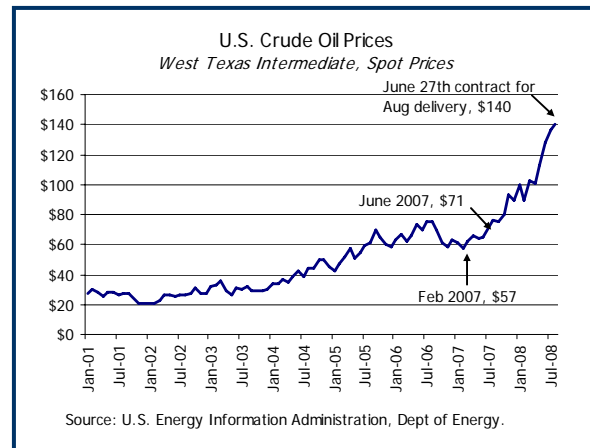
Economic News Briefing

July 3, 2008

- In this issue:** The recent steep rise in crude oil prices worries economic policymakers in U.S. and across the world.
- Local consumer prices have risen nearly 5% compared to last year and the rate of inflation has accelerated in the last few months.
 - U.S. inflation accelerates in May compelling Federal Reserve Bank to halt cuts in interest rates.
 - Local job losses continue for a fifth consecutive month and the number of unemployed rose to 57,200 (16,700 more than in May 2007) even as the unemployment rate held steady at 4.7%

Rise in Crude Oil Prices Affecting U.S. Economy and Raising Global Concerns

The price of a barrel of crude oil for Aug delivery hit over \$140 on the New York Mercantile Exchange at the end of June. The price of oil has risen by over 90 percent over the past 12 months and by nearly 145 percent since its prior low just a year and a half ago.¹ The current rising trend in oil prices began in 2004, as U.S. and global economic growth began to accelerate, although oil prices retreated somewhat in the latter half of 2006. The positive trend in crude oil prices regained its momentum in February of last year. Oil prices, however, have jumped 40 percent since April 1, 2008.

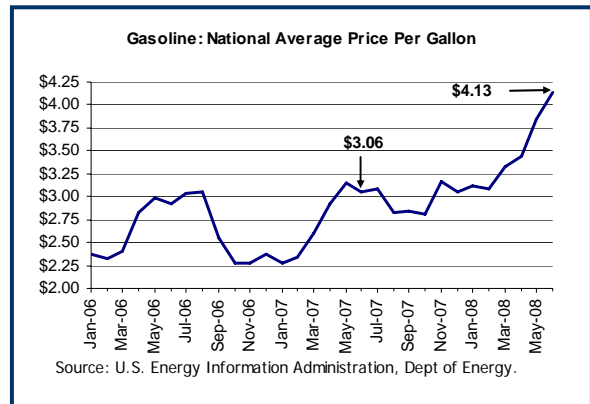


The rising trend in oil prices is fundamentally the result of increasing demand outpacing the rise in supply. This imbalance has continued even as economic growth in the U.S. and other industrial nations has begun to slow. U.S. consumption of petroleum declined by 2.5 percent from 2004 to 2007, and declined by 1.1 percent in the first quarter of this year compared to the first quarter of 2007. European demand for crude oil declined by 2.4 percent in 2007, and remained unchanged in the first quarter of 2008. Global demand for oil, however, rose by 1.3 percent in 2007 and is expected to rise by 1.2 percent in 2008.² The recent increase in global demand has been led by consumption in rapidly developing economies, particularly China and India, but oil consumption by Middle Eastern oil producing countries has also grown rapidly.

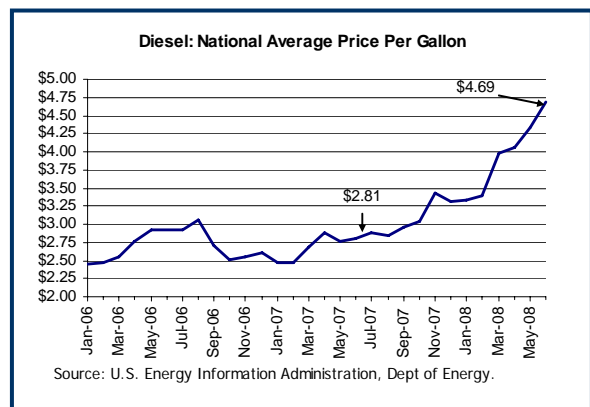
¹ The average price of barrel of West Texas Intermediate grade petroleum sold for \$57.35 in early February of 2007.

² Projections according to Organization for Economic Cooperation and Development (OECD), International Energy Agency – a multilateral international organization.

While oil consumption in the industrialized nations as a group declined by nearly one percent between 2004 and 2007, oil consumption in emerging market and less developed economies grew by nearly 11 percent over that same period.³ China's and India's consumption of oil rose by 20 percent and 12 percent, respectively, over the past three years. These two countries alone have accounted for roughly 38 percent of the global increase in oil consumption over the last five years and China has been the world's second largest consumer of oil behind the U.S. since 2003. The rapid economic growth experienced by both China and India are the principal factors behind the large increases in oil consumption in both nations, but the practice of subsidizing the price of gasoline and other forms of energy have been an important contributing factor to this growth as well. In fact, the practice of subsidizing energy costs is widespread in the developing world and also among Middle Eastern oil producing countries.⁴ The International Energy Agency (IEA) predicts that oil consumption in the developing world will account for 90 percent of the total growth in world energy consumption over the next five years, despite recent reductions in fuel subsidies by China and India and likely reductions in fuel subsidies in other non-oil producing developing countries.



The recent increase in oil prices has, of course, been leading to sharp increases in the prices of gasoline, diesel and aviation fuels, increasing the cost of transportation and thereby increasing the cost of production in general.⁵ Gasoline prices in the U.S. typically rise during the summer months when driving usually increases, refiners reduce production to perform routine maintenance and refining adjustments are made in response to summer temperatures. Gasoline prices generally come down when summer ends, but prices deviated from the general pattern in the fall of 2007. Gasoline prices began the current upward trend in November 2007 rather than returning to pre-summer levels, and currently stand about 35 percent higher than in May 2007. Gasoline prices have almost doubled in the span of three years.



³ These statistics are from Energy Information Administration, Office of Energy Markets and End Use, International Energy Statistics Team.

⁴ Oil consumption among Middle Eastern oil producers grew by 27% between 2001 and 2006, and accounted for 17% of the growth in world oil demand between 2001 and 2006. High income countries from North America and Europe accounted for 19% of the growth in world oil consumption during that period.

⁵ Rising crude oil prices also directly affect important petroleum-based products, such as fertilizer, that directly affects the cost of producing agricultural commodities.

The price of diesel fuel has risen even faster than the price of gasoline, squeezing profit margins in the transportation sector not only in the U.S., but also in the major industrialized countries. Diesel fuel has risen 67 percent over the course of the past year, and by 106 percent in three years.

The trend of rising oil prices are expected to continue for the next five years according to the latest IEA forecast. Slower economic growth in industrial countries over the balance of this year and into 2009, anticipated investments in oil production capacity and price induced reductions in oil consumption will moderate future increases in oil prices, but these factors are not likely to be sufficient to reverse the positive trend in crude oil and oil derivative fuels. The president of OPEC recently predicted that crude oil prices will reach between \$150 and \$170 per barrel by the end of 2008 and the market has closed in on the bottom of that range within the last two weeks. Heightened uncertainties regarding intermittent supply disruptions due to political and social unrest in oil producing regions, moreover, should also maintain the high level of volatility in oil prices.

As oil prices rise, so does the price of energy in general. The cascading influence of the higher prices for transportation (and the cost of energy in general) is having an adverse impact on the overall rate of price inflation. This is occurring not just in the U.S., but also in most other economies in the world. The United Kingdom and the other major economies of Europe have recently experienced a significant acceleration in price inflation. Inflation in the European Union countries, as a group, was 3.9% in May (relative to May 2007), reaching a rate not seen in 16 years. The European Central Bank (ECB) has made clear that it considers inflation the greatest threat to European economies and showed an unwillingness to cut interest rates even in the face of a slowing economic growth, a broad credit squeeze and the negative trade impacts from an appreciating currency. The ECB's concern that Europe's economy (and actually the world economy) is close to the edge of an inflationary wage-price spiral led it to raise short term interest rates on July 3rd from 4.0% to 4.25%. The Bank's action indicates the seriousness of their concern since this move is very likely to strengthen the euro, hurt European exports and diminish the global competitiveness of its import competing industries.

The U.S. Federal Reserve Bank officials have shown signs that they too are concerned with inflationary pressure. The Fed recently halted its reductions in short term interest rates even as employment has declined for six consecutive months, unemployment has risen significantly, and residential construction and housing sector are weak and show signs of weakening further. The Fed is clearly looking for signals that would indicate a need to shift its focus to combating inflation rather than stimulating growth.

Local Consumer Prices Rise by 4.9% from April 2007 to April 2008

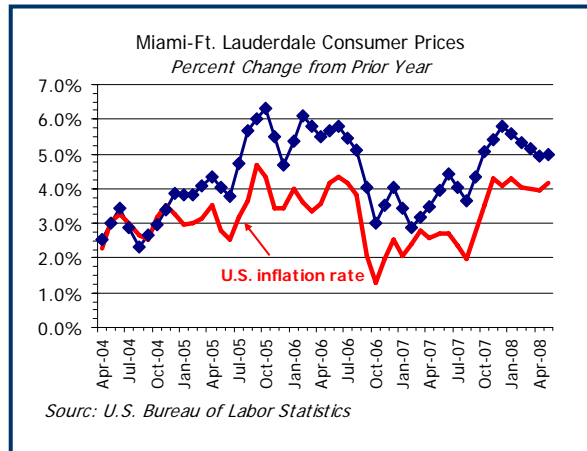
The latest U.S. Bureau of Labor Statistics estimates of the consumer price index show that prices in the Miami–Fort Lauderdale metro region increased by nearly 5 percent over the last year.⁶ The increase in local prices has likely been outpacing the increase in average wages and thereby eroding the purchasing power of labor income since at least the summer of 2005.⁷ The rate of inflation once again accelerated above the 3 to 4 percent per year range in August of last year. Local consumer price inflation since

⁶ The Miami–Fort Lauderdale metro region is comprised of the Miami-Dade, Broward and Palm Beach tri-county area.

⁷ Official estimates of average wages and salaries are not yet available for the period after September 2007.

October of 2007 has been in the 5 to 6 percent per year range. An inflation rate of 5 percent (year-over-year) was likely registered in May, according to past correlations between local and national inflation rates.

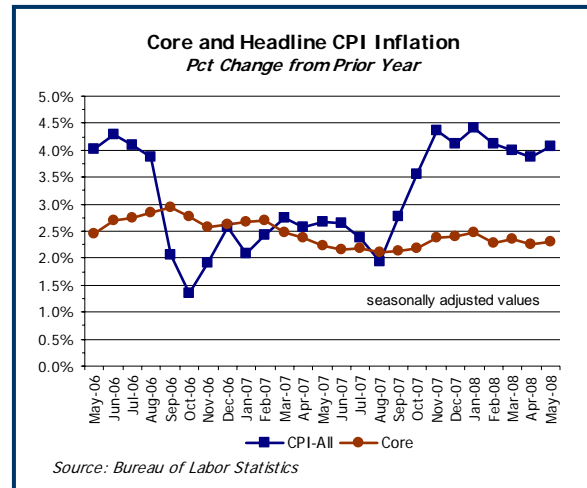
The most recent increase in the local average price of consumer goods has been led by the rising trend in energy and food prices. Over the past twelve months, energy prices paid by consumers have risen by 15 percent. Prices in May for motor fuel alone were nearly 25 percent higher a year earlier and prices for food and beverage have risen 5.4 percent over the past 12 months.



The rate of inflation in the tri-county area began to rise above the national rate of inflation in November of 2004. The local rate of price inflation, however, should begin to track national inflation rates more closely going forward. The significant gap between local and national inflation rates was the result of the comparatively rapid increase in housing costs.⁸ Local increases in the prices consumers pay for housing, however, are no longer significantly above those rates of increase observed at the national level and not expected to be above those rates anytime soon. This suggests a moderation in the local rate of consumer price inflation for the balance of this year and into 2009 as it begins to more closely track national inflation rates.

Fed Halts Decline in Short Term Interest Rates Over Inflation Worries

Prices for consumer goods at the national level increased in May by 0.65 percent, or at an equivalent annual rate of 8 percent, and continued along a trend that began last summer. The rate of inflation in consumer prices as a whole (“headline inflation”) began to accelerate in August of 2007, and since November of 2007 the annual rate of price inflation has been approximately 4 percent per year. The acceleration in consumer price inflation coincides with the rapid increase in the prices paid for energy and, to a lesser extent, food, since both of these commodities are significant components of the overall consumer price index.



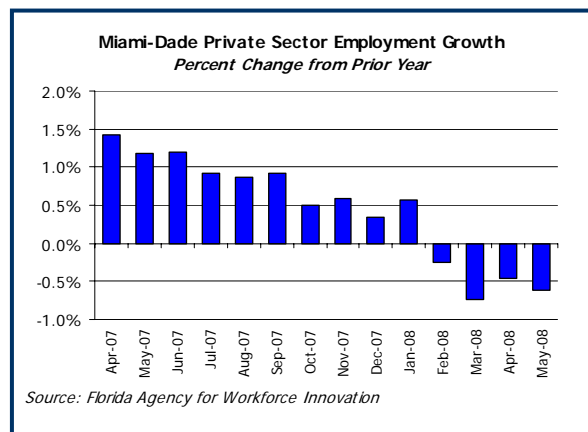
Since the late 1990’s the Federal Reserve Bank (whose mission is maintaining price stability and full

⁸ Housing costs in the Consumer Price Index are measured primarily by rents and the implicit rent of owner-occupied dwellings. Housing costs in the CPI are not directly related to interest rates or the sales price of new or existing homes.

employment) has suggested that inflation in the “range” of 2 percent per year is “optimal.” For policy purposes, however, the Fed focuses its attention on inflation in consumer prices other than food and energy (“core inflation”) to avoid reacting to temporary swings in these volatile commodity prices. The Fed has historically raised interest rates when core inflation is rising near 2 percent and the economy is clearly growing with signs of increasing labor scarcity. While core inflation has hovered around 2.5 percent, economic growth is essentially flat, the economy continues to shed jobs and unemployment is rising. There has yet been any sign that higher inflation is leading to rising wages and labor costs. Foreign central banks, however, are strongly encouraging the Fed to enlist in a campaign to curb rising world inflation. For now, the Fed appears ready to wait for signs of an upward trend in U.S. core inflation and greater confidence that the economy can avoid a general recession before raising interest rates and reducing credit availability. The Fed may become more sensitive to the risks of a global inflation/wage spiral after October, even without an acceleration in U.S. core inflation.

Latest Employment Data Shows Continued Job Losses in Miami-Dade County

Employment data for May shows that Miami-Dade County lost approximately 2,800 from May of 2007, but the job losses in private sector employment over the same period is about 5,600. May marked the third consecutive monthly decline in total jobs on a year-over-year basis, and the fourth consecutive decline in private sector jobs. Local employment levels usually decline between December and May. The decline in total employment from December to May was 5,600 last year, but the drop in employment between December and May this year has been 16,000. The decline in private sector employment in the first five months of 2008 was 16,200 compared with 7,400 in the first five months of 2007.



The local labor market is clearly under stress, but not all industries lost jobs May compared to May 2007. The greatest declines in employment were observed in construction (-8,100), professional and technical business services (-5,100), retail sales (-2,800), and manufacturing (-1,800). The industries with the biggest employment gains compared to last May were healthcare and private education (+7,200), federal, state and local government (+2,800), leisure and hospitality (+2,200) and wholesale trade (+1,600).

The unemployment rate in Miami-Dade held steady in May compared to April at 4.7 percent, but still significantly higher than the 3.9 percent rate seen in March, and the 3.4 percent rate in May of 2007. The number of unemployed in Miami-Dade reached 57,200 compared to 40,500 in May of last year.

Robert D. Cruz, PhD
 Economic Policy Coordinator and Chief Economist
cruzr1@miamidade.gov
 (305) 375-1879