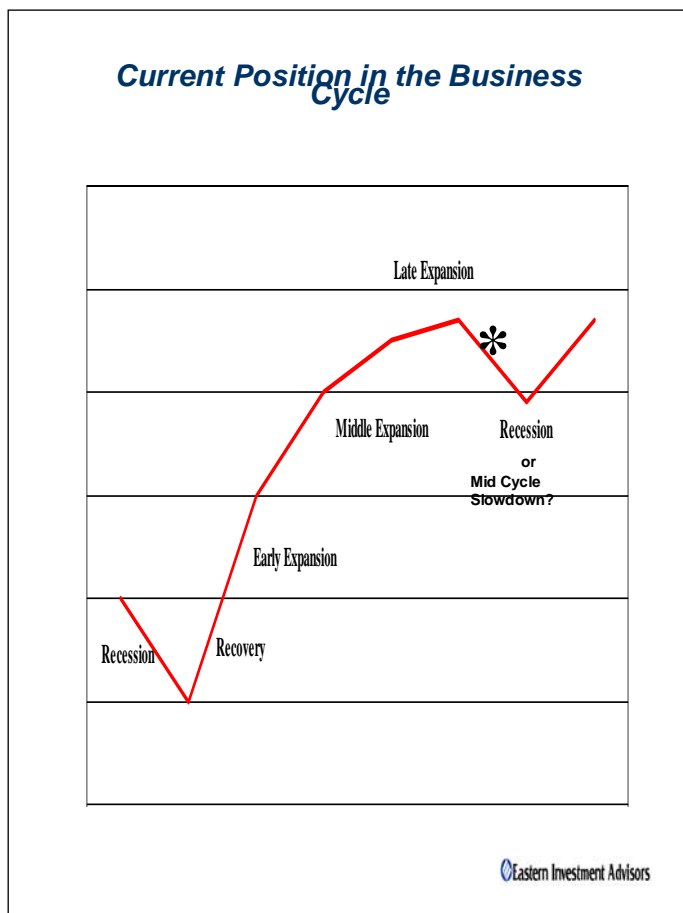


# Eastern Mortgage Capital

April, 2007 - Eastern Mortgage Capital's parent puts out distinguished research on economic and interest rate trends through our Chief Economist.

## The Economy:

2006 was a year of economic deceleration. After beginning the year at a 5.6% real rate of growth, the economy slowed to 2.2% in the fourth quarter. The real growth rate of the GDP in 2006 was 3.3% vs. 3.2% the previous year. The primary reason for the slower rate of economic growth was the sharp decline in the residential real estate market. Also, the Federal Reserve Bank increased short-term interest rates 100 basis points during the first six months of the year. The industrial slowdown was confined primarily to the automobile and residential construction industries. Therefore, most areas of the economy experienced strong growth and good earnings gains. As a result, stocks returned 16% as measured by the Standard and Poor's 500 Index.

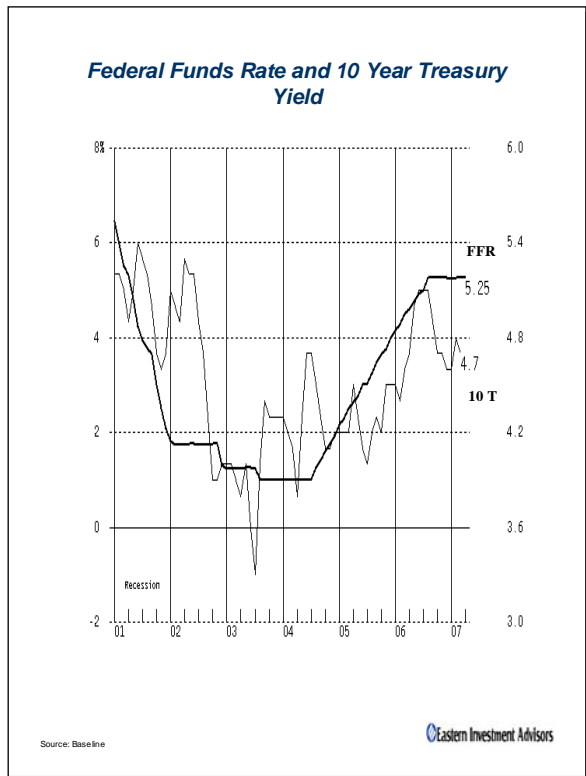


2007 will lift the cloud of uncertainty about the duration and magnitude of the economic slowdown. We expect real GDP growth to be between 2.0% and 2.5% during the first half of 2007. Higher unemployment and lower capacity utilization, economic growth below its inflationary threshold and core inflation only slightly above the Fed's comfort level could encourage the Fed to gradually lower the federal funds rate in order to keep the economic expansion on track. Evidence of stable real estate prices and improving sales in the spring will entice reluctant buyers into the market. Slightly lower short-term interest rates and a stable housing market is expected to provide the catalyst for a gradual acceleration of economic growth to between 2.75% and 3.0% by the end of the year and into 2008.

The current expansion has been underway for five years. The average length of the previous two expansions has been about nine years. Therefore, it is not unreasonable to postulate that the current deceleration in the pace of economic growth is a midcycle slowdown, not the prelude to a recession.

Interest Rates:

The drag from the weak real estate market has enabled the Fed to reduce the growth rate of the economy to below the noninflationary rate of growth without increasing the federal funds rate above the critical level of 6%, which in the past has triggered a recession. Also, mortgage rates, which have increased, are not so high as to prevent potential buyers from purchasing a home. Next year economic growth is expected to remain below its potential noninflationary growth rate, which will reduce the upward pressure on the core rate of inflation. We also expect a gradual increase in the unemployment rate to 5% due to softness in the residential construction and building material markets. Economic growth below its noninflationary potential, waning inflationary pressures and gradually rising unemployment should keep the Fed on hold through the first half of next year.



Lower rates of resource utilization due to higher unemployment and lower capacity utilization, economic growth below its inflationary threshold and core inflation only slightly above the Fed's comfort level could encourage the Fed to gradually lower the federal funds rate to 4.75% by mid year. This will help to keep the economic expansion on track. Longer-term interest rates will remain in a broad trading range during the first half of the year. However, by year's end, the markets will be focused on the possibility of accelerating economic growth in 2008. For this reason **we would not be surprised to see the 10 year U.S. Treasury yield, currently at 4.60% rise to 5.0% by year end 2007.** The result would be a flat yield curve, which is consistent with the possibility of gradually accelerating economic growth.