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Economy at Its Slowest in 4 Years

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By [EDUARDO PORTER](#) and [JEREMY W. PETERS](#)

Published: April 28, 2007

Economic growth slowed to its weakest pace in four years during the first three months of 2007, underscoring how the persistent slump in the housing market continued to serve as a drag on the American economy.

In its first estimate of economic growth for the quarter, the Commerce Department said the nation's gross domestic product, the most comprehensive measure of overall economic activity, expanded 1.3 percent for the quarter, barely over half the rate recorded in the final quarter of last year.

The abrupt slowdown was not enough to put a brake on inflation, however. The consumer price index most carefully monitored by the Federal Reserve, which excludes food and energy, rose 2.2 percent in the quarter, at an annual rate, above the Fed's stated comfort ceiling.

"It's sort of more inflation, less growth," said Stuart Hoffman, chief economist of PNC Financial. "That's not a tasty combination."

On Wall Street, economists had forecast a slide in growth, but not one this sharp. The dollar plunged against the euro, briefly falling to a record low as investors factored in expectations of faster growth and rising interest rates in Europe against low growth and the possibility of lower rates in the United States.

But bond yields rose slightly, indicating deeper concern about potentially higher inflation. Stocks — which have risen almost uninterruptedly since early March, defying concerns

over a potential economic weakening — ended mixed.

Economists said that the latest report card left the Fed in even more of a quandary over interest rates, with a weaker economy prodding it to cut rates to stimulate growth but inflationary pressures pushing it toward higher rates to curb price increases. The end result is likely to be a decision by the central bank to keep rates where they are until a clearer picture emerges.

“It’s a bugaboo for the Fed,” said John Silvia, chief economist at the [Wachovia Corporation](#), the bank holding company. “It is a difficult spot to be in.”

As throughout much of last year, the housing slump was the biggest anchor on the economy. Home construction recorded its sixth consecutive quarterly decline, falling 17 percent at an annual rate and subtracting almost a full percentage point from G.D.P.

Still, there were several upbeat signals in the economic report that suggested to many economists that the pace of growth could pick up this year. Business investment rebounded from its slowdown late last year to expand at a 2 percent annual rate in the first quarter. Silicon Valley was a key to the revival: investment in information technology contributed more than half a percentage point to growth in the quarter.

And despite the worrisome state of housing, Americans continued to borrow and buy. In the first quarter consumer spending grew 3.8 percent, a fairly vigorous pace.

But economic weakness also spread beyond housing. After a sharp cut in inventories in the fourth quarter of last year, businesses slimmed their stockpiles a little more in the first quarter of 2007, shaving 0.3 percentage points from economic growth. A decline in military spending by the government trimmed a quarter of a percentage point percent from total output.

Trade provided the biggest surprise, when exports fell unexpectedly and imports continued growing, subtracting half a percentage point from economic growth, according to the report.

Economists pointed out that the preliminary data on trade is particularly sketchy because the government did not yet have a good handle on exports and imports in March. But the data bewildered some analysts, who pointed out that the combination of a weak dollar and faster growth in Europe and elsewhere should be providing a lift to exports.

“We completely discount this number,” said Nariman Behravesh, chief economist at Global Insight of Lexington, Mass. “It’s inconsistent with everything else going on in the world.”

He suggested the estimate for first-quarter exports could be revised upward. And if not, he predicted, exports should record a sharp upswing in the spring quarter that is under way now.

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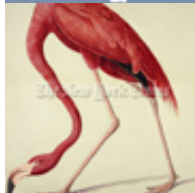


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