

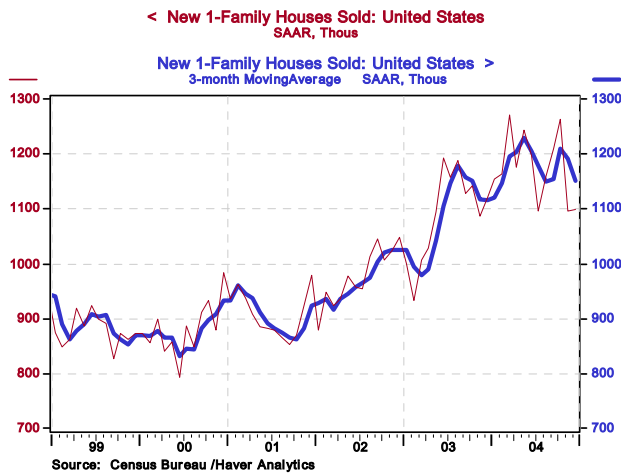


Data Suggest that Housing Market Is Vulnerable

Single-family homes sold at an annual rate of 1.098 million units during December, little different from the 1.097 million pace in November. In 2004, sales of new single-family homes rose 8.1% compared with a 11.6% increase in 2003.

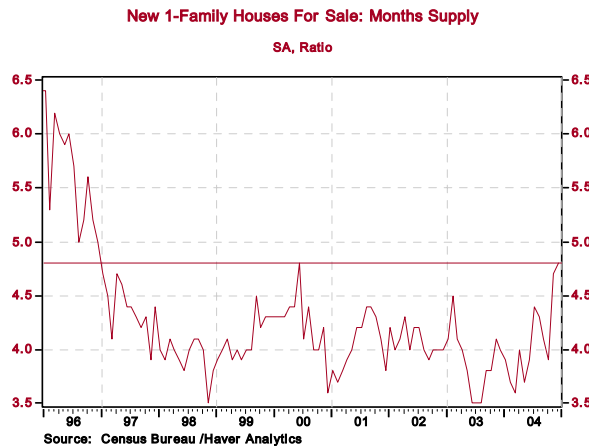
On a regional basis, sales of new-single family rose in the Midwest (+55.5%) and West (+6.3%) but declined in the Northeast (-15.7%) and South (-16.3%) in December.

Chart 1



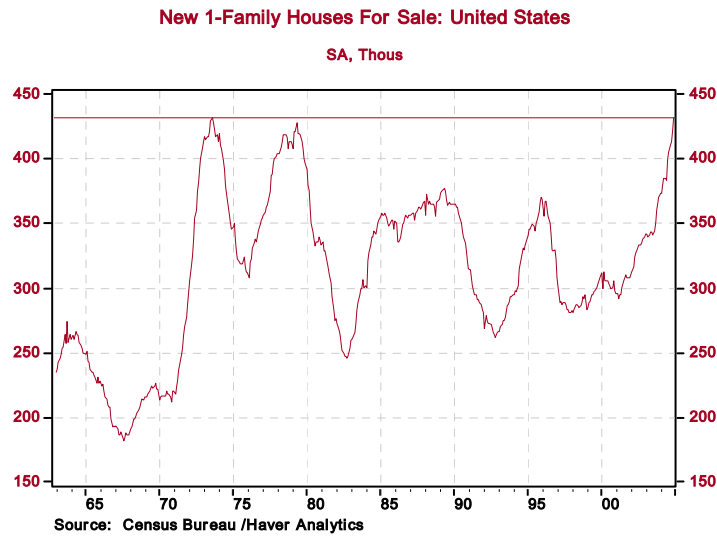
There was a 4.8-month inventory of unsold homes in the market during December. This is highest level since June 2000.

Chart 2



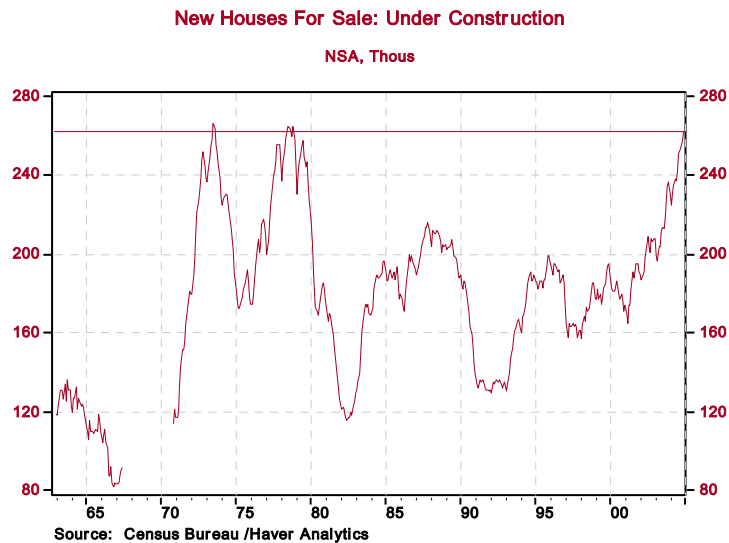
There were 432,000 new houses for sale at the end of December, matching the record set in August 1973.

Chart 3



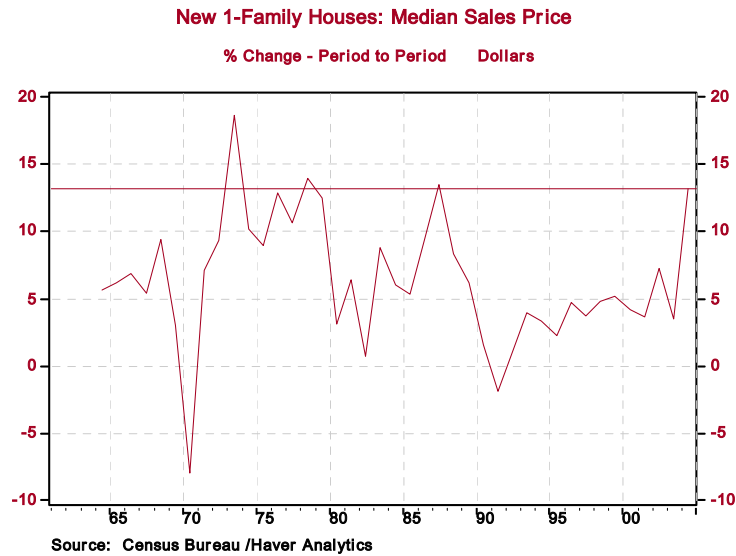
Of these houses for sale, a large percentage makes up homes under construction. According to Chart 4, the number of new unsold single-family homes under construction is close to the highs seen in 1973 and 1979.

Chart 4



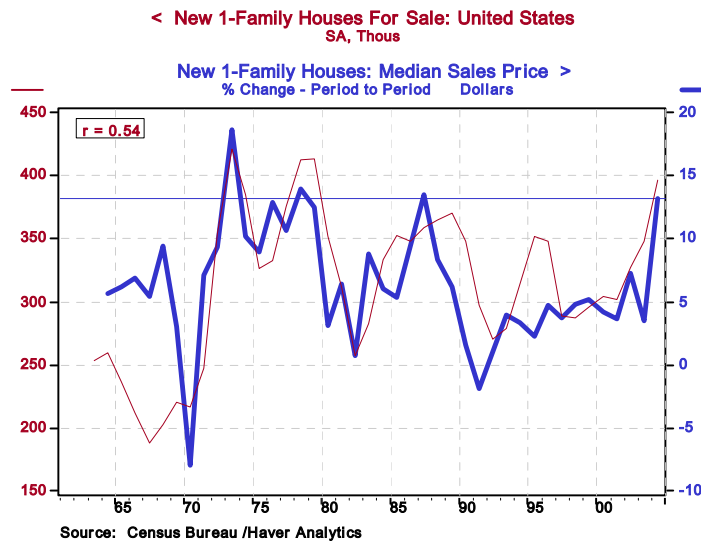
The median price of a new single-family home rose to \$222,000 in December, up 13.3% from a year ago. On average, the median price of a single-family home advanced 13.2% in 2004, the largest annual gain since 1987.

Chart 5



Putting the information in Chart 3 and Chart 5 together in Chart 6, it appears that periods of rapid gains in home prices and rising number of unsold homes in the market place do occur simultaneously. These occurrences have been followed by a significant deceleration in home prices. The current status of the housing market is a close match to the three episodes of 1973, 1979, and mid-1980 to late-1980s. Based on this historical information, a sharp deceleration of single-family home prices in the near term is not far fetched.

Chart 6



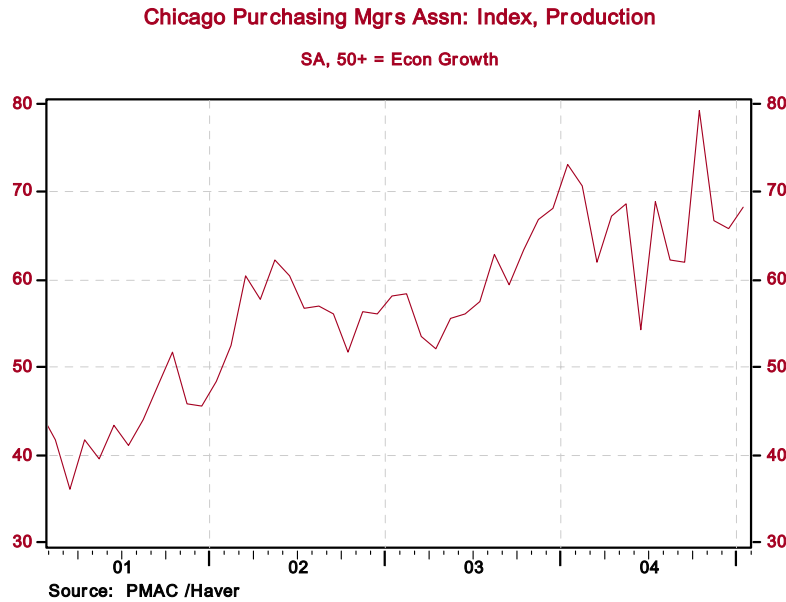
Chicago's Factory Report Indicates Improvement in January

The Chicago Purchasing Managers' business index increased 0.5 points to 62.4 in January, but it is still below the November level. Indexes tracking new orders, employment and production rose, while indexes tracking inventories, vendor deliveries, and prices dropped in January. The

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improvement in January is only a partial recovery from the downward trend of November and December.

Chart 7



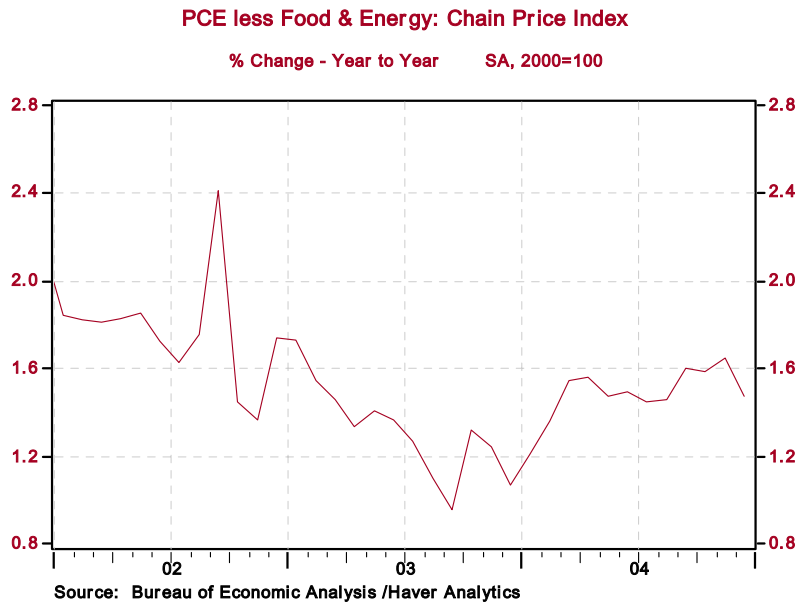
Chicago Purchasing Managers' Survey – January 2005

| | Aug-2004 | Sep-2004 | Oct-2004 | Nov-2004 | Dec-2004 | Jan-2005 |
|--------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Business Index | 56.8 | 64.3 | 67.7 | 63.8 | 61.9 | 62.4 |
| Production | 62.2 | 62.0 | 79.2 | 66.6 | 65.9 | 68.3 |
| New Orders | 58.2 | 71.8 | 79.7 | 68.1 | 64.9 | 65.8 |
| Backlogs | 51.4 | 55.7 | 59.8 | 53.3 | 54.3 | 53.7 |
| Inventories | 58.9 | 60.8 | 56.0 | 55.4 | 56.3 | 53.2 |
| Employment | 50.2 | 53.3 | 54.0 | 58.9 | 51.1 | 52.8 |
| Vendor Deliveries | 56.5 | 59.8 | 58.8 | 60.0 | 64.4 | 58.3 |
| Prices Paid | 86.6 | 86.9 | 84.7 | 88.9 | 84.4 | 76.5 |

Microsoft Dividend Gives Extra Lift to Personal Income in December

Personal income increased 3.7% in December after a 0.4% gain in the prior month. A special dividend payment by Microsoft led to this large increase in personal income. Excluding this special factor, personal income advanced 0.6% in December. Inflation adjusted consumer spending rose a hefty 0.9% in December, led by a 4.3% jump in purchases of durable goods (mostly cars). A moderation in consumer spending is predicted for January. The price index of personal consumption expenditures declined 0.1% in December vs. a 0.2% increase in the preceding month. The price index of personal consumption expenditures excluding food and energy (the Fed's preferred inflation measure) held steady in December, taking the year-to-year increase to 1.47%, a 40 basis point increase since December 2003. This mild increase in the Fed's preferred inflation measure gives the FOMC flexibility in the implementation of monetary policy.

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The advance estimate of fourth quarter real GDP (+3.1%) will be revised in a day or two to reflect corrections of Canada's trade numbers arising due to technical problems.

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