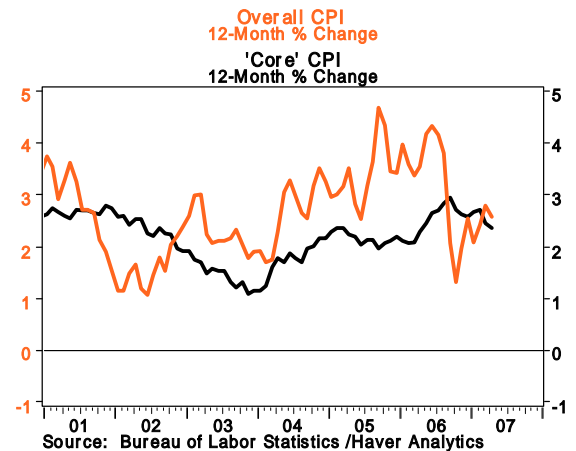


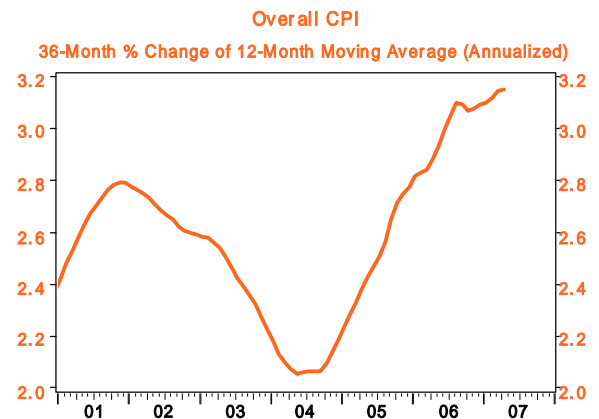
APRIL CPI

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- The Consumer Price Index (CPI) increased 0.4% in April, slightly less than the consensus expected. The CPI is up 2.6% versus a year ago.
- Energy prices increased 2.4% in April. Excluding food and energy, the core CPI was up 0.2% in April, as the consensus expected, and up 2.3% versus a year ago.
- The rise in the core CPI was mostly due to lodging away from home (hotels), which increased 1.9%, and owners' equivalent rent (what we theoretically pay ourselves to live in our own homes), which rose 0.2%.



Implications: We do not share the sentiment in some quarters that today's CPI report signals inflation is not a threat. That sentiment is the result of too much focus on measures of inflation that exclude food and energy prices. Traditionally, many economists have used core inflation to gauge the underlying trend in inflation. It does make sense to exclude those commodities when those prices are volatile both up and down. However, for the past four years almost all the volatility has been to the upside. Consumers still buy food and energy even if those items are left out of the "core." The chart to the right presents an alternative measure of the underlying inflation trend and it is not a pretty picture. We took a 12-month moving average of the CPI and then looked at how that average has changed over 36-month periods. The goal is to count food and energy (unlike the core) but smooth out the data to try to discern an underlying trend (like the core). That measure shows that in the past three years CPI inflation is up at a 3.2% annual rate, the fastest since 1994. In other news today, the Empire State Manufacturing Index rebounded to 8.0 in May from 3.8 in April. This is consistent with the recent increase in the national ISM index showing a manufacturing rebound is underway.



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| CPI - U <i>All Data Seasonally Adjusted</i> | Apr-07 | Mar-07 | Feb-07 | 3-mo % Ch. annualized | 6-mo % Ch. annualized | Yr to Yr % Change |
|--|--------------|--------|--------|--------------------------|--------------------------|----------------------|
| Consumer Price Index | 0.4% | 0.6% | 0.4% | 5.7% | 4.2% | 2.6% |
| <i>Ex Food & Energy</i> | 0.2% | 0.1% | 0.2% | 1.9% | 2.0% | 2.3% |
| <i>Ex Energy</i> | 0.2% | 0.1% | 0.3% | 2.6% | 2.4% | 2.6% |
| Energy | 2.4% | 5.9% | 0.9% | 43.3% | 25.6% | 2.9% |
| Food and Beverages | 0.4% | 0.3% | 0.8% | 6.1% | 4.3% | 3.7% |
| Housing | 0.2% | 0.2% | 0.4% | 3.4% | 3.9% | 3.4% |
| Owners Equivalent Rent | 0.2% | 0.3% | 0.3% | 3.0% | 3.2% | 3.9% |
| New Vehicles | 0.0% | 0.3% | -0.1% | 0.8% | -1.0% | -1.0% |
| Medical Care | 0.4% | 0.1% | 0.5% | 3.9% | 4.4% | 4.0% |
| Services (Excluding Energy Services) | 0.3% | 0.1% | 0.3% | 2.9% | 3.1% | 3.5% |
| Real Average Hourly Earnings | -0.2% | -0.5% | 0.0% | -2.8% | -1.0% | 1.2% |
| Real Average Weekly Earnings | -0.5% | 0.1% | -0.3% | -2.9% | -1.5% | 0.9% |

Source: U.S. Department of Labor

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