

Economic Overview

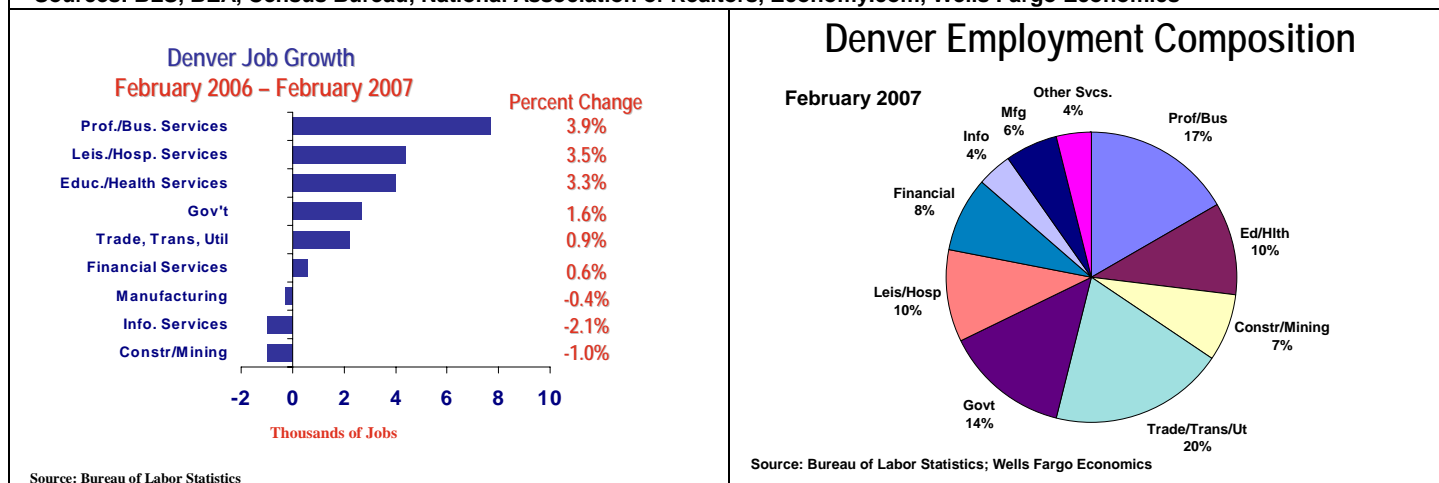
Although still on a decent footing, Denver's economy has cooled. Employment growth has slowed from a peak of 2.5% y/y in June 2006 to just 1.7% in February 2007, slightly higher than the national rate of 1.5%. In addition, according to the Bureau of Labor Statistics' benchmark revisions in March, it is apparent that Denver employment growth was largely in line with that of the nation over the past couple years, contrary to previous numbers that showed Denver employment growth nearly doubling the national pace. The unemployment rate was 3.9% in February compared to the national rate of 4.5% and has been below the national rate since November 2006. While this is good news, a closer look reveals that the decline in the unemployment rate has come as both household employment growth and labor force growth have slowed on a year-ago basis. However, household employment and labor force growth both remain above their recent four-year averages. While professional/business services and education/health care continue to thrive, manufacturing, information services and construction are shedding payrolls. Despite the ongoing public works projects in the metro area, the construction industry is losing jobs on a year-ago basis amid the swift slowdown in the housing market. Home prices are now below year-ago levels.

Outlook

We expect the Denver economy to continue to slow in 2007 and into 2008, in line with the nation, as the housing slowdown leads to further job losses in construction, real estate and financial services slow, and manufacturing and information services contract amid a slowdown in business spending. Employment growth is forecast to slow to about 1.3% y/y in 2007. The unemployment rate is forecast to climb from currently low levels, averaging 4.4% this year. Personal income growth is expected to moderate to about 5.3%, while home prices are forecast to fall 2.8%.

	Denver							
	2001	2002	2003	2004	2005	2006e	2007f	2008f
Gross Metro Product, % chg.	0.9	-0.9	1.9	3.0	3.7	3.5	2.2	2.0
Employment (ths.)	1,209	1,172	1,158	1,167	1,190	1,215	1,230	1,243
Employment growth, % chg.	(0.2)	(3.0)	(1.2)	0.8	2.0	2.1	1.3	1.0
Unemployment rate, %	4.0	6.1	6.5	5.8	5.1	4.6	4.4	4.7
Personal Income growth, % chg.	6.6	0.2	0.7	6.3	6.0	5.7	5.3	5.0
Population (ths.)	2,244	2,276	2,299	2,325	2,359	2,394	2,421	2,449
Population growth, % chg.	2.3	1.4	1.0	1.1	1.5	1.5	1.1	1.2
Net migration (ths.)	28.7	9.0	0.2	3.7	12.4	11.7	4.2	4.7
Median existing home prices, Ths. \$'s	217.1	228.2	237.3	238.5	246.3	249.5	242.5	237.2
(Percent change in home prices)	10.7	5.1	4.0	0.5	3.3	1.3	-2.8	-2.2
Housing Starts, # of units	25,603	22,157	18,082	20,924	19,571	17,681	15,865	16,640
Single-family, # of units	15,063	14,734	14,751	18,396	17,257	14,134	11,125	11,007
Multi-family, # of units	10,540	7,423	3,332	2,528	2,314	3,547	4,740	5,633

Sources: BLS, BEA, Census Bureau, National Association of Realtors, Economy.com, Wells Fargo Economics



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Local Banker Observations

Local bankers believe that the economy is holding steady. While they have noticed the economy slow somewhat recently amid higher interest rates, several public works projects including the FasTracks light rail and public transit project, a new soccer stadium and a new justice center are helping to support the economy. Another positive note is the United Launch Alliance, a joint venture between Boeing and Lockheed Martin to produce, engineer, test and launch rockets for the U.S. government. The headquarters for the venture is based in Denver, which has resulted in the relocation of highly paid engineers from California to Denver. In addition, the Denver airport is expanding international routes, helping the city to grow in importance as a regional business hub. Oil and gas state tax revenue has tapered off as prices have fallen from their peaks, but these industries continue to do quite well.

Professional/business services clients are also seeing solid business. In the downtown area, high-end condos and a hotel are going up, retail and restaurant business is solid amid strong wage growth, and commercial vacancy rates are down from a year ago. On the other hand, residential builders and sub-contractors are struggling amid the housing slump, while information services, manufacturing and transportation/warehousing are all contracting.

The passage of TABOR (Taxpayer Bill of Rights) in 1992 limited state revenue growth to the rate of state population growth plus inflation - the sum of which has been lower in recent years compared to when the bill was first passed - with the excess being refunded to taxpayers. When revenues plummeted during the tech recession, this limit on the portion of revenue the state could keep led to huge government cuts, especially in education. The passage of Referendum C in November 2005 freed up \$3.7 billion for transportation, health care and education that would have otherwise been refunded back to taxpayers. However, the rejection of Referendum D, which would have allowed the state to take on an additional \$2.1 billion in debt, showed voters are still in favor of some form of fiscal discipline.

Over the next year, local bankers see three main risks to Denver's economy. First, the state is highly dependent on tourism, so unfavorable weather or a decline in travel due to high gas prices or another terrorist attack are big concerns. Second, immigration policy is a big issue in Denver, with undocumented workers forming a significant portion of the labor force for restaurants, construction and cleaning. Thus many local businesses will be keeping their eyes on the immigration policy debate. Finally, the AFL-CIO was upset after Colorado Governor Bill Ritter vetoed the Labor Peace Act (Colorado Bill 1072) in February, which would have made it easier to organize a union. In response, union leaders are threatening to withdraw their support for the upcoming Democratic National Convention in August 2008 and urging Democrats to hold it elsewhere. The Convention is still expected to take place in Denver, but the uncertainty surrounding the dispute as well as the effects on union membership is cause for concern.

Housing Market

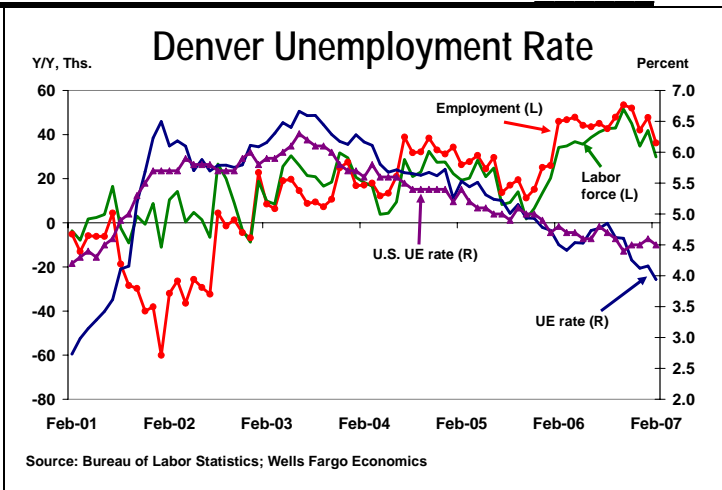
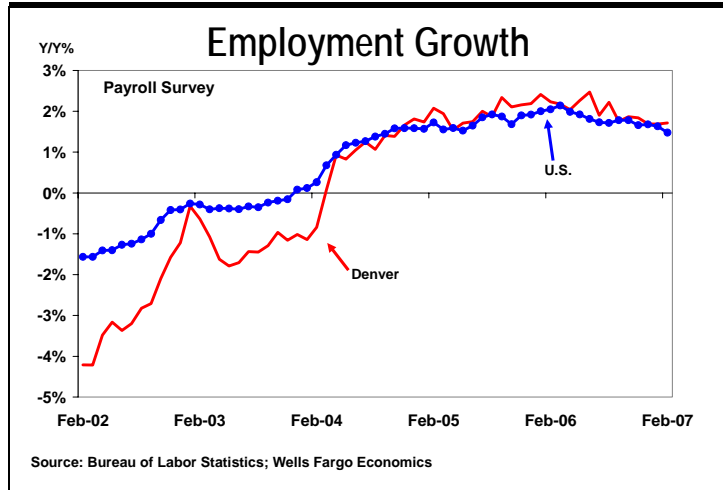
Just when Denver's housing market appeared to be on the rebound, along came higher interest rates, and home price growth has once again returned to negative territory. Home prices fell 0.8% on a year-ago basis in Q406, down from the recent peak of 4.2% in Q405 and following a drop of 0.1% in Q306. Housing permits have fallen from year-ago levels for the past two quarters, down 37.0% in Q406. However, while single-family permits have been falling since Q105, multi-family permits have been very strong, only falling in Q406 for the first time since Q205. The story is similar for housing starts, with single-family starts dropping 33.7% in Q406 while multi-family starts rose 56.2% as demand for rental units increased amid high home prices and tightening mortgage standards.

As home prices and mortgage rates rose over the past few years, the housing affordability index declined from a peak of 135.6 in Q104 to 121.2 in Q306 before rebounding to 125.5 in Q406. As home price growth has slowed and mortgage rates have come down recently, housing affordability is starting to show signs of improvement in Denver and across the nation. However, this has not yet translated into stronger sales. Existing home sales have declined on a year-ago basis for the past three quarters in Denver, falling 12.3% in Q406. Moderating employment growth, rising sub-prime mortgage defaults, tightening mortgage standards and increasing debt burdens will all put downward pressure on home prices over the next couple years. However, home prices in Denver did not rise nearly as much as in other metro areas during the recent boom, so the correction in Denver's housing market is not expected to be as significant as it will be in many other parts of the nation.

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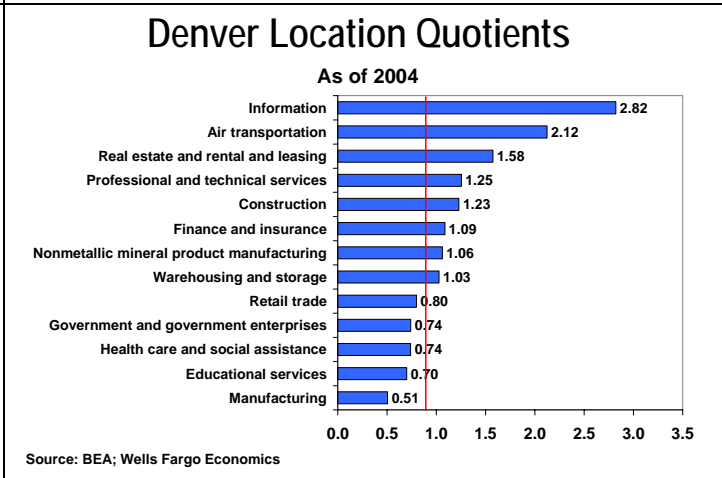
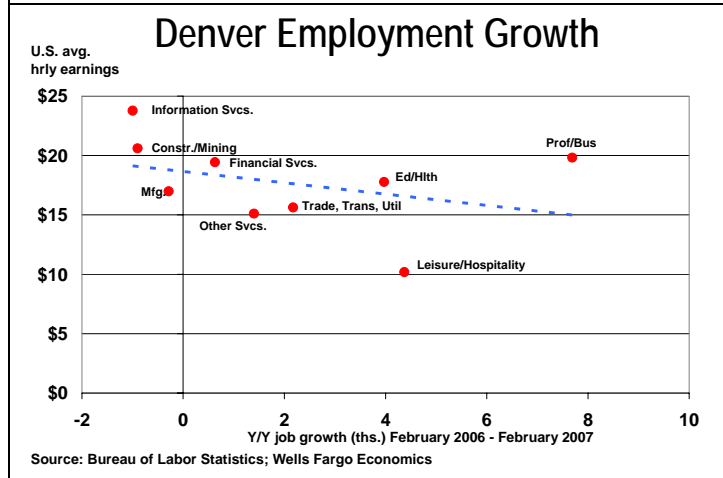
Wells Fargo Economics Regional Analysis

Denver



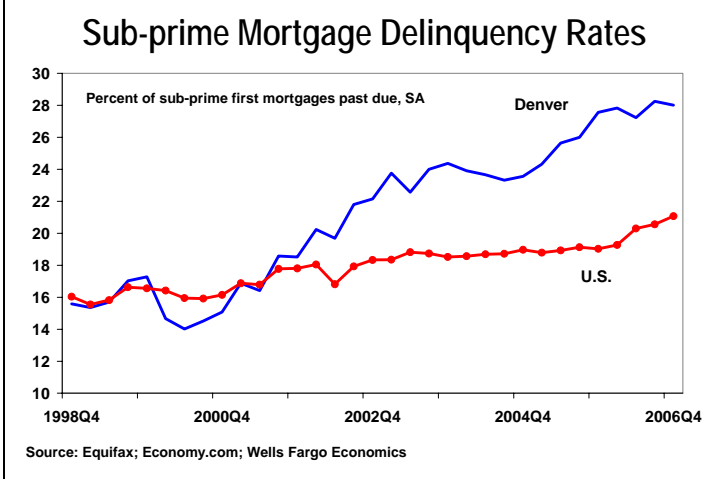
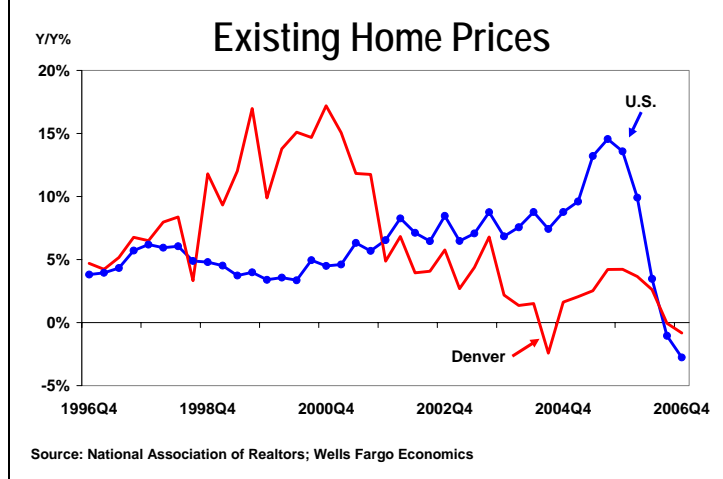
Benchmark revisions show that Denver's employment growth did not outpace the nation's as much as previously thought over the past couple years, but was rather largely in line with the U.S.

Denver's unemployment rate dipped below that of the U.S. recently. However, as the chart shows, this has come amid slowing growth in both employment and the labor force.



Denver's employment mix has become less favorable as construction and manufacturing are now shedding payrolls and job growth has slowed for financial services and TTU.

High exposure in the weak information services industry, the oil-price sensitive air transportation industry and interest-rate sensitive real estate industry poses risk to economic growth.



Just as Denver's housing market appeared to be rebounding from the bursting of the tech bubble, along came higher interest rates, and home price growth has stalled, in line with the nation.

Rising sub-prime mortgage delinquencies are a growing concern in the nation, and in Denver in particular, where sub-prime delinquency rates have been higher than the U.S. since 2001.