PCA Portland Cement Association

THE Monitor Forecast Report

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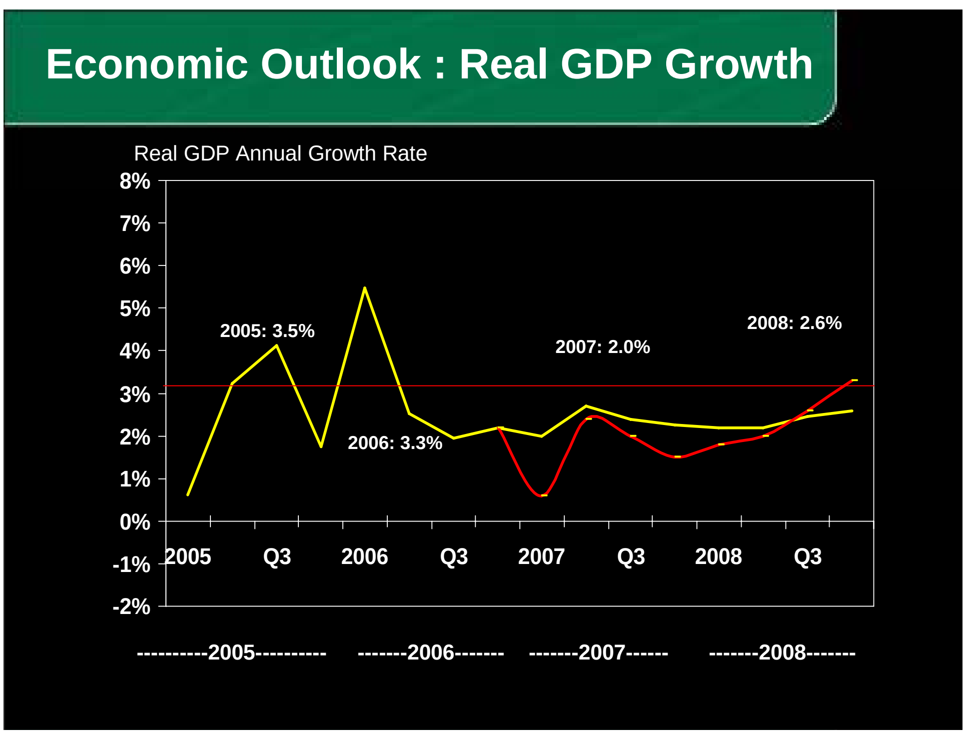
Recent Data Suggests Spring Forecast Optimistic

Overview

Recent data suggest the economy, residential construction, cement intensity and import volumes are underperforming compared to PCA's spring forecast. Highlights of PCA's spring forecast projections for 2007 included: real GDP (Gross Domestic Product) growth of 2.4%; a housing start decline of 18% (20% for single family); strong gains in nonresidential and public construction; a cement intensity gain of 1.5%; and an 8% decline in import volume.

PCA concluded that the national cement market would decline 1.5% during 2007 and, due to a reduction in imports, lead to somewhat tighter inventory conditions. PCA now believes that the decline in cement consumption for 2007 could exceed 3% and despite weaker demand, inventories may tighten even more than expected.



Economic Growth

The Bureau of Economic Analysis updated first quarter real GDP growth. According to the report, the economy grew at a 0.6% annual rate – far below PCA's expectation of 2% and the slowest level since 2002. While somewhat stronger growth rates are expected during the remainder of the year, the first quarter weakness makes PCA's 2.4% real GDP growth projection unlikely given the current sub-prime and energy price environment.

Despite the weak economic growth reported for the first quarter, consumer spending performed surprisingly well – recording a 4.2% annual increase. This is both encouraging and worrisome. Consumer spending accounts for more than two-thirds of overall U.S. economic activity. A strong performance in this sector may suggest that the economy is on stronger footing than the overall growth rates suggest. However, one has to ask, "Can such strong consumer spending growth be counted on as the year progresses?" If consumer spending grew as PCA expected, first- quarter real GDP growth would have been negative. Given high debt burdens, the sub-prime issue and a tightening in lending standards, debt-based consumer spending activity is expected to moderate as the year progresses.

In addition to debt issues, high gasoline prices will steal additional strength from consumer spending. The spring forecast for 2007 projected gasoline prices at $2.65 per gallon – roughly 12% higher than 2006 levels. To date, gasoline prices have averaged $2.59 per gallon – in line with PCA projections. Gasoline prices, however, are currently at $3.20 per gallon - significantly higher than PCA expected and these levels suggest a greater adverse impact on consumer spending may materialize during the next several quarters.

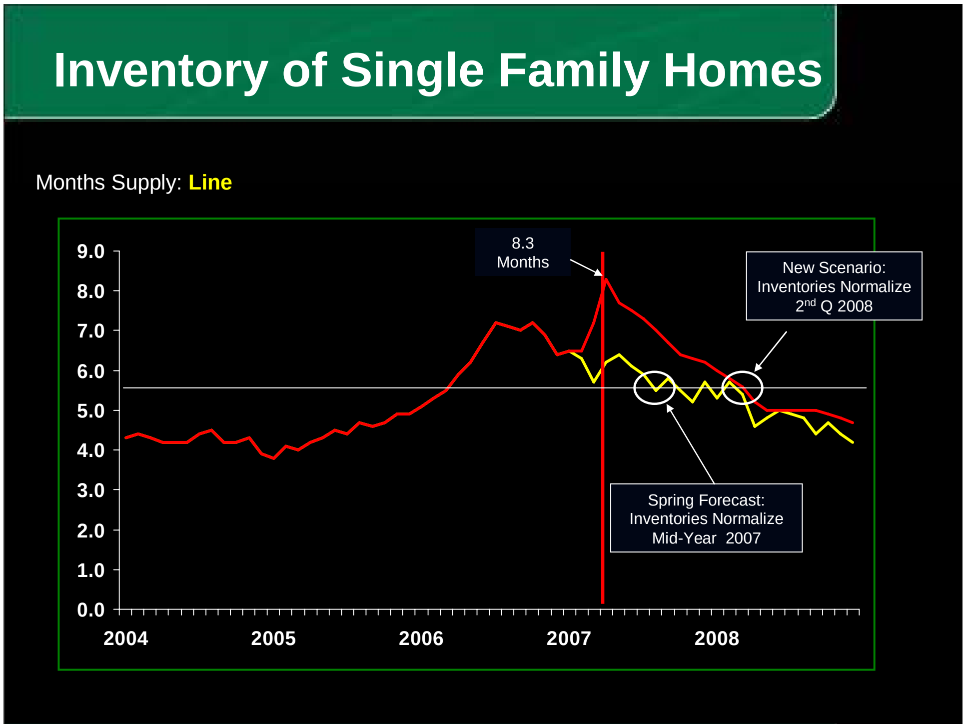
Finally, employment growth averaged 143,000 net new jobs during the first quarter. During the past three months employment growth averaged 118,000 net new jobs per month. Even slower job creation is expected during the remainder of the year. PCA had expected a pace of slightly more than 100,000 net new jobs per month during the remainder of 2007. This now seems optimistic.

Sub-prime issues, high consumer debt burdens, tight lending standards, high gasoline prices, and the prospects of slower job creation all point to much more moderate growth in consumer spending as the year progresses. Furthermore, investment spending is expected to suffer an even larger drag than previously expected from the housing sector. Other sectors of the economy are either too small or lack enough positive dynamics to significantly change PCA's more modest outlook for economic growth. PCA now believes the U.S. economy will struggle to reach 2% growth during 2007.

Housing Sector

The on-going correction in the housing sector will impact economic growth as well as construction activity and cement consumption. The key issue in this sector is the ability of the market to burn off excess inventories. The inventory correction process is not just the difference between sales and starts. It must also consider the number of homes supplied to the market via foreclosure. During 2006, 400,000 homes went into foreclosure. PCA's spring forecast expected roughly 450,000 homes go into foreclosure during 2007 – a 16% increase. PCA's estimate was based on a default rate of 6%. Unfortunately, some experts expect the foreclosure rate to be substantially higher and result in the venting of up to 2.2 million homes on the market – and worsening the inventory situation. PCA believes that some sort of intervention will materialize before this dire scenario unfolds. Nevertheless, higher default rates than assumed in the PCA spring forecast seem likely.

This additional source of supply to housing inventory will force deeper cuts in starts and prolong the correction process. This is particularly true in regional markets that experienced very strong appreciation rates, a high presence of speculators, and a large inventory overhang when the speculators withdrew – such as Florida. Rough estimates suggest that an additional 50,000 to



70,000 reduction in single-family starts to PCA's already conservative spring forecast estimates of 1.47 million housing starts. In addition, month's supply does not reach a point to trigger a resumption of growth in starts activity (5.2-5.5 month's supply) until early in the second quarter of 2008 – compared to late 2007 as earlier forecast.

Higher-than-expected sub-prime foreclosures also suggest additional adverse drag on overall consumer spending activity. Appreciation gains forced many potential homebuyers out of the market due to affordability issues using conventional financing. The use of exotic mortgages, such as interest-only loans, emerged in late 2003. These mortgages were characterized by extremely low initial rates which dramatically reduced the monthly mortgage payments and enabled otherwise unqualified buyers to purchase homes. The rates on these mortgages, however, were adjustable to prevailing market rates after a one-, three- or five-year period. After resetting to prevailing interest rates, mortgage payments could increase by 50% or more for some of homeowners. During the past three years income has grown, but not at rate to keep pace with the potential mortgage payment increases after resets.

The potential of a large increase in monthly mortgage payments not offset by an increase in income implies new pressure on a many new homeowners. Tighter lending standards may inhibit the ability of homeowners facing resets to refinance at lower rates. Due to these new budgetary pressures consumers will eventually be forced to curb spending activity. Many of these homeowners may try to maintain their standard of living by running up credit card debt. This is a temporary and potentially lethal fix. Debt will increase. Increases in loan delinquencies and defaults may emerge. Credit quality could deteriorate. Lenders may impose even tighter credit standards. Eventually these events could lead to a significant reduction in consumer spending.

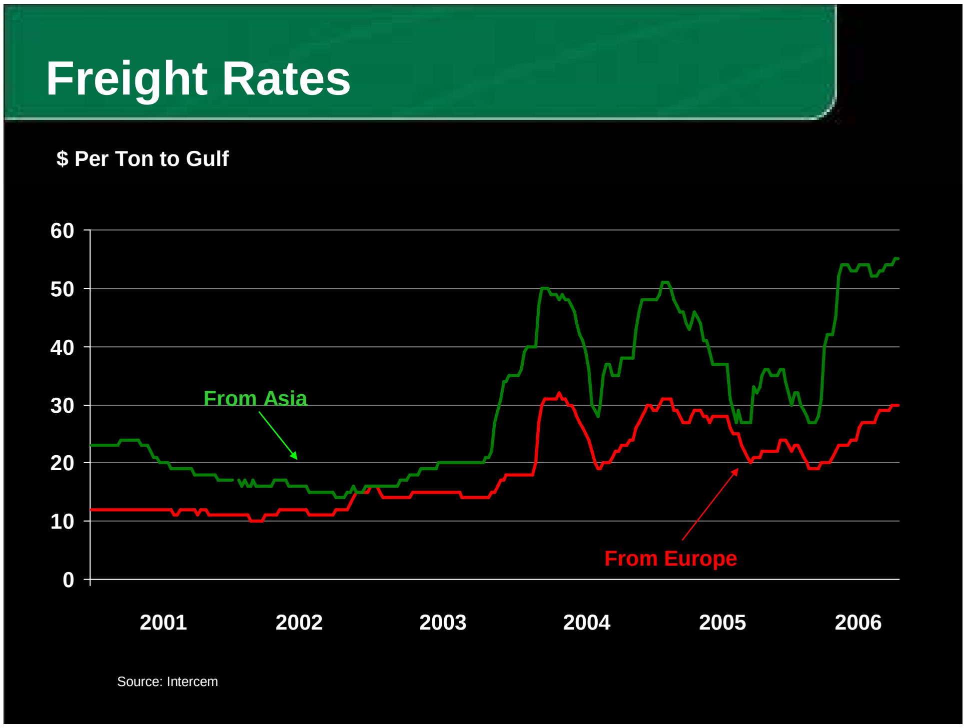
Total Construction

PCA expected a harsh correction in residential construction. It is beginning to appear, however, that our projections were not pessimistic enough. In addition, PCA expected rather strong growth in nonresidential and public construction. On this count, PCA may not have been optimistic enough.

Year-to-date real nonresidential construction has grown at a 17.7% annual rate – well in excess of PCA's spring projection of 8.6%. Keep in mind that as economic growth slows, a signal will be sent to potential commercial developers that expected ROI on investments may not be as high as projected under a stronger economic growth assumption. The current momentum in nonresidential was expected to subside in the context of slower second half 2007 growth. With even slower growth now envisioned, greater nonresidential momentum is expected to be lost in the second half of 2007. In net, the competing effects of underestimating current nonresidential strength against an even slower economic growth environment leave PCA's spring projection of 8.6% growth relatively intact.

According to government data, public construction is vibrant. Year-to-date public construction is growing at an average annual rate of 8.9% with highways and street construction growing at a 9.8% rate. PCA's spring forecast had expected strong growth of 5% for total public construction and 6.1% for highway and street construction. Current momentum is extremely strong. In the context of slower economic growth, due to lags, public construction is slower to lose its current momentum than other construction sectors. Lacking an immediate and sustained economic growth signal, the 2007 momentum already in place will most likely subside slowly. For this sector, 2008 is more at risk. In net, PCA's spring projections may underestimate the strength in public construction – even in the context of slower 2007 economic growth.

The latest GDP report showed a strong increase in state and local expenditures (3.9%) – reinforcing the strength seen in public construction activity. Nearly 95% of public construction is performed at the state and local level. This suggests that an increase in 2007 public construction is warranted, but potentially at the expense of 2008 activity.



In total, PCA's spring projections of a 3.1% decline in real construction spending may be somewhat optimistic. Weighing the current trends among residential, nonresidential, and public construction activity, PCA now believes construction spending could decline by 4%.

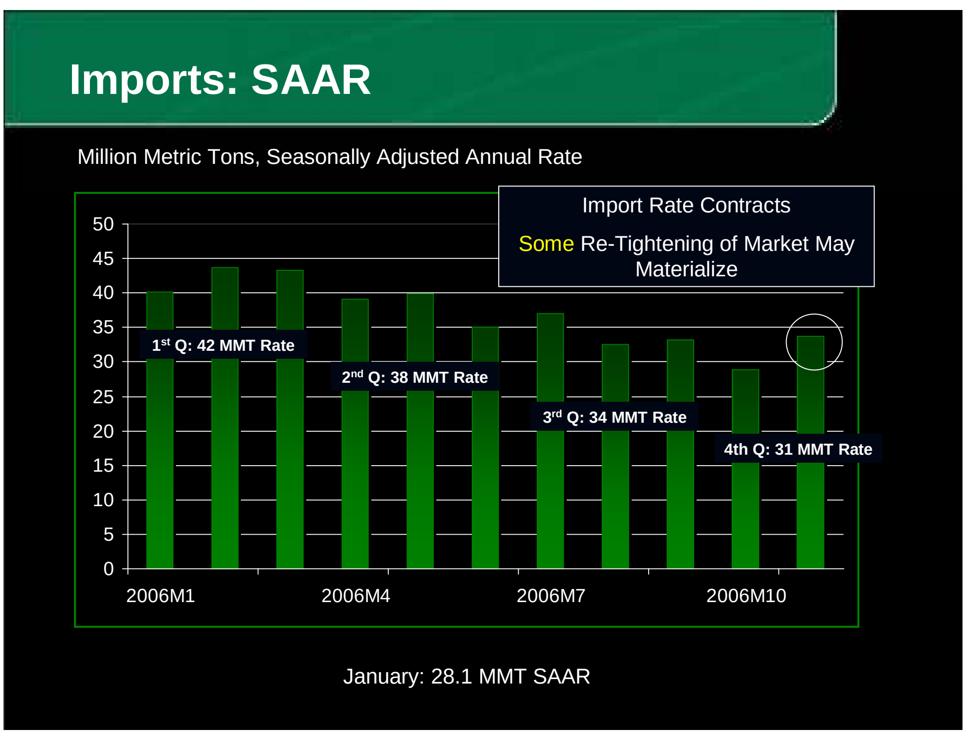
Cement Intensity

PCA's spring forecast expected a 1.5% gain in cement intensity during 2007 – with most of the gains materializing in the second half of the year. Cement intensity measures the amount of cement consumed per dollar of construction activity. These gains were largely based on expected changes in the composition of construction and improved relative price of concrete against competing materials – particularly asphalt and steel.

Monthly cement intensity is highly volatile and trends can be masked by weather and unique transitory changes in construction activity. Year-to-date, cement intensity is off nearly 17% from 2006 levels (January & February data). Warm weather in 2006 and harsh weather in 2007 probably explains much of the large decline observed thus far in 2007. Not as easily dismissed, however, is 11 straight months of decline. While it may be too early to assess, recent data poses serious questions regarding PCA's spring projection of a 1.5% gain in intensity. Gains in cement intensity were expected to provide some cushion the industry from declines in overall construction. If cement intensity remains flat during 2007, a 4% decline in cement consumption may materialize. Due to limited data it is too early to back away from our spring estimates for intensity growth. Nevertheless, the downside risks to this projection are unfolding.

Imports

While several factors determine import volumes, freight rates play an especially important role. Freight rates have more than doubled since February 2006. Imports, as a result, have followed a sustained reduction in volume. During the first quarter of 2006 imports averaged a 42 million ton



seasonally adjusted annual rate (SAAR). By the end of 2006, the rate had steadily dropped to a 32 million metric ton SAAR. January 2007 import data reported a 28.1 million tons SAAR and February reported a 25.5 million tons SAAR.

There is clearly a large pull back in imports materializing. While much of this is tied to freight rates, inventory growth during 2006 and pessimism regarding 2007 volume probably have also contributed to this pullback.

PCA's spring forecast projected an 8% decline in imports – resulting in 33.1 million tons or a 2.8 million ton reduction in imports. That projection now seems far off. Compared to strong 2006 levels, the recent import performance reflects a 36% decline. If current import rates are sustained, this implies an 8 million ton import retrenchment. PCA expects a 5 million ton to 6 million ton reduction in imports from 2006 levels.

Inventories

According to the U.S. Geological Survey (USGS), more than 1.1 million tons were added to inventories during 2006 and pushing supply up to 21 days – the highest levels since 2002. In the context of easing demand, high freight rates, and a contraction in imports, a 770,000 metric ton inventory correction was expected in the spring forecast – bringing the supply down to 19 days. The reduction in imports may lead to more tightening in inventories than previously expected. The combination of a 3% decline in demand coupled with imports contracting to a 30 million ton rate suggest a 1.5 million ton to 2.0 million ton tightening in inventories – pushing supply down from 21 days in 2006 to 17-18 days in 2007.