

Part 1

September 15, 2004

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Summary and Outlook

Prepared for the Federal Open Market Committee
by the staff of the Board of Governors of the Federal Reserve System

September 15, 2004

Summary and Outlook

Summary of the Near-Term Outlook
(Percent change at annual rate except as noted)

Measure	2004:Q3		2004:Q4	
	Aug. GB	Sept. GB	Aug. GB	Sept. GB
Real GDP	3.9	3.6	4.7	4.1
Private domestic final purchases	4.8	4.2	5.2	4.8
Personal consumption expenditures	4.1	3.7	4.4	4.1
Residential investment	-1.2	-.8	-4.9	-.5
Business fixed investment	13.4	10.9	17.0	12.6
Government outlays for consumption and investment	2.5	3.9	1.8	1.2
	Contribution to growth (percentage points)			
Inventory investment	-.4	-.7	.6	.2
Net exports	-.2	-.0	-.7	-.4

project real GDP to increase at annual rates of 3-1/2 percent in the third quarter and 4 percent in the fourth quarter.

In the labor market, firms appear to be exhibiting greater caution in their hiring than they did in the spring: Over the past three months, payrolls have risen only about 100,000 per month on average. For the remainder of the year, we anticipate that private payrolls will rise a bit more rapidly—roughly 200,000 per month—as economic activity firms. This pickup, which should be sufficient to begin to ease households' discouragement about limited job prospects, is expected to keep the unemployment rate at 5-1/2 percent for the rest of the year.

Manufacturing production climbed 0.5 percent in August. Motor vehicle assemblies rebounded from their decline over the preceding three months, and manufacturing activity excluding motor vehicles and parts moved up again. However, because incoming news on the high-tech sector has been less favorable and motor vehicle inventories remain elevated, we have revised down our forecast for factory production in the second half, from an annual rate of 6-3/4 percent in the August Greenbook to a pace of 6 percent in this projection. The rate of factory utilization rises to just 77-1/2 percent by the end of the year, still about 2-1/2 percentage points below its 1972-2003 average.

Projections of Real GDP
(Percent change at annual rate from end
of preceding period except as noted)

Measure	2004		2005	2006
	H1	H2		
Real GDP	3.9	3.8	3.8	4.0
Previous	3.8	4.3	3.6	...
Final sales	2.9	4.1	4.0	4.0
Previous	3.1	4.3	3.8	...
PCE	2.8	3.9	3.9	4.1
Previous	2.6	4.3	3.9	...
Residential investment	10.5	-.6	2.5	3.9
Previous	10.6	-3.1	.0	...
BFI	8.0	11.8	9.4	9.9
Previous	6.8	15.2	9.9	...
Government purchases	2.4	2.5	2.4	2.7
Previous	2.5	2.1	2.2	...
Exports	7.3	9.6	7.2	6.4
Previous	9.8	10.0	7.6	...
Imports	11.6	7.8	6.8	8.6
Previous	10.0	9.7	7.8	...
Contribution to growth (percentage points)				
Inventory change	1.0	-.3	-.2	.0
Previous	.7	.1	-.1	...
Net exports	-.9	-.2	-.3	-.7
Previous	-.5	-.4	-.4	...

... Not applicable.

August Greenbook. However, although we project a wider output gap in the near term, we still expect it to be eliminated by the end of the projection period—now 2006.

Turning to the details of this forecast, we have marked up slightly the growth of real output in 2005 because the monetary policy tightening in this forecast is assumed to be more gradual than in our previous projection. We believe that an improving labor market and the slight decline in long rates that accompanies our assumed path of the federal

Decomposition of Structural Labor Productivity

(Percent change, Q4 to Q4, except as noted)

Measure	1974-95	1996-2001	2002	2003	2004	2005	2006
Structural labor productivity	1.5	2.7	3.2	3.7	3.0	2.7	2.8
Previous	1.5	2.7	3.2	3.7	3.1	2.8	...
<i>Contributions</i> ¹							
Capital deepening	.7	1.4	.6	.6	.8	.9	1.0
Previous	.7	1.4	.6	.6	.8	1.0	...
Multifactor productivity	.5	1.1	2.4	2.8	2.0	1.6	1.5
Previous	.5	1.1	2.4	2.8	2.0	1.6	...
Labor composition	.3	.3	.3	.3	.3	.3	.3
MEMO							
Potential GDP	3.0	3.4	3.4	3.8	3.4	3.3	3.4
Previous	3.0	3.4	3.4	3.8	3.4	3.4	...

NOTE. Components may not sum to totals because of rounding. For multiyear periods, the percent change is the annual average from Q4 of the year preceding the first year shown to Q4 of the last shown.

1. Percentage points.

... Not applicable.

The Outlook for the Labor Market

(Percent change, Q4 to Q4, except as noted)

Measure	2003	2004	2005	2006
Output per hour, nonfarm business	5.6	2.2	1.8	2.6
Previous	5.6	2.2	1.9	...
Nonfarm private payroll employment	-.2	1.9	2.5	2.2
Previous	-.2	2.6	2.2	...
Household survey employment	1.2	1.4	1.8	1.7
Previous	1.2	1.5	1.7	...
Labor force participation rate ¹	66.1	66.2	66.5	66.6
Previous	66.1	66.2	66.5	...
Civilian unemployment rate ¹	5.9	5.5	5.3	5.1
Previous	5.9	5.5	5.3	...
MEMO				
GDP gap ²	1.7	1.2	.7	.1
Previous	1.6	1.0	.8	...

1. Percent, average for the fourth quarter

2. Percent difference between potential and actual GDP in the fourth quarter of the year indicated. A positive number indicates that the economy is operating below potential.

... Not applicable.

Inflation Projections
(Percent change, Q4 to Q4, except as noted)

Measure	2003	2004	2005	2006
PCE chain-weighted price index	1.7	2.2	1.3	1.3
Previous	1.7	2.4	1.2	...
Food and beverages	2.7	2.8	1.9	1.7
Previous	2.7	2.7	1.8	...
Energy	7.2	11.0	-2.4	-1.4
Previous	7.2	10.8	-4.1	...
Excluding food and energy	1.2	1.6	1.4	1.3
Previous	1.2	1.8	1.5	...
Consumer price index	1.9	2.8	1.5	1.5
Previous	1.9	2.9	1.4	...
Excluding food and energy	1.2	2.0	1.8	1.7
Previous	1.2	2.2	1.9	...
GDP chain-weighted price index	1.7	2.0	1.7	1.6
Previous	1.7	2.0	1.7	...
ECI for compensation of private industry workers ¹	4.0	4.1	4.1	4.2
Previous	4.0	4.1	4.0	...
NFB compensation per hour	5.4	3.6	4.1	4.2
Previous	5.3	4.1	4.0	...
Prices of core nonfuel imports	1.6	3.7	.2	.1
Previous	1.6	3.5	-.3	...

1. December to December.

... Not applicable.

Productivity and the labor market. We believe that, after the current period of below-average employment gains, employers will need to hire workers at a robust pace early next year. We anticipate monthly payroll gains on the order of 290,000 jobs in the first part of 2005—and increases in output per hour well below the rise in structural labor productivity—before payroll increases settle in at a more sustainable pace. As labor market conditions improve, we expect individuals who are currently out of the labor force to be drawn back. Thus, the rapid job gains will have a muted effect on the unemployment rate, which should hold fairly steady next year before falling to near 5 percent by the end of our projection period.

Alternative Scenarios(Percent change, annual rate, from end of preceding period,
except as noted)

Measure and scenario	2004		2005		2006
	H1	H2	H1	H2	
<i>Real GDP</i>					
Baseline	3.9	3.8	3.7	3.9	4.0
Surging demand	3.9	4.8	4.6	4.4	4.1
Higher saving rate	3.9	3.4	2.8	2.6	2.4
Near-term weakness	3.9	2.5	3.2	4.3	4.4
Less room to grow	3.9	3.9	3.8	4.0	4.1
Lower markup	3.9	3.9	3.8	3.9	3.7
Market-based funds rate	3.9	3.7	3.6	3.6	3.5
<i>Civilian unemployment rate¹</i>					
Baseline	5.6	5.5	5.4	5.3	5.1
Surging demand	5.6	5.3	5.0	4.7	4.5
Higher saving rate	5.6	5.6	5.7	5.9	6.6
Near-term weakness	5.6	5.7	5.9	5.7	5.1
Less room to grow	5.6	5.3	5.1	5.0	4.6
Lower markup	5.6	5.5	5.3	5.2	5.1
Market-based funds rate	5.6	5.5	5.4	5.4	5.5
<i>PCE prices excluding food and energy</i>					
Baseline	1.9	1.2	1.5	1.4	1.3
Surging demand	1.9	1.2	1.6	1.5	1.5
Higher saving rate	1.9	1.2	1.5	1.3	.9
Near-term weakness	1.9	1.2	1.4	1.3	1.2
Less room to grow	1.9	1.3	1.7	1.7	1.8
Lower markup	1.9	.8	1.0	.8	1.0
Market-based funds rate	1.9	1.2	1.5	1.3	1.2

1. Average for the final quarter of the period.

funds rate that is being held down relative to historical norms. In this scenario, we assume that the forces holding down the equilibrium real rate dissipate rapidly. The surge in demand resulting from the greater effective monetary stimulus causes economic slack to disappear much more rapidly than it does in the baseline projection. All told, real GDP grows nearly 4-3/4 percent at an annual rate in the second half of this year and about 4-1/2 percent in 2005, before moderating to 4 percent in 2006; the unemployment rate falls to 4-1/2 percent by the end of 2006. The swing to tight labor and product markets offsets the restraint on aggregate prices in the baseline from falling oil prices and

**Selected Greenbook Projections and 70 Percent
Confidence Intervals Derived from Historical Forecast
Errors and FRB/US Simulations**

Measure	2004	2005	2006
<i>Real GDP</i> (percent change, Q4 to Q4)			
Projection	3.9	3.8	4.0
Confidence interval			
Greenbook forecast errors ¹	2.9–4.8	1.8–5.8	2.3–5.8
FRB/US stochastic simulations	3.2–4.5	2.4–5.6	2.3–6.0
<i>Civilian unemployment rate</i> (percent, Q4)			
Projection	5.5	5.3	5.1
Confidence interval			
Greenbook forecast errors ¹	5.2–5.8	4.5–6.1	3.9–6.3
FRB/US stochastic simulations	5.2–5.8	4.5–6.1	3.9–6.1
<i>PCE prices</i> <i>excluding food and energy</i> (percent change, Q4 to Q4)			
Projection	1.6	1.4	1.3
Confidence interval			
Greenbook forecast errors ²	1.3–1.9	.6–2.2	.3–2.4
FRB/US stochastic simulations	1.3–1.8	.7–2.2	.5–2.2

NOTE. Shocks underlying stochastic simulations are randomly drawn from the 1978–2003 set of model equation residuals.

1. 1978–2003.

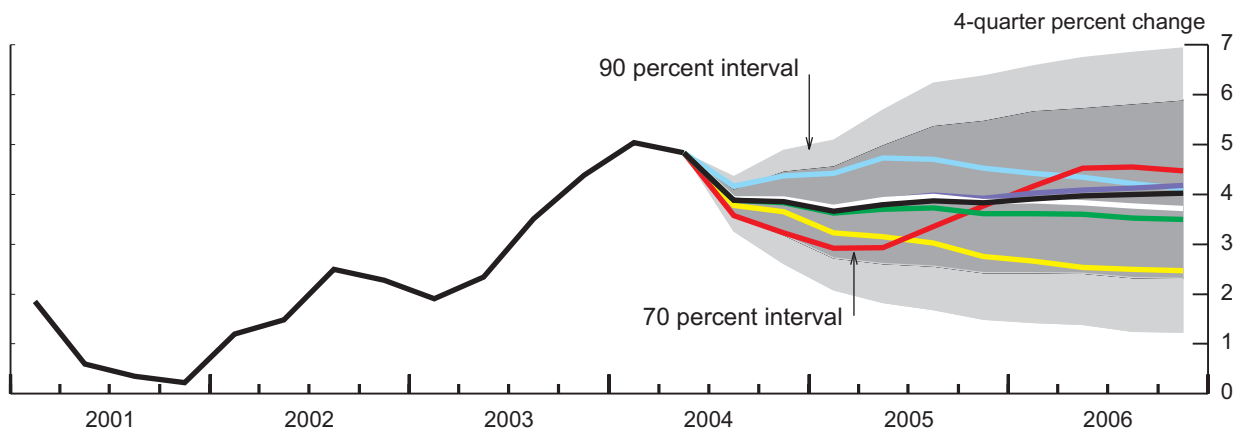
2. 1981–2003.

Forecast Confidence Intervals and Alternative Scenarios

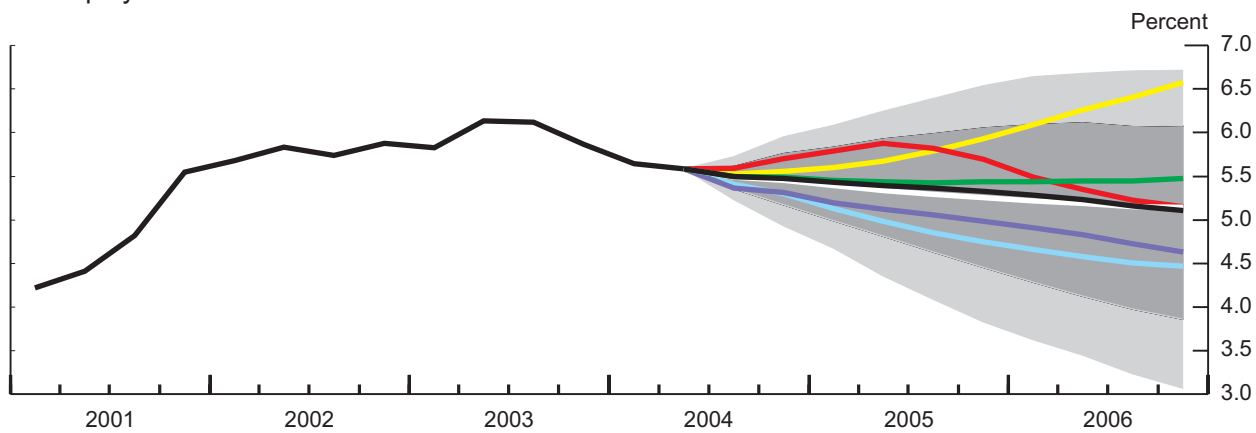
Confidence Intervals Based on FRB/US Stochastic Simulations

- | | |
|---------------------------|-------------------------|
| Greenbook baseline | Less room to grow |
| Surging demand | Lower markup |
| Rising saving rate | Market-based funds rate |
| Weaker near-term activity | |

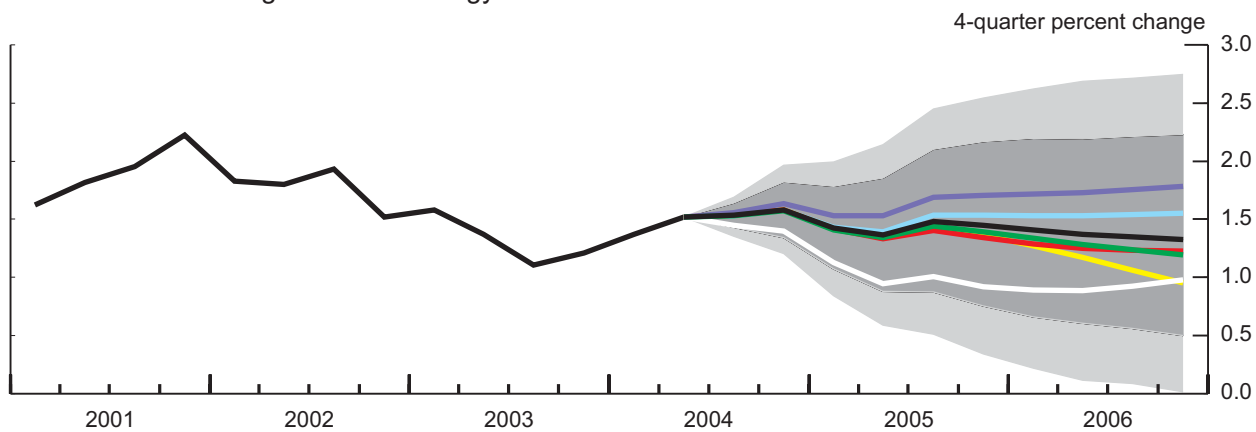
Real GDP



Unemployment Rate



PCE Prices excluding Food and Energy



STAFF PROJECTIONS OF CHANGES IN GDP, PRICES, AND UNEMPLOYMENT
(Percent, annual rate)

		Nominal GDP		Real GDP		GDP chain-weighted price index		Consumer price index ¹		Unemployment rate ²	
Interval		08/05/04	09/15/04	08/05/04	09/15/04	08/05/04	09/15/04	08/05/04	09/15/04	08/05/04	09/15/04
ANNUAL											
2002		3.5	3.5	1.9	1.9	1.7	1.7	1.6	1.6	5.8	5.8
2003		4.9	4.9	3.0	3.0	1.8	1.8	2.3	2.3	6.0	6.0
2004		6.5	6.4	4.4	4.4	2.0	2.0	2.6	2.5	5.6	5.5
2005		5.5	5.5	3.9	3.8	1.6	1.6	1.7	1.7	5.4	5.4
2006			5.7		4.0		1.6		1.5		5.2
QUARTERLY											
2003	Q1	4.9	4.9	1.9	1.9	2.7	2.7	3.8	3.8	5.8	5.8
	Q2	5.3	5.3	4.1	4.1	1.1	1.1	0.7	0.7	6.1	6.1
	Q3	8.8	8.8	7.4	7.4	1.4	1.4	2.4	2.4	6.1	6.1
	Q4	5.7	5.7	4.2	4.2	1.6	1.6	0.7	0.7	5.9	5.9
2004	Q1	7.4	7.4	4.5	4.5	2.8	2.8	3.5	3.5	5.6	5.6
	Q2	6.4	6.6	3.1	3.3	3.2	3.2	4.8	4.8	5.6	5.6
	Q3	4.9	4.5	3.9	3.6	0.9	0.8	2.1	1.8	5.6	5.5
	Q4	6.0	5.2	4.7	4.1	1.2	1.1	1.3	1.1	5.5	5.5
2005	Q1	5.9	5.8	3.9	3.7	1.9	2.1	1.2	1.6	5.4	5.4
	Q2	5.2	5.5	3.6	3.8	1.6	1.7	1.5	1.5	5.4	5.4
	Q3	5.2	5.5	3.6	3.9	1.6	1.5	1.5	1.5	5.4	5.4
	Q4	5.1	5.5	3.6	3.9	1.5	1.5	1.6	1.5	5.3	5.3
2006	Q1		6.0		4.0		1.9		1.5		5.3
	Q2		5.6		4.0		1.5		1.5		5.2
	Q3		5.6		4.0		1.5		1.5		5.2
	Q4		5.5		4.0		1.4		1.5		5.1
TWO-QUARTER ³											
2003	Q2	5.1	5.1	3.0	3.0	1.9	1.9	2.2	2.2	0.2	0.2
	Q4	7.2	7.2	5.8	5.8	1.5	1.5	1.5	1.5	-0.2	-0.2
2004	Q2	6.9	7.0	3.8	3.9	3.0	3.0	4.2	4.2	-0.3	-0.3
	Q4	5.4	4.8	4.3	3.8	1.0	1.0	1.7	1.5	-0.1	-0.1
2005	Q2	5.6	5.7	3.7	3.7	1.8	1.9	1.3	1.6	-0.1	-0.1
	Q4	5.2	5.5	3.6	3.9	1.5	1.5	1.6	1.5	-0.1	-0.1
2006	Q2		5.8		4.0		1.7		1.5		-0.1
	Q4		5.5		4.0		1.4		1.5		-0.1
FOUR-QUARTER ⁴											
2002	Q4	3.8	3.8	2.3	2.3	1.6	1.6	2.2	2.2	0.3	0.3
2003	Q4	6.2	6.2	4.4	4.4	1.7	1.7	1.9	1.9	0.0	0.0
2004	Q4	6.1	5.9	4.1	3.9	2.0	2.0	2.9	2.8	-0.4	-0.4
2005	Q4	5.4	5.6	3.6	3.8	1.7	1.7	1.4	1.5	-0.1	-0.1
2006	Q4		5.7		4.0		1.6		1.5		-0.2

1. For all urban consumers.

2. Level, except as noted.

3. Percent change from two quarters earlier; for unemployment rate, change in percentage points.

4. Percent change from four quarters earlier; for unemployment rate, change in percentage points.

Strictly Confidential <FR>
Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, ANNUAL VALUES
(Seasonally adjusted annual rate)

September 15, 2004

		- - - - - Projected - - - - -								
Item	Units ¹	1998	1999	2000	2001	2002	2003	2004	2005	2006
Expenditures										
Nominal GDP	Bill. \$	8747.0	9268.4	9817.0	10128.0	10487.0	11004.0	11713.1	12354.4	13053.1
Real GDP	Bill. Ch. \$	9066.9	9470.3	9817.0	9890.7	10074.8	10381.3	10837.6	11248.3	11695.6
Real GDP	% change	4.5	4.7	2.2	0.2	2.3	4.4	3.9	3.8	4.0
Gross domestic purchases		5.5	5.5	3.0	0.4	3.1	4.3	4.2	3.9	4.5
Final sales		4.8	4.2	2.9	1.5	1.2	4.5	3.5	4.0	4.0
Priv. dom. final purchases		6.4	5.3	4.3	1.0	1.7	4.9	4.2	4.5	4.8
Personal cons. expenditures		5.4	4.9	4.1	2.8	2.5	3.8	3.4	3.9	4.1
Durables		14.4	7.3	4.7	10.8	1.5	9.9	4.9	6.9	5.9
Nondurables		4.7	4.9	3.0	1.9	2.3	4.6	3.5	4.2	4.8
Services		3.8	4.4	4.5	1.6	2.9	2.2	3.0	3.2	3.4
Business fixed investment		10.9	7.7	7.8	-9.6	-6.0	9.4	9.9	9.4	9.9
Equipment & Software		13.5	10.8	7.5	-9.0	-2.2	12.1	12.2	10.5	11.8
Nonres. structures		4.0	-0.9	8.8	-11.1	-16.1	1.5	2.5	6.0	3.9
Residential structures		10.3	3.6	-1.8	1.4	6.9	12.0	4.8	2.5	3.9
Exports		2.6	5.6	6.5	-11.9	3.5	6.1	8.4	7.2	6.4
Imports		11.0	12.1	11.2	-7.6	9.7	4.9	9.7	6.8	8.6
Gov't. cons. & investment		3.3	4.2	0.4	5.0	3.8	2.2	2.5	2.4	2.7
Federal		0.1	4.2	-2.2	6.4	8.2	5.5	4.5	2.2	2.5
Defense		-1.2	4.3	-3.5	6.5	8.5	8.5	5.1	2.2	2.6
State & local		5.1	4.2	1.7	4.2	1.6	0.4	1.3	2.5	2.8
Change in bus. inventories	Bill. Ch. \$	72.6	68.9	56.5	-31.7	11.7	-0.8	44.6	35.9	22.4
Nonfarm		71.2	71.5	57.8	-31.8	13.5	-1.1	42.5	34.9	21.2
Net exports		-203.8	-296.2	-379.5	-399.1	-472.1	-518.5	-576.2	-609.7	-679.4
Nominal GDP	% change	5.7	6.3	4.6	2.7	3.8	6.2	5.9	5.6	5.7
GDP Gap ²	%	-1.5	-2.4	-2.5	0.2	1.6	2.2	1.4	0.9	0.3
Employment and Production										
Nonfarm payroll employment	Millions	125.9	129.0	131.8	131.8	130.3	129.9	131.3	134.0	136.6
Unemployment rate	%	4.5	4.2	4.0	4.7	5.8	6.0	5.5	5.4	5.2
Industrial prod. index	% change	4.4	4.9	2.3	-5.2	1.3	1.5	5.5	4.8	4.5
Capacity util. rate - mfg.	%	82.0	81.4	81.1	75.4	73.9	73.4	76.4	78.8	80.6
Housing starts	Millions	1.62	1.64	1.57	1.60	1.70	1.85	1.95	1.95	1.96
Light motor vehicle sales		15.52	16.90	17.35	17.12	16.79	16.62	16.73	17.47	18.02
North Amer. produced		13.48	14.41	14.48	14.04	13.49	13.32	13.36	13.95	14.45
Other		2.03	2.49	2.87	3.08	3.30	3.31	3.37	3.52	3.57
Income and Saving										
Nominal GNP	Bill. \$	8768.3	9302.2	9855.9	10171.6	10514.1	11059.2	11749.6	12351.7	13014.9
Nominal GNP	% change	5.5	6.5	4.7	2.9	3.5	6.5	5.2	5.4	5.3
Nominal personal income		7.0	5.5	7.1	2.2	1.9	4.6	6.6	5.3	6.6
Real disposable income		5.6	2.8	4.4	1.2	2.9	3.9	4.3	3.4	5.1
Personal saving rate	%	4.3	2.4	2.3	1.8	2.0	1.4	1.4	1.5	2.6
Corp. profits, IVA & CCAdj.	% change	-10.0	9.6	-8.6	-0.2	15.4	23.3	4.3	1.0	-0.5
Profit share of GNP	%	9.1	9.2	8.3	7.5	8.3	9.2	9.9	9.6	9.2
Excluding FR Banks	%	8.9	8.9	8.0	7.3	8.1	9.1	9.7	9.4	9.0
Federal surpl./deficit	Bill. \$	38.8	103.6	189.5	46.7	-254.5	-364.5	-378.0	-255.8	-325.2
State & local surpl./def.		52.0	50.4	50.0	4.8	-25.0	-3.2	9.5	13.1	19.1
Ex. social ins. funds		50.3	48.7	47.9	2.2	-26.6	-4.3	8.2	11.6	17.6
Gross natl. saving rate	%	18.2	18.0	18.0	16.3	14.1	13.5	13.6	13.9	14.0
Net natl. saving rate		7.4	6.9	6.7	4.2	2.0	1.4	2.0	2.4	2.6
Prices and Costs										
GDP chn.-wt. price index	% change	1.1	1.6	2.2	2.4	1.6	1.7	2.0	1.7	1.6
Gross Domestic Purchases										
chn.-wt. price index		0.7	2.0	2.4	1.6	1.8	1.8	2.5	1.4	1.3
PCE chn.-wt. price index		0.9	2.1	2.3	1.7	1.8	1.7	2.2	1.3	1.3
Ex. food and energy		1.4	1.6	1.5	2.2	1.5	1.2	1.6	1.4	1.3
CPI		1.5	2.6	3.4	1.8	2.2	1.9	2.8	1.5	1.5
Ex. food and energy		2.3	2.0	2.6	2.7	2.0	1.2	2.0	1.8	1.7
ECI, hourly compensation ³		3.5	3.4	4.4	4.2	3.2	4.0	4.1	4.1	4.2
Nonfarm business sector										
Output per hour		2.7	3.4	2.1	3.3	3.5	5.6	2.2	1.8	2.6
Compensation per Hour		5.5	5.2	6.4	3.5	2.9	5.4	3.6	4.1	4.2
Unit labor cost		2.7	1.7	4.3	0.3	-0.6	-0.2	1.3	2.2	1.5

1. Changes are from fourth quarter to fourth quarter.

2. Percent difference between potential and actual. A positive number indicates that the economy is operating below potential.

3. Private-industry workers.

Strictly Confidential <FR>
Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES
(Seasonally adjusted, annual rate except as noted)

September 15, 2004

		Projected									
Item	Units	2002 Q1	2002 Q2	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 Q3	2003 Q4	2004 Q1	2004 Q2
Expenditures											
Nominal GDP	Bill. \$	10338.2	10445.7	10546.5	10617.5	10744.6	10884.0	11116.7	11270.9	11472.6	11657.5
Real GDP	Bill. Ch. \$	9993.5	10052.6	10117.3	10135.9	10184.4	10287.4	10472.8	10580.7	10697.5	10784.0
Real GDP	% change	3.4	2.4	2.6	0.7	1.9	4.1	7.4	4.2	4.5	3.3
Gross domestic purchases		4.4	2.8	2.9	2.4	1.7	4.4	6.4	4.7	5.0	4.2
Final sales		0.3	1.8	2.0	0.7	2.4	5.2	6.8	3.7	3.3	2.5
Priv. dom. final purchases		0.7	1.7	2.4	1.9	2.6	5.1	7.2	4.8	4.2	3.6
Personal cons. expenditures		1.8	2.8	2.9	2.5	2.7	3.9	5.0	3.6	4.1	1.5
Durables		-8.5	4.4	14.0	-2.4	-0.1	20.6	16.5	3.9	2.2	0.1
Nondurables		3.8	0.8	-0.6	5.3	5.0	1.6	6.9	5.1	6.7	0.2
Services		3.3	3.5	2.4	2.2	2.1	1.8	1.9	2.8	3.3	2.5
Business fixed investment		-9.7	-9.6	-1.1	-3.2	-0.2	11.8	15.7	11.0	4.2	12.0
Equipment & Software		-6.3	-4.5	4.6	-2.0	4.5	11.0	21.7	12.0	8.0	13.6
Nonres. structures		-18.5	-22.6	-16.0	-6.6	-13.0	14.5	-1.3	7.9	-7.6	6.8
Residential structures		9.2	11.4	2.8	4.2	7.6	9.0	22.5	9.6	5.0	16.3
Exports		4.7	11.0	3.1	-4.2	-1.5	-1.6	11.3	17.5	7.3	7.3
Imports		12.5	11.4	5.4	9.6	-1.9	2.5	2.9	17.1	10.6	12.7
Gov't. cons. & investment		4.7	4.4	2.1	4.0	0.2	7.2	0.1	1.6	2.5	2.3
Federal		8.2	12.8	2.9	9.2	0.3	22.1	-3.3	4.8	7.1	2.7
Defense		5.9	11.4	3.4	13.5	-2.8	38.4	-7.7	11.6	10.6	1.8
State & local		2.9	0.3	1.7	1.4	0.1	-0.5	2.2	-0.1	-0.0	2.1
Change in bus. inventories	Bill. Ch. \$	-7.4	7.9	22.7	23.8	9.6	-17.6	-3.5	8.6	40.0	61.8
Nonfarm		-11.9	16.1	24.6	25.3	9.6	-15.7	-2.7	4.6	34.5	59.6
Net exports		-444.9	-458.1	-469.8	-515.4	-511.7	-525.2	-508.7	-528.3	-550.1	-580.5
Nominal GDP	% change	4.4	4.2	3.9	2.7	4.9	5.3	8.8	5.7	7.4	6.6
GDP Gap ¹	%	1.2	1.4	1.6	2.3	2.7	2.6	1.8	1.7	1.4	1.5
Employment and Production											
Nonfarm payroll employment	Millions	130.4	130.4	130.3	130.2	130.0	129.9	129.8	130.0	130.4	131.1
Unemployment rate	%	5.7	5.8	5.7	5.9	5.8	6.1	6.1	5.9	5.6	5.6
Industrial prod. index	% change	1.9	4.2	1.2	-1.9	0.9	-4.0	3.8	5.6	6.6	4.8
Capacity util. rate - mfg.	%	73.7	74.1	74.2	73.5	73.5	72.7	73.2	74.1	75.1	76.1
Housing starts	Millions	1.72	1.68	1.70	1.74	1.74	1.75	1.88	2.04	1.94	1.92
Light motor vehicle sales		16.60	16.54	17.41	16.60	16.09	16.38	17.23	16.80	16.51	16.54
North Amer. produced		13.29	13.29	14.08	13.31	12.71	13.10	13.89	13.57	13.25	13.15
Other		3.32	3.25	3.32	3.29	3.38	3.28	3.34	3.23	3.26	3.39
Income and Saving											
Nominal GNP	Bill. \$	10361.7	10461.6	10571.7	10661.2	10781.3	10929.0	11168.3	11358.1	11546.1	11693.7
Nominal GNP	% change	2.4	3.9	4.3	3.4	4.6	5.6	9.1	7.0	6.8	5.2
Nominal personal income		2.2	4.3	-0.1	1.1	3.8	4.7	4.6	5.3	5.0	6.1
Real disposable income		10.8	2.7	-1.7	0.2	1.8	4.3	8.2	1.4	2.4	2.5
Personal saving rate	%	2.7	2.7	1.6	1.2	1.0	1.1	1.9	1.3	1.0	1.2
Corp. profits, IVA & CCAdj.	% change	24.8	15.2	3.6	19.1	-1.5	36.7	32.0	30.2	13.6	1.6
Profit share of GNP	%	8.1	8.3	8.3	8.6	8.5	9.0	9.5	9.9	10.1	10.0
Excluding FR Banks		7.9	8.1	8.1	8.4	8.3	8.8	9.3	9.8	9.9	9.9
Federal surpl./deficit	Bill. \$	-208.5	-251.6	-255.1	-302.7	-281.6	-364.4	-433.0	-379.2	-391.0	-382.0
State & local surpl./def.		-28.8	-23.6	-21.3	-26.3	-49.0	-5.7	6.5	35.3	11.8	16.5
Ex. social ins. funds		-30.8	-25.3	-22.8	-27.6	-50.1	-6.7	5.4	34.1	10.6	15.1
Gross natl. saving rate	%	15.0	14.6	13.7	13.2	12.8	13.1	13.6	14.3	13.6	13.8
Net natl. saving rate		2.9	2.5	1.5	0.9	0.4	0.9	1.6	2.5	2.1	2.3
Prices and Costs											
GDP chn.-wt. price index	% change	1.4	1.5	1.7	2.0	2.7	1.1	1.4	1.6	2.8	3.2
Gross Domestic Purchases											
chn.-wt. price index		1.2	2.5	1.8	1.9	3.7	0.4	1.7	1.4	3.4	3.5
PCE chn.-wt. price index		0.9	2.9	2.0	1.4	3.2	0.7	1.6	1.2	3.3	3.2
Ex. food and energy		1.2	2.0	2.0	0.9	1.5	1.1	0.9	1.3	2.1	1.7
CPI		1.4	3.4	2.2	2.0	3.8	0.7	2.4	0.7	3.5	4.8
Ex. food and energy		2.1	2.3	2.1	1.7	1.3	1.0	1.5	0.8	1.9	2.9
ECI, hourly compensation ²		3.6	4.4	2.5	3.3	5.5	3.4	4.4	3.1	4.3	4.0
Nonfarm business sector											
Output per hour		6.9	1.1	4.5	1.6	3.7	6.7	9.0	3.1	3.7	3.0
Compensation per hour		5.5	3.4	1.5	1.2	5.4	5.7	6.1	4.4	2.0	4.4
Unit labor cost		-1.4	2.3	-2.9	-0.3	1.6	-1.0	-2.7	1.2	-1.6	1.3

1. Percent difference between potential and actual. A positive number indicates that the economy is operating below potential.
2. Private-industry workers.

Strictly Confidential <FR>
Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES
(Seasonally adjusted, annual rate except as noted)

September 15, 2004

		Projected									
Item	Units	2004 Q3	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4	2006 Q1	2006 Q2	2006 Q3	2006 Q4
EXPENDITURES											
Nominal GDP	Bill. \$	11785.7	11936.5	12106.6	12270.3	12436.4	12604.2	12788.5	12964.4	13141.1	13318.4
Real GDP	Bill. Ch. \$	10879.7	10989.3	11089.0	11193.1	11301.2	11409.9	11523.1	11637.2	11752.7	11869.4
Real GDP	% change	3.6	4.1	3.7	3.8	3.9	3.9	4.0	4.0	4.0	4.0
Gross domestic purchases		3.5	4.3	3.7	3.6	4.1	4.3	4.7	4.1	4.4	4.5
Final sales		4.4	3.9	2.9	4.7	4.4	4.0	3.7	4.5	4.0	3.8
Priv. dom. final purchases		4.2	4.8	3.2	5.0	5.0	4.9	4.8	4.9	4.8	4.7
Personal cons. expenditures		3.7	4.1	4.0	4.0	3.9	3.9	4.1	4.1	4.1	4.1
Durables		12.4	5.4	7.4	6.9	6.4	6.8	6.0	6.1	5.5	6.1
Nondurables		3.2	3.9	4.0	4.3	4.3	4.2	4.8	4.8	4.8	4.8
Services		2.2	3.9	3.3	3.2	3.1	3.2	3.5	3.4	3.5	3.4
Business fixed investment		10.9	12.6	-0.1	12.7	13.0	12.7	10.1	10.1	10.0	9.6
Equipment & Software		12.9	14.5	-1.4	15.1	14.8	14.2	11.6	11.9	12.0	11.6
Nonres. structures		4.7	6.7	4.0	5.1	7.1	7.8	5.0	4.1	3.6	3.0
Residential structures		-0.8	-0.5	0.2	3.3	4.1	2.5	3.7	5.4	4.2	2.2
Exports		8.6	10.6	5.5	7.5	7.4	8.5	5.2	6.4	6.3	7.7
Imports		5.9	9.7	5.1	5.1	7.5	9.6	9.6	6.2	8.4	10.1
Gov't. cons. & investment		3.9	1.2	2.0	2.5	2.5	2.5	2.5	2.6	2.6	2.9
Federal		8.0	0.5	1.7	2.8	2.3	2.0	2.1	2.4	2.3	3.1
Defense		9.2	-0.7	2.2	2.3	2.3	1.9	2.0	2.4	2.4	3.5
State & local		1.6	1.7	2.2	2.4	2.5	2.7	2.8	2.8	2.8	2.8
Change in bus. inventories	Bill. Ch. \$	35.9	40.5	61.4	36.5	24.8	21.0	29.9	17.8	17.9	23.8
Nonfarm		36.2	39.8	60.4	35.4	23.7	19.9	28.7	16.7	16.8	22.7
Net exports		-581.5	-592.7	-599.0	-599.7	-611.2	-628.8	-656.5	-665.9	-685.8	-709.6
Nominal GDP	% change	4.5	5.2	5.8	5.5	5.5	5.5	6.0	5.6	5.6	5.5
GDP Gap ¹	%	1.4	1.2	1.1	1.0	0.9	0.7	0.6	0.4	0.2	0.1
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	131.5	132.1	132.9	133.7	134.4	135.0	135.7	136.3	137.0	137.6
Unemployment rate	%	5.5	5.5	5.4	5.4	5.4	5.3	5.3	5.2	5.2	5.1
Industrial prod. index	% change	4.0	6.5	5.1	4.9	4.9	4.5	4.9	4.4	4.3	4.6
Capacity util. rate - mfg.	%	76.8	77.5	78.0	78.6	79.1	79.5	80.1	80.5	80.8	81.2
Housing starts	Millions	1.98	1.94	1.94	1.95	1.95	1.95	1.96	1.96	1.97	1.97
Light motor vehicle sales		16.89	16.98	17.14	17.37	17.60	17.76	17.89	18.01	18.03	18.15
North Amer. produced		13.57	13.48	13.64	13.86	14.08	14.22	14.35	14.45	14.45	14.55
Other		3.32	3.50	3.50	3.51	3.52	3.54	3.54	3.56	3.58	3.60
INCOME AND SAVING											
Nominal GNP	Bill. \$	11815.1	11943.5	12112.7	12268.2	12431.5	12594.2	12765.4	12933.1	13099.5	13261.7
Nominal GNP	% change	4.2	4.4	5.8	5.2	5.4	5.3	5.5	5.4	5.2	5.0
Nominal personal income		3.8	11.5	2.4	6.3	6.3	6.3	7.9	6.3	6.2	6.0
Real disposable income		2.4	10.0	-0.3	4.6	4.6	4.6	6.2	4.9	4.7	4.5
Personal saving rate	%	0.9	2.3	1.3	1.4	1.6	1.8	2.3	2.5	2.7	2.8
Corp. profits, IVA & CCAdj.	% change	-15.0	20.8	3.6	-1.8	1.3	1.0	1.5	0.6	-0.7	-3.2
Profit share of GNP	%	9.5	9.9	9.8	9.6	9.5	9.4	9.4	9.2	9.1	8.9
Excluding FR Banks		9.3	9.7	9.6	9.5	9.4	9.3	9.2	9.1	9.0	8.8
Federal surpl./deficit	Bill. \$	-385.9	-352.9	-278.7	-255.6	-240.5	-248.6	-313.0	-321.3	-330.6	-336.0
State & local surpl./def.		-3.2	13.0	13.0	10.3	12.9	16.2	17.2	17.7	19.1	22.5
Ex. social ins. funds		-4.6	11.5	11.5	8.8	11.4	14.7	15.7	16.2	17.6	21.0
Gross natl. saving rate	%	13.4	13.6	13.7	13.8	13.9	14.0	13.9	14.1	14.1	14.0
Net natl. saving rate		1.3	2.1	2.3	2.4	2.5	2.6	2.5	2.7	2.7	2.6
PRICES AND COSTS											
GDP chn.-wt. price index	% change	0.8	1.1	2.1	1.7	1.5	1.5	1.9	1.5	1.5	1.4
Gross Domestic Purchases											
chn.-wt. price index		1.6	1.4	1.8	1.4	1.3	1.3	1.6	1.2	1.2	1.2
PCE chn.-wt. price index		1.3	1.2	1.4	1.3	1.3	1.3	1.3	1.2	1.3	1.3
Ex. food and energy		1.0	1.5	1.5	1.5	1.4	1.4	1.3	1.3	1.3	1.3
CPI		1.8	1.1	1.6	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Ex. food and energy		1.5	1.8	1.9	1.9	1.8	1.8	1.7	1.7	1.7	1.7
ECI, hourly compensation ²		4.0	4.0	4.0	4.0	4.1	4.1	4.1	4.1	4.2	4.2
Nonfarm business sector											
Output per hour		0.6	2.0	1.0	1.7	2.3	2.4	2.6	2.6	2.6	2.6
Compensation per hour		4.2	4.0	4.2	4.1	4.1	4.1	4.2	4.1	4.2	4.2
Unit labor cost		3.6	2.0	3.1	2.4	1.8	1.6	1.6	1.5	1.5	1.5

1. Percent difference between potential and actual. A positive number indicates that the economy is operating below potential.
2. Private-industry workers.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	- - Projected - -										Projected			
	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 Q3	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4	02Q4/ 01Q4	03Q4/ 02Q4	04Q4/ 03Q4	
Real GDP	2.6	0.7	1.9	4.1	7.4	4.2	4.5	3.3	3.6		2.3	4.4	3.9	
Gross dom. purchases	3.0	2.4	1.8	4.6	6.8	4.9	5.3	4.4	3.6		3.2	4.5	4.4	
Final sales	2.0	0.7	2.4	5.1	6.8	3.7	3.3	2.5	4.3		1.2	4.5	3.5	
Priv. dom. final purchases	2.1	1.6	2.2	4.3	6.2	4.1	3.6	3.1	3.6		1.4	4.2	3.6	
Personal cons. expenditures	2.0	1.7	1.8	2.7	3.6	2.5	2.9	1.1	2.6		1.8	2.7	2.4	
Durables	1.2	-0.2	-0.0	1.6	1.4	0.3	0.2	0.0	1.0		0.1	0.8	0.4	
Nondurables	-0.1	1.0	1.0	0.3	1.4	1.0	1.3	0.1	0.7		0.5	0.9	0.7	
Services	1.0	0.9	0.9	0.8	0.8	1.2	1.4	1.0	0.9		1.2	0.9	1.2	
Business fixed investment	-0.1	-0.3	-0.0	1.1	1.5	1.1	0.4	1.2	1.1		-0.6	0.9	1.0	
Equipment & Software	0.3	-0.2	0.3	0.8	1.5	0.9	0.6	1.0	1.0		-0.2	0.9	0.9	
Nonres. structures	-0.5	-0.2	-0.3	0.3	-0.0	0.2	-0.2	0.2	0.1		-0.5	0.0	0.1	
Residential structures	0.1	0.2	0.4	0.4	1.1	0.5	0.3	0.8	-0.0		0.3	0.6	0.3	
Net exports	-0.4	-1.7	0.1	-0.5	0.6	-0.7	-0.8	-1.1	-0.0		-0.9	-0.1	-0.6	
Exports	0.3	-0.4	-0.2	-0.2	1.0	1.6	0.7	0.7	0.8		0.3	0.6	0.8	
Imports	-0.7	-1.3	0.3	-0.3	-0.4	-2.2	-1.5	-1.8	-0.9		-1.3	-0.7	-1.4	
Government cons. & invest.	0.4	0.8	0.1	1.4	0.0	0.3	0.5	0.4	0.7		0.7	0.4	0.5	
Federal	0.2	0.6	0.0	1.4	-0.2	0.3	0.5	0.2	0.5		0.5	0.4	0.3	
Defense	0.1	0.5	-0.1	1.5	-0.4	0.5	0.5	0.1	0.4		0.3	0.4	0.2	
Nondefense	0.1	0.0	0.2	-0.1	0.1	-0.2	0.0	0.1	0.1		0.2	-0.0	0.1	
State and local	0.2	0.2	0.0	-0.1	0.3	-0.0	0.0	0.3	0.2		0.2	0.1	0.2	
Change in bus. inventories	0.6	0.1	-0.5	-1.0	0.6	0.5	1.2	0.8	-0.7		1.1	-0.1	0.4	
Nonfarm	0.4	0.1	-0.5	-0.9	0.5	0.3	1.1	0.9	-0.8		1.0	-0.2	0.3	
Farm	0.2	0.0	0.1	-0.1	0.1	0.2	0.1	-0.1	0.1		0.0	0.1	0.0	

Note: Components may not sum to totals because of rounding.

Item	Projected												Projected			
	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4	2006 Q1	2006 Q2	2006 Q3	2006 Q4	04Q4/ 03Q4	05Q4/ 04Q4	06Q4/ 05Q4	04Q4/ 03Q4	05Q4/ 04Q4	06Q4/ 05Q4	
Real GDP	4.1	3.7	3.8	3.9	3.9	4.0	4.0	4.0	4.0	3.9	3.8	4.0	3.9	3.8	4.0	
Gross dom. purchases	4.5	3.9	3.8	4.3	4.5	4.9	4.3	4.7	4.8	4.4	4.1	4.7	4.4	4.1	4.7	
Final sales	3.9	2.9	4.7	4.3	4.0	3.7	4.4	4.0	3.8	3.5	4.0	4.0	3.5	4.0	4.0	
Priv. dom. final purchases	4.1	2.8	4.2	4.3	4.2	4.2	4.2	4.2	4.0	3.6	3.9	4.2	3.6	3.9	4.2	
Personal cons. expenditures	2.9	2.8	2.8	2.7	2.7	2.9	2.9	2.9	2.9	2.4	2.7	2.9	2.4	2.7	2.9	
Durables	0.5	0.6	0.6	0.5	0.6	0.5	0.5	0.5	0.5	0.4	0.6	0.5	0.4	0.6	0.5	
Nondurables	0.8	0.8	0.9	0.9	0.8	0.9	0.9	1.0	1.0	0.7	0.8	1.0	0.7	0.8	1.0	
Services	1.6	1.4	1.3	1.3	1.3	1.4	1.4	1.4	1.4	1.2	1.3	1.4	1.2	1.3	1.4	
Business fixed investment	1.3	-0.0	1.3	1.3	1.3	1.1	1.1	1.1	1.0	1.0	1.0	1.1	1.0	1.0	1.1	
Equipment & Software	1.1	-0.1	1.1	1.2	1.1	0.9	1.0	1.0	1.0	0.9	0.8	1.0	0.9	0.8	1.0	
Nonres. structures	0.2	0.1	0.1	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	
Residential structures	-0.0	0.0	0.2	0.2	0.1	0.2	0.3	0.2	0.1	0.3	0.1	0.2	0.3	0.1	0.2	
Net exports	-0.4	-0.2	-0.0	-0.4	-0.6	-0.9	-0.3	-0.6	-0.7	-0.6	-0.3	-0.7	-0.6	-0.3	-0.7	
Exports	1.0	0.6	0.8	0.7	0.9	0.5	0.7	0.7	0.8	0.8	0.7	0.7	0.8	0.7	0.7	
Imports	-1.4	-0.8	-0.8	-1.1	-1.4	-1.5	-1.0	-1.3	-1.5	-1.4	-1.1	-1.3	-1.4	-1.1	-1.3	
Government cons. & invest.	0.2	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.4	0.5	0.5	0.4	0.5	
Federal	0.0	0.1	0.2	0.2	0.1	0.1	0.2	0.2	0.2	0.3	0.2	0.2	0.3	0.2	0.2	
Defense	-0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.1	0.1	0.2	0.1	0.1	
Nondefense	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	
State and local	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.3	0.3	0.2	0.3	0.3	
Change in bus. inventories	0.2	0.7	-0.9	-0.4	-0.1	0.3	-0.4	0.0	0.2	0.4	-0.2	0.0	0.4	-0.2	0.0	
Nonfarm	0.1	0.7	-0.9	-0.4	-0.1	0.3	-0.4	0.0	0.2	0.3	-0.2	0.0	0.3	-0.2	0.0	
Farm	0.0	0.0	0.0	0.0	0.0	-0.0	-0.0	0.0	-0.0	0.0	0.0	-0.0	0.0	0.0	-0.0	

Note: Components may not sum to totals because of rounding.

Staff Projections of Federal Sector Accounts and Related Items
(Billions of dollars except as noted)

September 15, 2004

Item	Fiscal year				2004				2005				2006			
	2003 ^a	2004	2005	2006	Q1 ^a	Q2 ^a	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Unified budget					Not seasonally adjusted											
Receipts ¹	1782	1875	2053	2214	410	550	475	468	445	630	511	516	482	675	542	530
Outlays ¹	2156	2296	2417	2565	580	576	569	607	607	600	603	624	662	644	635	668
Surplus/deficit ¹	-374	-421	-363	-351	-171	-26	-94	-139	-162	30	-92	-108	-180	30	-93	-138
On-budget	-535	-575	-534	-543	-193	-99	-103	-181	-198	-49	-106	-153	-222	-57	-111	-188
Off-budget	161	155	170	192	23	73	9	42	36	78	15	45	42	88	18	50
Means of financing																
Borrowing	374	389	373	358	136	41	94	148	136	-5	94	88	180	3	87	123
Cash decrease	26	-5	-5	0	12	-23	4	-6	2	-15	15	15	0	-30	15	15
Other ²	-25	37	-5	-7	23	8	-4	-3	24	-9	-17	5	0	-4	-8	-0
Cash operating balance, end of period	35	40	45	45	21	45	40	47	45	60	45	30	30	60	45	30
NIPA federal sector					Seasonally adjusted annual rates											
Receipts	1863	1931	2151	2311	1915	1947	1964	2022	2151	2192	2239	2266	2308	2323	2345	2370
Expenditures	2209	2316	2433	2614	2306	2329	2349	2375	2430	2447	2479	2515	2621	2645	2676	2706
Consumption expenditures	646	694	735	772	691	700	715	718	734	741	748	754	771	778	785	793
Defense	425	468	496	520	465	474	483	484	495	500	504	508	519	524	529	535
Nondefense	221	226	239	251	226	226	231	234	239	242	243	245	252	253	255	257
Other spending	1563	1622	1698	1842	1615	1629	1635	1657	1696	1706	1732	1761	1850	1867	1892	1913
Current account surplus	-345	-385	-282	-303	-391	-382	-386	-353	-279	-256	-241	-249	-313	-321	-331	-336
Gross investment	92	103	110	114	102	105	108	108	109	110	112	113	114	115	116	117
Gross saving less gross investment ³	-347	-395	-296	-318	-402	-394	-401	-367	-293	-270	-255	-263	-327	-336	-345	-351
Fiscal indicators⁴																
High-employment (HEB) surplus/deficit	-270	-345	-260	-302	-354	-348	-356	-326	-254	-235	-226	-238	-308	-322	-338	-349
Change in HEB, percent of potential GDP	1.2	0.5	-0.8	0.2	0.2	-0.1	0.0	-0.3	-0.6	-0.2	-0.1	0.1	0.5	0.1	0.1	0.1
Fiscal impetus (FI) percent of GDP	1.0	1.0	-0.2	0.3	0.3	0.1	0.2	0.1	-0.4	0.0	0.0	0.0	0.1	0.1	0.1	0.1

1. OMB's July 2004 baseline surplus estimates are -\$444 billion in FY 2004, -\$292 billion in FY 2005, and -\$234 billion in FY 2006, and surplus estimates under enactment of its proposed policies are -\$445 billion, -\$331 billion, and -\$261 billion respectively. CBO's September 2004 baseline surplus estimates are -\$422 billion in FY 2004, -\$348 billion in FY 2005 and -\$298 billion in FY 2006. Budget receipts, outlays, and surplus/deficit include corresponding social security (OASDI) categories. The OASDI surplus and the Postal Service surplus are excluded from the on-budget surplus and shown separately as off-budget, as classified under current law.

2. Other means of financing are checks issued less checks paid, accrued items, and changes in other financial assets and liabilities.

3. Gross saving is the current account surplus plus consumption of fixed capital of the general government as well as government enterprises.

4. HEB is gross saving less gross investment (NIPA) of the federal government in current dollars, with cyclically sensitive receipts and outlays adjusted to the staff's measure of potential output and the NAIRU. Quarterly figures for change in HEB and FI are not at annual rates. The sign on Change in HEB, as a percent of nominal potential GDP, is reversed. FI is the weighted difference of discretionary changes in federal spending and taxes in chained (2000) dollars, scaled by real GDP. The annual FI estimates are on a calendar year basis. Also, for FI and the change in HEB, positive values indicate aggregate demand stimulus.

a--Actual

Strictly Confidential (FR) September 15, 2004
 Class II FOMC Change in Debt of the Domestic Nonfinancial Sectors
(Percent)

Period ¹	Total	Federal government	Nonfederal					Memo: Nominal GDP
			Total	Households		Consumer credit	Business	State and local governments
				Total	Home mortgages			
<i>Year</i>								
1999	6.3	-1.9	8.8	8.1	9.1	7.4	10.6	3.4
2000	4.9	-8.0	8.4	8.7	8.3	10.7	9.4	1.3
2001	6.2	-0.2	7.7	9.0	9.8	8.0	6.1	8.9
2002	6.9	7.6	6.7	9.6	11.9	4.1	2.8	11.1
2003	8.1	10.9	7.5	10.2	12.7	4.3	4.3	8.2
2004	8.2	10.4	7.7	9.7	11.3	4.7	5.4	7.3
2005	7.0	7.0	7.0	7.8	8.6	6.1	6.4	4.6
2006	7.0	8.2	6.7	7.4	8.0	6.2	6.4	4.0
<i>Quarter</i>								
2004:1	9.1	12.0	8.5	11.3	13.1	6.1	4.8	9.5
2	7.7	10.7	7.0	9.5	11.1	2.2	4.4	4.6
3	7.4	5.8	7.8	8.7	10.1	4.7	5.9	11.3
4	7.6	11.4	6.8	8.1	9.2	5.4	5.8	3.1
2005:1	7.7	10.9	7.0	7.9	8.8	5.7	6.3	4.7
2	6.7	5.7	6.9	7.6	8.4	5.9	6.4	4.7
3	6.5	5.4	6.7	7.4	8.1	6.1	6.3	4.6
4	6.5	5.4	6.7	7.4	8.0	6.2	6.3	4.3
2006:1	7.9	13.8	6.6	7.3	7.9	6.1	6.2	4.0
2	6.5	6.0	6.6	7.2	7.8	6.0	6.3	4.0
3	6.1	4.4	6.5	7.1	7.7	5.9	6.3	4.0
4	6.8	7.8	6.5	7.1	7.6	5.9	6.3	3.7

Note. Quarterly data are at seasonally adjusted annual rates.

1. Data after 2004:Q2 are staff projections. Changes are measured from end of the preceding period to end of period indicated except for annual nominal GDP growth, which is calculated from Q4 to Q4.

2.6.3 FOF

Strictly Confidential (FR)
Class II FOMIC

Flow of Funds Projections: Highlights
(Billions of dollars at seasonally adjusted annual rates except as noted)

September 15, 2004

Category	2004					2005				2006					
	2003	2004	2005	2006	2004		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
					Q3	Q4									
Net funds raised by domestic nonfinancial sectors															
1 Total	1615.2	1677.4	1564.0	1733.9	1552.3	1608.0	1642.3	1524.5	1531.4	1557.7	1976.9	1629.3	1565.7	1763.8	
2 Net equity issuance	-57.8	-153.5	-124.0	-71.0	-174.0	-198.0	-216.0	-110.0	-89.0	-81.0	-71.0	-71.0	-71.0	-71.0	
3 Net debt issuance	1672.9	1830.9	1688.0	1804.9	1726.3	1806.0	1858.3	1634.5	1620.4	1638.7	2047.9	1700.3	1636.7	1834.8	
Borrowing sectors															
Nonfinancial business															
4 Financing gap ¹	-18.7	47.4	157.2	205.6	14.1	179.3	133.0	144.3	167.1	184.4	193.7	188.0	206.3	234.4	
5 Net equity issuance	-57.8	-153.5	-124.0	-71.0	-174.0	-198.0	-216.0	-110.0	-89.0	-81.0	-71.0	-71.0	-71.0	-71.0	
6 Credit market borrowing	302.5	397.5	503.9	533.7	450.8	450.0	493.3	504.8	504.7	512.7	517.8	528.9	537.1	551.0	
Households															
7 Net borrowing ²	856.6	901.1	793.3	808.5	844.4	809.5	802.1	790.1	786.1	795.1	799.9	804.5	809.1	820.6	
8 Home mortgages	756.1	757.7	637.0	644.0	720.0	668.6	654.6	635.9	626.5	631.2	635.9	640.5	645.2	654.6	
9 Consumer credit	83.0	95.0	130.1	138.5	97.0	113.7	120.6	127.7	133.9	138.3	138.2	138.1	137.9	140.0	
10 Debt/DPI (percent) ³	108.0	112.5	116.1	117.4	114.0	113.3	115.3	115.8	116.3	116.8	116.8	117.2	117.5	117.9	
State and local governments															
11 Net borrowing	117.8	114.4	77.8	69.8	183.0	51.7	78.8	78.8	78.8	74.8	70.8	70.8	70.8	66.8	
12 Current surplus ⁴	176.2	170.5	173.2	184.7	152.6	169.8	171.0	169.7	173.6	178.3	180.7	182.6	185.4	190.2	
Federal government															
13 Net borrowing	396.0	417.9	313.0	392.9	248.1	494.8	484.2	260.9	250.9	256.1	659.4	296.1	219.7	396.4	
14 Net borrowing (n.s.a.)	396.0	417.9	313.0	392.9	93.7	147.7	135.9	-5.3	94.4	88.1	179.7	3.5	86.6	123.1	
15 Unified deficit (n.s.a.)	396.2	429.6	332.4	380.9	94.2	139.0	162.2	-29.7	91.9	108.0	180.2	-30.5	93.2	138.1	
Depository institutions															
16 Funds supplied	476.4	686.6	545.2	570.2	391.1	482.8	620.7	474.5	575.1	510.6	660.2	511.0	600.2	509.5	
Memo (percentage of GDP)															
17 Domestic nonfinancial debt ⁵	194.6	198.0	201.9	204.5	198.9	200.0	201.0	201.9	202.5	203.0	203.7	204.5	205.0	205.5	
18 Domestic nonfinancial borrowing	15.2	15.6	13.7	13.8	14.6	15.1	15.3	13.3	13.0	13.0	16.0	13.1	12.5	13.8	
19 Federal government ⁶	3.6	3.6	2.5	3.0	2.1	4.1	4.0	2.1	2.0	2.0	5.2	2.3	1.7	3.0	
20 Nonfederal	11.6	12.1	11.1	10.8	12.5	11.0	11.4	11.2	11.0	11.0	10.9	10.8	10.8	10.8	

Note. Data after 2004:Q2 are staff projections.

1. For corporations: Excess of capital expenditures over U.S. internal funds.

2. Includes change in liabilities not shown in lines 8 and 9.

3. Average debt levels in the period (computed as the average of period-end debt positions) divided by disposable personal income.

2.6.4 FOF

4. NIPA state and local government saving plus consumption of fixed capital and net capital transfers.

5. Average debt levels in the period (computed as the average of period-end debt positions) divided by nominal GDP.

6. Excludes government-insured mortgage pool securities.

n.s.a. Not seasonally adjusted.

International Developments

Strong global demand and ongoing concerns about oil supply have kept oil prices high, but so far we have seen limited effects of elevated oil prices on economic activity abroad. Although our estimates of second-quarter GDP were revised down for several countries and more recent indicators have been mixed, taken together they still point to solid growth in the third quarter at about the pace we had anticipated in the August Greenbook. The trade-weighted average of foreign growth stepped down from 4.6 percent in the first quarter to 3.8 percent in the second quarter; growth is projected to edge down further over the forecast period to 3¼ percent in the extension of our forecast to 2006.

Our forecast for high-tech exporters in Asia has been marked down a bit from the previous Greenbook to reflect a somewhat weaker projection for demand for high-tech products. We also expect some negative effects of higher oil prices on oil-importing countries, particularly in Asia. Some offset from positive terms-of-trade effects is likely for oil exporters, notably Mexico. High energy prices have contributed to increased foreign headline inflation this year, but to date we have seen little effect on core consumer prices. We continue to expect that headline inflation will ease in coming quarters as oil and other commodity prices decline somewhat and as excess capacity persists in many countries.

Summary of Staff Projections
(Percent change from end of previous period, s.a.a.r.)

Indicator	2003		2004: H1	Projection		
	H1	H2		2004: H2	2005	2006
Foreign output	1.0	4.6	4.2	3.6	3.4	3.3
<i>Previous GB</i>	<i>1.0</i>	<i>4.6</i>	<i>4.2</i>	<i>3.5</i>	<i>3.5</i>	<i>...</i>
Foreign CPI	2.0	2.1	2.8	2.8	2.2	2.1
<i>Previous GB</i>	<i>2.0</i>	<i>2.1</i>	<i>2.8</i>	<i>2.6</i>	<i>2.1</i>	<i>...</i>

NOTE. Changes for years are measured as Q4/Q4; for half-years, Q2/Q4 or Q4/Q2.

... Not applicable.

The exchange value of the dollar has fluctuated in recent weeks but on balance is little changed from the time of the August FOMC meeting. The broad real dollar index is projected to decline at an annual rate of 1½ percent, slightly faster than in the August Greenbook. Our projection for the dollar has been influenced by the revised staff

post a similar increase. Next year, prices of imported core goods are projected to decelerate to just ½ percent (a.r.), in part driven by the expiration of the Multi-Fiber Agreement (MFA), which is expected to depress prices of imported apparel. The projection for 2005 is half a percentage point higher than in the August Greenbook, in part owing to a somewhat stronger path for commodity prices. In 2006, with exchange rate effects being quite limited, prices of imported core goods are expected to be essentially unchanged; a positive contribution from foreign inflation offsets the continuing effects of the expiration of the MFA.

Staff Projections of Selected Trade Prices

(Percent change from end of previous period excepted as noted; s.a.a.r.)

Trade category	2003		2004: H1	Projection		
	H1	H2		2004: H2	2005	2006
<i>Exports</i>						
Core goods	3.5	3.3	6.9	1.7	1.9	2.0
<i>Imports</i>						
Non-oil core goods	2.4	1.1	5.2	2.9	.6	.1
Oil (dollars per barrel)	26.42	27.74	34.55	39.45	35.78	33.34

NOTE. Prices for core exports and non-oil core imports, which exclude computers and semiconductors, are on a NIPA chain-weighted basis.

The price of imported oil for multiquarter periods is the price for the final quarter of the period.

After increasing almost 7 percent (a.r.) in the first half of this year, prices of exported core goods are estimated to be flat in the third quarter, held down by falling prices for agricultural products, but to pick up in the fourth quarter as agricultural prices stabilize. In 2005 and 2006, prices of exported core goods are projected to continue rising at a rate of about 2 percent. The projection for 2005 is ½ percentage point higher than in the last Greenbook, reflecting stronger producer price inflation and slightly higher agricultural export prices.

Trade in Goods and Services

In the second quarter, an unexpected surge in imports in June together with data revisions for previous months underpinned a 13 percent increase at an annual rate in real imports of goods and services, a rate more than 3 percentage points higher than anticipated in the

Staff Projections for Trade in Goods and Services

(Percent change from end of previous period, s.a.a.r.)

Measure	2003		2004: H1	Projection		
	H1	H2		2004: H2	2005	2006
Real exports	-1.6	14.3	7.3	9.6	7.2	6.4
<i>Previous GB</i>	<i>-1.6</i>	<i>14.3</i>	<i>9.8</i>	<i>10.0</i>	<i>7.6</i>	<i>...</i>
Real imports	.2	9.7	11.6	7.8	6.8	8.6
<i>Previous GB</i>	<i>.2</i>	<i>9.7</i>	<i>10.0</i>	<i>9.7</i>	<i>7.8</i>	<i>...</i>

NOTE. Changes for years are measured as Q4/Q4; for half-years, Q2/Q4 or Q4/Q2.

Alternative Simulations

The effects of rising interest rates on U.S. external debt service payments and the fading of the effects of dollar depreciation on net exports have led us to project a rapid widening in the current account deficit to unprecedented levels over the forecast period. This widening follows several years in which the deficit remained in a fairly narrow range of roughly 4 percent to 5 percent of GDP. Given the recent foreign exchange market attention to the U.S. external balances, a risk to our forecast is that sentiment on the dollar could turn sour abruptly when the pace at which the current account deficit is expanding becomes even more evident.

In our alternative simulations, we use the FRB/Global model to assess the effects of a rise in the risk premium on the dollar in foreign exchange markets that would generate a large and sharp dollar depreciation. The shock has been scaled so that the real value of our broad dollar index would fall 30 percent in the absence of endogenous adjustments in long-term interest rates, and is phased in over only two quarters beginning in 2005:Q1. The size and timing of this shock are somewhat arbitrary. A dollar depreciation of this magnitude occurred over a three-year period in the mid-1980s after the current account deficit reached a then-record level. We have penciled in a faster depreciation in our alternative simulations to highlight the risk that foreign exchange markets may react much more quickly to the large deficit.

Alternative Simulations:
30 Percent Depreciation of the Broad Real Dollar
 (Percent change from previous period, annual rate)

Indicator and simulation	2004		2005		2006	
	H1	H2	H1	H2	H1	H2
<i>U.S. real GDP</i>						
Baseline	3.9	3.8	3.7	3.9	4.0	4.0
Depreciation: Fixed funds rate	3.9	3.8	4.1	6.4	7.0	6.7
Depreciation: Taylor rule	3.9	3.8	4.1	5.8	5.6	4.8
<i>U.S. PCE prices excluding food and energy</i>						
Baseline	1.9	1.2	1.5	1.4	1.3	1.3
Depreciation: Fixed funds rate	1.9	1.2	2.4	1.9	2.0	2.1
Depreciation: Taylor rule	1.9	1.2	2.4	1.8	1.8	1.8

Note. H1 is Q2/Q4; H2 is Q4/Q2. In the “Fixed funds rate” simulations, the nominal federal funds rate remains unchanged from baseline. In the “Taylor rule” simulations, the federal funds rate follows a Taylor rule. In all simulations, the monetary authorities in major foreign economies adjust their policy rates according to a Taylor rule.

We have simulated this shock under two different technical assumptions about U.S. monetary policy. The first is our standard procedure that holds the nominal federal funds rate unchanged from baseline. As can be seen in the table, the boost to net exports raises U.S. GDP growth $2\frac{1}{2}$ percentage points relative to baseline in the second half of 2005 and nearly 3 percentage points relative to baseline in 2006. Core PCE inflation rises $\frac{3}{4}$ percentage point above baseline in 2005, mainly because of the direct effect of higher prices for imported goods and services. Inflation stays $\frac{3}{4}$ percentage point above baseline in 2006, reflecting the effects of increased capacity utilization on domestic prices. Because such a large and sustained increase in U.S. growth and inflation would very likely engender a monetary policy response, we also show simulation results under the assumption that the federal funds rate follows a Taylor rule. In this simulation, the funds rate rises 160 basis points above baseline by the end of 2005 and 220 basis points above baseline by the end of 2006. As can be seen in the table, the initial effects of the shock on output and inflation are similar regardless of the monetary policy response. However, over time the more active monetary policy does succeed in damping the effects on both output and inflation relative to the case with a fixed federal funds rate.

The effects of the depreciation on the U.S. economy are strongly expansionary because there is a direct shifting of global demand to U.S.-produced goods and services. The effects on foreign economies are correspondingly contractionary, and in many cases

OUTLOOK FOR FOREIGN REAL GDP AND CONSUMER PRICES: SELECTED COUNTRIES
(Percent, Q4 to Q4)

Measure and country	1998	1999	2000	2001	2002	2003	2004	2005	2006
REAL GDP (1)									

Total foreign	1.5	5.0	4.3	0.3	3.0	2.8	3.9	3.4	3.3
Industrial Countries	2.7	4.4	3.6	0.7	2.7	1.9	3.0	2.7	2.5
of which:									
Canada	4.4	5.9	4.1	1.4	3.8	1.7	3.7	3.4	3.1
Japan	-1.2	0.4	3.9	-2.2	1.8	3.5	2.7	1.9	2.0
United Kingdom	2.8	3.3	3.0	2.2	1.9	2.9	3.2	2.6	2.2
Euro Area (2)	2.0	3.9	2.7	0.7	1.1	0.7	2.0	2.0	1.9
Germany	0.7	3.3	1.9	0.5	0.5	0.0	1.5	1.5	1.4
Developing Countries	-0.3	6.1	5.3	-0.3	3.4	4.2	5.2	4.5	4.4
Asia	-2.2	8.6	5.9	0.9	5.8	6.0	5.8	4.9	4.9
Korea	-5.4	11.4	4.5	4.7	7.7	4.1	3.3	4.6	4.7
China	9.8	7.0	7.6	6.9	8.3	10.0	7.9	7.4	8.2
Latin America	1.2	4.2	4.4	-1.3	1.4	2.2	4.6	4.2	3.9
Mexico	2.9	5.4	4.8	-1.2	1.9	2.0	4.6	4.4	4.2
Brazil	-1.6	3.4	3.8	-0.8	3.8	-0.1	5.0	3.0	3.0
CONSUMER PRICES (3)									

Industrial Countries	0.9	1.1	1.7	0.9	2.1	1.3	1.6	1.4	1.4
of which:									
Canada	1.1	2.4	3.1	1.1	3.8	1.7	2.5	1.8	1.9
Japan	0.7	-1.1	-1.2	-1.3	-0.5	-0.4	-0.1	0.3	0.5
United Kingdom (4)	1.4	1.2	1.0	1.0	1.6	1.3	1.3	1.7	2.0
Euro Area (2)	0.8	1.5	2.5	2.1	2.3	2.0	2.1	1.9	1.6
Germany	0.3	1.1	1.7	1.5	1.2	1.2	1.9	1.4	0.7
Developing Countries	9.0	4.6	4.1	2.8	2.9	3.0	4.2	3.2	3.0
Asia	4.4	0.1	1.8	1.1	0.6	2.1	3.8	2.5	2.3
Korea	5.8	1.2	2.6	3.4	3.4	3.5	4.5	3.9	2.7
China	-1.2	-1.0	0.9	-0.1	-0.6	2.6	4.4	2.1	2.1
Latin America	15.4	12.5	8.4	5.3	6.4	4.9	5.0	4.2	3.9
Mexico	17.3	13.5	8.7	5.1	5.3	3.9	4.6	3.9	3.7
Brazil	2.0	8.4	6.4	7.5	10.7	11.5	7.1	5.2	4.7

1. Foreign GDP aggregates calculated using shares of U.S. exports.
2. Harmonized data for euro area from Eurostat.
3. Foreign CPI aggregates calculated using shares of U.S. non-oil imports.
4. CPI excluding mortgage interest payments, which is the targeted inflation rate.

OUTLOOK FOR FOREIGN REAL GDP AND CONSUMER PRICES: SELECTED COUNTRIES
(Percent changes)

Measure and country	2004				Projected 2005				2006			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
REAL GDP (1)	----- Quarterly changes at an annual rate -----											
Total foreign	4.6	3.8	3.6	3.5	3.5	3.4	3.4	3.4	3.3	3.3	3.2	3.2
Industrial Countries	3.4	3.1	2.7	2.9	2.8	2.7	2.7	2.7	2.6	2.5	2.5	2.5
of which:												
Canada	3.0	4.3	3.8	3.7	3.5	3.4	3.3	3.3	3.2	3.1	3.0	3.0
Japan	6.4	1.3	1.0	2.2	2.0	1.8	1.9	2.0	2.0	2.0	2.0	2.0
United Kingdom	2.9	3.8	3.1	3.0	2.9	2.7	2.5	2.5	2.2	2.2	2.2	2.2
Euro Area (2)	2.3	2.0	1.8	1.9	2.0	2.0	2.0	1.9	1.9	1.9	1.9	1.9
Germany	1.7	1.9	1.0	1.2	1.4	1.5	1.5	1.5	1.5	1.4	1.4	1.4
Developing Countries	6.4	4.8	4.8	4.6	4.6	4.5	4.4	4.4	4.4	4.4	4.4	4.4
Asia	7.6	4.8	5.6	5.4	4.9	4.9	4.8	4.8	4.9	4.9	4.9	4.9
Korea	3.0	2.3	3.8	4.2	4.5	4.5	4.8	4.7	4.8	4.8	4.8	4.8
China	14.4	2.8	7.3	7.3	7.3	7.3	7.5	7.5	8.2	8.2	8.2	8.2
Latin America	5.7	4.9	4.2	3.8	4.3	4.1	4.1	4.1	4.0	3.9	3.9	3.9
Mexico	5.5	4.9	4.3	3.8	4.6	4.3	4.3	4.3	4.3	4.2	4.2	4.2
Brazil	7.2	6.1	3.5	3.5	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
CONSUMER PRICES (3)	----- Four-quarter changes -----											
Industrial Countries	0.8	1.5	1.6	1.6	1.6	1.5	1.5	1.4	1.4	1.4	1.4	1.4
of which:												
Canada	0.9	2.2	2.4	2.5	2.4	2.1	1.9	1.8	1.8	1.9	1.9	1.9
Japan	-0.3	-0.2	-0.1	-0.1	-0.1	-0.0	0.2	0.3	0.3	0.4	0.4	0.5
United Kingdom (4)	1.2	1.4	1.4	1.3	1.3	1.6	1.6	1.7	1.8	1.9	2.0	2.0
Euro Area (2)	1.7	2.3	2.3	2.1	2.3	2.0	1.9	1.9	1.8	1.7	1.7	1.6
Germany	1.0	1.9	2.0	1.9	2.0	1.6	1.5	1.4	1.2	1.0	0.9	0.7
Developing Countries	3.0	3.6	4.5	4.2	4.1	3.8	3.3	3.2	3.1	3.0	3.0	3.0
Asia	2.2	3.3	4.2	3.8	3.8	3.1	2.5	2.5	2.4	2.4	2.3	2.3
Korea	3.3	3.4	4.6	4.5	4.7	5.2	4.3	3.9	3.4	3.1	2.9	2.7
China	2.8	4.4	5.3	4.4	4.2	2.9	2.1	2.1	2.1	2.1	2.1	2.1
Latin America	4.7	4.5	5.0	5.0	4.7	4.8	4.4	4.2	4.1	4.0	4.0	3.9
Mexico	4.3	4.3	4.7	4.6	4.3	4.4	4.1	3.9	3.8	3.7	3.7	3.7
Brazil	6.8	5.5	6.9	7.1	6.6	6.3	5.4	5.2	5.1	5.1	4.8	4.7

1. Foreign GDP aggregates calculated using shares of U.S. exports.
2. Harmonized data for euro area from Eurostat.
3. Foreign CPI aggregates calculated using shares of U.S. non-oil imports.
4. CPI excluding mortgage interest payments, which is the targeted inflation rate.

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1998	1999	2000	2001	2002	2003	----- 2004	Projected 2005	----- 2006
NIPA REAL EXPORTS and IMPORTS									
	Percentage point contribution to GDP growth, Q4/Q4								
Net Goods & Services	-1.1	-1.0	-0.9	-0.2	-0.9	-0.1	-0.6	-0.3	-0.7
Exports of G&S	0.3	0.6	0.7	-1.3	0.3	0.6	0.8	0.7	0.7
Imports of G&S	-1.4	-1.6	-1.6	1.1	-1.3	-0.7	-1.4	-1.1	-1.3
	Percentage change, Q4/Q4								
Exports of G&S	2.6	5.6	6.5	-11.9	3.5	6.1	8.4	7.2	6.4
Services	4.4	5.3	1.8	-8.9	9.8	3.8	6.4	6.2	5.8
Computers	7.3	13.4	22.7	-23.5	-1.0	11.2	8.8	13.0	14.4
Semiconductors	9.5	34.6	27.6	-34.6	9.9	38.8	10.5	26.1	29.1
Other Goods 1/	1.2	3.3	5.9	-10.2	0.4	5.0	9.4	6.2	5.0
Imports of G&S	11.0	12.1	11.2	-7.6	9.7	4.9	9.7	6.8	8.6
Services	10.4	6.5	10.7	-5.9	8.9	3.7	4.7	4.7	5.0
Oil	4.2	-3.4	13.3	3.7	4.2	1.8	0.6	1.0	2.4
Computers	26.4	26.0	22.9	-13.6	13.4	16.9	27.8	13.1	17.5
Semiconductors	-7.7	34.2	22.8	-51.1	10.0	0.3	33.5	24.3	29.1
Other Goods 2/	11.2	12.9	10.5	-6.5	9.9	4.9	10.6	7.3	9.2
	Billions of Chained 2000 Dollars								
Net Goods & Services	-203.8	-296.2	-379.5	-399.1	-472.1	-518.5	-576.2	-609.7	-679.4
Exports of G&S	966.5	1008.2	1096.3	1036.7	1012.4	1031.8	1128.8	1215.9	1297.9
Imports of G&S	1170.3	1304.5	1475.8	1435.8	1484.4	1550.2	1705.0	1825.5	1977.4
	Billions of dollars								
US CURRENT ACCOUNT BALANCE	-209.6	-296.8	-413.5	-385.7	-473.9	-530.7	-674.1	-758.4	-840.0
Current Acct as Percent of GDP	-2.4	-3.2	-4.2	-3.8	-4.5	-4.8	-5.7	-6.1	-6.4
Net Goods & Services (BOP)	-164.9	-263.3	-378.4	-362.7	-421.7	-496.5	-607.6	-650.5	-696.6
Investment Income, Net	8.3	18.4	25.3	28.7	12.6	38.8	16.9	-22.7	-58.1
Direct, Net	65.5	78.2	94.9	115.9	100.8	118.9	124.1	132.4	139.9
Portfolio, Net	-57.2	-59.8	-69.7	-87.2	-88.2	-80.1	-107.2	-155.1	-198.0
Other Income & Transfers, Net	-53.0	-52.0	-60.4	-51.7	-64.8	-72.9	-83.4	-85.3	-85.3

1. Merchandise exports excluding computers and semiconductors.
2. Merchandise imports excluding oil, computers, and semiconductors.

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	2001				2002				2003			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
NIPA REAL EXPORTS and IMPORTS												
	Percentage point contribution to GDP growth											
Net Goods & Services	-0.0	0.5	-0.6	-0.7	-1.1	-0.5	-0.4	-1.7	0.1	-0.5	0.6	-0.7
Exports of G&S	-0.6	-1.4	-2.0	-1.1	0.4	1.0	0.3	-0.4	-0.2	-0.2	1.0	1.6
Imports of G&S	0.6	1.9	1.5	0.5	-1.5	-1.4	-0.7	-1.3	0.3	-0.3	-0.4	-2.2
	Percentage change from previous period, s.a.a.r.											
Exports of G&S	-5.3	-12.7	-18.2	-10.8	4.7	11.0	3.1	-4.2	-1.5	-1.6	11.3	17.5
Services	-5.0	-0.6	-13.7	-15.3	21.7	4.5	3.5	10.5	-12.7	-3.5	14.1	20.6
Computers	-9.8	-35.7	-24.9	-21.3	-20.4	11.9	-3.8	12.3	-4.5	-3.4	38.2	19.8
Semiconductors	-30.0	-54.0	-45.3	3.7	24.9	38.8	11.4	-24.4	40.9	28.0	40.8	45.9
Other Goods 1/	-2.5	-11.5	-17.6	-8.6	-2.1	12.6	2.7	-10.3	2.4	-2.4	6.6	13.9
Imports of G&S	-3.7	-12.6	-10.3	-3.4	12.5	11.4	5.4	9.6	-1.9	2.5	2.9	17.1
Services	-5.1	12.9	-18.3	-10.4	24.6	-5.7	2.8	16.5	-2.4	-9.4	17.9	11.0
Oil	63.5	-33.8	-28.2	49.1	-5.6	-17.5	-10.8	69.9	-6.0	-2.8	0.6	16.6
Computers	-22.6	-23.3	-13.4	8.4	50.2	7.2	2.6	0.2	7.0	15.9	12.0	34.2
Semiconductors	-43.9	-70.1	-55.4	-23.7	42.3	33.9	-6.7	-17.6	-4.0	2.4	-1.5	4.4
Other Goods 2/	-5.5	-10.6	-3.7	-5.9	8.3	19.4	8.5	4.1	-1.8	5.5	-0.9	17.9
	Billions of Chained 2000 Dollars, s.a.a.r.											
Net Goods & Services	-398.2	-385.2	-398.4	-414.6	-444.9	-458.1	-469.8	-515.4	-511.7	-525.2	-508.7	-528.3
Exports of G&S	1097.2	1060.6	1008.7	980.3	991.6	1017.8	1025.5	1014.5	1010.6	1006.5	1033.8	1076.2
Imports of G&S	1495.4	1445.8	1407.1	1394.9	1436.5	1475.9	1495.3	1529.8	1522.3	1531.7	1542.5	1604.5
Billions of dollars, s.a.a.r.												
US CURRENT ACCOUNT BALANCE	-426.8	-390.2	-367.6	-358.3	-440.8	-471.6	-476.0	-507.4	-552.8	-535.5	-526.5	-507.8
Current Account as % of GDP	-4.3	-3.9	-3.6	-3.5	-4.3	-4.5	-4.5	-4.8	-5.1	-4.9	-4.7	-4.5
Net Goods & Services (BOP)	-389.3	-356.1	-357.1	-348.3	-375.0	-413.5	-427.7	-470.7	-501.6	-493.5	-489.0	-502.0
Investment Income, Net	23.9	29.8	1.5	59.7	9.2	1.8	10.6	28.8	21.5	29.1	34.5	70.1
Direct, Net	106.2	116.1	95.0	146.2	100.6	95.1	94.9	112.8	101.3	105.4	114.6	154.2
Portfolio, Net	-82.3	-86.3	-93.5	-86.6	-91.4	-93.2	-84.3	-84.0	-79.8	-76.3	-80.1	-84.1
Other Inc. & Transfers, Net	-61.3	-63.9	-12.0	-69.7	-75.0	-59.9	-59.0	-65.4	-72.8	-71.0	-72.0	-76.0

1. Merchandise exports excluding computers and semiconductors.

2. Merchandise imports excluding oil, computers, and semiconductors.

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	2004				Projected 2005				2006			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Percentage point contribution to GDP growth								Percentage change from previous period, s.a.a.r.			
NINIPA REAL EXPORTS and IMPORTS												
Net Goods & Services	-0.8	-1.1	-0.0	-0.4	-0.2	-0.0	-0.4	-0.6	-0.9	-0.3	-0.6	-0.7
Exports of G&S	0.7	0.7	0.8	1.0	0.6	0.8	0.7	0.9	0.5	0.7	0.7	0.8
Imports of G&S	-1.5	-1.8	-0.9	-1.4	-0.8	-0.8	-1.1	-1.4	-1.5	-1.0	-1.3	-1.5
Exports of G&S	7.3	7.3	8.6	10.6	5.5	7.5	7.4	8.5	5.2	6.4	6.3	7.7
Services	3.4	10.5	4.8	7.1	6.7	6.3	6.1	5.9	5.8	5.9	5.8	5.9
Computers	-8.3	-4.3	32.3	20.9	9.5	14.0	14.3	14.3	14.4	14.4	14.4	14.4
Semiconductors	12.5	-9.9	1.6	44.9	18.3	28.2	29.1	29.1	29.1	29.1	29.1	29.1
Other Goods 1/	10.1	7.7	9.8	9.8	3.9	6.5	6.3	8.2	3.2	5.0	4.9	7.1
Imports of G&S	10.6	12.7	5.9	9.7	5.1	5.1	7.5	9.6	9.6	6.2	8.4	10.1
Services	1.1	11.6	1.6	4.7	4.5	4.5	4.9	4.9	5.1	5.0	5.0	5.0
Oil	39.0	-33.1	-2.5	13.1	13.4	-19.6	-3.1	17.9	15.7	-21.1	-0.5	21.1
Computers	12.8	39.4	32.0	28.6	2.5	16.2	17.1	17.3	17.5	17.5	17.5	17.5
Semiconductors	42.2	21.2	25.8	46.4	12.6	27.7	28.6	29.1	29.1	29.1	29.1	29.1
Other Goods 2/	8.9	19.4	6.0	8.3	4.0	8.1	8.6	8.8	9.0	9.2	9.2	9.2
Billions of Chained 2000 Dollars, s.a.a.r.												
Net Goods & Services	-550.1	-580.5	-581.5	-592.7	-599.0	-599.7	-611.2	-628.8	-656.5	-665.9	-685.8	-709.6
Exports of G&S	1095.4	1114.8	1138.0	1167.1	1182.7	1204.2	1225.8	1250.9	1267.0	1286.8	1306.7	1331.2
Imports of G&S	1645.5	1695.3	1719.6	1759.8	1781.7	1803.9	1836.9	1879.7	1923.4	1952.8	1992.5	2040.8
Billions of dollars, s.a.a.r.												
US CURRENT ACCOUNT BALANCE	-588.7	-664.7	-699.3	-743.7	-754.8	-747.0	-756.7	-775.1	-819.7	-819.1	-843.1	-878.1
Current Account as % of GDP	-5.1	-5.7	-5.9	-6.2	-6.2	-6.1	-6.1	-6.1	-6.4	-6.3	-6.4	-6.6
Net Goods & Services (BOP)	-554.4	-601.1	-626.6	-648.1	-648.6	-642.4	-649.0	-661.8	-684.2	-685.4	-698.7	-718.1
Investment Income, Net	54.3	16.7	9.5	-12.9	-13.8	-22.1	-24.9	-30.0	-43.1	-51.2	-61.5	-76.6
Direct, Net	139.1	116.2	118.4	122.7	126.1	130.8	134.4	138.2	136.6	138.9	142.5	141.6
Portfolio, Net	-84.8	-99.5	-108.9	-135.6	-139.8	-152.9	-159.3	-168.2	-179.7	-190.1	-204.0	-218.2
Other Inc. & Transfers, Net	-88.5	-80.3	-82.2	-82.7	-92.4	-82.5	-82.9	-83.3	-92.4	-82.5	-82.9	-83.3

1. Merchandise exports excluding computers and semiconductors.

2. Merchandise imports excluding oil, computers, and semiconductors.

Part 2

September 15, 2004

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

September 15, 2004

Recent Developments

Production of Domestic Autos and Trucks

(Millions of units at an annual rate except as noted; FRB seasonals)

Item	2003	2004			2004		
		Q1	Q2	Q3 ¹	July	Aug.	Sept. ¹
U.S. production	12.1	12.4	11.9	11.9	11.5	12.0	12.1
Autos	4.5	4.4	4.2	4.3	4.1	4.3	4.5
Trucks	7.6	8.0	7.7	7.6	7.4	7.7	7.6
Days' supply ²	73	75	78	n.a.	74	78	n.a.
Autos	63	63	63	n.a.	59	65	n.a.
Trucks	80	84	88	n.a.	83	87	n.a.
Inventories ³	3.17	3.26	3.33	n.a.	3.33	3.41	n.a.
Autos	1.13	1.11	1.09	n.a.	1.05	1.09	n.a.
Trucks	2.04	2.14	2.24	n.a.	2.28	2.32	n.a.

Note. Components may not sum to totals because of rounding.

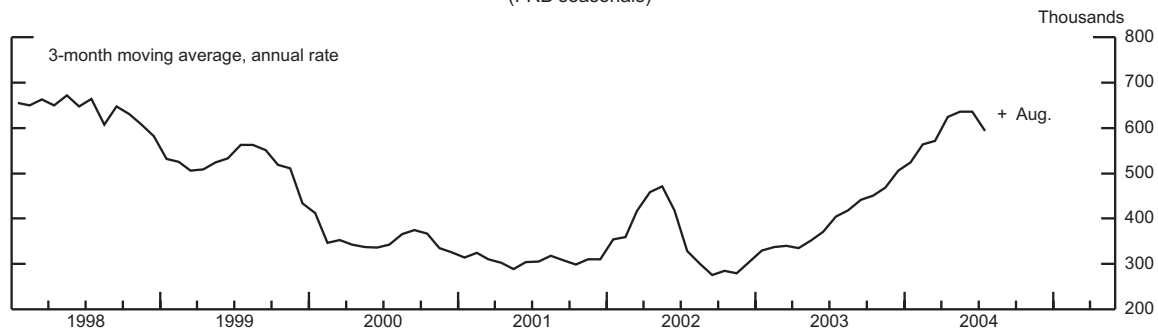
1. Production rates for the third quarter and September reflect the latest schedules from Ward's Communications.

2. Quarterly and annual values are calculated with end-of-period stocks and average reported sales; excludes medium and heavy trucks.

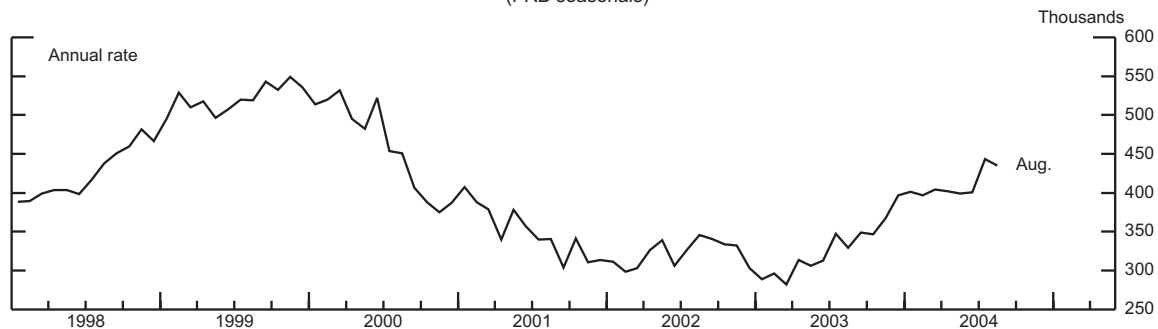
3. End-of-period stocks; excludes medium and heavy trucks.

n.a. Not available

Medium and Heavy Truck Orders (FRB seasonals)



Medium and Heavy Truck Sales (FRB seasonals)



September 17, 2004

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Supplemental Notes

Prepared for the Federal Open Market Committee
by the staff of the Board of Governors of the Federal Reserve System

Broad Measures of Inflation
(Percent change, Q2 to Q2)

Measure	2001	2002	2003	2004
<i>Product prices</i>				
GDP price index	2.5	1.5	1.9	2.3
Less food and energy	2.0	2.0	1.6	1.9
Nonfarm business chain price index	2.0	.9	1.2	1.5
<i>Expenditure prices</i>				
Gross domestic purchases price index	2.3	1.3	1.9	2.5
Less food and energy	1.8	1.8	1.6	1.9
PCE price index	2.4	1.2	1.8	2.3
Less food and energy	1.8	1.8	1.4	1.5
PCE price index, market-based components	2.3	.9	1.8	2.4
Less food and energy	1.7	1.6	1.2	1.5
CPI	3.4	1.3	2.2	2.8
Less food and energy	2.7	2.4	1.5	1.8
Chained CPI	2.7	1.0	1.9	2.3
Less food and energy	2.0	1.9	1.3	1.3
Median CPI	3.5	3.6	2.2	2.5
Trimmed mean CPI	2.9	2.2	1.9	2.1

Surveys of Inflation Expectations
(Percent)

Period	Actual CPI inflation ¹	University of Michigan				Professional forecasters (10-year) ⁴
		1 year ²		5 to 10 years ³		
		Mean	Median	Mean	Median	
2002:Q4	2.2	2.7	2.5	3.3	2.8	2.5
2003:Q1	2.9	3.2	2.8	3.0	2.7	2.5
Q2	2.1	2.6	2.2	3.1	2.7	2.5
Q3	2.2	2.8	2.3	3.1	2.7	2.5
Q4	1.9	3.0	2.6	3.1	2.8	2.5
2004:Q1	1.8	3.1	2.7	3.4	2.9	2.5
Q2	2.9	4.0	3.3	3.3	2.8	2.5
Q3	n.a.	3.4	2.9	3.1	2.8	2.5
2004:Apr.	2.3	4.0	3.2	3.2	2.7	...
May	3.1	3.9	3.3	3.3	2.8	...
June	3.3	4.0	3.3	3.4	2.9	2.5
July	3.0	3.5	3.0	3.1	2.8	...
Aug.	2.7	3.1	2.8	3.1	2.7	...
Sept.	n.a.	3.5	2.9	3.2	2.8	2.5

1. CPI; percent change from the same period in the preceding year.
 2. Responses to the question: By about what percent do you expect prices to go up, on average, during the next 12 months?
 3. Responses to the question: By about what percent per year do you expect prices to go up, on average, during the next 5 to 10 years?
 4. Quarterly CPI projections compiled by the Federal Reserve Bank of Philadelphia.
- n.a. Not available.
... Not applicable.