

## **Part 1**

January 26, 2005

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## **CURRENT ECONOMIC AND FINANCIAL CONDITIONS**

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### **Summary and Outlook**

Strictly Confidential (FR) Class II FOMC

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January 26, 2005

## **Summary and Outlook**

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

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

Measure	2004:Q4		2005:Q1	
	Dec. GB	Jan. GB	Dec. GB	Jan. GB
<b>Real GDP</b>	<b>3.7</b>	<b>3.5</b>	<b>3.4</b>	<b>3.8</b>
Private domestic final purchases	3.8	5.0	3.0	2.8
Personal consumption expenditures	3.3	4.6	3.7	3.7
Residential investment	1.0	3.9	2.6	3.1
Business fixed investment	9.1	8.3	-1.3	-3.2
Government outlays for consumption and investment	1.6	-.5	3.7	3.9
	Contribution to growth (percentage points)			
Inventory investment	.3	.8	.2	.3
Net exports	-.2	-1.5	-.0	.4

year-end push by motor vehicle manufacturers to boost sales of new vehicles, and retail sales of other goods were brisk. In addition, we assume that cold weather in December spurred a jump in the demand for energy services. The robust increase in spending in the fourth quarter left the personal saving rate—excluding the one-time Microsoft dividend—close to zero.<sup>2</sup>

We expect consumer spending to rise at a more moderate, but still solid, annual pace of 3½ percent in the current quarter. Sales of light vehicles are likely to drop back a bit from the high fourth-quarter level—we have them receding to an annual rate of just under 17 million units, a pace in line with last year's average. But spending on other non-energy goods is projected to remain relatively strong, and households are anticipated to sharply boost their outlays for fuel oil and energy services.

The rebound in homebuilding in December put the average level of new single-family housing starts during the fourth quarter at an annual rate of 1.61 million units, which matched the robust pace that prevailed earlier in the year. The issuance of new permits and the backlog of unused permits at year-end suggest that, in the near term, single-

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<sup>2</sup> We expect that the BEA will allocate three-fourths of the special Microsoft dividend payments to personal income, boosting the measured saving rate in 2004:Q4 by 1.1 percentage points; most of the remainder will be assigned to foreign shareholders.

<b>Projections of Real GDP</b> (Percent change at annual rate from end of preceding period except as noted)				
Measure	2004: H2	2005: H1	2005	2006
<b>Real GDP</b>	<b>3.7</b>	<b>3.9</b>	<b>3.9</b>	<b>3.6</b>
Previous	3.7	3.7	3.9	3.7
Final sales	3.9	4.3	4.1	3.6
Previous	4.1	4.0	4.0	3.7
PCE	4.9	3.8	3.8	3.7
Previous	4.2	3.9	4.0	3.9
Residential investment	2.7	3.7	2.7	1.0
Previous	1.2	2.6	2.5	1.4
BFI	10.6	3.2	5.9	8.3
Previous	10.9	3.6	6.4	8.3
Government purchases	.1	3.4	3.0	2.5
Previous	1.2	2.9	2.6	2.5
Exports	2.5	8.3	8.7	7.2
Previous	8.2	7.5	8.3	7.6
Imports	7.0	2.6	5.2	7.6
Previous	6.8	3.8	5.9	8.1
	Contribution to growth (percentage points)			
Inventory change	-.1	-.4	-.2	.1
Previous	-.4	-.3	-.1	.0
Net exports	-.8	.4	.0	-.4
Previous	-.2	.2	-.1	-.5

the debt that we are projecting. That said, the strength in consumer spending in late 2004 appears to have further depressed the already low personal saving rate. As a consequence, in addition to the slight drag on spending from household wealth in 2006, consumer spending should tend to be restrained by the need of households to rebuild savings.

Demand for housing over the next two years is expected to receive ongoing support from the availability of mortgages at interest rates as favorable as those that prevailed during

### Decomposition of Structural Labor Productivity

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

Measure	1974-95	1996-2001	2002	2003	2004	2005	2006
<b>Structural labor productivity</b>	<b>1.5</b>	<b>2.7</b>	<b>3.2</b>	<b>3.7</b>	<b>3.0</b>	<b>2.7</b>	<b>2.7</b>
Previous	1.5	2.7	3.2	3.7	3.0	2.7	2.7
<i>Contributions</i> <sup>1</sup>							
Capital deepening	.7	1.3	.6	.6	.8	.9	.9
Previous	.7	1.3	.6	.6	.8	.8	.9
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	1.5
Labor composition	.3	.3	.3	.3	.3	.3	.3
MEMO							
Potential GDP	3.0	3.4	3.4	3.8	3.4	3.2	3.2
Previous	3.0	3.4	3.4	3.8	3.4	3.1	3.2

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.

### 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	2.8	1.7	2.2
Previous	5.6	2.8	1.7	2.2
Nonfarm private payroll employment	-.2	1.8	2.2	1.9
Previous	-.2	1.8	2.2	2.0
Household survey employment	1.2	1.3	1.8	1.5
Previous	1.2	1.3	1.7	1.5
Labor force participation rate <sup>1</sup>	66.1	66.0	66.3	66.4
Previous	66.1	66.0	66.3	66.4
Civilian unemployment rate <sup>1</sup>	5.9	5.4	5.3	5.1
Previous	5.9	5.4	5.3	5.1
MEMO				
GDP gap <sup>2</sup>	1.7	1.3	.6	.2
Previous	1.7	1.3	.6	.1

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.

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

Measure	2003	2004	2005	2006
PCE chain-weighted price index	1.7	2.5	1.3	1.3
Previous	1.7	2.5	1.2	1.3
Food and beverages	2.7	2.9	2.0	1.8
Previous	2.7	3.0	2.0	1.8
Energy	7.2	17.8	-3.4	-1.2
Previous	7.2	17.8	-6.4	-0.3
Excluding food and energy	1.2	1.5	1.6	1.4
Previous	1.2	1.5	1.6	1.4
Consumer price index	1.9	3.4	1.5	1.6
Previous	1.9	3.4	1.4	1.7
Excluding food and energy	1.2	2.1	2.0	1.8
Previous	1.2	2.2	2.0	1.8
GDP chain-weighted price index	1.7	2.3	1.5	1.6
Previous	1.7	2.3	1.5	1.6
ECI for compensation of private industry workers <sup>1</sup>	4.0	4.0	4.3	4.2
Previous	4.0	4.0	4.2	4.1
NFB compensation per hour	5.4	4.0	4.2	4.2
Previous	5.4	3.8	4.2	4.2
Prices of core nonfuel imports	1.6	3.8	1.2	.2
Previous	1.6	3.7	1.0	.1

1. December to December.

**Prices and labor costs.** Our forecasts for total PCE price inflation are 1.3 percent in both 2005 and 2006—down sharply from the increase of 2½ percent during 2004. The revisions to our projections of energy prices in this forecast are relatively small: They add roughly 0.1 percentage point to overall consumer price inflation this year and subtract a similar amount in 2006. We continue to project that core PCE price inflation will average 1½ percent per year over the next two years—the same as during 2004. As has been the case for some time, the fundamental factors underlying this stability in our inflation forecast are little changed: Over the forecast period, the upward pressures on inflation from diminishing economic slack and from a slightly slower rise in structural productivity are offset by a waning of the influence of higher prices for energy and

### Alternative Scenarios

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

Measure and scenario	2004	2005		2006
	Q4	H1	H2	
<i>Real GDP</i>				
<b>Baseline</b>	<b>3.5</b>	<b>3.9</b>	<b>3.8</b>	<b>3.6</b>
Flat markup	3.5	3.9	3.8	3.7
And higher compensation inflation	3.5	3.8	3.6	3.6
Faster productivity growth	3.5	4.4	4.7	4.6
No investment pothole	3.5	4.7	4.3	4.3
Stronger consumption	3.5	4.1	4.2	4.0
Real estate slump	3.5	3.9	3.6	3.2
With a loss of consumer confidence	3.5	3.8	3.4	2.9
Higher long-term interest rates	3.5	3.8	3.0	2.6
Market-based funds rate	3.5	3.9	3.7	3.4
<i>Civilian unemployment rate<sup>1</sup></i>				
<b>Baseline</b>	<b>5.4</b>	<b>5.3</b>	<b>5.3</b>	<b>5.1</b>
Flat markup	5.4	5.3	5.3	5.1
And higher compensation inflation	5.4	5.4	5.5	5.4
Faster productivity growth	5.4	5.2	5.1	4.8
No investment pothole	5.4	5.2	5.1	4.6
Stronger consumption	5.4	5.3	5.2	4.7
Real estate slump	5.4	5.3	5.3	5.3
With a loss of consumer confidence	5.4	5.3	5.4	5.5
Higher long-term interest rates	5.4	5.3	5.5	5.8
Market-based funds rate	5.4	5.3	5.3	5.2
<i>PCE prices excluding food and energy</i>				
<b>Baseline</b>	<b>1.4</b>	<b>1.5</b>	<b>1.6</b>	<b>1.4</b>
Flat markup	1.4	1.7	1.8	1.8
And higher compensation inflation	1.4	2.0	2.3	2.4
Faster productivity growth	1.4	1.3	1.3	1.0
No investment pothole	1.4	1.5	1.6	1.4
Stronger consumption	1.4	1.5	1.6	1.5
Real estate slump	1.4	1.5	1.6	1.4
With a loss of consumer confidence	1.4	1.5	1.6	1.3
Higher long-term interest rates	1.4	1.4	1.5	1.2
Market-based funds rate	1.4	1.5	1.6	1.4

1. Average for the final quarter of the period.

**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> <i>(percent change, Q4 to Q4)</i>			
Projection	3.8	3.9	3.6
Confidence interval			
Greenbook forecast errors <sup>1</sup>	3.6–4.0	2.2–5.5	1.9–5.3
FRB/US stochastic simulations	3.6–3.9	2.5–5.4	1.9–5.4
<i>Civilian unemployment rate</i> <i>(percent, Q4)</i>			
Projection	5.4	5.3	5.1
Confidence interval			
Greenbook forecast errors <sup>1</sup>	5.4–5.4	4.7–5.8	4.1–6.1
FRB/US stochastic simulations	5.4–5.5	4.6–5.9	4.0–6.0
<i>PCE prices</i> <i>excluding food and energy</i> <i>(percent change, Q4 to Q4)</i>			
Projection	1.5	1.6	1.4
Confidence interval			
Greenbook forecast errors <sup>2</sup>	1.4–1.6	1.0–2.1	.4–2.3
FRB/US stochastic simulations	1.5–1.6	1.0–2.2	.6–2.3

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

1. 1978–2003.

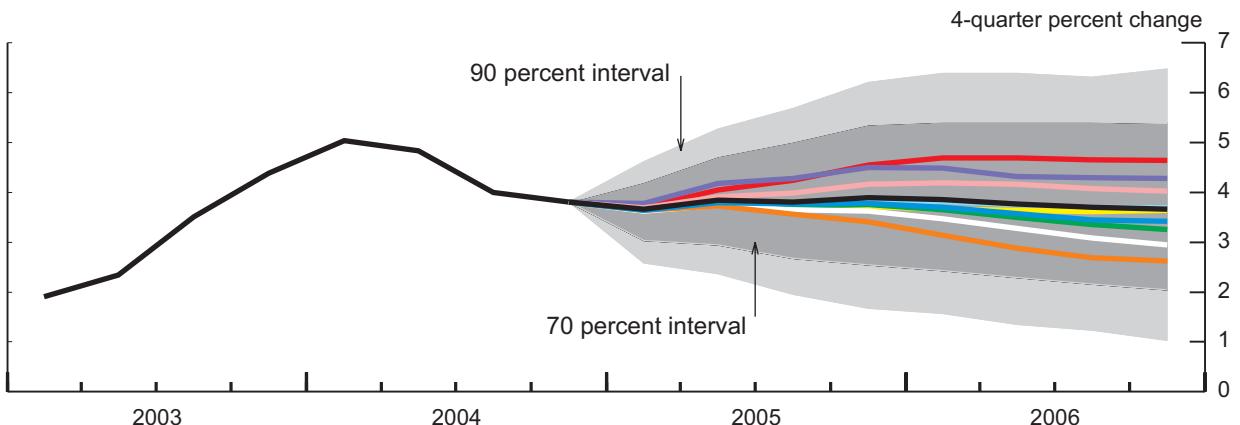
2. 1981–2003.

## Forecast Confidence Intervals and Alternative Scenarios

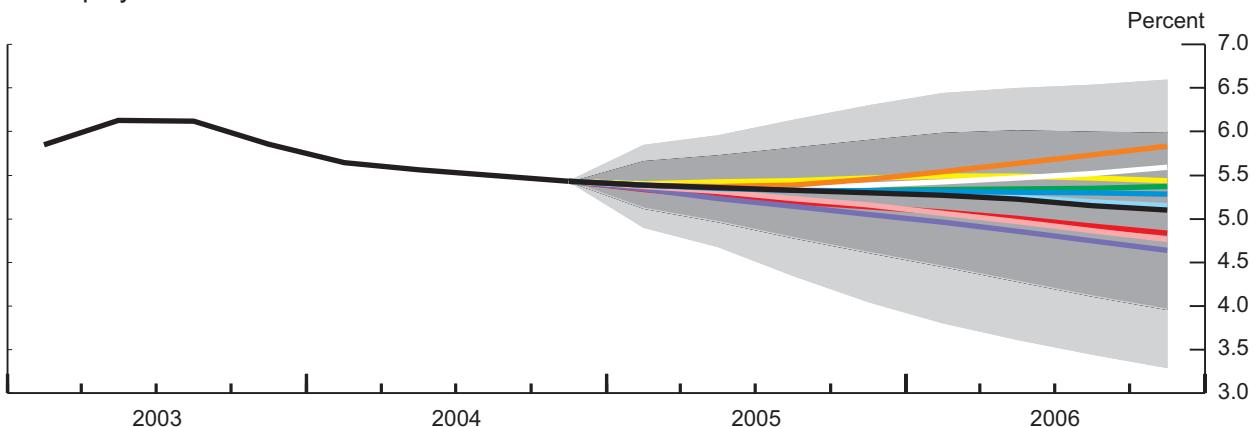
### Confidence Intervals Based on FRB/US Stochastic Simulations

- |  |   |
|--|---|
| <ul style="list-style-type: none"> <li><span style="color: black;">█</span> Greenbook baseline</li> <li><span style="color: lightblue;">█</span> Flat markup</li> <li><span style="color: yellow;">█</span> Flat markup and higher compensation inflation</li> <li><span style="color: red;">█</span> Faster productivity growth</li> <li><span style="color: purple;">█</span> No investment pothole</li> </ul> | <ul style="list-style-type: none"> <li><span style="color: pink;">█</span> Stronger consumption</li> <li><span style="color: green;">█</span> Real estate slump</li> <li><span style="color: white;">█</span> Real estate slump with a loss of consumer confidence</li> <li><span style="color: orange;">█</span> Higher long-term interest rates</li> <li><span style="color: blue;">█</span> Market-based funds rate</li> </ul> |
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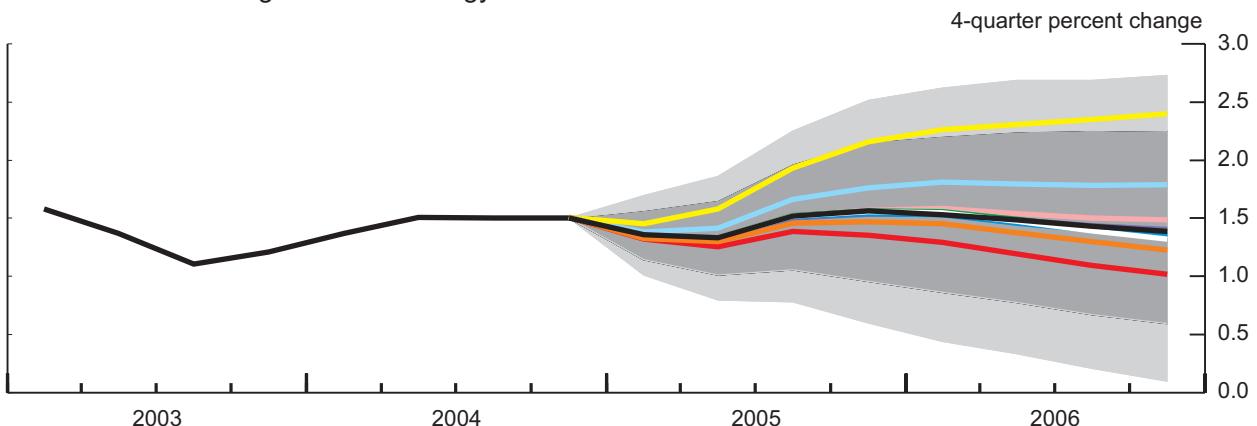
Real GDP



Unemployment Rate



PCE Prices excluding Food and Energy



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

Interval	Nominal GDP		Real GDP		GDP chain-weighted price index		Consumer price index <sup>1</sup>		Unemployment rate <sup>2</sup>		
	12/08/04	1/26/05	12/08/04	1/26/05	12/08/04	1/26/05	12/08/04	1/26/05	12/08/04	1/26/05	
<b>ANNUAL</b>											
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		6.6	6.6	4.4	4.4	2.1	2.1	2.7	2.7	5.5	5.5
2005		5.5	5.5	3.8	3.8	1.6	1.6	1.9	2.1	5.3	5.3
2006		5.5	5.4	3.9	3.7	1.6	1.6	1.7	1.6	5.2	5.2
<b>QUARTERLY</b>											
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	6.6	6.6	3.3	3.3	3.2	3.2	4.8	4.8	5.6	5.6
	Q3	5.1	5.5	3.7	4.0	1.3	1.4	1.9	1.9	5.5	5.5
	Q4	5.6	5.4	3.7	3.5	1.9	1.9	3.6	3.4	5.4	5.4
2005	Q1	5.1	5.1	3.4	3.8	1.6	1.3	0.6	1.0	5.4	5.4
	Q2	5.4	5.6	4.0	4.0	1.3	1.6	1.4	1.8	5.3	5.3
	Q3	5.7	5.6	4.1	3.9	1.5	1.6	1.7	1.7	5.3	5.3
	Q4	5.7	5.4	4.0	3.8	1.6	1.5	1.7	1.6	5.3	5.3
2006	Q1	5.8	5.7	3.8	3.7	1.9	1.9	1.7	1.6	5.2	5.3
	Q2	5.3	5.2	3.7	3.6	1.5	1.6	1.6	1.6	5.2	5.2
	Q3	5.2	5.1	3.7	3.6	1.5	1.5	1.7	1.6	5.1	5.2
	Q4	5.2	5.1	3.7	3.6	1.5	1.4	1.7	1.6	5.1	5.1
<b>TWO-QUARTER<sup>3</sup></b>											
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	7.0	7.0	3.9	3.9	3.0	3.0	4.2	4.2	-0.3	-0.3
	Q4	5.4	5.4	3.7	3.7	1.6	1.6	2.7	2.6	-0.2	-0.2
2005	Q2	5.3	5.3	3.7	3.9	1.5	1.4	1.0	1.4	-0.1	-0.1
	Q4	5.7	5.5	4.1	3.8	1.6	1.6	1.7	1.6	0.0	0.0
2006	Q2	5.5	5.4	3.7	3.6	1.7	1.7	1.7	1.6	-0.1	-0.1
	Q4	5.2	5.1	3.7	3.6	1.5	1.5	1.7	1.6	-0.1	-0.1
<b>FOUR-QUARTER<sup>4</sup></b>											
2002	Q4	3.8	3.8	2.3	2.3	1.6	1.6	2.2	2.2	0.3	0.4
2003	Q4	6.2	6.2	4.4	4.4	1.7	1.7	1.9	1.9	0.0	0.0
2004	Q4	6.2	6.2	3.8	3.8	2.3	2.3	3.4	3.4	-0.5	-0.5
2005	Q4	5.5	5.4	3.9	3.9	1.5	1.5	1.4	1.5	-0.1	-0.1
2006	Q4	5.4	5.3	3.7	3.6	1.6	1.6	1.7	1.6	-0.2	-0.1

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.

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

Item	Units <sup>1</sup>	Projected - - - - -									
		1998	1999	2000	2001	2002	2003	2004	2005	2006	
<b>Expenditures</b>											
Nominal GDP	Bill. \$	8747.0	9268.4	9817.0	10128.0	10487.0	11004.0	11728.9	12369.8	13038.8	
Real GDP	Bill. Ch. \$	9066.9	9470.3	9817.0	9890.7	10074.8	10381.3	10839.3	11248.0	11665.0	
Real GDP	% change	4.5	4.7	2.2	0.2	2.3	4.4	3.8	3.9	3.6	
Gross domestic purchases		5.5	5.5	3.0	0.4	3.1	4.3	4.5	3.6	3.8	
Final sales		4.8	4.2	2.9	1.5	1.2	4.5	3.4	4.1	3.6	
Priv. dom. final purchases		6.4	5.3	4.3	1.0	1.7	4.9	4.7	4.0	4.1	
Personal cons. expenditures		5.4	4.9	4.1	2.8	2.5	3.8	3.9	3.8	3.7	
Durables		14.4	7.3	4.7	10.8	1.5	9.9	5.6	6.0	6.3	
Nondurables		4.7	4.9	3.0	1.9	2.3	4.6	4.4	4.5	4.4	
Services		3.8	4.4	4.5	1.6	2.9	2.2	3.3	3.0	2.9	
Business fixed investment		10.9	7.7	7.8	-9.6	-6.0	9.4	9.4	5.9	8.3	
Equipment & Software		13.5	10.8	7.5	-9.0	-2.2	12.1	12.8	6.6	9.8	
Nonres. structures		4.0	-0.9	8.8	-11.1	-16.1	1.5	-1.2	3.6	3.4	
Residential structures		10.3	3.6	-1.9	1.4	6.9	12.0	6.6	2.7	1.0	
Exports		2.6	5.6	6.5	-11.9	3.5	6.1	4.9	8.7	7.2	
Imports		11.0	12.1	11.2	-7.6	9.7	4.9	9.3	5.2	7.6	
Gov't. cons. & investment		3.3	4.2	0.4	5.0	3.8	2.2	1.2	3.0	2.5	
Federal		0.1	4.2	-2.2	6.4	8.2	5.5	2.6	4.0	1.9	
Defense		-1.2	4.3	-3.5	6.5	8.5	8.5	3.6	5.4	2.3	
State & local		5.1	4.2	1.7	4.2	1.6	0.4	0.4	2.5	2.8	
Change in bus. inventories	Bill. Ch. \$	72.6	68.9	56.5	-31.7	11.7	-0.7	47.6	39.2	37.5	
Nonfarm		71.2	71.5	57.8	-31.8	13.5	-1.1	43.9	36.7	35.3	
Net exports		-203.8	-296.2	-379.5	-399.1	-472.1	-518.5	-584.5	-609.5	-648.4	
Nominal GDP	% change	5.7	6.3	4.6	2.7	3.8	6.2	6.2	5.4	5.3	
GDP Gap <sup>2</sup>	%	-1.6	-2.4	-2.5	0.1	1.6	2.2	1.4	0.9	0.4	
<b>Employment and Production</b>											
Nonfarm payroll employment	Millions	125.9	129.0	131.8	131.8	130.3	129.9	131.3	133.8	136.4	
Unemployment rate	%	4.5	4.2	4.0	4.7	5.8	6.0	5.5	5.3	5.2	
Industrial prod. index	% change	4.2	5.2	1.9	-5.1	1.5	1.2	4.2	5.3	4.4	
Capacity util. rate - mfg.	%	81.8	81.1	80.6	74.5	73.5	73.7	76.7	79.2	81.3	
Housing starts	Millions	1.62	1.64	1.57	1.60	1.70	1.85	1.95	1.96	1.94	
Light motor vehicle sales		15.52	16.90	17.35	17.12	16.79	16.62	16.83	17.31	17.86	
North Amer. produced		13.48	14.41	14.48	14.04	13.49	13.32	13.44	13.83	14.28	
Other		2.03	2.49	2.87	3.08	3.30	3.31	3.39	3.48	3.58	
<b>Income and Saving</b>											
Nominal GNP	Bill. \$	8768.3	9302.2	9855.9	10171.6	10514.1	11059.2	11768.0	12367.0	12992.0	
Nominal GNP	% change	5.5	6.5	4.7	2.9	3.5	6.5	5.5	5.2	4.9	
Nominal personal income		7.0	5.5	7.1	2.2	1.9	4.6	6.1	5.4	6.3	
Real disposable income		5.6	2.8	4.4	1.2	2.9	3.9	3.7	3.4	4.7	
Personal saving rate	%	4.3	2.4	2.3	1.8	2.0	1.4	1.0	0.6	1.7	
Corp. profits, IVA & CCAdj.	% change	-10.0	9.6	-8.6	-0.2	15.4	23.3	7.3	1.2	-1.4	
Profit share of GNP	%	9.1	9.2	8.3	7.5	8.3	9.2	9.9	9.9	9.4	
Excluding FR Banks		8.9	8.9	8.0	7.3	8.1	9.1	9.8	9.8	9.2	
Federal surpl./deficit	Bill. \$	38.8	103.6	189.5	46.7	-254.5	-364.5	-376.5	-269.3	-319.2	
State & local surpl./def.		52.0	50.4	50.0	4.8	-25.0	-3.2	10.7	7.7	9.2	
Ex. social ins. funds		50.3	48.7	47.9	2.2	-26.6	-4.3	9.3	6.1	7.6	
Gross natl. saving rate	%	18.2	18.0	18.0	16.3	14.1	13.5	13.5	13.3	13.5	
Net natl. saving rate		7.4	6.9	6.7	4.2	2.0	1.4	1.7	1.8	2.0	
<b>Prices and Costs</b>											
GDP chn.-wt. price index	% change	1.1	1.6	2.2	2.4	1.6	1.7	2.3	1.5	1.6	
Gross Domestic Purchases		0.7	2.0	2.4	1.6	1.8	1.8	2.8	1.5	1.4	
chn.-wt. price index		0.9	2.1	2.3	1.7	1.8	1.7	2.5	1.3	1.3	
PCE chn.-wt. price index		1.4	1.6	1.5	2.2	1.5	1.2	1.5	1.6	1.4	
Ex. food and energy											
CPI		1.5	2.6	3.4	1.8	2.2	1.9	3.4	1.5	1.6	
Ex. food and energy		2.3	2.0	2.6	2.7	2.0	1.2	2.1	2.0	1.8	
ECI, hourly compensation <sup>3</sup>		3.5	3.4	4.4	4.2	3.2	4.0	4.0	4.3	4.2	
Nonfarm business sector		2.7	3.4	2.1	3.3	3.5	5.6	2.8	1.7	2.2	
Output per hour		5.5	5.2	6.4	3.5	2.9	5.4	4.0	4.2	4.2	
Compensation per Hour		2.7	1.7	4.3	0.3	-0.6	-0.2	1.1	2.4	2.0	
Unit labor cost											

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.

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

Item	Units	2002 Q1	2002 Q2	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 Q3	2003 Q4	2004 Q1	2004 Q2
<b>Expenditures</b>											
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	10784.7
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	3.7
Personal cons. expenditures		1.8	2.8	2.9	2.5	2.7	3.9	5.0	3.6	4.1	1.6
Durables		-8.5	4.4	14.0	-2.4	-0.1	20.6	16.5	3.9	2.2	-0.3
Nondurables		3.8	0.8	-0.6	5.3	5.0	1.6	6.9	5.1	6.7	0.1
Services		3.3	3.5	2.4	2.2	2.1	1.8	1.9	2.8	3.3	2.7
Business fixed investment		-9.7	-9.6	-1.1	-3.2	-0.1	11.8	15.7	11.0	4.2	12.5
Equipment & Software		-6.3	-4.5	4.6	-2.0	4.5	11.0	21.7	12.0	8.0	14.2
Nonres. structures		-18.5	-22.6	-16.0	-6.6	-13.0	14.5	-1.3	7.9	-7.6	6.9
Residential structures		9.3	11.3	2.8	4.2	7.5	9.1	22.4	9.6	5.0	16.5
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	12.6
Gov't. cons. & investment		4.7	4.4	2.1	4.0	0.2	7.2	0.1	1.6	2.5	2.2
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	1.9
State & local		2.9	0.3	1.7	1.4	0.1	-0.5	2.2	-0.1	-0.0	1.9
Change in bus. inventories	Bill. Ch. \$	-7.4	7.9	22.7	23.8	9.6	-17.6	-3.5	8.6	40.0	61.1
Nonfarm		-11.9	16.1	24.6	25.3	9.6	-15.7	-2.7	4.6	34.5	58.8
Net exports		-444.9	-458.1	-469.8	-515.4	-511.7	-525.2	-508.7	-528.3	-550.1	-580.3
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 <sup>1</sup>	%	1.2	1.4	1.6	2.2	2.7	2.6	1.8	1.7	1.4	1.5
<b>Employment and Production</b>											
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	2.3	4.4	1.7	-2.3	-0.7	-4.0	4.1	5.7	5.6	4.3
Capacity util. rate - mfg.	%	73.0	73.6	74.0	73.5	73.5	73.0	73.7	74.8	75.6	76.5
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	13.14
Other		3.32	3.25	3.32	3.29	3.38	3.28	3.34	3.23	3.26	3.40
<b>Income and Saving</b>											
Nominal GNP	Bill. \$	10361.7	10461.6	10571.7	10661.2	10781.3	10929.0	11168.3	11358.1	11546.1	11693.6
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	6.4
Real disposable income		10.8	2.7	-1.7	0.2	1.8	4.3	8.2	1.4	2.4	2.8
Personal saving rate	%	2.7	2.7	1.6	1.2	1.0	1.1	1.9	1.3	1.0	1.3
Corp. profits, IVA & CCAdj.	% change	24.8	15.2	3.6	19.1	-1.5	36.7	32.0	30.2	13.6	2.9
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	-380.0
State & local surpl./def.		-28.8	-23.6	-21.3	-26.3	-49.0	-5.7	6.5	35.3	11.8	18.3
Ex. social ins. funds		-30.8	-25.3	-22.8	-27.6	-50.1	-6.7	5.4	34.1	10.6	16.9
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
<b>Prices and Costs</b>											
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	3.1
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 <sup>2</sup>		3.6	4.4	2.5	3.3	5.5	3.4	4.4	3.1	4.3	4.0
Nonfarm business sector		6.9	1.1	4.5	1.6	3.7	6.7	9.0	3.1	3.7	3.9
Output per hour		5.5	3.4	1.5	1.2	5.3	5.7	6.1	4.4	2.0	5.9
Compensation per hour		-1.4	2.3	-2.9	-0.3	1.6	-1.0	-2.7	1.2	-1.6	1.9
Unit labor cost											

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

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

Item	Units	Projected									
		2004 Q3	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4	2006 Q1	2006 Q2	2006 Q3	2006 Q4
<b>EXPENDITURES</b>											
Nominal GDP	Bill. \$	11814.9	11970.7	12120.2	12286.1	12454.6	12618.1	12793.0	12957.2	13120.8	13284.1
Real GDP	Bill. Ch. \$	10891.0	10983.9	11086.6	11194.8	11302.9	11407.7	11510.9	11613.6	11716.2	11819.4
Real GDP	% change	4.0	3.5	3.8	4.0	3.9	3.8	3.7	3.6	3.6	3.6
Gross domestic purchases		3.9	4.9	3.2	3.3	3.9	4.0	4.1	3.4	3.8	4.0
Final sales		5.0	2.7	3.5	5.1	4.1	3.6	3.3	4.1	3.5	3.3
Priv. dom. final purchases		5.8	5.0	2.8	4.7	4.3	4.1	4.1	4.1	4.1	4.1
Personal cons. expenditures		5.1	4.6	3.7	4.0	3.8	3.7	3.7	3.7	3.7	3.7
Durables		17.2	4.2	2.7	8.3	6.9	6.0	5.9	6.5	6.4	6.4
Nondurables		4.7	6.0	4.8	4.5	4.4	4.4	4.4	4.4	4.4	4.4
Services		3.0	4.0	3.3	2.9	2.9	2.9	2.9	2.9	2.8	2.8
Business fixed investment		13.0	8.3	-3.2	10.0	9.1	8.4	8.2	8.5	8.5	8.2
Equipment & Software		17.5	11.6	-5.1	12.5	10.7	9.3	9.4	9.9	10.1	9.8
Nonres. structures		-1.1	-2.5	3.2	2.2	3.7	5.3	4.3	3.7	3.1	2.6
Residential structures		1.6	3.9	3.1	4.2	1.5	1.8	1.4	1.1	0.4	1.0
Exports		6.0	-0.8	7.8	8.9	8.4	9.6	6.2	7.4	7.0	8.2
Imports		4.6	9.4	2.4	2.9	6.6	9.3	8.5	4.6	7.5	9.8
Gov't. cons. & investment		0.7	-0.5	3.9	2.9	2.7	2.7	2.4	2.4	2.4	2.5
Federal		4.8	-4.0	6.6	3.7	3.1	2.5	1.7	1.9	1.8	2.1
Defense		10.1	-7.1	8.9	4.9	4.2	3.7	2.0	2.3	2.3	2.8
State & local		-1.7	1.5	2.3	2.5	2.5	2.8	2.8	2.8	2.8	2.8
Change in bus. inventories	Bill. Ch. \$	34.5	54.8	62.3	32.6	29.0	33.0	44.0	31.5	33.5	40.9
Nonfarm		30.4	52.0	59.3	29.6	27.0	30.9	41.8	29.4	31.4	38.8
Net exports		-583.2	-624.2	-613.2	-601.1	-605.6	-618.2	-637.6	-636.6	-649.7	-669.7
Nominal GDP	% change	5.5	5.4	5.1	5.6	5.6	5.4	5.7	5.2	5.1	5.1
GDP Gap <sup>1</sup>	%	1.3	1.3	1.2	1.0	0.8	0.6	0.5	0.4	0.3	0.2
<b>EMPLOYMENT AND PRODUCTION</b>											
Nonfarm payroll employment	Millions	131.5	132.1	132.7	133.4	134.1	134.9	135.5	136.1	136.7	137.3
Unemployment rate	%	5.5	5.4	5.4	5.3	5.3	5.3	5.3	5.2	5.2	5.1
Industrial prod. index	% change	2.7	4.1	6.6	4.6	5.1	5.1	5.2	4.5	4.0	4.1
Capacity util. rate - mfg.	%	77.0	77.6	78.4	78.8	79.4	80.1	80.7	81.1	81.4	81.8
Housing starts	Millions	1.97	1.96	1.97	1.96	1.95	1.95	1.95	1.94	1.94	1.94
Light motor vehicle sales		17.07	17.20	16.88	17.28	17.50	17.58	17.65	17.79	17.93	18.08
North Amer. produced		13.80	13.56	13.51	13.77	13.98	14.04	14.11	14.23	14.33	14.46
Other		3.27	3.65	3.37	3.51	3.52	3.54	3.56	3.60	3.62	3.62
<b>INCOME AND SAVING</b>											
Nominal GNP	Bill. \$	11853.0	11979.2	12135.2	12286.0	12446.0	12600.7	12761.1	12918.3	13070.7	13217.8
Nominal GNP	% change	5.6	4.3	5.3	5.1	5.3	5.1	5.2	5.0	4.8	4.6
Nominal personal income		3.4	9.7	2.8	6.3	6.3	6.3	7.4	6.1	6.0	5.7
Real disposable income		2.0	7.7	0.1	4.4	4.5	4.7	5.8	4.5	4.5	4.2
Personal saving rate	%	0.5	1.2	0.4	0.5	0.7	0.9	1.4	1.6	1.8	1.9
Corp. profits, IVA & CCAdj.	% change	-17.7	37.8	6.4	0.1	0.8	-2.5	0.2	-0.2	-1.8	-3.6
Profit share of GNP	%	9.4	10.1	10.1	10.0	9.9	9.7	9.6	9.5	9.3	9.1
Excluding FR Banks		9.3	10.0	10.0	9.9	9.8	9.6	9.5	9.3	9.2	9.0
Federal surpl./deficit	Bill. \$	-384.1	-351.0	-294.3	-272.9	-252.9	-257.2	-312.8	-315.2	-323.1	-325.5
State & local surpl./def.		4.5	8.2	8.3	6.0	7.9	8.6	9.6	9.0	8.8	9.5
Ex. social ins. funds		3.0	6.6	6.7	4.4	6.3	7.0	8.0	7.4	7.2	7.9
Gross natl. saving rate	%	13.5	13.0	13.1	13.2	13.3	13.4	13.3	13.5	13.5	13.5
Net natl. saving rate		1.0	1.5	1.7	1.8	1.9	1.9	1.9	2.1	2.1	2.1
<b>PRICES AND COSTS</b>											
GDP chn.-wt. price index	% change	1.4	1.9	1.3	1.6	1.6	1.5	1.9	1.6	1.5	1.4
Gross Domestic Purchases chn.-wt. price index		1.9	2.4	1.5	1.6	1.4	1.3	1.6	1.3	1.3	1.3
PCE chn.-wt. price index		1.3	2.3	0.9	1.6	1.4	1.4	1.3	1.3	1.3	1.3
Ex. food and energy		0.9	1.4	1.4	1.6	1.6	1.5	1.4	1.4	1.4	1.4
CPI		1.9	3.4	1.0	1.8	1.7	1.6	1.6	1.6	1.6	1.6
Ex. food and energy		1.6	2.3	1.9	2.0	2.0	1.9	1.9	1.9	1.8	1.8
ECI, hourly compensation <sup>2</sup>		3.5	4.1	4.3	4.2	4.2	4.2	4.2	4.2	4.2	4.2
Nonfarm business sector		1.8	2.1	1.6	1.8	1.7	1.7	1.9	2.1	2.2	2.3
Output per hour		3.6	4.4	3.8	4.3	4.3	4.3	4.2	4.2	4.2	4.2
Compensation per hour		1.8	2.3	2.2	2.5	2.6	2.6	2.2	2.0	1.9	1.8
Unit labor cost											

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	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 Q3	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4	02Q4/ 01Q4	03Q4/ 02Q4	Projected 04Q4/ 03Q4
<b>Real GDP Gross dom. purchases</b>	2.6	0.7	1.9	4.1	7.4	4.2	4.5	3.3	4.0	2.3	4.4	3.8	3.8
<b>Final sales Priv. dom. final purchases</b>	2.0	0.7	2.4	5.1	6.8	3.7	3.3	2.5	5.0	1.2	4.5	3.4	4.7
<b>Personal cons. expenditures</b>	2.0	1.7	1.8	2.7	3.6	2.5	2.9	1.1	3.6	1.8	2.7	2.7	4.0
<b>Durables</b>	-1.2	-0.2	-0.0	1.6	1.4	0.5	0.2	-0.1	1.4	0.1	0.8	0.5	0.5
<b>Nondurables</b>	-0.1	1.0	1.0	0.3	1.4	1.0	1.3	0.0	0.9	0.5	0.9	0.9	0.9
<b>Services</b>	1.0	0.9	0.9	0.8	0.8	1.2	1.4	1.1	1.3	1.2	0.9	1.4	1.4
<b>Business fixed investment</b>	-0.1	-0.3	-0.0	1.1	1.5	1.1	0.4	1.2	1.3	-0.6	0.9	0.9	0.9
<b>Equipment &amp; Software</b>	0.3	-0.2	0.3	0.8	1.5	0.9	0.6	1.1	1.3	-0.2	0.9	1.0	1.0
<b>Nonres. structures</b>	-0.5	-0.2	-0.3	0.3	0.5	0.0	-0.2	0.2	0.0	-0.5	0.0	-0.0	-0.0
<b>Residential structures</b>	0.1	0.2	0.4	0.4	1.1	0.5	0.3	0.9	0.1	0.3	0.6	0.4	0.4
<b>Net exports</b>	-0.4	-1.7	0.1	-0.5	0.6	-0.7	-0.8	-1.1	-0.1	-0.9	-0.1	-0.9	-0.9
<b>Exports</b>	0.3	-0.4	-0.2	-0.2	1.0	1.6	0.7	0.7	0.6	0.3	0.6	0.5	0.5
<b>Imports</b>	-0.7	-1.3	0.3	-0.3	-0.4	-2.2	-1.5	-1.8	-0.7	-1.3	-0.7	-1.3	-1.3
<b>Government cons. &amp; invest.</b>	0.4	0.8	0.1	1.4	0.0	0.3	0.5	0.4	0.1	0.7	0.4	0.2	0.2
<b>Federal</b>	0.2	0.6	0.0	1.4	-0.2	0.3	0.5	0.2	0.3	0.5	0.4	0.2	0.2
<b>Defense</b>	0.1	0.5	-0.1	1.5	-0.4	0.5	0.5	0.1	0.5	0.3	0.4	0.2	0.2
<b>Nondefense</b>	0.1	0.0	0.2	-0.1	0.1	-0.2	0.0	0.1	-0.1	-0.0	0.2	0.0	0.0
<b>State and local</b>	0.2	0.2	0.0	-0.1	0.3	-0.0	0.0	0.2	-0.2	0.2	0.1	0.1	0.1
<b>Change in bus. inventories</b>	0.6	0.1	-0.5	-1.0	0.6	0.5	1.2	0.8	-1.0	1.1	-0.1	0.4	0.4
<b>NonFarm</b>	0.4	0.1	-0.5	-0.9	0.5	0.3	1.1	0.9	-1.0	1.0	-0.2	0.4	0.4
<b>Farm</b>	0.2	0.0	0.1	-0.1	0.1	0.2	0.1	-0.1	0.1	0.0	0.1	-0.0	-0.0

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

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	Projected								Projected	
	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4	2006 Q1	2006 Q2	2006 Q3	2006 Q4	2006 Q4/03Q4
Real GDP Gross dom. purchases	3.5 5.1	3.8 3.4	4.0 3.5	3.9 4.1	3.8 4.2	3.7 4.3	3.6 4.0	3.6 4.2	3.6 4.2	3.8 4.0
Final sales Priv. dom. final purchases	2.7 4.3	3.5 2.4	5.0 4.1	4.0 3.7	3.6 3.5	3.3 3.5	4.0 3.5	3.5 3.5	3.4 4.0	3.4 3.5
Personal cons. expenditures	3.2 0.4	2.6 0.2	2.8 0.7	2.7 0.6	2.6 0.5	2.6 0.5	2.6 0.5	2.6 0.5	2.7 0.5	2.7 0.5
Durables	1.2 1.6	1.0 1.4	0.9 1.2							
Nondurables										
Services										
Business fixed investment	0.8 0.9 -0.1 0.2	-0.3 -0.4 0.1 0.2	1.0 1.0 0.1 0.2	0.9 0.8 0.1 0.1	0.9 0.7 0.1 0.1	0.8 0.7 0.1 0.1	0.9 0.8 0.1 0.1	0.9 0.8 0.1 0.1	0.9 0.8 0.1 0.1	0.9 0.8 0.1 0.1
Equipment & Software										
Nonresidential structures										
Residential structures										
Net exports	-1.5 -0.1 -1.4	0.4 0.8 -0.4	0.4 0.9 -0.5	-0.2 -0.8 -1.0	-0.4 -1.0 -1.4	-0.7 -1.0 -1.3	0.0 0.6 -0.7	-0.4 0.8 -1.2	-0.7 0.8 -1.5	-0.9 0.5 -1.3
Exports										
Imports										
Government cons. & invest.	-0.1 -0.3 -0.3 0.1 0.2	0.7 0.4 0.4 0.0 0.3	0.5 0.2 0.2 0.0 0.3	0.5 0.2 0.2 0.0 0.3	0.5 0.2 0.2 0.0 0.3	0.5 0.1 0.1 0.0 0.3	0.5 0.1 0.1 0.0 0.3	0.5 0.1 0.1 0.0 0.3	0.5 0.1 0.1 0.0 0.3	0.2 0.2 0.2 0.0 0.3
Federal										
Defense										
Nondefense										
State and local										
Change in bus. inventories	0.8 0.8 -0.0	0.3 0.3 0.0	0.3 -1.1 -0.1	-1.1 -0.1 0.0	-0.1 0.1 0.0	0.1 0.4 0.0	0.4 -0.4 0.0	0.1 0.1 0.0	0.3 0.2 0.0	0.4 0.4 0.0
NonFarm										
Farm										

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

05Q4/04Q4

Item	Fiscal year			2004				2005				2006				
	2003 <sup>a</sup>	2004 <sup>a</sup>	2005	2006	Q1 <sup>a</sup>	Q2 <sup>a</sup>	Q3 <sup>a</sup>	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>Unified budget</b>																
Receipts <sup>1</sup>	1782	1880	2082	2223	410	550	479	487	437	636	522	524	470	678	551	536
Outlays <sup>1</sup>	2159	2292 <sup>2</sup>	2447	2580	580	576	565	606	620	608	612	633	645	636	660	
Surplus/deficit <sup>1</sup>	-377	-412	-365	-358	-171	-26	-86	-119	-183	27	-90	-109	-196	32	-85	-125
On-budget	-538	-568	-539	-537	-193	-99	-96	-172	-217	-49	-102	-151	-234	-52	-100	-171
Off-budget	161	155	174	180	23	73	10	53	34	76	12	42	39	84	14	46
Means of financing																
Borrowing	374	378	371	365	136	41	83	103	152	19	98	94	180	-3	94	115
Cash decrease	26	-1	1	0	12	-23	8	12	15	-35	10	10	15	-25	0	10
Other <sup>2</sup>	-22	35	-8	-7	23	8	-6	4	17	-11	-17	5	0	-4	-8	-0
Cash operating balance, end of period	35	36	35	35	21	45	36	25	10	45	35	25	10	35	35	25
<b>NIPA federal sector</b>																
Receipts	1863	1930	2150	2298	1915	1949	1957	2020	2152	2190	2236	2260	2295	2309	2329	2352
Expenditures	2209	2314	2442	2600	2306	2329	2341	2371	2446	2463	2489	2517	2608	2624	2652	2677
Consumption expenditures	646	694	732	770	691	700	713	709	732	740	747	753	770	776	781	788
Defense	425	469	499	530	465	474	487	480	498	505	511	517	529	534	538	544
Nondefense	221	225	233	241	226	227	226	229	234	235	236	236	241	242	243	244
Other spending	1563	1620	1711	1830	1615	1629	1628	1662	1714	1742	1764	1838	1848	1871	1890	
Current account surplus	-345	-384	-293	-302	-391	-380	-384	-351	-294	-273	-253	-257	-313	-315	-323	-326
Gross investment	92	102	108	114	102	104	104	104	107	109	111	113	114	115	116	117
Gross saving less gross investment <sup>3</sup>	-347	-393	-305	-317	-402	-391	-395	-361	-307	-286	-267	-272	-328	-330	-338	-341
<b>Fiscal indicators<sup>4</sup></b>																
High-employment (HEB) surplus/deficit	-271	-343	-270	-301	-354	-345	-352	-318	-268	-253	-240	-250	-310	-317	-328	-335
Change in HEB, percent of potential GDP	1.2	0.5	-0.7	0.1	0.2	-0.1	0.0	-0.3	-0.4	-0.1	0.1	0.4	0.0	0.1	0.0	0.0
Fiscal impetus (FI) Percent of GDP	1.0	0.9	0.0	0.3	0.2	0.1	0.1	0.1	-0.2	0.1	0.1	0.0	0.1	0.1	0.1	0.0

1. CBO's January 2005 baseline surplus estimates are -\$412 billion in FY 2004, -\$368 billion in FY 2005 and -\$295 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)  
Class II FOMC**

**Change in Debt of the Domestic Nonfinancial Sectors  
(Percent)**

January 26, 2005

Period <sup>1</sup>	Total	Federal government	Nonfederal				Memo: Nominal GDP	
			Households		Business	State and local governments		
			Total	Home mortgages				
<i>Year</i>								
1999	6.4	-1.9	8.9	8.3	9.2	7.8	10.7	
2000	4.9	-8.0	8.3	8.6	8.3	10.7	9.4	
2001	6.2	-0.2	7.6	8.8	9.7	8.0	6.0	
2002	6.9	7.6	6.7	9.6	11.9	4.4	2.7	
2003	8.1	10.9	7.5	10.0	12.4	4.5	11.1	
2004	7.8	9.0	7.6	9.7	11.6	4.5	3.8	
2005	7.2	8.2	7.0	8.1	8.9	6.1	5.0	
2006	6.6	8.1	6.3	6.9	7.4	5.8	5.0	
<i>Quarter</i>								
2004:1	9.2	12.0	8.6	11.4	13.2	6.2	4.8	
2	6.9	10.7	6.1	8.5	9.8	1.8	3.6	
3	7.1	4.9	7.6	9.2	11.4	6.1	5.1	
4	7.2	7.3	7.2	8.3	9.9	3.5	6.3	
2005:1	8.3	12.4	7.4	8.5	9.7	5.6	6.2	
2	7.0	7.9	6.8	8.0	8.7	6.2	6.0	
3	6.4	5.7	6.6	7.5	8.1	6.2	6.0	
4	6.3	6.0	6.4	7.2	7.8	6.0	5.9	
2006:1	7.7	13.9	6.3	7.0	7.5	5.9	6.0	
2	6.0	5.5	6.2	6.8	7.3	5.8	6.0	
3	5.9	5.0	6.1	6.6	7.1	5.6	6.0	
4	6.2	7.2	6.0	6.5	7.0	5.4	6.0	

Note. Quarterly data are at seasonally adjusted annual rates.

1. Data after 2004:Q3 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 FOMC**
**Flow of Funds Projections: Highlights  
(Billions of dollars at seasonally adjusted annual rates except as noted)**

January 26, 2005

Category	2003	2004	2005	2006	2004				2005				2006				
					Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
<i>Net funds raised by domestic nonfinancial sectors</i>																	
1 Total	1600.6	1536.2	1512.2	1625.8	1440.8	1312.0	1732.7	1492.0	1390.7	1433.4	1883.5	1507.5	1496.4	1616.1			
2 Net equity issuance	-57.8	-210.1	-215.0	-81.0	-203.2	-395.2	-264.0	-226.0	-205.0	-165.0	-103.0	-79.0	-71.0	-71.0			
3 Net debt issuance	1658.4	1746.3	1727.2	1706.8	1644.0	1707.2	1966.7	1718.0	1595.7	1598.4	1986.5	1586.5	1567.4	1687.1			
<i>Borrowing sectors</i>																	
Nonfinancial business																	
4 Financing gap <sup>1</sup>	-21.1	27.7	-20.5	145.9	-37.3	156.3	-33.9	-38.7	-15.8	6.3	136.5	127.8	146.2	172.9			
5 Net equity issuance	-57.8	-210.1	-215.0	-81.0	-203.2	-395.2	-264.0	-226.0	-205.0	-165.0	-103.0	-79.0	-71.0	-71.0			
6 Credit market borrowing	303.8	374.1	481.4	508.3	389.2	480.3	482.5	476.0	481.8	485.1	499.2	503.0	511.6	519.5			
Households																	
7 Net borrowing <sup>2</sup>	840.7	894.8	817.2	758.5	897.3	824.2	867.4	825.2	796.2	780.1	770.7	760.0	752.9	750.5			
8 Home mortgages	734.9	769.4	658.8	600.7	800.9	721.5	718.7	663.5	633.6	619.6	610.2	600.9	595.3	596.2			
9 Consumer credit	88.4	91.6	131.5	131.7	127.8	73.3	120.7	134.5	136.2	134.6	134.5	133.0	131.4	127.9			
10 Debt/DPI (percent) <sup>3</sup>	108.0	112.5	116.5	117.8	113.9	113.6	115.7	116.4	116.9	117.3	117.4	117.7	118.0	118.3			
State and local governments																	
11 Net borrowing	117.8	114.6	66.2	54.8	150.5	87.9	99.6	57.8	53.8	53.8	54.8	54.8	54.8	54.8			
12 Current surplus <sup>4</sup>	176.2	189.3	169.6	176.7	198.4	166.7	168.1	167.1	170.4	172.6	175.0	175.7	177.0	179.1			
Federal government																	
13 Net borrowing	396.0	362.7	362.4	385.2	207.0	314.9	547.1	358.9	263.9	279.4	661.8	268.7	248.2	362.3			
14 Net borrowing (n.s.a.)	396.0	362.7	362.4	385.2	83.4	102.8	151.7	19.2	97.6	93.9	180.3	-3.4	93.7	114.6			
15 Unified deficit (n.s.a.)	399.1	400.7	355.0	373.2	85.7	118.6	183.1	-27.3	90.3	108.8	195.7	-32.3	85.3	124.5			
<i>Depository institutions</i>																	
16 Funds supplied	476.4	671.5	558.3	565.9	438.9	378.3	600.3	500.4	597.0	535.5	647.3	500.4	594.0	522.1			
Memo (percentage of GDP)																	
17 Domestic nonfinancial debt <sup>5</sup>	194.5	197.3	201.2	204.0	197.9	198.9	200.2	201.3	201.9	202.5	203.2	204.1	204.5	205.1			
18 Domestic nonfinancial borrowing	15.1	14.9	14.0	13.1	13.9	14.3	16.5	14.0	12.8	12.7	15.5	12.2	11.9	12.7			
19 Federal government <sup>6</sup>	3.6	3.1	2.9	3.0	1.8	2.6	4.5	2.9	2.1	2.2	5.2	2.1	1.9	2.7			
20 Nonfederal	11.5	11.8	11.0	10.1	12.2	11.6	12.0	11.1	10.7	10.5	10.4	10.2	10.1	10.0			

Note. Data after 2004:Q3 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

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Although foreign economic growth has slowed somewhat from the first half of 2004, there has been little in recent data to alter our view that the global economy will pick up going forward. The primary causes of the slowdown—higher oil prices and softness in exports resulting from some cooling of high-tech demand and, in some cases, domestic currency appreciation—are expected to abate, and the data suggest that China, in particular, will continue to grow robustly. As a result, projected foreign GDP growth throughout the forecast period is little changed from the December Greenbook.

### Summary of Staff Projections

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

Indicator	2004		Projection				2006	
	H1	Q3	2004: Q4	2005				
				Q1	Q2	H2		
Foreign output <i>December GB</i>	4.1 4.1	2.6 2.7	3.1 3.1	3.0 3.0	3.3 3.2	3.4 3.2	3.3 3.2	
Foreign CPI <i>December GB</i>	2.9 2.8	2.9 2.8	2.3 2.6	1.7 2.0	2.2 2.2	2.2 2.2	2.2 2.2	

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

The third-quarter slowdown in foreign industrial economies continued into the fourth quarter, but we project their average GDP growth to firm slightly by the middle of 2005. In emerging market economies, average GDP growth is estimated to have picked up to 4¾ percent in the fourth quarter from 3¾ percent in the third quarter and is projected to maintain roughly that pace through the forecast period.

The spot price of West Texas intermediate (WTI) crude oil has risen since late December to around \$49 per barrel, about \$6 higher than its December average. We now project the spot price will decline to \$43 per barrel by the end of the forecast period.

The foreign exchange value of the dollar, although experiencing high day-to-day volatility, has changed little on a trade-weighted basis since the December FOMC meeting. In part reflecting some appreciation between the day of the December Greenbook and the FOMC meeting, the starting point for the projected path of the exchange value of the broad real dollar is 1¼ percent higher than in the previous forecast. From there, we continue to project that the dollar will depreciate at an annual rate of

### Staff Projections of Selected Trade Prices

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

Indicator	2004		Projection				2006	
	H1	Q3	2004: Q4	2005				
				Q1	Q2	H2		
<i>Exports</i>								
Core goods	6.9	1.9	5.4	2.2	2.3	1.8	2.3	
<i>Imports</i>								
Non-oil core goods	5.2	2.3	4.4	3.3	.8	.6	.2	
Oil (dollars per barrel)	34.55	37.54	40.60	41.57	42.46	41.24	39.59	

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.

### Trade in Goods and Services

Since the December Greenbook we have received trade data for October and November. Nominal imports of goods and services grew briskly in both these months after declining slightly in September. Real imports of goods and services are now estimated to have climbed almost 9½ percent in the fourth quarter, up from relatively subdued growth of 4½ percent in third quarter. This estimate is about 1¾ percentage points higher than in the December Greenbook, reflecting stronger-than-anticipated data. While much of the pickup in import growth from its third-quarter pace resulted from a surge in real oil imports, strength was widespread across different categories of core imports as well, despite rising import prices.

In the first two quarters of 2005, real import growth is projected to slow to below 3 percent, as oil import growth drops back precipitously and as capital goods imports weaken in response to the expiration of partial expensing tax incentives. Largely as a consequence, total real import growth is expected to moderate to about 5¼ percent in 2005, following growth of 9¼ percent in 2004. This projection is about ¾ percentage points lower than in the December Greenbook, mainly reflecting the impact of slightly higher core import prices on core imports, as well as a decrease in our projection for real oil imports. Real import growth is projected to pick up to over 7½ percent in 2006, as oil imports bottom out and imports of core goods and services accelerate. The pickup in imports of core goods reflects the recovery of capital goods imports as well as the waning impact of sizeable recent increases in core import prices. Similarly, imports of services

accelerate with the diminishing effect of the recent sharp rise in their prices, which have been boosted by the fall in the dollar late last year.

Nominal exports increased slightly in October before plummeting in November. The unexpectedly weak data led us to revise our forecast of real exports down to a decline of  $\frac{3}{4}$  percent in the fourth quarter, a dramatic markdown from the  $1\frac{1}{4}$  percent growth projected in the December Greenbook. Although services and high-tech exports also were disappointing, the shortfall in overall exports came primarily from an estimated 5 percent falloff in real core exports, with weakness widespread within this category. Because none of the fundamental determinants of exports moved in such a way as to explain the negative surprise, we see no reason to carry this weakness forward in our projection. Accordingly, we expect a portion of the shortfall to be made up subsequently, and real exports are projected to grow  $7\frac{3}{4}$  percent in the first quarter, up  $1\frac{1}{4}$  percentage points from the December Greenbook.

In 2005 as a whole, real export growth is expected to pick up to  $8\frac{3}{4}$  percent. This rise reflects both the first-quarter bounce-back—which explains the upward revision in the forecast for this year—and the lagged effects of the previous decline in the dollar on core exports and services. As the positive effect of the lower dollar dissipates, reducing support for exports of core goods and services, real export growth is expected to moderate to  $7\frac{1}{4}$  percent in 2006. This growth is a bit lower than in the December Greenbook, reflecting the higher projected path for the dollar. Foreign GDP growth remains steady throughout the forecast period, and thus has little impact on the pattern of export growth.

**Summary of Staff Projections  
for Trade in Goods and Services**  
(Percent change from end of previous period, s.a.a.r.)

Indicator	2004		Projection					2006	
	H1	Q3	2004: Q4	2005					
				Q1	Q2	H2			
Real exports	7.3	6.0	-.8	7.8	8.9	9.0	7.2		
<i>December GB</i>	7.3	6.3	10.2	6.5	8.5	9.2	7.6		
Real imports	11.6	4.6	9.4	2.4	2.9	7.9	7.6		
<i>December GB</i>	11.6	6.0	7.6	4.4	3.1	8.1	8.1		

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

### Alternative Simulation

Despite a 15 percent depreciation of the dollar on a real trade-weighted basis since early 2002, the upward pressure on import prices has been relatively modest. However, it is possible that foreign profit margins may have reached unsustainably low levels and that foreign producers will increase the prices of their exports to the United States more than in the baseline forecast. Accordingly, in our alternative scenario, we consider the effects of an exogenous rise in U.S. core import prices, beginning in the first quarter of 2005, that raises import prices by 5 percent relative to baseline by the end of this year.

The rise in import prices boosts U.S. real GDP growth roughly 0.4 percentage point above baseline in 2005 and 2006. Real GDP rises because higher import prices induce expenditure switching toward relatively cheaper U.S.-produced goods and because real exports increase as foreign producers spend on U.S. goods some of their increased revenues. The import-price hike boosts core consumer price inflation about 0.3 percentage point in 2005 and a bit less in 2006. Although higher import prices induce an immediate expansion of the trade deficit of 0.4 percentage point of GDP relative to baseline, this deterioration is largely reversed after a year by the gradual fall in real imports and modest export expansion.

**Alternative Simulation:  
The Effect of Higher U.S. Import Prices**  
(Percent change from previous period, annual rate)

Indicator and simulation	2005		2006	
	H1	H2	H1	H2
<i>U.S. real GDP</i>				
Baseline	3.9	3.8	3.6	3.6
Higher import prices	4.1	4.3	4.1	4.0
<i>U.S. PCE prices excluding food and energy</i>				
Baseline	1.5	1.6	1.4	1.4
Higher import prices	2.0	1.8	1.6	1.5
<i>U.S. trade balance (share of GDP)</i>				
Baseline	-5.6	-5.4	-5.4	-5.4
Higher import prices	-6.0	-5.6	-5.5	-5.5

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

January 26, 2005

Measure and country	1998	1999	2000	2001	2002	2003	2004	2005	2006	-----Projected-----
<b>REAL GDP (1)</b>										
Total foreign	1.5	5.0	4.2	0.3	3.0	2.8	3.5	3.3	3.3	
Industrial Countries of which:	2.7	4.4	3.5	0.8	2.6	1.6	2.4	2.4	2.4	
Canada	4.4	5.9	4.1	-1.4	3.8	1.7	3.0	3.0	3.0	
Japan	-1.2	0.1	3.2	-2.0	1.4	2.0	1.8	1.4	1.8	
United Kingdom	2.8	3.3	3.0	-2.2	1.9	2.7	2.8	2.5	2.2	
Euro Area (2)	2.0	3.9	2.7	0.8	1.1	0.8	1.7	1.5	1.6	
Germany	0.7	3.3	1.9	0.5	0.5	0.0	1.1	1.0	1.3	
Developing Countries Asia	-0.3	6.0	5.3	-0.4	3.5	4.4	5.2	4.6	4.5	
Korea	-2.2	8.6	5.9	0.9	5.8	6.2	5.8	5.0	5.0	
China	-5.4	11.4	4.5	4.7	7.7	4.1	2.8	3.9	4.2	
Latin America	9.8	17.0	7.6	6.9	8.3	10.0	9.5	7.1	7.5	
Mexico	1.2	4.2	4.4	-1.3	1.4	2.3	4.5	4.1	4.2	
Brazil	2.9	5.4	4.8	-1.2	1.9	2.0	4.1	4.1	4.3	
-1.7	3.5	3.9	-0.9	4.2	0.8	4.9				
<b>CONSUMER PRICES (3)</b>										
Industrial Countries of which:	0.9	1.1	1.7	0.9	2.1	1.3	1.7	1.2	1.4	
Canada	1.1	2.4	3.1	1.1	3.9	1.7	2.3	1.6	2.0	
Japan	0.7	-1.1	-1.2	-1.3	-0.5	-0.4	0.3	-0.5	0.2	
United Kingdom (4)	1.4	-1.2	-1.0	-1.0	-1.5	1.3	1.4	-1.8	1.8	
Euro Area (2)	0.9	1.5	2.5	2.1	2.3	2.1	2.3	1.8	1.7	
Germany	0.3	1.1	1.7	1.5	1.2	1.2	2.1	1.1	0.7	
Developing Countries Asia	9.0	4.6	4.1	2.8	2.9	3.0	3.9	3.1	3.0	
Korea	4.4	0.1	1.8	1.1	0.7	2.1	3.0	2.4	2.3	
China	5.8	1.2	2.6	3.4	3.4	3.5	3.4	4.0	3.3	
Latin America	-1.2	-1.0	0.9	-0.1	-0.6	2.6	3.2	1.7	1.9	
Mexico	15.4	12.5	8.4	5.3	6.4	5.0	5.6	4.3	4.2	
Brazil	17.3	13.5	8.7	5.1	5.3	3.9	5.3	3.8	3.8	
2.0	8.4	6.4	7.5	10.7	11.5	7.2	5.7	5.1	5.7	

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.

Measure and country	2004				2005				Projected				2006			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>REAL GDP (1)</b>																
Total foreign	4.7	3.6	2.6	3.1	3.0	3.3	3.4	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Industrial Countries of which:	3.2	2.5	1.9	2.0	2.1	2.4	2.5	2.6	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4
Canada	2.7	3.9	3.2	2.2	2.6	2.9	3.2	3.3	3.1	3.1	3.1	3.0	3.0	3.0	3.0	3.0
Japan	6.8	-0.6	0.2	1.0	1.2	1.4	1.5	1.6	1.7	1.8	1.8	1.8	1.8	1.8	1.8	1.8
United Kingdom	3.0	3.5	1.8	3.0	2.1	2.6	2.6	2.6	2.3	2.2	2.2	2.2	2.2	2.2	2.2	2.2
Euro Area (2)	2.7	1.7	1.1	1.4	1.4	1.5	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
Germany	1.7	1.7	0.4	0.6	0.8	1.0	1.1	1.2	1.2	1.2	1.2	1.3	1.3	1.3	1.3	1.3
Developing Countries	7.0	5.1	3.8	4.8	4.4	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
Asia	8.0	5.1	4.8	5.5	4.8	5.2	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
Korea	3.0	2.6	2.6	3.0	3.5	4.0	4.0	4.2	4.3	4.2	4.2	4.2	4.2	4.2	4.2	4.2
China	14.4	2.8	10.1	11.2	7.1	7.1	7.1	7.1	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5
Latin America	6.1	4.9	2.9	4.0	4.0	4.0	4.1	4.1	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
Mexico	5.5	4.5	2.6	4.0	4.0	4.1	4.2	4.3	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
Brazil	7.5	5.5	4.2	2.5	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
<b>CONSUMER PRICES (3)</b>																
Industrial Countries of which:	0.8	1.6	1.5	1.7	1.7	1.4	1.5	1.2	1.3	1.4	1.4	1.4	1.4	1.4	1.4	1.4
Canada	0.8	2.2	2.0	2.3	2.3	1.7	1.9	1.6	1.7	1.9	1.9	2.0	2.0	2.0	2.0	2.0
Japan	-0.3	-0.2	0.3	0.3	-0.2	-0.2	-0.2	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
United Kingdom (4)	1.2	1.4	1.3	1.4	1.6	1.8	1.9	1.8	1.7	1.7	1.7	1.8	1.8	1.8	1.8	1.8
Euro Area (2)	1.7	2.3	2.3	2.3	2.4	2.1	2.0	1.8	1.8	1.8	1.8	1.7	1.7	1.7	1.7	1.7
Germany	1.0	1.9	2.0	2.1	2.1	1.7	1.5	1.1	1.1	1.1	1.1	0.9	0.9	0.9	0.9	0.9
Developing Countries	3.0	3.7	4.5	3.9	3.6	3.3	2.8	3.1	3.2	3.2	3.2	3.1	3.1	3.1	3.1	3.1
Asia	2.3	3.4	4.3	3.0	2.8	2.2	1.6	2.4	2.5	2.5	2.5	2.4	2.4	2.4	2.4	2.4
Korea	3.3	3.4	4.3	3.4	3.5	4.1	3.5	4.0	3.9	3.9	3.9	3.6	3.6	3.6	3.6	3.6
China	2.8	4.4	5.3	3.2	2.6	1.4	0.6	1.7	2.0	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Latin America	4.7	4.6	5.2	5.6	5.2	4.9	4.9	4.9	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
Mexico	4.3	4.3	4.8	5.3	4.8	4.9	4.5	3.8	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Brazil	6.8	5.5	6.8	7.2	7.2	7.0	6.1	5.7	5.7	5.7	5.7	5.2	5.2	5.2	5.2	5.2

- 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.

	1998	1999	2000	2001	2002	2003	---- 2004	---- 2005	Projected 2006
<b>NIPA REAL EXPORTS and IMPORTS</b>									
Percentage point contribution to GDP growth, Q4/Q4									
Net Goods & Services	-1.1	-1.0	-0.9	-0.2	-0.9	-0.1	-0.9	0.0	-0.4
Exports of G&S	0.3	0.6	0.7	-1.3	0.3	0.6	0.5	0.9	0.7
Imports of G&S	-1.4	-1.6	-1.6	1.1	-1.1	-0.7	-1.3	-0.8	-1.2
Percentage change, Q4/Q4									
Exports of G&S Services	2.6	5.6	6.5	-11.9	3.5	6.1	4.9	8.7	7.2
Computers	4.4	5.3	1.8	-8.9	9.8	3.8	4.6	6.7	5.9
Semiconductors	7.3	13.4	22.7	-23.5	-1.9	11.2	2.5	14.8	14.4
Other Goods 1/	9.5	34.6	27.6	-34.6	9.9	38.8	-3.9	26.5	29.1
Imports of G&S Services	1.2	3.3	5.9	-10.2	0.4	5.0	5.8	8.2	6.2
Oil	11.0	12.1	11.2	-7.6	9.7	4.9	9.3	5.2	7.6
Computers	10.4	6.5	10.7	-5.9	8.9	3.7	1.7	3.8	4.5
Semiconductors	4.2	-3.4	13.3	3.7	4.2	1.8	9.9	-5.7	1.8
Other Goods 2/	26.4	26.0	13.9	-13.6	13.4	16.9	21.6	13.7	17.5
Net Goods & Services	-7.7	34.2	22.8	-51.1	10.0	0.3	14.1	22.1	29.1
Exports of G&S	11.2	12.9	10.5	-6.5	9.9	4.9	10.0	6.7	8.2
Imports of G&S									
Net Goods & Services	-203.8	-296.2	-379.5	-399.1	-472.1	-518.5	-584.5	-609.5	-648.4
Exports of G&S	966.5	1008.2	1096.3	1036.7	1012.4	1031.8	1117.5	1187.7	1279.6
Imports of G&S	1170.3	1304.5	1475.8	1435.8	1484.4	1550.2	1702.0	1797.3	1927.9
Billions of Chained 2000 Dollars									
US CURRENT ACCOUNT BALANCE									
Current Acct as Percent of GDP	-209.6	-296.8	-413.5	-385.7	-473.9	-530.7	-669.9	-781.3	-848.3
-2.4	-3.2	-4.2	-3.8	-4.5	-4.5	-4.8	-5.7	-6.3	-6.5
Net Goods & Services (BOP)	-164.9	-263.3	-378.4	-362.7	-421.7	-496.5	-617.3	-681.8	-704.8
Investment Income, Net	8.3	18.4	25.3	28.7	12.6	38.8	26.1	-14.2	-58.2
Direct Net Portfolio, Net	65.5	78.2	94.9	115.9	100.8	118.9	129.4	142.2	150.2
-57.2	-59.8	-69.7	-87.2	-88.2	-80.1	-103.2	-156.3	-208.4	
Other Income & Transfers, Net	-53.0	-52.0	-60.4	-51.7	-64.8	-72.9	-78.8	-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

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	2004								2005								Projected								2006							
	Q1				Q2				Q3				Q4				Q1				Q2				Q3				Q4			
	NIPA REAL EXPORTS and IMPORTS								Percentage point contribution to GDP growth								s.a.a.r.								s.a.a.r.							
Net Goods & Services	-0.8	-1.1	-0.1	-1.5	-0.1	-1.5	-0.4	0.4	0.4	0.9	0.8	-0.2	-0.4	-0.4	-0.4	0.0	0.0	-0.4	-0.4	0.0	0.0	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7				
Exports of G&S	0.7	0.7	0.6	0.7	0.6	0.7	0.4	0.8	0.8	0.9	0.9	-1.0	-1.0	-1.0	-1.0	-0.6	-0.6	0.8	0.8	-0.7	-0.7	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2				
Imports of G&S	-1.5	-1.8	-0.7	-0.7	-1.4	-1.4	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3			
Exports of G&S								Percentage change from previous period, s.a.a.r.								s.a.a.r.								s.a.a.r.								
Services	7.3	7.3	6.0	-0.8	7.8	8.9	8.4	8.4	8.4	9.6	9.6	9.6	9.6	9.6	9.6	9.6	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	8.2	
Computers	3.4	10.2	-1.8	-22.4	0.3	16.5	14.1	14.1	14.1	14.3	14.3	14.3	14.3	14.3	14.3	14.3	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4	14.4		
Semiconductors	-8.3	-10.1	-20.7	6.6	19.3	28.5	29.2	29.2	29.2	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1			
Other Goods 1/	10.1	7.7	11.1	-4.9	6.9	8.5	7.7	7.7	7.7	9.8	9.8	9.8	9.8	9.8	9.8	9.8	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	8.0	
Imports of G&S								Percentage point contribution to GDP growth								s.a.a.r.								s.a.a.r.								
Services	10.6	12.6	4.6	9.4	2.4	2.9	6.6	6.6	6.6	9.3	9.3	8.5	8.5	8.5	8.5	8.5	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	9.8	
Oil	3.9	-33.1	2.8	-7.0	2.5	-5.5	-5.5	-5.5	-5.5	-4.6	-4.6	-4.6	-4.6	-4.6	-4.6	-4.6	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	11.4	
Computers	12.8	38.6	29.9	7.5	4.1	-16.7	16.7	16.7	16.7	17.3	17.3	17.3	17.3	17.3	17.3	17.3	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5		
Semiconductors	42.2	21.2	7.4	-8.5	4.1	28.2	28.2	28.2	28.2	29.2	29.2	29.2	29.2	29.2	29.2	29.2	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1	29.1			
Other Goods 2/	8.9	19.6	3.7	8.3	3.7	7.3	7.3	7.3	7.3	7.9	7.9	8.0	8.0	8.0	8.0	8.0	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3			
Billions of Chained 2000 Dollars, s.a.a.r.								Billions of Chained 2000 Dollars, s.a.a.r.								s.a.a.r.								s.a.a.r.								
Net Goods & Services	-550.1	-580.3	-583.2	-624.2	-613.2	-601.1	-605.6	-618.2	-618.2	-637.6	-636.6	-636.6	-636.6	-636.6	-636.6	-636.6	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7	-649.7		
Exports of G&S	1095.4	1114.8	1131.1	1128.9	1150.2	1175.0	1199.0	1226.8	1226.8	1245.5	1245.5	1245.5	1245.5	1245.5	1245.5	1245.5	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1267.9	1315.3	
Imports of G&S	1645.5	1695.1	1714.3	1753.1	1763.4	1776.1	1804.5	1845.0	1845.0	1883.1	1883.1	1883.1	1883.1	1883.1	1883.1	1883.1	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	1904.4	
US CURRENT ACCOUNT BALANCE								Billions of dollars, s.a.a.r.								s.a.a.r.								s.a.a.r.								
Current Account as % of GDP	-5.1	-5.6	-5.6	-6.5	-6.5	-7.4	-7.4	-7.4	-7.4	-7.3	-7.3	-7.3	-7.3	-7.3	-7.3	-7.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	-6.3	
Net Goods & Services (BOP)	-554.4	-604.3	-621.4	-688.9	-686.1	-676.4	-677.4	-677.4	-677.4	-687.5	-687.5	-687.5	-687.5	-687.5	-687.5	-687.5	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-702.6	-719.7	
Investment Income, Net	54.3	26.3	26.8	-2.8	3.7	-11.4	-20.0	-28.9	-28.9	-43.3	-43.3	-43.3	-43.3	-43.3	-43.3	-43.3	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-143.7	-77.7
Direct, Net Portfolio, Net	139.1	125.1	125.6	127.7	139.7	142.5	142.8	143.7	143.7	147.9	147.9	147.9	147.9	147.9	147.9	147.9	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-172.5	-156.7
Other Inc. & Transfers, Net	-88.5	-79.5	-64.3	-82.7	-92.4	-82.5	-82.9	-83.3	-83.3	-92.4	-92.4	-92.4	-92.4	-92.4	-92.4	-92.4	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-82.5	-83.3

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

## **Part 2**

January 26, 2005

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# **CURRENT ECONOMIC AND FINANCIAL CONDITIONS**

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## **Recent Developments**

Confidential (FR) Class III FOMC

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January 26, 2005

## **Recent Developments**

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

### CBO Budget Projections and Economic Assumptions

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
<b>Baseline budget projections<sup>1</sup> (fiscal years)</b>	Billions of dollars										
Total surplus	-368	-295	-261	-235	-207	-189	-80	71	85	115	141
On-budget	-541	-484	-471	-464	-454	-451	-357	-217	-212	-190	-169
Off-budget	173	190	210	229	246	262	277	289	298	305	310
<b>Adjusted budget (fiscal years)</b>											
Adjusted surplus	-398	-384	-390	-381	-362	-346	-397	-376	-404	-421	-443
Total adjustments	-30	-89	-129	-146	-155	-157	-317	-447	-489	-536	-584
Iraq	-30	-70	-75	-65	-45	-30	-25	-26	-27	-27	-28
Expiring taxes	0	-16	-45	-65	-86	-95	-248	-358	-378	-401	-422
Debt service	0	-3	-9	-16	-24	-32	-44	-63	-84	-108	-134
<b>Economic assumptions (calendar years)</b>	Percent change, year over year										
Nominal GDP	5.7	5.3	5.4	5.2	5.0	4.8	4.6	4.5	4.5	4.4	4.4
Real GDP	3.8	3.7	3.7	3.4	3.1	2.9	2.8	2.7	2.7	2.6	2.5
CPI-U	2.4	1.9	2.1	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
	Percent, annual average										
Unemployment rate	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
Treasury yields											
Three-month	2.8	4.0	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
Ten-year	4.8	5.4	5.5	5.5	5.5	5.5	5.5	5.5	5.5	5.5	5.5

1. The on-budget surplus excludes the Social Security surplus and the Postal Service (which are off-budget). The baseline assumes that budget authority for discretionary programs grows with inflation after fiscal 2005. In addition, it assumes that no new mandatory spending or tax legislation is enacted.

Source. Congressional Budget Office, *The Budget and Economic Outlook* (January 2005).

**Venezuelan Economic Indicators**  
 (Percent change from previous period, s.a., except as noted)

Indicator	2003	2004	2004					
			Q3	Q4	Oct.	Nov.	Dec.	
Real GDP <sup>1</sup>		7.0	n.a.	-.8	n.a.	...	...	...
Unemployment rate <sup>2</sup>	18.0	15.1	14.5	14.1	14.3	14.7	13.2	
Consumer prices <sup>3</sup>	27.1	19.2	21.5	19.5	19.7	19.5	19.2	
Non-oil trade balance <sup>4</sup>	-5.5	n.a.	23.7	n.a.	n.a.	n.a.	n.a.	
Trade balance <sup>4</sup>	16.5	n.a.	53.5	n.a.	n.a.	n.a.	n.a.	
Current account <sup>5</sup>	11.5	n.a.	16.4	n.a.	...	...	...	

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Russia**, real GDP slid ½ percent in the third quarter, as the strong contribution by exports was not enough to offset surging imports and declining investment. While November indicators of economic activity were quite strong across a range of sectors, industrial production was flat in December, bringing full-year growth to 6 percent. Consumer price inflation edged down to 0.7 percent in December from 0.9 in November, although full-year inflation was 11.6 percent, well above the government's 8-10 percent inflation projection.

The government auctioned Yukos' key production facility, Yuganskneftegaz, on December 19. Before the auction, Yukos' management filed for Chapter 11 bankruptcy protection in Houston. The auction, however, took place as scheduled, and the winner was Baikal Finance Group, with a bid of \$9.4 billion dollars, above the \$8.7 billion minimum price but less than the amount of Yukos' tax bill. There was some uncertainty over the winner's identity for several days until state-owned Rosneft, which is in the process of merging with Gazprom, purchased the financing group, effectively re-nationalizing the facility. The bankruptcy filing severely complicated the Kremlin's plan for merging Gazprom, Rosneft, and Yuganskneftegaz, with Russian officials saying that the Gazprom-Rosneft merger will take place as scheduled, but without Yuganskneftegaz.

**Russian Economic Indicators**  
 (Percent change from previous period, s.a., except as noted)

Indicator	2003	2004	2004					
			Q3	Q4	Oct.	Nov.	Dec.	
Real GDP <sup>1</sup>		7.5	n.a.	-.5	n.a.	...	...	...
Industrial production		6.7	6.0	.0	-.4	-.4	2.6	.0
Unemployment rate <sup>2</sup>		8.5	n.a.	7.7	n.a.	7.5	7.3	n.a.
Consumer prices <sup>3</sup>		12.0	11.6	11.0	11.6	11.5	11.6	11.6
Trade balance <sup>4</sup>		59.9	n.a.	90.7	n.a.	101.4	102.9	n.a.
Current account <sup>4</sup>		35.6	n.a.	64.2	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate.

n.a. Not available. ... Not applicable.

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January 28, 2005

## CURRENT ECONOMIC AND FINANCIAL CONDITIONS

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### **Supplemental Notes**

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

**Commercial Bank Credit**  
(Percent change, annual rate, except as noted; seasonally adjusted)

Type of credit	2003	2004	Q3 2004	Q4 2004	Dec. 2004	Jan. <sup>e</sup> 2005	Level, Jan. 2005 <sup>e</sup> (\$ billions)
<b>Total</b>							
<b>1. Adjusted<sup>1</sup></b>	<b>5.9</b>	<b>8.9</b>	<b>4.9</b>	<b>6.4</b>	<b>3.8</b>	<b>13.5</b>	<b>6,587</b>
2. Reported	5.6	8.3	5.4	6.2	4.1	10.7	6,740
<i>Securities</i>							
3. Adjusted <sup>1</sup>	8.6	6.7	-7.7	2.2	2.5	30.9	1,784
4. Reported	7.3	5.1	-4.8	2.1	3.7	19.6	1,936
5. Treasury and agency	8.8	5.0	-4.0	-10.7	3.3	31.6	1,180
6. Other <sup>2</sup>	5.0	5.2	-6.2	23.4	4.5	1.3	756
<i>Loans<sup>3</sup></i>							
7. Total	4.9	9.6	9.8	7.9	4.2	7.1	4,803
8. Business	-9.4	.7	5.8	4.9	11.0	22.4	906
9. Real estate	11.1	13.6	8.0	12.8	10.6	11.6	2,562
10. Home equity	30.8	43.3	37.1	37.3	15.9	18.4	404
11. Other	8.8	9.5	3.4	8.6	9.7	10.3	2,158
12. Consumer	5.4	8.6	19.6	-1.6	14.6	10.9	680
13. Adjusted <sup>4</sup>	5.8	6.0	12.4	3.0	11.6	11.0	1,061
14. Other <sup>5</sup>	6.7	9.0	11.7	3.6	-37.6	-33.3	656

Note. Data are adjusted to remove estimated effects of consolidation related to FIN 46 and for breaks caused by reclassifications. Monthly levels are pro rata averages of weekly (Wednesday) levels. Quarterly levels (not shown) are simple averages of monthly levels. Annual levels (not shown) are levels for the fourth quarter. Growth rates are percentage changes in consecutive levels, annualized but not compounded.

- 1. Adjusted to remove effects of mark-to-market accounting rules (FIN 39 and FAS 115).
- 2. Includes private mortgage-backed securities, securities of corporations, state and local governments, foreign governments, and any trading account assets that are not Treasury or agency securities, including revaluation gains on derivative contracts.
- 3. Excludes interbank loans.
- 4. Includes an estimate of outstanding loans securitized by commercial banks.
- 5. Includes security loans and loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.

e Estimated.