<u>Prefatory Note</u>

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Confidential (FR) Class II FOMC

Part 1

March 11, 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

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Domestic Developments

The data we have received since the January Greenbook have been somewhat weaker, on net, than we had expected. According to the most recent estimate from the BEA, real GDP increased about 3/4 percentage point less in the fourth quarter than we had projected in January. The labor market reports for January and February fell below our expectations, and by enough to cause us to scale back our projection for employment gains in the next several months. And although household spending is on track to post another solid increase this quarter and equipment outlays have strengthened, the latest indicators of construction activity have been on the weak side of our projection. All told, we have cut our forecast for the growth of real GDP in the current quarter 1/2 percentage point, to 4-1/2 percent at an annual rate, and trimmed our estimate for the year as a whole 1/4 percentage point, to 5.0 percent.

That said, we have interpreted the near-term developments as refinements to a basic picture that has not changed greatly since the January Greenbook. The combination of accommodative monetary policy, expansionary fiscal policy, and continued rapid growth in structural productivity is expected to sustain above-potential growth over the forecast period and to bring the unemployment rate down gradually to 5-1/4 percent by the end of 2005. Although higher energy prices are expected to boost overall consumer prices this year, we have not changed in any material way our projection of core inflation: The core PCE price index is forecast to rise about 1 percent in 2004 and 2005—about the same as in 2003.

Key Background Factors

Our monetary policy assumptions are unchanged from the January Greenbook: The federal funds rate is assumed to remain at 1 percent through 2004 and then to rise gradually to 2 percent by the end of 2005. Futures quotes have moved down since the last meeting. Market participants now anticipate that the funds rate will not begin to move up until late this year; they also now expect less tightening over the forecast period. In line with these revised expectations, the 10-year Treasury rate dropped about 30 basis points on net during the intermeeting period, and we have assumed that it will continue on a lower path for the remainder of 2004 and in 2005. But we expect the contour of rates to be much the same as before, with a slow updrift over the forecast period prompted by the anticipated monetary tightening.

We have marked down the level of equity prices about 2 percent in response to the stock market decline since the time of the January Greenbook. We continue to assume that, beyond the current quarter, share prices will rise at an average annual rate of 6-1/4 percent, maintaining risk-adjusted parity with the projected yield on long-term Treasury securities.

We have not changed our assumptions about fiscal policy. The Administration's budget proposals for fiscal 2004 and 2005, and their reception on Capitol Hill, have not indicated a need to depart from our January assumptions. In particular, for fiscal 2004, our previous assumption about defense spending is in line with the most recent projections of defense expenditures made by both the Administration and the CBO. For fiscal 2005, our projection of defense spending continues to assume that a supplemental appropriation will be enacted to keep real outlays on Iraq constant at 2004 levels.

We expect the federal unified deficit to be $473 billion in fiscal 2004 but to fall to $377 billion in fiscal 2005. Our assumptions imply that federal fiscal policy will provide considerable stimulus to aggregate demand in 2004 but will then swing to a slightly restrictive stance next year, reflecting the expiration of the partial-expensing provision and a projected slowing in the growth of defense expenditures.

Since the January Greenbook, the foreign exchange value of the dollar has increased about 1 percent. Nevertheless, we continue to assume that the real dollar will depreciate over the rest of 2004 and over 2005, at an annual rate of about 1-1/4 percent. Foreign real GDP growth now appears to have been about 1/2 percentage point (annual rate) stronger in the latter half of 2003 than suggested by earlier data. However, we are not inclined to carry this surprise forward, partly because some of the revision reflects temporary factors such as a large inventory buildup in Canada and an export surge in Japan. We project that, on a trade-weighted basis, foreign GDP will increase about 3-3/4 percent this year and 3-1/2 percent next year.

Spot prices for crude oil have risen about $2 per barrel since the time of the January Greenbook. This jump was largely in response to OPEC's announcement on February 10 that it would lower its production target by 1 million barrels per day, effective April 1. Other factors sustaining the current high level of oil prices include low oil inventories in the United States, strong world economic activity, and concerns about oil supplies from several regions. Nevertheless, futures quotes reflect the expectation that an expansion of oil exports from Iraq and non-OPEC countries will gradually put downward pressure on crude prices. In line with the futures quotes, our forecast assumes that the spot price of West Texas intermediate crude declines from its current level of more than $36 per barrel to less than $30 per barrel by the end of 2005. Compared with the January Greenbook, the oil price trajectory is about $3 per barrel higher in 2004 and $2.50 per barrel higher in 2005.

Recent Developments and the Near-Term Outlook

We are forecasting real GDP to grow at annual rates of 4-1/2 percent in the current quarter and 5 percent in the second quarter. Despite the sluggish performance of the labor market, consumer spending appears to be trending upward. Equipment spending also seems to be on a strong trajectory, stimulated by the partial-expensing provision and the need to replace aging machines. Federal outlays are expected to pick up after the lull in the second half of last year.

Labor demand appears to be increasing, but at a pace well below our forecast in the January Greenbook. The average monthly increase in private payrolls was only 50,000 in the first two months of this year, and aggregate hours in February stood just 0.2 percent above the fourth-quarter average. We still expect payroll gains to step up over the first half of this year but now to a monthly rate of only 200,000 by June, compared with a monthly rate of almost 350,000 in the January Greenbook.

Industrial production is forecast to increase at an annual rate of about 7 percent in the first quarter, boosted by a large weather-related increase in the output of utilities. Manufacturing production is expected to increase at a pace of 6-1/4 percent in the first quarter and 6-3/4 percent in the second quarter. Motor vehicle assemblies are increasing briskly in the current quarter, but days' supply is rising, so we do not expect motor vehicle production to contribute significantly to the growth of manufacturing output in the second quarter. Aside from motor vehicles, the trend in new orders and the upbeat tone of recent purchasing managers' reports point to a gradual ramping up of production over the first half of the year.

Real PCE is projected to rise at annual rates of 3-1/2 percent in the current quarter and 4-3/4 percent in the second quarter. Retail sales excluding motor vehicles rose solidly on average in January and February, and spending on services was strong at the beginning of the year. In contrast, the demand for new motor vehicles has been more sluggish of late. Sales of light vehicles fell to an average pace of 16.2 million units in January and February, as incentives were reduced and unfavorable weather disrupted sales in some regions of the country. With dealer inventories on the rise, we anticipate a sweetening of incentives in the months ahead that, together with strong growth in real disposable income, should boost light vehicle sales back to an annual rate of 17 million units in the second quarter.

Activity in housing markets, though still strong, has come in somewhat below our expectations at the time of the January Greenbook. Although down from the sizzling pace of the fourth quarter, single-family housing starts were still at a

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

Measure	2004:Q1 Jan. GB	2004:Q1 Mar. GB	2004:Q2 Jan. GB	2004:Q2 Mar. GB
Real GDP	**5.0**	**4.4**	**5.4**	**4.9**
Private domestic final purchases	4.8	4.2	5.7	6.1
Personal consumption expenditures	3.6	3.4	4.6	4.8
Residential investment	11.3	4.1	2.2	6.9
Business fixed investment	10.0	10.1	15.0	14.7
Government outlays for consumption and investment	4.0	2.9	3.1	3.1
	Contribution to growth (percentage points)			
Inventory investment	.5	.7	.4	-.5
Net exports	-.4	-.5	-.4	-.4

robust annual rate of 1.54 million units in January and are projected to remain at about that pace through the first half of this year. Multifamily starts also slipped a bit to a pace of 370,000 units in January and are forecast to slow to a pace of 340,000 units in coming months. Moreover, a drop in home sales has led to a fall in real estate commissions, which is holding down overall outlays for residential investment. Based on these factors, we now expect real residential investment to increase at an annual rate of 5-1/2 percent in the first half of this year—a substantial increase but well below the gain of 15 percent in the second half of last year.

The incoming information on business fixed investment has been mixed. The latest data on orders and shipments for nondefense capital goods showed widespread strength. Spending on high-tech capital is continuing to recover, and the demand for other capital equipment (excluding transportation) appears to be rising at a double-digit pace in real terms. Business purchases of transportation equipment are expected to increase only slowly this quarter but to pick up in the second quarter. In contrast, data on construction put-in-place through January indicate continued weakness in outlays for nonresidential buildings, while oil and gas drilling seems to be responding positively to high current and expected prices for crude oil and natural gas.

Real nonfarm inventory investment is forecast to contribute about 3/4 percentage point to the increase in real GDP growth in the current quarter but to restrain growth by 1/2 percentage point in the second quarter. This swing is driven by motor vehicle inventories. Automakers have not cut their assemblies in response to unexpectedly weak sales, and dealer stocks have risen; we expect the resulting extra inventories to be worked off in the second quarter. Other businesses are expected to build stocks at a modest but increasing rate.

Regarding the federal sector, we expect the growth of both defense and nondefense real expenditures to ratchet up sharply in the first half of 2004. A step-up in outlays related to Iraq boosts the growth of real defense spending to an average annual rate of 8 percent, double its pace of last quarter. Real nondefense spending is projected to rise at an average rate of 5-1/4 percent over the first and second quarters, following a decline of 3-1/4 percent last quarter.

Both consumption and investment expenditures by state and local governments were softer than anticipated last quarter, and incoming data suggest further declines in construction activity. Although state governments have begun to report some amelioration of their budgetary distress, the growth in spending seems unlikely to bounce back quickly because governments appear intent on rebuilding rainy-day funds without appreciably raising tax rates.

Net exports are expected to exert an arithmetic drag of about 1/2 percentage point on GDP growth, on average, in the first half of this year. Consistent with the most recent report on international trade, growth in real exports is expected to slow substantially from the 21 percent annual pace posted in the fourth quarter. Growth in real imports also is expected to slow in the first quarter but not enough to keep the trade deficit from widening further.

The CPI excluding food and energy increased 0.2 percent in January, after posting smaller increases in November and December. Nevertheless, as in the January Greenbook, we expect core CPI to run at an annual rate of 1-1/4 percent over the first half of the year, roughly in line with the pace of inflation over 2003. Core PCE prices rose 0.1 percent in January, in line with the average increase posted in the preceding two months, and we are projecting that core PCE prices will also increase at an annual rate of about 1-1/4 percent in the first half of this year. Overall measures of consumer price inflation are projected to rise at a somewhat faster pace, reflecting the pass-through of higher crude oil prices to consumer energy prices.

The Longer-Term Outlook for the Economy

Beyond the first half of 2004, the basic contours of the forecast are little changed from the January Greenbook. Real GDP is projected to increase at an annual rate of 5-1/4 percent over the second half of this year, a pace well above potential. Growth should be supported by accommodative monetary policy,

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

Measure	2004 H1	2004 H2	2005
Real GDP	**4.7**	**5.3**	**4.0**
Previous	5.2	5.4	4.0
Final sales	4.5	5.0	3.9
Previous	4.7	4.9	3.9
PCE	4.1	4.3	4.0
Previous	4.1	4.4	4.0
Residential investment	5.5	-.2	-.4
Previous	6.7	-2.5	-.6
BFI	12.4	16.7	8.8
Previous	12.5	16.4	9.0
Government purchases	3.0	1.7	2.1
Previous	3.5	1.6	1.9
Exports	8.2	13.2	10.8
Previous	9.8	13.3	11.1
Imports	8.8	9.3	9.0
Previous	9.5	9.2	8.8
	Contribution to growth (percentage points)		
Inventory change	.1	.3	.1
Previous	.4	.5	.1
Net exports	-.5	-.1	-.2
Previous	-.4	.0	-.2

expansionary fiscal policy, and strong gains in structural productivity. We anticipate that this pace of growth will encourage businesses to lay aside any lingering doubts about the size and sustainability of the recovery. As a result, we project inventory investment and employment growth to pick up. We expect real GDP growth to slow to 4 percent in 2005, owing in large part to a payback in business fixed investment from the expiration of the partial-expensing allowance. The rise in the federal funds rate and the waning of the stimulus from the 2003 personal tax cuts should also cause growth to moderate in 2005.

Household spending. We expect that strong growth in real disposable income will support real consumer spending increases of about 4-1/4 percent this year and 4 percent in 2005. The sharp rises in equity prices and house prices over the past half year should exert a sizable positive influence on spending growth this year, but wealth should be a neutral influence in 2005. We expect households to use some of their income gains over the next two years to boost the saving rate.

The outlook for homebuilding remains favorable: Although the current forecast for employment growth is not as bright as that in the January Greenbook, mortgage rates are lower than we had assumed in the previous projection. We project single-family starts of 1.55 million units this year and a small fallback over 2005 to 1.52 million units, as income growth slows and as mortgage rates creep up a bit in response to the monetary tightening. Multifamily starts are forecast to level off at an annual rate of 340,000 units for the remainder of this year and for 2005.

Business investment. We have been surprised on the upside by recent gains in equipment and software investment, and we have interpreted that news as evidence that—at least with respect to capital spending—business caution is at last lifting. We expect a further boost to equipment investment as the year progresses, with firms accelerating their expenditures to take advantage of the more generous depreciation allowances that expire at year-end. Cutting through the volatility in equipment spending induced by the partial-expensing provision, we expect equipment investment over the next two years to respond both to the pickup in business output and to the very favorable profits picture.

After edging down about 1-1/4 percent last year, investment in nonresidential structures is projected to rise only slightly this year. Vacancy rates for office buildings remain elevated, and the vacancy rate for industrial space is only a touch below its record high. We expect that these vacancy rates will have to fall somewhat before we see any significant pickup in the pace of construction. An exception to the sluggish forecast for most components of construction is drilling and mining, which should be supported by the continued high levels of energy prices this year. With energy prices moderating next year, we anticipate some pullback in drilling activity in 2005.

Inventory stockbuilding has been negligible even as the recovery has gained speed. We believe that this situation has primarily reflected business caution about the firmness of final demand rather than any steepening of the downward trend in firms' desired inventory-sales ratios. As the recovery proceeds, inventory investment should gradually return to a pace more consistent with ongoing sales growth. We project it to contribute 1/4 percentage point to the rise of real GDP this year but to be an essentially neutral factor in growth next year.

Government spending. Even allowing for a jump in the first half of this year in defense outlays related to Iraq, the rate of increase in real federal expenditures for consumption and investment is anticipated to slow from the 6 percent pace observed over 2003 to 4-1/2 percent this year and to 1-3/4 percent in 2005. This projected moderation in spending growth is due to the expectation that, by midyear 2004, the growth rate of real defense spending will settle down to an average annual rate of 1-1/2 percent and the growth rate of real nondefense spending—which has been boosted over the past two years by extraordinary increases for homeland security—will stabilize at an average rate of 2-1/2 percent.

Despite the improved outlook for many state governments, we continue to anticipate increases in real state and local spending this year of only about 1 percent.[1] Because tax receipts should increase as the economic expansion firms, we expect real consumption and investment expenditures of state and local governments to rise about 2-1/4 percent in 2005, only a little below the average 2-1/2 percent annual rise over the past decade.

Net exports. Both exports and imports are projected to step up sharply from their average pace in 2003. The pickup in export growth is attributable to the past and projected dollar depreciation as well as to the expectation that foreign economic activity will continue the rebound that began in the second half of 2003. Although the dollar depreciation should encourage U.S. businesses and households to tilt their demand toward domestically produced goods and services, this effect is overwhelmed by the acceleration in U.S. economic activity. [*The International Developments section provides more detail on the outlook for the external sector.*]

Aggregate Supply, the Labor Market, and Inflation

We have not revised the supply-side assumptions in this forecast in any significant way.[2] After increasing 3-3/4 percent last year, structural productivity is projected to grow 3-1/4 percent in 2004 and 3 percent next year; potential

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1. The fiscal condition of local governments is harder to discern. Although property values have increased sharply of late and about 1/3 of the revenues of local governments are derived from this source, state governments have apparently been cutting aid to local jurisdictions.

2. The few small changes from the January Greenbook reflect the fine-tuning of our estimates after receipt of data on labor productivity that fully incorporated the comprehensive NIPA revision; in the January Greenbook, our projections were based on staff estimates of output per hour.

Decomposition of Structural Labor Productivity
(Percent change, Q4 to Q4, except as noted)

Measure	1974-95	1996-2001	2002	2003	2004	2005
Structural labor productivity	1.5	2.7	3.3	3.8	3.3	3.1
Previous	1.5	2.8	3.3	3.7	3.3	3.1
Contributions[1]						
Capital deepening	.7	1.4	.6	.7	1.0	1.2
Previous	.6	1.3	.6	.6	1.0	1.1
Multifactor productivity	.5	1.1	2.4	2.9	2.1	1.7
Previous	.6	1.2	2.4	2.9	2.1	1.7
Labor composition	.3	.3	.3	.3	.3	.3
MEMO						
Potential GDP	3.0	3.4	3.6	4.1	3.7	3.7
Previous	2.9	3.4	3.6	4.0	3.7	3.7

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.

output is forecast to increase at an annual rate of 3-3/4 percent over the projection period. However, with the downward revision to actual GDP growth in this forecast, the GDP gap is a little wider throughout the projection period than it was in the previous forecast; in the current Greenbook, it falls from 2-1/4 percent at the end of 2003 to 3/4 percent by the fourth quarter of 2005; in the January Greenbook, the gap was essentially eliminated by the end of the projection period.

Productivity and the labor market. Even taking account of the impressive gains in structural productivity, the pace of payroll growth in the nonfarm business sector still seems remarkably low. As noted above, we attribute this lack of hiring to a lingering sense of business caution, but we continue to believe that the maturing of the recovery will cause this hesitancy to lift. As it lifts, we expect to see a step-up in hours and employment growth over this year and next. We expect average monthly increases in private payrolls to climb to around 300,000 by year-end; growth in private payrolls then moderates to around 260,000 per month in 2005 as the pace of economic growth slows. As this adjustment occurs, we project productivity growth to slow from 5-1/4 percent in 2003 to 3 percent in 2004 and to 1-1/2 percent in 2005.

The Outlook for the Labor Market
(Percent change, Q4 to Q4, except as noted)

Measure	2002	2003	2004	2005
Output per hour, nonfarm business	4.3	5.3	3.0	1.6
Previous	4.1	5.5	2.6	1.7
Nonfarm private payroll employment	-.9	-.2	2.0	2.8
Previous	-.7	-.1	2.9	2.8
Household survey employment	.3	1.2	1.9	1.8
Previous	.3	1.2	2.5	1.9
Labor force participation rate[1]	66.5	66.1	66.5	66.7
Previous	66.5	66.1	66.5	66.8
Civilian unemployment rate[1]	5.9	5.9	5.5	5.2
Previous	5.9	5.9	5.3	5.0
MEMO				
GDP gap[2]	2.4	2.2	1.0	.7
Previous	2.4	1.9	.4	.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.

The downward revision to GDP growth has led us to nudge up our projection of the unemployment rate in this forecast. We now expect only a modest decline in the unemployment rate from its current level of 5.6 percent, to 5.5 percent in the last quarter of this year and to 5.2 percent in the last quarter of 2005.

Prices and wages. The outlook for core consumer price inflation is essentially the same as in the January Greenbook. Although the pass-through of higher energy and import prices is expected to exert somewhat more upward pressure on core prices in the current projection, this is offset by a slightly lower rate of resource utilization. Thus, core PCE inflation is projected to remain at an annual rate of about 1 percent over the forecast period. The increase in overall PCE prices is the same as that in core inflation this year, but it falls below the core rate in 2005 because of the decline in energy prices.

For hourly compensation, we project that the employment cost index will increase 3.6 percent this year and 3.7 percent next year, a touch below our previous projection, reflecting both lower incoming wage data and the lower level of resource utilization compared with the last forecast.

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

Measure	2002	2003	2004	2005
PCE chain-weighted price index	1.8	1.4	1.1	.9
Previous	1.8	1.4	1.0	1.0
Food and beverages	1.4	2.6	1.6	1.4
Previous	1.4	2.7	1.6	1.4
Energy	7.9	7.8	.7	-2.8
Previous	7.9	8.5	-1.7	-.4
Excluding food and energy	1.6	.9	1.1	1.0
Previous	1.6	.8	1.0	1.0
Consumer price index	2.2	1.9	1.4	1.1
Previous	2.2	1.9	1.2	1.2
Excluding food and energy	2.0	1.2	1.4	1.4
Previous	2.1	1.2	1.4	1.4
GDP chain-weighted price index	1.4	1.6	1.0	1.1
Previous	1.4	1.6	.9	1.1
ECI for compensation of private industry workers[1]	3.2	4.0	3.6	3.7
Previous	3.2	4.1	3.7	3.8
NFB compensation per hour	1.8	3.6	3.3	3.6
Previous	2.0	3.1	3.4	3.7
Prices of core non-oil merchandise imports	.5	1.8	4.2	.5
Previous	.5	1.8	3.3	.7

1. December to December.

Financial Flows and Conditions

Domestic nonfinancial debt has continued to expand robustly, owing largely to heavy borrowing by households and the federal government. The growth of debt is anticipated to average 8-1/4 percent this year—about the same pace as in 2003—before tapering down to 7 percent in 2005.

After having risen 12-1/2 percent in 2003, home mortgage debt is expected to rise 10-1/2 percent this year and 8-1/2 percent in 2005. This moderation is more gradual than we had projected in January because of the higher level of home prices and the lower path for mortgage rates in this forecast. Only part of this additional borrowing is expected to be offset by slower growth in consumer credit, leaving total household debt growth a little stronger than it was in the last

Greenbook. All told, we expect household debt growth to decline from 10-1/4 percent in 2003 to about 9 percent this year and 7-3/4 percent in 2005.

Corporate borrowing has picked up from the very sluggish pace in the second half of 2003. This rebound can be traced to a rise in C&I loans and commercial paper after more than two years of runoffs; we expect moderate increases in short-term borrowing over the remainder of this year and next year, reflecting in part our forecast of generally rising inventory accumulation. Net bond issuance in the current quarter has remained close to the tepid pace observed in the second half of 2003, and with companies still flush with liquid assets, we do not anticipate much increase in issuance until the second half of this year. On the whole, we expect nonfinancial corporate debt, after having risen 3 percent in 2003, to grow 4-1/2 percent this year and 6-1/4 percent in 2005.

Federal debt is estimated to have risen almost 11 percent last year and is projected to expand another 12-1/4 percent in 2004 as a result of the anticipated rise in the budget deficit. Federal debt growth drops back to about 8 percent in 2005, as the partial-expensing provision lapses and personal tax payments increase.

State and local government debt grew about 8-1/4 percent in 2003 but is projected to rise only about 5-1/2 percent this year and 4-1/2 percent next year with the expected improvement in budget positions and a decline in advance refunding activity. The recent vote in California to approve the issuance of $15 billion in long-term bonds will result in a paydown of short-term notes and is not expected to have any net effect on total borrowing.

After contracting last quarter, M2 advanced at an average annual rate of about 5-1/2 percent during January and February. We expect M2 to continue to increase more slowly than nominal income because of ongoing asset reallocation to capital market instruments this year and the assumed monetary policy tightening in 2005.

Alternative Simulations

In this section we explore several risks to the staff forecast using simulations of the FRB/US model. The first three scenarios explore alternatives to the outlook for aggregate spending, including a pair in which aggregate output is restrained by unexpected declines in asset prices and one in which household spending is even more robust than in the baseline. We then present an alternative in which firms continue to be reluctant to make substantial additions to their payrolls and inventory stocks. The next pair of scenarios examines risks to the inflation outlook. In all these simulations, the federal funds rate is held at baseline. The

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

Measure	2003: H2	2004 H1	2004 H2	2005
Real GDP				
Baseline	**6.1**	**4.7**	**5.3**	**4.0**
Higher bond yields	6.1	4.7	5.1	2.8
Real estate slump	6.1	4.7	5.0	2.6
Buoyant household sector	6.1	4.9	6.2	4.9
Cautious firms	6.1	4.4	5.0	4.0
Rising inflation expectations	6.1	4.7	5.3	4.3
Declining price markup	6.1	4.8	5.4	4.0
Market-based funds rate	6.1	4.7	5.3	3.9
Civilian unemployment rate[1]				
Baseline	**5.9**	**5.6**	**5.5**	**5.2**
Higher bond yields	5.9	5.6	5.5	5.7
Real estate slump	5.9	5.6	5.5	5.9
Buoyant household sector	5.9	5.6	5.3	4.5
Cautious firms	5.9	5.9	6.0	6.0
Rising inflation expectations	5.9	5.6	5.5	5.1
Declining price markup	5.9	5.6	5.5	5.1
Market-based funds rate	5.9	5.6	5.5	5.2
PCE prices excluding food and energy				
Baseline	**.9**	**1.2**	**1.0**	**1.0**
Higher bond yields	.9	1.2	.9	.9
Real estate slump	.9	1.2	.9	.8
Buoyant household sector	.9	1.2	1.0	1.2
Cautious firms	.9	1.2	.9	.8
Rising inflation expectations	.9	1.2	1.2	1.7
Declining price markup	.9	.9	.7	.5
Market-base funds rate	.9	1.2	1.0	1.0

1. Average for the final quarter of the period.

final scenario assumes that the funds rate follows a path consistent with current readings from the futures market.

Higher bond yields. Should the economy evolve as we project, we expect that bond yields will not change significantly over the forecast period. There is a risk, however, that markets will become "spooked" in the second half of this year when they see an economy that is growing rapidly and payrolls that are increasing briskly. Markets might also become more concerned later in the year about the implications of projected large future budget deficits. This scenario assumes that bond yields are bid up 75 basis points relative to baseline over the second half of this year and that this higher level of yields persists through the end of the forecast. As a result of higher real interest rates and the consequent decline in the stock market, real GDP increases only 2-3/4 percent in 2005, the unemployment rate edges back up to 5-3/4 percent, and core inflation dips below 1 percent.

Real estate slump. Residential real estate values have climbed rapidly in recent years, and we expect average house prices to continue to rise, albeit at a more moderate pace over the forecast period. However, the rise in long rates portrayed in the previous scenario might trigger a major decline in real estate values. This scenario augments the rise in bond yields contained in the previous scenario with a drop in house prices of 10 percent between the middle of 2004 and the end of 2005 (rather than the 4 percent increase assumed in the baseline). Such a decline, when expressed relative to the change in core PCE prices, would be somewhat larger and more rapid than seen in past housing market slumps. Over time, the decline in real estate prices would be expected to restrain household spending and raise the saving rate about 1 percentage point. But the adjustment to the lower level of wealth is only partly completed by the end of 2005, so the incremental restraint on real GDP growth in that year is a modest 1/4 percentage point. The effects of the real estate slump on output would worsen after 2005.

Buoyant household sector. In the Greenbook baseline, the contribution of households to real activity is tempered by their inclination to boost personal saving and to trim the rate of investment in housing. An upside risk to our outlook is that households will not rein in their spending. In this scenario, we assume that the personal saving rate holds at 1-3/4 percent, rather than rising to 2-1/2 percent by late 2005, and that single-family housing starts level off at an annual rate of 1.58 million units (their average in the second half of 2003) rather than falling back to a pace of 1.52 million units next year. The buoyant tone of household spending also spills over into house prices, causing them to be 7 percent above baseline at the end of next year; this additional boost to the net worth of households contributes to the flattening of the saving rate. Under these conditions, real GDP increases 5-1/2 percent this year and 5 percent next year, and the unemployment rate drops to 4-1/2 percent by the end of 2005. Core inflation picks up slightly in 2005.

Cautious firms. This scenario assumes that the caution that has pervaded the hiring and stockbuilding decisions of firms will continue well into 2005 rather than abating later this year. Specifically, through various actions that are unsustainable in the longer run, firms are able to economize on new hires and boost actual output per hour 3-1/2 percent this year and 2 percent next year, or about 1/2 percentage point faster per year than in the baseline. Caution also spurs firms to keep stocks leaner than in the staff outlook, with the result that the inventory-sales ratio declines over the next two years about as much as it has dropped over the past two years. Under these conditions, and mainly owing to the slower pace of inventory accumulation, real GDP grows 1/4 percentage point more slowly than in the baseline in 2004 and at the baseline rate in 2005. The increase in output per hour, because it is viewed as temporary, has little effect on aggregate demand: The reduction in household outlays associated with less labor income is largely offset by the stimulus to consumption and investment from higher profits, dividends, and stock market wealth. The effects of faster productivity growth are seen more clearly in the unemployment rate, which rises to 6 percent by the end of 2004 and then remains at that elevated level, and in core inflation, which edges down to 3/4 percent in 2005.

Rising inflation expectations. In our baseline projection, continued slack in labor and product markets helps to hold inflation expectations in check. An upside risk to our inflation projection is that, despite this underutilization of resources, rapid economic growth and a low funds rate might lead to a significant rise in expectations of long-run inflation. In this scenario, such expectations gradually rise 1 percentage point. This revision slowly feeds into actual inflation, which picks up to 1-3/4 percent in 2005. The associated decline of real interest rates provides a modest stimulus to real GDP.

Declining price markup. The markup of price over unit labor costs has risen to elevated levels in both the nonfarm business and the nonfinancial corporate sectors. Our baseline projection assumes that firms will be able to sustain much of this high level of profitability through the end of next year. In this scenario, competitive pressures prove to be more intense than in the baseline and, through a combination of lower prices and higher wages, substantially pare back the size of the markup. In 2005, core PCE inflation slows to 1/2 percent, 1/2 percentage point less than in the baseline. At the same time, growth in compensation per hour rises 1/2 percentage point above that in the baseline. This alternative outlook for prices and labor costs reduces corporate profits and increases labor compensation. But as in the “cautious firms” scenario, such shifts in the composition of income have only limited effects on aggregate activity, so real GDP and the unemployment rate are little affected.

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

Measure	2004	2005
Real GDP (percent change, Q4 to Q4)		
Projection	5.0	4.0
Confidence interval		
Greenbook forecast errors[1]	3.4–6.6	2.3–5.7
FRB/US stochastic simulations	3.8–6.3	2.5–5.8
Civilian unemployment rate (percent, Q4)		
Projection	5.5	5.2
Confidence interval		
Greenbook forecast errors[1]	4.9–6.1	4.2–6.2
FRB/US stochastic simulations	4.9–6.0	4.1–6.1
PCE prices excluding food and energy (percent change, Q4 to Q4)		
Projection	1.1	1.0
Confidence interval		
Greenbook forecast errors[2]	.5–1.7	.0–1.9
FRB/US stochastic simulations	.6–1.6	.2–1.8

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

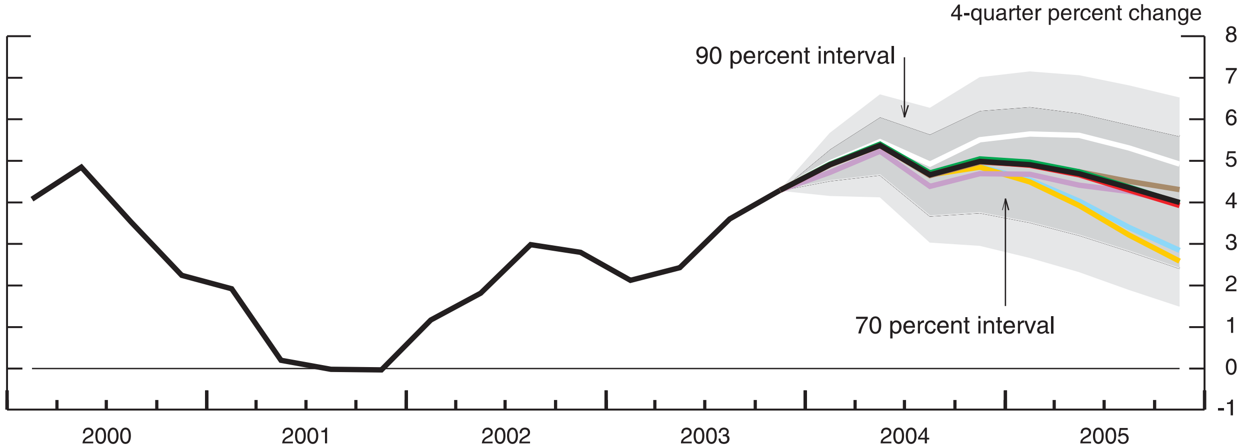
1. 1978–2003.
2. 1981–2003.

Forecast Confidence Intervals and Alternative Scenarios

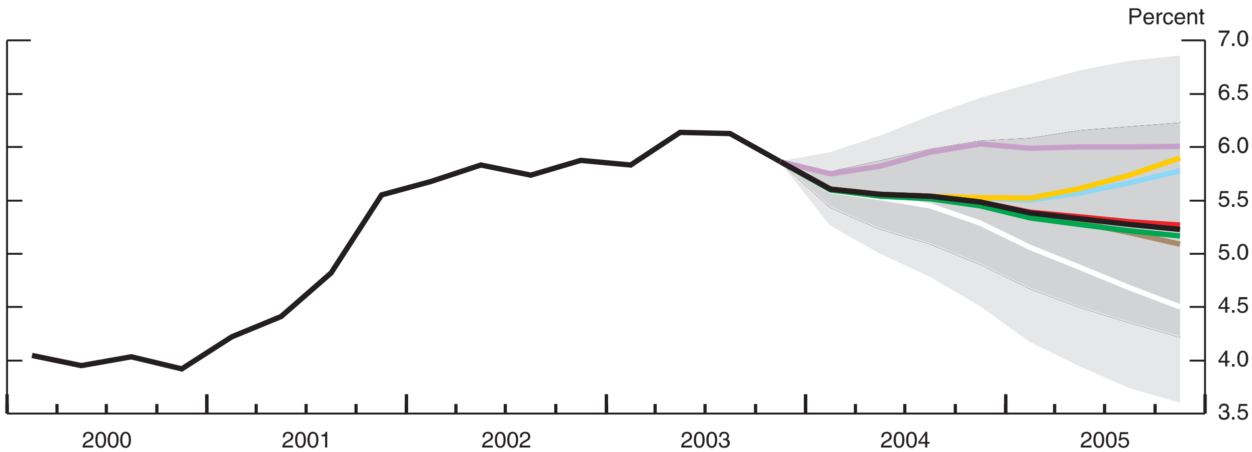
Confidence Intervals Based on FRB/US Stochastic Simulations

- Greenbook baseline
- Higher bond yields
- Real estate slump
- Buoyant household sector
- Cautious firms
- Rising inflation expectations
- Declining price markup
- Market-based funds rate

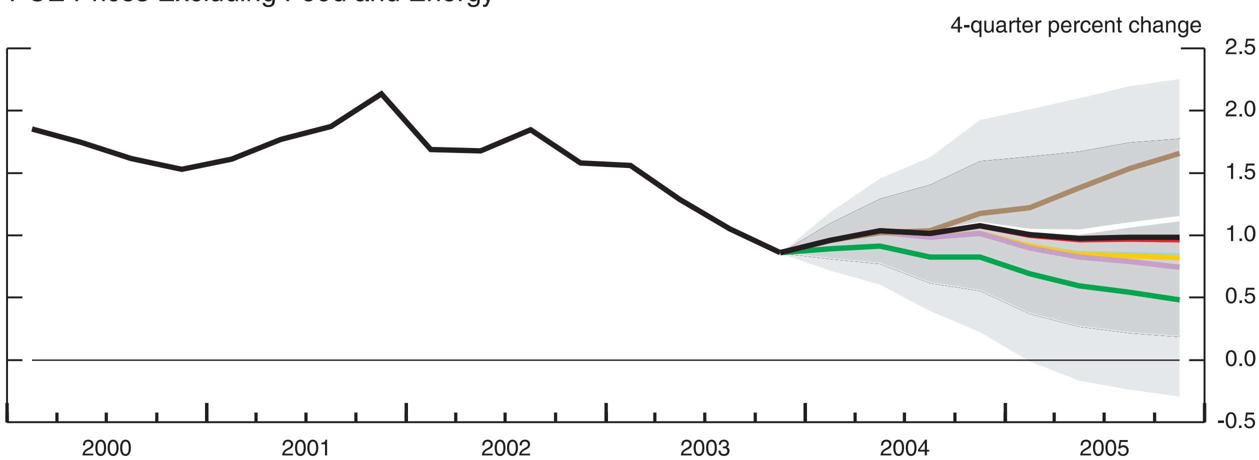
Real GDP



Unemployment Rate



PCE Prices Excluding Food and Energy



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Market-based funds rate. Quotes from futures markets are consistent with a federal funds rate that begins to rise late this year and reaches nearly 2-1/4 percent by late 2005—little different from the assumed path of the funds rate in the baseline. Accordingly, adopting the market-based path for the funds rate has virtually no effect on the outlook for real activity and inflation.

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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[1]		Unemployment rate[2]	
		01/21/04	03/11/04	01/21/04	03/11/04	01/21/04	03/11/04	01/21/04	03/11/04	01/21/04	03/11/04
ANNUAL											
2001		2.9	2.9	0.5	0.5	2.4	2.4	2.8	2.8	4.7	4.7
2002		3.8	3.8	2.2	2.2	1.5	1.5	1.6	1.6	5.8	5.8
2003		4.9	4.8	3.2	3.1	1.7	1.7	2.3	2.3	6.0	6.0
2004		6.6	6.3	5.4	5.0	1.2	1.3	1.4	1.6	5.5	5.5
2005		5.5	5.5	4.5	4.5	1.0	1.0	1.0	0.9	5.1	5.3
QUARTERLY											
2002	Q1	5.4	5.4	4.7	4.7	1.1	1.1	1.4	1.4	5.7	5.7
	Q2	3.9	3.9	1.9	1.9	1.5	1.5	3.4	3.4	5.8	5.8
	Q3	4.4	4.4	3.4	3.4	1.5	1.5	2.2	2.2	5.7	5.7
	Q4	3.1	3.1	1.3	1.3	1.7	1.7	2.0	2.0	5.9	5.9
2003	Q1	4.3	4.3	2.0	2.0	2.3	2.3	3.8	3.8	5.8	5.8
	Q2	4.2	4.2	3.1	3.1	1.1	1.1	0.7	0.7	6.1	6.1
	Q3	10.0	10.0	8.2	8.2	1.6	1.6	2.4	2.4	6.1	6.1
	Q4	6.3	5.3	4.8	4.0	1.4	1.3	0.9	0.7	5.9	5.9
2004	Q1	6.6	6.6	5.0	4.4	1.6	2.1	2.5	3.3	5.8	5.6
	Q2	6.1	5.8	5.4	4.9	0.6	0.9	0.7	1.4	5.6	5.6
	Q3	6.0	5.7	5.4	5.3	0.6	0.4	0.6	0.2	5.4	5.5
	Q4	6.2	6.0	5.4	5.3	0.8	0.7	0.9	0.7	5.3	5.5
2005	Q1	5.5	5.5	4.1	4.1	1.3	1.3	1.1	1.0	5.2	5.4
	Q2	5.1	5.1	4.0	4.0	1.0	1.1	1.2	1.1	5.1	5.3
	Q3	5.1	5.1	4.0	4.0	1.1	1.1	1.2	1.1	5.1	5.3
	Q4	4.9	5.0	3.8	3.9	1.0	1.1	1.3	1.2	5.0	5.2
TWO-QUARTER[3]											
2002	Q2	4.7	4.7	3.3	3.3	1.3	1.3	2.4	2.4	0.2	0.2
	Q4	3.8	3.8	2.3	2.3	1.6	1.6	2.1	2.1	0.1	0.1
2003	Q2	4.2	4.2	2.5	2.5	1.7	1.7	2.2	2.2	0.2	0.2
	Q4	8.1	7.6	6.5	6.1	1.5	1.5	1.6	1.5	-0.2	-0.2
2004	Q2	6.3	6.2	5.2	4.7	1.1	1.5	1.6	2.3	-0.3	-0.3
	Q4	6.1	5.9	5.4	5.3	0.7	0.5	0.8	0.5	-0.3	-0.1
2005	Q2	5.3	5.3	4.1	4.1	1.2	1.2	1.1	1.0	-0.2	-0.2
	Q4	5.0	5.0	3.9	3.9	1.0	1.1	1.3	1.2	-0.1	-0.1
FOUR-QUARTER[4]											
2001	Q4	2.4	2.4	-0.0	-0.0	2.4	2.4	1.8	1.8	1.7	1.7
2002	Q4	4.2	4.2	2.8	2.8	1.4	1.4	2.2	2.2	0.3	0.3
2003	Q4	6.2	5.9	4.5	4.3	1.6	1.6	1.9	1.9	-0.0	-0.0
2004	Q4	6.2	6.0	5.3	5.0	0.9	1.0	1.2	1.4	-0.6	-0.4
2005	Q4	5.1	5.2	4.0	4.0	1.1	1.1	1.2	1.1	-0.2	-0.3

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.

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

								- - - - - Projected - - - -		
Item	Units[1]	1997	1998	1999	2000	2001	2002	2003	2004	2005
Expenditures										
Nominal GDP	Bill. $	8304.3	8747.0	9268.4	9817.0	10100.8	10480.8	10985.3	11680.0	12321.1
Real GDP	Bill. Ch. $	8703.5	9066.9	9470.3	9817.0	9866.6	10083.0	10397.0	10914.7	11404.4
Real GDP	% change	4.3	4.5	4.7	2.2	-0.0	2.8	4.3	5.0	4.0
Gross domestic purchases		5.1	5.5	5.5	3.0	0.1	3.6	4.1	5.0	4.1
Final sales		3.7	4.8	4.2	2.9	1.1	1.8	4.3	4.8	3.9
Priv. dom. final purchases		5.2	6.4	5.3	4.3	0.8	2.3	4.6	5.3	4.3
Personal cons. expenditures		4.3	5.4	4.9	4.1	2.7	2.7	3.9	4.2	4.0
Durables		9.9	14.4	7.3	4.7	9.4	1.8	11.0	5.2	7.0
Nondurables		2.5	4.7	4.9	3.0	1.7	2.8	4.9	5.6	5.0
Services		4.0	3.8	4.4	4.5	1.8	2.9	2.0	3.3	2.9
Business fixed investment		11.4	10.9	7.7	7.8	-10.2	-2.8	7.3	14.5	8.8
Equipment & Software		13.8	13.5	10.8	7.5	-9.4	1.6	10.1	18.4	9.8
Nonres. structures		4.6	4.0	-0.9	8.8	-12.4	-14.9	-1.3	1.5	5.0
Residential structures		3.1	10.3	3.6	-1.8	1.7	7.1	9.5	2.6	-0.4
Exports		8.3	2.6	5.6	6.5	-11.5	3.3	6.4	10.7	10.8
Imports		14.3	11.0	12.1	11.2	-7.4	9.4	4.4	9.1	9.0
Gov't. cons. & investment		1.2	3.3	4.2	0.4	3.6	4.5	2.2	2.3	2.1
Federal		-0.5	0.1	4.2	-2.2	6.3	10.1	6.1	4.5	1.8
Defense		-1.5	-1.2	4.3	-3.5	6.6	10.9	8.4	4.6	1.6
State & local		2.2	5.1	4.2	1.7	2.3	1.6	0.0	1.1	2.2
Change in bus. inventories	Bill. Ch. $	71.2	72.6	68.9	56.5	-36.0	5.7	0.5	30.6	64.9
Nonfarm		68.5	71.2	71.5	57.8	-36.3	9.3	1.7	31.2	65.1
Net exports		-104.6	-203.7	-296.2	-379.5	-398.1	-470.6	-508.8	-538.9	-564.1
Nominal GDP	% change	5.9	5.7	6.3	4.6	2.4	4.2	5.9	6.0	5.2
GDP Gap[2]	%	-0.8	-1.5	-2.3	-2.3	0.6	1.9	2.6	1.5	0.8
Employment and Production										
Nonfarm payroll employment	Millions	122.8	125.9	129.0	131.8	131.8	130.4	129.9	131.1	134.4
Unemployment rate	%	4.9	4.5	4.2	4.0	4.7	5.8	6.0	5.5	5.3
Industrial prod. index	% change	8.1	4.4	4.9	2.3	-5.2	1.3	1.4	5.5	4.0
Capacity util. rate - mfg.	%	82.6	82.0	81.4	81.1	75.4	73.9	73.4	76.1	78.1
Housing starts	Millions	1.47	1.62	1.64	1.57	1.60	1.70	1.85	1.89	1.86
Light motor vehicle sales		15.13	15.52	16.90	17.36	17.12	16.79	16.65	17.06	17.61
North Amer. produced		13.19	13.48	14.41	14.48	14.04	13.50	13.34	13.68	14.12
Other		1.95	2.03	2.49	2.87	3.08	3.30	3.31	3.38	3.50
Income and Saving										
Nominal GNP	Bill. $	8337.3	8768.3	9302.2	9855.9	10135.9	10502.3	11020.9	11743.0	12372.6
Nominal GNP	% change	5.8	5.5	6.5	4.7	2.6	3.8	5.9	6.2	5.0
Nominal personal income		6.4	7.0	5.5	7.1	2.4	2.4	3.9	5.5	5.7
Real disposable income		4.3	5.6	2.8	4.4	1.3	3.5	3.4	4.7	4.2
Personal saving rate	%	3.6	4.3	2.4	2.3	1.7	2.3	2.0	2.0	2.4
Corp. profits, IVA & CCAdj.	% change	9.1	-10.0	9.6	-8.6	8.7	8.3	24.4	9.9	-2.0
Profit share of GNP	%	10.4	9.1	9.2	8.3	7.6	8.6	9.6	10.6	10.1
Excluding FR Banks		10.1	8.9	8.9	8.0	7.3	8.4	9.4	10.4	10.0
Federal surpl./deficit	Bill. $	-30.0	53.0	122.7	172.5	-2.8	-240.0	-417.8	-448.1	-299.7
State & local surpl./def.		46.1	63.0	55.3	35.4	-3.0	-3.2	-2.0	-0.6	8.3
Ex. social ins. funds		38.0	50.3	48.7	47.9	14.0	-6.6	-5.5	-4.1	4.7
Gross natl. saving rate	%	17.5	18.2	18.0	18.0	16.4	14.7	13.3	13.8	14.5
Net natl. saving rate		6.6	7.4	6.9	6.7	4.4	2.7	1.6	2.5	3.2
Prices and Costs										
GDP chn.-wt. price index	% change	1.5	1.1	1.6	2.2	2.4	1.4	1.6	1.0	1.1
Gross Domestic Purchases chn.-wt. price index		1.0	0.7	2.0	2.4	1.6	1.7	1.6	1.2	0.9
PCE chn.-wt. price index		1.3	0.9	2.1	2.3	1.6	1.8	1.4	1.1	0.9
Ex. food and energy		1.4	1.4	1.6	1.5	2.1	1.6	0.9	1.1	1.0
CPI		1.9	1.5	2.6	3.4	1.8	2.2	1.9	1.4	1.1
Ex. food and energy		2.2	2.3	2.0	2.6	2.7	2.0	1.2	1.4	1.4
ECI, hourly compensation[3]		3.4	3.5	3.4	4.4	4.2	3.2	4.0	3.6	3.7
Nonfarm business sector										
Output per hour		2.0	2.8	3.2	2.1	2.9	4.3	5.3	3.0	1.6
Compensation per Hour		4.0	5.7	4.9	6.5	3.8	1.8	3.6	3.3	3.6
Unit labor cost		2.0	2.7	1.6	4.3	0.8	-2.4	-1.6	0.4	2.0

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.

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

Item	Units	2001 Q1	2001 Q2	2001 Q3	2001 Q4	2002 Q1	2002 Q2	2002 Q3	2002 Q4	2003 Q1	2003 Q2
Expenditures											
Nominal GDP	Bill. $	10024.8	10088.2	10096.2	10193.9	10329.3	10428.3	10542.0	10623.7	10735.8	10846.7
Real GDP	Bill. Ch. $	9882.2	9866.3	9834.6	9883.6	9997.9	10045.1	10128.4	10160.8	10210.4	10288.3
Real GDP	% change	-0.2	-0.6	-1.3	2.0	4.7	1.9	3.4	1.3	2.0	3.1
Gross domestic purchases		-0.7	-0.4	-0.8	2.4	5.2	3.1	3.4	2.7	1.1	4.3
Final sales		1.4	0.7	-0.7	3.2	2.6	1.3	1.8	1.7	2.7	3.3
Priv. dom. final purchases		-0.1	-0.0	0.5	2.8	2.9	2.2	1.7	2.2	2.3	3.8
Personal cons. expenditures		0.5	2.3	1.9	6.2	4.1	2.6	2.0	2.2	2.5	3.3
Durables		1.7	9.8	0.7	27.3	1.6	0.5	5.0	0.3	0.5	17.7
Nondurables		0.4	-1.1	2.9	4.7	6.1	0.4	0.2	4.6	5.7	1.2
Services		0.3	2.4	1.6	2.8	3.8	4.1	2.2	1.5	1.5	1.7
Business fixed investment		-4.5	-13.6	-8.4	-14.0	-7.0	-3.0	-1.1	-0.1	-0.6	7.0
Equipment & Software		-4.0	-16.4	-12.2	-4.1	-0.2	1.2	3.7	1.7	0.5	8.0
Nonres. structures		-5.9	-5.6	2.2	-35.3	-23.9	-14.5	-14.6	-5.6	-4.0	3.9
Residential structures		2.6	3.7	3.1	-2.5	8.7	8.9	4.2	6.8	4.5	4.5
Exports		-4.5	-13.4	-17.7	-9.8	4.4	8.7	4.3	-3.7	-2.0	-1.1
Imports		-6.2	-8.6	-10.8	-3.8	8.4	17.1	4.1	8.2	-6.8	9.1
Gov't. cons. & investment		5.8	5.8	-4.1	7.4	4.6	4.0	2.5	7.1	-0.4	7.4
Federal		8.9	6.7	0.0	9.9	8.4	10.5	3.9	18.2	-0.2	23.5
Defense		7.7	2.6	2.4	14.2	8.2	9.5	4.5	22.1	-5.6	41.9
State & local		4.3	5.3	-6.1	6.1	2.7	0.7	1.7	1.5	-0.5	-0.8
Change in bus. inventories	Bill. Ch. $	4.3	-28.8	-44.0	-75.5	-23.5	-8.0	32.8	21.5	1.6	-4.5
Nonfarm		-2.1	-26.9	-45.8	-70.3	-28.6	4.2	36.0	25.4	0.3	-2.4
Net exports		-385.9	-391.7	-401.3	-413.4	-431.2	-467.6	-471.9	-511.5	-490.0	-526.0
Nominal GDP	% change	2.9	2.6	0.3	3.9	5.4	3.9	4.4	3.1	4.3	4.2
GDP Gap[1]	%	-0.8	0.2	1.3	1.7	1.4	1.8	1.9	2.4	2.9	3.1
Employment and Production											
Nonfarm payroll employment	Millions	132.5	132.2	131.8	130.9	130.4	130.4	130.3	130.2	130.0	129.9
Unemployment rate	%	4.2	4.4	4.8	5.6	5.7	5.8	5.7	5.9	5.8	6.1
Industrial prod. index	% change	-6.3	-5.0	-5.2	-4.5	1.9	4.2	1.2	-1.9	0.9	-4.0
Capacity util. rate - mfg.	%	77.5	76.0	74.6	73.5	73.7	74.1	74.2	73.5	73.5	72.7
Housing starts	Millions	1.61	1.63	1.60	1.57	1.72	1.68	1.70	1.74	1.74	1.74
Light motor vehicle sales		17.07	16.70	16.18	18.54	16.47	16.52	17.56	16.62	15.96	16.37
North Amer. produced		14.17	13.65	13.20	15.15	13.17	13.24	14.22	13.36	12.60	13.06
Other		2.90	3.06	2.98	3.39	3.30	3.28	3.34	3.27	3.36	3.31
Income and Saving											
Nominal GNP	Bill. $	10052.1	10115.5	10107.8	10268.3	10351.3	10435.9	10560.5	10661.6	10763.7	10880.0
Nominal GNP	% change	1.8	2.5	-0.3	6.5	3.3	3.3	4.9	3.9	3.9	4.4
Nominal personal income		4.6	1.2	1.7	2.0	1.5	5.0	1.4	1.7	3.0	4.4
Real disposable income		-0.3	-1.4	12.2	-4.4	10.6	4.1	-0.9	0.6	2.4	4.9
Personal saving rate	%	1.9	1.1	2.8	1.0	2.5	2.8	2.1	1.8	1.9	2.3
Corp. profits, IVA & CCAdj.	% change	-18.0	-3.8	-17.4	114.5	7.9	10.3	-0.9	16.5	-3.3	48.1
Profit share of GNP	%	7.5	7.4	7.1	8.4	8.5	8.6	8.5	8.8	8.6	9.4
Excluding FR Banks		7.2	7.1	6.8	8.2	8.3	8.4	8.3	8.6	8.4	9.2
Federal surpl./deficit	Bill. $	156.1	128.9	-80.1	-2.8	-188.8	-232.0	-242.9	-296.3	-320.4	-424.7
State & local surpl./def.		36.1	24.6	11.6	-3.0	-7.4	-11.9	6.8	-0.4	-40.6	-14.7
Ex. social ins. funds		33.1	21.3	8.1	-6.6	-10.8	-15.3	3.4	-3.8	-44.0	-18.1
Gross natl. saving rate	%	17.1	16.3	15.9	16.1	15.3	15.1	14.4	13.8	12.9	13.2
Net natl. saving rate		5.6	4.4	3.3	4.4	3.5	3.2	2.5	1.8	0.9	1.4
Prices and Costs											
GDP chn.-wt. price index	% change	3.2	3.2	1.6	1.6	1.1	1.5	1.5	1.7	2.3	1.1
Gross Domestic Purchases chn.-wt. price index		2.6	2.3	1.0	0.5	1.0	2.4	1.6	1.7	3.4	0.4
PCE chn.-wt. price index		3.2	2.5	0.5	0.4	0.7	2.9	2.0	1.7	2.8	0.5
Ex. food and energy		2.8	1.9	1.3	2.5	1.0	1.9	2.0	1.5	0.9	0.8
CPI		3.7	3.2	1.1	-0.7	1.4	3.4	2.2	2.0	3.8	0.7
Ex. food and energy		2.9	2.6	2.8	2.4	2.1	2.3	2.1	1.7	1.3	1.0
ECI, hourly compensation[2]		4.6	3.7	3.9	4.4	3.6	4.4	2.5	3.0	5.5	3.4
Nonfarm business sector											
Output per hour		-0.1	3.1	1.6	7.0	9.8	0.7	4.5	2.3	3.4	6.2
Compensation per hour		5.6	2.4	3.0	4.0	1.2	2.3	1.3	2.2	4.0	4.9
Unit labor cost		5.7	-0.7	1.3	-2.8	-7.8	1.6	-3.1	-0.1	0.6	-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> March 11, 2004
Class II FOMC

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

			- - - Projected - - -								
Item	Units	2003 Q3	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4
EXPENDITURES											
Nominal GDP	Bill. $	11107.0	11251.9	11433.2	11596.6	11758.6	11931.4	12093.0	12244.6	12397.4	12549.6
Real GDP	Bill. Ch. $	10493.1	10596.3	10711.8	10840.3	10982.0	11124.7	11238.2	11348.9	11460.2	11570.3
Real GDP	% change	8.2	4.0	4.4	4.9	5.3	5.3	4.1	4.0	4.0	3.9
Gross domestic purchases		7.0	4.1	4.7	5.1	5.3	5.0	4.2	4.2	4.0	3.7
Final sales		8.3	3.1	3.7	5.4	4.8	5.2	2.9	4.0	4.2	4.4
Priv. dom. final purchases		8.4	3.9	4.2	6.1	5.5	5.5	3.3	4.7	4.7	4.6
Personal cons. expenditures		6.9	2.8	3.4	4.8	4.4	4.2	4.1	4.0	4.0	3.8
Durables		28.0	0.1	-3.2	8.7	8.1	7.5	7.7	7.2	6.7	6.3
Nondurables		7.3	5.3	6.0	6.0	5.4	5.1	5.0	5.0	5.0	4.9
Services		2.8	2.2	3.6	3.4	3.1	3.1	2.9	2.9	2.9	2.7
Business fixed investment		12.8	10.5	10.1	14.7	15.4	18.0	-0.2	11.7	12.0	12.1
Equipment & Software		17.6	15.0	15.5	18.1	18.4	21.7	-1.3	13.7	13.8	13.8
Nonres. structures		-1.8	-3.2	-6.8	3.1	4.9	5.1	4.1	4.5	5.3	6.0
Residential structures		21.9	7.9	4.1	6.9	0.6	-1.1	-0.4	-0.7	-0.4	-0.1
Exports		9.9	20.5	4.6	11.9	12.2	14.3	8.7	11.1	10.8	12.6
Imports		0.8	16.0	6.6	11.1	9.7	8.9	8.0	10.4	8.9	8.6
Gov’t. cons. & investment		1.8	0.3	2.9	3.1	1.6	1.8	1.9	2.0	2.1	2.2
Federal		1.2	1.6	7.7	6.5	2.0	1.9	1.7	1.8	1.6	1.9
Defense		-1.3	4.3	7.8	8.1	1.4	1.3	1.5	1.7	1.3	1.8
State & local		2.1	-0.6	0.2	1.1	1.4	1.7	2.0	2.1	2.3	2.4
Change in bus. inventories	Bill. Ch. $	-9.1	13.8	32.1	19.4	33.9	36.8	71.6	71.6	65.2	51.1
Nonfarm		-5.9	14.9	33.0	21.3	34.1	36.4	72.0	72.0	65.4	50.9
Net exports		-505.2	-514.0	-527.5	-539.5	-545.6	-543.0	-551.7	-563.7	-570.5	-570.6
Nominal GDP	% change	10.0	5.3	6.6	5.8	5.7	6.0	5.5	5.1	5.1	5.0
GDP Gap[1]	%	2.2	2.2	2.0	1.8	1.4	1.0	0.9	0.8	0.7	0.7
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	129.8	130.0	130.2	130.5	131.3	132.3	133.3	134.1	134.9	135.5
Unemployment rate	%	6.1	5.9	5.6	5.6	5.5	5.5	5.4	5.3	5.3	5.2
Industrial prod. index	% change	3.8	5.4	7.0	5.7	4.5	4.7	4.3	3.8	3.8	3.9
Capacity util. rate - mfg.	%	73.2	74.1	75.0	75.9	76.4	77.0	77.5	77.9	78.3	78.7
Housing starts	Millions	1.88	2.03	1.90	1.89	1.89	1.89	1.88	1.87	1.86	1.85
Light motor vehicle sales		17.42	16.84	16.47	17.00	17.37	17.42	17.51	17.57	17.64	17.73
North Amer. produced		14.07	13.64	13.26	13.61	13.91	13.94	14.03	14.09	14.15	14.20
Other		3.36	3.21	3.20	3.39	3.46	3.48	3.48	3.48	3.49	3.53
INCOME AND SAVING											
Nominal GNP	Bill. $	11144.8	11295.1	11490.5	11665.0	11821.5	11995.1	12153.4	12302.0	12445.6	12589.4
Nominal GNP	% change	10.1	5.5	7.1	6.2	5.5	6.0	5.4	5.0	4.8	4.7
Nominal personal income		4.3	3.8	4.6	5.7	5.7	6.1	6.7	5.7	5.4	5.2
Real disposable income		6.3	-0.0	4.7	4.2	5.1	4.9	4.6	4.3	4.1	3.9
Personal saving rate	%	2.3	1.6	1.9	1.8	2.0	2.2	2.3	2.4	2.4	2.5
Corp. profits, IVA & CCAdj.	% change	46.0	14.5	15.8	9.9	6.4	7.7	-4.5	-1.6	-2.5	0.6
Profit share of GNP	%	10.1	10.3	10.5	10.6	10.6	10.7	10.4	10.2	10.0	9.9
Excluding FR Banks		9.9	10.1	10.3	10.4	10.4	10.5	10.2	10.1	9.9	9.8
Federal surpl./deficit	Bill. $	-499.4	-426.5	-473.8	-477.4	-442.6	-398.3	-343.2	-297.8	-279.0	-278.9
State & local surpl./def.		13.1	34.1	-1.9	1.8	-4.2	2.0	5.5	5.9	9.5	12.4
Ex. social ins. funds		9.6	30.6	-5.4	-1.7	-7.7	-1.6	1.9	2.3	5.9	8.8
Gross natl. saving rate	%	13.2	13.7	13.4	13.6	13.9	14.3	14.3	14.5	14.5	14.6
Net natl. saving rate		1.6	2.4	2.1	2.3	2.7	3.1	3.1	3.2	3.2	3.3
PRICES AND COSTS											
GDP chn.-wt. price index	% change	1.6	1.3	2.1	0.9	0.4	0.7	1.3	1.1	1.1	1.1
Gross Domestic Purchases chn.-wt. price index		1.8	1.0	2.8	1.2	0.3	0.6	1.1	0.8	0.9	0.9
PCE chn.-wt. price index		1.8	0.7	2.6	1.3	0.1	0.6	0.8	0.9	0.9	0.9
Ex. food and energy		1.0	0.7	1.3	1.1	1.0	1.0	1.0	1.0	1.0	1.0
CPI		2.4	0.7	3.3	1.4	0.2	0.7	1.0	1.1	1.1	1.2
Ex. food and energy		1.5	0.8	1.3	1.3	1.4	1.4	1.4	1.4	1.4	1.4
ECI, hourly compensation[2]		4.2	2.9	3.4	3.6	3.6	3.7	3.7	3.7	3.7	3.7
Nonfarm business sector											
Output per hour		9.5	2.1	3.5	3.2	3.0	2.3	0.7	1.4	1.9	2.3
Compensation per hour		3.3	2.2	3.1	3.4	3.4	3.5	3.5	3.5	3.6	3.6
Unit labor cost		-5.6	0.1	-0.3	0.2	0.4	1.2	2.8	2.1	1.7	1.3

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	2001 Q3	2001 Q4	2002 Q1	2002 Q2	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 Q3	01Q4/ 00Q4	02Q4/ 01Q4	Projected 03Q4/ 02Q4
Real GDP	-1.3	2.0	4.7	1.9	3.4	1.3	2.0	3.1	8.2	-0.0	2.8	4.3
Gross dom. purchases	-0.9	2.5	5.4	3.2	3.5	2.8	1.2	4.4	7.4	0.1	3.7	4.3
Final sales	-0.8	3.2	2.7	1.3	1.8	1.7	2.7	3.3	8.3	1.1	1.9	4.3
Priv. dom. final purchases	0.4	2.4	2.5	1.9	1.5	1.9	1.9	3.3	7.2	0.7	1.9	3.9
Personal cons. expenditures	1.3	4.2	2.9	1.8	1.4	1.6	1.8	2.3	4.9	1.8	1.9	2.7
Durables	0.1	2.1	0.1	0.0	0.4	0.0	0.0	1.4	2.2	0.8	0.2	0.9
Nondurables	0.6	0.9	1.2	0.1	0.0	0.9	1.1	0.3	1.5	0.3	0.6	1.0
Services	0.6	1.2	1.6	1.7	0.9	0.7	0.6	0.7	1.2	0.7	1.2	0.9
Business fixed investment	-1.0	-1.7	-0.8	-0.3	-0.1	-0.0	-0.1	0.7	1.3	-1.3	-0.3	0.7
Equipment & Software	-1.1	-0.4	-0.0	0.1	0.3	0.1	0.0	0.6	1.3	-0.8	0.1	0.8
Nonres. structures	0.1	-1.4	-0.8	-0.4	-0.4	-0.1	-0.1	0.1	-0.0	-0.4	-0.4	-0.0
Residential structures	0.1	-0.1	0.4	0.4	0.2	0.3	0.2	0.2	1.1	0.1	0.3	0.5
Net exports	-0.4	-0.5	-0.7	-1.3	-0.2	-1.5	0.8	-1.3	0.8	-0.2	-0.9	-0.0
Exports	-2.0	-1.0	0.4	0.8	0.4	-0.4	-0.2	-0.1	0.9	-1.3	0.3	0.6
Imports	1.6	0.5	-1.1	-2.1	-0.6	-1.1	1.0	-1.2	-0.1	1.1	-1.2	-0.6
Government cons. & invest.	-0.7	1.3	0.9	0.7	0.5	1.3	-0.1	1.4	0.3	0.6	0.8	0.4
Federal	0.0	0.6	0.5	0.6	0.3	1.1	-0.0	1.5	0.1	0.4	0.6	0.4
Defense	0.1	0.5	0.3	0.4	0.2	0.9	-0.3	1.6	-0.1	0.2	0.4	0.4
Nondefense	-0.1	0.0	0.2	0.3	0.1	0.3	0.2	-0.1	0.2	0.1	0.2	0.0
State and local	-0.7	0.7	0.3	0.1	0.2	0.2	-0.1	-0.1	0.3	0.3	0.2	0.0
Change in bus. inventories	-0.5	-1.2	2.0	0.6	1.6	-0.4	-0.7	-0.2	-0.1	-1.2	0.9	-0.0
Nonfarm	-0.7	-0.9	1.6	1.3	1.3	-0.4	-0.9	-0.1	-0.1	-1.1	0.9	-0.1
Farm	0.1	-0.3	0.4	-0.6	0.3	-0.0	0.2	-0.1	-0.0	-0.1	0.0	0.1

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

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4	03Q4/ 02Q4	04Q4/ 03Q4	05Q4/ 04Q4
					- - - Projected - - -						- - Projected - -	
Real GDP	4.0	4.4	4.9	5.3	5.3	4.1	4.0	4.0	3.9	4.3	5.0	4.0
Gross dom. purchases	4.3	4.9	5.3	5.6	5.2	4.4	4.4	4.2	3.9	4.3	5.2	4.2
Final sales	3.2	3.7	5.3	4.8	5.2	2.9	4.0	4.2	4.4	4.3	4.8	3.9
Priv. dom. final purchases	3.4	3.6	5.2	4.7	4.8	2.9	4.0	4.1	4.0	3.9	4.6	3.7
Personal cons. expenditures	2.0	2.4	3.4	3.1	2.9	2.9	2.8	2.8	2.6	2.7	2.9	2.8
Durables	0.0	-0.3	0.7	0.7	0.6	0.6	0.6	0.6	0.5	0.9	0.4	0.6
Nondurables	1.0	1.2	1.2	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.1	1.0
Services	0.9	1.5	1.4	1.3	1.3	1.2	1.2	1.2	1.1	0.9	1.4	1.2
Business fixed investment	1.0	1.0	1.5	1.5	1.8	-0.0	1.2	1.3	1.3	0.7	1.5	1.0
Equipment & Software	1.1	1.2	1.4	1.4	1.7	-0.1	1.1	1.2	1.2	0.8	1.4	0.8
Nonres. structures	-0.1	-0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	-0.0	0.0	0.1
Residential structures	0.4	0.2	0.4	0.0	-0.1	-0.0	-0.0	-0.0	-0.0	0.5	0.1	-0.0
Net exports	-0.3	-0.5	-0.4	-0.2	0.1	-0.3	-0.4	-0.2	0.0	-0.0	-0.3	-0.2
Exports	1.8	0.4	1.1	1.2	1.4	0.9	1.1	1.1	1.3	0.6	1.1	1.1
Imports	-2.1	-0.9	-1.6	-1.4	-1.3	-1.2	-1.5	-1.3	-1.3	-0.6	-1.3	-1.3
Government cons. & invest.	0.1	0.5	0.6	0.3	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Federal	0.1	0.5	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.4	0.3	0.1
Defense	0.2	0.3	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.4	0.2	0.1
Nondefense	-0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0	0.1	0.1
State and local	-0.1	0.0	0.1	0.2	0.2	0.2	0.2	0.3	0.3	0.0	0.1	0.3
Change in bus. inventories	0.8	0.7	-0.5	0.5	0.1	1.2	0.0	-0.2	-0.5	-0.0	0.2	0.1
Nonfarm	0.8	0.7	-0.4	0.5	0.1	1.2	0.0	-0.2	-0.5	-0.1	0.2	0.1
Farm	0.1	0.1	-0.0	0.1	0.0	-0.0	0.0	0.0	-0.0	0.1	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)

Item	Fiscal year				2003				2004				2005			
	2002[a]	2003[a]	2004	2005	Q1[a]	Q2[a]	Q3[a]	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Unified budget					Not seasonally adjusted											
Receipts[1]	1853	1782	1820	2019	398	528	429	441	403	517	460	465	439	604	510	509
Outlays[1]	2011	2158	2293	2396	543	544	534	569	581	578	565	604	601	594	597	618
Surplus/deficit[1]	-158	-375	-473	-377	-145	-17	-105	-129	-178	-62	-104	-139	-162	11	-87	-108
On-budget	-317	-536	-627	-556	-169	-91	-113	-178	-200	-134	-115	-181	-201	-69	-105	-156
Off-budget	160	161	154	179	24	75	9	50	22	72	11	41	39	80	18	48
Means of financing																
Borrowing	221	374	485	403	64	106	108	119	149	102	115	131	154	28	89	84
Cash decrease	-17	26	-1	-9	20	-17	-5	2	14	-26	9	6	0	-30	15	15
Other[2]	-46	-24	-11	-17	62	-73	2	8	15	-15	-20	2	7	-9	-17	9
Cash operating balance, end of period	61	35	36	45	13	30	35	33	20	45	36	30	30	60	45	30
NIPA federal sector					Seasonally adjusted annual rates											
Receipts	1895	1843	1877	2098	1864	1864	1784	1871	1852	1870	1915	1981	2087	2142	2182	2206
Expenditures	2062	2228	2332	2428	2184	2289	2284	2299	2326	2348	2358	2380	2430	2440	2461	2485
Consumption expenditures	573	649	700	735	636	669	672	673	700	712	716	721	736	740	745	750
Defense	370	426	467	489	409	448	444	449	466	476	478	480	489	492	495	498
Nondefense	202	223	233	246	227	221	229	224	234	236	238	241	247	248	250	252
Other spending	1489	1579	1632	1692	1548	1620	1612	1625	1626	1636	1642	1659	1694	1700	1716	1735
Current account surplus	-167	-385	-455	-330	-320	-425	-499	-428	-474	-477	-443	-398	-343	-298	-279	-279
Gross investment	87	92	102	105	87	96	97	100	100	103	104	104	105	105	106	107
Gross saving less gross investment[3]	-165	-387	-464	-339	-318	-430	-505	-436	-482	-487	-453	-408	-353	-308	-289	-289
Fiscal indicators[4]																
High-employment (HEB) surplus/deficit	-107	-302	-405	-311	-230	-332	-429	-359	-418	-434	-407	-373	-324	-282	-266	-268
Change in HEB, percent of potential GDP	1.9	1.7	0.7	-0.9	0.1	0.9	0.8	-0.7	0.5	0.1	-0.3	-0.3	-0.4	-0.4	-0.2	-0.0
Fiscal impetus (FI) percent of GDP	1.0	1.2	1.0	-0.2	0.1	0.5	0.4	0.3	0.3	0.2	0.1	0.2	-0.4	0.0	0.0	0.0

1. OMB's February 2004 baseline surplus estimates are -$527 billion in FY 2004 and -$393 billion in FY 2005 and surplus estimates under enactment of its proposed policies (which do not include additional funding for Iraq) are -$521 billion and -$364 billion, respectively. CBO's March 2004 baseline surplus estimates are -$477 billion in FY 2004 and -$363 billion in FY 2005. 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) 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

Change in Debt of the Domestic Nonfinancial Sectors
(Percent)

			Nonfederal						
				Households					
Period [1]	Total	Federal government	Total	Total	Home mortgages	Consumer credit	Business	State and local governments	Memo: Nominal GDP
Year									
1998	6.9	-1.4	9.7	8.2	8.6	7.3	12.2	6.3	5.7
1999	6.3	-1.9	8.8	8.2	9.1	7.8	10.6	3.4	6.3
2000	4.9	-8.0	8.4	8.7	8.3	10.7	9.5	1.3	4.6
2001	6.3	-0.2	7.7	9.1	10.0	8.0	6.0	8.9	2.4
2002	7.1	7.6	7.0	10.0	12.5	4.4	2.8	11.1	4.2
2003	8.1	10.9	7.5	10.3	12.5	5.2	3.9	8.2	5.9
2004	8.2	12.3	7.3	9.1	10.6	5.3	5.5	5.4	6.0
2005	7.1	7.9	6.9	7.8	8.5	6.1	6.2	4.6	5.2
Quarter									
2003:1	6.5	4.5	6.9	9.9	12.1	4.2	3.5	5.7	4.3
2	11.3	20.4	9.4	11.8	13.8	6.1	5.9	12.3	4.2
3	7.0	8.2	6.8	9.9	11.5	6.1	3.0	6.1	10.0
4	6.6	9.0	6.1	8.3	10.5	3.9	3.0	7.9	5.3
2004:1	8.0	12.9	6.9	8.9	10.6	4.4	4.9	4.0	6.6
2	8.7	17.0	6.8	9.0	10.6	5.1	4.8	3.0	5.8
3	7.6	7.8	7.5	9.0	10.3	5.4	5.6	8.0	5.7
4	7.7	9.5	7.3	8.3	9.4	5.6	6.2	6.3	6.0
2005:1	7.9	12.0	6.9	7.9	8.8	5.8	6.0	5.3	5.5
2	7.1	8.8	6.8	7.7	8.5	5.9	6.0	4.5	5.1
3	6.3	5.0	6.6	7.5	8.1	6.0	6.0	4.2	5.1
4	6.2	4.8	6.5	7.1	7.6	6.0	6.2	4.2	5.0

Note. Quarterly data are at seasonally adjusted annual rates.
1. Data after 2003:Q4 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

March 11, 2004

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

Category	2002	2003	2004	2005	2003 Q3	2003 Q4	2004 Q1	2004 Q2	2004 Q3	2004 Q4	2005 Q1	2005 Q2	2005 Q3	2005 Q4
Net funds raised by domestic nonfinancial sectors														
1 Total	1331.7	1622.1	1756.3	1630.1	1470.7	1416.0	1723.4	1908.9	1692.9	1700.1	1774.2	1701.6	1524.6	1520.0
2 Net equity issuance	-41.6	-49.1	-88.5	-79.0	-44.9	-34.2	-59.0	-78.0	-81.0	-136.0	-135.0	-65.0	-63.0	-53.0
3 Net debt issuance	1373.3	1671.2	1844.8	1709.1	1515.6	1450.2	1782.4	1986.9	1773.9	1836.1	1909.2	1766.6	1587.6	1573.0
Borrowing sectors														
Nonfinancial business														
4 Financing gap [1]	37.9	-38.7	-38.1	139.7	-77.9	-68.5	-53.1	-70.7	-35.7	7.1	91.9	136.3	165.0	165.4
5 Net equity issuance	-41.6	-49.1	-88.5	-79.0	-44.9	-34.2	-59.0	-78.0	-81.0	-136.0	-135.0	-65.0	-63.0	-53.0
6 Credit market borrowing	196.2	278.0	407.2	481.9	221.4	216.3	363.8	362.2	427.5	475.2	467.2	474.0	484.4	502.1
Households														
7 Net borrowing [2]	775.7	878.4	855.0	795.4	885.1	758.9	834.1	868.6	879.4	837.8	813.5	805.9	795.1	767.2
8 Home mortgages	673.9	758.1	726.2	641.5	743.0	696.5	724.8	743.0	743.4	693.6	666.8	652.1	638.7	608.3
9 Consumer credit	81.4	100.2	107.2	129.9	121.6	77.9	90.6	105.7	113.6	118.7	123.8	129.4	132.3	134.1
10 Debt/DPI (percent) [3]	103.2	109.1	113.7	116.9	109.3	111.7	112.2	113.2	114.2	115.1	115.8	116.6	117.3	118.0
State and local governments														
11 Net borrowing	143.9	118.7	84.8	75.8	91.6	121.6	62.8	46.8	126.8	102.8	86.8	74.8	70.8	70.8
12 Current surplus [4]	170.1	169.8	153.0	166.8	199.3	184.5	150.0	154.9	149.9	157.3	162.0	163.6	168.6	173.0
Federal government														
13 Net borrowing	257.5	396.0	497.9	356.0	317.5	353.4	521.7	709.4	340.2	420.3	541.8	412.0	237.4	232.9
14 Net borrowing (n.s.a.)	257.5	396.0	497.9	356.0	107.6	118.6	149.4	102.3	115.1	131.1	154.4	28.0	89.3	84.2
15 Unified deficit (n.s.a.)	230.6	394.7	483.5	345.9	104.5	128.7	178.2	61.8	104.2	139.2	161.9	-11.0	86.9	108.2
Depository institutions														
16 Funds supplied	482.5	479.9	462.3	507.3	152.6	391.0	516.7	443.5	499.9	389.0	511.0	515.9	566.5	436.0
Memo (percentage of GDP)														
17 Domestic nonfinancial debt [5]	190.7	196.0	199.6	203.7	196.2	197.2	197.8	199.1	200.3	201.2	202.4	203.6	204.5	205.2
18 Domestic nonfinancial borrowing	13.1	15.2	15.8	13.9	13.6	12.9	15.6	17.1	15.1	15.4	15.8	14.4	12.8	12.5
19 Federal government [6]	2.5	3.6	4.3	2.9	2.9	3.1	4.6	6.1	2.9	3.5	4.5	3.4	1.9	1.9
20 Nonfederal	10.6	11.6	11.5	11.0	10.8	9.7	11.0	11.0	12.2	11.9	11.3	11.1	10.9	10.7

Note. Data after 2003:Q4 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.
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.

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International Developments

Economic activity among our foreign trading partners appears to be strengthening broadly in line with our previous expectations. Notwithstanding an upward revision to growth in the second half of last year, our outlook for future aggregate foreign growth is about unchanged from that in the January Greenbook. Similarly, our outlook for foreign consumer price inflation is little different, except for a slightly higher projection in the near term caused by the recent runup in oil and other commodity prices. The modest appreciation of the dollar over the intermeeting period has only slightly diminished the stimulus to our outlook for U.S. real net exports that stems from the sizable net depreciation of the dollar over the past two years.

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

Indicator	2003		Projection				
	H1	Q3	2003: Q4	2004 Q1	2004 Q2	2004 H2	2005
Foreign output	.8	4.2	4.5	3.7	3.8	3.8	3.5
January GB	*.6*	*3.9*	*3.9*	*3.8*	*3.8*	*3.8*	*3.5*
Foreign CPI	1.9	1.3	3.1	2.8	2.0	1.9	1.9
January GB	*1.9*	*1.4*	*3.1*	*2.6*	*1.9*	*1.9*	*1.9*

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

Prices for crude oil and many other commodities have increased appreciably over the intermeeting period. The spot price of West Texas intermediate has averaged more than $36.50 per barrel since the beginning of March, about $2 per barrel above its average in January and February. In line with quotes from futures markets, we have marked up our oil price projection about $3 per barrel this year and nearly as much next year. Concerns about oil supplies appear to have figured prominently in these price increases, although strong demand has also played a role. For other commodities, particularly raw materials and industrial metals, increased demand (notably from China) appears to have been the primary force behind the runup in prices. Record-high shipping rates for bulk cargo and reports of bottlenecks in certain ports support the view that much of the rise in primary commodity prices has been driven by demand. Higher commodity prices have led us to mark up our projection for import prices.

Since the January FOMC meeting, the exchange value of the dollar has been unusually volatile and has risen about 2 percent on balance as measured by the staff's broad index. Our forecast for the path of the dollar begins at this higher level, and we have retained the slight downward tilt over the forecast period as the need to finance the large U.S. current account deficit will likely remain a source of downward pressure on the dollar. Recognizing that exchange rate adjustments are far from predictable, we consider the implications of further dollar appreciation in the alternative simulation.

We continue to project that the U.S. current account deficit will widen in dollar terms over the forecast period, edging above $600 billion at the end of 2005. Compared with the January Greenbook, the projected deficit is somewhat larger, importantly reflecting the effect of higher oil prices on nominal imports. As a share of GDP, the current account deficit is expected to remain close to 5 percent, about the same as in 2003. Assuming no faster depreciation of the dollar and no further pickup in economic growth abroad relative to the United States than we project for the next couple of years, the current account deficit as a share of GDP would likely resume widening shortly beyond the forecast horizon.

Real net exports are now estimated to have made a negative arithmetic contribution of 0.3 percentage point to U.S. GDP growth in the fourth quarter of 2003, compared with the neutral contribution estimated in the January Greenbook. The revision is due mainly to the December trade report, which contained surprisingly strong imports. This year and next, net exports are projected to subtract about ¼ percentage point from U.S. GDP growth, a projection that is little changed from the January Greenbook.

Oil Prices

The spot price of WTI crude oil closed at $36.13 per barrel on March 10, up from an average of $34.25 per barrel in January. Oil prices edged down in early February but reversed course after OPEC's surprise decision to decrease its production target 1 million barrels per day as of April. In the past two weeks, an escalation of political turmoil in Venezuela has renewed concerns about that country's reliability as an oil supplier. Oil exports from Iraq continue but still have not reached pre-war levels. Additional upward pressure on oil prices, which are quoted in dollars, has come from the net depreciation of the dollar over the past two years as well as strong global demand. The projected path of oil prices, in line with recent quotes from futures markets, calls for the spot price of WTI to fall to about $33 per barrel by the fourth quarter of 2004 and to less than $30 per barrel by the fourth quarter of 2005. Compared with that in the January Greenbook, this price path is about $3 per barrel higher this year and about $2.50 per barrel higher next year.

International Financial Markets

Foreign exchange rates fluctuated over a wide range during the intermeeting period. The dollar strengthened following the FOMC's announcement in

January but soon resumed its earlier trend of depreciation and touched multiyear lows against the European currencies and the yen in mid-February. In a turnaround that appeared only loosely related to economic fundamentals, the dollar appreciated over the following two weeks, rising about 5 percent against the yen, the euro, and sterling. The release of the weaker-than-expected February employment report on March 5 prompted a sharp drop in the dollar's exchange value against the major European currencies; downward pressures on the dollar against the yen that day were checked by exceptionally large purchases of dollars by the Japanese monetary authorities. Since March 5, the dollar has partially retraced this decline. On a trade-weighted basis, the dollar appreciated almost 3 percent on balance against the major foreign currencies and ½ percent against the currencies of our other important trading partners.

The dollar appreciated 4¾ percent on balance against the yen over the intermeeting period, between 3 and 4 percent against the major continental European currencies, and 1½ percent against the Canadian dollar and sterling. Japanese monetary authorities continued to intervene frequently and heavily during the intermeeting period, not only to counter upward pressure on the yen as in previous months but also to strengthen downward pressure on the yen during its recent decline. Total purchases of dollars for yen by Japan's Ministry of Finance over the intermeeting period were about $70 billion. The dollar appreciated about 1 percent on net vis-à-vis the Mexican peso, appreciated 20 percent against the Venezuelan bolivar because of a shift in the bolivar's peg, and was generally little changed against the currencies of developing Asian economies.

Reflecting these intermeeting developments in foreign exchange markets, the broad real dollar index is now expected to be about 2 percent stronger in the second quarter than projected in the January Greenbook. We project that on balance the broad real dollar will depreciate at an annual rate of about 1¼ percent over the forecast period as a result of the need to finance the large U.S. current account deficit.

The Bank of England tightened policy in February, and market expectations are for further tightening in coming months. The European Central Bank did not adjust its policy stance over the intermeeting period. The yield curve derived from contracts on near-dated euro interest rate futures continues to suggest that market participants do not anticipate any rate hikes by the ECB before year-end and even place small odds on a rate cut, owing in part to the inflation-restraining effects of the euro's strength. Canadian short- and long-term interest rates declined in reaction to the Bank of Canada's March 2 decision to ease policy. On net over the intermeeting period, ten-year sovereign yields declined almost 30 basis points in Canada and Germany and nearly 20 basis points in the United

Kingdom; much of these declines occurred after the release of the U.S. employment report for February. In contrast, the yield on the benchmark JGB changed little. Share prices moved up further in European industrial countries over most of the intermeeting period, but fell very late in the period, especially on March 11. In contrast, Japanese equities rose 5 percent on balance over the intermeeting period, reflecting in part the improved outlook for Japan. On the morning of March 11, news of the terrorist event in Spain rattled financial markets, prompting some shifts toward safe-haven assets.

Brazil's EMBI+ spread widened 135 basis points over the intermeeting period but remains relatively low compared with recent history, and Brazilian share prices dropped about 11 percent, in part because a campaign-finance scandal affecting President Lula's party fueled concerns that economic and fiscal reform is slowing. Late in the intermeeting period, the Argentine government and the IMF agreed that Argentina would make a scheduled debt payment of $3.1 billion on March 9 and that the IMF's Board would approve the current review of Argentina's program. Argentine financial asset prices, which had declined in the days prior to the reaching of the agreement, subsequently recovered modestly. The Argentine EMBI+ spread was little changed on balance over the intermeeting period and remains sky-high.

. The Desk did not intervene during the period for the accounts of the System or the Treasury.

Foreign Industrial Countries

Real GDP in the foreign industrial countries is projected to grow 2¾ percent in the current quarter, following growth of 3½ percent in the fourth quarter. The recovery that began in the second half of 2003 is expected to continue, with projected growth for 2004 and 2005 averaging slightly less than 3 percent, a notable pickup from the 1¾ percent recorded in 2003. Recent indicators of economic activity have come in stronger than expected in Japan and the United Kingdom, and we have revised up our outlook accordingly. In contrast, we have marked down our outlook for the euro area and Canada, particularly for this year, as incoming data have been somewhat weaker than expected. The higher projected path for oil prices is judged to have only a marginal effect on the outlook for growth in these countries. On balance, our projection of real GDP growth in foreign industrial countries is about unchanged from the January Greenbook. Twelve-month headline inflation rates are expected to remain moderate in most foreign industrial countries. In Japan, deflation has lessened markedly, and consumer prices are projected to stabilize during the forecast period.

Our outlook for Japan calls for real GDP growth to slow from 3½ percent in 2003, including growth of 6½ percent in the fourth quarter, to 2½ percent in 2004 and 2 percent in 2005. Much of Japan's recovery in recent quarters has been due to buoyant exports to developing Asia; with growth in this region slated to moderate from its brisk second-half rebound, the stimulus from exports and export-related investment will likely diminish. We assume that fiscal policy will be contractionary over the forecast period as the government takes steps toward fiscal consolidation, including raising some taxes. Although labor market conditions have improved somewhat, real wage growth remains anemic, and personal consumption is projected to be sluggish. We anticipate that aggregate demand over the forecast period will be strong enough to stabilize consumer prices, but not sufficiently robust to push inflation into positive territory. Therefore, we assume that the Bank of Japan will continue its policy of quantitative easing.

In the euro area, real GDP is expected to increase around 2 percent in 2004 and 2005, after growing only ½ percent in 2003. Stronger consumption and a rebound in investment, after three years of weakness, are expected to support economic activity going forward. Recent indicators of consumer and business confidence have been mixed but generally point to a firming of activity. Retail sales in January ticked up, supporting our projected 1¾ percent increase in real GDP in the current quarter, a modest rise from the fourth quarter's 1¼ percent pace. With twelve-month inflation below the upper limit of 2 percent, we assume that the ECB will leave its policy rate at 2 percent through mid 2005 and will increase rates slightly thereafter.

In the United Kingdom, real GDP is projected to maintain its strong expansion into the first quarter, with growth slightly more than 3½ percent. British growth has been supported by a considerable increase in government spending and by robust consumption, partly from wealth effects associated with the rapid increase in house prices. We expect consumption growth to soften as the rate of house price appreciation moderates, leading real GDP growth to subside gradually to 2½ percent by the end of the forecast period. Inflation is expected to trend up, reaching the Bank of England's 2 percent target by the end of 2005. We assume that the Bank of England, in consequence, will continue to gradually tighten monetary policy.

In Canada, real GDP grew 3¾ percent in the fourth quarter, as a sizable accumulation of inventories masked relatively weak final domestic demand. The pace of growth is expected to slow a bit as the boost from inventories fades but then is expected to climb to 3½ percent by early 2005 as the negative effects of the past appreciation of the Canadian dollar wane. Inflation is expected to remain below the 2 percent midpoint of the Bank of Canada's inflation target band throughout the forecast period. With inflationary pressures quiescent and the currency relatively strong, we assume that the Bank of Canada will leave its policy rate unchanged through mid 2005; we assume some modest tightening thereafter.

Other Countries

For developing Asia, data released since the January Greenbook indicate that growth has generally continued to be robust, largely as a result of strong exports, particularly of high-tech products. Our estimate of fourth-quarter GDP growth remains about unchanged at 7 percent. We continue to expect the pace of expansion in developing Asia to moderate to about 5½ percent, on average, over the next two years. The apparent strength of global demand for high-tech goods may be the source of some upside risk to the forecast for several high-tech-oriented economies.

Incoming data for China, Hong Kong, and Taiwan have been distorted by the change in the Lunar New Year holiday from February last year to January this year. Adjusting for this effect, economic activity appears to have remained strong in January. We continue to project that real GDP growth in China will average 8 percent over the forecast period, reflecting strong domestic and external demand. Chinese authorities have been attempting to curb credit growth out of concern that the continued accumulation of foreign reserves (which now total more than $400 billion) will fuel money supply growth and inflation. Nonetheless, we maintain our working assumption that China will retain its exchange rate peg at least through 2005. Growth in other Asian economies is expected to be in the range of 4 percent to 6 percent over the forecast period as external demand remains strong, reflecting both robust demand from China and rising global demand for high-tech products. In Korea, the strong external sector should keep real GDP growth near 5¼ percent this year and next, even as high consumer debt, the nuclear standoff with North Korea, and political uncertainty ahead of the April elections weigh on the outlook for domestic demand.

Mexico appears to have broken out of its economic slump. Real GDP grew 5 percent in the fourth quarter and brought the historical relationship between Mexican GDP and U.S. industrial production back on track. The Bank of Mexico, citing concerns about building inflationary pressures, tightened monetary policy in late February. In consequence, we have marked down our outlook for Mexican GDP growth slightly but still expect it to average

4½ percent over the forecast period. In Brazil, real GDP grew 6 percent in the fourth quarter, higher than we had anticipated in the January Greenbook. Nonetheless, we have tempered our outlook for Brazilian GDP growth, in large part because market interest rates have moved up following a pause in the central bank's lowering of policy interest rates.

Prices of Internationally Traded Goods
After a 1½ percent (a.r.) increase in the fourth quarter of 2003, prices of imported core goods are projected to rise 6¼ percent in the current quarter. Monthly data from the BLS indicated that import prices stepped up markedly in January and February. Much of the increase reflected higher prices for industrial supplies, largely natural gas and metals, although prices in other categories also rose. For the remainder of the year, we project core import prices to rise at an annual rate of about 3½ percent. We have revised up our projection for core import price inflation in 2004 nearly 1 percentage point from the January Greenbook because of both the strong January and February data and the considerable rise in commodity prices over the intermeeting period. In 2005, core import price inflation is expected to fall sharply as commodity prices ease and the effects of the previous dollar depreciation wane.

Selected Trade Prices
(Percent change from end of previous period except as noted; s.a.a.r.)

Trade category	2003		Projection				
	H1	Q3	2003: Q4	2004			2005
				Q1	Q2	H2	
Exports							
Core goods	3.5	1.1	5.4	6.6	3.4	.4	.4
Imports							
Non-oil core goods	2.5	.6	1.5	6.2	3.6	3.6	.5
Oil (dollars per barrel)	26.46	28.03	27.75	31.42	33.21	30.18	27.16

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.

We project prices of exported core goods to rise 6½ percent in the current quarter, even faster than in the fourth quarter. These price increases are driven by higher prices for agricultural products, especially soybeans and wheat, as well as higher prices for petroleum products and intermediate materials. Core export price inflation is projected to moderate in the second quarter and to fall considerably thereafter; the contour of this projection is driven largely by the path for agricultural prices.

Trade in Goods and Services
Real exports of goods and services are estimated to have risen at an annual rate of nearly 21 percent in the fourth quarter of 2003, somewhat faster than we estimated in the January Greenbook as exports in December came in stronger than expected. Conversely, exports in January came in weaker than expected, leading us to project an even sharper slowing of real export growth in the current quarter. Factors behind this slowdown include the tendency of core exports to grow more slowly in the first quarter; a tempering of growth in services exports after their strong, travel-related rebound in the second half of last year; and bans on U.S. beef imposed by our trading partners. Given the volatility of the trade statistics, we do not interpret January's drop in exports as a sign of flagging export demand. Notwithstanding our downward revision to the growth rate of real exports, the level of real exports projected for the current quarter is down only slightly from that in the January Greenbook.

We continue to assume that bans on foreign imports of U.S. beef will gradually be lifted over the forecast period. Consistent with this assumption, Mexico announced on March 4 that it will begin to accept shipments of certain types of U.S. beef products. Since the January Greenbook, many countries have also initiated selective bans on U.S. poultry following several outbreaks of avian flu. The effects of the poultry bans are expected to be small and short-lived. U.S. exports may also be reduced, but only slightly, by the imposition of tariffs by the European Union on several categories of U.S. goods. These tariffs were imposed in retaliation for U.S. noncompliance with a World Trade Organization decision that the Foreign Sales Corporation (FSC) tax benefit constitutes an illegal export subsidy. The Congress is expected to repeal the FSC act, at which point the tariffs will be eliminated.

Over the remainder of the forecast period, we have made only minor changes to our outlook for real exports of goods and services. Exported core goods are projected to grow about 10 percent at an average annual rate over the rest of 2004 and 2005. Expanding economic activity abroad accounts for more than 4 percentage points of this growth each year, and the effects of the dollar's previous real depreciation account for about 3 percentage points. In addition, about 2½ percentage points of growth reflects a projected return of core exports to their historical relationship with relative prices and foreign income. Real exports of services are projected to grow nearly 8 percent in 2004 but then to slow to a 6½ percent pace in 2005 as the boost from the previous depreciation of the dollar plays out relatively quickly. Exports of computers and semiconductors are expected to grow at double-digit rates, reflecting a strong recovery in the global high-tech sector.

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

Measure	2003		Projection				
	H1	Q3	2003: Q4	2004 Q1	2004 Q2	2004 H2	2005
Real exports	-1.5	9.9	20.5	4.6	11.9	13.2	10.8
January GB	*-1.5*	*9.9*	*17.9*	*7.6*	*12.0*	*13.3*	*11.1*
Real imports	.9	.8	16.0	6.6	11.1	9.3	9.0
January GB	*.9*	*.8*	*11.8*	*7.9*	*11.2*	*9.2*	*8.8*

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

Real imports of goods and services are estimated to have risen at an annual rate of 16 percent in the fourth quarter of 2003, well above the 12 percent pace we estimated in the January Greenbook. The upward revision is due mainly to imports in December, which came in notably stronger than expected. In the current quarter, real imports of goods and services are projected to expand at a more moderate, 6½ percent pace. As with exports, imports of goods and services edged down in January from their high level in December. Imports of core goods in January came in somewhat weaker than anticipated but were partially offset by stronger-than-expected imports of services, oil, and computers. As a consequence, we have revised down our projection for real import growth in the current quarter.

We expect real imports of goods and services to grow briskly in 2004 and 2005, but at a rate somewhat below that of real exports. Real imports of core goods are projected to grow at an average annual rate of 9½ percent over the rest of 2004 as the restraining influence of higher core import prices is more than offset by strong U.S. GDP growth. In 2005, core import growth is projected to slow slightly, reflecting the deceleration of U.S. economic activity. Real imports of services are projected to grow about 5 percent this year and next. Although the slowdown in U.S. GDP growth reduces the growth of services imports in 2005, this effect is offset by the diminishing drag from the previous depreciation of the dollar. As with exports, real imports of computers and semiconductors are projected to grow at double-digit rates over the forecast period.

Beyond the current quarter, our projection for real imports of goods and services is little changed from the January Greenbook, despite the downward revision to U.S. GDP growth and the upward revision to U.S. import price inflation. Based on the strength of imports in the fourth quarter, we have notched up the pace at which core imports are projected to return to the level consistent with their long-run relationship with U.S. GDP and relative prices.

Alternative Simulation

We project that the United States will continue to grow faster than the rest of the world throughout the forecast period. This relatively favorable outlook for the U.S. economy may increase the appetite of investors for U.S. dollar assets relative to what is implied in our projections. In our alternative simulation, we use the FRB/Global model to assess the effects of a fall in the risk premium on the dollar in foreign exchange markets that would generate substantial dollar appreciation. The shock is assumed to occur in 2004:Q2 and has been scaled so that the real value of our broad dollar index would rise 10 percent in the absence of endogenous adjustments in long-term interest rates. This shock depresses net exports, lowering U.S. GDP growth 0.2 percentage point relative to baseline in 2004:H2, and about 0.5 percentage point in 2005. Core PCE inflation falls 0.1 percentage point below baseline in 2004:H2 because of the direct effect of lower prices for imported goods and services. In 2005, inflation is about 0.1 percentage point below baseline, reflecting in part the effects of reduced resource utilization on domestic prices.

Alternative Simulation:
10 Percent Appreciation of the Broad Real Dollar
(Percent change from previous period, annual rate)

Indicator and simulation	2004		2005	
	H1	H2	H1	H2
U.S. real GDP				
Baseline	4.7	5.3	4.1	3.9
Dollar Appreciation	4.6	5.1	3.7	3.3
U.S. PCE prices excl. food and energy				
Baseline	1.2	1.0	1.0	1.0
Dollar Appreciation	1.1	.9	.9	.9

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.

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

Measure and country	1997	1998	1999	2000	2001	2002	2003	Projected 2004	2005
REAL GDP (1)									
Total foreign	4.2	1.5	5.0	4.3	0.3	2.8	2.6	3.7	3.5
Industrial Countries	3.4	2.7	4.4	3.7	0.6	2.5	1.8	2.9	2.8
of which:									
Canada	4.4	4.4	5.9	4.2	1.4	3.5	1.6	3.2	3.5
Japan	0.4	-1.2	0.4	3.8	-2.3	1.7	3.6	2.6	2.1
United Kingdom	3.4	2.8	3.3	2.9	1.9	2.0	2.8	3.4	2.6
Euro Area (2)	3.2	2.0	3.9	2.7	0.8	1.1	0.6	2.1	2.0
Germany	1.7	0.7	3.3	1.9	0.5	0.5	0.0	2.0	1.6
Developing Countries	5.4	-0.3	6.1	5.3	-0.2	3.3	3.8	5.1	4.6
Asia	5.0	-2.2	8.7	6.2	1.0	5.6	5.4	5.8	5.4
Korea	3.4	-5.2	13.8	5.1	4.2	7.0	1.3	5.2	5.2
China	8.7	9.5	4.1	8.0	7.5	8.0	9.9	8.3	7.7
Latin America	6.1	1.2	4.2	4.4	-1.3	1.3	2.1	4.6	3.9
Mexico	6.8	2.9	5.4	4.8	-1.3	1.8	2.0	5.1	4.2
Brazil	2.3	-1.7	3.5	3.8	-0.8	3.7	-0.2	3.0	3.0
CONSUMER PRICES (3)									
Industrial Countries	1.5	0.9	1.1	1.7	0.9	2.1	1.3	1.3	1.3
of which:									
Canada	1.0	1.1	2.4	3.1	1.1	3.8	1.7	1.5	1.6
Japan	2.1	0.7	-1.1	-1.2	-1.3	-0.5	-0.4	-0.1	0.0
United Kingdom (4)	1.7	1.4	1.2	1.0	1.0	1.6	1.3	1.7	2.0
Euro Area (2)	1.5	0.8	1.5	2.5	2.1	2.3	1.9	1.8	1.6
Germany	1.5	0.3	1.1	1.7	1.5	1.2	1.2	1.1	1.0
Developing Countries	6.8	9.0	4.6	4.1	2.8	2.9	3.0	3.2	2.7
Asia	2.7	4.4	0.1	1.8	1.1	0.7	2.1	2.4	2.2
Korea	5.0	5.8	1.2	2.6	3.4	3.4	3.5	3.1	3.0
China	0.8	-1.2	-1.0	0.9	-0.1	-0.5	2.7	2.3	1.7
Latin America	15.5	15.4	12.5	8.4	5.3	6.5	4.9	4.5	3.5
Mexico	17.0	17.3	13.4	8.7	5.1	5.3	4.0	4.1	3.1
Brazil	4.6	2.0	8.4	6.4	7.5	10.7	11.5	6.0	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.

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

	2003				Projected 2004				Projected 2005			
Measure and country	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
REAL GDP (1)	Quarterly changes at an annual rate											
Total foreign	1.2	0.4	4.2	4.5	3.7	3.8	3.8	3.7	3.6	3.6	3.5	3.4
Industrial Countries	1.6	0.1	1.8	3.5	2.7	2.9	2.9	2.9	2.9	2.9	2.8	2.8
of which:												
Canada	2.5	-1.0	1.3	3.8	2.9	3.2	3.3	3.3	3.6	3.6	3.4	3.4
Japan	2.2	3.5	2.5	6.4	3.1	2.7	2.3	2.1	2.2	2.1	2.2	2.2
United Kingdom	1.2	2.6	3.4	3.8	3.6	3.5	3.4	3.1	2.8	2.7	2.5	2.5
Euro Area (2)	-0.1	-0.4	1.6	1.2	1.7	2.2	2.3	2.3	2.2	2.0	2.0	1.9
Germany	-1.0	-0.6	0.8	0.9	1.6	2.2	2.2	2.1	1.8	1.6	1.5	1.4
Developing Countries	0.6	0.8	7.9	5.9	5.1	5.1	5.0	5.0	4.7	4.7	4.5	4.4
Asia	3.2	-3.4	15.6	7.0	5.8	5.8	5.8	5.8	5.6	5.6	5.2	5.1
Korea	-1.6	-2.7	4.7	5.0	5.2	5.2	5.3	5.2	5.5	5.5	5.0	5.0
China	16.3	-2.9	19.6	7.9	8.4	8.4	8.2	8.2	8.0	8.0	7.5	7.5
Latin America	-2.4	4.6	1.2	5.3	4.8	4.7	4.6	4.4	3.9	3.9	3.9	3.9
Mexico	-0.3	3.1	0.2	4.9	5.4	5.2	5.0	4.8	4.2	4.2	4.2	4.2
Brazil	-3.2	-3.7	0.4	6.1	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
CONSUMER PRICES (3)	Four-quarter changes											
Industrial Countries	2.4	1.7	1.4	1.3	0.9	1.4	1.4	1.3	1.1	1.2	1.3	1.3
of which:												
Canada	4.5	2.8	2.1	1.7	1.1	1.8	1.7	1.5	1.2	1.4	1.6	1.6
Japan	-0.3	-0.2	-0.5	-0.4	-0.4	-0.3	-0.1	-0.1	-0.1	-0.0	0.0	0.0
United Kingdom (4)	1.5	1.3	1.4	1.3	1.3	1.8	1.7	1.7	1.7	1.8	1.9	2.0
Euro Area (2)	2.3	1.9	2.0	1.9	1.8	2.0	2.0	1.8	1.6	1.5	1.6	1.6
Germany	1.1	0.9	1.0	1.2	1.1	1.5	1.4	1.1	1.0	0.9	0.9	1.0
Developing Countries	3.5	3.0	2.6	3.0	3.0	3.4	3.7	3.2	2.9	2.8	2.8	2.7
Asia	1.3	1.1	1.1	2.1	2.2	2.8	3.1	2.4	2.2	2.1	2.1	2.2
Korea	4.1	3.3	3.2	3.5	3.2	3.5	3.7	3.1	3.0	3.0	3.0	3.0
China	0.5	0.6	0.9	2.7	3.1	3.7	3.7	2.3	1.8	1.8	1.8	1.7
Latin America	7.1	6.4	5.4	4.9	4.7	4.7	4.8	4.5	4.1	3.8	3.7	3.5
Mexico	5.5	4.7	4.1	4.0	4.3	4.5	4.4	4.1	3.6	3.3	3.2	3.1
Brazil	15.7	17.0	15.3	11.5	6.7	5.3	5.9	6.0	5.6	5.5	5.3	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.

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1997	1998	1999	2000	2001	2002	2003	Projected 2004	2005
NIPA REAL EXPORTS and IMPORTS									
Percentage point contribution to GDP growth, Q4/Q4									
Net Goods & Services	-0.8	-1.1	-1.0	-0.9	-0.2	-0.9	-0.0	-0.3	-0.2
Exports of G&S	0.9	0.3	0.6	0.7	-1.3	0.3	0.6	1.1	1.1
Imports of G&S	-1.7	-1.4	-1.6	-1.6	1.1	-1.2	-0.6	-1.3	-1.3
Percentage change, Q4/Q4									
Exports of G&S	8.3	2.6	5.6	6.5	-11.5	3.3	6.4	10.7	10.8
Services	0.4	4.4	5.3	1.8	-8.3	9.3	4.8	7.9	6.6
Computers	26.7	7.3	13.4	22.7	-22.8	-0.9	11.4	35.4	31.1
Semiconductors	21.1	9.5	34.6	27.6	-34.9	9.7	38.8	36.0	33.5
Other Goods 1/	9.8	1.2	3.3	5.9	-9.8	0.4	5.0	8.7	9.6
Imports of G&S	14.3	11.0	12.1	11.2	-7.4	9.4	4.4	9.1	9.0
Services	11.9	10.4	6.5	10.7	-4.6	6.7	0.2	4.9	5.0
Oil	4.2	4.2	-3.4	13.3	0.1	3.7	2.2	0.0	1.5
Computers	32.6	26.4	26.0	13.9	-12.9	13.5	16.9	38.6	31.1
Semiconductors	32.5	-7.7	34.2	22.8	-51.3	9.7	0.5	38.5	33.5
Other Goods 2/	13.1	11.2	12.9	10.5	-6.2	10.3	5.0	8.6	8.4
Billions of Chained 2000 Dollars									
Net Goods & Services	-104.6	-203.8	-296.3	-379.5	-398.1	-470.6	-508.8	-538.9	-564.1
Exports of G&S	943.7	966.5	1008.2	1096.3	1039.0	1014.2	1034.7	1144.9	1274.3
Imports of G&S	1048.3	1170.3	1304.5	1475.8	1437.1	1484.7	1543.5	1683.8	1838.5
Billions of dollars									
US CURRENT ACCOUNT BALANCE	-127.7	-204.7	-290.8	-411.5	-393.7	-480.9	-547.2	-575.2	-606.9
Current Acct as Percent of GDP	-1.5	-2.3	-3.1	-4.2	-3.9	-4.6	-5.0	-4.9	-4.9
Net Goods & Services (BOP)	-107.0	-163.2	-261.2	-375.4	-357.8	-418.0	-489.9	-547.8	-570.0
Investment Income, Net	25.1	11.5	22.3	24.2	15.7	1.3	13.8	41.3	29.7
Direct, Net	72.4	65.5	78.2	94.9	106.5	93.5	94.1	126.7	137.1
Portfolio, Net	-47.3	-54.1	-55.9	-70.7	-90.8	-92.2	-80.3	-85.4	-107.4
Other Income & Transfers,Net	-45.7	-53.0	-52.0	-60.3	-51.6	-64.1	-71.1	-68.7	-66.7

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

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	2000				2001				2002			
	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	-1.5	-0.9	-0.8	-0.1	0.5	-0.2	-0.4	-0.5	-0.7	-1.3	-0.2	-1.5
Exports of G&S	0.7	1.3	1.1	-0.3	-0.5	-1.5	-2.0	-1.0	0.4	0.8	0.4	-0.4
Imports of G&S	-2.2	-2.2	-2.0	0.3	1.0	1.3	1.6	0.5	-1.1	-2.1	-0.6	-1.1
Percentage change from previous period, s.a.a.r.												
Exports of G&S	6.6	12.3	10.7	-2.7	-4.5	-13.4	-17.7	-9.8	4.4	8.7	4.3	-3.7
Services	1.4	8.4	-6.6	4.5	-2.0	-0.6	-14.7	-15.0	22.9	1.6	4.4	9.4
Computers	32.7	47.0	30.1	-10.7	-7.7	-40.8	-20.1	-18.6	-22.2	3.2	4.6	14.6
Semiconductors	24.2	73.7	35.0	-8.9	-29.5	-54.1	-45.7	2.3	26.6	40.5	11.8	-27.1
Other Goods 1/	5.9	7.5	16.0	-4.5	-2.7	-12.1	-16.6	-7.4	-2.8	10.8	3.7	-9.0
Imports of G&S	16.7	16.5	14.1	-1.6	-6.2	-8.5	-10.8	-3.8	8.4	17.1	4.1	8.2
Services	20.9	10.6	14.3	-1.8	-3.2	12.5	-18.1	-6.9	19.3	-3.7	0.7	12.1
Oil	28.5	40.6	-2.6	-6.4	23.3	7.1	-26.8	3.7	-19.3	35.3	-10.9	18.9
Computers	-2.2	44.9	35.4	-12.3	-25.7	-20.5	-10.9	9.3	38.4	11.5	6.5	0.9
Semiconductors	25.0	45.4	71.1	-26.9	-43.5	-70.4	-55.4	-24.6	44.5	34.6	-6.5	-20.3
Other Goods 2/	16.4	12.2	12.2	1.8	-6.1	-10.0	-4.8	-4.0	5.9	21.4	7.0	7.5
Billions of Chained 2000 Dollars, s.a.a.r.												
Net Goods & Services	-350.6	-374.5	-395.6	-397.2	-385.9	-391.7	-401.3	-413.4	-431.2	-467.6	-471.9	-511.5
Exports of G&S	1060.9	1092.0	1120.0	1112.3	1099.6	1060.9	1010.6	984.8	995.4	1016.5	1027.3	1017.5
Imports of G&S	1411.5	1466.5	1515.6	1509.5	1485.5	1452.7	1411.9	1398.2	1426.7	1484.1	1499.2	1529.0
Billions of dollars, s.a.a.r.												
US CURRENT ACCOUNT BALANCE	-380.1	-396.5	-434.3	-435.0	-416.0	-399.9	-414.5	-344.6	-426.9	-491.3	-490.9	-514.3
Current Account as % of GDP	-3.9	-4.0	-4.4	-4.4	-4.1	-4.0	-4.1	-3.4	-4.1	-4.7	-4.7	-4.8
Net Goods & Services (BOP)	-346.9	-364.5	-391.8	-398.4	-373.8	-357.8	-356.2	-343.5	-360.2	-419.5	-427.9	-464.5
Investment Income, Net	19.9	23.2	15.8	37.8	8.6	8.2	-8.3	54.3	2.2	-12.4	-1.9	17.2
Direct, Net	84.5	88.9	91.9	114.5	94.5	96.7	91.3	143.5	95.7	85.6	87.7	104.9
Portfolio, Net	-64.5	-65.7	-76.1	-76.6	-86.0	-88.4	-99.6	-89.2	-93.5	-98.1	-89.6	-87.7
Other Inc. & Transfers, Net	-53.1	-55.2	-58.3	-74.5	-50.8	-50.3	-50.0	-55.4	-68.9	-59.3	-61.1	-67.1

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

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	2003				Projected 2004				Projected 2005			
	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	0.8	-1.3	0.8	-0.3	-0.5	-0.4	-0.2	0.1	-0.3	-0.4	-0.2	0.0
Exports of G&S	-0.2	-0.1	0.9	1.8	0.4	1.1	1.2	1.4	0.9	1.1	1.1	1.3
Imports of G&S	1.0	-1.2	-0.1	-2.1	-0.9	-1.6	-1.4	-1.3	-1.2	-1.5	-1.3	-1.3
Percentage change from previous period, s.a.a.r.												
Exports of G&S	-2.0	-1.1	9.9	20.5	4.6	11.9	12.2	14.3	8.7	11.1	10.8	12.6
Services	-10.2	0.3	12.7	18.7	6.4	9.0	8.5	7.9	7.2	6.7	6.3	6.0
Computers	-7.4	-11.2	48.7	25.9	26.3	38.6	38.6	38.6	23.9	33.6	33.6	33.6
Semiconductors	44.1	30.1	35.2	46.4	21.6	41.2	41.2	41.2	26.3	36.1	36.1	36.1
Other Goods 1/	0.1	-3.0	4.8	19.3	1.2	9.7	10.4	14.0	7.1	9.8	9.3	12.4
Imports of G&S	-6.8	9.1	0.8	16.0	6.6	11.1	9.7	8.9	8.0	10.4	8.9	8.6
Services	-7.6	-10.9	13.5	7.6	0.9	5.7	6.4	6.7	5.3	4.9	4.9	4.7
Oil	-12.7	55.8	-3.2	-17.0	1.1	16.3	-1.0	-14.0	3.3	19.9	-3.5	-11.2
Computers	-0.4	18.9	15.8	36.2	38.6	38.6	38.6	38.6	23.9	33.5	33.5	33.5
Semiconductors	-0.4	3.1	-1.5	0.8	31.1	41.1	41.1	41.1	26.2	36.0	36.0	36.0
Other Goods 2/	-6.4	9.1	-2.5	22.2	6.1	9.2	9.3	9.7	7.6	8.4	8.7	9.0
Billions of Chained 2000 Dollars, s.a.a.r.												
Net Goods & Services	-490.1	-526.0	-505.2	-514.0	-527.5	-539.5	-545.6	-543.0	-551.7	-563.7	-570.5	-570.6
Exports of G&S	1012.4	1009.6	1033.7	1083.0	1095.2	1126.3	1159.2	1198.6	1224.0	1256.5	1289.0	1327.8
Imports of G&S	1502.5	1535.7	1538.9	1597.0	1622.7	1665.9	1704.9	1741.7	1775.7	1820.2	1859.6	1898.4
Billions of dollars, s.a.a.r.												
US CURRENT ACCOUNT BALANCE	-554.5	-557.2	-541.5	-535.6	-569.1	-569.8	-582.5	-579.4	-598.7	-599.6	-611.8	-617.7
Current Account as % of GDP	-5.2	-5.1	-4.9	-4.8	-5.0	-4.9	-5.0	-4.9	-5.0	-4.9	-4.9	-4.9
Net Goods & Services (BOP)	-486.2	-496.4	-486.6	-490.5	-527.8	-549.6	-556.8	-557.2	-563.2	-571.0	-574.1	-571.5
Investment Income, Net	6.3	12.1	15.3	21.5	35.6	46.7	41.2	41.9	38.7	35.7	26.6	18.0
Direct, Net	88.3	88.8	95.9	103.5	118.6	131.0	127.3	130.1	132.1	137.1	138.1	141.1
Portfolio, Net	-82.0	-76.7	-80.6	-82.0	-83.0	-84.4	-86.1	-88.2	-93.4	-101.4	-111.6	-123.1
Other Inc. & Transfers, Net	-74.6	-73.0	-70.2	-66.7	-76.9	-66.9	-66.9	-64.2	-74.2	-64.2	-64.2	-64.3

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