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Confidential (FR) Class II FOMC

Part 1

August 16, 2001

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

Confidential (FR) Class II FOMC

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Domestic Developments

Although we have once again trimmed our projection for the growth of real GDP over the next six quarters, the economy still does not appear to be slipping into full-scale recession. On the downside, very weak orders for equipment and bleak anecdotes about the high-tech sector have led us again to revise down our near-term outlook for capital goods spending. More broadly, indicators of overall manufacturing output remain weak, and the inventory correction appears less far along than we had expected. Also, activity abroad seems to be flagging more than we anticipated. Nonetheless, the latest employment report suggests that the weakness in manufacturing has not seeped further into other sectors. Consumer sentiment has remained relatively stable, and consumer spending has continued to rise at a moderate rate through the early part of the third quarter. In the second half of the year, consumer purchases should get a sizable boost from the tax rebate, and in addition, housing and consumer durables should continue to be supported by favorable borrowing rates. All told, we expect real GDP to increase at annual rates of 1 percent in the third quarter and 1½ percent in the fourth quarter.

Next year, we are projecting that real GDP will rise 2¾ percent. Several factors account for this pickup. The current drawdown of inventories should have run its course by the end of this year, economic activity abroad should perk up, the permanent portion of the tax cut will be ramping up, and the projected decline in energy prices should free up disposable income. Also, business investment, buoyed by favorable borrowing rates and still-considerable opportunities for profitable implementation of new technologies, should begin to recover.

The Bureau of Economic Analysis revised the level of real GDP at the beginning of this year down about 1 percent. As noted in the memo sent earlier this week to the FOMC, we have revised down our estimate of potential GDP by a like amount, leaving the gap between actual and potential in recent years about unchanged. Looking ahead, we now expect that structural labor productivity will increase 2 percent on average this year and next and that potential output will rise about 3 percent this year and 2¾ percent next year. These downward revisions partly carry forward the now-less-spectacular appearance of recent history and partly reflect our once-again more pessimistic assessment of the prospects for business spending on equipment and software.

Over the forecast period, we have marked down actual output about in line with potential output. Accordingly, we still expect the unemployment rate to rise 5½ percent by the end of next year. On the inflation front, PCE prices are projected to decelerate noticeably this year and a little more next year. The decline in energy prices is the most important factor, but the widening margin of slack in labor and product markets should also put some downward pressure on wage and price increases later in the forecast period.

Key Background Factors

In our baseline forecast, we have assumed that the target federal funds rate will remain unchanged at its current level. We think that the effective stance of monetary policy over the forecast period has changed little since the June meeting because the downward revision to our funds rate path roughly matches the downward revision in our estimate of the equilibrium real interest rate. Futures markets expect about 50 basis points of easing by early next year, followed by roughly 100 basis points of tightening over 2002. Although market participants apparently continue to expect a stronger recovery in economic activity next year than does the staff, the discrepancy in views is considerably smaller now than at the time of the June Greenbook. On net, we expect that yields on longer-term Treasuries, which have moved down a bit since the June FOMC meeting, will remain essentially unchanged over the forecast period.

Equity prices have moved down somewhat since the June Greenbook. We assume that, if the Committee leaves the target funds rate unchanged at this meeting, the broader stock indexes will move a bit lower in the near term and stabilize at a lower level. This path for share prices is a bit lower than that in the last Greenbook. We are cognizant of the downside risks that attend these stock market assumptions. Even though market analysts have trimmed their earnings expectations, they are still more optimistic than we are, and they could be in for a rude shock if earnings follow our forecast path. That said, we should note that our assumed path for the stock market is more pessimistic than a "neutral" profile in which share prices rise in line with the return on bonds adjusted for the equity premium and the dividend yield. (In the alternative simulations section of the Greenbook, we explore the implications of a weaker path for the stock market.)

Credit quality appears to have deteriorated a bit further, about in line with our expectations. Although defaults and downgrades have continued, investment-grade businesses have generally found credit markets to be receptive to their borrowing demands. Bond issuance has moderated from the heavy pace earlier in the year — when market conditions were perceived as quite favorable — now that many businesses have already satisfied their needs for new funding and have refinanced old debt. Looking ahead, we expect borrowing rates to remain low, and we do not see credit availability as an important constraint on economic activity.

Our fiscal policy assumptions — including our assumptions about the influence of the tax cut on consumer spending — are little changed from the last Greenbook. The one minor difference is that we have incorporated information from the Treasury suggesting that the tax rebate currently being paid out will amount to $35 billion rather than $38 billion. Incoming data on tax receipts have been very weak, and we have noticeably marked down our revenue forecast for this year and next. Our projection for the unified budget surplus is $156 billion in fiscal 2001 and $167 billion in fiscal 2002. In terms of on-budget numbers (that is, excluding social security and the Postal Service), we now project *deficits* of $11 billion in fiscal 2001 and $7 billion in fiscal 2002.

Measured against the currencies of a broad group of our trading partners, the real trade-weighted foreign exchange value of the dollar has weakened a bit in the intermeeting period. We anticipate a little further depreciation, leaving the real exchange value of the dollar at the end of 2002 about 1½ percent lower than its level in the June Greenbook.

We have marked down our projection of foreign growth in response to weaker news — including a more dire outlook for Argentina — as well as a softer outlook for the United States. We expect that emerging economies in Asia will be hit especially hard by the greater weakness in the high-tech sector around the world. We now estimate that foreign real GDP increased at an annual rate of only ½ percent in the first half of this year and that it will pick up to an annual rate of only 1½ percent in the second half. We project a recovery next year to about 3 percent. Compared with the last Greenbook, our forecast for economic activity abroad for this year has been cut ¾ percentage point, and our projection for 2002 has been reduced ½ percentage point.

World demand for oil is being restrained by the economic slowdown; however, OPEC appears willing to reduce supply sufficiently to keep prices on a path that it finds attractive, even if doing so means a loss of market share. We expect the spot price of WTI to remain near its current level through the end of the summer and then to decline gradually to about $24 per barrel by the end of the forecast period as additional non-OPEC production comes on line. This path is consistent with quotes in futures markets and is little changed from the path we assumed in the last Greenbook.

Recent Developments and the Near-Term Forecast

With foreign trade for June the only major piece of second-quarter data still outstanding, we are estimating that real GDP eked out an increase last quarter, rising at a meager annual rate of 0.2 percent. This estimate is down ½ percentage point from the BEA's advance release, reflecting weaker incoming data on inventories and construction than the BEA had assumed.

In the third quarter, the economy is expected to remain on a sluggish track, with real GDP rising at an annual rate of just 1 percent. Several powerful negative factors will probably pull down growth again this quarter: Based on the most recent orders data, we think that spending for equipment and software will post an equally gloomy reading this quarter as that in the last. In addition, investment in nonresidential structures should decline again, and net exports are

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

Measure	2001:Q2			2001:Q3	
	June GB	BEA[1]	Aug. GB	June GB	Aug. GB
Real GDP	**.6**	**.7**	**.2**	**1.3**	**1.0**
Private domestic final purchases	-.1	-.1	-.2	1.5	.6
Personal consumption expenditures	1.6	2.1	2.1	2.3	2.9
Residential investment	.7	7.4	4.8	-.8	-.2
Business fixed investment	-8.4	-13.6	-13.4	-2.1	-11.2
Government outlays for consumption and investment	2.2	5.5	5.4	2.9	2.0
	Contribution to growth, percentage points				
Inventory investment	1.0	.0	-.4	.1	.5
Net exports	-.7	-.1	-.2	-.6	-.4

1. Release, July 27, 2001.

likely to make another negative contribution to growth. However, we anticipate that real PCE will be bolstered by the tax cut. Also, even though we expect that firms will continue liquidating inventories this quarter, we think the runoff in nonfarm inventories will be less rapid than it was in the second quarter.

Private payrolls declined further in June and July, about in line with our expectations. Overall, we see labor market developments as consistent with sluggish growth in the economy. As for August, the latest readings on initial claims point to a further decline in payrolls at about the same pace as in July. We are a bit puzzled by the recent behavior of the unemployment rate — in particular, by the fact that it has held at 4.5 percent for a while. As usual, however, we believe that the payroll survey is sending the more-reliable signal about high-frequency changes in labor market conditions and that the underlying weakness will show through to the unemployment rate in coming months. For the third quarter as a whole, we expect the unemployment rate to average 4.7 percent.

Manufacturing production has contracted further since the last Greenbook, and we expect additional declines in coming months. Orders have been quite soft, and despite ongoing liquidation, inventories still appear excessive in many industries. For the third quarter as a whole, we are looking for manufacturing IP to drop at an annual rate of about 5 percent, somewhat less than the average pace of decline in the first half of the year and down about ½ percentage point from our forecast in the June Greenbook.

As indicated above, we expect nonfarm inventories to be shed at a slower pace this quarter than last, and the resulting swing should add about ½ percentage point to real GDP growth. This swing reflects developments in the motor vehicle sector. Although light truck stocks are above the comfortable range, truck production schedules so far this quarter remain surprisingly aggressive; consequently, we think that light truck inventories will move from merely uncomfortable to bloated by the end of the current quarter.

Outside the motor vehicle sector, another sizable inventory liquidation is expected in the current quarter. Indeed, we believe that, with overhangs remaining evident in many areas, the inventory correction still has a way to go, and we are now anticipating considerably more inventory liquidation in the second half of this year than we anticipated in the June Greenbook. Nevertheless, because inventory investment came in lower than expected in the second quarter, inventories are only a small negative for real GDP growth in the second half. As in recent forecasts, we assume that the tax cut is important in the second-half liquidation, as merchandisers use inventories to partially smooth through the demand swings induced by the tax cuts.

PCE remains the key area providing some support to final sales in the near term, and the tax cut plays a leading role in the outlook. The tax cut is expected to boost real PCE growth more than 1½ percentage points this quarter and next, accounting for about half of the gain in real PCE. This extra kick to consumption provides a substantial offset to an array of lackluster fundamentals: negative wealth effects, declining payrolls and sluggish income gains, and cautious consumers facing a rising unemployment rate. Indeed, if not for the tax cut, real PCE would be very weak in the second half of the year.

We estimate that real PCE excluding motor vehicles in July was about 0.5 percent (not at an annual rate) above the second-quarter average. Sales of light vehicles were down in July from the second quarter, and we project that sales in August and September will be lower still. For the third quarter as a whole, we expect light vehicle sales to run at an annual rate of 16 million units, down about ¾ million units from the second-quarter pace. All told, real PCE should increase about 3 percent this quarter.

Homebuilding, supported by favorable financing conditions, has held up well this year. Indeed, this year's decline in mortgage rates has roughly offset the drag from weak income and employment growth. Single-family starts in July were about in line with their second-quarter pace, and we expect no further deterioration from this point. We think that multifamily starts will come in at an annual rate of 340,000 units in the current quarter, about the same as their pace in recent quarters.

We have slashed our projection of real outlays for equipment and software in the near term. The orders data for June were extremely weak, and the revised NIPA data indicate a lower level of profits than before. Published reports and conversations with business contacts also paint a bleak picture. We now expect real spending for equipment and software to drop at an annual rate of 12¾ percent this quarter, about the same pace as that in the second quarter; we anticipate a further decrease of 5¼ percent in the fourth quarter. Outlays for high-tech goods are expected to contract substantially again this quarter — although at a less rapid pace than that in the second quarter — and to stabilize in the fourth quarter. This weakness in the high-tech sector appears to be spreading more widely to other types of equipment. Indeed, outside high-tech and transportation, the retrenchment in investment outlays is projected to steepen in the third quarter.

The weakness in the business sector has now carried over to demand for nonresidential structures. After having risen rapidly through the first quarter, real outlays turned down sharply in the second quarter. Also, with a weaker economic outlook, worse incoming construction data than we had been expecting, and rising vacancy rates, we have built in a more-pronounced downturn in nonresidential structures in the near term. We project that investment in this category will decline at an annual rate of 4¾ percent in the second half of the year, with decreases in outlays for all types of buildings.

After having risen at a robust annual rate of 5½ percent in the second quarter, real government purchases are projected to increase at an annual rate of about 2½ percent in the second half of the year. A sizable part of the slowdown represents a step-down in the pace of state and local highway construction after a couple of blistering quarters.

Net exports are projected to arithmetically subtract about 1/3 percentage point from real GDP growth in the current quarter, a slightly less negative contribution than we anticipated in the June Greenbook. We have revised down our projection of real imports in the third quarter and now expect them to be about unchanged; the revision reflects the markdown of U.S. growth and the expectation that some of the unusual weakness in incoming import data will persist into the current quarter. We have also pushed our projection for the growth rate of real exports into negative territory, owing to weaker foreign demand.

Inflation should remain subdued this quarter. We expect that PCE prices will increase at an annual rate of just 0.7 percent, held down by a plunge in energy prices. With inventories of gasoline and natural gas returning to more-normal seasonal levels, margins have narrowed considerably, and prices of these items have fallen sharply. We expect PCE prices, excluding those for food and energy, to increase at an annual rate of 1.9 percent this quarter, a pace that is higher than the atypically low reading in the second quarter. As for the core CPI, the incoming monthly data point to a more-subdued pace than earlier in the year.

The Longer-Term Outlook for the Economy

Although we have revised down our projection, the basic contour of our forecast still calls for a pickup in real GDP growth next year. By the beginning of next year, excess inventories should have been worked off. The permanent portion of the tax cut should begin to support consumer spending more fully, foreign growth is projected to improve, and energy prices are expected to decline.

Household spending. We expect that real PCE growth will slow to an annual rate of about 2¼ percent in 2002, about ½ percentage point less than in the June Greenbook. The downward revision reflects the less sanguine outlook for permanent income growth in light of the slower structural productivity growth in this forecast.

The revised NIPA numbers show a path for the personal saving rate that is more consistent with our estimate of the likely influence on consumer spending of the reduction in household net worth over the past year and a half. With the wealth-income ratio declining, the saving rate is projected to rise to about 2 percent by the end of the forecast period.

Housing activity has held up relatively well. Although mortgage rates are projected to be a touch lower than in the June Greenbook, income and employment are now expected to be rising more slowly than previously forecast. All told, we expect single-family starts to remain near their current level. Multifamily starts are projected to run at an annual rate of about 340,000 units over the forecast period, the same as in the June Greenbook.

Business spending on equipment and software. We have allowed this year's weakness in equipment and software spending to spill over into next year, and we have lowered our projection for spending to 5½ percent in 2002 — largely in line with the deceleration in business output. In addition, the substantial historical revision to software outlays reported in the new NIPA numbers points to a weaker trajectory going forward than we had thought.

We expect high-tech investment to stabilize by the end of this year, and we are projecting a modest upturn by early next year. Over the longer term, continued technological advances and price declines should make new equipment more

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

Measure	2001 H1	2001 H2	2002
Real GDP	**.8**	**1.3**	**2.7**
Previous	.9	2.1	3.5
Final sales	2.3	1.3	2.2
Previous	2.1	2.0	3.0
PCE	2.6	3.1	2.2
Previous	2.3	2.8	2.7
Residential investment	6.7	-.4	1.3
Previous	2.2	.3	3.0
BFI	-7.0	-8.0	4.0
Previous	-2.8	-.9	6.8
Government purchases	5.4	2.5	3.3
Previous	3.6	2.9	3.5
Exports	-6.0	-0.5	3.9
Previous	-1.8	2.9	5.3
Imports	-6.0	1.4	6.4
Previous	-2.6	4.5	7.4
	Contribution to growth, percentage points		
Inventory change	-1.5	-.1	.5
Previous	-1.2	.0	.5
Net exports	.2	-.3	-.5
Previous	.2	-.3	-.5

attractive. However, the recovery we have penciled in for next year — an increase of 13½ percent in high-tech investment — is mild by historical standards. We do not expect real outlays outside high-tech and transportation to turn up until the second half of next year, in line with the timing of accelerator effects. Attractive borrowing rates also should provide some support for spending in this category next year.

Nonresidential structures. We expect that real spending for nonresidential structures will be flat next year, as a small decline in outlays for buildings is offset by continued increases in spending for electricity-generating facilities. Outlays for oil and gas drilling should drop off by the end of next year in response to lower oil prices.

Despite the retrenchment in purchases of nonresidential structures that we are projecting, the decreases fall well short of former episodes of decline. During the past couple of years, when vacancy rates were quite low, builders were reasonably restrained and avoided the excesses of past booms. Also, although delinquencies in the CMBS market are up a bit recently, spreads in this market have remained fairly flat. This pattern suggests that the commercial real estate market is not overbuilt to the same degree that it has been at times in the past.

Inventory investment. As nonfarm inventory investment turns positive next year, inventories should contribute ½ percentage point to real GDP growth. Despite these accumulations, nonfarm inventory-sales ratios are still projected to decline, on balance, over the forecast period and to move closer to their pre-slowdown trends.

Government spending. Real federal purchases should increase about 3 percent next year, a pace well above the average in recent years. Despite the revenue loss associated with the tax cut, our estimates suggest that this pace of spending growth can be maintained with only a small on-budget deficit. We anticipate that state and local purchases will rise 3½ percent next year following an increase of 4¼ percent this year. As state revenues come under increasing downward pressure later this year and next, we believe that states will dip further into rainy day funds to sustain spending.

Net exports. We expect that real exports, after falling 3¼ percent this year, will rise 4 percent next year as foreign growth recovers; this path is weaker than that in the June Greenbook largely because of the more sluggish outlook for foreign growth. Following a decline of 2¼ percent this year, real imports are expected to increase 6½ percent next year as the U.S. economy strengthens. Overall, we project that net exports will subtract ½ percentage point from real GDP growth in 2002. (The International Developments section provides a more detailed discussion of the outlook for the external sector.)

Aggregate Supply, the Labor Market, and the Outlook for Inflation

As noted earlier, we have revised down our estimate of structural labor productivity growth. We now believe that, from 1998 to 2000, structural labor productivity increased at an average annual rate of 2.7 percent per year, down 0.4 percentage point from our previous estimate. We assume that, going forward, multifactor productivity growth will increase at the same 1.0 percent pace that we believe has prevailed since 1998. However, the contribution of capital deepening drops off sharply this year, and we estimate that structural

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

Measure	1973-95	1996-98	1999	2000	2001	2002
Structural labor productivity	**1.4**	**2.4**	**2.8**	**2.6**	**2.1**	**1.8**
Previous	1.4	2.5	3.1	3.2	2.5	2.5
Contributions[1]						
Capital deepening	.6	1.1	1.5	1.3	.8	.5
Previous	.6	1.2	1.6	1.7	1.0	1.0
Multifactor productivity	.6	.9	1.0	1.0	1.0	1.0
Previous	.6	1.0	1.2	1.2	1.2	1.2
Labor composition	.3	.3	.3	.3	.3	.3

1. Percentage points. Components may not sum to totals because of rounding.

labor productivity will increase at an average of only about 2 percent this year and next. As for potential output, we now estimate that growth will average a little less than 3 percent this year and next, down an average of ½ percentage point from the June Greenbook.

As discussed in the recent special memo to the FOMC, our assumptions about the short-run NAIRU have changed little since the last Greenbook. However, we have moved down our estimate of the long-run NAIRU to 5¼ percent from the 5½ percent that we had previously assumed. Briefly, the post-1995 productivity acceleration now explains only a smaller part of the favorable inflation experience of that time. But because the inflation picture was not revised appreciably, other, more structural factors appear to have played a larger role in holding down inflation. For the purposes of our forecast, we reduced our long-run NAIRU assumption as a way of capturing the greater contribution of these other factors.

Productivity and the labor market. Although the second-quarter pickup in productivity growth and the upward revision to the first-quarter figure were received with considerable fanfare in many media accounts, our reading of those numbers is a bit more subdued. In particular, recent readings on labor productivity in the nonfarm business sector have been bounced around by swings in the reported data for hours worked by the self-employed. Abstracting from these swings, we think that output per hour rose at an annual rate of about 1 percent in the first half of this year, down substantially from the average rates that prevailed during the past several years. Though sizable, the amount of slowing over the past year appears to be about in line with typical cyclical behavior. We expect that, as the economy strengthens, productivity growth will

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

Measure	2000	2001	2002
Output per hour, nonfarm business	2.3	1.2	2.3
Previous	3.3	1.5	2.9
Nonfarm private payroll employment	1.8	-.4	.5
Previous	1.8	-.3	.6
Household employment survey	1.0	-.4	.5
Previous	1.0	-.4	.5
Labor force participation rate[1]	67.1	66.9	66.9
Previous	67.1	67.0	66.9
Civilian unemployment rate[1]	4.0	5.1	5.6
Previous	4.0	5.2	5.6

1. Percent, average for the fourth quarter.

pick up to a slightly faster-than-trend rate of 2¼ percent next year; by the end of next year the level of actual productivity is expected to come back into line with structural productivity.

Private payroll employment is forecast to fall about 80,000 per month through the end of the third quarter. By the autumn, the pace of decline should begin to taper off, and we project that payrolls will begin turning up around the middle of next year. However, increases are expected to be tepid as firms wait to see that the economy truly is improving. With labor demand sluggish, we anticipate that the unemployment rate will rise to 5½ percent by the end of next year.

Wages and prices. We project that the broad measures of wage and price inflation will decelerate this year and next. Falling energy prices obviously hold down price inflation directly; they also imply less upward pressure on costs, even for non-energy items, and help put a damper on inflation expectations. Resource utilization rates in both labor and product markets are expected to drop over the forecast period, which should be a restraining influence on wage and price increases. The compensation forecast has been marked down somewhat since the June Greenbook, owing in part to the lower path for structural labor productivity but also to incoming data for the second quarter that suggested lower trends going forward.

After increasing 1.9 percent this year, core PCE prices are expected to increase 1.8 percent next year. The small deceleration reflects the slack that is projected to open up in labor and product markets. The forecast for core PCE inflation

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

Measure	2000	2001	2002
PCE chain-weighted price index	2.6	1.9	1.7
Previous	2.3	2.0	1.7
Food	2.5	3.3	2.6
Previous	2.5	3.1	2.5
Energy	15.4	-2.6	-2.9
Previous	15.9	-.5	-4.4
Excluding food and energy	1.9	1.9	1.8
Previous	1.6	2.0	1.9
Consumer price index	3.4	2.5	2.1
Previous	3.4	2.6	2.0
Excluding food and energy	2.5	2.7	2.5
Previous	2.5	2.6	2.5
GDP chain-weighted price index	2.4	2.2	1.9
Previous	2.3	2.2	1.8
ECI for compensation of private industry workers[1]	4.4	4.3	3.7
Previous	4.4	4.4	3.9
NFB compensation per hour	7.4	4.9	4.5
Previous	5.7	5.4	4.8
Prices of core non-oil merchandise imports	1.6	-1.5	1.8
Previous	1.4	-.2	2.1

1. December to December.

has been revised down 0.1 percentage point for this year and next from the June Greenbook. All else equal, the lower path for structural productivity growth would have pushed up price inflation; however, that effect was offset by the change in our long-run NAIRU assumption. In addition, core import prices are expected to be a little more favorable than in our last projection.

As a result of the NIPA revision, the discrepancy between the ECI and compensation per hour in 2000 is even larger than previously reported. While the ECI rose 4.4 percent in 2000, compensation per hour is now estimated to have increased a whopping 7.4 percent. In part, we think that this gap can be explained by the different treatment of stock options in the two measures: Stock options are excluded from the ECI concept of compensation but included in the compensation per hour concept. But even after one takes account of option exercises, the increase in compensation per hour in 2000 still appears outsized. Given these complications — as well as the possibility of future revisions to last year's compensation-per-hour figure — we have not taken these data at face value. That said, we project that increases in compensation per hour — which have already slowed to a 5 percent pace in the first half of this year — will come in at a 5 percent pace for 2001 as a whole and at a 4½ percent rate next year. For the ECI, we anticipate an increase of 4¼ percent this year and 3¾ percent next year.

Financial Flows and Conditions

Debt of domestic nonfinancial sectors is projected to rise at a 3½ percent rate over the second half of this year and only a touch faster next year. Paydowns of Treasury debt will continue to hold down overall debt growth. But the restraint will probably be less than we previously thought because sluggish tax receipts and lower income projections have reduced estimates of federal surpluses this year and next. The debt of nonfederal sectors is projected to slow to a growth pace of 4½ percent on average over the second half of this year and to rise to just above 5 percent next year as the economy regains momentum. Despite the reduced pace of borrowing, the debt service burdens of households and businesses are likely to continue causing some strains.

In the household sector, low mortgage interest rates and relatively solid housing activity are expected to keep growth of home mortgage debt at a pace around 6½ percent over the projection period. Consumer credit growth, which slowed sharply over the first half of this year, should remain sluggish, especially in light of the modest rise projected for consumer durables over the forecast period. The tax rebate is expected to damp debt growth somewhat in the near term as some households use part of their rebates to pay down outstanding debt. Low interest rates and efforts by households to strengthen balance sheets will limit the rise in loan delinquencies and personal bankruptcies over time, but we would not be surprised to see some further deterioration this year accompanied by additional firming in the supply of credit from banks and other lenders.

Business debt growth slowed appreciably over the first half, as corporations slashed capital outlays, liquidated inventories, and curtailed share repurchase programs and merger activity. We expect business borrowing to remain on its lower growth path for the remainder of this year and to pick up a bit next year as investment spending recovers. The weak outlook for profits and high level of default rates, meanwhile, portend the continuation of elevated risk premiums in securities markets for lower-rated credits and perhaps some additional tightening of standards and terms by lenders. Bond issuance is expected to remain at the moderate pace of the past couple of months, which is off substantially from the record issuance earlier in the year. After declining on net thus far this year, bank loans and commercial paper together are expected to turn up next year.

Following a spurt of advance refunding activity in the first half of this year, state and local governments are expected to hold down their net security issuance over the next year and a half. Besides retiring higher-yield bonds with proceeds from earlier refunding issues, governmental units are likely to be more cautious about issuing new bonds for capital programs until budget prospects improve.

The monetary aggregates appear to be slowing from their rapid pace of growth in the first half of the year, reflecting the waning effect of several factors that had boosted growth earlier, including reductions in opportunity costs, an active pace of mortgage refinancing, and stock market volatility. We project that M2 will expand significantly faster than the rate of growth in nominal income for the remainder of this year but about in line with nominal income in 2002.

Alternative Simulations

Data revisions and other incoming information have altered not only the baseline outlook but also the risks attached to the staff projection. These revisions have cast into sharper relief the uncertainty and risks attending our supply-side assumptions. To illustrate these risks, we use model simulations to generate several alternative scenarios. We begin with two scenarios involving more-pessimistic assumptions about the future pace of technological innovation and capital deepening. The next two scenarios involve more favorable supply-side possibilities, in particular a stronger rebound in capital formation and a lower NAIRU. The fifth scenario considers the implications of taking more seriously last year's surge in compensation per hour. The sixth scenario involves the stock market — specifically a fall in the price-earnings ratio to a more historically "normal" level. In all six of these scenarios, the funds rate is assumed to follow its baseline path. But in two final simulations, we show the effects of a further monetary easing and the implications of having the funds rate evolve as anticipated by the market.

Slower pace of technological innovation. Revised data show the post-1995 acceleration in productivity as having been less pronounced, raising the possibility that the 1995-2000 pickup in the pace of technological innovation was only temporary. In this scenario, we assume that the growth rate of structural multifactor productivity reverts to ½ percent per year — the average for the 1973-95 period — compared with 1 percent in the staff outlook. The more-pessimistic assumption for structural productivity yields a weaker outlook for profits and sales and puts a damper on next year's recovery in business investment. In addition, such a worsening in long-term growth prospects would imply lower equity prices and smaller income gains than in the baseline outlook

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

Measure	2001 H1	2001 H2	2002 H1	2002 H2
Real GDP				
Baseline	**.8**	**1.3**	**2.4**	**3.0**
Slower technological innovation	.8	.9	1.3	1.9
Less capital deepening	.8	.7	.8	1.1
Stronger investment rebound	.8	1.4	2.8	3.7
Low NAIRU	.8	1.4	2.6	3.2
Compensation-led inflation	.8	1.3	2.4	3.0
P-E ratio adjustment	.8	1.2	1.9	2.1
Further monetary easing	.8	1.3	2.6	3.2
Market-based funds rate expectations	.8	1.3	2.7	3.2
Civilian unemployment rate[1]				
Baseline	**4.5**	**5.1**	**5.5**	**5.6**
Slower technological innovation	4.5	5.1	5.6	5.8
Less capital deepening	4.5	5.1	5.7	6.0
Stronger investment rebound	4.5	5.1	5.4	5.4
Low NAIRU	4.5	5.1	5.4	5.4
Compensation-led inflation	4.5	5.1	5.5	5.6
P-E ratio adjustment	4.5	5.1	5.6	5.8
Further monetary easing	4.5	5.1	5.5	5.5
Market-based funds rate expectations	4.5	5.1	5.4	5.5
PCE prices excluding food and energy				
Baseline	**1.8**	**1.9**	**1.8**	**1.8**
Slower technological innovation	1.8	1.9	1.9	2.0
Less capital deepening	1.8	1.9	1.9	2.0
Stronger investment rebound	1.8	1.9	1.8	1.8
Low NAIRU	1.8	1.8	1.6	1.4
Compensation-led inflation	1.8	2.1	2.1	2.2
P-E ratio adjustment	1.8	1.9	1.8	1.8
Further monetary easing	1.8	1.9	1.8	1.9
Market-based funds rate expectations	1.8	1.9	1.9	1.9

1. Average for the final quarter of the period.

and, hence, less household spending. Overall, aggregate spending is held down more than potential output, causing the rise in the unemployment rate to be somewhat steeper than in the staff forecast. However, inflation is slightly higher as a consequence of the greater unit labor costs implied by smaller structural productivity gains.

Less capital deepening. High-tech investment has fallen sharply since its peak late last year. Going forward, the staff's baseline forecast anticipates a resumption of moderate growth next year. However, there is a risk that the recovery in high-tech spending may not materialize. In this scenario, we illustrate the risk by assuming that the slower pace of technological innovation in the first scenario is compounded by continued weakness in high-tech investment, returning its GDP share to the late 1997 level. As a result, growth in structural labor productivity falls to only about 1 percent by the second half of next year, compared with a little less than 2 percent in the staff forecast. The direct effects of weaker business spending, coupled with the indirect demand effects of slower productivity growth, hold the rise in real GDP to only 1 percent in 2002 and push the unemployment rate to 6 percent by the end of next year. Even so, inflation drifts up modestly, reflecting the adverse influence of slower structural productivity growth on unit labor costs.

Stronger investment rebound. While the preceding scenario highlights the downside possibilities attached to the investment outlook, there is also a risk of a more-pronounced rebound in high-tech spending. In this scenario, we assume that high-tech outlays as a share of nominal GDP return to their late 2000 peak by the end of next year, thereby yielding considerably more capital deepening. This more-optimistic assumption adds about ½ percentage point to GDP growth next year and restrains somewhat the rise in the unemployment rate. Inflation is about the same as in the baseline because the recovery in investment produces roughly as much aggregate supply as it does demand.

Low NAIRU. As noted above, we have revised our estimates of the long-run NAIRU. This shading in our view underscores the uncertainties regarding the causes of the simultaneous decline in inflation and unemployment in the latter half of the 1990s. With these uncertainties in mind, we consider the possibility that the NAIRU is substantially lower than the one we built into the forecast. Specifically, as we have done in alternative simulations in previous Greenbooks, we assume that the NAIRU fell gradually, but permanently, to 4 percent during the mid-1990s. In addition to holding down inflation, the lower NAIRU also moderately boosts the estimated level of potential output. With the nominal funds rate held fixed, falling inflation implies a rise in the real rate relative to baseline; this increase tempers the near-term pickup in output and employment.

Compensation-led inflation. The previous scenario explored the possibility of lower inflation going forward, but the projection also has some upside risk. In particular, we have discounted the compensation data, which, if taken literally, would suggest more upward pressure on profit margins and prices. In this scenario, we consider the possibility that these data should be taken at face value and adjust the forecast so that it incorporates a straight translation of the historical revisions to compensation per hour into inflation, based on the

FRB/US wage-price equations. Doing so adds 0.4 percentage point to core PCE inflation by the second half of next year. However, the outlook for real activity would be little altered.

P-E ratio adjustment. The recent NIPA revisions caused us to be less optimistic about the outlook for potential growth. This change to the forcast raises the risk that the gap between the staff's estimate of long-run earnings growth and the estimate implicitly held by investors has increased; alternatively, the implicit premium on holding equity may be lower than we had previously thought. Either way, the chance of a substantial correction in equity prices may be higher now than before. A gradual decline in equity prices sufficient to return the price-earnings ratio for the S&P 500 from its current high reading of 26 to a level of 18, which is more in line with historical experience, by the end of next year would substantially reduce household wealth and restrain consumer spending. As a result, real GDP growth would average only 2 percent in 2002, and the unemployment rate would rise more than in the baseline.

Lower funds rate. The Greenbook assumes that the federal funds rate remains at its current level. In this scenario, we assume that the funds rate is reduced 25 basis points at the August meeting and remains at 3½ percent thereafter. This modest easing in monetary policy adds 0.2 percentage point to growth next year and shaves 0.1 percentage point from the rise in the unemployment rate, at the cost of a small increase in inflation.

Market-based funds rate. According to futures quotes, the market anticipates that the federal funds rate will fall about another 50 basis points by the first quarter of next year and then climb above 4 percent late next year and further in 2003. Although this profile for the funds rate does not differ substantially, on average, from that incorporated into the Greenbook, the funds rate is lower in the near term. Given the lagged impact of monetary policy, the easier policy in the near term pushes up GDP growth about ¼ percentage point next year and results in slightly higher inflation in 2002.

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Class II FOMC

August 16, 2001

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]	
		06/20/01	08/16/01	06/20/01	08/16/01	06/20/01	08/16/01	06/20/01	08/16/01	06/20/01	08/16/01
ANNUAL											
1998		5.7	5.6	4.4	4.3	1.3	1.2	1.6	1.6	4.5	4.5
1999		5.8	5.5	4.2	4.1	1.5	1.4	2.2	2.2	4.2	4.2
2000		7.1	6.5	5.0	4.1	2.1	2.3	3.4	3.4	4.0	4.0
2001		3.9	3.7	1.6	1.5	2.3	2.2	3.0	3.0	4.7	4.6
2002		4.6	3.9	2.8	2.0	1.7	1.9	1.9	2.0	5.5	5.5
QUARTERLY											
1999	Q1	5.9	4.9	3.5	3.1	2.2	1.7	1.7	1.7	4.3	4.3
	Q2	3.9	3.0	2.5	1.7	1.4	1.4	2.7	2.7	4.3	4.3
	Q3	6.7	6.1	5.7	4.7	1.1	1.4	2.9	2.9	4.2	4.2
	Q4	9.7	10.0	8.3	8.3	1.6	1.8	3.1	3.1	4.1	4.1
2000	Q1	8.3	6.3	4.8	2.3	3.3	3.8	4.3	4.3	4.1	4.1
	Q2	8.2	8.0	5.6	5.7	2.4	2.1	2.8	2.8	4.0	4.0
	Q3	3.8	3.3	2.2	1.3	1.6	1.9	3.5	3.5	4.0	4.0
	Q4	3.0	3.7	1.0	1.9	2.0	1.8	3.0	3.0	4.0	4.0
2001	Q1	4.6	4.6	1.2	1.3	3.2	3.3	4.2	4.2	4.2	4.2
	Q2	3.5	2.5	0.6	0.2	2.9	2.2	2.9	3.0	4.5	4.5
	Q3	2.5	2.5	1.3	1.0	1.3	1.5	1.5	0.5	4.9	4.7
	Q4	4.2	3.3	2.9	1.5	1.3	1.8	1.6	2.1	5.2	5.1
2002	Q1	5.2	4.7	3.2	2.4	1.9	2.2	1.8	2.1	5.4	5.3
	Q2	4.9	4.2	3.2	2.4	1.7	1.7	1.9	2.1	5.5	5.5
	Q3	5.6	4.7	3.7	2.9	1.8	1.8	2.1	2.1	5.6	5.6
	Q4	5.7	4.8	3.8	3.0	1.8	1.8	2.1	2.2	5.6	5.6
TWO-QUARTER[3]											
1999	Q2	4.9	4.0	3.0	2.4	1.8	1.5	2.2	2.2	-0.1	-0.1
	Q4	8.2	8.0	7.0	6.5	1.3	1.6	3.0	3.0	-0.2	-0.2
2000	Q2	8.2	7.2	5.2	4.0	2.8	2.9	3.6	3.6	-0.1	-0.1
	Q4	3.4	3.5	1.6	1.6	1.8	1.8	3.2	3.2	0.0	0.0
2001	Q2	4.1	3.5	0.9	0.8	3.1	2.7	3.6	3.6	0.5	0.5
	Q4	3.4	2.9	2.1	1.3	1.3	1.6	1.6	1.3	0.7	0.6
2002	Q2	5.1	4.4	3.2	2.4	1.8	2.0	1.9	2.1	0.3	0.4
	Q4	5.6	4.8	3.7	3.0	1.8	1.8	2.1	2.1	0.1	0.1
FOUR-QUARTER[4]											
1998	Q4	5.9	6.0	4.6	4.8	1.2	1.1	1.5	1.5	-0.3	-0.3
1999	Q4	6.5	6.0	5.0	4.4	1.6	1.6	2.6	2.6	-0.3	-0.3
2000	Q4	5.8	5.3	3.4	2.8	2.3	2.4	3.4	3.4	-0.1	-0.1
2001	Q4	3.7	3.2	1.5	1.0	2.2	2.2	2.6	2.5	1.2	1.1
2002	Q4	5.3	4.6	3.5	2.7	1.8	1.9	2.0	2.1	0.4	0.5

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)

August 16, 2001

Item	Units[1]	1994	1995	1996	1997	1998	1999	2000	----Projected---- 2001	2002
EXPENDITURES										
Nominal GDP	Bill. $	7054.3	7400.5	7813.2	8318.4	8781.5	9268.6	9872.9	10240.8	10643.5
Real GDP	Bill. Ch. $	7347.7	7543.8	7813.2	8159.5	8508.9	8856.5	9224.0	9359.1	9549.5
Real GDP	% change	4.1	2.2	4.1	4.3	4.8	4.4	2.8	1.0	2.7
Gross domestic purchases		4.3	1.7	4.3	5.0	5.8	5.3	3.5	1.0	3.1
Final sales		3.2	2.9	3.9	3.9	4.7	4.3	3.4	1.8	2.2
Priv. dom. final purchases		4.3	3.2	4.4	5.1	6.3	5.4	4.7	1.3	2.4
Personal cons. expenditures		3.6	2.8	3.1	4.1	5.0	5.2	4.2	2.9	2.2
Durables		6.4	3.7	5.0	8.8	12.7	11.3	5.3	4.5	4.3
Nondurables		4.1	2.5	3.2	2.5	5.0	5.0	3.6	2.6	1.4
Services		2.7	2.7	2.7	3.9	3.6	4.0	4.3	2.7	2.2
Business fixed investment		9.2	7.5	12.1	11.8	12.3	7.4	8.9	-7.5	4.0
Equipment & Software		12.0	8.9	11.8	13.7	14.9	11.2	8.3	-9.0	5.5
Nonres. structures		1.1	3.3	12.8	6.5	4.9	-3.6	10.8	-3.2	0.0
Residential structures		4.0	-1.5	5.6	3.5	10.0	3.4	-1.2	3.1	1.3
Exports		10.5	9.7	9.8	8.5	2.3	4.5	7.0	-3.3	3.9
Imports		12.2	5.0	11.2	14.3	10.8	11.5	11.3	-2.3	6.4
Gov't. cons. & investment		0.2	-0.8	2.7	2.4	2.7	4.0	1.2	3.9	3.3
Federal		-3.7	-5.3	2.0	0.1	0.6	4.5	-1.4	3.2	2.9
Defense		-5.9	-4.7	0.8	-1.4	-0.8	4.7	-2.2	3.7	2.3
State & local		2.8	2.1	3.0	3.7	3.8	3.7	2.5	4.3	3.5
Change in bus. inventories	Bill. Ch. $	--	--	--	63.8	76.7	62.1	50.6	-32.1	14.4
Nonfarm		--	41.9	21.2	60.6	75.0	63.5	52.3	-30.6	14.3
Net exports		-86.5	-78.4	-89.0	-113.3	-221.1	-316.9	-399.1	-413.1	-465.5
Nominal GDP	% change	6.2	4.3	6.0	6.2	6.0	6.0	5.3	3.2	4.6
EMPLOYMENT AND PRODUCTION										
Nonfarm payroll employment	Millions	114.1	117.2	119.6	122.7	125.8	128.9	131.8	132.4	132.6
Unemployment rate	%	6.1	5.6	5.4	4.9	4.5	4.2	4.0	4.6	5.5
Industrial prod. index	% change	6.3	3.6	5.6	7.2	3.2	5.1	4.2	-4.5	2.7
Capacity util. rate - mfg.	%	82.5	82.5	81.6	82.7	81.3	80.5	81.3	75.9	74.7
Housing starts	Millions	1.46	1.35	1.48	1.47	1.62	1.64	1.57	1.63	1.65
Light motor vehicle sales		15.01	14.77	15.05	15.06	15.43	16.78	17.25	16.23	15.38
North Amer. produced		12.88	12.87	13.34	13.12	13.41	14.30	14.39	13.27	12.52
Other		2.13	1.90	1.70	1.93	2.02	2.48	2.86	2.95	2.86
INCOME AND SAVING										
Nominal GNP	Bill. $	7071.1	7420.9	7831.2	8325.4	8778.1	9261.8	9860.8	10232.2	10624.2
Nominal GNP	% change	6.2	4.4	5.9	6.0	5.8	6.0	5.4	3.0	4.5
Nominal personal income		5.1	4.3	5.9	6.3	6.7	4.8	7.3	3.8	4.5
Real disposable income		2.9	1.7	2.6	3.8	5.0	2.1	4.0	2.2	3.7
Personal saving rate	%	6.1	5.6	4.8	4.2	4.7	2.4	1.0	1.4	2.1
Corp. profits, IVA & CCAdj.	% change	12.3	11.3	11.4	9.9	-9.6	11.3	-1.2	-12.9	0.7
Profit share of GNP	%	8.1	9.0	9.6	10.0	8.9	8.9	8.9	7.3	7.0
Excluding FR Banks		7.9	8.7	9.4	9.7	8.6	8.6	8.6	7.0	6.7
Federal surpl./deficit	Bill. $	-212.3	-192.0	-136.8	-53.3	43.8	119.2	218.6	150.7	97.6
State & local surpl./def.		8.6	15.3	21.4	31.0	40.7	42.1	32.8	16.9	16.3
Ex. social ins. funds		4.0	11.4	18.7	29.9	40.0	41.7	33.1	17.2	16.6
Gross natl. saving rate	%	16.3	16.9	17.2	18.0	18.8	18.4	18.1	16.8	16.7
Net natl. saving rate		4.3	5.1	5.7	6.7	7.5	6.8	6.3	4.4	4.2
PRICES AND COSTS										
GDP chn.-wt. price index	% change	2.1	2.1	1.9	1.8	1.1	1.6	2.4	2.2	1.9
Gross Domestic Purchases chn.-wt. price index		2.1	2.1	1.9	1.4	0.8	1.9	2.5	1.7	1.8
PCE chn.-wt. price index		2.1	2.1	2.3	1.5	1.1	2.0	2.6	1.9	1.7
Ex. food and energy		2.3	2.3	1.8	1.7	1.6	1.5	1.9	1.9	1.8
CPI		2.6	2.7	3.2	1.9	1.5	2.6	3.4	2.5	2.1
Ex. food and energy		2.8	3.0	2.6	2.2	2.4	2.0	2.5	2.7	2.5
ECI, hourly compensation[2]		3.1	2.6	3.1	3.4	3.5	3.4	4.4	4.3	3.7
Nonfarm business sector										
Output per hour		1.1	1.1	2.3	2.3	2.9	2.8	2.3	1.2	2.3
Compensation per Hour		2.2	2.6	3.2	3.5	5.3	4.3	7.4	4.9	4.5
Unit labor cost		1.0	1.5	0.9	1.1	2.3	1.5	5.0	3.7	2.2

1. Changes are from fourth quarter to fourth quarter.
2. Private-industry workers.

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Class II FOMC

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

August 16, 2001

Item	Units	1998 Q1	1998 Q2	1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2
EXPENDITURES											
Nominal GDP	Bill. $	8627.8	8697.3	8816.5	8984.5	9093.1	9161.4	9297.4	9522.5	9668.7	9857.6
Real GDP	Bill. Ch. $	8396.3	8442.9	8528.5	8667.9	8733.5	8771.2	8871.5	9049.9	9102.5	9229.4
Real GDP	% change	6.1	2.2	4.1	6.7	3.1	1.7	4.7	8.3	2.3	5.7
Gross domestic purchases		7.9	4.0	4.8	6.4	4.8	2.9	5.3	8.2	3.5	6.3
Final sales		4.0	5.4	2.8	6.5	3.0	3.9	4.2	6.1	4.8	3.9
Priv. dom. final purchases		7.7	7.2	3.8	6.6	5.3	5.9	4.9	5.5	7.5	4.6
Personal cons. expenditures		5.1	6.2	3.8	5.1	4.9	5.7	4.4	5.7	5.9	3.6
Durables		7.0	16.6	4.2	24.0	7.1	15.7	9.0	13.7	19.0	-2.5
Nondurables		5.6	6.0	3.2	5.2	5.6	4.3	2.6	7.6	5.1	4.7
Services		4.5	4.3	4.1	1.5	4.1	4.5	4.3	3.2	3.7	4.4
Business fixed investment		21.6	12.5	1.5	14.4	6.0	7.7	10.2	5.8	15.8	12.2
Equipment & Software		28.0	11.6	3.0	18.4	10.5	11.9	16.2	6.4	18.1	12.4
Nonres. structures		4.9	14.9	-2.7	3.3	-6.5	-4.3	-7.0	4.0	8.8	11.8
Residential structures		10.4	9.2	11.1	9.3	10.3	3.0	-0.8	1.6	8.5	-0.8
Exports		0.5	-4.0	-2.2	16.3	-6.8	4.2	9.7	12.1	9.0	13.5
Imports		15.9	11.3	4.2	12.2	8.4	13.3	13.8	10.5	17.1	16.4
Gov't. cons. & investment		-2.5	7.5	2.0	4.1	2.0	1.2	4.4	8.5	-1.1	4.4
Federal		-9.7	12.2	-3.9	5.3	-3.7	0.8	7.2	14.5	-12.8	15.9
Defense		-17.6	12.6	5.3	-0.8	-3.5	-3.5	12.8	14.3	-20.0	15.4
State & local		1.7	5.0	5.3	3.4	5.2	1.4	2.9	5.4	5.6	-1.1
Change in bus. inventories	Bill. Ch. $	113.1	42.0	71.8	80.0	83.4	32.7	39.6	92.7	28.9	78.9
Nonfarm		106.7	47.4	70.8	75.1	78.7	34.2	52.2	88.7	37.8	75.1
Net exports		-180.8	-223.1	-241.2	-239.2	-283.0	-313.4	-333.3	-337.8	-371.1	-392.8
Nominal GDP	% change	7.2	3.3	5.6	7.8	4.9	3.0	6.1	10.0	6.3	8.0
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	124.7	125.5	126.2	127.0	127.8	128.5	129.2	130.1	131.0	131.9
Unemployment rate	%	4.7	4.4	4.5	4.4	4.3	4.3	4.2	4.1	4.1	4.0
Industrial prod. index	% change	3.6	3.0	3.4	2.9	3.9	4.9	5.8	5.7	6.7	7.9
Capacity util. rate - mfg.	%	82.4	81.5	80.8	80.5	80.2	80.3	80.5	80.9	81.3	81.9
Housing starts	Millions	1.56	1.57	1.63	1.72	1.71	1.57	1.65	1.65	1.67	1.59
Light motor vehicle sales		14.88	16.03	14.58	16.23	16.17	16.76	17.06	17.11	18.13	17.27
North Amer. produced		12.96	14.07	12.55	14.06	13.87	14.32	14.58	14.41	15.25	14.40
Other		1.92	1.96	2.02	2.17	2.30	2.44	2.47	2.70	2.87	2.87
INCOME AND SAVING											
Nominal GNP	Bill. $	8634.5	8700.3	8802.1	8975.4	9089.5	9157.0	9283.8	9517.0	9650.7	9841.0
Nominal GNP	% change	7.5	3.1	4.8	8.1	5.2	3.0	5.7	10.4	5.7	8.1
Nominal personal income		9.1	7.2	6.0	4.6	3.0	4.7	5.2	6.3	8.6	8.5
Real disposable income		8.1	6.0	3.7	2.4	1.4	2.0	2.1	3.0	3.3	5.9
Personal saving rate	%	4.9	4.9	4.9	4.3	3.5	2.7	2.1	1.4	0.8	1.3
Corp. profits, IVA & CCAdj.	% change	-27.3	-8.7	6.5	-5.6	36.1	-10.2	-4.9	31.9	6.1	10.7
Profit share of GNP	%	9.1	8.8	8.9	8.6	9.2	8.8	8.6	9.0	9.0	9.1
Excluding FR Banks		8.8	8.6	8.6	8.3	8.9	8.6	8.3	8.7	8.7	8.8
Federal surpl./deficit	Bill. $	19.6	33.0	65.7	57.0	85.2	116.5	132.0	143.1	212.8	209.1
State & local surpl./def.		36.7	32.0	35.6	58.4	48.9	36.2	38.3	44.9	33.2	34.7
Ex. social ins. funds		36.0	31.3	34.9	57.9	48.4	35.8	38.0	44.7	33.3	34.9
Gross natl. saving rate	%	18.6	18.6	19.1	18.7	19.0	18.5	18.3	18.0	18.0	18.3
Net natl. saving rate		7.4	7.3	7.8	7.4	7.6	6.9	6.4	6.3	6.3	6.6
PRICES AND COSTS											
GDP chn.-wt. price index	% change	1.1	1.0	1.4	1.1	1.7	1.4	1.4	1.8	3.8	2.1
Gross Domestic Purchases chn.-wt. price index		0.1	0.7	1.1	1.2	1.5	2.0	2.0	2.2	4.2	1.9
PCE chn.-wt. price index		0.6	1.0	1.4	1.4	1.3	2.0	2.2	2.4	4.0	2.1
Ex. food and energy		1.6	1.7	1.6	1.5	1.4	1.2	1.5	1.8	2.9	1.7
CPI		1.0	1.2	1.7	2.0	1.7	2.7	2.9	3.1	4.3	2.8
Ex. food and energy		2.6	2.1	2.3	2.3	1.8	2.1	1.8	2.5	2.5	2.7
ECI, hourly compensation[1]		3.0	3.3	4.4	2.6	1.4	4.6	3.4	4.6	5.6	4.7
Nonfarm business sector											
Output per hour		4.7	0.5	2.2	4.5	2.4	-1.4	3.0	7.4	-0.6	6.3
Compensation per hour		6.8	5.6	5.0	4.0	3.8	4.2	5.2	4.2	6.2	7.6
Unit labor cost		2.0	5.1	2.7	-0.4	1.3	5.6	2.1	-2.9	6.8	1.2

1. Private-industry workers.

Strictly Confidential <FR>
Class II FOMC

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

August 16, 2001

					- - - - - - - - - Projected - - - - - - - - - - - - - - - - - - -						
Item	Units	2000 Q3	2000 Q4	2001 Q1	2001 Q2	2001 Q3	2001 Q4	2002 Q1	2002 Q2	2002 Q3	2002 Q4
EXPENDITURES											
Nominal GDP	Bill. $	9937.5	10027.9	10141.7	10203.8	10267.1	10350.7	10469.1	10577.1	10700.3	10827.5
Real GDP	Bill. Ch. $	9260.1	9303.9	9334.5	9339.8	9363.7	9398.3	9454.8	9511.2	9580.1	9651.8
Real GDP	% change	1.3	1.9	1.3	0.2	1.0	1.5	2.4	2.4	2.9	3.0
Gross domestic purchases		2.0	2.2	0.7	0.4	1.4	1.6	3.1	3.0	3.3	2.8
Final sales		2.3	2.4	4.0	0.6	0.5	2.2	0.9	1.7	2.8	3.3
Priv. dom. final purchases		3.9	2.6	2.8	-0.2	0.6	2.1	1.4	2.1	3.1	3.0
Personal cons. expenditures		4.3	3.1	3.0	2.1	2.9	3.4	1.7	1.8	2.8	2.6
Durables		8.2	-2.1	10.6	5.9	0.4	1.2	2.3	3.4	6.4	4.9
Nondurables		4.2	0.6	2.4	0.3	4.1	3.5	1.2	1.4	1.7	1.6
Services		3.5	5.6	1.8	2.3	2.8	3.8	1.7	1.7	2.6	2.6
Business fixed investment		7.1	1.0	-0.2	-13.4	-11.2	-4.6	0.3	4.1	5.8	5.8
Equipment & Software		4.7	-1.1	-4.1	-13.2	-12.8	-5.3	0.8	5.6	7.9	8.0
Nonres. structures		15.2	7.6	12.3	-13.7	-6.7	-2.8	-0.8	0.3	0.4	0.1
Residential structures		-10.4	-1.1	8.5	4.8	-0.2	-0.5	-0.5	1.7	1.8	2.0
Exports		10.6	-4.0	-1.2	-10.5	-3.7	2.8	-0.3	3.3	4.5	8.4
Imports		13.0	-0.5	-5.0	-6.9	-0.2	3.1	5.4	7.8	7.2	5.4
Gov't. cons. & investment		-1.8	3.3	5.3	5.4	2.0	2.9	2.7	3.4	3.5	3.6
Federal		-10.4	4.6	3.2	1.6	3.4	4.6	1.8	3.3	3.2	3.2
Defense		-10.4	10.5	7.5	1.9	2.8	2.6	2.7	2.2	2.1	2.1
State & local		3.0	2.7	6.4	7.4	1.3	2.1	3.1	3.5	3.6	3.7
Change in bus. inventories	Bill. Ch. $	51.7	42.8	-27.1	-37.2	-23.8	-40.4	-0.4	18.6	23.0	16.3
Nonfarm		56.6	39.7	-27.3	-35.2	-21.2	-38.5	1.1	18.1	22.4	15.7
Net exports		-411.2	-421.1	-404.5	-408.3	-417.9	-421.9	-443.0	-463.4	-478.6	-476.8
Nominal GDP	% change	3.3	3.7	4.6	2.5	2.5	3.3	4.7	4.2	4.7	4.8
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	131.9	132.3	132.6	132.5	132.3	132.2	132.2	132.4	132.7	133.0
Unemployment rate	%	4.0	4.0	4.2	4.5	4.7	5.1	5.3	5.5	5.6	5.6
Industrial prod. index	% change	3.5	-0.9	-6.8	-4.2	-4.6	-2.5	1.5	2.9	3.4	3.2
Capacity util. rate - mfg.	%	81.7	80.3	77.9	76.4	75.1	74.2	74.2	74.4	74.8	75.2
Housing starts	Millions	1.51	1.54	1.63	1.62	1.64	1.64	1.64	1.65	1.65	1.66
Light motor vehicle sales		17.30	16.32	16.89	16.65	15.98	15.38	15.29	15.29	15.46	15.46
North Amer. produced		14.47	13.45	13.96	13.62	13.03	12.49	12.42	12.42	12.61	12.61
Other		2.83	2.87	2.93	3.03	2.96	2.89	2.87	2.87	2.85	2.85
INCOME AND SAVING											
Nominal GNP	Bill. $	9919.4	10032.1	10131.3	10202.6	10257.3	10337.4	10453.4	10558.1	10679.6	10805.9
Nominal GNP	% change	3.2	4.6	4.0	2.8	2.2	3.2	4.6	4.1	4.7	4.8
Nominal personal income		5.5	6.8	5.8	3.5	2.8	3.2	4.9	4.1	4.4	4.5
Real disposable income		2.7	4.2	2.7	2.2	10.6	-5.9	8.2	2.1	2.4	2.4
Personal saving rate	%	0.8	1.0	1.1	1.1	2.9	0.6	2.1	2.2	2.1	2.1
Corp. profits, IVA & CCAdj.	% change	1.0	-19.6	-24.6	-23.7	-9.3	10.0	2.3	-1.0	-1.5	3.0
Profit share of GNP	%	9.0	8.4	7.8	7.2	7.0	7.1	7.1	7.0	6.9	6.9
Excluding FR Banks		8.7	8.1	7.5	6.9	6.7	6.8	6.8	6.7	6.6	6.6
Federal surpl./deficit	Bill. $	229.9	222.5	205.3	176.3	46.4	174.8	85.1	94.2	106.2	104.8
State & local surpl./def.		34.8	28.6	22.3	17.2	11.7	16.4	18.6	15.7	15.2	15.8
Ex. social ins. funds		35.1	29.1	22.6	17.4	12.1	16.8	18.9	16.0	15.5	16.1
Gross natl. saving rate	%	18.2	17.9	17.3	16.9	16.7	16.3	16.6	16.7	16.8	16.8
Net natl. saving rate		6.4	6.0	5.1	4.4	4.2	3.8	4.1	4.2	4.2	4.2
PRICES AND COSTS											
GDP chn.-wt. price index	% change	1.9	1.8	3.3	2.2	1.5	1.8	2.2	1.7	1.8	1.8
Gross Domestic Purchases chn.-wt. price index		2.3	1.7	2.7	1.5	1.0	1.8	2.1	1.7	1.7	1.7
PCE chn.-wt. price index		2.4	2.0	3.2	1.7	0.7	1.8	1.7	1.7	1.7	1.7
Ex. food and energy		1.6	1.5	2.6	1.1	1.9	1.9	1.9	1.8	1.8	1.8
CPI		3.5	3.0	4.2	3.0	0.5	2.1	2.1	2.1	2.1	2.2
Ex. food and energy		2.5	2.4	3.1	2.6	2.5	2.6	2.6	2.5	2.5	2.5
ECI, hourly compensation[1]		3.8	3.5	4.6	4.0	4.3	4.1	3.9	3.8	3.7	3.7
onfarm business sector											
Output per hour		1.4	2.3	0.1	1.9	1.2	1.8	2.4	2.2	2.2	2.3
Compensation per hour		7.1	8.9	5.1	4.8	5.0	4.9	4.7	4.5	4.4	4.4
Unit labor cost		5.6	6.4	5.0	2.9	3.8	3.1	2.4	2.3	2.2	2.0

1. Private-industry workers.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2	2000 Q3	98Q4/ 97Q4	99Q4/ 98Q4	0Q4/ 99Q4
Real GDP	4.1	6.7	3.1	1.7	4.7	8.3	2.3	5.7	1.3	4.8	4.4	2.8
Gross dom. purchases	4.9	6.5	4.9	2.9	5.4	8.4	3.6	6.5	2.0	5.9	5.4	3.6
Final sales	2.8	6.4	2.9	3.9	4.2	6.2	4.7	3.9	2.3	4.6	4.2	3.3
Priv. dom. final purchases	3.2	5.5	4.4	4.8	4.2	4.8	6.2	4.0	3.3	5.2	4.5	3.9
Personal cons. expenditures	2.6	3.4	3.2	3.8	3.0	4.0	3.9	2.5	2.9	3.4	3.5	2.9
Durables	0.3	1.7	0.6	1.2	0.7	1.1	1.5	-0.2	0.7	1.0	0.9	0.4
Nondurables	0.6	1.0	1.1	0.8	0.5	1.5	1.0	1.0	0.8	1.0	1.0	0.7
Services	1.6	0.7	1.6	1.8	1.7	1.4	1.5	1.8	1.4	1.4	1.6	1.7
Business fixed investment	0.2	1.7	0.7	0.9	1.3	0.8	1.9	1.5	0.9	1.5	0.9	1.1
Equipment & Software	0.3	1.6	0.9	1.1	1.5	0.6	1.6	1.2	0.5	1.3	1.0	0.8
Nonres. structures	-0.1	0.1	-0.2	-0.1	-0.2	0.1	0.3	0.4	0.5	0.2	-0.1	0.3
Residential structures	0.4	0.4	0.4	0.1	-0.0	0.1	0.4	-0.0	-0.5	0.4	0.1	-0.1
Net exports	-0.8	0.2	-1.8	-1.2	-0.8	-0.2	-1.3	-0.8	-0.7	-1.1	-1.0	-0.8
Exports	-0.2	1.7	-0.8	0.4	1.0	1.3	1.0	1.4	1.1	0.3	0.5	0.8
Imports	-0.5	-1.5	-1.0	-1.6	-1.8	-1.4	-2.3	-2.3	-1.8	-1.3	-1.5	-1.6
Government cons. & invest.	0.4	0.7	0.4	0.2	0.8	1.5	-0.2	0.8	-0.3	0.5	0.7	0.2
Federal	-0.2	0.3	-0.2	0.1	0.4	0.9	-0.8	0.9	-0.7	0.0	0.3	-0.1
Defense	0.2	-0.0	-0.1	-0.1	0.5	0.6	-0.9	0.6	-0.4	-0.0	0.2	-0.1
Nondefense	-0.5	0.4	-0.1	0.2	-0.1	0.3	0.0	0.3	-0.2	0.1	0.1	0.0
State and local	0.6	0.4	0.6	0.2	0.3	0.7	0.6	-0.1	0.3	0.4	0.4	0.3
Change in bus. inventories	1.3	0.3	0.1	-2.1	0.4	2.2	-2.3	1.8	-1.0	0.2	0.2	-0.5
Nonfarm	1.1	0.1	0.2	-1.9	0.9	1.5	-2.0	1.5	-0.8	0.2	0.1	-0.5
Farm	0.2	0.2	-0.0	-0.2	-0.4	0.6	-0.3	0.3	-0.2	-0.0	0.0	-0.0

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

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	2000 Q4	2001 Q1	2001 Q2	2001 Q3	2001 Q4	2002 Q1	2002 Q2	2002 Q3	2002 Q4	00Q4/ 99Q4	01Q4/ 00Q4	02Q4/ 01Q4
Real GDP	1.9	1.3	0.2	1.0	1.5	2.4	2.4	2.9	3.0	2.8	1.0	2.7
Gross dom. purchases	2.3	0.7	0.4	1.4	1.6	3.2	3.1	3.5	2.9	3.6	1.0	3.2
Final sales	2.4	3.9	0.6	0.5	2.2	0.9	1.7	2.8	3.3	3.3	1.8	2.2
Priv. dom. final purchases	2.2	2.4	-0.2	0.5	1.8	1.2	1.8	2.7	2.5	3.9	1.1	2.0
Personal cons. expenditures	2.1	2.1	1.4	2.0	2.3	1.2	1.3	1.9	1.8	2.9	2.0	1.5
Durables	-0.2	0.8	0.5	0.0	0.1	0.2	0.3	0.5	0.4	0.4	0.4	0.3
Nondurables	0.1	0.5	0.1	0.8	0.7	0.2	0.3	0.3	0.3	0.7	0.5	0.3
Services	2.2	0.7	0.9	1.1	1.5	0.7	0.7	1.1	1.1	1.7	1.1	0.9
Business fixed investment	0.1	-0.0	-1.8	-1.5	-0.6	0.0	0.5	0.7	0.7	1.1	-1.0	0.5
Equipment & Software	-0.1	-0.4	-1.3	-1.2	-0.5	0.1	0.5	0.6	0.7	0.8	-0.9	0.5
Nonres. structures	0.2	0.4	-0.5	-0.2	-0.1	-0.0	0.0	0.0	0.0	0.3	-0.1	0.0
Residential structures	-0.1	0.4	0.2	-0.0	-0.0	-0.0	0.1	0.1	0.1	-0.1	0.1	0.1
Net exports	-0.4	0.6	-0.2	-0.4	-0.1	-0.8	-0.7	-0.5	0.1	-0.8	-0.0	-0.5
Exports	-0.5	-0.1	-1.2	-0.4	0.3	-0.0	0.3	0.5	0.8	0.8	-0.4	0.4
Imports	0.1	0.8	1.0	0.0	-0.4	-0.7	-1.0	-1.0	-0.8	-1.6	0.3	-0.9
Government cons. & invest.	0.6	0.9	0.9	0.4	0.5	0.5	0.6	0.6	0.7	0.2	0.7	0.6
Federal	0.3	0.2	0.1	0.2	0.3	0.1	0.2	0.2	0.2	-0.1	0.2	0.2
Defense	0.4	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1	-0.1	0.1	0.1
Nondefense	-0.1	-0.1	0.0	0.1	0.2	0.0	0.1	0.1	0.1	0.0	0.0	0.1
State and local	0.3	0.7	0.9	0.2	0.3	0.4	0.4	0.4	0.5	0.3	0.5	0.4
Change in bus. inventories	-0.5	-2.6	-0.4	0.5	-0.7	1.5	0.7	0.2	-0.2	-0.5	-0.8	0.5
Nonfarm	-0.7	-2.6	-0.3	0.6	-0.7	1.5	0.7	0.2	-0.2	-0.5	-0.8	0.5
Farm	0.2	0.0	-0.1	-0.0	-0.0	-0.0	0.1	-0.0	-0.0	-0.0	-0.0	0.0

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

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

Item	Fiscal year[1]				2000				2001				2002			
	1999[a]	2000[a]	2001	2002	Q1[a]	Q2[a]	Q3[a]	Q4[a]	Q1[a]	Q2[a]	Q3	Q4	Q1	Q2	Q3	Q4
Unified budget					Not seasonally adjusted											
Receipts[2]	1827	2025	2007	2108	434	656	492	461	460	660	426	501	440	663	504	481
Outlays[2]	1703	1789	1851	1941	449	444	431	464	482	467	439	494	486	483	477	511
Surplus/deficit[2]	125	236	156	167	-15	212	60	-2	-22	194	-13	7	-47	180	27	-31
On-budget	1	87	-11	-7	-44	148	46	-13	-88	119	-29	-45	-76	105	9	-87
Off-budget	124	150	168	174	29	64	14	11	65	75	17	52	29	75	18	57
Surplus excluding deposit insurance	119	233	154	165	-18	211	60	-3	-23	193	-13	7	-47	179	27	-31
Means of financing																
Borrowing	-89	-223	-111	-130	-27	-190	-54	-25	24	-157	47	2	36	-135	-32	24
Cash decrease	-18	4	8	0	39	-13	5	32	-7	-15	-1	15	10	-40	15	20
Other[3]	-18	-18	-52	-37	4	-10	-12	-4	6	-21	-33	-23	0	-4	-10	-14
Cash operating balance, end of period	56	53	45	45	45	57	53	21	28	44	45	30	20	60	45	25
NIPA federal sector					Seasonally adjusted annual rates											
Receipts	1836	2012	2046	2069	2003	2043	2064	2078	2087	2080	1938	2097	2037	2058	2082	2109
Expenditures	1738	1813	1882	1953	1790	1833	1834	1855	1882	1900	1891	1923	1952	1964	1976	2004
Consumption expenditures	463	492	507	537	483	504	494	494	508	511	515	523	537	542	547	553
Defense	306	322	337	353	314	327	321	325	338	341	342	345	354	356	359	361
Nondefense	157	170	171	184	170	176	173	169	169	171	173	178	183	186	189	192
Other spending	1275	1321	1375	1416	1307	1330	1341	1361	1375	1388	1376	1400	1415	1422	1428	1451
Current account surplus	98	199	164	115	213	209	230	223	205	180	47	175	85	94	107	105
Gross investment	91	96	99	105	95	97	94	100	98	99	101	103	104	105	107	108
Current and capital account surplus	7	102	64	11	118	112	136	122	108	81	-55	72	-19	-11	-0	-3
Fiscal indicators[4]																
High-employment (HEB) surplus/deficit	-83	-9	-9	-11	12	-7	24	24	21	18	-98	40	-41	-27	-16	-19
Change in HEB, percent of potential GDP	-.7	-.8	-0	0	-.8	.2	-.3	0	0	0	1	-1	.8	-.1	-.1	0
Fiscal impetus (FI) percent, calendar year	6	2	9	12	-6	6	-2	-.4	3	2	11	-7	10	.7	.8	1

1. Fiscal year data for the unified budget come from OMB; quarterly data come from the Monthly Treasury Statement and may not sum to OMB fiscal year totals.
2. OMB's April 2001 baseline surplus estimates are $284 billion in FY2001 and $283 billion in FY 2002. CBO's May 2001 baseline surplus estimates, assuming discretionary spending grows with inflation beginning in FY 2002, are $275 billion in FY2001 and $304 billion in FY 2002. These baseline estimates exclude the recently enacted tax bill which, according to estimates from the Joint Commitee on Taxation, will reduce the surplus by $74 billion in FY 2001 and by $38 billion in FY 2002. 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.
3. Other means of financing are checks issued less checks paid, accrued items, and changes in other financial assets and liabilities.
4. HEB is the NIPA current and capital account surplus in current dollars, with cyclically sensitive receipts and outlays adjusted to the level of potential output associated with an unemployment rate of 6 percent. 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 (1996) dollars, scaled by real federal consumption plus investment. For FI and the change in HEB, negative values indicate aggregate demand restraint.
a--Actual

Change in Debt of the Domestic Nonfinancial Sectors
(Percent)

			Nonfederal						
				Households					
Period[1]	Total[2]	Federal government[3]	Total[4]	Total	Home mortgages	Consumer credit	Business	State and local governments	Memo: Nominal GDP
Year									
1991	4.3	11.1	2.2	5.1	6.8	-1.3	-2.2	8.6	4.0
1992	4.6	10.9	2.6	4.8	5.8	0.8	0.3	2.2	6.4
1993	4.9	8.3	3.7	5.5	4.7	7.3	1.1	6.0	5.0
1994	4.5	4.7	4.4	7.6	5.9	14.5	3.5	-4.0	6.2
1995	5.5	4.1	6.0	8.0	6.0	14.1	6.6	-4.6	4.3
1996	5.3	4.0	5.8	7.3	7.3	7.9	5.7	-0.6	6.0
1997	5.6	0.6	7.3	6.5	7.0	4.3	8.9	5.3	6.2
1998	6.6	-1.4	9.3	8.5	9.6	5.4	10.7	7.2	6.0
1999	6.7	-1.9	9.3	8.8	9.8	7.1	10.9	4.4	6.0
2000	5.0	-8.0	8.5	8.6	8.6	9.3	9.6	2.2	5.3
2001	4.0	-2.0	5.4	6.1	6.9	5.1	4.6	5.7	3.2
2002	3.7	-3.2	5.1	5.6	6.8	3.0	5.2	2.2	4.6
Quarter									
2000:3	4.2	-6.2	6.8	8.0	8.5	8.2	6.4	1.9	3.3
4	4.6	-9.6	8.0	8.1	8.1	8.1	8.5	4.8	3.7
2001:1	5.3	-0.3	6.6	7.9	7.8	10.2	5.1	7.0	4.6
2	3.4	-6.6	5.6	6.0	6.4	4.5	4.5	8.7	2.5
3	4.8	5.6	4.6	5.2	6.3	3.5	4.1	3.3	2.5
4	2.5	-6.7	4.5	4.6	6.7	1.8	4.5	3.1	3.3
2002:1	4.1	1.1	4.7	5.1	6.5	3.0	4.8	2.2	4.7
2	3.0	-5.9	4.9	5.2	6.4	2.7	5.1	2.2	4.2
3	3.7	-4.0	5.2	5.8	6.8	3.1	5.2	2.2	4.7
4	3.7	-4.2	5.3	5.9	6.7	3.2	5.2	2.1	4.8

Note. Quarterly data are at seasonally adjusted annual rates.
1. Data after 2001:Q1 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. On a monthly average basis, total debt is projected to grow 4.3 percent in 2001 and 3.5 percent in 2002.
3. On a monthly average basis, federal debt is projected to grow -2.5 percent in 2001 and -3.6 percent in 2002.
4. On a monthly average basis, nonfederal debt is projected to grow 5.9 percent in 2001 and 5.0 percent in 2002.

2.6.3 FOF

Flow of Funds Projections: Highlights
(Billions of dollars except as noted)

Category	Calendar year				Seasonally adjusted annual rates									
					2000		2001				2002			
	1999	2000	2001	2002	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net funds raised by domestic nonfinancial sectors														
1 Total	945.3	696.0	712.1	693.3	664.5	434.3	936.4	586.1	855.9	470.2	791.2	572.3	700.4	709.3
2 Net equity issuance	-143.5	-166.6	-23.4	-3.1	-87.7	-394.8	-33.9	-35.2	-32.0	7.5	18.1	-7.6	-10.0	-12.8
3 Net debt issuance	1088.8	862.7	735.5	696.4	752.2	829.1	970.3	621.3	887.9	462.7	773.1	579.9	710.4	722.1
Borrowing sectors														
Nonfinancial business														
4 Financing gap [1]	260.0	308.3	281.4	271.0	322.1	335.0	304.8	292.2	278.2	250.4	258.3	266.7	282.5	276.7
5 Net equity issuance	-143.5	-166.6	-23.4	-3.1	-87.7	-394.8	-33.9	-35.2	-32.0	7.5	18.1	-7.6	-10.0	-12.8
6 Credit market borrowing	575.3	565.2	298.2	350.2	397.6	537.9	326.5	291.8	272.7	301.7	322.7	349.7	361.6	366.7
Households														
7 Net borrowing [2]	532.4	566.2	434.1	423.6	550.5	565.2	564.8	439.1	385.9	346.8	383.3	398.0	450.4	462.7
8 Home mortgages	409.8	397.8	347.7	362.7	407.3	399.5	390.3	325.2	325.2	350.2	350.2	350.2	375.2	375.2
9 Consumer credit	94.4	132.3	79.8	49.9	122.5	123.7	160.5	72.3	56.4	30.2	49.1	44.5	51.9	54.2
10 Debt/DPI (percent) [3]	95.2	97.5	99.2	100.2	97.8	98.4	99.0	99.7	98.4	100.7	99.5	99.9	100.2	100.7
State and local governments														
11 Net borrowing	52.3	27.2	72.3	29.4	23.6	60.4	89.9	113.8	43.8	41.8	29.4	29.4	29.4	29.4
12 Current surplus [4]	188.6	192.3	190.4	200.3	195.0	192.0	190.6	190.2	186.9	194.0	198.7	198.3	200.4	203.8
Federal government														
13 Net borrowing	-71.2	-295.9	-69.1	-106.8	-219.5	-334.5	-10.8	-223.4	185.5	-227.6	37.7	-197.2	-131.0	-136.6
14 Net borrowing (quarterly, n.s.a.)	-71.2	-295.9	-69.1	-106.8	-53.8	-25.0	23.7	-157.4	47.5	1.7	35.8	-135.4	-31.7	24.4
15 Unified deficit (quarterly, n.s.a.)	-158.6	-254.8	-165.5	-129.4	-60.4	2.3	22.5	-193.7	12.7	-6.9	46.6	-179.6	-27.0	30.6
Depository institutions														
16 Funds supplied	404.3	446.6	160.5	246.7	456.0	268.8	197.9	149.9	115.8	178.5	198.7	233.7	271.7	282.7
Memo (percentage of GDP)														
17 Domestic nonfinancial debt [5]	181.5	180.5	181.9	181.8	180.6	181.1	181.3	182.1	182.8	183.0	182.4	182.1	181.5	181.1
18 Domestic nonfinancial borrowing	11.7	8.7	7.2	6.5	7.6	8.3	9.6	6.1	8.6	4.5	7.4	5.5	6.6	6.7
19 Federal government [6]	-0.8	-3.0	-0.7	-1.0	-2.2	-3.3	-0.1	-2.2	1.8	-2.2	0.4	-1.9	-1.2	-1.3
20 Nonfederal	12.5	11.7	7.9	7.5	9.8	11.6	9.7	8.3	6.8	6.7	7.0	7.3	7.9	7.9

Note. Data after 2001:Q1 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 surplus less changes in retirement fund assets plus consumption of fixed capital.
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.

2.6.4 FOF

International Developments

Overview
We have again substantially marked down our forecast for foreign economic growth but continue to expect a return to moderate expansion next year. In assessing the magnitude of the downward revision over the forecast period, we have taken into account three factors. First, incoming data on activity abroad have been substantially weaker than expected for both industrial and developing countries. Second, the outlook for growth in the United States has worsened, with more protracted weakness in the U.S. high-tech sector expected to have a particularly adverse impact on the exports of Asian emerging-market economies. Third, in light of recent events, it now appears that Argentina will not be able to avoid a severe economic crisis and related substantial drop in activity, with some negative spillover to neighboring Latin American countries. The projected revival in foreign growth is based on an expected strengthening of U.S. growth as well as somewhat stimulative macroeconomic policy abroad. Lower energy prices are also expected to provide some support to activity, although oil prices are being held up to some extent by OPEC's apparent willingness to cut back production in response to reduced world demand for oil.

The dollar has depreciated about 2 percent on balance in terms of the broad index of our trading-partner currencies since the June Greenbook, as market concerns about the relative strength of the U.S. economy have mounted. We project that the dollar will decline somewhat further between now and the end of next year. The possibility of a sharp fall rather than moderate decline in the dollar remains an important risk to the outlook. (See the alternative scenario discussion at the end of this section.)

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

Indicator	2000		Projection		
			2001		2002
	H1	H2	H1	H2	
Foreign output	5.6	2.7	.6	1.4	2.9
June GB	*5.5*	*2.7*	*1.2*	*2.3*	*3.4*
Foreign CPI	2.2	3.5	2.6	2.5	2.5
June GB	*2.1*	*3.5*	*2.2*	*3.1*	*2.7*

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

As a consequence of the weakening global economy and the still-elevated level of the dollar, exports are expected to make an unusual negative contribution to U.S. real output growth this year. Very low U.S. growth should result in a positive contribution from imports, despite the strong dollar. Accordingly, real net exports of goods and services are projected to make an arithmetic contribution of about zero to U.S. GDP growth this year as imports and exports have offsetting effects. However, we project that net exports will resume making a negative arithmetic contribution to growth next year, given the substantial size of the trade deficit and the stronger rebound in imports.

Recent Developments

International financial markets. On balance, the trade-weighted index of the dollar's value against major currencies declined nearly 3 percent, with most of this decline coming late in the intermeeting period. Indications that sluggish U.S. economic activity will continue longer than anticipated have weighed on the dollar, although economic activity is also slowing more than previously expected in the euro area, Canada, and Japan.

On August 14, the Bank of Japan moved to ease monetary policy, raising its target for the outstanding balance of bank accounts held at the Bank and increasing the pace of its outright purchases of government bonds. The other notable changes in monetary policy stances by major foreign industrial countries during the intermeeting period were reductions of 25 basis points in target interest rates by the Bank of Canada and the Bank of England. In all three of these cases, weakening activity was cited as the main reason for the change. Foreign long-term interest rates generally declined, and broad equity indexes in most major industrial countries moved lower over the period.

The main focus of market attention on emerging financial markets was Argentina, where widespread pessimism about the country's ability to stave off default and avoid a change in its currency regime led to a sharp rise in the yield spreads on Argentine sovereign debt, large-scale withdrawals of currency from the Argentine banking system, and a drop in share prices. Late in the period, speculation that the IMF and other multilateral organizations would extend Argentina an enhanced support package led to a slight improvement in financial market conditions. Although there has been some negative financial market spillover from Argentina to Brazil, other emerging financial markets appear unscathed so far.

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

Economic activity abroad. Recent data suggest that growth weakened further in the second quarter in almost all of the major foreign industrial countries. In Japan, the economy appears to be sliding into another recession. Euro area economic growth looks to have slowed sharply in the second quarter, particularly in Germany and Italy. The situation has been somewhat less bleak in Canada, where domestic demand has held up fairly well. However, recently Canadian employment has started to fall off. Consumer price inflation in the foreign industrial countries has begun to ease as oil prices moved below last year's highs and growth turned anemic.

Recent activity indicators for emerging-market economies have been very sluggish, and we now estimate that output declined slightly in the first half of this year in both developing Asia and Latin America. The continuing falloff in global demand for electronic goods, particularly semiconductors, has had a strong negative impact on the exports of a number of Asian emerging-market economies, most notably Korea, Taiwan, and Singapore. In Latin America, Mexican real GDP has fallen three consecutive quarters largely owing to reduced demand from the United States. Output in Brazil has weakened as fallout from the worsening problems of Argentina prompted a tightening of monetary policy and domestic energy shortages constrained production.

Prices of internationally traded goods. The prices of imported non-oil goods declined for the sixth consecutive month in July. Oil prices have recently come under conflicting pressures--depressed by a resumption of oil exports by Iraq, increased oil inventories, and weak global demand but boosted by OPEC's decision to cut production targets. On balance, oil prices are little changed from the last Greenbook. Prices of U.S. goods exports also decreased for the sixth consecutive month in July.

U.S. international transactions. In May, the U.S. trade deficit in goods and services narrowed dramatically, and for April and May combined the deficit at an annual rate was lower than in the first quarter. The value of exports increased in May, following sharp declines the previous two months. However, for April and May combined, the value of exports was still substantially below the first quarter rate, reflecting mainly weakness in exported capital goods (especially computers and semiconductors) and industrial supplies. The value of imports registered a broad-based decrease in May, and, for April and May combined, the value of imports showed a double-digit annual rate decline from the first quarter.

Outlook

The dollar. The downward pressure on the dollar in recent days appears to reflect a heightened focus on weaker-than-expected U.S. growth prospects and the large imbalance in the U.S. external accounts. It may be that market participants, who have been aware of these negatives for the dollar for some time, now see these factors as more relevant for near-term exchange rate developments. The possibility that this downward pressure will continue constitutes a major risk to our overall forecast. However, such an eventuality is by no means certain, as the factors that have kept the dollar strong for so long--in particular, the weakness of foreign economies, notably Japan--remain in place. In an attempt to balance these considerations, we have adopted a projection of a dollar depreciation of about 2½ percent relative to the euro and a lesser decline against the Canadian dollar over the forecast period. In contrast, the dollar is assumed to remain unchanged against the yen, given Japan's poor economic prospects. Based on these projections and estimated inflation differentials, our forecast assumes that the broad real dollar index will decline about 2 percent over the forecast period. This projected depreciation from a lower starting point results in a dollar path that is somewhat below that in the June Greenbook.

Foreign industrial countries. We have substantially lowered our forecast for growth in the foreign industrial countries, reflecting both recent data that have disappointed expectations and the worsened outlook for the United States. Average growth in the foreign industrial countries is now expected to continue in the third quarter at its sluggish second-quarter pace of below 1 percent before reviving moderately in the fourth quarter and more robustly next year.

Japanese economic activity appears to have contracted sharply in the second quarter and is projected to shrink further in the current quarter, as private investment spending continues to decline from the overly-optimistic levels reached late last year and fiscal policy turns contractionary. Japanese growth is forecast to be near zero in the fourth quarter and to turn slightly positive next year, as the correction in private investment is completed. The Bank of Japan's recent monetary easing should provide some support to the economy going forward, but growth is still expected to be quite weak, as uncertain employment conditions hold down consumption growth and weak activity in Japan's key trading partners keeps export demand sluggish.

In the euro area, growth is estimated to have slowed to a rate below 1 percent in the second quarter and is projected to remain weak in the second half of this year. Sentiment indicators suggest an increasingly pessimistic tone to spending. The manufacturing sector will likely continue to contract in the near term, as firms work through excessive inventories, and consumption growth may be slowed by increased uncertainty about job prospects. Some further monetary stimulus and a boost to disposable income from the projected further easing of energy prices, along with an ending of the inventory cycle, should facilitate a pickup in growth next year.

In Canada, relatively robust domestic demand partially offset weakness in exports to the United States in the first half of the year. Some deceleration in real GDP is expected in the second half of the year to an average annual growth rate of about 1¾ percent. Monetary and fiscal stimulus already in place and an eventual pickup in U.S. demand should stimulate faster Canadian growth next year.

Headline inflation rates in Canada and Europe are projected to decline gradually to below 2 percent next year, as prices for food and energy moderate and pressures on resources diminish. Japanese consumer prices are projected to continue to decline over the next year and a half, as the Japanese economy remains very weak.

We are assuming moderate further easing in foreign monetary policy in the second half of this year. Specifically, the European Central Bank is expected to reduce official rates by a total of 50 basis points over the next few months as signs of slow growth accumulate and inflation pressures subside, and the Bank of Canada is expected to trim rates another 25 basis points.

Other countries. The forecast for growth in the major developing-country trading partners of the United States has been lowered sharply since the June Greenbook. This worsened outlook reflects both much weaker-than-expected recent activity data as well as poorer prospects for high-tech exports by Asian emerging-market economies, particularly to the United States. In addition, we are now assuming that Argentina will be unable to extricate itself from its severe economic crisis and so have significantly written down our projection for real output growth. Although our forecast is not based on the assumption of either a devaluation or a default by Argentina over the forecast period, such events certainly cannot be ruled out. The worsened situation in Argentina is likely to generate some additional negative spillover to its Latin American neighbors. Accordingly, we have also lowered growth projections for Brazil and Chile, although by lesser amounts. As of now, it is impossible for us to anticipate just how exchange rate developments will unfold as resolution of this crisis proceeds. Our current forecast incorporates somewhat weaker exchange values for the Mexican peso and Brazilian *real*. We project that average real GDP in the developing countries taken as a group, which is estimated to have declined slightly in the first half of this year, will resume positive but low growth in the second half of the year. Growth is then expected to strengthen in 2002.

Prices of internationally traded goods. Our forecast for oil prices is little changed from that in the June Greenbook. In line with recent futures quotes, we project that the spot price of West Texas intermediate will remain above $27 per barrel for the rest of this year and will gradually decline to around $24 per barrel by the end of next year. Core import prices will decline further during the second half of this year largely owing to near-term weakness in materials prices. Next year, core import prices are projected to increase nearly 2 percent, reflecting the expected depreciation of the dollar. Prices of exported core goods are projected to decline a bit through most of this year and then increase at an average rate of nearly 1 percent next year.

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

Trade category	2000		Projection		
			2001		2002
	H1	H2	H1	H2	
Exports					
Core goods	2.7	.7	-.3	-.5	.7
Imports					
Non-oil core goods	1.7	1.5	-1.2	-1.9	1.8
Oil (dollars per barrel)	26.18	28.87	24.16	24.18	21.75

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 multi-quarter periods is the price for the final quarter of the period.

U.S. international transactions. The decline in real imports of goods and services that occurred in the first quarter was repeated in the second quarter. This exceptional weakness mainly reflects the cyclical downturn in U.S. investment. The decline in imports was concentrated in computers, semiconductors and capital goods. We project that the continued weak near-term outlook for U.S. spending on investment goods should keep imports of those products declining in the second half of this year before increasing moderately next year. In contrast, imported consumer goods were about flat in the second quarter and are expected to bounce back in the second half of the year, largely in response to the boost to consumption from fiscal stimulus. On balance, total real imports of goods and services are forecast to be about unchanged in the current quarter and to pick up modestly in the fourth quarter. We project that imports will respond to the rebound in U.S. output growth next year and will rise more than 6 percent. The lagged effect of the dollar's appreciation over the past six quarters is expected to result in relative prices providing some slight stimulus to imports through the middle of next year, but the primary boost derives from revived U.S. growth and the high U.S. marginal propensity to import.

Real exports of goods and services declined an estimated 10 percent at an annual rate in the second quarter, as foreign growth slowed abruptly. The drop in exports of high-tech goods was particularly pronounced. We expect that exports will decrease slightly further in the second half of this year, owing to continued sluggish economic growth abroad and the lagged effects of past dollar appreciation. However, export growth is projected to accelerate next year, as foreign economic growth moves up along with U.S. growth.

Summary of Staff Projections for Trade in Goods and Services

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

Measure	2000		Projection		
			2001		
	H1	H2	H1	H2	2002
Real exports	11.2	3.0	-6.0	-.5	3.9
June GB	*10.2*	*3.2*	*-1.8*	*2.9*	*5.3*
Real imports	16.8	6.0	-6.0	1.4	6.4
June GB	*15.2*	*7.5*	*-2.6*	*4.5*	*7.4*

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

The U.S. current account deficit as a share of GDP is projected to be about 4-1/4 percent this year, down slightly from last year as the nominal trade deficit narrows. We expect that the current account deficit as a share of GDP will resume its rise next year.

Alternative simulation. We consider an alternative scenario in which declining confidence in the prospects for the United States relative to the other major industrial countries and some key developing economies causes the dollar to depreciate substantially. In particular, the shock consists of an exogenous 30 percent decline in the risk premium on euro-, sterling-, and yen-denominated assets. The assets of major Asian developing economies are assumed to experience a similar 30 percent decline in their risk premium, while that on the Canadian dollar falls by half as much. Risk premiums on the assets of Latin American countries are assumed unchanged.

These changes in risk premiums cause the broad real value of the dollar to experience a decline of nearly 25 percent by early next year. Afterwards, the path of the real exchange rate depends on the response of monetary policy at home and abroad. We consider two cases. The first case holds the real federal funds rate unchanged from its baseline path, and the second assumes that policy is adjusted according to a Taylor rule. (In both cases, the major foreign central banks adjust their policy rates according to a Taylor rule.) When U.S. monetary policy does not respond, real GDP growth is ¾ percentage point higher at an annual rate than in the baseline in the first half of next year and about 1½ percentage points higher in the second half of the year. Rising import prices and higher rates of resource utilization put upward pressure on inflation; the core PCE inflation rate rises about 1¼ percentage points by the second half of next year. Under a Taylor rule the federal funds rate rises more than 200 basis points by the end of next year, nearly twice the magnitude of the response under the policy that keeps the real funds rate unchanged. Accordingly, in this case output growth rises only about 1 percentage point above baseline in the second half of next year. Because the effects of policy actions on inflation occur with a somewhat longer lag than those on output, there is little difference in the responses of core PCE inflation across the monetary policy cases considered through the end of next year.

Alternative Simulation:
Weaker Dollar
(Percent change from previous period, annual rate)

Indicator and simulation	2001		2002	
	H1	H2	H1	H2
U.S. real GDP				
Baseline	0.8	1.3	2.4	3.0
Unchanged real funds rate	0.8	1.4	3.1	4.5
Taylor rule	0.8	1.4	3.1	4.1
U.S. PCE prices excl. food and energy				
Baseline	1.9	1.9	1.9	1.8
Unchanged real funds rate	1.9	1.9	2.7	3.2
Taylor rule	1.9	1.9	2.7	3.2

NOTE. H1 is Q2/Q4; H2 is Q4/Q2.

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

Measure and country	1994	1995	1996	1997	1998	1999	2000	--Projected- 2001	2002
REAL GDP (1)									
Total foreign	5.3	2.4	4.0	4.2	1.4	4.8	4.1	1.0	2.9
Industrial Countries	4.0	1.9	2.6	3.5	2.6	3.8	3.2	1.2	2.6
of which:									
Canada	5.3	1.5	2.6	4.5	4.2	5.1	3.5	1.9	3.0
Japan	1.7	2.6	2.9	0.7	-1.4	0.4	2.5	-1.3	0.8
United Kingdom	4.6	1.9	2.9	3.5	2.0	3.2	2.6	1.7	2.5
Euro Area (2)	3.0	1.4	1.6	3.1	2.1	3.4	2.9	1.1	2.4
Germany	2.9	1.1	1.3	1.6	1.0	2.5	2.6	0.5	2.1
Developing Countries	7.1	3.0	6.0	5.1	-0.2	6.2	5.5	0.7	3.2
Asia	9.5	6.9	6.6	4.8	-2.0	8.6	6.2	0.8	3.6
Korea	9.1	7.5	6.4	3.4	-5.2	13.8	5.2	0.9	3.0
China	23.3	10.4	5.3	8.7	9.5	4.1	8.0	7.3	7.4
Latin America	5.3	-3.7	5.9	6.2	1.2	4.3	4.8	0.1	2.6
Mexico	5.2	-7.1	7.1	6.7	2.8	5.5	5.2	0.1	3.0
Brazil	10.2	-0.7	3.3	2.4	-0.8	3.5	4.3	-0.2	2.5
CONSUMER PRICES (3)									
Industrial Countries	1.1	1.3	1.4	1.5	1.0	1.1	1.9	1.8	1.1
of which:									
Canada	-0.0	2.0	2.0	1.0	1.1	2.3	3.1	2.8	1.7
Japan	0.8	-0.8	0.1	2.0	0.8	-1.3	-1.1	-0.8	-0.9
United Kingdom (4)	2.3	2.9	3.2	2.7	2.5	2.2	2.1	2.3	2.4
Euro Area (2)	NA	NA	1.9	1.5	0.8	1.5	2.7	2.4	1.8
Germany	2.8	1.4	1.3	1.5	0.3	1.1	2.5	2.2	1.3
Developing Countries	22.8	16.5	11.1	6.8	9.0	4.6	4.2	3.5	4.4
Asia	10.7	5.8	4.8	2.7	4.4	0.2	1.9	2.1	3.3
Korea	5.8	4.3	5.0	4.9	5.9	1.2	2.8	4.4	2.7
China	26.9	11.1	6.8	0.9	-1.2	-0.9	0.9	1.4	3.7
Latin America	54.0	42.0	25.8	15.5	15.4	12.5	8.4	5.4	6.2
Mexico	7.0	48.7	28.0	17.0	17.4	13.6	8.8	5.2	6.3
Brazil	1196.9	21.5	9.6	4.6	1.5	8.2	6.1	6.6	6.2

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.

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

							------- Projected	-------	-------	-------	-------	-------
	2000				2001				2002			
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	7.6	3.6	3.8	1.7	1.0	0.2	1.1	1.8	2.4	2.7	3.1	3.2
Industrial Countries	5.8	2.4	2.7	2.1	1.9	0.6	0.7	1.6	2.3	2.4	2.8	2.9
of which:												
Canada	6.1	1.9	4.5	1.6	2.5	1.7	1.3	2.1	2.6	2.9	3.2	3.3
Japan	10.0	0.5	-2.7	2.6	0.5	-2.7	-2.7	-0.2	0.9	0.5	0.7	1.1
United Kingdom	1.7	3.7	3.4	1.8	1.8	1.2	1.9	2.0	2.4	2.4	2.6	2.6
Euro Area (2)	3.8	3.2	2.4	2.4	2.0	0.4	0.8	1.3	1.8	2.1	2.9	2.8
Germany	3.9	4.8	1.1	0.8	1.5	-0.5	0.0	0.9	1.5	1.7	2.6	2.5
Developing Countries	10.4	5.4	5.3	1.0	-0.4	-0.5	1.6	2.0	2.6	3.1	3.4	3.6
Asia	11.1	5.2	6.0	2.6	-0.4	-0.4	1.6	2.4	3.1	3.4	3.7	4.0
Korea	6.6	6.4	9.8	-1.7	1.2	0.0	1.0	1.5	2.5	2.8	3.1	3.5
China	11.3	8.1	7.5	5.2	8.1	7.5	6.8	6.8	7.0	7.5	7.5	7.5
Latin America	10.4	5.5	4.9	-1.2	-0.9	-1.0	1.2	1.3	1.8	2.6	3.1	3.1
Mexico	12.0	6.0	5.7	-2.4	-1.4	-1.0	1.2	1.5	2.0	3.0	3.5	3.5
Brazil	5.2	5.8	4.7	1.3	1.0	-3.9	1.0	1.0	2.0	2.3	2.8	3.0
CONSUMER PRICES (3)	Four-quarter changes											
Industrial Countries	1.6	1.5	1.7	1.9	1.8	2.3	1.9	1.8	1.6	1.2	1.1	1.1
of which:												
Canada	2.7	2.4	2.7	3.1	2.8	3.6	3.1	2.8	2.9	1.9	1.8	1.7
Japan	-0.8	-0.9	-1.1	-1.1	-0.6	-0.7	-0.8	-0.8	-1.3	-0.9	-0.9	-0.9
United Kingdom (4)	2.1	2.1	2.1	2.1	1.9	2.3	2.3	2.3	2.3	2.3	2.4	2.4
Euro Area (2)	2.1	2.1	2.5	2.7	2.5	3.1	2.7	2.4	2.4	1.7	1.8	1.8
Germany	2.0	1.7	2.2	2.5	2.4	3.2	2.6	2.2	1.8	1.2	1.3	1.3
Developing Countries	3.9	3.8	4.0	4.2	3.8	4.1	3.7	3.5	4.2	4.3	4.4	4.4
Asia	0.5	0.8	1.4	1.9	1.8	2.4	2.3	2.1	2.6	3.0	3.1	3.3
Korea	1.5	1.5	3.2	2.8	4.2	5.3	4.5	4.4	4.0	3.1	2.6	2.7
China	0.1	0.2	0.3	0.9	0.6	1.6	1.7	1.4	2.1	2.9	3.3	3.7
Latin America	10.0	9.2	8.7	8.4	7.2	6.8	5.8	5.4	6.5	6.3	6.5	6.2
Mexico	10.5	9.6	9.0	8.8	7.5	6.9	5.7	5.2	6.5	6.3	6.6	6.3
Brazil	7.8	6.7	7.6	6.1	6.2	7.1	6.6	6.6	7.0	7.0	6.2	6.2

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.

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1994	1995	1996	1997	1998	1999	2000	Projected 2001	2002
NIPA REAL EXPORTS and IMPORTS									
	Percentage point contribution to GDP growth, Q4/Q4								
Net Goods & Services	-0.3	0.4	-0.2	-0.8	-1.1	-1.0	-0.8	-0.0	-0.5
Exports of G&S	1.0	1.0	1.1	1.0	0.3	0.5	0.8	-0.4	0.4
Imports of G&S	-1.3	-0.6	-1.3	-1.7	-1.3	-1.5	-1.6	0.3	-0.9
	Percentage change, Q4/Q4								
Exports of G&S	10.5	9.7	9.8	8.5	2.3	4.5	7.0	-3.3	3.9
Services	8.2	8.8	8.9	1.4	2.9	1.9	4.1	1.0	4.6
Computers	27.4	39.1	21.6	25.8	8.1	13.8	23.1	-17.4	21.5
Semiconductors	66.9	79.6	44.6	21.3	9.1	34.6	26.9	-27.0	22.7
Other Goods 1/	7.9	4.6	7.3	9.8	1.3	3.2	5.7	-2.0	1.3
Imports of G&S	12.2	5.0	11.2	14.3	10.8	11.5	11.3	-2.3	6.4
Services	1.8	5.5	5.3	14.0	8.5	2.8	12.2	3.1	3.4
Oil	-0.2	2.4	7.8	3.9	4.1	-3.4	12.4	0.7	1.7
Computers	39.0	35.0	17.8	33.0	25.8	25.1	13.6	-11.5	21.5
Semiconductors	54.5	92.4	56.7	32.9	-8.7	33.5	22.5	-43.6	22.7
Other Goods 2/	12.3	-1.2	10.4	12.7	11.5	12.9	10.4	-1.2	6.2
	Billions of chained 1996 dollars								
Net Goods & Services	-86.5	-78.4	-89.0	-113.3	-221.1	-316.9	-399.1	-413.1	-465.5
Exports of G&S	732.8	808.2	874.2	981.5	1002.4	1034.8	1133.2	1117.3	1127.8
Imports of G&S	819.4	886.6	963.1	1094.8	1223.5	1351.7	1532.3	1530.4	1593.2
	Billions of dollars								
US CURRENT ACCOUNT BALANCE	-118.2	-109.9	-120.9	-139.8	-217.5	-324.4	-444.7	-429.3	-480.0
Current Acct as Percent of GDP	-1.7	-1.5	-1.5	-1.7	-2.5	-3.5	-4.5	-4.2	-4.5
Net Goods & Services (BOP)	-96.7	-96.4	-101.8	-107.8	-166.8	-261.8	-375.7	-365.8	-403.5
Investment Income, Net	21.1	25.0	25.5	13.6	-1.2	-8.5	-9.6	-5.1	-15.7
Direct, Net	55.2	64.9	69.4	72.4	66.3	67.0	81.2	91.2	89.5
Portfolio, Net	-34.1	-39.9	-43.9	-58.8	-67.5	-75.6	-90.9	-96.3	-105.2
Other Income & Transfers,Net	-42.7	-38.6	-44.6	-45.7	-49.4	-54.0	-59.3	-58.4	-60.8

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1997				1998				1999			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
IPA REAL EXPORTS and IMPORTS												
Percentage point contribution to GDP growth												
Net Goods & Services	-1.0	-0.3	-0.8	-0.9	-1.8	-1.8	-0.8	0.2	-1.8	-1.2	-0.7	-0.1
Exports of G&S	0.8	1.9	1.2	-0.1	0.1	-0.5	-0.2	1.7	-0.8	0.4	1.0	1.3
Imports of G&S	-1.8	-2.2	-2.0	-0.8	-1.9	-1.4	-0.5	-1.5	-1.0	-1.6	-1.7	-1.3
Percentage change from previous period, s.a.a.r.												
Exports of G&S	7.5	17.6	10.6	-0.8	0.5	-4.0	-2.2	16.3	-6.8	4.2	9.7	12.1
Services	-5.8	9.4	6.0	-3.3	2.4	8.0	-8.4	10.5	-3.9	3.8	2.0	6.0
Computers	60.0	44.5	25.7	-14.0	-8.3	8.2	12.0	22.8	0.5	26.8	18.3	11.0
Semiconductors	50.3	22.1	19.6	-1.4	5.9	-17.2	272.7	-56.6	45.4	31.6	36.5	25.8
Other Goods 1/	8.4	19.2	10.9	1.5	0.0	-9.2	-9.3	27.8	-11.5	1.1	11.0	14.2
Imports of G&S	15.3	18.8	17.3	6.4	15.9	11.3	4.2	12.2	8.4	13.3	13.8	10.5
Services	20.0	5.6	23.1	8.3	21.3	6.7	7.0	0.1	-8.2	1.8	7.9	11.0
Oil	-7.5	36.8	5.7	-12.9	3.6	42.8	1.1	-21.6	3.9	29.8	-5.8	-31.5
Computers	46.6	45.8	32.4	10.5	38.4	18.5	6.4	43.6	40.6	41.1	8.3	13.8
Semiconductors	78.1	26.0	31.6	5.6	8.5	-25.4	-6.3	-8.2	37.0	47.5	12.7	39.6
Other Goods 2/	11.6	17.2	14.8	7.5	14.2	11.9	4.1	16.2	9.0	11.3	17.6	14.0
Billions of chained 1996 dollars, s.a.a.r.												
Net Goods & Services	-94.0	-100.6	-119.6	-139.2	-180.8	-223.1	-241.2	-239.2	-283.0	-313.4	-333.3	-337.8
Exports of G&S	940.3	979.2	1004.2	1002.1	1003.4	993.1	987.6	1025.6	1007.6	1018.0	1041.8	1072.1
Imports of G&S	1034.3	1079.8	1123.8	1141.2	1184.2	1216.2	1228.9	1264.8	1290.6	1331.4	1375.1	1409.8
Billions of dollars, s.a.a.r.												
S CURRENT ACCOUNT BALANCE	-138.0	-119.3	-133.3	-168.7	-174.0	-209.6	-242.1	-244.1	-265.8	-309.5	-352.3	-369.9
urrent Account as % of GDP	-1.7	-1.4	-1.6	-2.0	-2.0	-2.4	-2.7	-2.7	-2.9	-3.4	-3.8	-3.9
Net Goods & Services (BOP)	-110.6	-96.8	-103.1	-120.6	-139.5	-169.9	-181.9	-176.0	-211.5	-251.5	-284.5	-299.9
Investment Income, Net	13.5	19.4	13.0	8.6	9.9	5.8	-12.3	-8.3	-5.2	-6.6	-15.5	-6.7
Direct, Net	69.3	76.8	74.4	69.0	74.2	69.8	57.8	63.3	66.2	63.0	63.3	75.7
Portfolio, Net	-55.8	-57.4	-61.4	-60.4	-64.2	-64.0	-70.1	-71.5	-71.4	-69.6	-78.8	-82.5
Other Inc. & Transfers, Net	-40.8	-41.9	-43.2	-56.7	-44.4	-45.5	-47.9	-59.8	-49.1	-51.5	-52.2	-63.3

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	2000				Projected 2001				Projected 2002			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
IPA REAL EXPORTS and IMPORTS												
Percentage point contribution to GDP growth												
Net Goods & Services	-1.3	-0.8	-0.7	-0.4	0.6	-0.2	-0.4	-0.1	-0.8	-0.7	-0.5	0.1
Exports of G&S	0.9	1.4	1.1	-0.5	-0.1	-1.2	-0.4	0.3	-0.0	0.3	0.5	0.8
Imports of G&S	-2.2	-2.2	-1.8	0.1	0.8	1.0	0.0	-0.4	-0.7	-1.0	-1.0	-0.7
Percentage change from previous period, s.a.a.r.												
Exports of G&S	9.0	13.5	10.6	-4.0	-1.2	-10.5	-3.7	2.8	-0.3	3.3	4.5	8.4
Services	10.3	9.9	-6.7	3.7	1.8	0.2	-0.3	2.5	3.8	4.5	5.0	5.1
Computers	32.7	49.2	25.8	-7.9	-5.8	-41.6	-15.1	-0.4	17.0	21.6	21.6	26.2
Semiconductors	29.9	64.5	35.0	-10.2	-22.4	-47.3	-28.4	-3.0	17.0	21.6	26.2	26.2
Other Goods 1/	5.3	9.1	16.3	-6.5	-0.1	-8.7	-2.4	3.5	-4.4	0.4	1.8	7.7
Imports of G&S	17.1	16.4	13.0	-0.5	-5.0	-6.9	-0.2	3.1	5.4	7.8	7.2	5.4
Services	20.6	12.4	17.1	0.0	4.9	2.9	2.0	2.5	3.2	2.8	3.6	3.8
Oil	29.7	40.3	-4.9	-7.7	27.1	1.3	-6.7	-14.6	-8.6	22.7	11.8	-14.7
Computers	12.8	34.4	18.4	-7.2	-11.0	-25.2	-7.8	-0.2	17.0	21.5	21.5	26.2
Semiconductors	45.6	24.9	64.9	-24.9	-31.8	-76.4	-34.4	-3.9	17.0	21.6	26.2	26.2
Other Goods 2/	14.6	13.1	11.9	2.4	-8.4	-3.6	1.9	5.9	6.4	6.3	6.1	6.0
Billions of chained 1996 dollars, s.a.a.r.												
Net Goods & Services	-371.1	-392.8	-411.2	-421.1	-404.5	-408.3	-417.9	-421.9	-443.0	-463.4	-478.6	-476.8
Exports of G&S	1095.5	1130.6	1159.3	1147.5	1144.1	1112.7	1102.4	1109.9	1109.1	1118.0	1130.5	1153.5
Imports of G&S	1466.6	1523.4	1570.6	1568.5	1548.6	1521.0	1520.2	1531.8	1552.1	1581.4	1609.0	1630.3
Billions of dollars, s.a.a.r.												
CURRENT ACCOUNT BALANCE	-419.6	-432.5	-461.2	-465.3	-438.3	-413.2	-421.8	-443.7	-453.2	-474.9	-489.9	-502.1
urrent Account as % of GDP	-4.3	-4.4	-4.6	-4.6	-4.3	-4.0	-4.1	-4.3	-4.3	-4.5	-4.6	-4.6
Net Goods & Services (BOP)	-349.3	-363.1	-389.4	-401.2	-380.1	-360.0	-359.0	-364.0	-383.9	-401.9	-415.2	-413.0
Investment Income, Net	-17.5	-14.4	-14.5	7.9	-6.9	2.4	-6.2	-9.6	-12.1	-15.4	-17.2	-18.0
Direct, Net	65.5	72.5	84.2	102.8	93.1	95.1	88.5	88.2	88.9	88.7	89.6	90.8
Portfolio, Net	-83.0	-86.8	-98.7	-94.9	-100.0	-92.7	-94.7	-97.8	-101.1	-104.1	-106.8	-108.9
Other Inc. & Transfers, Net	-52.8	-55.0	-57.4	-72.0	-51.3	-55.6	-56.6	-70.1	-57.1	-57.6	-57.6	-71.1

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