## Prefatory Note

The attached document represents the most complete and accurate version available based on original copies culled from the files of the FOMC Secretariat at the Board of Governors of the Federal Reserve System. This electronic document was created through a comprehensive digitization process which included identifying the best-preserved paper copies, scanning those copies,[1] and then making the scanned versions text-searchable.[2] Though a stringent quality assurance process was employed, some imperfections may remain.

Please note that this document may contain occasional gaps in the text. These gaps are the result of a redaction process that removed information obtained on a confidential basis. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

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[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

[2] A two-step process was used. An advanced optimal character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

Confidential (FR) Class III FOMC

# Part 2

October 31, 2001

# CURRENT ECONOMIC AND FINANCIAL CONDITIONS

## Recent Developments

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

Confidential (FR) Class III FOMC

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# Domestic Nonfinancial Developments

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## Overview

Real GDP edged down at an annual rate of 0.4 percent in the third quarter after posting a slight increase in the second quarter, and most indicators suggest that aggregate activity is contracting early in the fourth quarter.[1] Initial claims for unemployment insurance have risen to levels usually associated with a significant decline in payroll employment, and anecdotes as well as available data point to another sharp drop in factory output in October. Demand looks soft, but just how soft is difficult to say; some of the extraordinary weakness in the September data on retail sales and new orders for capital goods likely was temporary, as is the phenomenal surge in vehicle sales that seems to have taken place in October.

## Labor Market Developments

The labor market surveys for September were little affected by the attacks of September 11. Even so, they showed further deterioration of labor demand. Although the unemployment rate held steady at 4.9 percent that month after having jumped in August, private nonfarm payroll employment fell 196,000, and aggregate hours of production or nonsupervisory workers dropped 0.3 percent.[2] The decline in payroll employment in September was spread more widely than in preceding months: While manufacturing and the related industries of wholesale trade and help supply continued to shed jobs, substantial losses also occurred in retail trade and services. From the second quarter to the third quarter, the average unemployment rate rose from 4.5 percent to 4.8 percent, and aggregate hours paid fell at an annual rate of 3.1 percent.

Initial claims for unemployment insurance actually fell during the week ending on September 15, possibly because potential claimants postponed filing for benefits in the wake of the tragedy. But claims then moved back up to around 450,000 the following week and spiked to 535,000 in the week ending on September 29. Claims during that week were especially high in New York and Virginia and in states with large tourist industries, suggesting that much of the

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1. The third-quarter NIPA data were released on October 31, the same day that the Greenbook went to print. Additional detail will be released on November 1 and will be discussed in the Supplement.

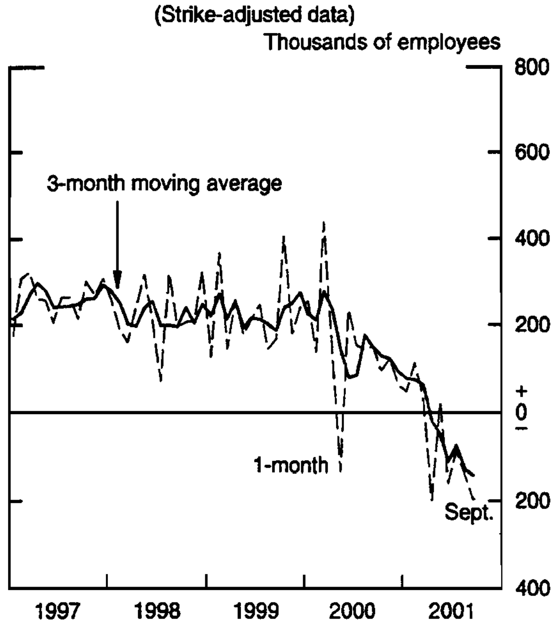
2. The week of September 11 was the reference week for both the establishment and household surveys. However, because the employment concepts in both surveys refer to work paid or performed during any part of the week (and often longer in the establishment survey), none of the measures of employment or unemployment in September appear to have been significantly affected by the terrorist attacks. In the establishment survey, the average workweek was little affected, as the survey measures hours paid rather than hours worked, and many workers were paid for lost hours during the week of September 11. In the household survey, the number of persons who reported working part time that week for economic reasons rose 25 percent, probably because of disruptions in business activity caused by the attacks. (In the household survey, the question refers to hours worked rather than hours paid.)

CHANGES IN EMPLOYMENT
(Thousands of employees; based on seasonally adjusted data)

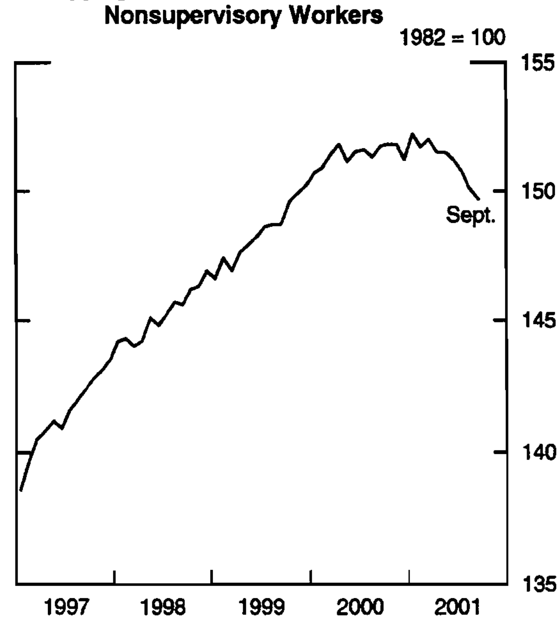
| | 2000 | | 2001 | | 2001 | | |
|---|---|---|---|---|---|---|---|
| | H1 | H2 | Q2 | Q3 | July | Aug. | Sept. |
| | --Average monthly change-- | | | | | | |
| Nonfarm payroll employment[1] | 267 | 66 | -74 | -88 | 18 | -84 | -199 |
| *Previous* | *267* | *66* | *-74* | | *13* | *-113* | |
| Private | 178 | 121 | -113 | -142 | -86 | -144 | -196 |
| Mining | 1 | 1 | 3 | 1 | 2 | 2 | 0 |
| Manufacturing | 5 | -29 | -120 | -103 | -69 | -146 | -93 |
| Construction | 16 | 21 | -22 | -2 | 3 | -4 | -4 |
| Transportation and utilities | 13 | 16 | -3 | -16 | -10 | -32 | -7 |
| Retail trade | 31 | 21 | 35 | -10 | 45 | -32 | -44 |
| Wholesale trade | 9 | 8 | -15 | -11 | -5 | -6 | -21 |
| Finance, insurance, real estate | -7 | 7 | 4 | 1 | -13 | 3 | 14 |
| Services | 110 | 76 | 4 | -3 | -39 | 71 | -41 |
| Help supply services | 15 | -19 | -44 | -20 | -34 | -18 | -9 |
| Total government | 90 | -54 | 39 | 54 | 104 | 60 | -3 |
| Total employment (household survey) | 114 | 109 | -283 | 83 | 447 | -986 | 788 |
| Nonagricultural | 116 | 115 | -227 | 8 | 397 | -1058 | 685 |
| Memo: | | | | | | | |
| Aggregate hours of private production workers (percent change)[1,2] | 2.1 | 0.2 | -1.5 | -3.1 | -0.3 | -0.5 | -0.3 |
| Average workweek (hours)[1] | 34.5 | 34.3 | 34.2 | 34.1 | 34.2 | 34.0 | 34.1 |
| Manufacturing (hours) | 41.8 | 41.3 | 40.8 | 40.7 | 40.8 | 40.7 | 40.5 |

Note. Average change from final month of preceding period to final month of period indicated.
1. Survey of establishments.
2. Annual data are percent changes from Q4 to Q4. Quarterly data are percent changes from preceding quarter at an annual rate. Monthly data are percent changes from preceding month.

**Private Payroll Employment Growth**
(Strike-adjusted data)



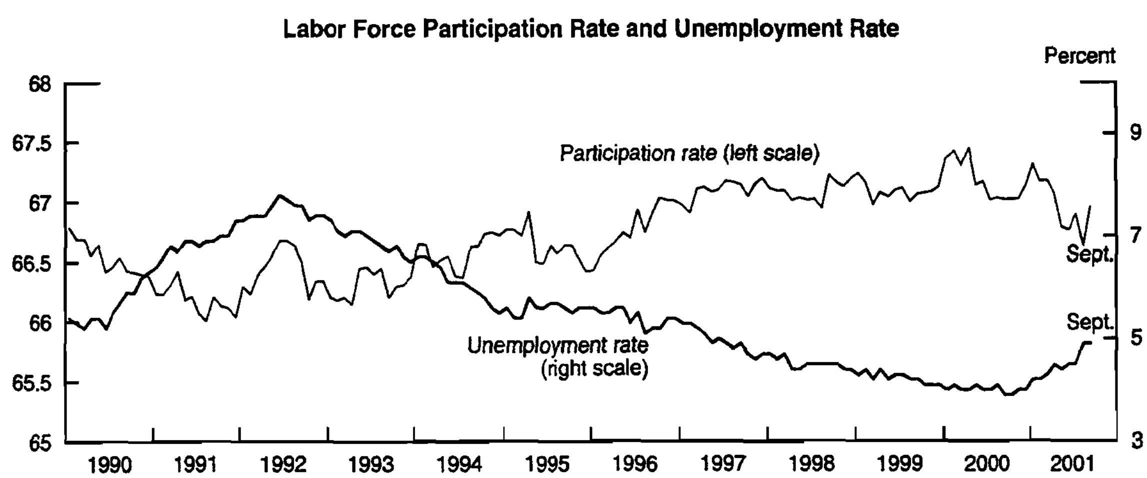

**Aggregate Hours of Production or Nonsupervisory Workers**

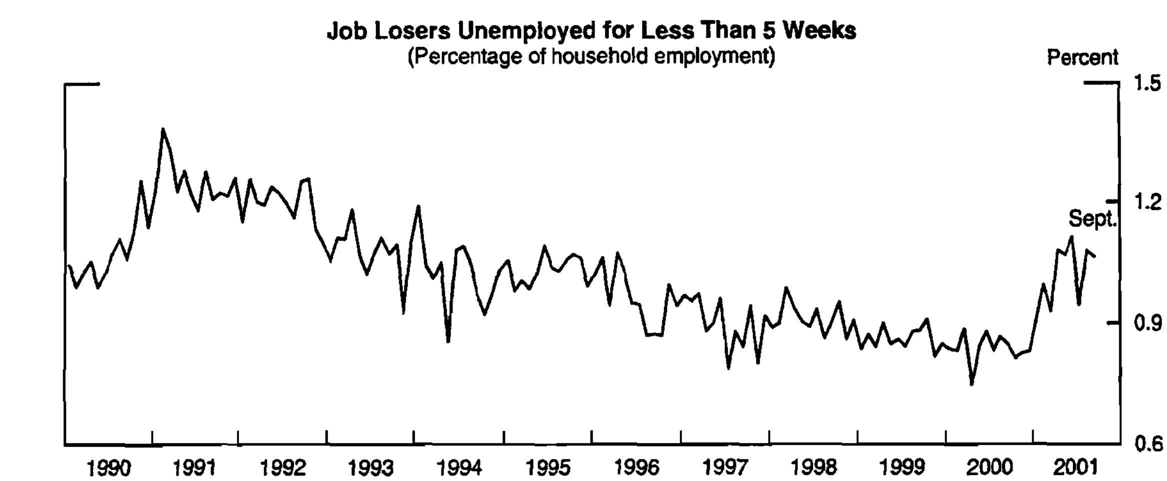


SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES
(Percent; based on seasonally adjusted data, as published)

| | 1999 | 2000 | 2001 Q1 | 2001 Q2 | 2001 Q3 | 2001 July | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|---|---|
| Civilian unemployment rate (16 years and older) | 4.2 | 4.0 | 4.2 | 4.5 | 4.8 | 4.5 | 4.9 | 4.9 |
| Teenagers | 13.9 | 13.1 | 13.7 | 14.0 | 15.2 | 14.8 | 16.1 | 14.7 |
| 20-24 years old | 7.5 | 7.1 | 7.4 | 8.1 | 8.4 | 7.5 | 9.0 | 8.5 |
| Men, 25 years and older | 3.0 | 2.8 | 3.1 | 3.4 | 3.6 | 3.5 | 3.7 | 3.7 |
| Women, 25 years and older | 3.3 | 3.2 | 3.3 | 3.4 | 3.7 | 3.4 | 3.7 | 3.9 |
| Labor force participation rate | 67.1 | 67.2 | 67.2 | 66.9 | 66.8 | 66.9 | 66.6 | 67.0 |
| Teenagers | 52.0 | 52.2 | 51.3 | 49.7 | 49.1 | 50.0 | 47.4 | 49.8 |
| 20-24 years old | 77.6 | 77.9 | 78.2 | 76.6 | 77.0 | 76.7 | 76.8 | 77.6 |
| Men, 25 years and older | 76.1 | 76.0 | 75.9 | 75.9 | 75.9 | 75.8 | 75.8 | 75.9 |
| Women, 25 years and older | 59.5 | 59.7 | 59.9 | 59.6 | 59.7 | 59.7 | 59.6 | 59.7 |
| Memo: Potential worker rate[1] | 7.2 | 6.9 | 7.1 | 7.4 | 7.8 | 7.5 | 8.0 | 7.8 |

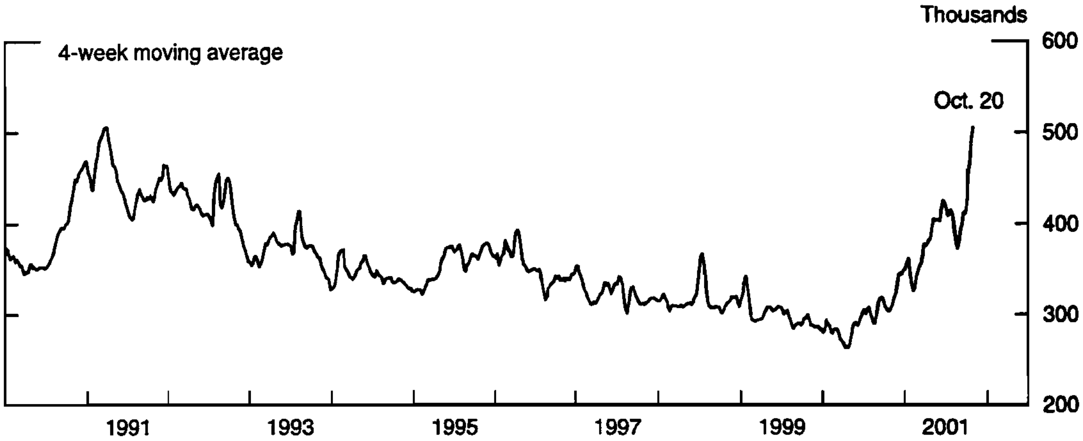
1. The potential worker rate equals the number of civilian unemployed plus those who are not in the labor force and want a job as a percentage of the civilian labor force plus those who are not in the labor force and want a job.



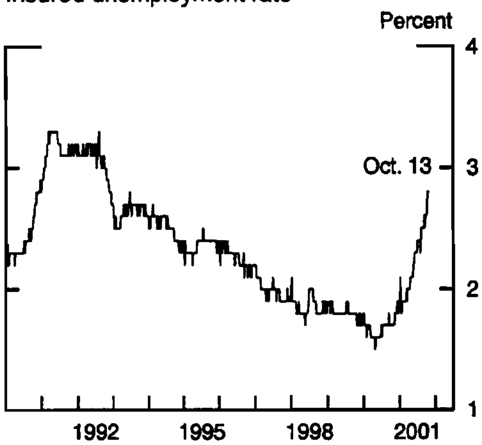



# Labor Market Indicators

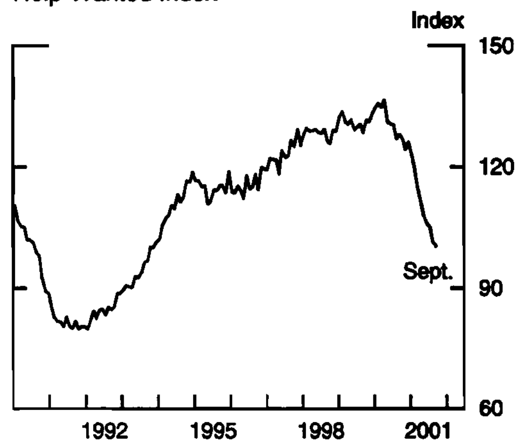
Initial Claims



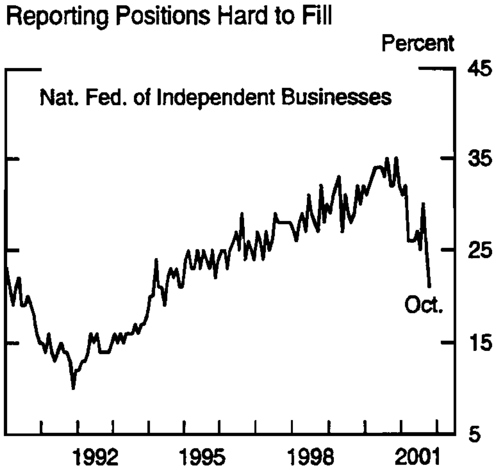

Insured unemployment rate



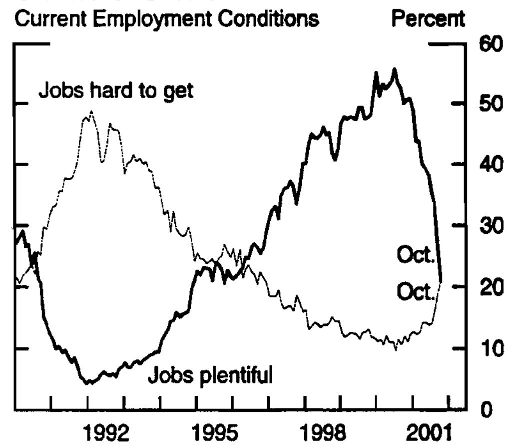

Help-Wanted Index




Reporting Positions Hard to Fill




Conference Board:
Current Employment Conditions



increase may have been fallout from the attacks. Since then, claims have edged off but have remained near 500,000 per week—well above the levels that prevailed before September 11.[3] At the same time, the insured unemployment rate has continued to rise over the past month, reaching a high of 2.8 percent for the week ending on October 13.

Reports of job losses have been widespread in recent weeks. Since September 11, we have counted announcements of job losses or other reductions in staff totaling 348,000 jobs.[4] Admittedly, the connection between such announcements and monthly changes in payroll employment typically is tenuous.[5] However, many of the nearly 120,000 job reductions we have counted in the airline and hotel industries probably occurred in time to be measured in the October employment report. (Of course, we expect the payroll survey also to record many job reductions beyond those two industries.)

Other indicators underscore the perception that labor markets have continued to deteriorate. The Conference Board's index of help-wanted advertising edged down in September, and the percentage of employers surveyed by the National Federation of Independent Business reporting difficulty in filling positions retraced its August increase in September and moved lower again in October. In the Conference Board survey of consumer attitudes, households' views of employment conditions continued to worsen in October.

The Bureau of Labor Statistics will release its initial estimate of productivity for the third quarter on November 7. Based on the NIPA data released October 31 and the data on hours published to date, we estimate that output per hour in the nonfarm business sector increased at an annual rate of roughly 2-1/2 percent in the third quarter of 2001. Over the four quarters ended last quarter, we estimate that productivity rose 1-3/4 percent, about 2 percentage points less than the increase recorded over the previous four quarters.

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3. Initial claims have been running a bit higher when measured using the FRB seasonal adjustment procedure, but the pattern of increase has been similar.

4. These data are compiled by the staff from news reports.

5. One reason for the weakness of the connection is that the timing of the announced reductions is typically vague; many occur months after the announcement, and some may not occur at all.

SELECTED COMPONENTS OF INDUSTRIAL PRODUCTION
(Percent change from preceding comparable period)

| | Proportion 2000 | 2001 Q1 | 2001 Q2 | 2001 Q3 | 2001 July | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|---|
| | | ----Annual rate----- | | | --Monthly rate--- | | |
| Total | 100.0 | -6.8 | -4.4 | -6.2 | -.1 | -.7 | -1.0 |
| Previous | | -6.8 | -4.4 | | -.1 | -.8 | |
| Manufacturing | 87.8 | -7.9 | -5.1 | -6.6 | .1 | -.9 | -1.1 |
| Ex. motor veh. and parts | 82.1 | -6.6 | -7.3 | -7.6 | -.2 | -.7 | -.9 |
| Ex. high-tech industries | 72.7 | -6.7 | -5.6 | -6.1 | -.1 | -.7 | -.8 |
| Mining | 6.3 | 6.0 | 7.5 | -5.3 | -1.0 | -.3 | .3 |
| Utilities | 5.9 | -3.4 | -7.9 | -1.0 | -.7 | 1.9 | -1.8 |
| Selected industries | | | | | | | |
| High technology | 9.4 | -6.1 | -20.8 | -21.0 | -2.1 | -1.0 | -2.4 |
| Computers | 2.7 | -3.5 | -12.8 | -14.3 | -.8 | -.5 | -2.5 |
| Communication equipment | 2.0 | -1.7 | -17.1 | -24.8 | -3.7 | -.9 | -2.3 |
| Semiconductors[1] | 4.7 | -9.6 | -26.9 | -22.8 | -2.0 | -1.3 | -2.3 |
| Motor vehicles and parts | 5.7 | -27.2 | 37.4 | 8.6 | 4.8 | -3.0 | -3.6 |
| Aircraft and parts | 2.2 | -5.6 | -3.1 | -3.9 | .1 | .0 | -1.0 |
| Market groups, excluding energy and selected industries | | | | | | | |
| Consumer goods | 22.5 | -.1 | -1.8 | -5.1 | -.3 | -.8 | -.4 |
| Durables | 3.5 | -5.0 | -2.5 | -8.7 | -1.1 | -.8 | -1.2 |
| Nondurables | 19.0 | .8 | -1.7 | -4.5 | -.2 | -.7 | -.3 |
| Business equipment | 8.4 | -7.6 | -13.3 | -13.5 | .0 | -.6 | -2.2 |
| Construction supplies | 6.1 | -3.1 | -3.0 | -2.7 | .0 | -.4 | -.6 |
| Business supplies | 7.1 | -12.1 | -11.4 | -8.5 | -.2 | -1.0 | -1.0 |
| Materials | 24.2 | -11.4 | -5.8 | -4.8 | .1 | -.4 | -.7 |
| Durables | 15.9 | -9.4 | -3.4 | -4.7 | .2 | -.5 | -1.0 |
| Nondurables | 8.3 | -15.1 | -10.2 | -5.0 | .0 | -.2 | -.1 |

1. Includes related electronic components.

CAPACITY UTILIZATION
(Percent of capacity)

| | 1967-2000 Avg. | 1988-89 High | 1990-91 Low | 2001 Q1 | 2001 Q2 | 2001 Q3 | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|---|---|
| Manufacturing | 81.1 | 85.7 | 76.6 | 77.9 | 76.4 | 74.7 | 74.8 | 73.8 |
| High-tech industries | 80.4 | 81.9 | 72.4 | 77.3 | 69.3 | 63.2 | 63.5 | 61.4 |
| Excluding high-tech | 81.2 | 86.1 | 76.8 | 77.6 | 76.9 | 75.8 | 75.9 | 75.1 |

**Labor Output per Hour**
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

| Sector | 1999[1] | 2000[1] | 2001 | | |
|---|---|---|---|---|---|
| | | | Q1 | Q2 | Q3[2] |
| Nonfarm businesses | | | | | |
| All persons[3] | 2.8 | 2.3 | .1 | 2.1 | 2.4 |
| All employees[4] | 2.3 | 1.9 | .9 | 1.3 | 2.4 |
| Nonfinancial corporations[5] | 2.9 | 4.2 | .6 | 2.8 | n.a. |

1. Changes are from the fourth quarter of the preceding year to the fourth quarter of the year shown.
2. Staff estimate.
3. Includes the non-employees (published definition).
4. Assumes that the growth rate of hours of all persons equals the growth rate of hours of all employees.
5. The nonfinancial corporate sector consists of all corporations doing business in the United States with the exception of banks, stock and commodity brokers, and finance and insurance companies; the sector accounts for about two-thirds of business employment.
n.a. Not available.

### Industrial Production

Industrial production fell 1 percent in September after declining 0.7 percent in August. In September, production dropped in most market groups and industries, and the three-month diffusion index fell to 29.4, a level only slightly above the low reached in the 1990-91 recession. Motor vehicle assemblies stepped down 400,000 units after a similar reduction in August, and the production of high-technology goods fell 2.4 percent. Production in other manufacturing industries dropped 0.8 percent in September. In total, the cumulative drop in industrial output over the past year was 5.8 percent, and the overall factory operating rate in September reached 73.8 percent, the lowest reading since May 1983.[6]

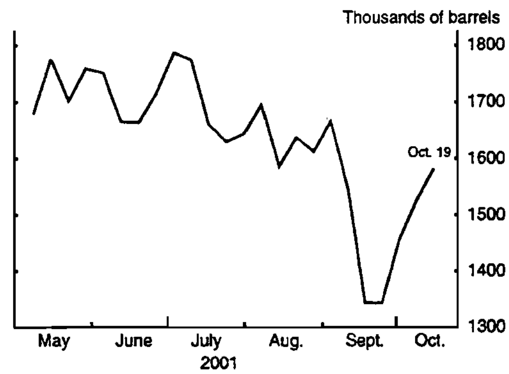
Available indicators suggest that production is likely to post a sizable drop in October. Real adjusted durable goods orders plunged in September, and anecdotal reports suggest that conditions for manufacturers have worsened since September 11. In addition, most weekly production measures are down for the

6. The steep fall in utilization of the high-tech sector accounts for only part of the drop in the overall operating rate; excluding that sector, capacity utilization declined to 75.1 percent, the lowest reading since July 1983.

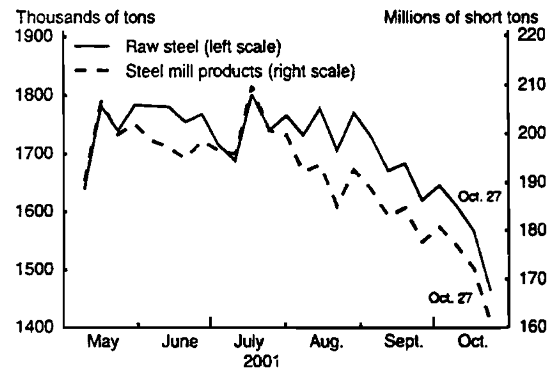
# Indicators of Manufacturing Activity

## Selected Weekly Production Series

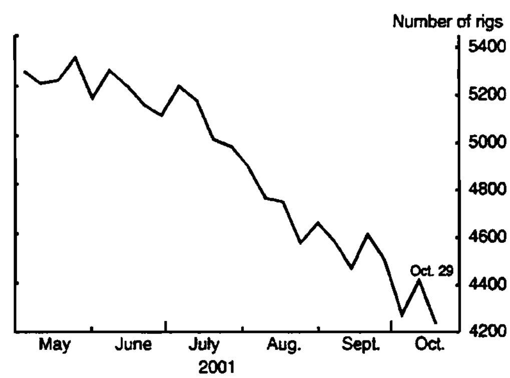
### Jet Fuel



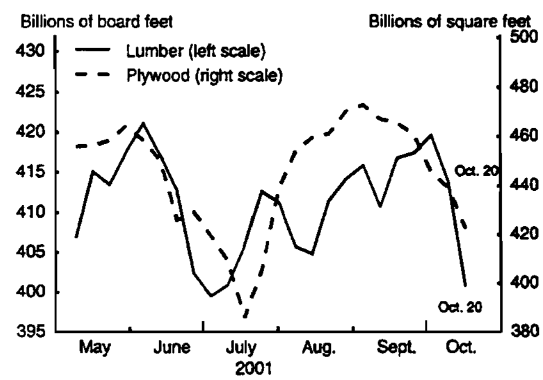

### Steel Products




### Rotary Oil and Gas Rigs in Operation



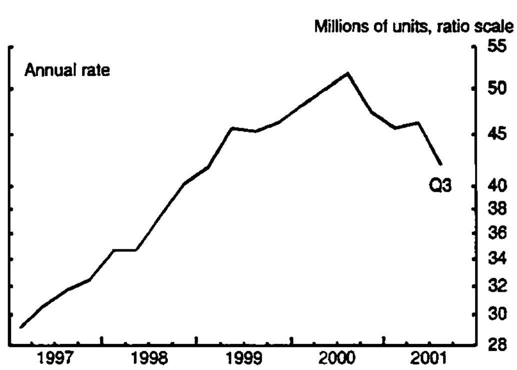

### Wood Products




Note. 3-week moving average.

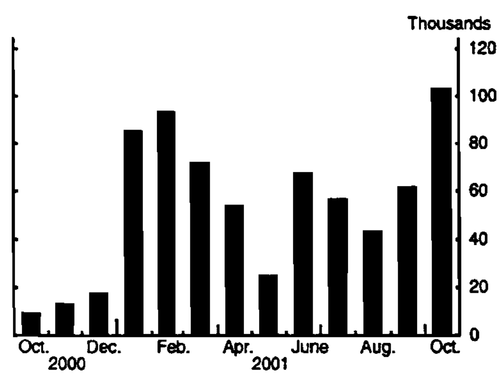
## Other Indicators

### Personal Computer Sales




Note. FRB seasonals. Includes notebooks.
Source. Dataquest.

### Announced Manufacturing Layoffs




Note. Data are through October 30, 2001.
Source. Compiled by staff from news reports.

month and are expected to reduce total IP growth by 0.4 percentage point.[7] Production has fallen this past month in every industry for which weekly data are available except petroleum refining, which had dropped sharply in September because of a huge decline in the output of jet fuel. Production of both raw steel and steel products is down around 7 percent so far in October in response to continued import competition and falling demand.[8] An October decline in the number of oil rigs in operation continued the slide that has been evident since late spring. The output of two construction materials, lumber and plywood, also fell.

**New Orders for Durable Goods**
(Percent change from preceding period; seasonally adjusted)

| Component | Share, 2001:H1 | 2001 | | | | |
|---|---|---|---|---|---|---|
| | | Q2 | Q3 | July | Aug. | Sept. |
| **Total orders** | **100.0** | **-2.3** | **-4.8** | **-1.0** | **-.5** | **-8.5** |
| Adjusted orders[1] | 73.0 | -4.2 | -5.4 | -1.9 | -.3 | -9.2 |
| Computers | 5.0 | -14.0 | -19.2 | -7.3 | -8.9 | -6.2 |
| Communications equipment | 4.0 | -26.3 | -17.1 | 14.6 | -.3 | -41.4 |
| Semiconductors and related devices | 4.0 | -19.4 | -3.9 | -24.3 | 20.4 | 16.0 |
| Other capital goods | 20.0 | .4 | -4.8 | 0.0 | - 1.8 | -8.3 |
| Other[2] | 40.0 | -1.4 | -3.2 | -1.5 | 0.2 | -9.3 |
| Memo: | | | | | | |
| Real adjusted orders | ... | -3.4 | -4.4 | -1.6 | .5 | -8.6 |
| Excluding high tech | ... | -1.3 | -12.6 | -.4 | -.4 | -9.2 |

1. Orders excluding defense capital goods, nondefense aircraft, and motor vehicle parts.
2. Includes primary metals, most fabricated metals, most stone, clay, and glass products, household appliances, scientific instruments, and miscellaneous durable goods.
... Not applicable.

In the motor vehicle industry, automakers had anticipated a slowdown in sales in the second half of this year and accordingly scheduled a step-down in fourth-quarter production. Even with an apparent October surge in vehicle sales, automakers remain wary about the future path of sales, and they have trimmed production further in October by temporarily closing several plants. These shutdowns, along with weekly data in hand, suggest that motor vehicle

7. October weekly production data are available for a variety of industries, including motor vehicles, lumber, plywood, raw steel, steel products, appliances, petroleum products, meat products, coal, drilling activity, and electricity generation.
8. Reflecting the troubled state of this industry, Bethlehem Steel, the second largest integrated steel maker in the United States, filed for bankruptcy on October 15.

assemblies slipped to a 10-3/4 million unit annual pace in October; relative to schedules at the beginning of the month, this is an underbuild of about 4 percent. Current schedules for the last two months of the fourth quarter average nearly 11-1/2 million units (annual rate), but in our view the risk that schedules might be revised down outweighs the upside risk at this point.

**Production of Domestic Autos and Trucks**
(Millions of units at an annual rate except as noted; FRB seasonal basis)

| Item | 2001 | | | 2001 | | | | |
|---|---|---|---|---|---|---|---|---|
| | Q2 | Q3 | Q4[1] | June | July | Aug. | Sept. | Oct.[1] |
| U.S. production | 11.7 | 11.6 | 11.2 | 11.7 | 12.1 | 11.6 | 11.2 | 10.8 |
| Autos | 5.1 | 4.7 | 4.7 | 5.1 | 4.9 | 4.6 | 4.6 | 4.5 |
| Trucks | 6.6 | 6.9 | 6.5 | 6.6 | 7.2 | 7.0 | 6.6 | 6.3 |
| Days' supply[2] | 62.0 | n.a. | n.a. | 60.0 | 63.9 | 64.5 | 64.1 | n.a. |
| Autos | 49.3 | n.a. | n.a. | 49.0 | 49.7 | 52.6 | 50.4 | n.a. |
| Light trucks[3] | 73.0 | n.a. | n.a. | 69.2 | 75.8 | 73.9 | 75.2 | n.a. |
| Inventories[4] | 2.75 | n.a. | n.a. | 2.75 | 2.78 | 2.77 | 2.69 | n.a. |

Note. Components may not sum to totals because of rounding.
1. Production rates reflect Ward's Communications' latest estimates.
2. Quarterly average calculated using end-of-period stocks and average reported sales.
3. Excludes medium and heavy (classes 3-8) trucks.
4. End-of-period stocks; excludes medium and heavy (class 3-8) trucks.
n.a. Not available.

In the high-tech area, conditions in the semiconductor industry remain weak. According to the Semiconductor Industry Association, capital spending by chip makers in 2001 is now likely to be 40 percent below the 2000 level; at midyear, the forecast was for a 25 percent to 30 percent decline. New orders for equipment by semiconductor manufacturers fell 11 percent in September after having been flat since May. The weakness in the semiconductor industry is attributable, in part, to the poor performance in downstream industries, such as communications equipment and computers. According to Dataquest, personal computer (PC) sales for the third quarter fell 9.2 percent (not at an annual rate, FRB seasonals).[9] Since the fourth quarter of last year, PC sales have declined 18.7 percent.

After September 11, manufacturers apparently became markedly more pessimistic about their prospects. By our count, manufacturing firms announced job losses totaling 103,000 in October, compared with 61,700 in September and

9. Most desktop PCs sold in the United States are assembled here.

only 43,600 in August. In the Federal Reserve Bank of Philadelphia's *Business Outlook Survey* for October, the diffusion indexes for new orders and employment fell sharply. Responding to a special question, more than half of the respondents in that survey reported that new orders fell after September 11. In a survey conducted by the National Association of Business Economists during early October, 14 percent of goods producers expected sales to increase moderately for the remainder of the year; 38 percent expected no change; 38 percent expected sales to fall moderately; and 10 percent expected sales to fall markedly. That survey also indicated that since September 11, 43 percent of goods producers have lowered their expectations about sales for the remainder of the year, compared with 5 percent that raised their sales expectations.

**Consumer Spending**

Real personal consumption expenditures rose at an annual rate of 1-1/4 percent in the third quarter. Retail sales data indicate that outlays on goods likely dropped sharply in September, thereby offsetting moderate increases in the previous two months; spending on services appears to have declined as well.[10] The pace of light vehicle sales apparently surged to near-record levels in October. However, available indicators and anecdotal reports suggest that non-auto spending was quite soft for the month.

The third-quarter gain in real PCE reflected relatively modest increases in each of the major spending categories—durable goods, nondurable goods, and services. Within the services category, third-quarter outlays on transportation and recreation services declined last quarter, likely because of September drops in spending on airline travel and other items affected by the attacks of September 11. Meanwhile, real disposable income surged at an annual rate of 12-3/4 percent in the third quarter because of a significant decrease in net tax payments and a sharp drop in energy prices.[11] The personal saving rate jumped 2-3/4 percentage points last quarter.

In the aftermath of the events of September 11, the major automakers, led by General Motors, offered reduced financing rates, and sales of vehicles have surged since late September.[12] Based on confidential industry estimates, sales of light vehicles in October are expected to be at least 19-1/2 million units (annual

10. The monthly detailed data on personal consumption expenditures will not be available until November 1.

11. In particular, households received rebates in the third quarter worth $140 billion at an annual rate and benefited from $13-3/4 billion in reduced withholding associated with lower marginal tax rates. Regarding energy prices, the PCE price index for energy plunged at an annual rate of nearly 21 percent in the third quarter, holding down overall PCE inflation by about 1 percentage point.

12. The incentives do not apply to consumer leases. The new financing rates typically include zero percent financing for thirty-six month loans and reduced rates for longer-term loans. Several other firms, including Toyota, have introduced similar, but more limited, programs.

RETAIL SALES
(Percent change; seasonally adjusted)

| | 2001 | | 2001 | | |
|---|---|---|---|---|---|
| | Q2 | Q3 | July | Aug. | Sept. |
| Total retail trade and food services | 1.3 | -.3 | .2 | .4 | -2.4 |
| Previous estimate | 1.3 | | .2 | .3 | |
| Retail control[1] | .6 | -.1 | .1 | .5 | -1.7 |
| Memo: | | | | | |
| Real PCE control[2] | .5 | .5 | .8 | .6 | -2.2 |

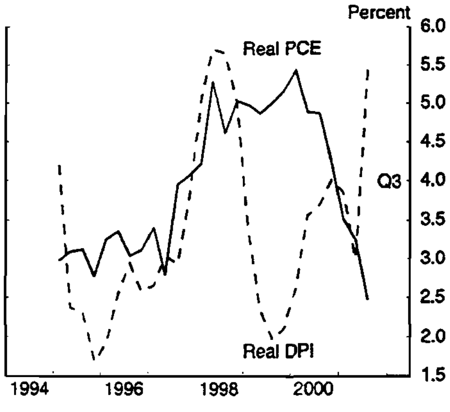
1. Total retail trade and food services less sales at building material and supply stores and automobile and other motor vehicle dealers.
2. PCE data from July through September are staff estimates.

REAL PERSONAL CONSUMPTION EXPENDITURES
(Percent change from the preceding period unless otherwise noted)

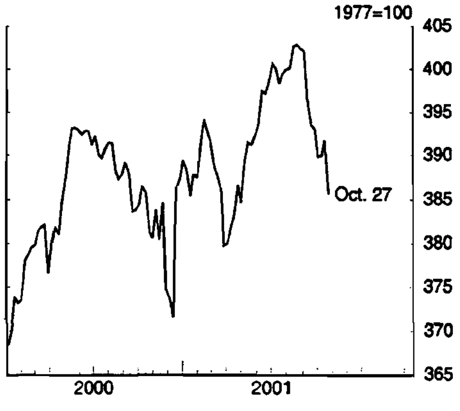
| | | 2001 | | |
|---|---|---|---|---|
| | 2000 | Q1 | Q2 | Q3 |
| | Q4/Q4 | --- Annual rate --- | | |
| Total real PCE | 4.2 | 3.0 | 2.5 | 1.2 |
| Durable goods | 5.3 | 10.6 | 7.0 | 1.7 |
| Motor vehicles | 1.6 | 16.1 | 5.6 | .0 |
| Nondurable goods | 3.6 | 2.4 | .3 | .6 |
| Services | 4.3 | 1.8 | 2.8 | 1.4 |
| Electricity and natural gas | 12.2 | -11.2 | -13.8 | .3 |
| Transportation | 2.6 | 1.0 | -.4 | -3.1 |
| Medical | 3.0 | 2.9 | 4.6 | 3.6 |
| Recreation | 2.6 | 6.5 | 1.0 | -1.9 |
| Housing | 2.0 | 2.2 | 1.7 | 1.9 |
| Memo: | | | | |
| Real disposable personal income | 4.0 | 2.7 | 2.4 | 12.8 |
| NIPA personal saving rate[1] | 1.0 | 1.1 | 1.1 | 3.8 |

1. Data are in levels. Annual and quarterly values are averages over the period indicated.

Real Consumer Spending and Income




Weekly Chain Store Sales




Source: Bank of Tokyo-Mitsubishi

SALES OF AUTOMOBILES AND LIGHT TRUCKS
(Millions of units at an annual rate, FRB seasonals)

| | 1999 | 2000 | 2001 Q2 | 2001 Q3 | 2001 July | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|---|
| Total[1] | 16.8 | 17.2 | 16.6 | 16.1 | 16.4 | 16.2 | 15.8 |
| Autos | 8.7 | 8.8 | 8.4 | 7.9 | 8.1 | 7.9 | 7.7 |
| Light trucks | 8.1 | 8.4 | 8.2 | 8.2 | 8.2 | 8.3 | 8.1 |
| North American[2] | 14.3 | 14.4 | 13.6 | 13.1 | 13.4 | 13.2 | 12.9 |
| Autos | 7.0 | 6.8 | 6.3 | 5.9 | 6.1 | 5.8 | 5.7 |
| Light trucks | 7.3 | 7.5 | 7.3 | 7.3 | 7.3 | 7.4 | 7.1 |
| Foreign-produced | 2.5 | 2.9 | 3.0 | 3.0 | 3.0 | 3.0 | 2.9 |
| Autos | 1.7 | 2.0 | 2.1 | 2.0 | 2.0 | 2.1 | 1.9 |
| Light trucks | .8 | .8 | 1.0 | 1.0 | 1.0 | 1.0 | .9 |
| Memo: | | | | | | | |
| Total retail sales (confidential)[3] | 13.7 | 13.9 | 13.4 | 13.1 | 12.9 | 13.3 | 13.1 |

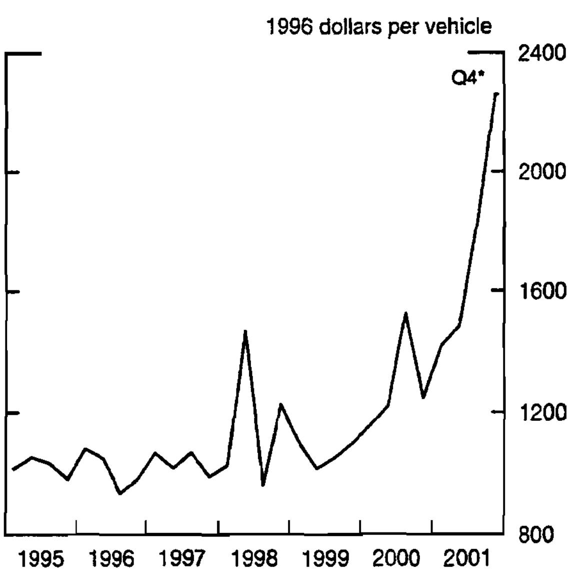
Note. Components may not sum to totals because of rounding. Data on sales of trucks and imported autos for the most recent month are preliminary and subject to revision.

1. The automakers' changes in reporting periods have no effect on the figures shown.

2. Excludes some vehicles produced in Canada that are classified as imports by the industry.

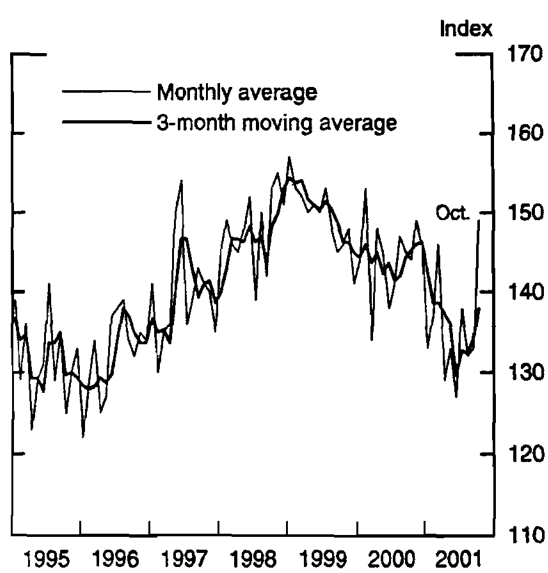
3. Sales include consumer purchases and leases of light vehicles.

**Marketing Incentives for Light Vehicles**



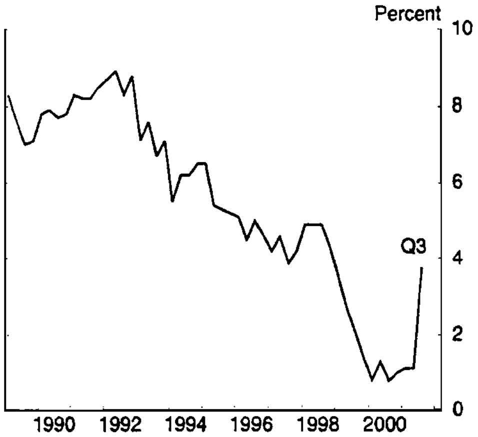

Note. Nominal industry data from GM and deflated by total CPI.
*Staff estimate.

**Michigan Survey Index of Car-Buying Attitudes**

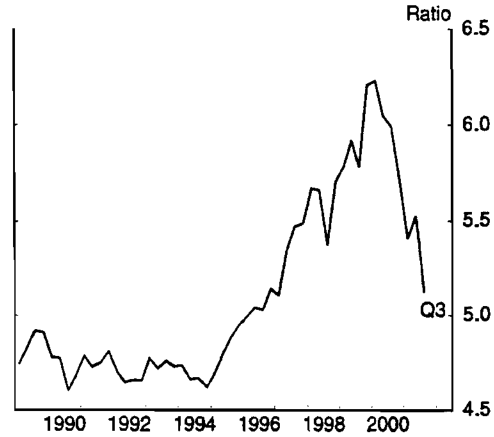


## Household Indicators

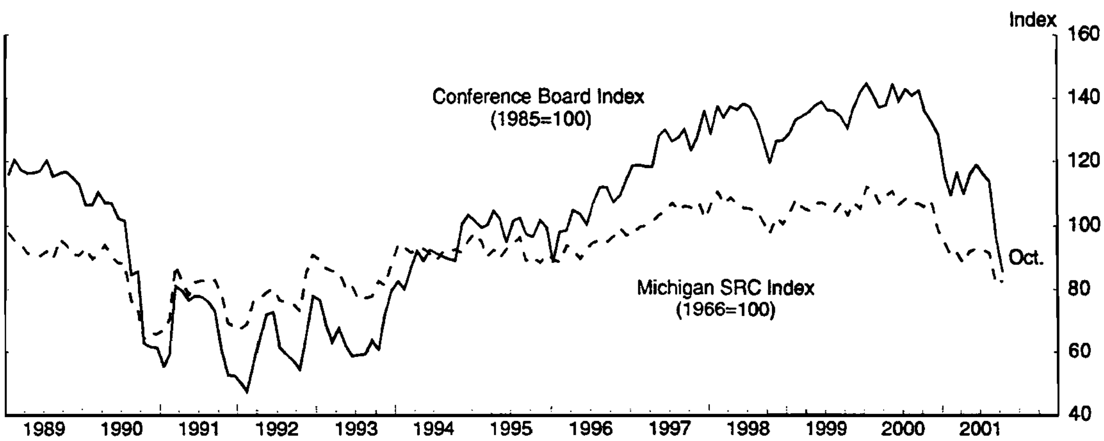
Personal Saving Rate



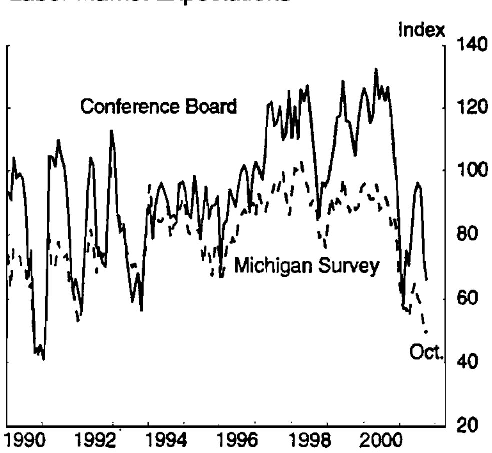

Ratio of Household Net Worth to DPI



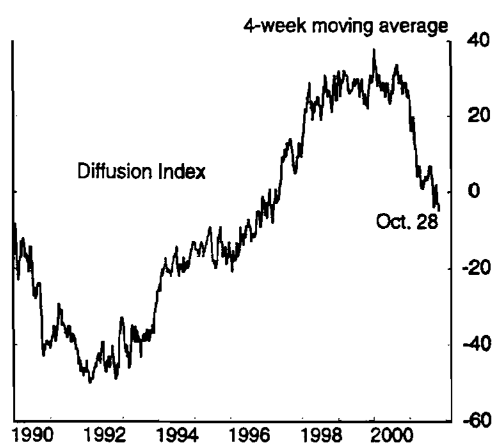

Consumer Confidence




Labor Market Expectations




ABC News/Money Magazine Consumer Comfort Index



rate), with a spike in retail sales likely to more than account for the overall gain. The consumer response to the incentives has far exceeded automakers' expectations. Nonetheless, producers also believe that much of the jump in demand likely has been shifted from future months, and sales are expected to fall sharply after these special financing rates expire. The special financing plans are currently set to expire by November 20, but other types of incentives will still be available.

Outside of reports from motor vehicle producers, available indicators present a mixed picture regarding consumer spending in October. According to the Bank of Tokyo/Mitsubishi (BTM), weekly chain store sales fell back in the fourth week of October after having turned up slightly in the middle of the month. Many retailers indicated to BTM that sales for the month were likely to come in "below plan." In addition, the latest readings from around the country suggest that moderate temperatures in October could result in a slight decline in real outlays on energy services. On the plus side, physical product data from the Department of Energy point to a 2-1/4 percent rise in real consumer purchases of gasoline in October after a drop of almost 3-1/2 percent in September. In addition, stock market volumes rose even higher in October than in September, indicating another increase in real PCE for brokerage services.

The most recent report from the University of Michigan Survey Research Center (SRC) suggests that the attitudes of consumers have been fairly resilient in the aftermath of September 11: After having registered a sharp decline in September, the headline consumer sentiment indexes ticked up in October. By contrast, the Conference Board's (CB) index of consumer confidence fell sharply in October after having posted an even larger decline in the previous month. Looking back over a longer time frame, however, both indexes have retreated substantially over the past year, and their October levels were below their respective long-run averages. Regarding labor-market expectations, both the SRC and CB surveys indicate that consumers anticipate further deterioration in the coming months.

**Housing Markets**

Housing activity appears to have been softening before September 11—albeit to a level that remains comparatively high—and may have weakened further since then. Although single-family starts edged up in September to an annual rate of 1.27 million units, adjusted permits for single-family construction dropped 5-3/4 percent, to about the same level as in June and July of last year. The ratio of starts to the statistically more reliable permits series was noticeably above its long-run average in September, suggesting that starts will drop back in the fourth quarter. After September 11, contracts with suppliers and subcontractors likely gave builders only limited flexibility with regard to home construction planned for the balance of the month. But builders could easily have postponed applying for additional building permits. For the third quarter as a whole,

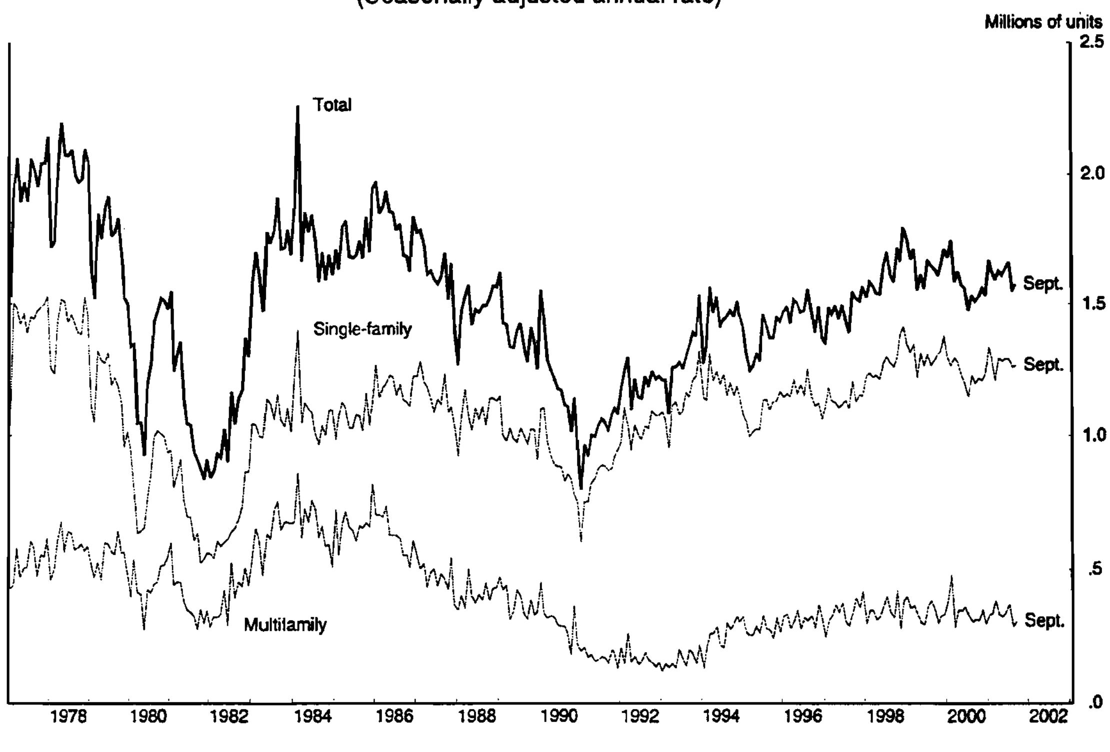
## Private Housing Activity
(Millions of units; seasonally adjusted annual rate)

| | 2000 | 2001 Q1 | 2001 Q2 | 2001 Q3p | 2001 Julyr | 2001 Aug.r | 2001 Sept.p |
|---|---|---|---|---|---|---|---|
| *All units* | | | | | | | |
| Starts | 1.57 | 1.63 | 1.62 | 1.59 | 1.66 | 1.55 | 1.57 |
| Permits | 1.59 | 1.67 | 1.60 | 1.56 | 1.57 | 1.57 | 1.52 |
| *Single-family units* | | | | | | | |
| Starts | 1.23 | 1.28 | 1.29 | 1.27 | 1.29 | 1.26 | 1.27 |
| Permits | 1.20 | 1.24 | 1.22 | 1.19 | 1.21 | 1.21 | 1.16 |
| Adjusted permits[1] | 1.25 | 1.28 | 1.27 | 1.23 | 1.25 | 1.26 | 1.18 |
| New home sales | .88 | .95 | .89 | .88 | .90 | .88 | .86 |
| Existing home sales | 5.11 | 5.27 | 5.30 | 5.21 | 5.20 | 5.54 | 4.89 |
| *Multifamily units* | | | | | | | |
| Starts | .34 | .35 | .33 | .32 | .37 | .29 | .31 |
| Permits | .39 | .43 | .38 | .36 | .36 | .36 | .36 |
| *Mobile homes* | | | | | | | |
| Shipments | .25 | .18 | .19 | n.a. | .19 | .20 | n.a. |

1. Adjusted permits equals permit issuance plus total starts outside of permit-issuing areas.

p Preliminary. r Revised. n.a. Not available.

## Private Housing Starts
(Seasonally adjusted annual rate)



single-family starts were only about 1 percent below the average for the first half of this year.

Sales of new homes, which have been trending down from extraordinarily high levels earlier in the year, edged still lower in September, to an annual rate of 864,000 units. Sales of existing homes dropped 11-3/4 percent, to a 4.9 million unit pace in September after a record high sales pace in August. Although some of the decline in existing home sales may reflect postponement of closings in the wake of the terrorist attacks, the inherent lag in existing home sales suggests that the number of sales contracts signed likely was falling before September 11.[13] In addition, increases in both the repeat-sales price index for existing homes and the constant-quality price index for new homes moderated in the third quarter.

Our more timely indicators of housing demand have continued to show signs of softening in recent weeks on balance. In the Michigan Survey, the October reading on households' attitudes toward homebuying remained quite favorable, a result partly reflecting a further decline in mortgage rates to a level near their thirty-year lows. However, builders' rating of new home sales fell in October to the lowest level since early 1996, and the four-week moving average for the Mortgage Bankers Association index of purchase applications for home mortgages dropped to the lowest level in two years.

Moreover, builders themselves may be turning more cautious. In a survey of 360 builders conducted in the first ten days of October by the National Association of Home Builders, one-third indicated that they had reduced the number of housing starts planned for the fourth quarter of this year, and one-fourth reported that they had lowered the number of starts planned for the first half of next year; the magnitude of these intended reductions is not known.[14]

In the multifamily sector, starts rose 6-1/4 percent in September, to an annual rate of 306,000 units, but they still were 9-1/2 percent below the average for the first eight months of this year. For the third quarter as a whole, multifamily starts averaged 321,000 units, down nearly 6 percent from the average during the two preceding quarters. Multifamily starts were well in line with adjusted permits in September.

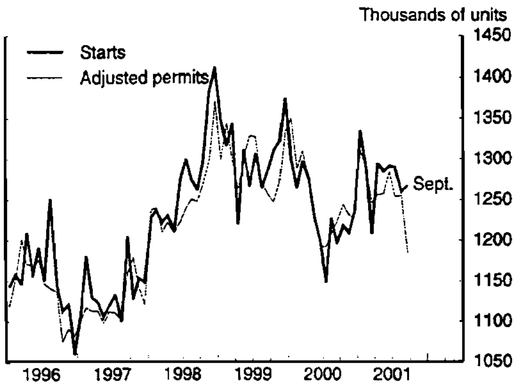
---

13. Existing home sales are recorded primarily on the basis of closings; hence, the sales series lags changes in housing market conditions by about a month. However, according to the National Association of Realtors, as many as 15 percent of sales ordinarily are closed within the first two weeks after a contract is signed, and about 28 percent are closed within three weeks.

14. The results of the latest NAHB survey differ from a much smaller sampling conducted on September 19 and 20 that was reported in the September Greenbook. The earlier NAHB survey found that most builders were not making major changes to their plans over the next one or two quarters.

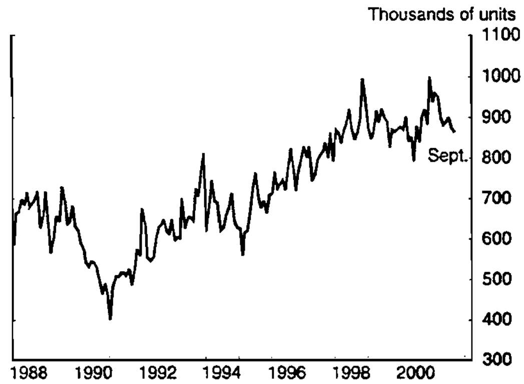
# Indicators of Single-Family Housing

## Starts and Adjusted Permits



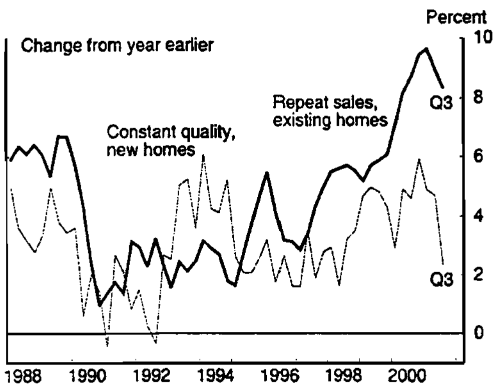

Note. Adjusted permits calculated by Board staff.
Source. Census Bureau.

## New Home Sales



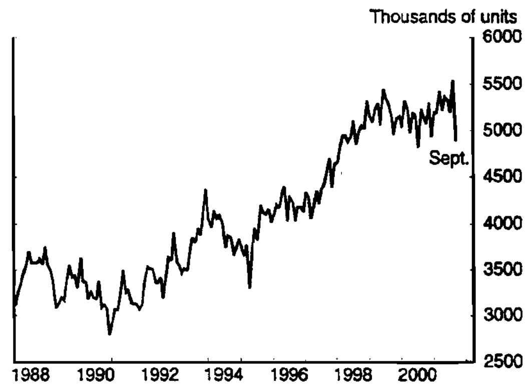

Source. Census Bureau.

## House Prices



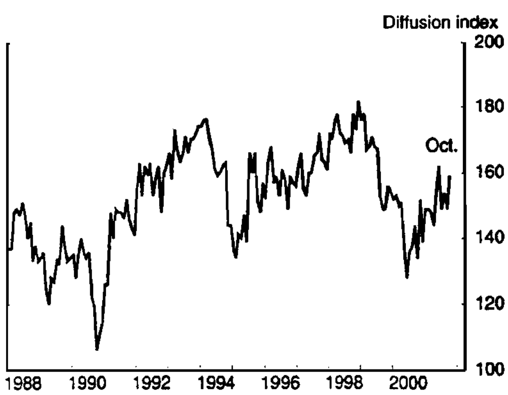

Source. Census Bureau (new); Fannie Mae and Freddie Mac (existing).

## Existing Home Sales



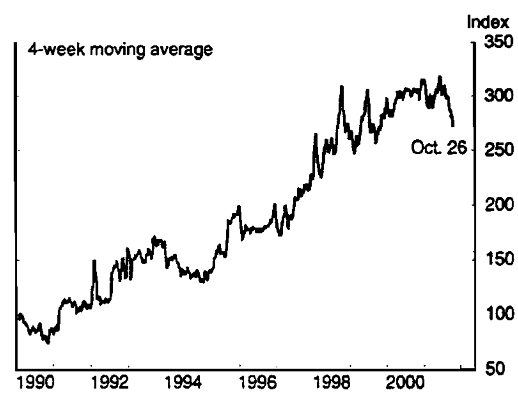

Source. National Association of Realtors.

## Perceived Homebuying Conditions




Source. Michigan Survey, not seasonally adjusted.

## MBA Index of Purchase Applications



## Business Fixed Investment

**Equipment and software.** Real outlays for equipment and software fell at an annual rate of 11-3/4 percent in the third quarter and appear to be headed for an even sharper decline this quarter. New orders for nondefense capital goods excluding aircraft plunged 9 percent in September after a 3/4 percent decline in August. New orders in all high-tech sectors fell in September, with orders for communications equipment extraordinarily weak; orders fell in almost every category outside of the high-tech sector as well. Meanwhile, shipments of nondefense capital goods excluding aircraft fell 3.9 percent in September. Shipments for computers and related equipment were among the few components that increased in September, but that rise followed a large decline in August. The level of new orders for nondefense capital goods (excluding aircraft) has been running below the level of shipments since January, and as a result, the backlog of unfilled orders has moved below its level of a year ago. Although some of the observed decline in orders and shipments likely reflects the pause in activity immediately following September 11, these data signal an underlying weakness that probably is greater than we had previously thought.

This pessimism about investment spending is borne out by recent surveys of businesses. According to the Conference Board survey of chief executive officers (CEOs) completed before September 11, business confidence was deteriorating in the third quarter. Nearly 50 percent of CEOs reported that they had scaled back spending plans, and more than 20 percent expected conditions to worsen in the next six months. Furthermore, in the October NABE survey, about two-thirds of respondents to this survey reported reduced sales expectations after the September 11 attacks.[15] Moreover, more businesses reported that they plan to cut capital spending than plan to increase spending over the next year, and more than one-third of respondents have revised downward their capital spending plans since July.

In the aircraft sector, Boeing and Airbus recently revised down their production schedules in light of reduced demand by air carriers. Boeing plans to reduce production in the first half of next year, and deliveries in 2002 may fall to a low of 350 planes. In the near-term, Boeing says that deliveries for 2001 could number 522 planes, about the same as thought at the time of the last Greenbook but well below anticipations as of early September. Airbus has cut its announced target for deliveries in 2002 from 375 planes to around 330 planes, and company officials conjectured that Airbus deliveries may drop even lower, to around 300.

15. This survey covers firms in the manufacturing, transportation, utilities, communications, financial services, and other services industries.

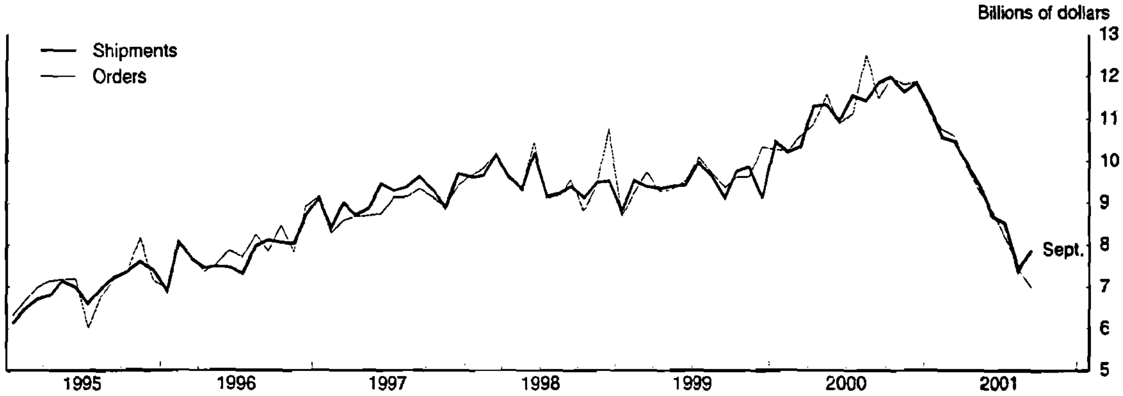
BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period;
based on seasonally adjusted data, in current dollars)

| | 2001 | | 2001 | | |
|---|---|---|---|---|---|
| | Q2 | Q3 | July | Aug. | Sept. |
| Equipment and software | | | | | |
| Shipments of nondefense capital goods | -5.6 | -6.4 | -2.4 | -2.5 | -3.2 |
| Excluding aircraft | -5.8 | -6.7 | -1.7 | -2.2 | -3.9 |
| Computers and related equipment | -13.1 | -15.3 | -1.9 | -13.3 | 6.5 |
| Communications equipment | -12.8 | -10.8 | -6.9 | -2.5 | -3.2 |
| All other categories | -2.8 | -4.2 | -.8 | .0 | -5.7 |
| Shipments of complete aircraft | 2.5 | n.a. | 22.1 | -15.7 | n.a. |
| Medium & heavy truck sales (units) | -5.1 | -6.2 | -5.6 | .5 | -6.9 |
| Orders for nondefense capital goods | -7.1 | -10.0 | -3.1 | -.7 | -11.4 |
| Excluding aircraft | -7.7 | -8.2 | -2.5 | -.8 | -9.0 |
| Computers and related equipment | -14.0 | -19.2 | -7.3 | -8.9 | -6.2 |
| Communications equipment | -26.3 | -17.1 | 14.6 | -.3 | -41.4 |
| All other categories | -2.8 | -4.7 | -3.4 | .7 | -5.1 |
| Nonresidential structures | | | | | |
| Construction put in place, buildings | -4.0 | n.a. | -3.2 | -3.6 | n.a. |
| Office | -7.0 | n.a. | -5.7 | -6.3 | n.a. |
| Other commercial | -2.8 | n.a. | -3.7 | -1.7 | n.a. |
| Institutional | -.1 | n.a. | -1.5 | -1.1 | n.a. |
| Industrial | -4.3 | n.a. | .9 | -7.3 | n.a. |
| Lodging and miscellaneous | -4.8 | n.a. | -4.5 | -.8 | n.a. |
| Rotary drilling rigs in use[1] | 9.3 | -5.0 | .0 | -4.6 | -5.6 |

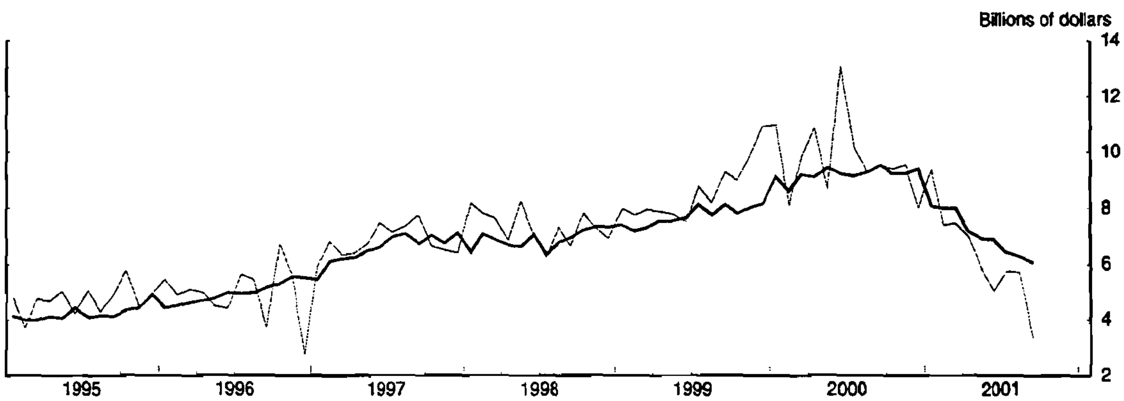
1. Percent change of number of rigs in use, seasonally adjusted.

# Recent Data on Orders and Shipments

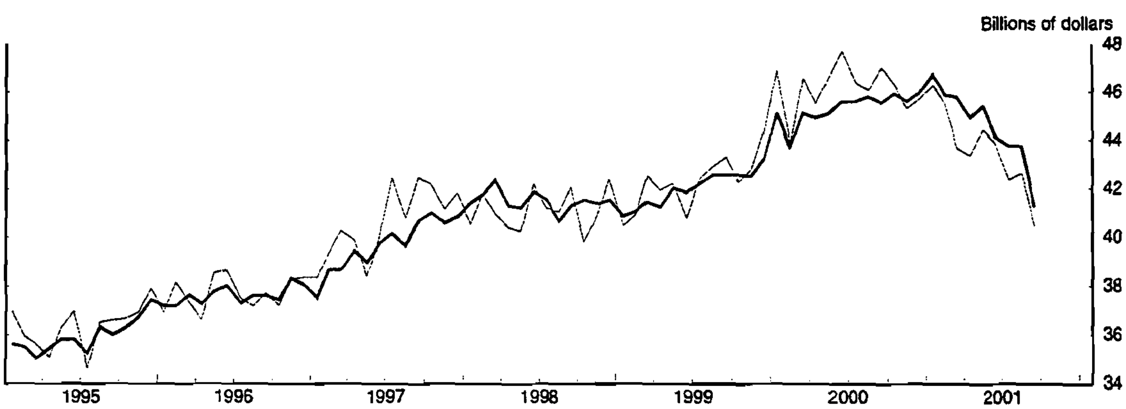
Computers and Related Equipment



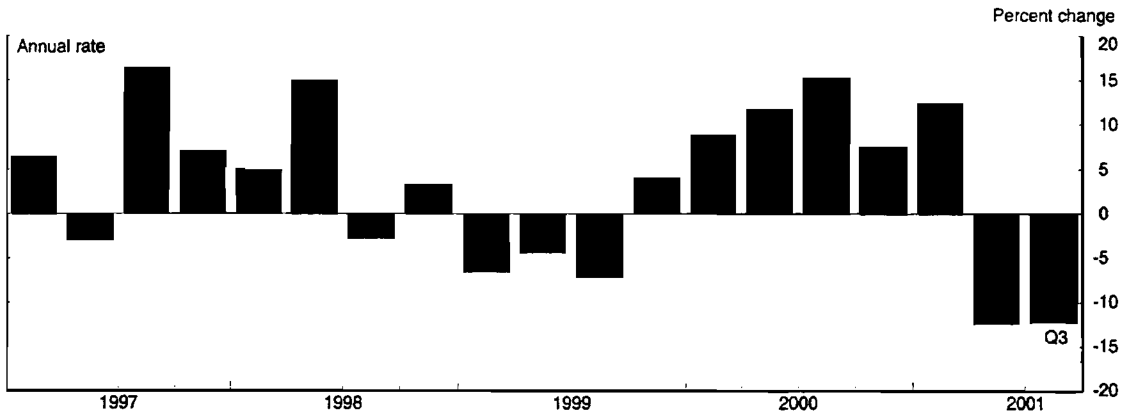

Communications Equipment




Other Equipment (Total Ex. Transportation, Computers, Communications)



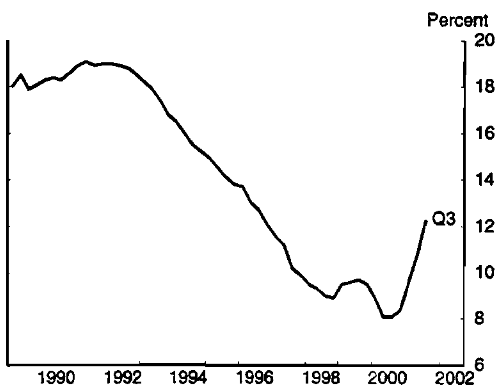
## Real Nonresidential Investment




## Commercial Real Estate Markets

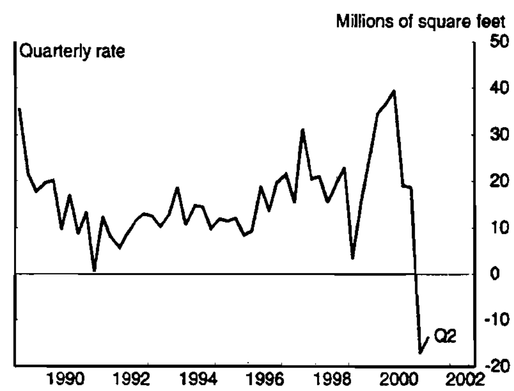
### Office Buildings

Vacancy Rate




Source. Torto Wheaton Research.

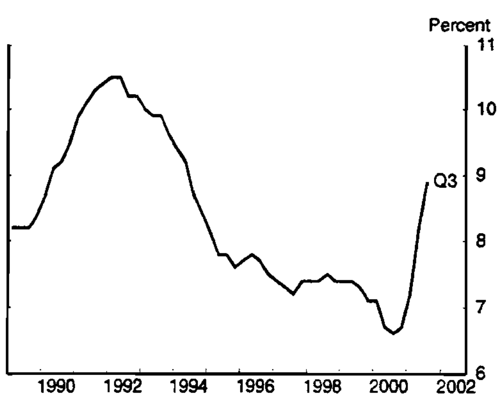
Change in Occupied Space




Source. Torto Wheaton Research.

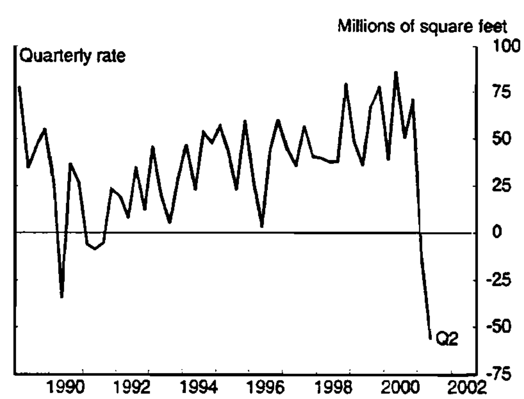
### Industrial Buildings

Vacancy Rate




Source. Torto Wheaton Research.

Change in Occupied Space




Source. Torto Wheaton Research.

Business demand for motor vehicles is expected to plunge this quarter. Fleet sales have been hit hard by the effects of the terrorist attacks. In particular, demand from rental car companies has plummeted as airline travel for both business and personal use has fallen dramatically. In addition, consumer leases, which are included in business spending and are not eligible for the special financing packages, are expected to drop sharply as consumers, instead, take advantage of the latest purchasing incentives. Meanwhile, orders for medium and heavy trucks remain depressed, and backlogs are quite low. These factors, along with concerns about the overall economy in the aftermath of the events of September 11, suggest that declines in sales of medium and heavy trucks, which began in late 1999, will continue in the near term.

**Nonresidential construction.** Real outlays for nonresidential construction were reported to have decreased at an annual rate of 12 percent in the third quarter, about the same rate of decline as in the second quarter. However, the published data were boosted by the lease of the World Trade Center (WTC) in July from the Port Authority of New York to two private companies; excluding this special factor, private construction spending would have shown a decline of 25 percent last quarter.[16] The July and August data for construction spending suggest that the declines were most likely a reflection of an accelerating contraction in expenditures for office buildings and other commercial structures. The vacancy rate for office buildings rose to 12.3 percent in the third quarter from 10.8 percent in the second quarter, a level that is still fairly moderate by historical standards.[17]

For industrial structures, the data on construction spending suggest that expenditures fell in the third quarter, although the rate of decline appeared to be smaller than the 18 percent annual rate observed in the second quarter. The vacancy rate for industrial buildings increased from 8.2 percent in the second quarter to 8.9 percent in the third quarter, which is the highest level since mid-1994.

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16. The WTC was leased for 99 years—longer than the life of the asset—and was therefore treated by BEA as a sale in the NIPAs. The boost to nonresidential investment spending was offset by a reduction in spending by state and local governments and had no effect on GDP.

17. Great uncertainties remain in the market for office space in New York City. Recently, a number of large tenants moved outside the Wall Street area in an effort to resume normal operations as quickly as possible. Their longer-term locations probably are also in doubt, especially given the reduced premium on centralized operations resulting from technological developments in recent years. Some firms are reported to have been considering reductions in relatively expensive downtown office space before September 11, and increased consciousness of the risk of concentrated operations may reduce demand in that segment of the New York City market and perhaps in some other cities as well. The longer-term balancing of these crosscurrents affecting rents and property values remains highly uncertain.

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars; annual rate except as noted;
based on seasonally adjusted Census book value)

| Category | 2001 Q1 | 2001 Q2 | 2001 Q3 | 2001 July | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|
| Manufacturing and trade | -24.0 | -43.3 | n.a. | -72.2 | -12.8 | n.a. |
| Less wholesale and retail motor vehicles | -10.0 | -40.4 | n.a. | -88.0 | -17.2 | n.a. |
| Manufacturing | -11.9 | -34.4 | n.a. | -43.1 | -37.3 | n.a. |
| Less aircraft and parts | -9.3 | -35.3 | n.a. | -43.6 | -38.2 | n.a. |
| Merchant wholesalers | -5.0 | .2 | n.a. | -34.0 | -4.3 | n.a. |
| Less motor vehicles | -2.4 | 3.3 | n.a. | -33.0 | .3 | n.a. |
| Retail trade | -7.2 | -9.0 | n.a. | 4.9 | 28.8 | n.a. |
| Automotive dealers | -11.5 | .3 | n.a. | 16.9 | 9.0 | n.a. |
| Less automotive dealers | 4.3 | -9.3 | n.a. | -12.0 | 19.8 | n.a. |

SELECTED INVENTORY-SALES RATIOS IN MANUFACTURING AND TRADE
(Months' supply, based on seasonally adjusted Census book value)

| Category | 2001 Q1 | 2001 Q2 | 2001 Q3 | 2001 July | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|
| Manufacturing and trade | 1.42 | 1.42 | n.a. | 1.42 | 1.42 | n.a. |
| Less wholesale and retail motor vehicles | 1.38 | 1.38 | n.a. | 1.38 | 1.38 | n.a. |
| Manufacturing | 1.38 | 1.38 | n.a. | 1.38 | 1.38 | n.a. |
| Durables | 1.59 | 1.59 | 1.60 | 1.59 | 1.59 | 1.67 |
| Nondurables | 1.13 | 1.12 | n.a. | 1.13 | 1.12 | n.a. |
| Merchant wholesalers | 1.30 | 1.32 | n.a. | 1.31 | 1.30 | n.a. |
| Less motor vehicles | 1.28 | 1.31 | n.a. | 1.30 | 1.29 | n.a. |
| Durable goods | 1.62 | 1.61 | n.a. | 1.60 | 1.58 | n.a. |
| Nondurable goods | .97 | 1.03 | n.a. | 1.01 | 1.02 | n.a. |
| Retail trade | 1.59 | 1.56 | n.a. | 1.56 | 1.57 | n.a. |
| Less automotive dealers | 1.50 | 1.47 | n.a. | 1.47 | 1.47 | n.a. |
| Automotive dealers | 1.85 | 1.80 | n.a. | 1.81 | 1.82 | n.a. |
| General merchandise | 1.94 | 1.92 | n.a. | 1.90 | 1.92 | n.a. |
| Apparel | 2.41 | 2.41 | n.a. | 2.37 | 2.40 | n.a. |
| Food | .85 | .86 | n.a. | .85 | .85 | n.a. |

**Inventories**

According to the advance NIPA data, real private inventories were run off in the third quarter at a $12 billion annual rate, a similar rate of drawdown as in the first half of the year. A complete set of monthly book-value data is only available through August, and those data show that stocks continued to move lower, although not so rapidly as in July. The average annual rate of decline for the two months excluding motor vehicles, $52.6 billion, was a bit larger than the second-quarter decrease. However, the continued overall reduction masks a sharp increase in non-auto retail inventories in August, and overhangs persist in several industries, notably computers and electronics manufacturing. The sharp drop in September production points to a further inventory liquidation in that month, although some backup at the retail level appears likely.

The book value of manufacturers' inventories decreased at an annual rate of $37.3 billion in August, and the average decline for July and August, at $40.2 billion, was a bit larger than the runoff in the second quarter. In September, the book value of durable goods inventories, which make up about two-thirds of the total manufacturing stock, fell a little more rapidly than in August. Even so, with shipments off substantially in September, the inventory-shipments ratio for durable goods manufacturers increased; all major categories of durable goods now have ratios at the high end of the ranges seen in recent years.

The book value of wholesale inventories excluding motor vehicles was essentially unchanged in August after having fallen at an annual rate of $33 billion in July. The decline for the two months averaged $16 billion and follows a small accumulation in the second quarter. Sales at non-auto wholesalers rose 0.4 percent in August, and the inventory-sales ratio for the sector edged down to 1.29, which is still toward the high end of readings during the past two years.

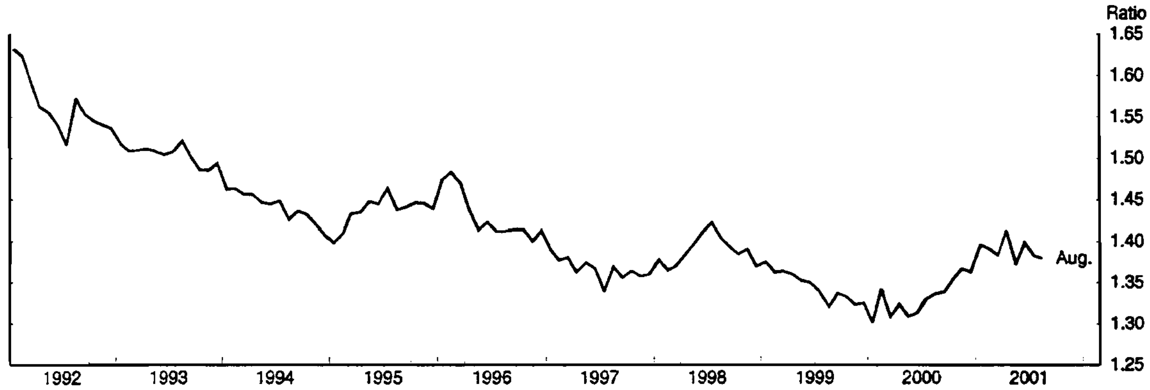
The book value of retail inventories excluding motor vehicles rose at an annual rate of $19.8 billion in August after having fallen at a $12 billion rate in July. Non-auto retail sales rose 0.5 percent in August, and the inventory-sales ratio for this sector held steady at 1.47, the low end of the range that has prevailed since early last year. Looking forward, the steep fall in retail sales in September suggests some unintended backup in stock building that likely will prompt further efforts at inventory reduction among retailers in the fourth quarter.

## Government Sector

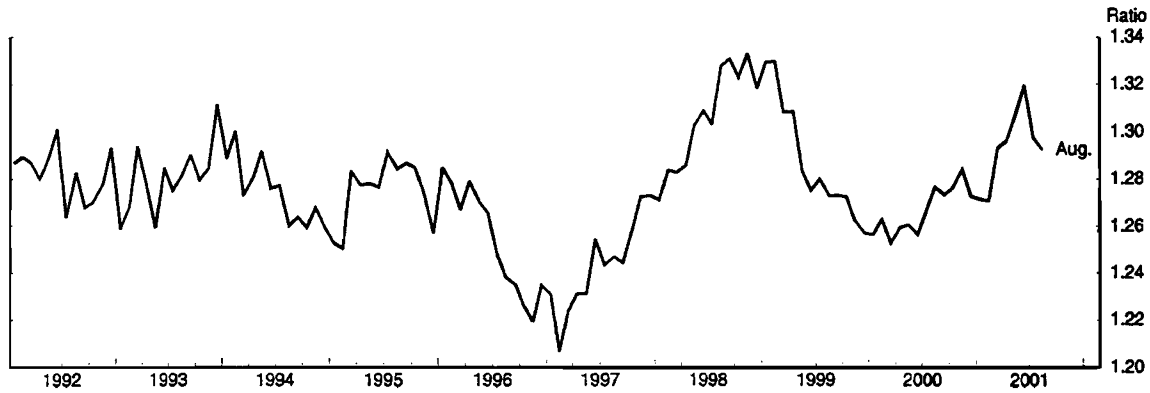
**Federal.** On October 24, the U.S. House of Representatives passed a fiscal stimulus package that reduces revenues about $100 billion in fiscal 2002 and an additional $60 billion over the following nine years. Key provisions include an

## Inventory-Sales Ratios
(Seasonally adjusted book value)

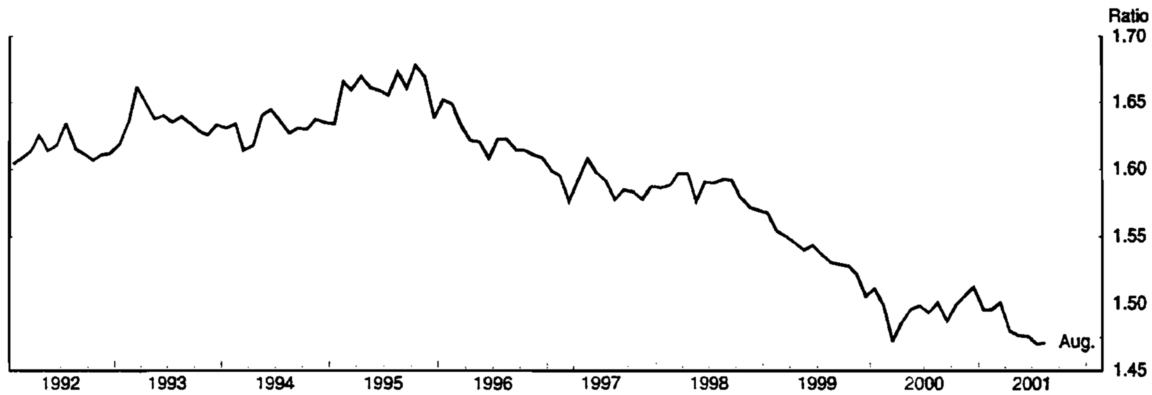
Manufacturing




Wholesale Trade Excluding Motor Vehicles




Retail Trade Excluding Motor Vehicles



investment depreciation bonus, elimination of the corporate alternative minimum tax, accelerated implementation of recently enacted tax cuts, and additional tax rebate checks. In the Senate, Finance Committee Chairman Baucus has proposed $35 billion in tax cuts for fiscal 2002, split between businesses and individuals, and $35 billion in additional spending on unemployment insurance and health care. Separately, Senate Appropriations Committee Chairman Byrd has proposed $20 billion in additional spending over several years. How the Congress will resolve the substantial differences in these bills remains unclear.

Final passage of the thirteen regular appropriations bills has been slow this year. However, the House and Senate have agreed on spending levels and are in the process of ironing out other policy differences. The congressional spending target is $6 billion (or 1 percent) above the President's August budget request; the extra money is dedicated to education grants and the Federal Emergency Management Agency.

According to the September Monthly Treasury Statement, federal unified budget receipts dropped nearly 30 percent below last year's level, with most of the decline reflecting policy changes.[18] The surplus for fiscal 2001 as a whole was $127 billion, the second highest in history but well below the fiscal 2000 record of $237 billion. Receipts dropped 2 percent in fiscal 2001, the first decline since 1983, reflecting, in part, the effects of the tax act. But even excluding the tax law changes, we estimate that receipts would have risen only 1 percent, a rate still well below the growth of nominal GDP. Fiscal 2001 outlays rose 5 percent after accounting for timing shifts and the effects of spectrum auction sales and subsidies.

**State and local governments.** Real purchases by state and local governments were reported to have increased at an annual rate of just 0.4 percent in the third quarter after rising at a 6.5 percent average pace during the first two quarters of the year. However, excluding BEA's treatment of the July lease of the WTC, real state and local purchases rose at an annual rate of 4.5 percent last quarter. Within consumption, the pace of growth in both compensation and other services was boosted a bit in the wake of the September 11 attacks: The increases reflect overtime put in by police, firemen, and sanitation workers and contracts for debris removal at the site of the WTC in New York.

18. Refunds were boosted by $11 billion from the final tranche of the rebate checks; withheld income taxes were held down a bit because of the lower withholding rates; and nonwithheld income tax payments were depressed by the extension of filing deadlines for those affected by the terrorist attacks. In addition, corporate payments were reduced approximately $25 billion because most corporations took advantage of the extension of the deadline to file estimated payments (from September 17 to October 1 generally, and to January for those firms affected by the terrorist attacks).

## Federal Government Receipts and Outlays

(Unified basis; billions of dollars)

| Function or Source | September 2000 | September 2001 | September Percent change | 12 months ending in Sept. 2000 | 12 months ending in Sept. 2001 | 12 months ending in Sept. Percent change |
|---|---|---|---|---|---|---|
| Outlays | 153.7 | 123.1 | -19.9 | 1,788.1 | 1,863.0 | 4.2 |
| Deposit insurance | -0.2 | -0.1 | ... | -3.1 | -1.5 | ... |
| Spectrum auctions | 0.0 | 12.4 | ... | -0.2 | -1.0 | ... |
| Sale of major assets | 0.0 | 0.0 | ... | 0.0 | 0.0 | ... |
| Other | 153.9 | 110.8 | -28.0 | 1,791.3 | 1,865.5 | 4.1 |
| Receipts | 219.5 | 158.5 | -27.8 | 2,025.0 | 1,990.2 | -1.7 |
| Surplus | 65.7 | 35.4 | ... | 236.9 | 127.2 | -46.3 |
| | Outlays excluding deposit insurance, spectrum auction, and sale of major assets are adjusted for payment timing shifts[1] | | | | | |
| Outlays | 147.2 | 146.9 | -0.2 | 1,784.2 | 1,869.8 | 4.8 |
| National defense | 25.7 | 26.7 | 4.0 | 291.3 | 307.4 | 5.5 |
| Net interest | 12.6 | 9.1 | -27.6 | 223.4 | 206.1 | -7.8 |
| Social security | 34.8 | 36.4 | 4.5 | 409.4 | 433.0 | 5.7 |
| Medicare | 15.5 | 18.6 | 19.8 | 197.1 | 214.7 | 8.9 |
| Medicaid | 10.5 | 10.5 | -0.3 | 117.9 | 129.4 | 9.7 |
| Other health | 3.1 | 3.6 | 18.1 | 36.3 | 42.5 | 17.2 |
| Income security | 17.7 | 18.3 | 3.4 | 245.0 | 265.8 | 8.5 |
| Agriculture | 6.8 | -1.1 | -116.8 | 38.5 | 28.3 | -26.3 |
| Other | 20.5 | 24.9 | 21.7 | 225.2 | 242.6 | 7.7 |
| Receipts | 219.5 | 158.5 | -27.8 | 2,025.0 | 1,990.2 | -1.7 |
| Individual income and payroll taxes | 159.7 | 136.4 | -14.6 | 1,620.1 | 1,651.1 | 1.9 |
| Withheld + FICA | 109.3 | 98.7 | -9.7 | 1,361.5 | 1,413.9 | 3.8 |
| Nonwithheld + SECA | 54.0 | 51.8 | -4.2 | 392.7 | 419.5 | 6.8 |
| Refunds (-) | 3.6 | 14.1 | 291.8 | 134.0 | 182.3 | 36.0 |
| Corporate | 43.4 | 7.5 | -82.8 | 207.3 | 151.1 | -27.1 |
| Gross | 46.2 | 9.5 | -79.4 | 235.7 | 186.7 | -20.8 |
| Refunds (-) | 2.7 | 2.1 | -25.1 | 28.4 | 35.7 | 25.7 |
| Other | 16.3 | 14.6 | -10.3 | 197.6 | 188.0 | -4.8 |
| Surplus | 72.3 | 11.6 | ... | 240.9 | 120.4 | -50.0 |

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

1. A shift in payment timing occurs when the first of the month falls on a weekend or holiday, or when the first three days of a month are nonworking days. Outlays for defense, social security, Medicare, income security, and "other" have been adjusted to account for these shifts.

... Not applicable.

As a result of the slowdown in economic activity over the past year, and the recent weakness in the tourism and related industries, around forty states have reported that revenues in the third quarter—the first quarter of the fiscal year for most states—came in below expectations. Many states will therefore be forced to make midyear adjustments to avoid budget deficits this year. Currently, most states seem to be focusing on spending cuts. For example, New York's governor has a plan that includes a hiring freeze for nonessential services, an early retirement incentive, and a freeze on department spending levels. In addition, many states will take money out of reserve funds to balance their budgets. So far, only a few states are considering tax hikes.

**Prices and Labor Costs**

**Prices.** With energy prices moderating, on balance, this past year, the twelve-month change in the consumer price index has slowed to the same rate recorded for the core consumer price index—2.6 percent over the twelve months ending in September. Abstracting from the effects of insurance payments following the events of September 11, we estimate that core PCE prices would have risen 1-1/2 percent over the twelve months to September. In contrast to the core CPI, this series has decelerated somewhat over the past year.

After having fallen sharply during the previous three months, the CPI for energy rebounded 2.6 percent in September. The price of motor fuel jumped last month, as several refinery disruptions in August and early September drove down inventories. These price increases appear to have been reversed recently, and survey data suggest that retail prices of gasoline dropped considerably in October, more than offsetting the September increase. The index for natural gas fell another 5.5 percent in September, bringing the measure nearly back to its year-earlier level; electricity rates declined as well. Overall energy prices in September were up only 1.5 percent from a year earlier compared with a rise of more than 15 percent during the preceding twelve-month period.

In September, the CPI excluding food and energy moved up 0.2 percent for the third consecutive month; these modest increases left the three-month change for this series at an annual rate of 2.4 percent, a rate similar to the increase over the second quarter and well below the bump that occurred in the first few months of this year. In September, the index for commodities other than food and energy increased 0.3 percent after having declined in August; the rise reflected a rebound in tobacco prices after a drop in August that reflected heavy discounting. Prices of core goods excluding tobacco only ticked up in September and have declined 1/2 percent over the past twelve months. Falling prices of durable goods continued to reflect weak demand and a strong dollar: In September, prices of audio and video equipment slid, and computer prices tumbled for a second month, bringing the twelve-month decline in the index to

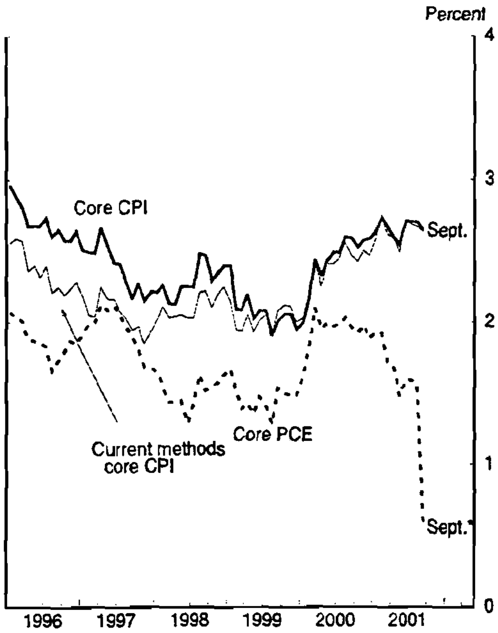
RECENT PRICE INDICATORS
(Percent)

| | From 12 months earlier | | From 3 months earlier | | 2001 | |
|---|---|---|---|---|---|---|
| | Sept. 2000 | Sept. 2001[1] | June 2001 | Sept. 2001 | Aug. | Sept.[1] |
| | | | -Annual rate- | | -Monthly rate- | |
| CPI | | | | | | |
| Total | 3.5 | 2.6 | 3.7 | 0.7 | 0.1 | 0.4 |
| Core | 2.6 | 2.6 | 2.6 | 2.4 | 0.2 | 0.2 |
| ex tobacco | 2.5 | 2.5 | 2.4 | 2.0 | 0.3 | 0.1 |
| Core commodities | 0.3 | 0.1 | -1.6 | 0.3 | -0.4 | 0.3 |
| ex tobacco | -0.2 | -0.5 | -2.5 | -1.1 | -0.2 | 0.1 |
| Core services | 3.5 | 3.8 | 4.5 | 3.1 | 0.5 | 0.1 |
| Current-methods | 3.4 | 2.6 | 3.7 | 0.7 | 0.1 | 0.4 |
| Core | 2.5 | 2.6 | 2.6 | 2.4 | 0.2 | 0.2 |
| ex tobacco | 2.4 | 2.5 | 2.4 | 2.0 | 0.3 | 0.1 |
| PCE Prices | | | | | | |
| Total | 2.7 | 0.9 | 1.6 | -2.2 | -0.0 | -0.5 |
| Core | 2.0 | 0.5 | 0.5 | -2.1 | 0.1 | -0.8 |
| ex tobacco | 1.9 | 0.4 | 0.3 | -2.4 | 0.1 | -0.9 |
| Core commodities | -0.4 | -1.0 | -2.3 | -0.8 | -0.5 | 0.2 |
| ex tobacco | -0.8 | -1.5 | -3.1 | -2.0 | -0.4 | -0.0 |
| Core services | 3.0 | 1.2 | 1.8 | -2.6 | 0.3 | -1.2 |
| Core market-based | 1.8 | 1.5 | 0.9 | 1.3 | 0.0 | 0.1 |
| Core nonmarket-based | 2.5 | -4.2 | -1.5 | -17.8 | 0.2 | -5.2 |
| PPI | | | | | | |
| Total finished goods | 3.5 | 1.6 | 0.3 | -0.8 | 0.4 | 0.4 |
| Core | 1.4 | 1.4 | 1.9 | 1.6 | -0.1 | 0.3 |
| ex tobacco | 1.4 | 0.8 | 0.8 | 1.7 | -0.1 | 0.3 |
| Core consumer goods | 1.5 | 1.8 | 2.3 | 1.8 | -0.1 | 0.4 |
| ex tobacco | 1.5 | 0.9 | 0.5 | 2.0 | -0.1 | 0.4 |
| Capital equipment | 1.4 | 0.6 | 1.2 | 1.1 | -0.1 | 0.1 |
| Core intermediate materials | 2.3 | -0.9 | -0.9 | -3.7 | -0.4 | -0.1 |
| Core crude materials | 2.7 | -10.1 | -13.7 | -6.0 | -0.8 | 0.2 |

1. PCE Prices for September are staff estimates.

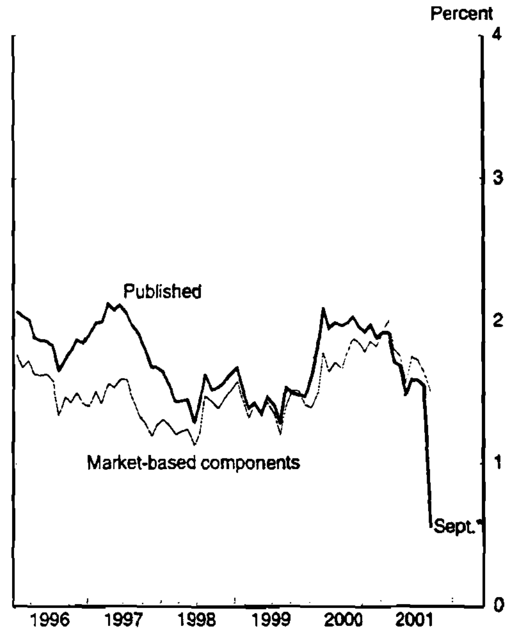
# Measures of Core Consumer Price Inflation
(12-month change except as noted)

CPI and PCE Excluding Food and Energy



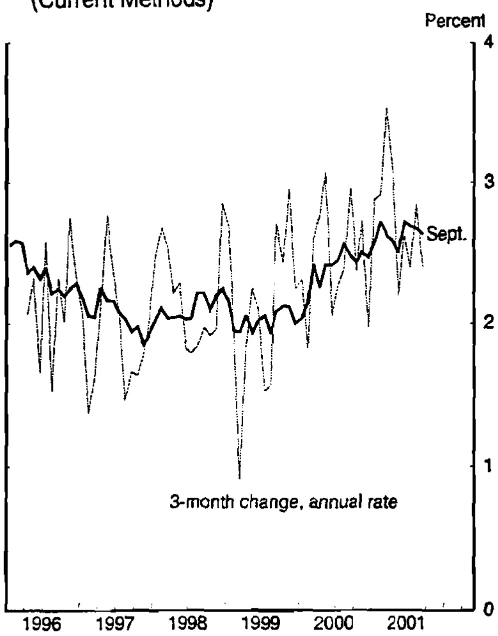

* Staff estimate

PCE Excluding Food and Energy

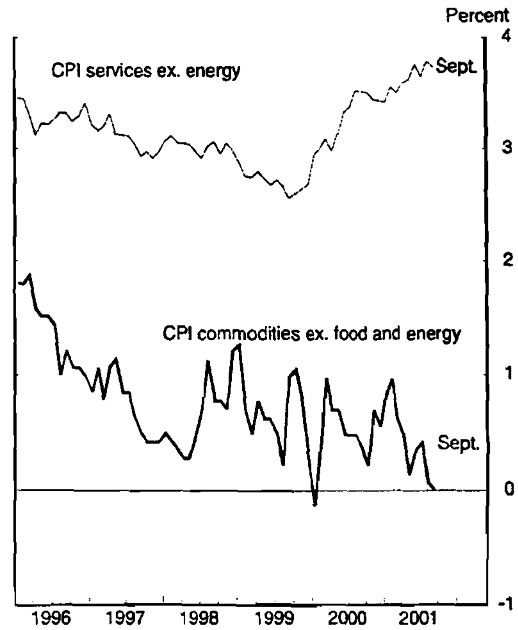



* Staff estimate

CPI Excluding Food and Energy
(Current Methods)




CPI Services and Commodities



BROAD MEASURES OF INFLATION
(4-quarter percent change)

| | 1998 Q3 | 1999 Q3 | 2000 Q3 | 2001 Q3 |
|---|---|---|---|---|
| Product prices | | | | |
| GDP chain price index | 1.2 | 1.4 | 2.4 | 2.3 |
| Less food and energy | 1.4 | 1.4 | 2.3 | 1.9 |
| Nonfarm business chain price index[1] | 0.8 | 1.0 | 2.1 | 1.8 |
| Expenditure prices | | | | |
| Gross domestic purchases chain price index | 0.8 | 1.6 | 2.7 | 1.3 |
| Less food and energy | 1.1 | 1.4 | 2.1 | 1.2 |
| PCE chain price index | 1.1 | 1.7 | 2.7 | 1.5 |
| Less food and energy | 1.5 | 1.4 | 2.0 | 1.2 |
| PCE chain price index, market-based components[2] | 0.9 | 1.7 | 2.7 | 2.0 |
| Less food and energy | 1.4 | 1.3 | 1.8 | 1.6 |
| CPI | 1.6 | 2.3 | 3.5 | 2.7 |
| Less food and energy | 2.3 | 2.0 | 2.6 | 2.7 |
| Current-methods CPI | 1.3 | 2.3 | 3.4 | 2.7 |
| Less food and energy | 2.1 | 2.0 | 2.5 | 2.7 |
| Median CPI | 3.0 | 2.4 | 2.8 | 3.7 |
| Trimmed mean CPI | 2.0 | 1.7 | 2.7 | 3.0 |

1. Excluding housing.
2. Values for 2001:Q3 are staff estimates.

SURVEYS OF (CPI) INFLATION EXPECTATIONS
(Percent)

| | Actual inflation[1] | University of Michigan: 1 year Mean[2] | University of Michigan: 1 year Median[2] | University of Michigan: 5 to 10 years Mean[3] | University of Michigan: 5 to 10 years Median[3] | Professional forecasters (10-year)[4] |
|---|---|---|---|---|---|---|
| 1999-Q4 | 2.6 | 3.5 | 2.9 | 3.3 | 2.9 | 2.5 |
| 2000-Q1 | 3.2 | 3.6 | 3.0 | 3.5 | 3.0 | 2.5 |
| Q2 | 3.3 | 3.5 | 3.0 | 3.3 | 2.8 | 2.5 |
| Q3 | 3.5 | 3.6 | 2.9 | 3.4 | 2.9 | 2.5 |
| Q4 | 3.4 | 3.8 | 3.0 | 3.7 | 3.0 | 2.5 |
| 2001-Q1 | 3.4 | 3.4 | 2.9 | 3.6 | 3.0 | 2.5 |
| Q2 | 3.4 | 3.9 | 3.1 | 3.6 | 3.0 | 2.5 |
| Q3 | 2.7 | 3.1 | 2.7 | 3.5 | 2.9 | 2.5 |
| July | 2.7 | 3.0 | 2.6 | 3.4 | 2.9 | |
| Aug. | 2.7 | 3.1 | 2.7 | 3.6 | 3.0 | |
| Sept. | 2.6 | 3.2 | 2.8 | 3.4 | 2.9 | 2.5 |
| Oct. | | 1.6 | 1.0 | 2.8 | 2.7 | |

1. CPI; percent change from the same period in the preceding year.
2. Responses to the question: By about what percent do you expect prices to go up, on the average, during the next 12 months?
3. Responses to the question: By about what percent per year do you expect prices to go up, on the average, during the next 5 to 10 years?
4. Compiled by the Federal Reserve Bank of Philadelphia.

about 31 percent. The index for new motor vehicles was unchanged in September and was down nearly 1 percent from a year earlier.[19]

The twelve-month change in the CPI for non-energy services—at 3.8 percent —is higher than a year earlier, mainly because of a pickup in owners' equivalent rent and tenants' rent. This upward trend in the services index appears to have eased recently, as the change over the past three months has fallen back from the rapid pace of the first half of 2001. Owners' equivalent rent increased only 0.2 percent in September, and the index for lodging away from home dropped 3.1 percent to a level more than 1 percent below its year-earlier level. Airfares declined further in September and were also lower than a year ago.

The core PCE price index apparently fell sharply in September reflecting BEA's treatment of insurance payments resulting from the events of September 11.[20] We expect this movement to be reversed in October. Even excluding this special factor, though, core PCE prices for both goods and services look to have decelerated over the past twelve months. The difference from the CPI reflects, in part, the wider scope of PCE, which includes a number of categories with non-market-based prices that have decelerated notably over the past year.

Prices for capital goods as measured by the PPI edged up in September, leaving the twelve-month change at 0.6 percent, less than half the rate recorded a year ago. The pace of computer price declines has picked up in recent months; over the twelve months ending in September, the PPI for computers has dropped a record 29 percent, nearly twice the rate of decline seen in the year-earlier period. Prices of most other capital goods have softened as well.

Turning to broader price indexes, the chain price index for GDP was affected by insurance adjustments to imported services and state and local government expenditures as well as to PCE.[21] Excluding the effects of all of these insurance adjustments, GDP prices would have increased 1.2 percent at an annual rate in the third quarter, considerably lower than the published increase of 2.1 percent. (As with PCE prices, we expect these effects on overall GDP prices to be reversed in the fourth quarter.) Over the past four quarters, we estimate that

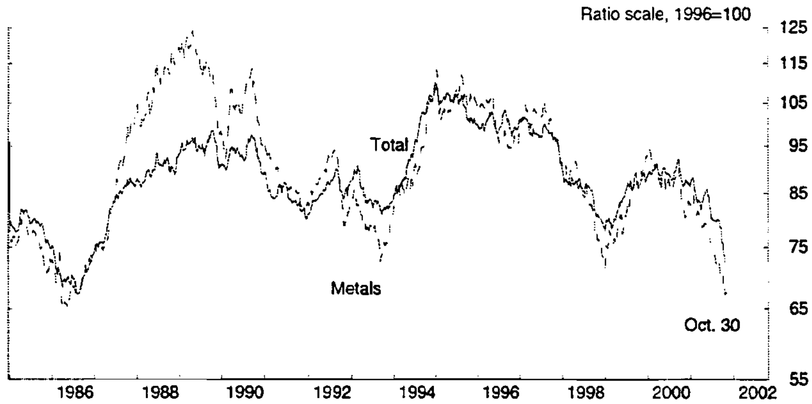
19. The September index did not reflect the recent financing incentives because finance charges are not included in the CPI.

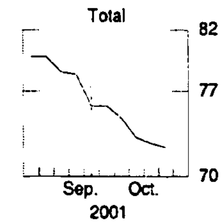
20. Payments for insurance claims worth $20.5 billion at an annual rate were subtracted from nominal consumption services, while real services were unaffected.

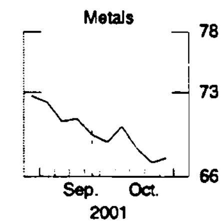
21. As with PCE, these insurance payments were subtracted from nominal services, while real services were unaffected. Because payments owed by foreign insurers exceed payments to be received by households or governments (with the remainder going to businesses and treated as intermediate inputs), the plunge in import prices had a larger effect on GDP prices than did the drop in consumer and government services inflation.

# Commodity Price Measures

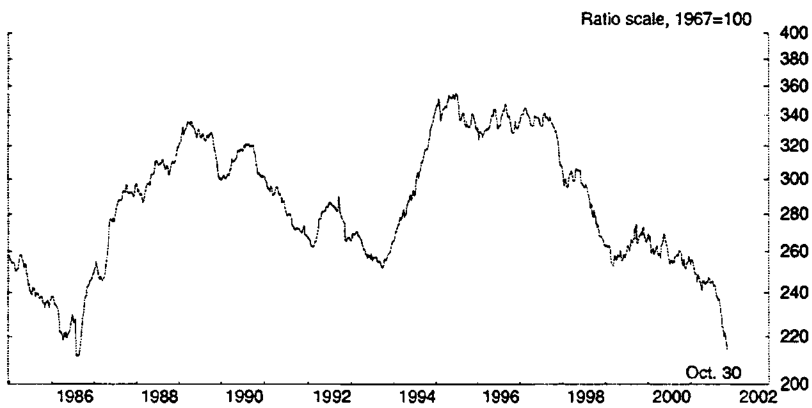
Journal of Commerce Index

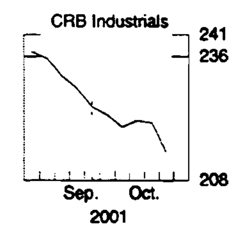


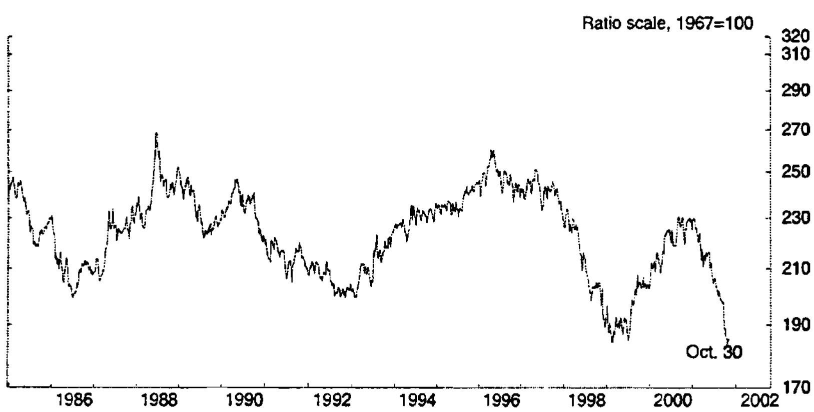



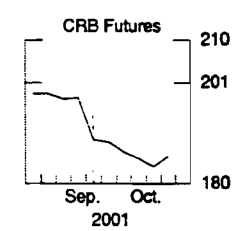

CRB Spot Industrials




CRB Futures




Note. Weekly data, Tuesdays. Vertical lines on small panels indicate week of last Greenbook. The Journal of Commerce index is based almost entirely on industrial commodities, with a small weight given to energy commodities, and the CRB spot price index consists entirely of industrial commodities, excluding energy. The CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities, and precious metals. Copyright for Journal of Commerce data is held by CIBCR, 1994.

SPOT PRICES OF SELECTED COMMODITIES

| | Current price (dollars) | 1999 | 2000 | Dec. 26 to Sept. 25[2] | Sept. 25[2] to Oct. 30 | Memo: Year earlier to date |
|---|---|---|---|---|---|---|
| | | Percent change[1] | | | | |
| **Metals** | | | | | | |
| Copper (lb.) | 0.670 | 26.1 | 3.4 | -24.2 | -2.9 | -24.7 |
| Steel scrap (ton) | 73.000 | 61.5 | -32.7 | 0.4 | -8.0 | -10.6 |
| Aluminum, London (lb.) | 0.576 | 27.7 | -0.8 | -15.3 | -3.7 | -13.5 |
| **Precious metals** | | | | | | |
| Gold (oz.) | 280.400 | -1.6 | -5.7 | 5.0 | -2.6 | 6.0 |
| Silver (oz.) | 4.265 | 5.5 | -10.9 | -2.2 | -6.6 | -10.8 |
| **Forest products[3]** | | | | | | |
| Lumber (m. bdft.) | 205.000 | 8.3 | -44.6 | 56.7 | -27.3 | 3.5 |
| Plywood (m. sqft.) | 280.000 | -3.2 | -8.2 | 13.6 | -11.9 | -4.1 |
| **Petroleum** | | | | | | |
| Crude oil (barrel) | 20.340 | 163.3 | -13.0 | -10.1 | 1.8 | -32.8 |
| Gasoline (gal.) | 0.550 | 132.9 | 5.2 | -15.8 | -11.0 | -40.5 |
| Fuel oil (gal.) | 0.614 | 140.7 | 34.4 | -35.5 | 0.2 | -34.4 |
| **Livestock** | | | | | | |
| Steers (cwt.) | 64.870 | 15.7 | 13.2 | -12.7 | -3.5 | -7.3 |
| Hogs (cwt.) | 37.000 | 194.0 | 7.1 | 19.2 | -17.8 | 9.6 |
| Broilers (lb.) | 0.554 | -4.0 | -13.7 | 23.4 | -9.6 | -3.2 |
| **U.S. farm crops** | | | | | | |
| Corn (bu.) | 1.835 | -10.2 | 10.1 | -9.4 | -2.4 | -2.7 |
| Wheat (bu.) | 3.430 | -17.4 | 31.9 | -9.5 | 8.7 | 4.6 |
| Soybeans (bu.) | 4.120 | -17.6 | 10.8 | -10.1 | -6.8 | -7.2 |
| Cotton (lb.) | 0.263 | -20.9 | 27.0 | -43.9 | -20.0 | -56.3 |
| **Other foodstuffs** | | | | | | |
| Coffee (lb.) | 0.368 | 5.1 | -43.1 | -39.7 | -10.4 | -50.7 |
| **Memo:** | | | | | | |
| JOC Industrials | 72.400 | 11.0 | -1.5 | -12.7 | -4.5 | -16.4 |
| JOC Metals | 67.600 | 26.3 | -10.3 | -16.7 | -2.7 | -18.7 |
| CRB Futures | 185.680 | 7.8 | 12.1 | -17.4 | -1.8 | -15.3 |
| CRB Spot Industrials | 214.400 | -0.1 | -3.5 | -12.4 | -4.6 | -15.3 |

1. Changes, if not specified, are from the last week of the preceding year to the last week of the period indicated.
2. Week of the September Greenbook.
3. Reflects prices on the Friday before the date indicated.

GDP prices excluding insurance adjustments increased around 2 percent, about 1/4 percentage point less than the increase over the preceding year. Gross domestic purchases prices—also excluding insurance adjustments—decelerated by somewhat more than GDP prices, reflecting the moderation in energy prices over the past year.

At earlier stages of processing, the producer price index for core intermediate materials has fallen sharply in recent months after having risen earlier this year. Over the twelve months ending in September, this index declined nearly 1 percent, a marked turnaround from a 2.3 percent rise recorded during the previous twelve months. Meanwhile, the PPI for core crude materials dropped more than 10 percent over the past year. Indexes of industrial materials prices (such as those of the *Journal of Commerce* and the Commodity Research Bureau) have weakened further since the last Greenbook. Price declines have been widespread across commodities and have included prices of farm products, which have been reduced by bountiful harvests and weaker demand.

Inflation expectations from the University of Michigan survey fell considerably in October. The median expectation for inflation over the coming year plunged to 1 percent after having exceeded 2-1/2 percent for almost three years; this sudden decline is the largest in nearly twenty years. The mean of these expectations also fell sharply in October. Over a five- to ten-year horizon, the median expectations moved down to 2.7 percent after having fluctuated around 3 percent over the past two years.

**Labor costs.** Recent data point to a slower rate of increase in compensation costs. The ECI for hourly compensation of private industry workers rose 4 percent over the twelve months ended in September, down 0.6 percentage point from the year-earlier period. The slowdown occurred in both the wages and salaries and the benefits components. The deceleration in wages and salaries was centered in the manufacturing and construction industries and among sales workers in the service-producing industries, especially finance, insurance, and real estate. Within the benefits component, the twelve-month increases for paid leave, nonproduction bonuses, and retirement and savings contributions were smaller than their increases over the preceding year.[22] By contrast, employer costs for workers' compensation have accelerated sharply over the past year, and health-insurance costs rose at the same rapid pace of nearly 9 percent both this year and last. Recent surveys of private-sector companies suggest that employers' costs for health insurance may increase even more rapidly in 2002. In particular, the Hewitt Associates' survey of health care

22. With the exception of health insurance, the benefits detail is unpublished and is provided to us by the BLS on a confidential basis.

EMPLOYMENT COST INDEX OF HOURLY COMPENSATION
FOR PRIVATE INDUSTRY WORKERS

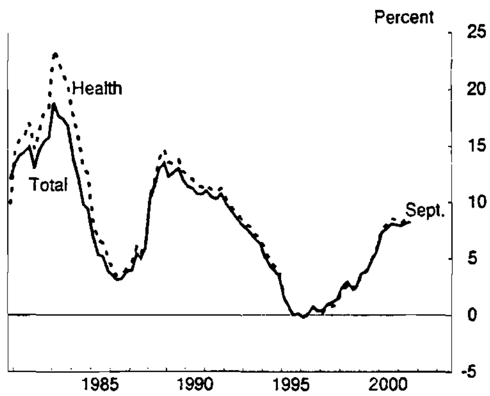
| | 2000 | | 2001 | | |
|---|---|---|---|---|---|
| | Sept. | Dec. | Mar. | June | Sept. |
| | -----Quarterly percent change------- (Compound annual rate) | | | | |
| Total hourly compensation[1] | 3.8 | 3.5 | 4.6 | 4.0 | 3.7 |
| Wages and salaries | 3.6 | 3.3 | 4.4 | 3.8 | 2.9 |
| Benefit costs | 5.0 | 4.4 | 5.9 | 3.8 | 5.5 |
| By industry | | | | | |
| Construction | 5.7 | 5.9 | 3.9 | 4.4 | 4.1 |
| Manufacturing | 3.9 | 2.2 | 4.6 | 3.2 | 2.1 |
| Trans., comm., and public utilities | 4.2 | 3.6 | 5.5 | 5.1 | 2.4 |
| Wholesale trade | 1.6 | 5.4 | 2.1 | 6.9 | 2.8 |
| Retail trade | 3.6 | 3.6 | 4.1 | 2.2 | 2.7 |
| FIRE | 5.6 | 1.3 | 5.8 | 4.1 | 3.6 |
| Services | 4.3 | 3.4 | 6.6 | 3.1 | 5.4 |
| By occupation | | | | | |
| White collar | 3.8 | 4.0 | 4.5 | 4.4 | 3.1 |
| Blue collar | 4.2 | 3.3 | 4.7 | 2.2 | 4.9 |
| Service occupations | 3.4 | 4.4 | 5.0 | 3.2 | 4.0 |
| Memo: | | | | | |
| State and local governments | 2.5 | 3.3 | 4.1 | 4.6 | 5.6 |
| | -----Twelve-month percent change---- | | | | |
| Total hourly compensation | 4.6 | 4.4 | 4.2 | 4.0 | 4.0 |
| Excluding sales workers | 4.6 | 4.4 | 4.4 | 4.2 | 4.1 |
| Wages and salaries | 4.1 | 3.9 | 3.8 | 3.8 | 3.6 |
| Excluding sales workers | 4.0 | 3.9 | 4.2 | 3.9 | 3.9 |
| Benefit costs | 6.0 | 5.6 | 5.0 | 4.8 | 4.9 |
| By industry | | | | | |
| Construction | 5.2 | 5.8 | 5.3 | 5.0 | 4.5 |
| Manufacturing | 4.6 | 4.0 | 3.6 | 3.5 | 3.1 |
| Trans., comm., and public utilities | 3.9 | 4.2 | 4.6 | 4.6 | 4.1 |
| Wholesale trade | 4.0 | 4.0 | 3.4 | 4.0 | 4.3 |
| Retail trade | 4.4 | 4.2 | 3.8 | 3.4 | 3.2 |
| FIRE | 5.1 | 5.0 | 3.9 | 4.2 | 3.7 |
| Services | 4.7 | 4.4 | 4.8 | 4.4 | 4.6 |
| By occupation | | | | | |
| White collar | 4.8 | 4.6 | 4.3 | 4.2 | 4.0 |
| Sales | 4.9 | 4.2 | 2.3 | 2.8 | 2.5 |
| Nonsales | 4.7 | 4.6 | 4.8 | 4.5 | 4.4 |
| Blue collar | 4.4 | 4.2 | 3.9 | 3.6 | 3.8 |
| Service occupations | 4.0 | 3.9 | 4.2 | 4.1 | 4.1 |
| Memo: | | | | | |
| State and local governments | 3.3 | 3.0 | 3.3 | 3.6 | 4.4 |

1. Seasonally adjusted by the BLS.

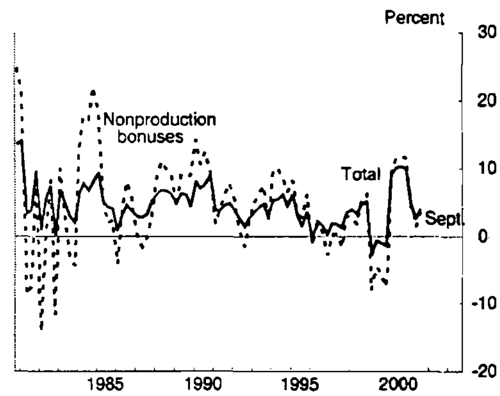
## Components of ECI Benefits Costs (CONFIDENTIAL)

(Private industry workers; 12-month change)

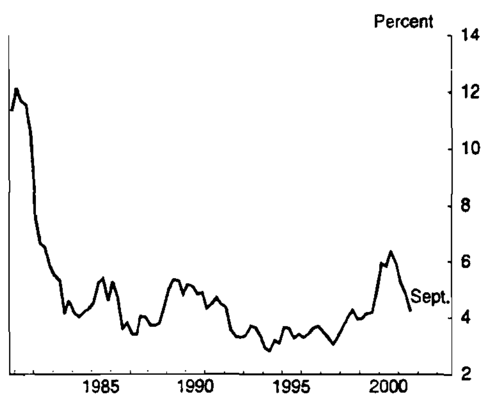
### Insurance Costs



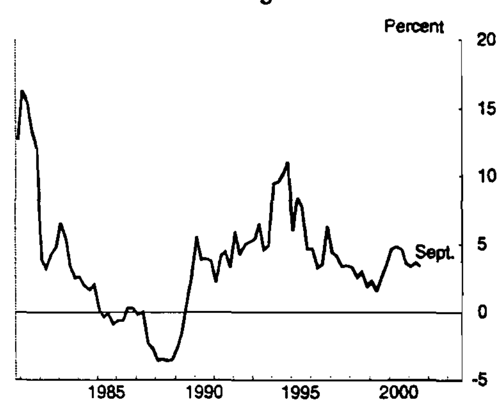

### Supplemental Pay



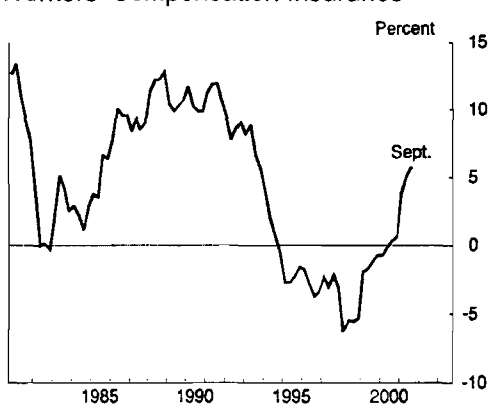

### Paid Leave



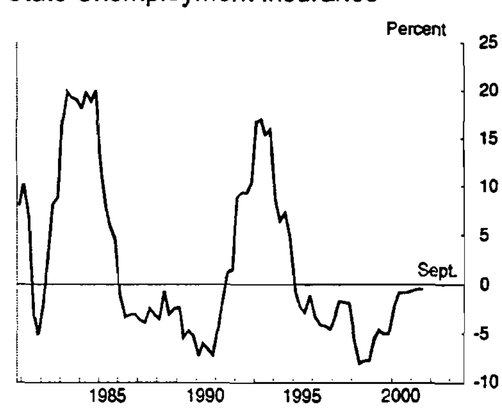

### Retirement and Savings




### Workers' Compensation Insurance




### State Unemployment Insurance




Note. Unpublished and confidential ECI benefits detail.

costs reports that the average increase expected for 2002 exceeds 15 percent compared with a 10.2 percent rise this year.

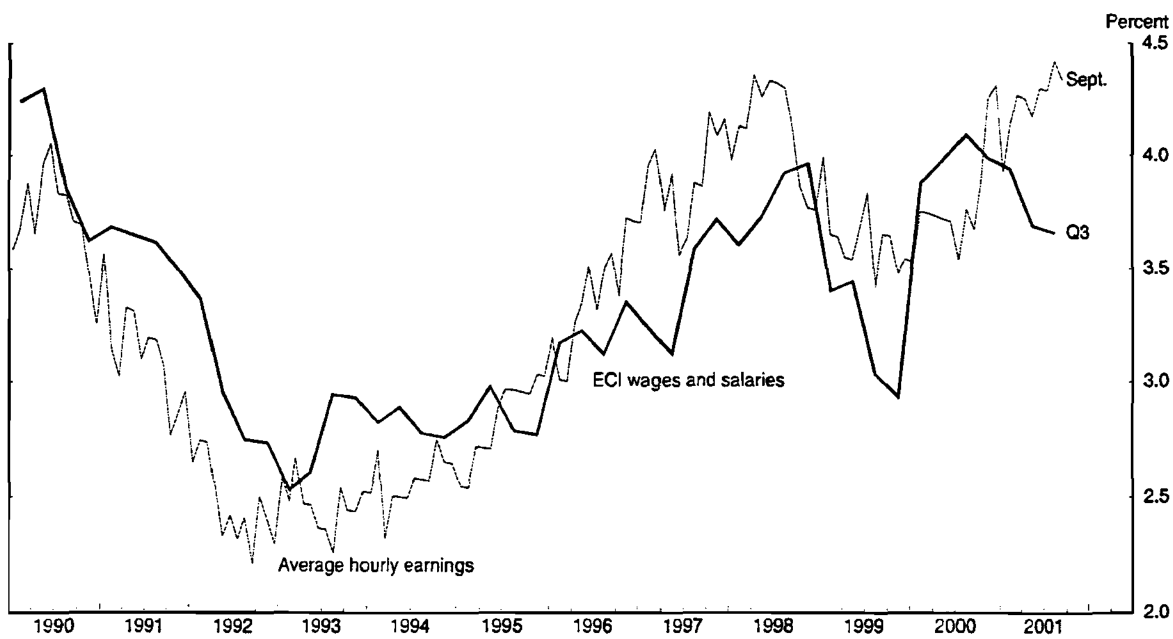
Average hourly earnings of production or nonsupervisory workers on private payrolls rose 0.2 percent in September after a 0.5 percent rise in August. Over the twelve months ending in September, average hourly earnings increased 4.3 percent. Although up from the year-earlier reading, this twelve-month change has held fairly steady for most of this year. By contrast, the ECI for wages and salaries of production or nonsupervisory workers—the ECI series that most closely corresponds to the average hourly earnings data—increased only 3.7 percent over the twelve months ending in September, down nearly 1/2 percentage point from the year-earlier pace.

Compensation per hour in the nonfarm business sector likely increased at an annual rate of only about 4 percent in the third quarter, down from a 4-3/4 percent average pace in the first half of this year. So far this year, the annual rate of change in nonfarm compensation per hour has exceeded the increase in the ECI by about 1/2 percentage point, a difference considerably more narrow than the 3 percentage point wedge recorded over the four quarters of 2000.

AVERAGE HOURLY EARNINGS
(Percent change; based on seasonally adjusted data)

| | 12-month percent change | | | Percent change to Sep 2001 from month indicated | | Percent change | |
|---|---|---|---|---|---|---|---|
| | Sept. 1999 | Sept. 2000 | Sept. 2001 | Mar. 2001 | June 2001 | Aug. 2001 | Sept. 2001 |
| | - - - - - - - - Annual rate- - - - - - - - - | | | | | -Monthly rate- | |
| Total private nonfarm | 3.6 | 3.7 | 4.3 | 3.8 | 3.7 | 0.5 | 0.2 |
| Manufacturing | 3.5 | 2.9 | 3.5 | 4.0 | 3.8 | 0.5 | 0.1 |
| Construction | 3.8 | 4.0 | 2.2 | 0.4 | 2.0 | 0.5 | 0.1 |
| Transportation and public utilities | 2.9 | 3.2 | 3.7 | 2.9 | 0.2 | 0.3 | -0.1 |
| Finance, insurance, and real estate | 3.8 | 3.3 | 5.7 | 5.7 | 4.9 | 0.5 | 0.4 |
| Retail trade | 3.7 | 4.1 | 3.4 | 2.9 | 1.2 | 0.2 | 0.0 |
| Wholesale trade | 3.7 | 4.3 | 4.2 | 3.7 | 2.8 | -0.1 | 0.9 |
| Services | 3.9 | 3.9 | 5.3 | 4.9 | 5.9 | 0.6 | 0.3 |

## Average Hourly Earnings for Production or Nonsupervisory Workers
(12-month change)



# Domestic Financial Developments

## Selected Financial Market Quotations

(One-day quotes in percent except as noted)

| Instrument | 2000 | 2001 | | | Change to Oct. 30 from selected dates (percentage points) | | |
|---|---|---|---|---|---|---|---|
| | June 26 | Sept. 10 | Oct. 1 | Oct. 30 | 2000 June 26 | 2001 Sept. 10 | 2001 Oct. 1 |
| *Short-term* | | | | | | | |
| FOMC intended federal funds rate | 6.50 | 3.50 | 3.00 | 2.50 | -4.00 | -1.00 | -.50 |
| Treasury bills [1] | | | | | | | |
| 3-month | 5.66 | 3.19 | 2.32 | 2.01 | -3.65 | -1.18 | -.31 |
| 6-month | 5.94 | 3.13 | 2.31 | 1.92 | -4.02 | -1.21 | -.39 |
| Commercial paper | | | | | | | |
| 1-month | 6.56 | 3.42 | 2.63 | 2.28 | -4.28 | -1.14 | -.35 |
| 3-month | 6.56 | 3.24 | 2.40 | 2.14 | -4.42 | -1.10 | -.26 |
| Large negotiable CDs [1] | | | | | | | |
| 1-month | 6.64 | 3.46 | 2.60 | 2.24 | -4.40 | -1.22 | -.36 |
| 3-month | 6.73 | 3.26 | 2.54 | 2.11 | -4.62 | -1.15 | -.43 |
| 6-month | 6.89 | 3.24 | 2.46 | 2.07 | -4.82 | -1.17 | -.39 |
| Eurodollar deposits [2] | | | | | | | |
| 1-month | 6.63 | 3.41 | 2.63 | 2.25 | -4.38 | -1.16 | -.38 |
| 3-month | 6.69 | 3.26 | 2.50 | 2.14 | -4.55 | -1.12 | -.36 |
| Bank prime rate | 9.50 | 6.50 | 6.00 | 5.50 | -4.00 | -1.00 | -.50 |
| *Intermediate- and long-term* | | | | | | | |
| U.S. Treasury [3] | | | | | | | |
| 2-year | 6.54 | 3.59 | 2.87 | 2.54 | -4.00 | -1.05 | -.33 |
| 10-year | 6.35 | 5.14 | 4.88 | 4.71 | -1.64 | -.43 | -.17 |
| 30-year | 6.22 | 5.55 | 5.48 | 5.30 | -.92 | -.25 | -.18 |
| U.S. Treasury 10-year indexed note | 4.09 | 3.26 | 3.14 | 3.03 | -1.06 | -.23 | -.11 |
| Municipal revenue (Bond Buyer) [4] | 5.99 | 5.25 | 5.41 | 5.35 | -.64 | .10 | -.06 |
| Private instruments | | | | | | | |
| 10-year swap | 7.38 | 5.62 | 5.25 | 5.09 | -2.29 | -.53 | -.16 |
| 10-year FNMA | 7.15 | 5.64 | 5.27 | 5.07 | -2.08 | -.57 | -.20 |
| 10-year AA [5] | 7.60 | 6.30 | 6.13 | 5.99 | -1.61 | -.31 | -.14 |
| 10-year BBB [5] | 8.49 | 7.08 | 7.07 | 6.94 | -1.55 | -.14 | -.13 |
| High yield [6] | 11.97 | 12.86 | 14.11 | 13.56 | 1.59 | .70 | -.55 |
| Home mortgages (FHLMC survey rate) [7] | | | | | | | |
| 30-year fixed | 8.14 | 6.89 | 6.72 | 6.64 | -1.50 | -.25 | -.08 |
| 1-year adjustable | 7.22 | 5.64 | 5.45 | 5.25 | -1.97 | -.39 | -.20 |

| Stock exchange index | Record high | | 2001 | | | Change to Oct. 30 from selected dates (percent) | | |
|---|---|---|---|---|---|---|---|---|
| | Level | Date | Sept. 10 | Oct. 1 | Oct. 30 | Record high | 2001 Sept. 10 | 2001 Oct. 1 |
| Dow-Jones Industrial | 11,723 | 1-14-00 | 9,606 | 8,837 | 9,122 | -22.19 | -5.03 | 3.23 |
| S&P 500 Composite | 1,527 | 3-24-00 | 1,093 | 1,039 | 1,060 | -30.62 | -3.00 | 2.05 |
| Nasdaq (OTC) | 5,049 | 3-10-00 | 1,695 | 1,480 | 1,667 | -66.97 | -1.65 | 12.63 |
| Russell 2000 | 606 | 3-9-00 | 441 | 398 | 423 | -30.24 | -4.06 | 6.35 |
| Wilshire 5000 | 14,752 | 3-24-00 | 10,104 | 9,518 | 9,778 | -33.71 | -3.23 | 2.73 |

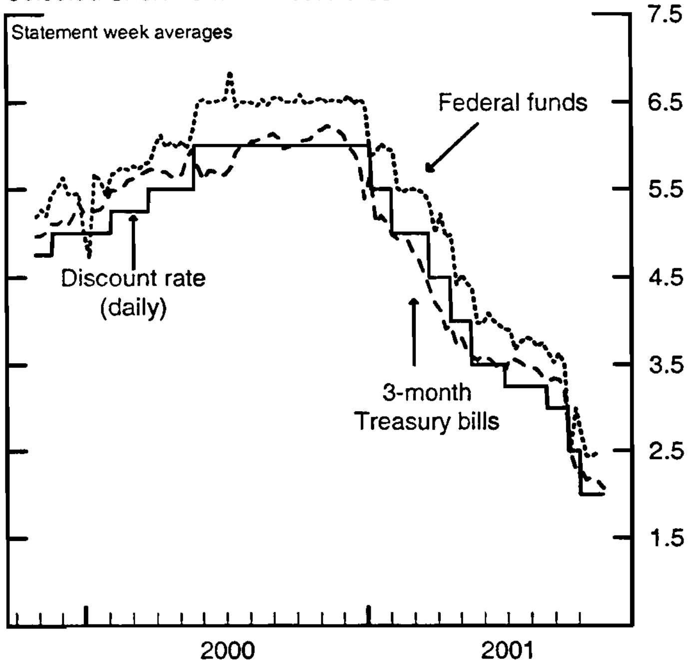
1. Secondary market.
2. Bid rates for Eurodollar deposits collected around 9:30 a.m. Eastern time.
3. Derived from a smoothed Treasury yield curve estimated using off-the-run securities.
4. Most recent Thursday quote.
5. Derived from smoothed corporate yield curves estimated using Merrill Lynch bond data.
6. Merrill Lynch 175 high-yield bond index composite.
7. For week ending Friday previous to date shown.

NOTES:

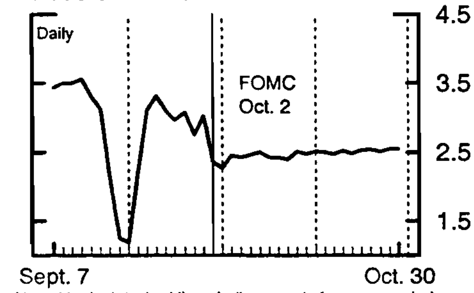
June 26, 2000 is the day before the FOMC meeting that ended the most recent period of policy tightening.
September 10, 2001 is the day before the terrorist attacks.
October 1, 2001 is the day before the most recent FOMC meeting.

# Selected Interest Rates

Selected Short-Term Interest Rates

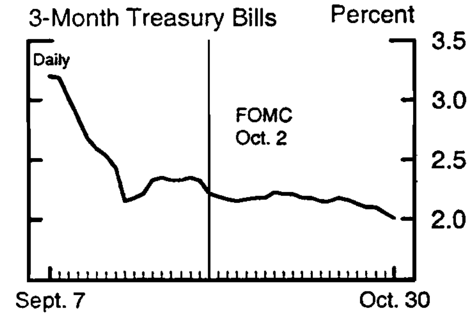



Federal Funds

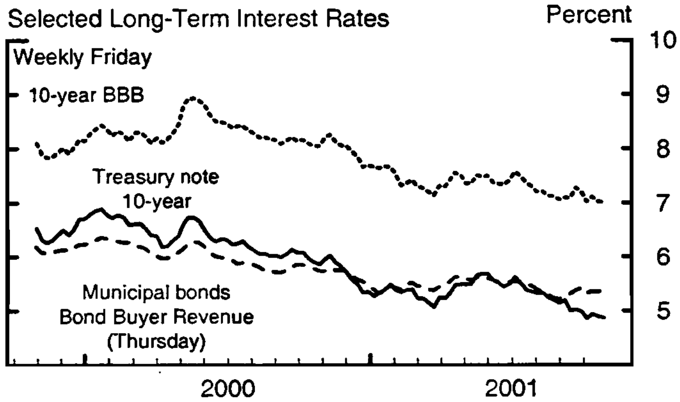


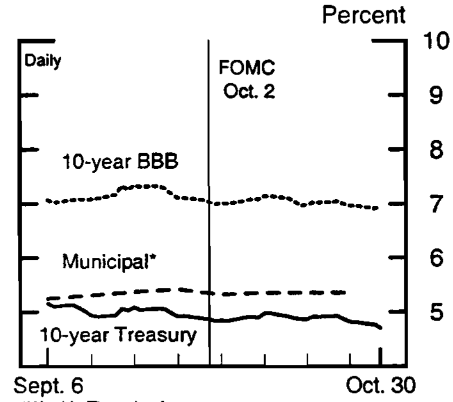

Note. Vertical dashed lines indicate end of reserve period.

3-Month Treasury Bills



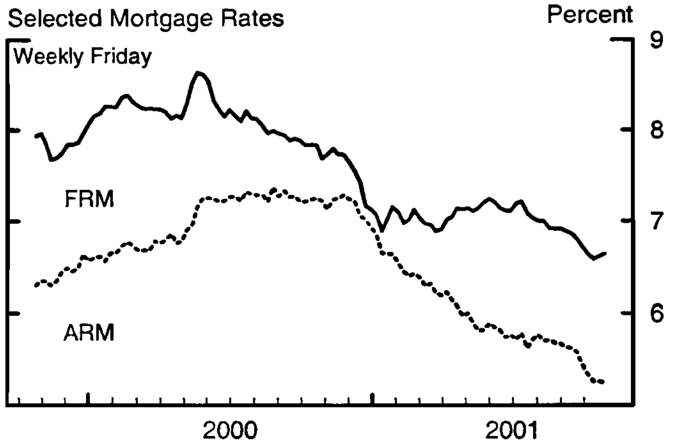

Selected Long-Term Interest Rates

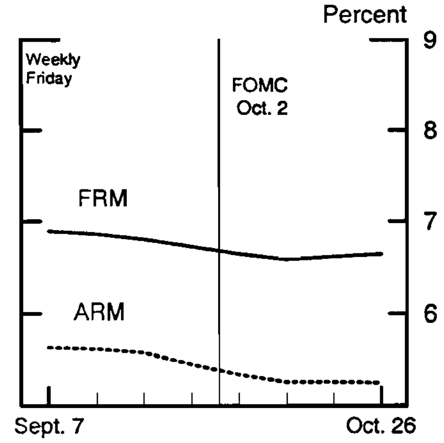



*Weekly Thursday frequency.

Selected Mortgage Rates



# Domestic Financial Developments

## Overview

The tenor of incoming data over the intermeeting period has been interpreted by market participants to be decidedly weak, prompting expectations of further monetary easings. As a result, interest rates have moved down. Despite bleak profits news and signs of deteriorating business credit quality, stock prices rallied during most of October—returning briefly to their pre-September 11 levels—before giving up some of these gains late in the month. The functioning of financial markets improved over the intermeeting period, with bid-asked spreads narrowing and trading volume increasing in a number of markets.

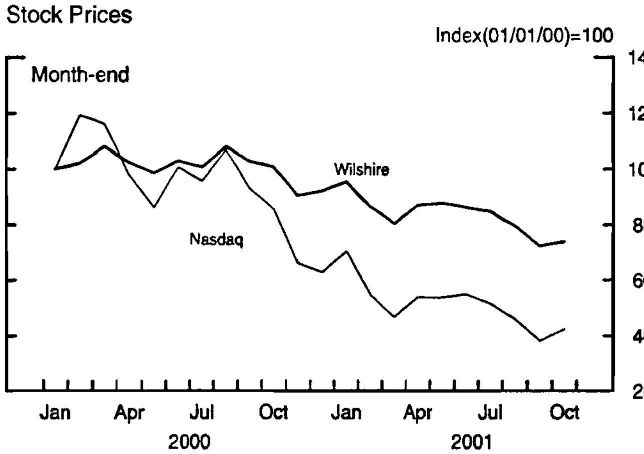
## Policy Expectations, Interest Rates, and Stock Prices

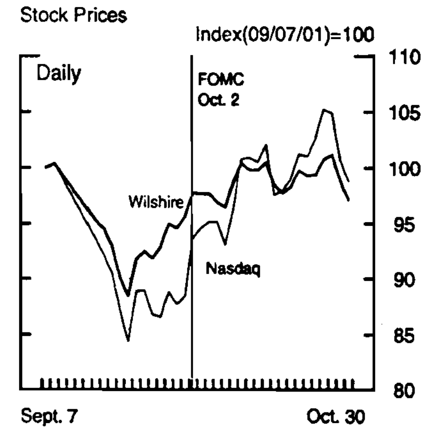
The FOMC's decision on October 2 to lower the target federal funds rate 50 basis points was largely anticipated and had relatively little effect on financial markets. Since then, deterioration in the economic outlook has heightened expectations of additional monetary easing over the balance of the year. Judging from current futures prices and surveys, market participants are certain of at least a 25 basis point reduction in the funds rate at the upcoming meeting, and they place about even odds on a 50 basis point cut. In addition, recent surveys suggest that investors anticipate that the Committee will continue to view the balance of risks as tilted toward economic weakness, at least through the January 2002 meeting. However, implied volatility from eurodollar contracts, while down a bit over the intermeeting period, remains quite elevated and indicates considerable uncertainty about the course of policy in the near term.

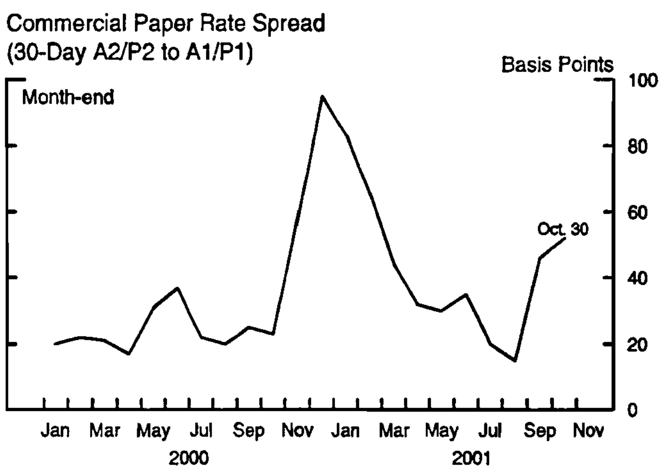
Treasury yields have moved down between 30 and 40 basis points at the short end of the maturity spectrum and 20 to 30 basis points at longer maturities.[1] Market participants have pointed to the likelihood of greater fiscal stimulus as a factor that has limited the decline in longer-term yields. Investment-grade private yields declined roughly in line with those on comparably dated Treasuries, but yields on speculative-grade debt dropped appreciably more. Although spreads on riskier debt have fallen from peaks after September 11, they remain about 3/4 percentage point above their pre-attack levels. In equity markets, the Wilshire 5000 index has risen 2-3/4 percent, on net, over the intermeeting period. On the perception that the tech sector may be bottoming out, prices of technology firms jumped sharply and lifted the Nasdaq about 12-1/2 percent.

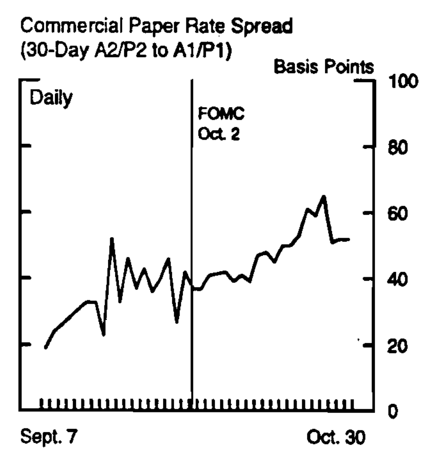
1. On October 31 (too late to be covered in Greenbook) the Treasury unexpectedly announced that it is suspending issuance of both nominal and inflation-indexed thirty-year bonds. Following the announcement, the yield on the thirty-year bond dropped sharply. Tables and charts in Greenbook do not reflect these rate movements.

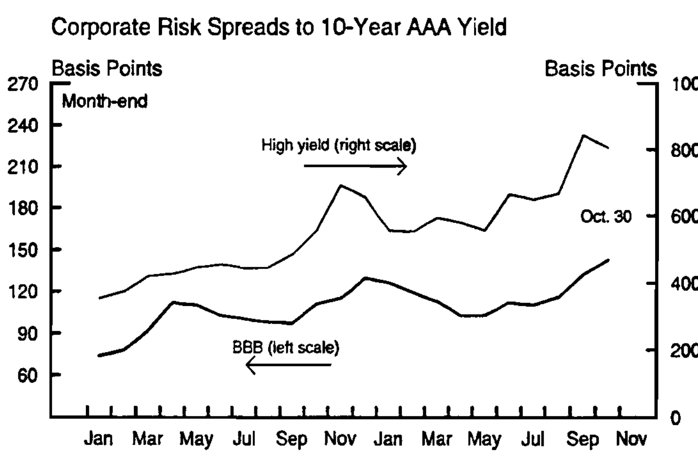
# Stock Prices and Risk Spreads

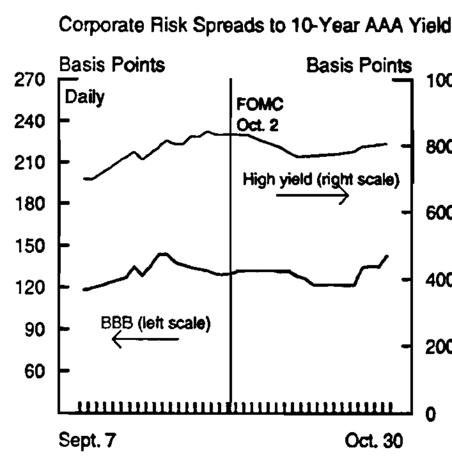


**Business Finance**

By late September, the corporate bond market had largely recovered from the disruptions associated with the terrorist attacks, and nonfinancial corporations sold nearly $18 billion of bonds in the last half of the month. The strong pace of investment-grade bond issuance was maintained in October, as firms continued taking advantage of low interest rates to retire existing long-term debt, to finance merger and acquisition activity, and to boost their holdings of liquid assets. Speculative-grade issuance, which all but ceased in September, returned to its modest summer pace, but investors continued to shun riskier issues.

Commercial paper rebounded after running off substantially in September. Some of the proceeds were apparently designated for merger and acquisition financing, while some reportedly were used to repay bank loans taken down in the aftermath of the terrorist attacks, likely contributing to the sharp contraction in business loans at commercial banks in October. According to the respondents to the Board's October senior loan officer survey, C&I loan demand slumped over the past three months, largely because of reduced investment spending. Moreover, a significant number of banks reported that they had tightened their commercial lending standards and terms. Even with the weakness in business loans, debt financing by nonfinancial firms, on net, in October is likely to surpass the strong first-half pace.

After stalling in September, public equity issuance regained some ground in October. The strong pickup in stock prices early in the month led to a number of seasoned equity issues by domestic nonfinancial firms, though initial public offerings remained at a near standstill. New filings have dropped, and with the cancellation of a large number of planned offerings, the number of firms slated to go public is now at a very low level relative to the norm of recent years. Venture capital investments contracted again in the third quarter to a level about one-quarter that of a year ago.

The SEC extended its temporary easing of restrictions on share repurchases through October 12, and reports from market contacts suggest that buyback activity was brisk throughout this period. Domestic cash-financed mergers remained relatively strong in the third quarter, and new deals continued to be announced. Although foreign acquisitions of U.S. companies have declined noticeably, on net, retirements of domestic equity are likely to remain sizable.

Corporate earnings reports for the third quarter have come in close to, or slightly ahead of, sharply reduced expectations among analysts. With about three-fourths of the S&P 500 firms having reported results for the third quarter, operating earnings per share are estimated to have fallen about 25 percent relative to a year ago. Results were particularly weak for the transportation and lodging sector, where earnings plunged 76 percent. In the technology and telecom sectors, earnings were also down sharply relative to a year ago,

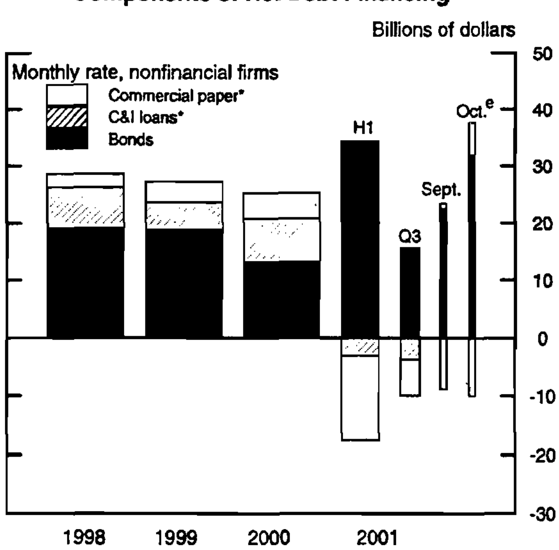
## Gross Issuance of Securities by U.S. Corporations
(Billions of dollars; monthly rates, not seasonally adjusted)

| Type of security | 1998 | 1999 | 2000 H1 | 2000 H2 | 2001 H1 | 2001 Q3 | Sept. | Oct.[e] |
|---|---|---|---|---|---|---|---|---|
| All U.S. corporations | 94.0 | 89.4 | 80.0 | 77.0 | 123.6 | 92.6 | 86.4 | n.a. |
| Stocks[1] | 10.6 | 11.0 | 14.1 | 8.4 | 10.5 | 7.2 | 5.1 | n.a. |
| Bonds | 83.5 | 78.4 | 65.9 | 68.6 | 113.1 | 85.4 | 81.3 | n.a. |
| *Nonfinancial corporations* | | | | | | | | |
| Stocks[1] | 6.2 | 9.2 | 12.4 | 7.3 | 7.5 | 3.3 | .1 | 3.5 |
| Initial public offerings | 2.2 | 4.2 | 5.7 | 3.1 | 3.2 | 1.0 | .0 | .5 |
| Seasoned offerings | 4.0 | 5.0 | 6.7 | 4.2 | 4.2 | 2.3 | .1 | 3.0 |
| Bonds[2] | 25.6 | 24.5 | 21.3 | 19.1 | 43.2 | 26.2 | 31.1 | 42.0 |
| Investment grade[3] | 14.1 | 13.9 | 11.5 | 12.4 | 28.9 | 20.9 | 27.1 | 35.0 |
| Speculative grade[3] | 10.2 | 7.5 | 5.4 | 3.7 | 11.9 | 3.8 | 1.2 | 6.5 |
| Other (sold abroad/unrated) | 1.3 | 3.1 | 4.4 | 3.1 | 2.4 | 1.5 | 2.8 | .5 |
| *Financial corporations* | | | | | | | | |
| Stocks[1] | 4.4 | 1.8 | 1.6 | 1.1 | 3.0 | 4.0 | 5.0 | n.a. |
| Bonds | 57.8 | 53.9 | 44.7 | 49.5 | 69.9 | 59.2 | 50.2 | n.a. |
| *Memo* | | | | | | | | |
| Net issuance of commercial paper, nonfinancial corporations[4] | 2.3 | 3.6 | 6.4 | 2.7 | -14.5 | -6.2 | -8.8 | 5.7 |
| Change in C&I loans at commercial banks[4] | 7.0 | 4.7 | 10.4 | 4.7 | -3.0 | -3.7 | .9 | -10.0 |

Note. Components may not sum to totals because of rounding. These data include speculative-grade bonds issued privately under Rule 144A. All other private placements are excluded. Total reflects gross proceeds rather than par value of original discount bonds.

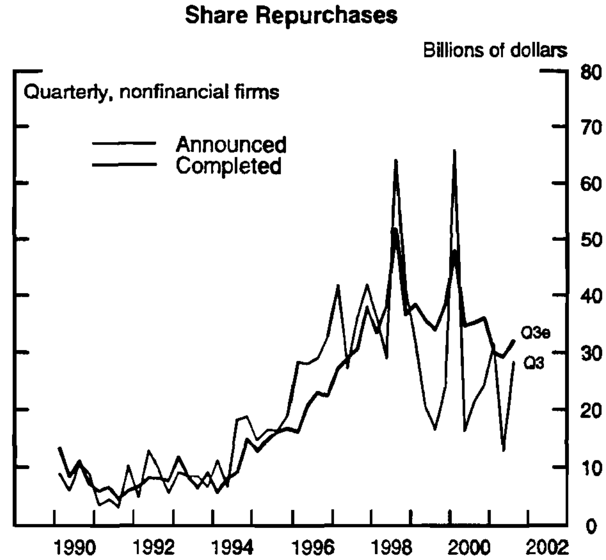
1. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings.
2. Excludes mortgage-backed and asset-backed bonds.
3. Bonds sold in U.S. categorized according to Moody's bond ratings, or to Standard Poor's if unrated by Moody's.
4. End-of-period basis, seasonally adjusted.
e Staff estimate.

### Components of Net Debt Financing




* Seasonally adjusted.
e Staff estimate.

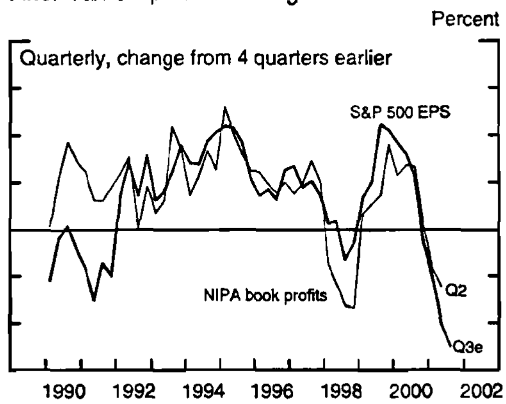
### Share Repurchases




Source. Compustat & Securities Data Company.
e Staff estimate.

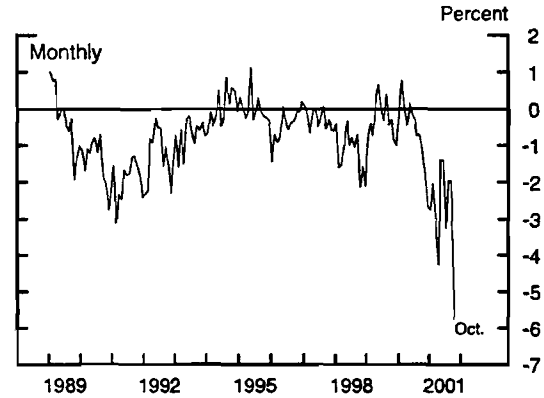
# Corporate Earnings and Credit Quality

## After-Tax Corporate Earnings



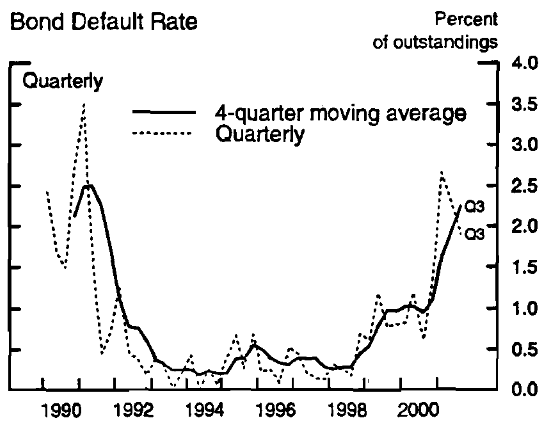

e Staff estimate.

## Revisions to S&P 500 Year-ahead Earnings



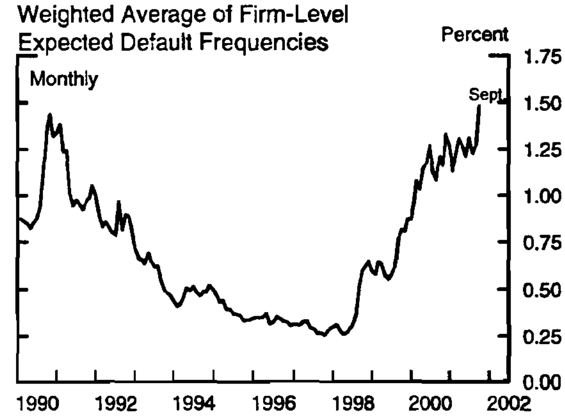

Source. I/B/E/S.

## Bond Default Rate




Source. Moody's.

## Weighted Average of Firm-Level Expected Default Frequencies




Source. KMV Corp.

## Downgrades by Sector, 2001*

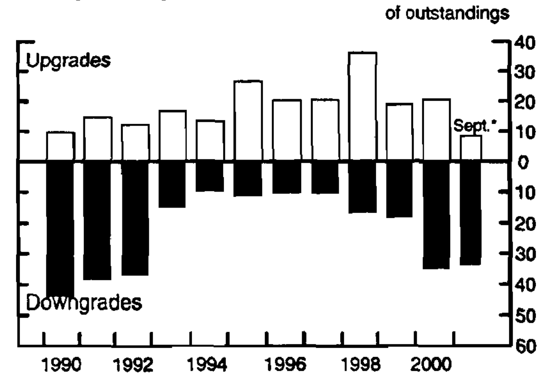
Percent of outstandings

Monthly rate

| | H1 | July-Aug. | Sept. |
|---|---|---|---|
| 1. Airlines | 2 | 1 | 81 |
| 2. Motor vehicles & parts | 9 | 2 | 0 |
| 3. Telecom | 5 | 8 | 3 |
| 4. Technology | 10 | 11 | 10 |
| 5. Other | 2 | 2 | 1 |
| TOTAL | 3 | 3 | 2 |

* Relative to par value at beginning of each period.
Source. Merrill Lynch.

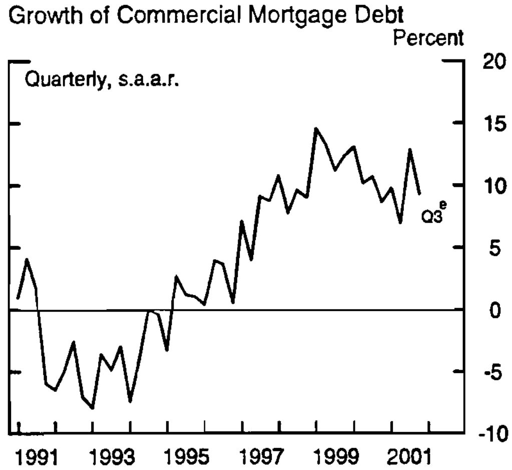
## Ratings Changes




*Year-to-date at an annual rate, with staff estimate for August and September.
Source. Moody's.

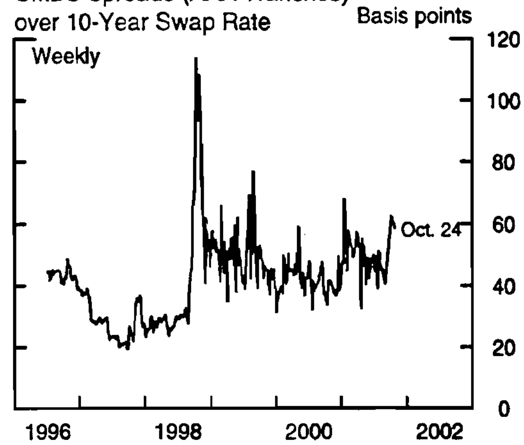
# Commercial Real Estate

Growth of Commercial Mortgage Debt



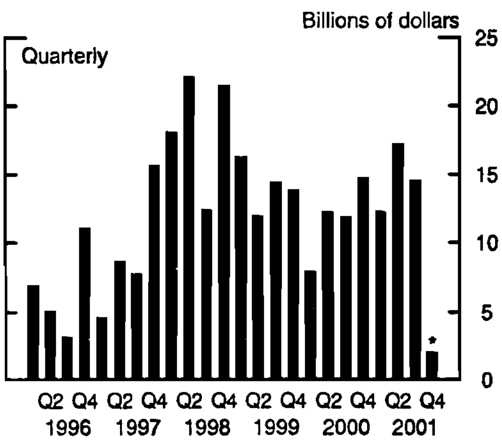

e. Staff estimate.

CMBS Spreads (AAA Tranches) over 10-Year Swap Rate



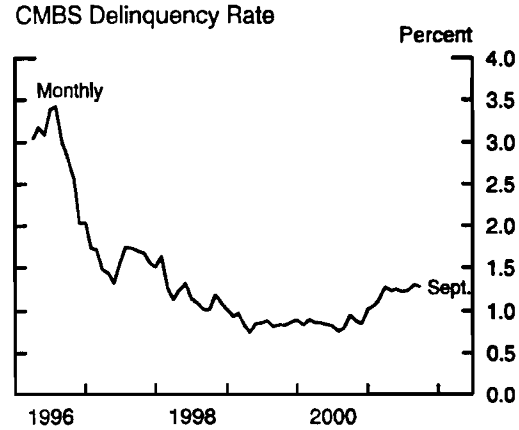

Source. Morgan Stanley.

Total CMBS Gross Issuance



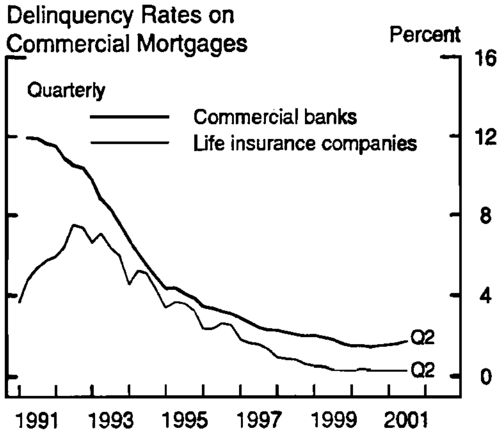

* Period to October 17, 2001.
Source. Commercial Mortgage Alert.

CMBS Delinquency Rate



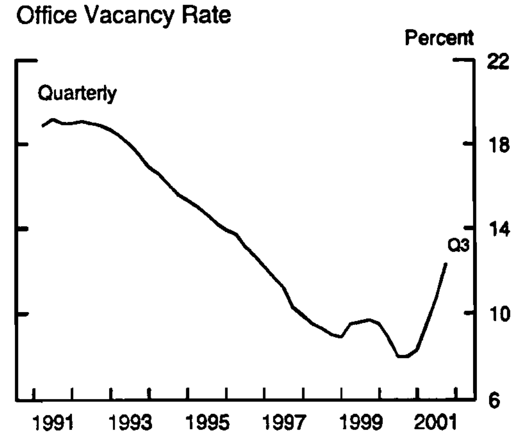

Source. Morgan Stanley.

Delinquency Rates on Commercial Mortgages




Source. ACLI, Call Report.

Office Vacancy Rate




Source. Torto Wheaton Research.

although the rate of decline appears to have slowed between the second and third quarters. Looking ahead, analysts have significantly scaled back their expectations for earnings growth next year, although they still anticipate a substantial rebound in the first half of 2002. Taken at face value, analysts' current forecasts imply a hefty 15 percent increase in earnings per share for the S&P 500 next year.

Measures of corporate credit quality continue to indicate a high degree of distress. Bond defaults remained at an elevated level in September, and model-based forecasts indicate that the default rate on bonds will continue to rise moderately over the next year. The number of ratings downgrades on corporate bonds was high in September, when 80 percent of all airline debt was downgraded. The pace of downgrades appears to have picked up significantly in October. Most notably, S&P downgraded the debt of GM and Ford (totaling $290 billion) from A to BBB+. In addition, a number of large businesses filed for bankruptcy over the past few weeks, including Polaroid and Bethlehem Steel.

Concerns about credit quality and ratings downgrades have led to a widening of spreads in the market for commercial paper. The spread of thirty-day A2/P2 paper over A1/P1 paper, which was running at typical levels of about 25 basis points before September 11, has jumped to 50 basis points. Because SEC regulations restrict the quantity of lower-tier paper that can be held by money funds, the downgrades of GM, Ford, and Disney to lower-tier status, along with expectations of other downgrades, are putting some strain on the market.

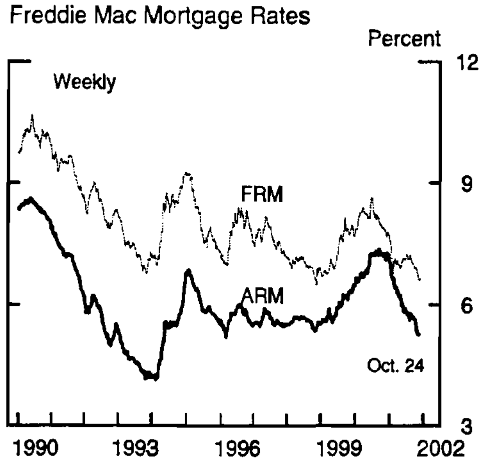
Despite pronounced weakness in nonresidential construction, the expansion of commercial mortgage debt appears to have been well maintained in the third quarter, although growth is estimated to have decelerated to an annual rate of about 9-1/4 percent. The market for commercial-mortgage-backed securities (CMBS) remained strong in September, with large volumes of issuance spurred by the low rates. The spread of investment-grade CMBS yields over swaps narrowed slightly in October after climbing 20 to 30 basis points in the week of September 11. The most recent reading on the CMBS delinquency rate for September remained low, indicating little change in commercial real estate credit quality. However, the market for office space continued to soften, as office vacancy rates rose a good bit further in the third quarter, and a significant number of loan officers reported that they had tightened lending standards on commercial real estate loans over the past three months.

**Household Finance**

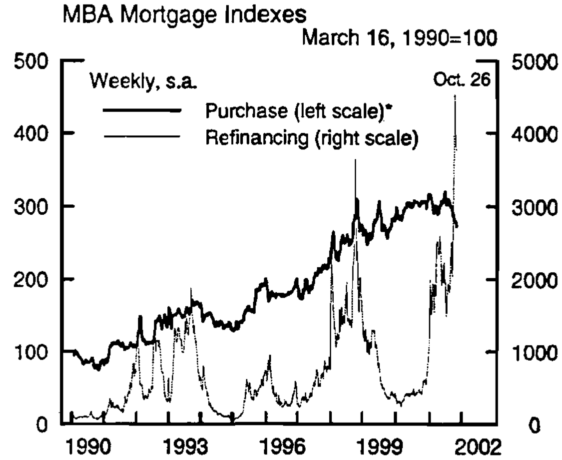
Mortgage rates have edged lower since the October FOMC meeting, with the average rate on thirty-year fixed-rate mortgages dropping to about 6.6 percent, its low of the past twenty years. The cumulative decline in mortgage rates has ignited a refinancing boom and has boosted the Mortgage Bankers Association

## Household Liabilities

Freddie Mac Mortgage Rates

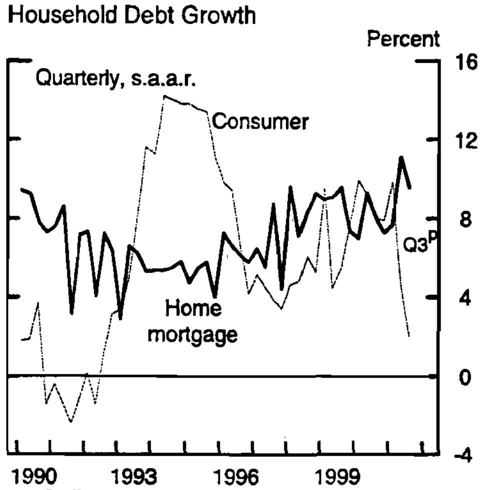



MBA Mortgage Indexes



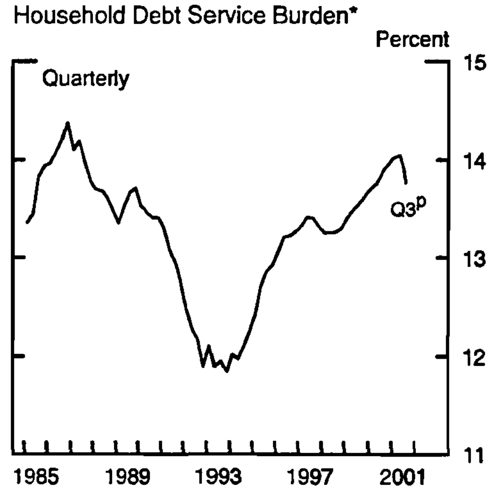

* 4-week moving average.

Household Debt Growth



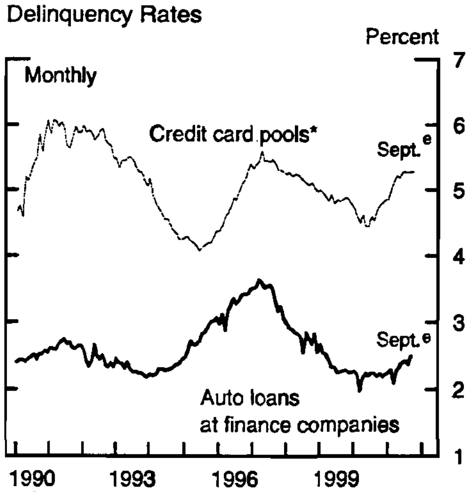

p. Staff projection.

Household Debt Service Burden*



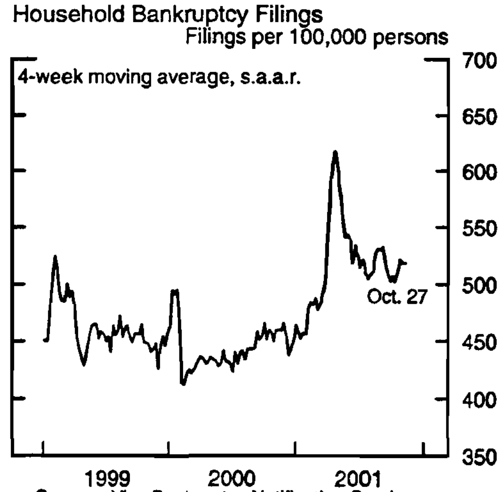

*Required debt payments relative to disposable personal income.

Delinquency Rates




* Securitized receivables (Moody's, seasonally adjusted).
e. Staff estimate.

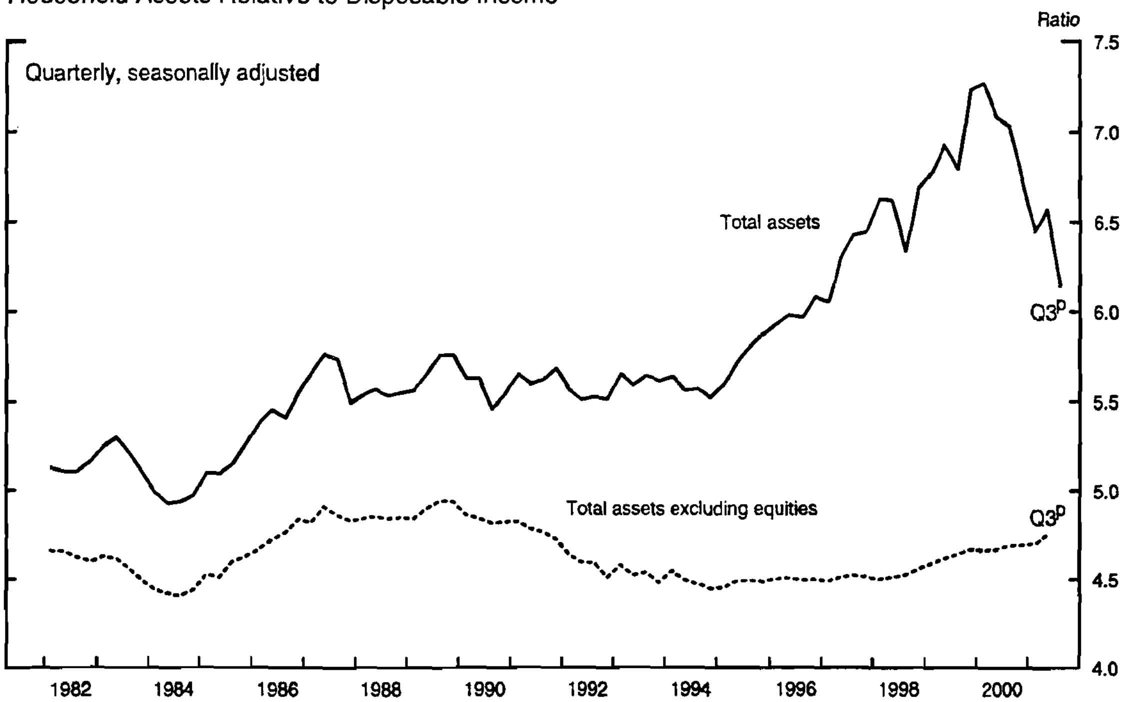
Household Bankruptcy Filings




Source. Visa Bankruptcy Notification Service.

## Household Assets

Household Assets Relative to Disposable Income




p. Staff projection.

### Net Flows into Long-Term Mutual Funds

(Excluding reinvested dividends; billions of dollars, monthly rates.)

| | 1999 | 2000 | 2001 H1 | 2001 Aug. | 2001 Sept. | 2001 Oct. e | Assets Sept. |
|---|---|---|---|---|---|---|---|
| **Total long-term funds** | **14.2** | **18.4** | **15.2** | **11.2** | **-23.1** | **16.5** | **4,254** |
| **Equity funds** | **15.7** | **25.1** | **8.3** | **-4.8** | **-29.5** | **1.7** | **3,020** |
| Domestic | 14.8 | 21.2 | 9.2 | -1.3 | -27.0 | 4.9 | 2,627 |
| Capital appreciation | 13.5 | 25.5 | 5.3 | -4.1 | -21.0 | 1.5 | 1,548 |
| Total return | 1.4 | -4.3 | 3.9 | 2.8 | -6.1 | 3.4 | 1,079 |
| International | 0.9 | 3.9 | -0.8 | -3.5 | -2.5 | -3.2 | 393 |
| **Hybrid funds** | **-1.0** | **-2.6** | **1.0** | **-0.7** | **-1.3** | **1.1** | **324** |
| **Bond funds** | **-0.5** | **-4.0** | **5.9** | **16.7** | **7.6** | **13.7** | **910** |
| International | -0.2 | -0.2 | 0.0 | 0.1 | -0.2 | -0.1 | 20 |
| High-yield | -0.2 | -1.0 | 0.9 | 0.3 | -2.0 | 1.1 | 88 |
| Other taxable | 1.0 | -1.6 | 4.2 | 13.3 | 10.1 | 10.6 | 505 |
| Municipals | -1.0 | -1.2 | 0.8 | 3.0 | -0.3 | 2.1 | 297 |

e. Staff estimates based on confidential ICI weekly data.

Source. Investment Company Institute (ICI).

# Treasury and Agency Finance

## Treasury Financing
(Billions of dollars)

| Item | 2001 | | | | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Aug. | Sept. | Oct.(e) |
| **Total surplus, deficit (-)** | **-22.5** | **193.7** | **-41.8** | **-80.0** | **35.4** | **n.a.** |
| Means of financing deficit | | | | | | |
| Net borrowing | 23.7 | -157.4 | 68.6 | 74.1 | .5 | -8.1 |
| Nonmarketable | 6.0 | 6.2 | -5.7 | -1.5 | -1.7 | 1.4 |
| Marketable | 17.6 | -163.6 | 74.4 | 75.6 | 2.3 | -9.5 |
| Bills | 65.0 | -92.1 | 114.8 | 79.5 | 2.3 | 1.3 |
| Coupons[1] | -39.4 | 62.3 | -32.6 | -.3 | .0 | -8.3 |
| Debt buybacks | -8.0 | -9.2 | -7.7 | -3.5 | .0 | -2.5 |
| Decrease in cash balance | -7.2 | -15.4 | -.5 | 16.8 | -37.9 | 17.2 |
| Other[2] | 6.0 | -20.9 | -26.3 | -10.9 | .5 | n.a. |
| MEMO | | | | | | |
| Cash balance, end of period | 28.3 | 43.7 | 44.2 | 6.3 | 44.2 | 27.0 |

NOTE. Components may not sum to totals because of rounding.
1. Does not include Treasury debt buybacks.
2. Direct loan financing, accrued items, checks issued less checks paid, and other transactions.
e. Estimated.
n.a. Not available.

## Net Borrowing of Government-Sponsored Enterprises
(Billions of dollars)

| Agency | 2001 | | | | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Aug. | Sept. | Oct. |
| FHLBs | 8.4 | -7.7 | 19.2 | -2.4 | 15.3 | n.a. |
| Freddie Mac | 34.4 | 35.4 | 37.7 | 6.7 | 18.8 | n.a. |
| Fannie Mae | 23.9 | 35.7 | 24.7 | 11.2 | 9.0 | n.a. |
| Farm Credit Banks | .0 | 2.2 | .1 | .0 | .1 | n.a. |
| Sallie Mae | 1.9 | .4 | 1.7 | 1.9 | -1.0 | n.a. |
| MEMO | | | | | | |
| *Outstanding noncallable reference and benchmark securities* | | | | | | |
| Notes and Bonds | 351.2 | 384.1 | 411.5 | 404.2 | 411.5 | 426.5 |
| Bills | 270.0 | 278.0 | 288.5 | 298.5 | 288.5 | 296.5 |
| Total | 621.2 | 662.1 | 700.0 | 702.7 | 700.0 | 723.0 |

NOTE. Excludes mortgage pass-through securities issued by Fannie Mae and Freddie Mac.
n.a. Not available

(MBA) refinancing index to the highest level since its inception in January 1980. Despite low mortgage rates, the MBA's home purchase index edged down over the intermeeting period.

Growth of residential mortgage debt remained strong in the third quarter, albeit not as fast as the extremely rapid pace in the second quarter. At the same time, the growth of consumer debt slowed sharply. The resulting deceleration in household debt, combined with lower mortgage rates, contributed to a drop in the debt service burden in the third quarter. The bulk of the decline, however, can be attributed to a temporary rise in personal income stemming from tax refunds.

While household credit quality has deteriorated some this year, delinquency rates still are below the levels of the early and middle 1990s. The delinquency rate on auto loans is estimated to have inched up in September, while that on credit card pools has hovered in a narrow, though elevated, range over the past several months. Personal bankruptcy rates moved up a bit in October.

Household assets relative to disposable income fell sharply in the third quarter, reflecting both the general downward trend in equity prices and a deceleration in home prices. Net flows into equity mutual funds, which contracted slightly in August as households responded to the falling and volatile stock market, plunged in September. The outflow in September was the largest ever recorded, though it was substantially smaller as a proportion of mutual fund assets than the outflow experience after the 1987 stock market crash. As the stock market stabilized in the first weeks of October, net flows turned positive.

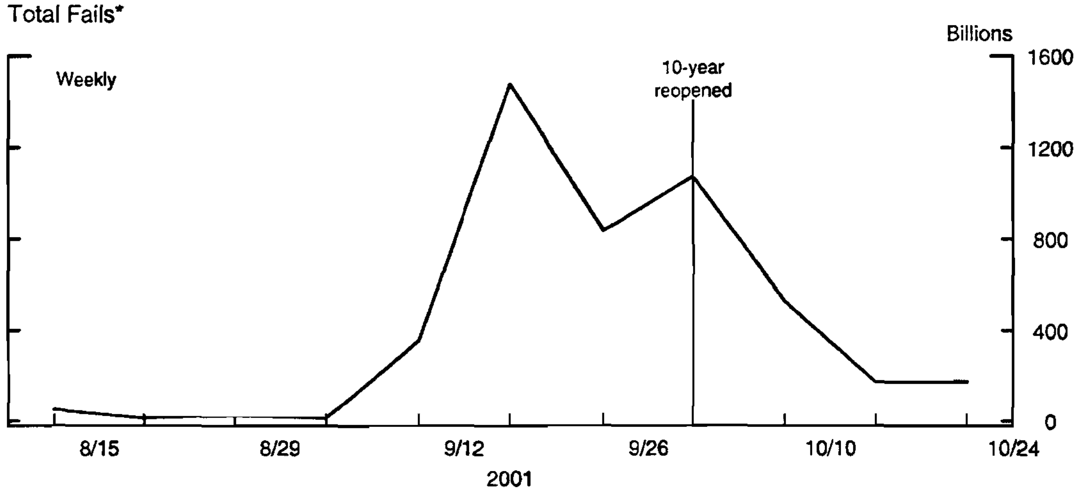
**Treasury and Agency Finance**

The federal government paid down marketable debt, on balance, over the intermeeting period. Buyback operations, which were cancelled in September in the wake of terrorist attacks, resumed in October and proceeded without a hitch, although smaller projected surpluses heightened speculation that the size of future buybacks could be pared.[2]

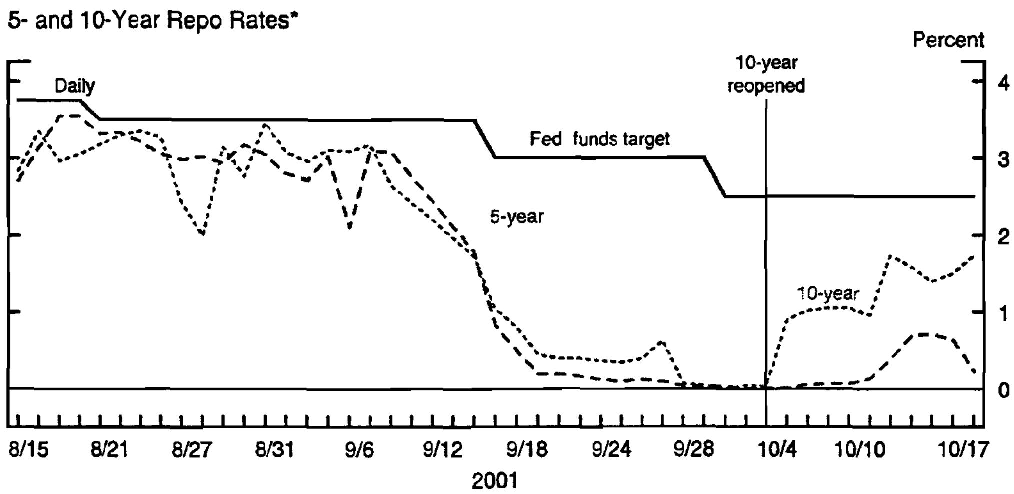
The Treasury securities market experienced an extraordinary volume of "fails-to-deliver" in the weeks following the terrorist attacks on September 11. Fails soared from less than $50 billion per week to $1.4 trillion by the week of September 19, and they were most pronounced among the on-the-run five- and ten-year notes. The difficulty in obtaining these securities was reflected in repo rates, which were quite low for much of the intermeeting period. According to

2. In its October 31 announcement, the Treasury indicated that no debt buyback operations would take place in January 2002 and that the amount and timing of future buybacks would be determined on a quarterly basis.

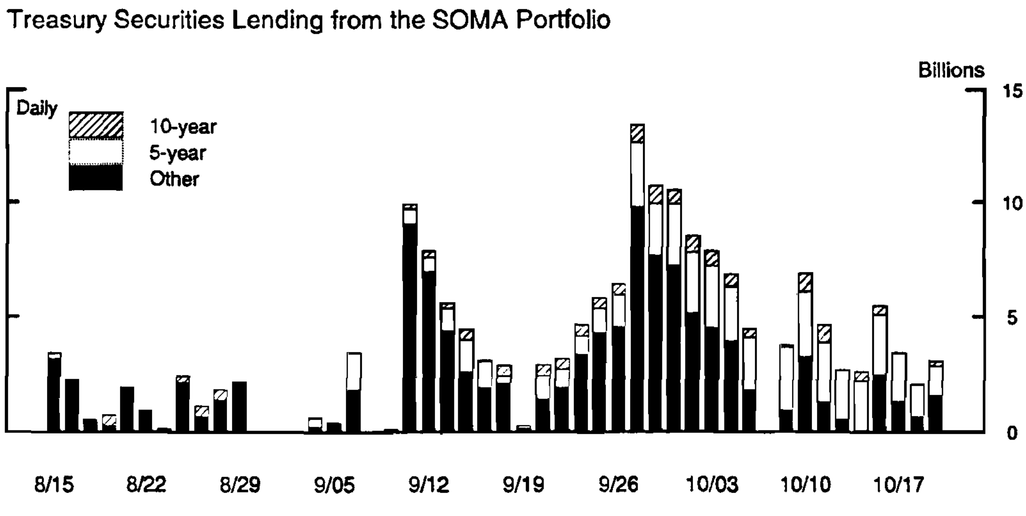
## Fails to Deliver in the Treasury Market




* Cumulative total during the week.




* On-the-run securities.




MFMA:APC

market participants, problems in the settlement of trades in Treasury securities following the attacks and the associated uncertainties may have created gridlock, as dealers feared that some counterparties would fail to deliver securities to them and chose, in turn, to fail in their delivery obligations.

To help ease the resulting supply pressures, the Federal Reserve Bank of New York eased restrictions on its Treasury securities lending program. Also, the Treasury reopened its ten-year note, selling an additional $6 billion worth of these securities on October 4. By the middle of the month, the situation in the repo market had stabilized, and on October 18, the Federal Reserve Bank of New York reimposed its normal rules for securities lending. Despite the lingering problems with fails, market participants report that liquidity in the secondary market for Treasury securities—as measured by bid-asked spreads and trading volumes—had returned to nearly normal levels by early October.

In the market for agency securities, the government-sponsored enterprises (GSEs) maintained their regular issuance of benchmark securities over the intermeeting period. However, there has been some speculation of late about the GSEs' commitment to issuing longer-term bonds. Recently, Fannie Mae announced an auction schedule for next year that included a smaller number of offerings. Anticipating this announcement, liquidity in the secondary market for these securities has reportedly deteriorated considerably in recent months.

**State and Local Government Finance**

Yields on long-term municipal bonds edged down in October to near their lowest levels since 1998. A rise in the issuance of long-term tax-exempt securities in October was spurred in part by low interest rates and the rescheduling of some September issues that were delayed by the terrorist attacks. New capital issuance topped its strong first-half pace.

The ratio of municipal to corporate AAA yields edged up in October, but it remains low, suggesting that deterioration in credit quality of the municipal sector is not a major concern. Indeed, upgrades continued to outpace downgrades, although there has been a slight pickup in the number of state and local entities that have been put on watch by the rating agencies for possible downgrades.

**Money and Bank Credit**

Growth of the broad monetary aggregates slowed considerably in October after their rapid expansion in September, when growth was boosted by the transactions disruptions and safe-haven demand for liquid assets. Even so, averaging through the recent distortions to money flows, M2 rose at a strong 12 percent annual rate over September and October, a step-up from the rapid pace posted early in the year; growth continues to be spurred by sharp declines

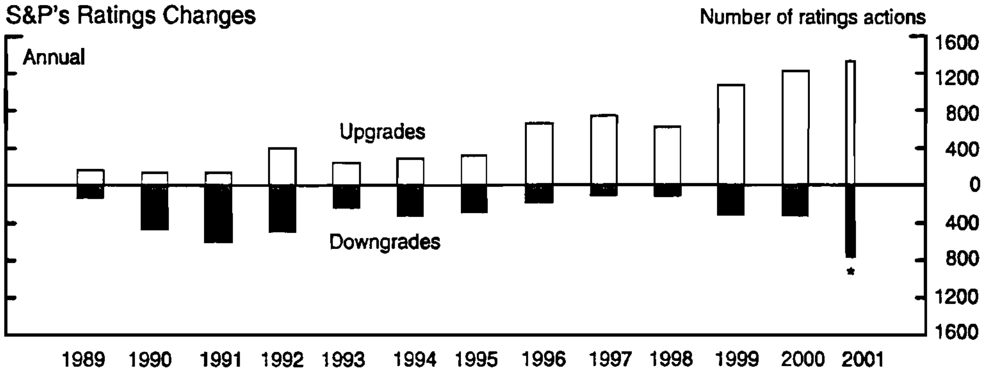
## State and Local Government Finance

Gross Offerings of Municipal Securities
(Billions of dollars; monthly rates, not seasonally adjusted)

| | | | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | 1999 | 2000 | H1 | Q3 | Aug. | Sept. | Oct.[e] |
| Long-term[1] | 18.0 | 15.0 | 21.4 | 17.8 | 21.2 | 13.2 | 27.0 |
| Refundings[2] | 4.5 | 2.2 | 6.4 | 5.0 | 7.6 | 3.0 | 8.0 |
| New capital | 13.5 | 12.9 | 15.0 | 12.9 | 13.5 | 10.1 | 19.0 |
| Short-term | 2.7 | 2.8 | 3.7 | 5.9 | 7.0 | 8.5 | 8.0 |
| Total tax-exempt | 20.6 | 17.9 | 25.0 | 23.8 | 28.1 | 21.7 | 35.0 |
| Total taxable | 1.1 | 0.7 | 1.2 | 0.7 | 0.3 | 0.7 | 0.7 |

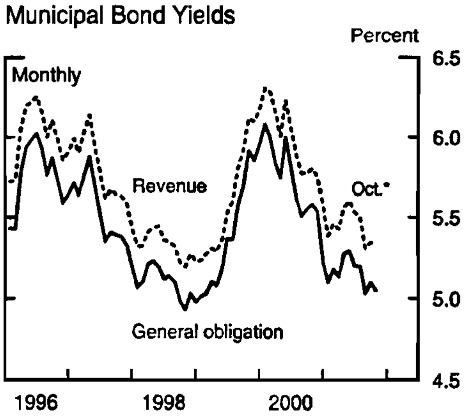
1. Includes issues for public and private purposes.
2. All issues that include any refunding bonds.
e. Staff estimate based on data through Oct. 25.

S&P's Ratings Changes



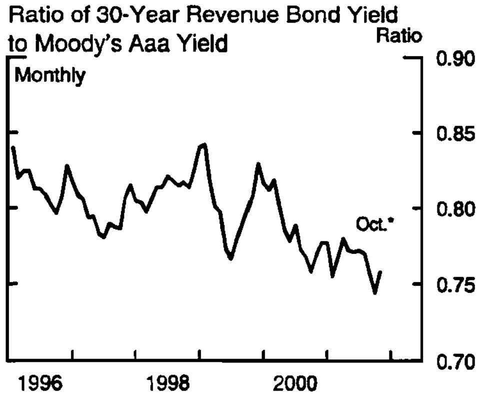

Source. S&P's Credit Week Municipal.
* Data through Oct. 11 at an annual rate.

Municipal Bond Yields




Note. Average of weekly data.
* Data through Oct. 25.

Ratio of 30-Year Revenue Bond Yield to Moody's Aaa Yield




Note. Average of weekly data.
* Data through Oct. 25.

## Monetary Aggregates
(Based on seasonally adjusted data)

| Aggregate or component | 2000 | 2001 Q2 | 2001 Q3 (p) | 2001 Aug. | 2001 Sept. | 2001 Oct. (p) | Level (bil. $) Oct. 01 (p) |
|---|---|---|---|---|---|---|---|
| *Aggregate* | Percent change (annual rate)[1] | | | | | | |
| 1. M2[2] | 6.2 | 10.4 | 10.5 | 7.7 | 25.1 | -1.3 | 5397.6 |
| 2. M3 | 9.3 | 15.0 | 9.1 | -0.3 | 22.5 | 9.3 | 7821.1 |
| *Selected components* | | | | | | | |
| 3. Currency | 4.2 | 6.0 | 11.7 | 18.9 | 11.5 | 7.4 | 567.8 |
| 4. Liquid deposits[3] | 3.2 | 17.2 | 20.0 | 19.1 | 43.8 | -6.3 | 2803.4 |
| 5. Small time deposits | 9.5 | -4.1 | -9.4 | -10.2 | -9.0 | -11.9 | 1006.0 |
| 6. Retail money market funds | 12.2 | 11.2 | 5.6 | -10.5 | 17.3 | 18.5 | 1012.0 |
| 7. M3 minus M2[4] | 17.2 | 25.3 | 6.1 | -17.7 | 16.7 | 33.0 | 2423.4 |
| 8. Large time deposits, net[5] | 13.6 | 0.7 | -3.2 | -17.3 | -1.9 | 12.5 | 804.0 |
| 9. Institution-only money market mutual funds | 24.0 | 54.9 | 21.0 | -20.9 | 52.9 | 77.8 | 1041.6 |
| 10. RPs | 11.7 | 21.0 | -9.7 | -11.9 | -40.8 | -21.8 | 358.0 |
| 11. Eurodollars | 17.9 | 7.9 | 1.8 | -14.8 | 17.7 | -15.3 | 219.8 |
| *Memo* | | | | | | | |
| 12. M1 | -1.7 | 5.4 | 13.6 | 8.1 | 52.3 | -43.4 | 1192.9 |
| 13. Sweep-adjusted M1[6] | 1.6 | 6.5 | 12.0 | 9.0 | 39.6 | -22.5 | 1629.9 |
| 14. Demand deposits | -10.9 | -4.2 | 22.4 | 6.1 | 171.4 | -124.2 | 359.3 |
| 15. Other checkable deposits | -0.8 | 16.5 | 6.4 | -12.9 | -0.9 | -43.4 | 257.3 |
| 16. Savings deposits | 6.7 | 20.9 | 21.3 | 24.9 | 30.4 | 17.4 | 2186.8 |
| 17. Monetary base | 1.4 | 5.4 | 14.7 | 15.4 | 47.3 | -15.8 | 639.7 |
| | Average monthly change (billions of dollars)[7] | | | | | | |
| *Selected managed liabilities at commercial banks* | | | | | | | |
| 18. Large time deposits, gross | 8.7 | 1.3 | -4.0 | -14.3 | -0.9 | 14.7 | 943.1 |
| 19. Net due to related foreign institutions | 1.3 | -10.3 | -3.0 | 3.1 | -24.3 | -3.3 | 169.7 |
| 20. U.S. government deposits at commercial banks | -1.4 | -2.4 | 5.3 | 44.1 | -39.4 | -9.7 | 19.7 |

1. For the years shown, Q4 to Q4 precent change. For the quarters shown, based on quarterly averages.
2. Sum of M1, retail money market funds, saving deposits, and small time deposits.
3. Sum of demand deposits, other checkable deposits, and saving deposits.
4. Sum of large time deposits, institutional money funds, RP liabilities of depository institutions, and Eurodollars held by U.S. addressees.
5. Net of holdings of depository institutions, money market mutual funds, U.S. government and foreign banks and official institutions.
6. Sweep figures used to adjust these series are the estimated national total of transaction account balances initially swept into MMDAs owing to the introduction of new sweep programs on the basis of monthly averages of daily data.
7. For the years shown, "average monthly change" is the Q4 to Q4 dollar change divided by 12. For the quarters shown, it is the quarter-to-quarter dollar change, divided by 3.
p--Preliminary

## Commercial Bank Credit

(Percent change, annual rate, except as noted; seasonally adjusted)

| Type of credit | 2000 | Q2 2001 | Q3 2001 | Aug. 2001 | Sept. 2001 | Oct.p 2001 | Level, Oct. 2001p ($ billions) |
|---|---|---|---|---|---|---|---|
| **Total** | | | | | | | |
| **1. Adjusted[1]** | **9.4** | **2.7** | **1.9** | **-.4** | **13.5** | **-10.3** | **5,195** |
| 2. Reported | 10.0 | 3.2 | 2.5 | 3.3 | 17.1 | -9.0 | 5,371 |
| *Securities* | | | | | | | |
| 3. Adjusted[1] | 1.7 | 4.2 | 11.6 | 16.7 | 7.1 | 4.0 | 1,278 |
| 4. Reported | 4.5 | 6.1 | 13.1 | 29.3 | 21.2 | 7.2 | 1,454 |
| 5. Treasury & Agency | -2.4 | -3.3 | 10.6 | 20.3 | 16.5 | 6.6 | 802 |
| 6. Other[2] | 16.7 | 18.7 | 16.2 | 40.7 | 27.1 | 8.0 | 652 |
| *Loans[3]* | | | | | | | |
| 7. Total | 12.0 | 2.2 | -1.2 | -5.9 | 15.6 | -14.9 | 3,917 |
| 8. Business | 9.0 | -4.3 | -9.9 | -7.9 | 2.9 | -16.6 | 1,049 |
| 9. Real estate | 14.1 | 6.2 | 3.1 | -3.4 | 4.1 | 4.2 | 1,721 |
| 10. Home equity | 27.4 | 13.3 | 13.2 | 10.9 | 20.0 | 23.8 | 149 |
| 11. Other | 13.1 | 5.6 | 2.1 | -4.7 | 2.6 | 2.4 | 1,571 |
| 12. Consumer | 10.5 | 3.9 | -2.0 | -3.5 | .4 | 1.8 | 548 |
| 13. Adjusted[4] | 7.2 | 5.1 | 2.1 | -.3 | 1.5 | 5.5 | 879 |
| 14. Other[5] | 13.4 | 1.6 | 3.4 | -11.5 | 84.7 | -77.2 | 599 |

Note. All data are adjusted for breaks caused by reclassifications. Monthly levels are pro rata averages of weekly (Wednesday) levels. Quarterly levels (not shown) are simple averages of monthly levels. Annual levels (not shown) are levels for the fourth quarter. Growth rates are percentage changes in consecutive levels, annualized but not compounded. These data have been benchmarked to the December 1999 Call Report.

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

p Preliminary.

in M2 opportunity cost owing to monetary policy easings this year as well as a volatile stock market.

Bank credit is estimated to have contracted at about a 10-1/4 percent annual rate in October, as the disruptions to business financing patterns and payments systems that bloated bank balance sheets after the terrorist attacks have largely dissipated. Business loans declined at a 16-1/2 percent annual rate in October. Among other loan categories, real estate lending at commercial banks continued to expand moderately, with home equity loans especially strong. Consumer lending also strengthened somewhat in October, after adjusting for loans that left banks' books in the form of securitizations.

# Appendix

## Senior Loan Officer Opinion Survey on Bank Lending Practices

The October 2001 Senior Loan Officer Opinion Survey on Bank Lending Practices focused on changes in the supply of, and demand for, bank loans to businesses and households over the past three months. The survey included supplementary questions on banks' internal credit risk ratings for business loan customers, on business loans for the purpose of share buybacks, and on liquidity in the secondary market for business loans. Loan officers from fifty-three large domestic banks and twenty U.S. branches and agencies of foreign banks participated in the survey.

The number of foreign and domestic banking institutions that reported tightening standards and terms on commercial and industrial (C&I) loans over the past three months increased notably after having edged down in the previous two surveys. The fraction of domestic institutions that tightened standards for commercial real estate loans in the October survey remained in the elevated range of the past year. Almost twice as many domestic respondents as in the August survey indicated that a less favorable or more uncertain economic outlook was a very important reason for tightening standards and terms on C&I loans, a rise in pessimism consistent with the weak tenor of recent economic data. Compared with the proportions in the August survey, considerably larger net fractions of domestic banks experienced weaker demand for both C&I and commercial real estate loans over the past three months.

In answer to the special questions in the current survey, most domestic banks and a substantial number of foreign institutions said they had downgraded between 1 percent and 10 percent of the dollar volume of C&I loans on their books over the past three months—in particular, loans to firms in the airline and hospitality industries. Much smaller shares of loans were upgraded. Both domestic and foreign respondents also noted that liquidity in the secondary loan market had deteriorated somewhat in the aftermath of the terrorist attacks.

The net fractions of domestic banks that tightened standards and increased spreads over their cost of funds for all types of consumer loans over the past three months moved up from the levels in the August survey, but they remained within the range of the past several quarters. According to the domestic respondents in the October survey, demand for consumer loans weakened over the report period, after little net change was reported in the previous two surveys. Standards for residential mortgage loans were largely unchanged over the past three months, and demand for mortgages to purchase homes was reported to be little changed.

**Lending to Businesses**

The October survey showed a rise in the fraction of domestic banks reporting that they had tightened standards on C&I loans over the past three months, a fraction that had slipped in the previous two surveys. The percentage of domestic banks that reported tightening their standards on C&I loans to large and middle-market firms rose to 49 percent in October from 40 percent in August. Results were similar for lending standards on loans to small firms—40 percent of domestic banks reported tighter standards over the past three months, up from 32 percent in August. The net fraction of

U.S. branches and agencies of foreign banks that reported tightening standards for C&I customers rose to 65 percent in October from 50 percent in August.

As in the August survey, more than half of domestic banks reported increasing spreads of loan rates over their cost of funds and charging higher premiums on riskier loans to large and middle-market firms. Larger fractions than in August imposed more stringent loan covenants and collateral requirements on these firms. In general, smaller net fractions of domestic respondents tightened terms on loans to small firms. However, the number of banks that tightened non-price-related loan terms for small firms rose considerably when compared with the August survey. Despite the overall tightening of standards and terms over the past three months, a few banks indicated a willingness to address the needs of business customers in areas affected by the atrocities of September 11.

The tightening of terms at U.S. branches and agencies of foreign banks was somewhat more pronounced than at their domestic counterparts. Compared with the previous survey, when 50 percent of foreign respondents increased spreads of loan rates over their cost of funds, 65 percent reported doing so in October. Similarly, the fraction of foreign institutions that raised premiums on riskier loans rose from 60 percent in August to 65 percent in the current survey. The fraction of foreign banks that increased the cost of credit lines and tightened collateral requirements over the past three months also rose relative to the previous survey.

All survey respondents pointed to a less favorable or more uncertain economic outlook as at least a somewhat important reason for changing their commercial lending policies; that reason was said to be "very important" for 64 percent of domestic banks, up significantly from 37 percent in the August survey. Most of the domestic and foreign respondents that had tightened standards or terms on C&I loans over the previous three months also continued to cite a worsening of industry-specific problems and a reduced tolerance for risk as important reasons for changing their lending policies. Concern about credit quality was cited as a reason for tightening credit by 46 percent of domestic banks and 72 percent of foreign branches and agencies.

Almost three-fourths of domestic banks, on net, reported weaker demand for C&I loans from large and middle-market firms over the past three months, up considerably from about one-half in the August survey. Loan demand from small firms also weakened, with more than 50 percent of domestic respondents, on net, noting weakness in October, compared with 42 percent in August. On net, 30 percent of foreign branches and agencies saw weaker demand over the past three months, compared with 25 percent in the previous survey. Many banks commented that the terrorist attacks exacerbated an ongoing slowdown in demand for business loans.

All but one domestic bank that reported weaker business loan demand cited a decline in customers' need for credit to finance capital expenditures as at least a somewhat important reason, and almost 40 percent chose the same reason as "very important." Most domestic respondents also noted a decline in demand to finance mergers and acquisitions, inventory accumulation, and accounts receivable. One-half of the foreign institutions that reported weaker loan demand pointed to the decline in demand for merger-related financing as a very important reason, and 38 percent also cited lower investment spending as being very important.

In light of the pace of net downgrades of corporate debt by the major credit rating agencies, the October survey included a series of questions about changes in banks' internal credit risk ratings. Essentially all domestic and foreign institutions indicated that more than three-fourths of the dollar volume of their C&I loans is internally rated. Almost half of the domestic banks surveyed had downgraded less than 5 percent of their C&I loan portfolio over the past three months. An additional 31 percent of them had downgraded between 6 percent and 10 percent, and 21 percent had downgraded between 11 percent and 30 percent of their business loans over the same period. Foreign branches and agencies had downgraded somewhat larger fractions of the C&I loans on their books. In particular, almost 16 percent of these institutions had downgraded more than 30 percent of their business loan portfolios. The reported downgrades in internal risk ratings at both domestic and foreign respondents were offset somewhat by upgrades: About 60 percent of domestic and foreign banks indicated that they had upgraded at least some loans in their C&I loan portfolios.

Almost 30 percent of domestic respondents and 40 percent of foreign respondents noted that they had downgraded considerably their loans to commercial airlines and other nondefense aerospace firms, with significant additional fractions reporting more moderate downgrades in these sectors. The portion of the banks' portfolios covering loans to travel and other leisure-related service businesses was also hard hit by downgrades, a move likely reflecting the disruptions caused by the terrorist attacks. Downgrades were pervasive among loans to high-technology firms and to automobile manufacturers and distributors, as well as to firms in consumer cyclical industries. Of the sectors named in the survey, only energy and defense avoided widespread downgrades over the past three months.

In the aftermath of the terrorist attacks, as market liquidity became a concern, the SEC temporarily eased restrictions on share repurchases, and reports from market participants suggest that buyback activity was elevated in the ensuing weeks. Very few domestic banks, however, reported an increase in demand for loans to finance share buybacks. By contrast, a modest fraction of foreign institutions did experience some increase in demand for this type of loan. About 30 percent of both foreign and domestic banks tightened standards for below-investment-grade firms on loans to finance equity repurchases.

A separate question asked banks about changes since September 11 in the liquidity of the secondary market for C&I loans. About one-fifth of domestic and foreign institutions reported that loan-trading volume had decreased considerably and more than 50 percent noted that it had decreased somewhat. The reports of diminished liquidity were corroborated by the widening of bid-asked spreads, with 21 percent of all institutions reporting that the spreads had widened considerably and 50 percent of them indicating that the spreads had widened somewhat. Separate comments by the loan officers indicated that the reduction in liquidity was particularly severe for loans rated as below investment grade.

More than 40 percent of domestic banks tightened standards on commercial real estate loans over the past three months, up a tad from the August survey. About one-fourth of the foreign institutions that engage in commercial real estate lending also tightened standards in the current survey. The demand for commercial real estate loans weakened over the survey period, with more than 50 percent of domestic and 27 percent of foreign respondents, on net, reporting lower demand for this type of loan.

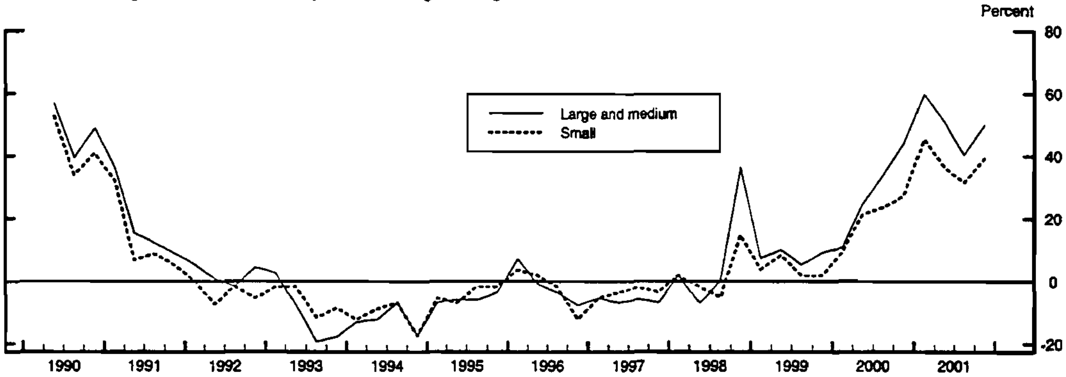
**Lending to Households**

Banks' credit standards for approving residential mortgage loans were largely unchanged over the past three months, with only two banks reporting that they had tightened lending standards somewhat. According to the domestic respondents, demand for residential mortgages remained unchanged, on net, over the same period.

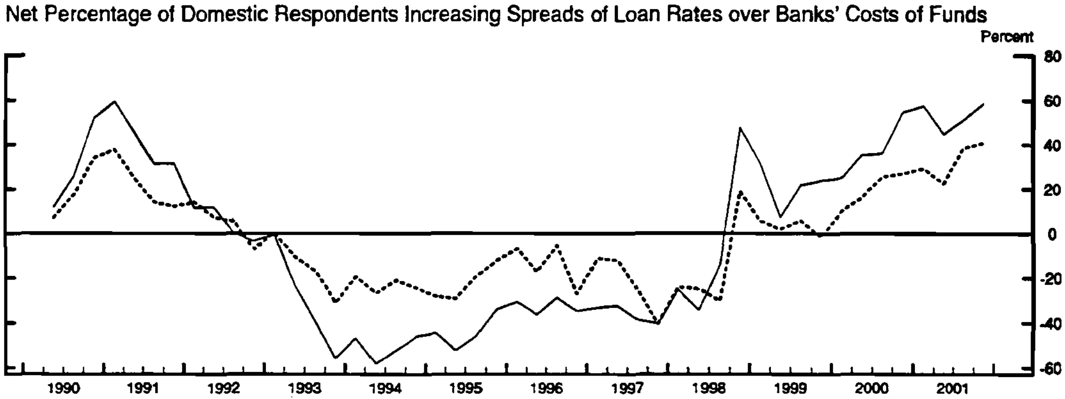
On net, 8 percent of domestic banks indicated that they are less willing to make consumer installment loans now as opposed to three months ago. Specifically, more than one-fifth of banks reported that they had tightened standards on both credit card and other types of consumer loans over the past three months, somewhat higher fractions than reported doing so in the August survey. In addition, 14 percent of domestic banks increased the minimum required credit score for credit card applications, and 21 percent of them raised spreads of interest rates charged on outstanding balances relative to their cost of funds. For other types of consumer loans, 14 percent of respondents raised the minimum required credit score, and 24 percent of them increased spreads over their cost of funds. Almost one-fourth of domestic banks, on net, reported moderately weaker demand for consumer loans over the past three months.

# Measures of Supply and Demand for C&I Loans, by Size of Firm Seeking Loan

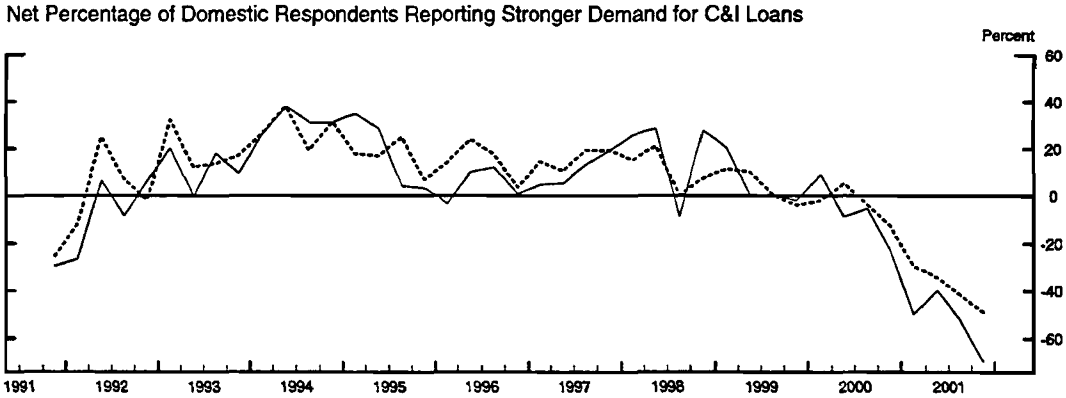
Net Percentage of Domestic Respondents Tightening Standards for C&I Loans




Net Percentage of Domestic Respondents Increasing Spreads of Loan Rates over Banks' Costs of Funds

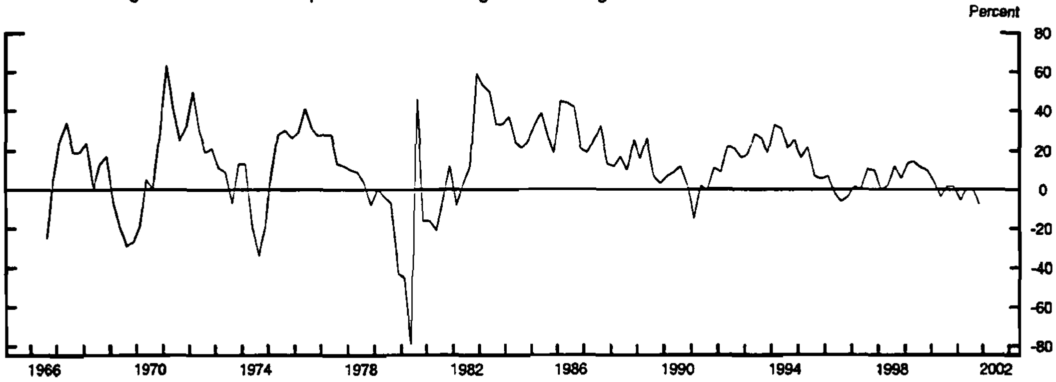



Net Percentage of Domestic Respondents Reporting Stronger Demand for C&I Loans

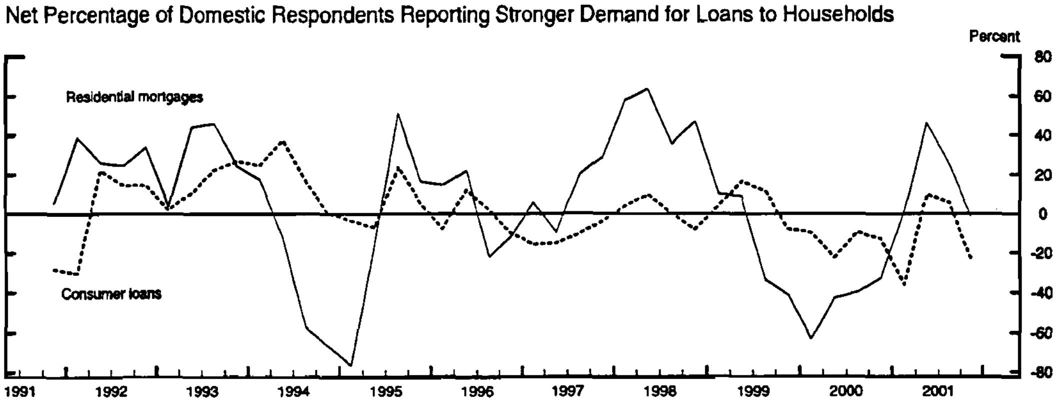


# Measures of Supply and Demand for Loans to Households

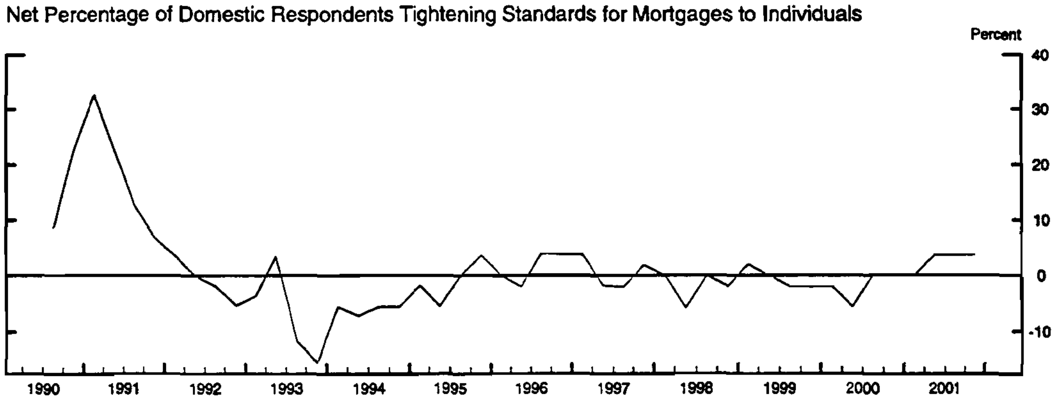
Net Percentage of Domestic Respondents Indicating More Willingness to Make Consumer Installment Loans




Net Percentage of Domestic Respondents Reporting Stronger Demand for Loans to Households




Net Percentage of Domestic Respondents Tightening Standards for Mortgages to Individuals



# International Developments

# International Developments

## U.S. International Transactions

### Trade in Goods and Services

The U.S. trade deficit in goods and services was $27.1 billion in August, $2 billion smaller than in July. For July-August combined, the deficit was $338 billion at a seasonally adjusted annual rate, considerably smaller than in the second quarter as imports fell more than exports declined.

**Net Trade in Goods and Services**
(Billions of dollars, seasonally adjusted)

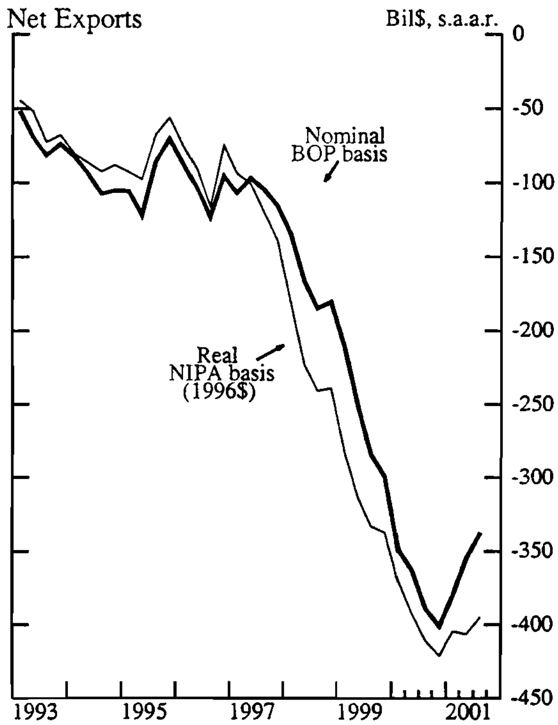
| | 2000 | Annual rate 2001 | | | Monthly rate 2001 | | |
|---|---|---|---|---|---|---|---|
| | | Q1 | Q2 | Q3[e] | June | July | Aug. |
| *Real NIPA*[1] | | | | | | | |
| Net exports of G&S | -399.1 | -404.5 | -406.7 | -395.0 | ... | ... | ... |
| *Nominal BOP* | | | | | | | |
| Net exports of G&S | -375.7 | -380.1 | -355.2 | -337.7 | -29.1 | -29.2 | -27.1 |
| Goods, net | -452.2 | -450.1 | -430.6 | -417.9 | -35.6 | -35.8 | -33.8 |
| Services, net | 76.5 | 70.0 | 75.4 | 80.2 | 6.5 | 6.7 | 6.7 |

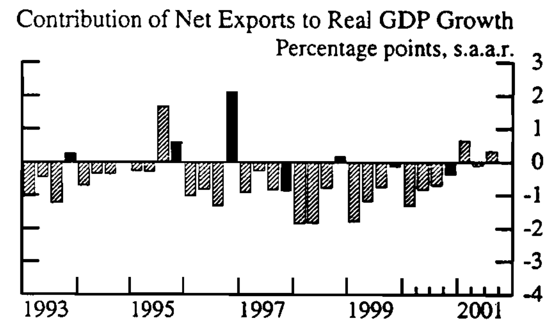
1. Billions of chained (1996) dollars.
e. BOP data are two months at an annual rate.
Source: U.S. Department of Commerce, Bureaus of Economic Analysis and Census.
n.a. Not available. ... Not applicable.

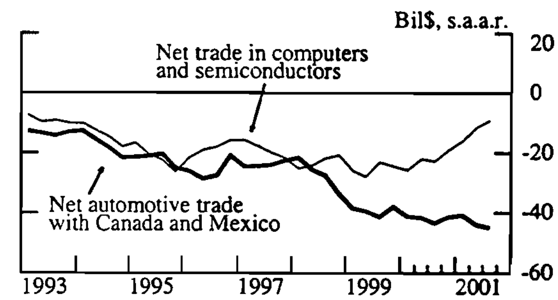
The value of imports fell 1.1 percent in August, the fifth sharp decline in seven months. Decreases were recorded in almost all major trade categories. The value of imported oil changed little as a small drop in quantity was offset by an increase in price. For July and August combined, the value of imports fell 14 percent at an annual rate from the second-quarter level; this follows a similar decrease in the second quarter. The decline in July-August was spread among all major trade categories other than automotive products, food, and to a much lesser extent aircraft, which rose.

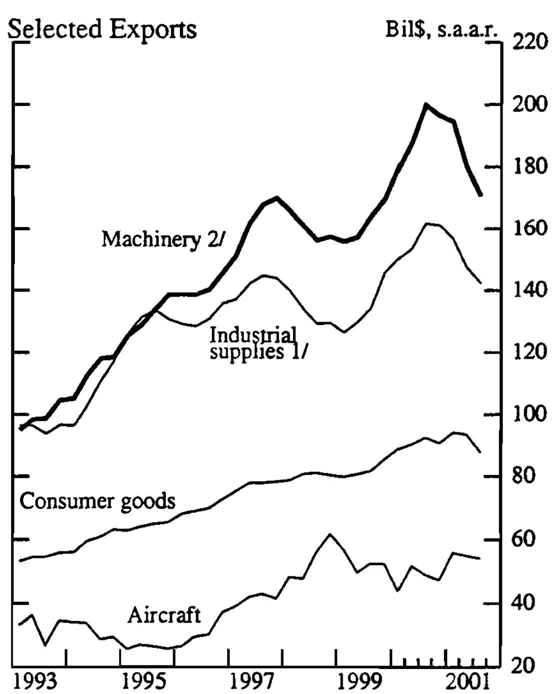
The value of exports increased 1 percent in August, only partly reversing the sharp drop recorded in July. Much of the increase was in automotive products, industrial supplies, and agricultural products. For July and August combined, the value of exports fell 12 percent at an annual rate from the second-quarter level; this follows a similar decrease in the second quarter. While the decline was concentrated in exported capital goods, there were also substantial decreases in exported consumer goods and industrial supplies.

# U.S. International Trade in Goods and Services

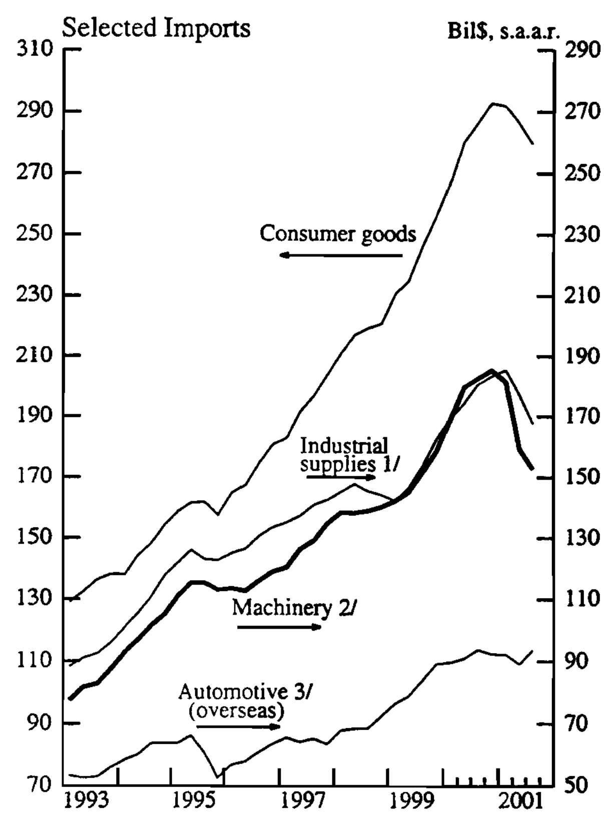



1. Excludes agriculture and gold.
2. Excludes computers and semiconductors.




1. Excludes oil and gold.
2. Excludes computers and semiconductors.
3. Excludes Canada and Mexico.

## U.S. Exports and Imports of Goods and Services
(Billions of dollars, s.a.a.r., BOP basis)

| | Levels | | | | Amount Change[1] | | | |
|---|---|---|---|---|---|---|---|---|
| | 2001 | | 2001 | | 2001 | | 2001 | |
| | Q2 | Q3e | July | Aug. | Q2 | Q3e | July | Aug. |
| **Exports of G&S** | **1042.1** | **1008.3** | **1003.1** | **1013.5** | **-34.2** | **-33.8** | **-27.6** | **10.3** |
| Goods exports | 743.5 | 708.9 | 704.3 | 713.5 | -36.3 | -34.6 | -25.9 | 9.3 |
| Gold | 7.6 | 2.8 | 3.0 | 2.6 | 0.9 | -4.8 | -4.0 | -0.5 |
| Other goods | 735.9 | 706.1 | 701.2 | 710.9 | -37.2 | 24.1 | -21.9 | 9.7 |
| Aircraft & parts | 55.1 | 54.2 | 54.0 | 54.3 | -0.9 | -0.9 | -0.5 | 0.3 |
| Computers | 48.6 | 45.4 | 45.9 | 44.9 | -7.4 | -3.2 | -2.1 | -1.0 |
| Semiconductors | 46.5 | 39.9 | 41.3 | 38.5 | -11.5 | -6.6 | -0.3 | -2.8 |
| Other capital gds | 182.7 | 172.9 | 174.6 | 171.3 | -14.6 | -9.7 | -5.5 | -3.4 |
| Automotive | 76.3 | 77.4 | 74.7 | 80.2 | 4.5 | 1.1 | -4.9 | 5.5 |
| to Canada | 42.2 | 41.1 | 40.1 | 42.2 | 4.7 | -1.1 | -4.0 | 2.1 |
| to Mexico | 15.9 | 15.2 | 12.8 | 17.5 | -0.3 | -0.7 | -3.8 | 4.7 |
| to ROW | 18.2 | 21.2 | 21.8 | 20.5 | 0.2 | 3.0 | 3.0 | -1.3 |
| Agricultural | 53.9 | 55.9 | 53.8 | 58.1 | -0.6 | 2.1 | 0.2 | 4.3 |
| Ind supplies (ex. ag) | 147.6 | 142.3 | 140.1 | 144.6 | -9.1 | -5.3 | -4.0 | 4.5 |
| Consumer goods | 93.6 | 87.7 | 89.2 | 86.2 | -0.5 | -5.9 | 0.9 | -3.0 |
| All other goods | 31.7 | 30.2 | 27.6 | 32.9 | 2.8 | -1.4 | -9.2 | 5.3 |
| Services exports | 298.7 | 299.4 | 298.9 | 300.0 | 2.1 | 0.7 | -1.7 | 1.1 |
| **Imports of G&S** | **1397.3** | **1346.0** | **1353.2** | **1338.8** | **-59.1** | **-51.3** | **-26.4** | **-14.3** |
| Goods imports | 1174.1 | 1126.8 | 1134.3 | 1119.3 | -55.8 | -47.3 | -22.5 | -15.1 |
| Petroleum | 114.3 | 102.5 | 102.6 | 102.4 | -3.0 | -11.7 | -9.3 | -0.1 |
| Gold | 6.5 | 2.1 | 1.9 | 2.3 | 0.4 | -4.4 | -4.2 | 0.4 |
| Other goods | 1053.3 | 1022.2 | 1029.8 | 1014.5 | -53.2 | -31.2 | -9.0 | -15.4 |
| Aircraft & parts | 31.1 | 31.8 | 33.8 | 29.8 | 0.0 | 0.7 | 2.0 | -4.0 |
| Computers | 75.9 | 70.0 | 72.1 | 68.0 | -9.8 | -5.9 | -0.6 | -4.1 |
| Semiconductors | 30.8 | 24.5 | 24.7 | 24.2 | -13.5 | -6.4 | -5.5 | -0.4 |
| Other capital gds | 162.1 | 154.9 | 153.0 | 156.9 | -22.6 | -7.2 | -4.9 | 3.9 |
| Automotive | 191.3 | 194.9 | 191.4 | 198.5 | 4.3 | 3.7 | -1.3 | 7.2 |
| from Canada | 61.0 | 61.0 | 59.6 | 62.5 | 5.0 | -0.0 | -3.0 | 2.9 |
| from Mexico | 41.1 | 40.3 | 38.1 | 42.5 | 2.5 | -0.8 | -4.6 | 4.3 |
| from ROW | 89.1 | 93.6 | 93.6 | 93.6 | -3.1 | 4.5 | 6.3 | -0.0 |
| Ind supplies | 177.3 | 167.7 | 173.2 | 162.3 | -8.2 | -9.5 | 1.5 | -10.9 |
| Consumer goods | 286.3 | 279.7 | 281.3 | 278.0 | -5.4 | -6.6 | -2.6 | -3.3 |
| Foods, feeds, bev. | 45.7 | 47.9 | 48.8 | 47.0 | -0.1 | 2.2 | 1.5 | -1.7 |
| All other goods | 52.9 | 50.7 | 51.7 | 49.7 | 2.0 | -2.3 | 1.0 | -2.0 |
| Services imports | 223.2 | 219.2 | 218.8 | 219.6 | -3.4 | -4.0 | -3.9 | 0.7 |
| *Memo:* | | | | | | | | |
| Oil quantity (mb/d) | 12.92 | 12.08 | 12.10 | 12.06 | 0.12 | -0.84 | -0.46 | -0.04 |
| Oil import price ($/bbl) | 24.22 | 23.24 | 23.21 | 23.26 | -0.86 | -0.98 | -1.18 | 0.05 |

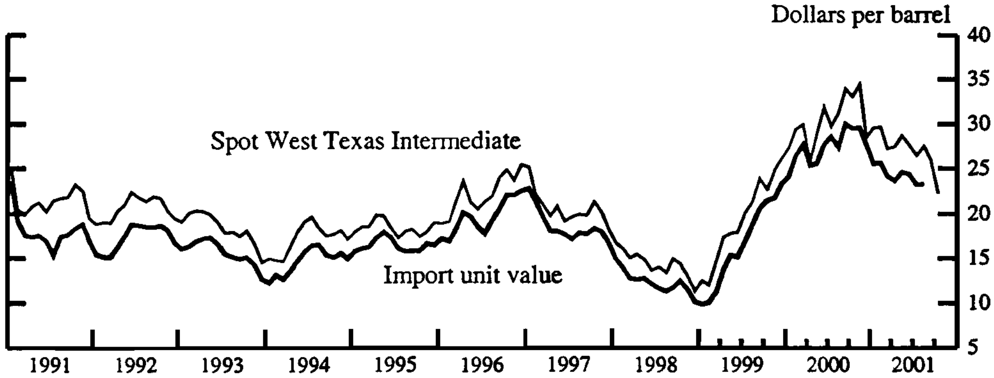
1. Change from previous quarter or month. e. Average of two months.
Source: U.S. Department of Commerce, Bureaus of Economic Analysis and Census.

## Prices of U.S. Imports and Exports
(Percentage change from previous period)

| | Annual rates 2001 Q1 | Annual rates 2001 Q2 | Annual rates 2001 Q3 | Monthly rates 2001 July | Monthly rates 2001 Aug. | Monthly rates 2001 Sept. |
|---|---|---|---|---|---|---|
| | ------------- BLS prices (1995 weights)------------- | | | | | |
| **Merchandise imports** | -5.3 | -6.9 | -6.8 | -1.5 | -0.2 | 0.3 |
| Oil | -44.8 | -10.9 | -10.3 | -5.4 | 1.7 | 2.6 |
| Non-oil | 2.4 | -6.4 | -6.2 | -1.0 | -0.4 | 0.0 |
| Core goods* | 3.1 | -6.1 | -6.1 | -1.0 | -0.4 | 0.1 |
| Computers | -4.3 | -12.6 | -13.3 | -2.2 | -0.4 | -2.1 |
| Semiconductors | -3.7 | -6.2 | -0.4 | 0.5 | 0.2 | -0.3 |
| Cap. goods ex comp & semi | -0.3 | -0.6 | -1.0 | -0.2 | -0.1 | 0.1 |
| Automotive products | -0.1 | -1.0 | -0.5 | -0.1 | -0.1 | 0.3 |
| Consumer goods | 0.6 | -1.2 | -0.7 | -0.1 | 0.0 | 0.2 |
| Foods, feeds, beverages | 0.1 | -8.8 | -6.9 | -1.1 | 0.1 | 0.7 |
| Industrial supplies ex oil | 12.4 | -18.1 | -21.0 | -3.7 | -1.8 | -0.1 |
| **Merchandise exports** | -0.3 | -2.1 | -2.8 | -0.3 | -0.2 | 0.1 |
| Core goods* | -0.1 | -1.7 | -2.1 | -0.2 | -0.2 | 0.1 |
| Computers | -2.4 | -4.9 | -7.9 | -0.5 | -1.1 | 0.2 |
| Semiconductors | -2.9 | -7.1 | -7.0 | -1.3 | 0.3 | 0.0 |
| Cap. goods ex comp & semi | 2.4 | 1.3 | 0.1 | 0.0 | 0.0 | 0.0 |
| Automotive products | 0.5 | 0.5 | 0.0 | 0.0 | 0.0 | 0.0 |
| Consumer goods | -0.7 | -1.0 | 0.3 | 0.0 | 0.0 | 0.3 |
| Agricultural products | 2.9 | -2.9 | 6.6 | 0.8 | 1.3 | -0.5 |
| Industrial supples ex ag | -4.1 | -6.3 | -11.4 | -1.9 | -0.8 | 0.6 |
| **Chain price index** | ---Prices in the NIPA accounts (1996 weights)--- | | | | | |
| Imports of goods & services | -3.0 | -6.0 | -17.5 | ... | ... | ... |
| Non-oil merchandise | 1.4 | -5.6 | -6.7 | ... | ... | ... |
| Core goods* | 2.2 | -5.0 | -6.2 | ... | ... | ... |
| Exports of goods & services | -0.1 | -1.0 | -1.4 | ... | ... | ... |
| Total merchandise | -0.4 | -1.6 | -2.1 | ... | ... | ... |
| Core goods* | 0.0 | -1.0 | -1.4 | ... | ... | ... |

*/ Excludes computers and semiconductors.
n.a. Not available. ... Not applicable.

## Oil Prices



**Prices of Internationally Traded Goods**
**Oil.** The BLS price of imported oil rose a bit more in September than in August but not enough to offset a sharp drop in July. For the third quarter as a whole, the price of imported oil fell 10 percent at an annual rate, about the same rate of decline as in the second quarter and much less than in the first quarter. A few days after the terrorist attacks of September 11, oil prices fell sharply as apprehensions about possible supply disruptions gave way to concerns about weaker world oil demand and the increasing difficulty OPEC will face in defending its price target. The spot price of West Texas Intermediate has recently been trading near $22 per barrel, down more than $5 per barrel from early September.

**Non-oil imports.** The price of imported non-oil goods was unchanged in September and the price of imported core goods rose 0.1 percent, both after declining for seven consecutive months. For core goods, price changes turned positive for all major trade categories other than industrial supplies, which declined (but at a much slower rate than in the previous four months). For the third quarter, the price of core goods fell just over 6 percent at an annual rate, about the same rate of decline as in the second quarter. As in the second quarter, the drop in price was led by decreases in the price of imported industrial supplies, with smaller price declines recorded in all other major trade categories.

**Exports.** Prices of U.S. goods exports (total and core) rose 0.1 percent in September following seven consecutive months of decline. The increase was led by a petroleum-driven rise in the price index for exported nonagricultural industrial supplies. In the third quarter the price of exported core goods declined about 1.5 percent at an annual rate, a slightly faster rate than recorded in the second quarter. A larger drop in the price of exported industrial supplies than in the second quarter was only partly offset by a swing from negative to positive in the price of agricultural exports.

**U.S. International Financial Transactions**
Private foreigners continued to acquire U.S. securities at a robust rate in August (line 4 of the Summary of U.S. International Transactions Table). Net purchases of Treasuries, agency bonds, and corporate bonds all were concentrated in international financial centers in the United Kingdom, Asia, and the Caribbean (lines 4a, b, and c). Canadians sold net both agency and corporate bonds. Net purchases of Treasuries were positive for the first month since May. Net purchases of agency bonds continued at the strong rate of the first and second quarters, while purchases of corporates slowed somewhat in conjunction with the decreased rate of gross bond issuance by U.S. firms. Of the $14.6 billion net purchases of U.S. stock in line 4d, $6.6 billion was in the form of a stock swap resulting from the Citibank acquisition of the Mexican bank, Grupo Financiero

Banamex Accival SA. There was no evidence, at least by the end of August, of any compensating net sales of U.S. stock by Mexican residents.

U.S. residents reduced their net holdings of foreign securities (line 5), as moderate acquisitions of foreign stock were more than offset by strong net sales of foreign bonds (lines 5b, 5c and 5a). Geographically, the net bond sales were widespread: more than $1 billion each in Germany, the United Kingdom, Japan, and Mexico.

Official foreigners reduced their net holdings in the United States by a moderate $8 billion in August. Argentina, Japan, and Venezuela registered significant reductions. Partial data show a $13 billion increase in official reserves held at FRBNY from the end of August through the second week of October; the increase in Japanese reserves at FRBNY during this period, primarily the result of intervention operations in September, more than accounted for the total.

Net inflows in the banking sector were up substantially in August over July (line 3); these were largely attributable to the activity of U.S. agencies and branches with their own foreign offices.

## Summary of U.S. International Transactions
(Billions of dollars, not seasonally adjusted except as noted)

| | 1999 | 2000 | 2000 Q3 | 2000 Q4 | 2001 Q1 | 2001 Q2 | 2001 July | 2001 Aug. |
|---|---|---|---|---|---|---|---|---|
| **Official financial flows** | **55.0** | **39.3** | **12.8** | **-5.4** | **4.8** | **-21.3** | **9.7** | **-7.8** |
| 1. Change in foreign official assets in the U.S. (increase, +) | 46.4 | 39.6 | 13.1 | -4.0 | 4.6 | -20.0 | 9.7 | -7.8 |
| a. G-10 countries | 49.7 | 12.3 | -4.2 | -.8 | -5.5 | -6.1 | -3.1 | -4.4 |
| b. OPEC countries | 2.0 | 10.7 | 3.4 | .6 | .8 | -2.1 | .8 | -3.0 |
| c. All other countries | -5.3 | 16.6 | 14.0 | -3.8 | 9.2 | -11.7 | 12.0 | -.4 |
| 2. Change in U.S. official reserve assets (decrease, +) | 8.6 | -.3 | -.3 | -1.4 | .2 | -1.3 | n.a. | n.a. |
| **Private financial flows** | **321.7** | **404.0** | **101.6** | **119.1** | **98.7** | **146.0** | **...** | **...** |
| Banks | | | | | | | | |
| 3. Change in net foreign positions of banking offices in the U.S.[1] | -12.4 | -6.9 | 24.1 | 13.3 | -79.2 | 29.0 | 2.3 | 20.9 |
| Securities[2] | | | | | | | | |
| 4. Foreign net purchases of U.S. securities (+) | 333.2 | 435.7 | 115.8 | 117.7 | 149.4 | 125.7 | 28.7 | 46.4 |
| a. Treasury securities | -19.9 | -52.4 | -12.9 | -10.1 | .6 | -8.6 | -10.5 | 5.3 |
| b. Agency bonds | 71.9 | 111.9 | 28.6 | 38.3 | 38.8 | 29.4 | 13.5 | 13.3 |
| c. Corporate and municipal bonds | 158.8 | 182.1 | 45.7 | 50.8 | 68.9 | 70.4 | 14.4 | 13.3 |
| d. Corporate stocks[3] | 122.4 | 194.0 | 54.4 | 38.8 | 41.7 | 34.5 | 11.2 | 14.6 |
| 5. U.S. net acquisitions (-) of foreign securities | -112.9 | -101.1 | -22.1 | -17.8 | -27.1 | -43.5 | .6 | 4.7 |
| a. Bonds | -5.7 | -4.1 | -9.0 | 3.3 | -2.0 | 8.8 | 5.6 | 9.4 |
| b. Stock purchases | 15.6 | -13.1 | -5.4 | 3.6 | -22.6 | -18.1 | -5.0 | -2.9 |
| c. Stock swaps[3] | -122.9 | -84.0 | -7.7 | -24.7 | -2.6 | -34.2 | .0 | -1.8 |
| Other flows (quarterly data, s.a.) | | | | | | | | |
| 6. U.S. direct investment (-) abroad | -155.4 | -152.4 | -41.6 | -39.1 | -40.9 | -35.6 | ... | ... |
| 7. Foreign direct investment in U.S. | 301.0 | 287.7 | 76.0 | 84.7 | 52.5 | 67.2 | ... | ... |
| 8. Foreign holdings of U.S. currency | 22.4 | 1.1 | .8 | 6.2 | 2.3 | 2.8 | ... | ... |
| 9. Other (inflow, + )[4] | -54.2 | -59.9 | -51.5 | -46.0 | 41.3 | .3 | ... | ... |
| **U.S. current account balance (s.a.)** | **-324.4** | **-444.7** | **-115.3** | **-116.3** | **-111.8** | **-106.5** | **...** | **...** |
| **Capital account balance (s.a.)[5]** | **-3.5** | **.7** | **.2** | **.2** | **.2** | **.2** | **...** | **...** |
| **Statistical discrepancy (s.a.)** | **-48.8** | **.7** | **.7** | **2.4** | **8.1** | **-18.4** | **...** | **...** |

NOTE. The sum of official and private financial flows, the current account balance, the capital account balance, and the statistical discrepancy is zero. Details may not sum to totals because of rounding.

1. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements). Includes changes in custody liabilities other than U.S. Treasury bills.

2. Includes commissions on securities transactions and excludes adjustments BEA makes to account for incomplete coverage; therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. Includes (4d) or represents (5c) stocks acquired through mergers.

4. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business

5. Consists of transactions in nonproduced nonfinancial assets and capital transfers.

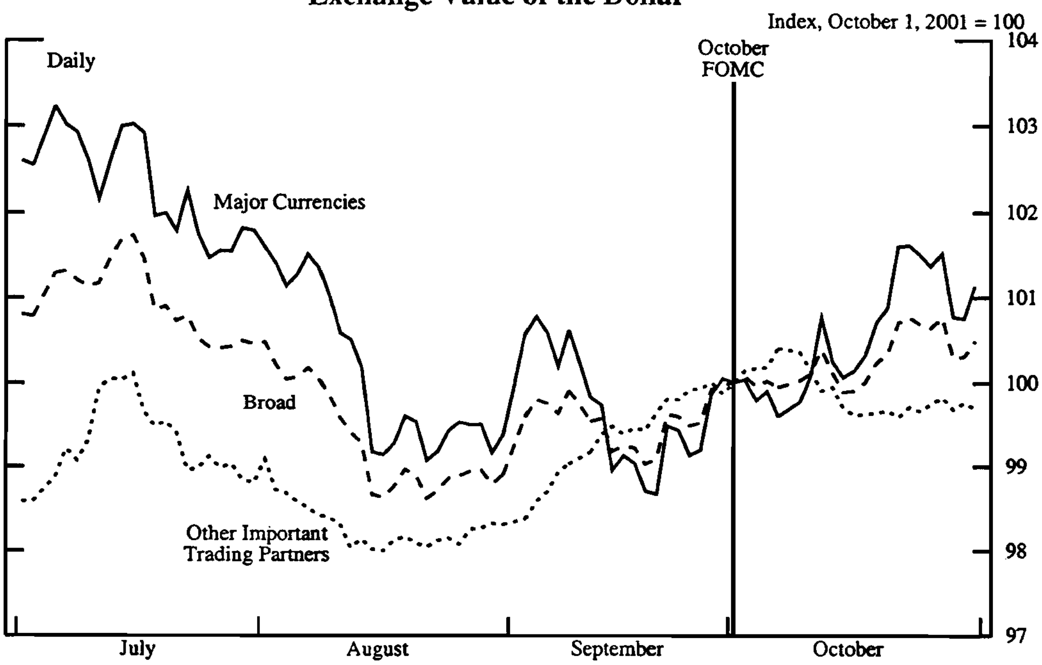
n.a. Not available. ... Not applicable.

## Foreign Exchange Markets

Data released during the intermeeting period suggesting dimmer prospects for foreign economic activity, particularly for the euro area but also for Japan, were not seen as eliciting policy reactions sufficient to counter the perceived downward momentum in those economies. In response, foreign long-term interest rates moved down more than the comparable U.S. rate, which may have been supported in part by U.S. fiscal policy actions, and foreign currency values declined against the dollar.

On net over the period following the October FOMC meeting, the trade-weighted, foreign exchange value of the dollar against the other major currencies rose more than 1 percent. The dollar appreciated about 1½ percent against the yen, sterling, and the euro, and ½ percent against the Canadian dollar. Over the same period, a trade weighted average of long-term government bond yields abroad declined more than 30 basis points, leaving the interest rate differential in favor of dollar-denominated assets about 20 basis points higher.

**Exchange Value of the Dollar**




Against a weighted average of currencies of other important trading partners, the dollar declined slightly, almost fully accounted for by a fall of 2¾ percent against the Mexican peso. The peso's rise nearly fully reversed the decline that occurred against the dollar in early September. The strength of the peso was not matched by currencies of other emerging market economies, and the Brazilian *real* and Chilean peso, in particular, appeared to suffer under concerns about prospects in neighboring Argentina, where equity prices declined significantly in the past week and bond yields moved to record highs.

Foreign short-term interest rates in the major industrial countries generally declined during the intermeeting period. The largest moves down were in Canada and the United Kingdom, where monetary authorities reduced policy interest rates 75 basis points and 25 basis points, respectively. In the euro area, short-term market interest rates declined 13 basis points. The ECB left its policy rates unchanged during the intermeeting period, but market rates drifted down as expectations for an easing of its stance by December or earlier remained in place. The Bank of Japan continued to leave an elevated amount of reserves in the banking system, keeping its current account positions above ¥6 trillion and short-term interest rates near zero.

**Financial Indicators in Major Industrial Countries**

| | Three-month rate | | Ten-year yield | | Equities |
|---|---|---|---|---|---|
| Country | Oct. 31 (Percent) | Percentage Point Change | Oct. 31 (Percent) | Percentage Point Change | Percent Change |
| Canada | 2.50 | -.71 | 4.99 | -.40 | .56 |
| Japan | .03 | .02 | 1.31 | -.10 | 1.18 |
| Euro area | 3.52 | -.13 | 4.41 | -.36 | 8.02 |
| United Kingdom | 4.10 | -.34 | 4.56 | -.33 | 6.10 |
| Switzerland | 1.99 | -.28 | 3.01 | -.29 | 2.24 |
| Australia | 4.24 | -.14 | 5.23 | -.31 | 4.96 |
| United States | 2.11 | -.43 | 4.43 | -.12 | 2.55 |
| Memo: Weighted-average foreign | 2.26 | -.29 | 4.20 | -.32 | n.a. |

NOTE. Change is from October 1 to October 31 (10 a.m. EDT).
n.a. Not available.

Despite a more pessimistic outlook for activity, foreign industrial country stock markets generally rose on net during the period, reflecting perhaps an unwinding of the sharp increase in risk aversion immediately following the terrorist attacks in September as well as some realized or prospective monetary policy easing.

Equity prices in many emerging market countries also rose during the period, as spillovers from building concerns about Argentina failed to check entirely an apparent return of willingness to accept risk. Stock prices in Mexico, Brazil, and

Chile registered net gains, even as Argentine equities slid more than 5 percent. Asian share performance was more mixed, with a double-digit increase in Korea and solid gains in Taiwan and Singapore balanced by very weak performance in the Philippines and declines in China, Malaysia, and Indonesia.

**Financial Indicators in Latin America, Asia, and Russia**

| | Currency/ US dollar | | Short-term Interest rates[1] | | Dollar-denominated bond spread[2] | | Equity prices |
|---|---|---|---|---|---|---|---|
| Economy | Oct. 31 | Percent Change | Oct.30/31 (Percent) | Percentage Point Change | Oct.30/31 (Percent) | Percentage Point Change | Percent Change |
| Mexico | 9.25 | -2.84 | 7.08 | -2.41 | 3.93 | -.43 | 3.50 |
| Brazil | 2.69 | .22 | 19.45 | -.65 | 11.62 | -.21 | 7.18 |
| Argentina | 1.00 | .00 | 22.00 | 4.00 | 20.44 | 3.92 | -5.24 |
| Chile | 711.50 | 2.20 | 6.80 | .38 | 2.90 | .17 | 2.63 |
| China | 8.28 | .00 | n.a. | n.a. | 1.42 | .06 | -4.29 |
| Korea | 1296.00 | -.92 | 4.20 | .00 | 1.55 | -.24 | 12.12 |
| Taiwan | 34.55 | -.14 | 2.92 | -.19 | ... | ... | 7.33 |
| Singapore | 1.83 | 3.14 | .63 | -1.00 | ... | ... | 2.93 |
| Hong Kong | 7.80 | .02 | 2.15 | -.44 | ... | ... | 1.24 |
| Malaysia | 3.80 | .00 | 2.90 | .00 | 1.54 | -.29 | -2.26 |
| Thailand | 44.74 | .34 | 2.75 | -.75 | 3.24 | .38 | .73 |
| Indonesia | 10450.00 | 6.09 | 17.81 | .07 | 5.26 | .06 | -1.27 |
| Philippines | 51.85 | 1.07 | 12.00 | -.63 | 6.71 | .03 | -11.71 |
| Russia | 29.71 | .87 | n.a. | n.a. | 9.21 | -.41 | 13.57 |

NOTE. Change is from October 1 to October 30/31.
1. One month interbank interest rate, except Chile: 30-day deposit rate; Korea: 1-week call rate. No reliable short-term interest rates exist for China or Russia.
2. Spread over similar maturity U.S. Treasury security yield. Mexico, Brazil, Argentina, Korea, the Philippines and Russia: EMBI+ yield. Chile and China: Global bond yield. Malaysia: Eurobond yield. Thailand and Indonesia: Yankee bond yield. Taiwan, Singapore, and Hong Kong do not have outstanding sovereign bonds denominated in dollars.
n.a. Not available. ... Not applicable.

Spillovers from the difficulties faced by Argentina were a bit more apparent in sovereign debt markets. While yield spreads for Mexico and Brazil moved lower on balance during the period, larger declines established earlier in the period had shrunk rapidly by the end as these yields moved up in sync with Argentina's. Sovereign debt yield spreads in Argentina rose nearly 400 basis points on net to about 2050 basis points, with much of that net rise occurring in the past ten days. By the end of the period, market participants were still waiting for an announcement from the government of Argentina on their plans for debt restructuring, and Argentina's debt had been downgraded to only two grades above default. Spillovers from Argentina seemed to show also in South American currency markets, as the Brazilian *real* declined about ¼ percent against the dollar, despite continued sales of dollar-indexed debt by Brazilian authorities, and the Chilean peso depreciated 2¼ percent.

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

## Developments in Foreign Industrial Countries

Economic activity in the foreign industrial economies showed signs of having begun to stabilize in August, but renewed weakness emerged in September. In Japan, recent data point to another sharp decline in output in the third quarter. Data for industrial production in the euro area and the United Kingdom suggest that activity was bottoming out in August, but business confidence collapsed following the terrorist attacks. Growth remained weak in Canada as exports continued to slide.

With oil prices trending down and economic activity weakening, inflation continued to decline. The twelve-month rate of consumer price inflation drifted lower in the euro area and Canada in September, while retail price inflation in the United Kingdom fell back below the Bank of England's 2½ percent target. Deflation continued in Japan.

Citing concerns about deteriorating business and consumer confidence, a number of central banks further eased monetary policy in October. On October 4, the Bank of England cut interest rates 25 basis points, while later that month the Bank of Canada announced a 75-basis-point cut. Banks' reserves held at the Bank of Japan have declined some since late September, but remain at elevated levels. The ECB kept its monetary policy stance unchanged.

Recent economic indicators for **Japan** remain consistent with a sharp contraction in the third quarter. Industrial production plunged 2.9 percent in September and the broader all-industry index moved lower in August. Shipments of machinery also dropped in September. Machinery orders were down steeply in July and August on average from their second-quarter levels, despite an increase in August that followed several months of sharp declines. Private consumption, which had been holding up reasonably well so far this year, also appears to have weakened, with workers' household expenditures down about ½ percent in the third quarter. New passenger car registrations rebounded strongly in August, but early indicators suggest that they plunged again in September. Residential and nonresidential building starts were about flat in August, but fell noticeably in September.

Labor market conditions continued to deteriorate. The unemployment rate rose to a record 5.3 percent in September, with employment down 2 percent from its recent peak in November of last year. The job-offers-to-applicants ratio fell to 0.57, its lowest level since May last year.

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

| Indicator | 2001 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | July | Aug. | Sep. | Oct. |
| Industrial production[1] | -3.6 | -4.1 | -4.3 | -3.0 | .8 | -2.9 | n.a. |
| All-industry index | .9 | -2.0 | n.a. | -1.3 | -.2 | n.a. | n.a. |
| Housing starts | -4.0 | -2.9 | 5.4 | 11.0 | -.4 | -3.4 | n.a. |
| Machinery orders[2] | -7.0 | 1.1 | n.a. | -1.6 | 8.7 | n.a. | n.a. |
| Machinery shipments | -4.6 | -7.2 | -5.3 | -3.6 | 1.2 | -5.8 | n.a. |
| New car registrations | 2.6 | 1.7 | n.a. | -3.6 | 9.6 | n.a. | n.a. |
| Unemployment rate[3] | 4.8 | 4.9 | 5.1 | 5.0 | 5.0 | 5.3 | n.a. |
| Job offers ratio[4] | .63 | .61 | .59 | .60 | .59 | .57 | n.a. |
| Business sentiment[5] | -22 | -27 | -36 | ... | ... | ... | ... |
| CPI (Core, Tokyo area)[6] | -1.4 | -1.3 | -1.2 | -1.1 | -1.2 | -1.2 | -1.0 |
| Wholesale prices[6] | -.5 | -.7 | -1.0 | -.9 | -1.0 | -1.1 | n.a. |

1. Mining and manufacturing.
2. Private sector, excluding ships and electric power.
3. Percent.
4. Level of indicator.
5. Tankan survey, diffusion index.
6. Percent change from year earlier, n.s.a.
n.a. Not available. ... Not applicable.

Prices continued to decline. Core consumer goods prices in the Tokyo area (which exclude fresh food but include energy) were down 1 percent in October from a year earlier. Deflation in wholesale prices for domestic goods has intensified as the impact of the earlier run-up in energy prices has faded.

The merchandise trade surplus (customs clearance basis) widened a little in the third quarter, as a 6 percent drop in imports, largely reflecting weakening domestic demand, outpaced a 4 percent decline in exports.

The Bank of Japan's closely watched Tankan index of business conditions plunged in September, with the diffusion index for all enterprises falling to -36 from -27 in June. The BOJ said it received 70 percent of the survey responses after the September 11 terrorist attacks, although it is not known what portion had actually been filled out before that date. The deterioration was broad-based, with the largest declines recorded in the manufacturing sector. Indicators of excessive inventory levels rose, and the number of firms that expect prices to fall increased for both input and output prices. Expectations for sales growth and profits were revised down, while capital investment was still expected to fall about 6 percent this fiscal year.

The BOJ continued to maintain the level of the outstanding balance of banks' deposits held at the central bank "at above ¥6 trillion." The balance rose to ¥12½ trillion in late September, but has since fallen back to between ¥8-10 trillion. In late October, the government announced plans for a supplemental budget of ¥2.7 trillion (about ½ percent of GDP) for the current fiscal year, of which about ¥1 trillion is expected to be "real-water" spending. Unlike previous spending packages, the focus will be on labor market programs rather than on public works. Press reports suggest that a second supplemental budget may be enacted early next year.

Recent data for the **euro area** suggest that although activity may have been stabilizing in August, the events of September 11 took a toll on business confidence, raising the risk of renewed economic deterioration in the current quarter. Euro-area industrial production rose 1.1 percent in August, after a sharp drop in July, and was just 0.3 percent below the second-quarter level for the two months on average. German manufacturing orders also rebounded in August, led by a notable improvement in domestic orders. In the only available activity data for September (including data from before and after the 11th), French household consumption of manufactured products edged up 0.2 percent following robust gains in the previous two months, as consumption was buoyed by new tax credits to low-income households.

Business sentiment took a sharp downturn in September, but incoming surveys are mixed regarding further deterioration in October. The September euro-area purchasing managers' survey for the manufacturing sector declined to the lowest level in its four-year history. The service sector purchasing managers' survey also declined sharply to just below the level that would indicate contraction of activity. The German Ifo index of business confidence registered its sharpest drop in September since the oil crisis in 1973, declining to a level normally associated with a mild recession. The ISAE Italian business confidence index suffered its worst ever monthly decline in September, falling to its lowest level since 1996. The German ZEW indicator, which is derived from a financial market survey, declined in October to a percent balance of +9.8, much lower than the average of survey responses (+20.8) taken prior to September 11, but a bit higher than the average of responses (+8.0) taken between September 12 and 15. The French INSEE business sentiment index was unchanged in October, as a deterioration in the outlook for manufacturing output–to its lowest level since July 1993–was offset by a less-negative assessment of orders.

**Euro-Area Economic Indicators[1]**
(Percent change from previous period except as noted, s.a.)

| Indicator | 2001 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | June | July | Aug. | Sep. |
| Industrial production[2] | -.1 | -.8 | n.a. | .8 | -1.3 | 1.1 | n.a. |
| Retail sales volume | .7 | .1 | n.a. | .1 | .3 | n.a. | n.a. |
| Unemployment rate[3] | 8.4 | 8.4 | n.a. | 8.4 | 8.3 | 8.3 | n.a. |
| Consumer confidence[4] | 1.0 | -1.7 | -7.7 | -3.0 | -6.0 | -8.0 | -9.0 |
| Industrial confidence[5] | 1.0 | -5.3 | -10.0 | -7.0 | -9.0 | -10.0 | -11.0 |
| Mfg. orders, Germany | -2.7 | -1.7 | n.a. | -2.3 | -1.5 | 1.2 | n.a. |
| CPI[6] | 2.5 | 3.1 | 2.7 | 3.0 | 2.8 | 2.7 | 2.5 |
| Producer prices[6] | 4.7 | 3.9 | n.a. | 3.4 | 2.3 | 1.9 | n.a. |
| M3[6] | 4.5 | 6.3 | 7.6 | 6.3 | 6.5 | 6.7 | 7.6 |

1. Euro-area indicators do not include Greece prior to 2001 but do include Greece as of January.
2. Excludes construction.
3. Euro-area standardized to ILO definition. Includes Eurostat estimates in some cases.
4. Diffusion index based on European Commission surveys in individual countries; Averages of responses to questions on financial situation, general economic situation, and purchasing attitudes.
5. Diffusion index based on European Commission surveys in individual countries; Averages of responses to questions on production expectations, orders, and stocks.
6. Eurostat harmonized definition, 12-month percent change.
n.a. Not available.

Labor market data for the euro area as a whole have yet to show much deterioration, as the harmonized unemployment rate edged down to 8.3 percent in July and remained at that rate in August. National statistics for September, however, show the French unemployment rate rising for the fourth consecutive month and an increase in the German unemployment rate.

The twelve-month rate of euro-area consumer price inflation fell to 2.5 percent in September, still above the ECB's 2 percent target ceiling, and CPI data for Germany and Italy suggest a further moderate decline in October. Core consumer price inflation (which excludes food, energy, alcohol and tobacco) edged up to 2.2 percent in September on a twelve-month basis, but the twelve-month rate of change in producer prices, which peaked at 6.6 percent last October, has moved down steadily this year.

In the **United Kingdom**, the preliminary estimate of real GDP showed a pickup in growth to 2.4 percent in the third quarter. The level of manufacturing output fell, while service sector growth slowed slightly. The preliminary estimate of real GDP is based on the first two months of the quarter, and therefore does not include any possible effects from the September attacks.

Indicators for the fourth quarter paint a mixed picture. Preliminary data suggest that consumer confidence fell slightly in October. Households' expectations of their own financial situation declined as well, but generally remained optimistic. However, business confidence plummeted in October to its lowest level in three years. September surveys of expectations in the service sector are consistent with growth slowing in the fourth quarter.

Labor market conditions continued to be tight. The official claims-based unemployment rate remained at 3.1 percent in September, the lowest rate in 26 years. The labor force survey measure of the unemployment rate increased from a record low of 5 percent for the three months centered in June to 5.1 percent for the three months centered in July.

Largely reflecting declines in gasoline and oil prices, the twelve-month rate of retail price inflation (excluding mortgage interest payments) fell to 2.3 percent in September, below the Bank of England's official target of 2.5 percent. In addition, producer input prices were down 6 percent in September from the same month a year earlier. Average annual earnings growth in August fell below the 4½ percent rate that the Bank of England believes to be compatible with its inflation target.

On October 4, the Monetary Policy Committee (MPC) of the Bank of England cut the official repo rate 25 basis points to 4.5 percent, the sixth 25-basis-point cut this year. In its statement, the MPC cited weaker-than-expected global growth and concerns about business and consumer confidence as reasons for its easing.

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

| Indicator | 2001 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | July | Aug. | Sep. | Oct. |
| Real GDP | 2.6 | 1.8 | 2.4* | ... | ... | ... | ... |
| Industrial production | -.6 | -1.1 | n.a. | -.5 | 1.0 | n.a. | n.a. |
| Retail sales | 1.6 | 1.7 | 1.4 | .6 | .5 | .4 | n.a. |
| Unemployment rate[1] | | | | | | | |
| Claims-based | 3.3 | 3.2 | 3.1 | 3.2 | 3.1 | 3.1 | n.a. |
| Labor force survey[2] | 5.1 | 5.0 | n.a. | 5.1 | n.a. | n.a. | n.a. |
| Business confidence[3] | 8.7 | -.7 | -6.0 | 3.0 | -13.0 | -8.0 | -23.0 |
| Retail prices[4] | 1.9 | 2.3 | 2.4 | 2.2 | 2.6 | 2.3 | n.a. |
| Producer input prices[5] | 4.9 | 4.4 | -3.3 | -1.0 | -3.0 | -6.0 | n.a. |
| Average earnings[5] | 5.0 | 4.8 | n.a. | 4.4 | 4.4 | n.a. | n.a. |

* Preliminary
1. Percent.
2. Three-month average centered on month shown.
3. Percentage of firms expecting output to increase in the next four months less percentage expecting output to decrease.
4. Excluding mortgage interest payments. Percent change from year earlier.
5. Percent change from year earlier.
n.a. Not available. ... Not applicable.

In **Canada**, indicators for the third quarter have tended to be weak. Real GDP was about flat in July and August on average. The trade surplus narrowed in August as exports weakened in all sectors except motor vehicles. Retail sales, however, rose in August, reversing a July decline. Manufacturing shipments increased in August, with gains concentrated in the oil and coal sectors, but new orders declined because of weakness in the aerospace sector. Canada's unemployment rate in September was flat at 7.2 percent, despite a small gain in employment. Consumer confidence fell in the third quarter, with the surveys collected after September 11 little changed from those obtained previously. Business confidence dropped dramatically in the quarter, however, to a level not seen since the 1990-91 recession.

The twelve-month rate of consumer price inflation declined slightly to 2.6 percent in September, comfortably within the Bank of Canada's target range of 1 to 3 percent. On October 23, the Bank lowered its policy rate 75 basis points to 3 percent, bringing the cumulative reduction for this year to 300 basis points. The accompanying announcement stressed the importance of underpinning confidence and supporting domestic demand growth in an environment of exceptional uncertainty.

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

| Indicator | 2001 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | June | July | Aug. | Sep. |
| GDP at basic prices | -.1 | .3 | n.a. | -.2 | -.1 | .1 | n.a. |
| Industrial production | -1.8 | .2 | n.a. | -.9 | -.2 | .1 | n.a. |
| New mfg. orders | -5.4 | 1.5 | n.a. | -3.9 | 1.1 | -.6 | n.a. |
| Retail sales | 1.3 | 2.1 | n.a. | -.2 | -.3 | .3 | n.a. |
| Employment | .2 | .3 | -.1 | -.1 | -.1 | -.1 | .1 |
| Unemployment rate[1] | 6.9 | 7.0 | 7.1 | 7.0 | 7.0 | 7.2 | 7.2 |
| Consumer prices[2] | 2.8 | 3.6 | 2.7 | 3.3 | 2.6 | 2.8 | 2.6 |
| Consumer attitudes[3] | 110.0 | 113.1 | 108.0 | ... | ... | ... | ... |
| Business confidence[3] | 117.5 | 131.6 | 93.0 | ... | ... | ... | ... |

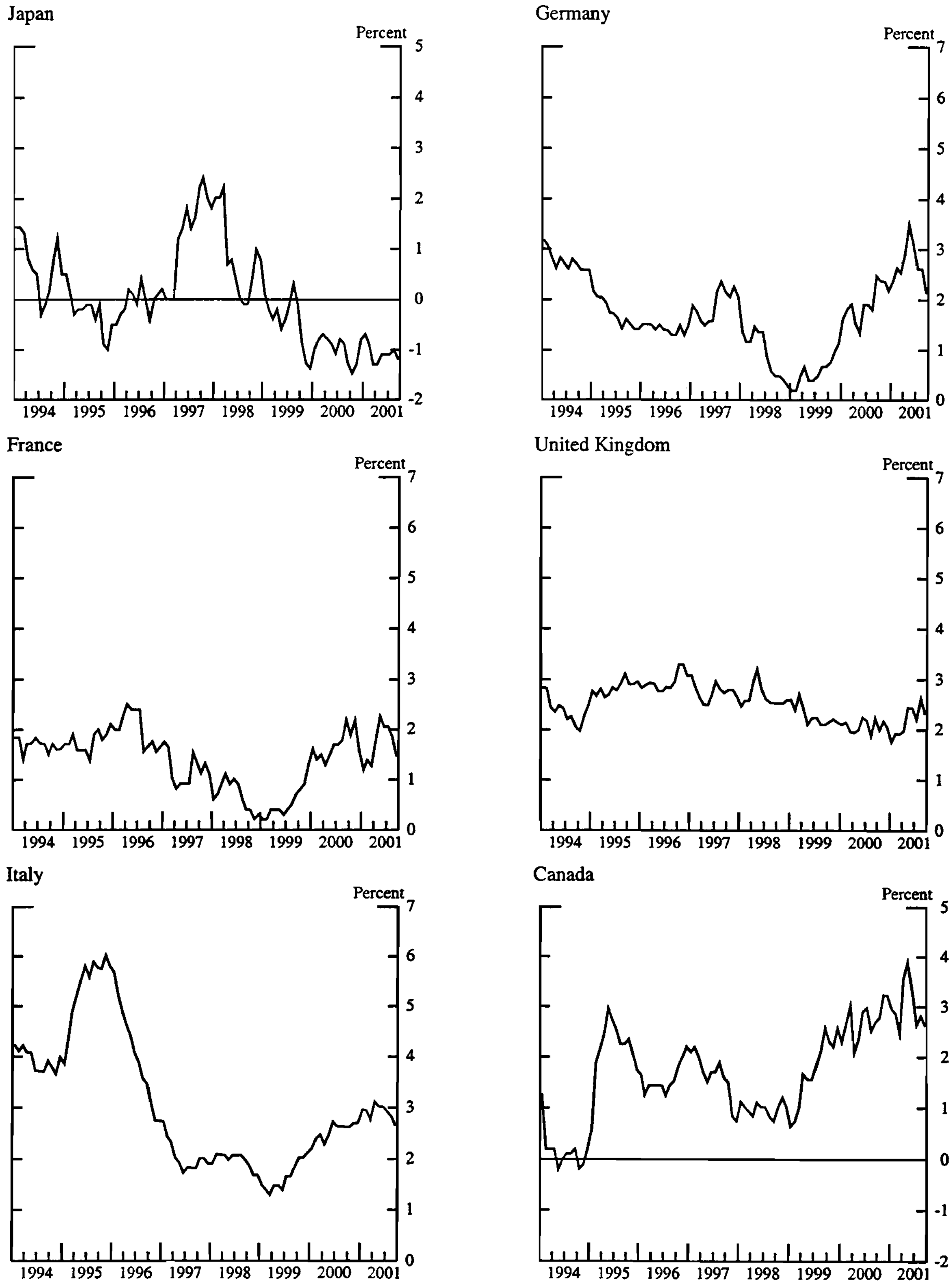
1. Percent.
2. Percent change from year earlier, n.s.a.
3. Level of index, 1991 = 100.
n.a. Not available. ... Not applicable.

**External Balances**
(Billions of U.S. dollars, s.a.a.r.)

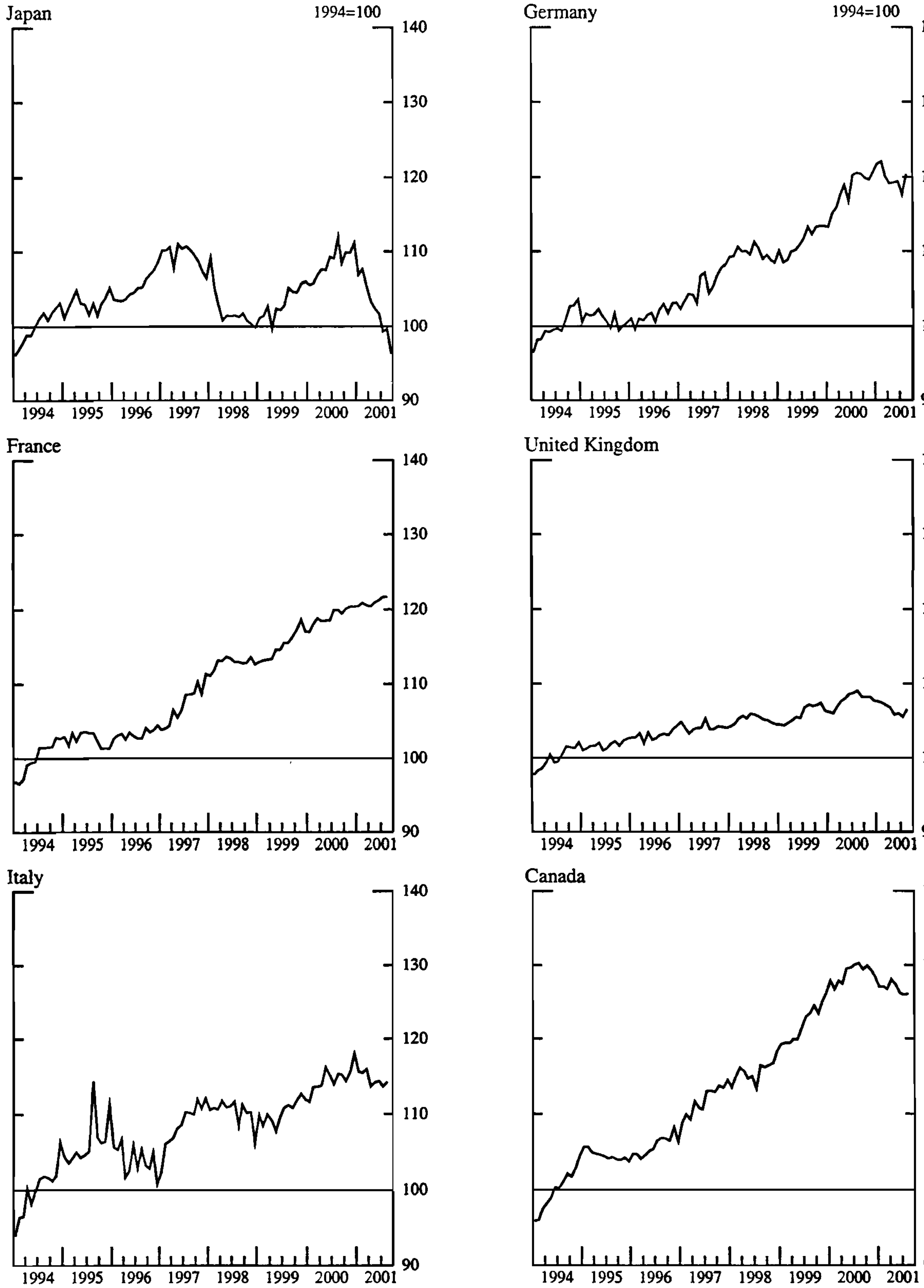
| Country and balance | 2001 | | | | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | July | Aug. | Sep. |
| *Japan* | | | | | | |
| Trade | 67.6 | 50.3 | 55.6 | 32.1 | 62.5 | 72.2 |
| Current account | 101.9 | 67.0 | n.a. | 84.7 | 85.9 | n.a. |
| *Euro area* | | | | | | |
| Trade[1] | -8.0 | 28.1 | n.a. | 95.2 | 58.7 | n.a. |
| Current account[1] | -39.4 | -39.9 | n.a. | -42.4 | 45.4 | n.a. |
| *Germany* | | | | | | |
| Trade | 73.5 | 66.3 | n.a. | 76.6 | 107.8 | n.a. |
| Current account | -3.6 | -8.0 | n.a. | -31.0 | 35.7 | n.a. |
| *France* | | | | | | |
| Trade | .6 | .6 | n.a. | .0 | 3.5 | n.a. |
| Current account | 4.0 | 1.5 | n.a. | 6.3 | 6.8 | n.a. |
| *Italy* | | | | | | |
| Trade | 8.9 | 6.5 | n.a. | -16.2 | .6 | n.a. |
| Current account[1] | -7.7 | .8 | n.a. | 37.2 | -6.3 | n.a. |
| *United Kingdom* | | | | | | |
| Trade | -45.7 | -52.3 | n.a. | -41.8 | -57.4 | n.a. |
| Current Account | -9.2 | -22.1 | n.a. | ... | ... | ... |
| *Canada* | | | | | | |
| Trade | 56.1 | 44.3 | n.a. | 42.5 | 34.5 | n.a. |
| Current Account | 35.3 | 25.6 | n.a. | ... | ... | ... |

1. Not seasonally adjusted.
n.a. Not available. ... Not applicable.

## Consumer Price Inflation in Selected Industrial Countries
(12-month change)



## Industrial Production in Selected Industrial Countries



## Economic Situation in Other Countries

Economic activity in our major developing country trading partners has generally continued to weaken, as adverse spillovers from the slowdown in the United States and other industrial countries have weighed on these economies. In addition, the poor performance of the global high-tech industry has continued to depress activity in emerging Asia, and Argentina's ongoing financial difficulties have caused problems for several of its Latin American neighbors, particularly for Brazil.

Sluggish domestic demand has generally allowed inflationary pressures in these countries to dissipate, although consumer price inflation in Mexico and Indonesia ticked up slightly in September. Developing country exports have remained very depressed, but anemic activity has also restrained imports, and external balances have actually improved in some countries.

Little good news has come out of **Argentina** since the last Greenbook. Industrial production fell almost 1 percent in September, and data for previous months were revised lower. Declines were reported in almost all sectors but were particularly striking in the automotive industry, where sales and output were down over 45 percent in September from their year-earlier levels. Deflation continued with consumer prices falling 1.1 percent over the twelve months ending in September. Tax revenues for September plunged 14 percent from a year earlier. Consumer confidence dropped in early October to its lowest level since mid-1998 when the series began.

Argentina held major elections for all of the seats of the Senate and half of those in the lower house in mid-October. The results showed a solid gain for the opposition Peronist party, which now has a majority in the Senate and the largest minority in the lower house. The result was expected. Nonetheless, it further complicates the process of achieving the government's goals of recording a zero fiscal deficit and implementing structural changes. Another problem facing the government is resolving the debate about possible restructuring of its debt. Although the government has indicated that it is now considering measures to reduce the near-term financing burden imposed by its debt (including debt to international creditors), no specifics have yet been announced. As a consequence of the uncertainty, the spread on Argentine foreign-currency denominated sovereign debt (as measured by the EMBI+ index), which fell more than 150 basis points to just below 1700 basis points after the elections, has recently soared above 2100 basis points. Outflows of reserves and deposits have also picked up again.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | -.6 | -2.4 | 1.1 | n.a. | ... | ... | ... |
| Industrial production | -5.8 | -1.9 | -1.1 | -3.5 | -.5 | -2.7 | -.9 |
| Unemployment rate[2] | 13.8 | 15.1 | 16.4 | ... | ... | ... | ... |
| Consumer prices[3] | -1.8 | -.7 | -.1 | -1.1 | -1.1 | -1.2 | -1.1 |
| Trade balance[4] | -.8 | 2.6 | 4.6 | n.a. | 8.7 | 9.4 | n.a. |
| Current account[5] | -12.0 | -9.0 | -4.0 | n.a. | ... | ... | ... |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent, n.s.a. Data are released for May and October only. Figures for Q2 reflect data for May.
3. Percent change from year-earlier period, except annual figures, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. ... Not applicable.

In **Mexico**, recent data releases further document that the economy continued to shrink in the third quarter. The index of overall economic activity--a proxy for monthly real GDP--declined in August, and industrial production was flat in that month. In line with the weakness of external and domestic demand, exports and imports fell in the third quarter, and the trade deficit widened a little. Although inflation crept up a little in September, the twelve-month inflation rate remained below the government's year-end target of 6½ percent.

Two recent indicators for September suggest that the Mexican economy continues to be hit hard by the slowdown in the United States, including effects resulting from the terrorist attacks. First, the Bank of Mexico's business confidence index plunged in September to a level not seen since the Russian crisis in August 1998. Second, according to Mexico's tourism minister, the number of tourist visits to Mexico declined 35 percent in September. However, the adverse effects on Mexican financial markets in the aftermath of the terrorist attacks appear to have been reversed to a large extent; recently, on balance, equity markets have risen and the Mexican peso has appreciated significantly, more than reversing the depreciation of the currency following the terrorist attacks.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | 5.4 | 5.2 | -1.0 | n.a. | ... | ... | ... |
| Overall economic activity | 3.8 | 6.8 | -.3 | n.a. | .1 | -.2 | n.a. |
| Industrial production | 4.5 | 6.3 | -1.2 | n.a. | -.4 | .0 | n.a. |
| Unemployment rate[2] | 2.5 | 2.2 | 2.3 | 2.4 | 2.5 | 2.3 | 2.3 |
| Consumer prices[3] | 12.2 | 8.9 | 6.9 | 6.0 | 5.9 | 5.9 | 6.1 |
| Trade balance[4] | -5.6 | -8.0 | -8.3 | -9.2 | -10.4 | -8.8 | -8.4 |
| Imports[4] | 142.0 | 174.5 | 170.5 | 166.6 | 168.0 | 165.8 | 166.2 |
| Exports[4] | 136.4 | 166.5 | 162.2 | 157.4 | 157.6 | 157.0 | 157.7 |
| Current account[5] | -14.4 | -18.7 | -13.5 | n.a. | ... | ... | ... |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent; counts as unemployed those working one hour a week or less.
3. Percent change from year-earlier period, except annual figures, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. ... Not applicable.

In **Brazil**, data releases since the last Greenbook have pointed to weak activity, particularly in consumption. Industrial production edged up a little in August, after several months of declines, supported by a 6 percent increase in capital goods production. However, output of consumer durable goods declined 7 percent in August. There was also a 5 percent seasonally-adjusted fall in auto production in September but, despite this, inventories rose that month. The consumer confidence indicator declined 9 percent in October. Weak domestic demand, and consequent weakness in imports, largely accounts for the improvement in the trade balance in the third quarter. Consumer prices rose 6.4 percent in September from their year-earlier levels, slightly above the 6 percent upper bound of the central bank's inflation target range.

The Brazilian *real* and other Brazilian asset prices continued to come under downward pressures, in part reflecting spillovers from the market jitters in Argentina, prompting the Brazilian government in late September to draw on the $4.7 billion in IMF funds that had been made available to it on September 14 upon approval of Brazil's new $15 billion support package. The government also issued sizeable amounts of dollar-indexed debt, raising the stock of the debt from $72 billion at end-August to $80 billion at end-September. The central bank kept its policy overnight interest rate steady at 19 percent, citing concerns about the effect of the depreciation of the currency on inflation.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | 4.0 | 4.3 | .1 | n.a. | ... | ... | ... |
| Industrial production | -.7 | 6.7 | -3.5 | n.a. | -.6 | .2 | n.a. |
| Unemployment rate[2] | 7.6 | 7.1 | 6.2 | 6.1 | 6.1 | 6.1 | 6.3 |
| Consumer prices[3] | 8.9 | 6.0 | 7.0 | 6.6 | 7.0 | 6.3 | 6.4 |
| Trade balance[4] | -1.3 | -.7 | -3.8 | 6.4 | .6 | 11.1 | 7.6 |
| Current account[5] | -25.4 | -24.6 | -27.4 | -16.3 | -24.4 | -13.7 | -10.8 |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent. "Open" unemployment rate.
3. Percent change from year-earlier period, except annual figures, which are Dec./Dec. Price index is IPC-A.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. ... Not applicable.

There has been little new information on the **Venezuelan** economy since the last Greenbook. Reports have pointed to strength in the construction and telecommunications industries, in part reflecting increased government expenditure. However, the decline in oil prices is beginning to temper the recovery and has worsened fiscal imbalances. After coming under pressure in September, international reserves have picked up slightly this month but remain below their end-2000 levels.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | -4.1 | 6.1 | 1.5 | n.a. | ... | ... | ... |
| Unemployment rate[2] | 15.2 | 13.4 | 13.6 | n.a. | n.a. | n.a. | n.a. |
| Consumer prices[3] | 20.0 | 13.4 | 12.4 | 12.7 | 13.0 | 12.9 | 12.3 |
| Non-oil trade balance[4] | -9.1 | -10.8 | -11.9 | n.a. | n.a. | n.a. | n.a. |
| Trade balance[4] | 7.6 | 18.0 | 11.8 | n.a. | n.a. | n.a. | n.a. |
| Current account[5] | 3.7 | 13.4 | 6.7 | n.a. | ... | ... | ... |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent, n.s.a.
3. Percent change from year-earlier period, except annual figures, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. ... Not applicable.

In **Korea**, industrial production registered significant increases in August and September following four consecutive monthly declines. The strong figure for industrial production in September appears to have overstated the underlying strength of production, as the Korean Thanksgiving holiday fell in early October this year, rather than in late September as it usually does, meaning that September had three more working days than usual. Even taking account of this apparent distortion, however, these production figures seem to suggest a surprising resiliency in activity in Korea. Despite the strong production figures, the index of business sentiment dropped sharply in September, falling to its lowest level in nine months.

Korean officials have indicated that the government hopes to announce soon a plan to reprivatize the banking system, selling off stakes in banks acquired after the 1997-1998 financial crisis, even if such sales result in substantial losses relative to the amount of funds that the government has put into the banks or if privatized banks wind up in foreign hands. The government currently has full equity control of seven major Korean banks and minority stakes in a number of others. So far, only one bank, Korean First Bank, has been sold by the government to private interests.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | 13.8 | 5.2 | 1.8 | n.a. | ... | ... | ... |
| Industrial production | 24.1 | 17.0 | -1.5 | 1.5 | -1.3 | 4.9 | 2.9 |
| Unemployment rate[2] | 6.3 | 4.1 | 3.7 | 3.5 | 3.7 | 3.6 | 3.3 |
| Consumer prices[3] | 1.3 | 3.1 | 5.3 | 4.3 | 5.1 | 4.7 | 3.2 |
| Trade balance[4] | 28.4 | 16.9 | 16.6 | 12.4 | 9.2 | 14.9 | 13.0 |
| Current account[5] | 24.5 | 11.4 | 14.7 | 4.3 | 5.3 | -2.3 | 9.8 |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent.
3. Percent change from year earlier, except annual changes, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. ... Not applicable.

Data for the ASEAN region continue to point to significant weakness. The decline in global demand for electronics has battered the economy of Singapore, where real GDP plummeted at a 10 percent annual rate in the third quarter. Industrial production in Malaysia, which exports significant quantities of electronic goods, has also posted recent declines, and output has also decreased in Indonesia in recent months, as demand for its consumer goods exports has fallen. In response to the weakness in activity, both Singapore and Malaysia have announced fiscal stimulus packages and loosened monetary policy. The Philippines also has lowered interest rates but is constrained in expanding fiscal policy due to an already high debt burden.

Despite the slump in external demand, the countries in the region, with the exception of the Philippines, continued to register trade surpluses. This reflects the fact that, although exports have fallen rapidly (especially exports of electronic goods), imports have also declined sharply, both because of the high import content of the region's exports and slowdowns in domestic demand. Indonesia continues to struggle with relatively high inflation, but inflation fell during the third quarter in the rest of the region, reflecting the weakness in domestic demand.

## ASEAN Economic Indicators: Growth

(Percent change from previous period, s.a., except as noted)

| Indicator and country | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| *Real GDP*[1] | | | | | | | |
| Indonesia | 6.4 | 5.7 | 6.5 | n.a. | ... | ... | ... |
| Malaysia | 11.5 | 6.4 | -8.5 | n.a. | ... | ... | ... |
| Philippines | 5.1 | 3.9 | 6.0 | n.a. | ... | ... | ... |
| Singapore | 8.0 | 11.0 | -10.7 | -9.7 | ... | ... | ... |
| Thailand | 6.4 | 3.1 | .6 | n.a. | ... | ... | ... |
| *Industrial production*[2] | | | | | | | |
| Indonesia[3] | -1.0 | 11.6 | 3.1 | n.a. | -1.9 | -2.2 | n.a. |
| Malaysia | 9.0 | 19.2 | -5.3 | n.a. | 3.8 | -1.2 | n.a. |
| Philippines | 3.5 | 15.1 | -.3 | n.a. | -8.7 | 14.1 | n.a. |
| Singapore | 13.7 | 15.4 | -6.1 | -8.6 | 1.4 | -2.6 | -5.3 |
| Thailand | 12.6 | 3.1 | -.1 | .2 | -.6 | 1.7 | .1 |

1. Annual rate. Annual figures are Q4/Q4.
2. Annual figures are annual averages.
3. Staff estimate.
n.a. Not available. ... Not applicable.

## ASEAN Economic Indicators: Trade Balance

(Billions of U.S. dollars, s.a.a.r.)

| Country | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Indonesia | 24.7 | 28.6 | 22.3 | n.a. | 26.5 | 29.1 | n.a. |
| Malaysia | 19.1 | 16.0 | 13.9 | n.a. | 15.7 | 14.5 | n.a. |
| Philippines | 4.3 | 6.7 | -1.3 | n.a. | .5 | -1.0 | n.a. |
| Singapore | 3.6 | 3.3 | 6.0 | 4.8 | 4.6 | 8.0 | 1.6 |
| Thailand | 9.3 | 5.5 | 3.2 | 3.7 | -1.4 | 10.5 | 2.0 |

n.a. Not available.

**ASEAN Economic Indicators: CPI Inflation**
(Percent change from year earlier, except as noted)

| Country | 1999[1] | 2000[1] | 2001 Q2 | 2001 Q3 | 2001 July | 2001 Aug. | 2001 Sept. |
|---|---|---|---|---|---|---|---|
| Indonesia | 2.0 | 9.3 | 11.1 | 12.8 | 13.0 | 12.2 | 13.0 |
| Malaysia | 2.5 | 1.3 | 1.6 | 1.4 | 1.4 | 1.3 | 1.4 |
| Philippines | 4.3 | 6.6 | 6.7 | 6.4 | 6.8 | 6.3 | 6.1 |
| Singapore | .9 | 2.1 | 1.7 | .8 | 1.3 | .7 | .5 |
| Thailand | .7 | 1.3 | 2.5 | 1.6 | 2.2 | 1.4 | 1.4 |

1. December/December.

In **China**, following two months of slower growth, industrial production rebounded in September. Retail sales also showed strength in September, rising 9.9 percent from a year earlier and up slightly from August. In response to the successful conclusion of China's negotiations with the WTO, indicators of current and future foreign direct investment (FDI) were up sharply in September, after pointing to a slowdown in August. This suggests that although the global investment climate has weakened, China is continuing to attract large quantities of foreign investment. The gains in FDI and consumer spending were somewhat offset by reduced investment by state-owned enterprises in September relative to August.

One potential sign of weakness in China has been a return to deflation; consumer prices declined slightly for the twelve months ending in September. Prices of food and services have increased in recent months, but prices of industrial goods have declined. The excess supply of industrial products may be a result of external weakness, which has led some exporters to turn to the domestic market. After sharp declines earlier in the year, exports recorded slow but steady growth for the third consecutive month in September, but imports fell from an unusually high level in August.

Data received since the last FOMC meeting suggest that economic conditions in **Hong Kong** continued to deteriorate. The unemployment rate increased to 5.3 percent in the third quarter, the highest level since early last year. The volume of retail sales was up less than 1 percent in August after plummeting nearly 7 percent in July. Also indicative of continued weak demand, consumer prices fell 1.2 percent over the twelve months ended September. Exports and imports both increased modestly in September, with little change in the trade balance.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | 4.1 | 8.0 | 7.5 | 6.9 | ... | ... | ... |
| Industrial production[2] | 8.0 | 11.4 | 10.6 | 8.5 | 8.1 | 8.1 | 9.5 |
| Consumer prices[2] | -1.0 | 1.5 | 1.6 | .8 | 1.5 | 1.0 | -.1 |
| Trade balance[3] | 29.2 | 24.1 | 21.1 | 8.3 | 18.6 | -8.4 | 14.9 |

1. Annual rate. Quarterly data estimated by staff from reported four-quarter growth rates. Annual figures are Q4/Q4.
2. Percent change from year earlier. Annual figures are year over year.
3. Billions of U.S. dollars, annual rate. Imports are c.i.f.
... Not applicable.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | 9.3 | 6.6 | -6.6 | n.a. | ... | ... | ... |
| Unemployment rate[2] | 6.3 | 5.1 | 4.5 | 5.3 | 4.7 | 4.9 | 5.3 |
| Consumer prices[3] | -4.0 | -2.1 | -1.3 | -1.1 | -.9 | -1.2 | -1.2 |
| Trade balance[4] | -5.6 | -11.0 | -11.5 | -14.0 | -15.8 | -12.8 | -13.4 |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent. Monthly numbers are averages of the current and previous two months.
3. Percent change from year-earlier period, except annual figures, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.
n.a. Not available. ... Not applicable.

Indicators released over the past month suggest that the recession in **Taiwan** has deepened. Unemployment continued its trend upward and industrial production plummeted nearly 8 percent in September (s.a.). Declines were fairly widespread across industries, but the information and electronics sectors suffered the sharpest drop. Exports declined 21 percent in September (s.a.), reflecting the effects of recent typhoons and, perhaps, the early implications of the terrorist attacks. Imports fell nearly 8 percent in September, following an already sharp decline in August, reflecting the weakness in demand, especially for imported inputs. Consumer prices decreased slightly in September from their year-earlier levels.

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

| Indicator | 1999 | 2000 | 2001 | | | | |
|---|---|---|---|---|---|---|---|
| | | | Q2 | Q3 | July | Aug. | Sept. |
| Real GDP[1] | 6.5 | 3.8 | -10.1 | n.a. | ... | ... | ... |
| Unemployment rate[2] | 2.9 | 3.0 | 4.4 | 4.9 | 4.7 | 4.8 | 5.0 |
| Industrial production | 7.7 | 7.4 | -2.9 | -1.5 | -1.2 | 5.5 | -7.8 |
| Consumer prices[3] | .1 | 1.7 | .0 | .0 | .1 | .4 | -.5 |
| Trade balance[4] | 10.9 | 8.3 | 13.7 | 9.2 | 7.7 | 18.2 | 1.8 |
| Current account[5] | 8.4 | 8.9 | 14.7 | n.a. | ... | ... | ... |

1. Annual rate. Annual figures are Q4/Q4.
2. Percent.
3. Percent change from year-earlier period, except annual figures, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.
5. Billions of U.S. dollars, n.s.a., annual rate.

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