JOINT ECONOMIC COMMITTEE
ROBERT F. BENNETT, VICE CHAIRMAN

RECENT ECONOMIC DEVELOPMENTS
MAY 1, 2006

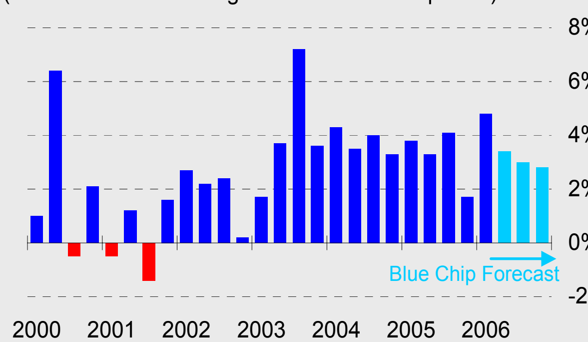
Economy Surges in the First Quarter

Growth in the inflation-adjusted (real) gross domestic product (GDP) surged to an annualized rate of 4.8%, the fastest growth in 2-½ years and more than twice the 1.7% rate posted in the 4th quarter of last year. Strong employment growth, averaging about 200,000 new payroll jobs in each of the first three months of this year, and continued low unemployment has helped support overall economic growth. Energy prices remain elevated, but recent accelerations have not passed through significantly to prices of other goods and services. Outside of energy prices, inflation remains generally well contained and measures of inflation expectations seem stable.

Highlights

- Annualized real GDP growth was a rapid 4.8% in the 1st quarter, on the heels of 1.7% annualized growth a quarter earlier. (Fig. 1)
- Payroll employment rose by a healthy 211,000 new jobs in March, the 31st consecutive month of employment gains (Fig. 2, next page).
- The unemployment rate edged down to 4.7% in March from 4.8% in February. The unemployment rate averaged a low of 4.7% in the 1st quarter.
- Energy prices accelerated in recent weeks, with benchmark futures prices of crude oil setting record highs above $70 a barrel. Gasoline prices have also risen.

Economic Growth Since 2000 Fig. 1
(Real annualized GDP growth rate in each quarter)



Sources: Bureau of Economic Analysis

4.8% Annualized GDP Growth in the First Quarter

The advance estimate of *GDP growth* for the 1st quarter soared to 4.8%, up from a moderate 1.7% rate in the 4th quarter of last year. The increase in GDP in the 1st quarter reflected robust growth in consumer spending (which increased 5.5%), nonresidential fixed investment (increased 14.3%) exports (increased 12.1%), and federal government spending (increased 10.8%). Those contributions to growth were partly offset by a reduction in inventory investment along with 13.0% growth in imports. Imports are a subtraction in the calculation of gross domestic product. There have been 18 consecutive quarters of positive growth in GDP, with growth averaging a healthy 3.2%. The *Blue Chip* forecast—a monthly consensus of private forecasters—is for real GDP growth to return toward healthy trend-like rates of between 3.4% and 2.8% during the remaining quarters of this year (Fig. 1).

Over 5.1 Million New Jobs in 31 Consecutive Months of Job Gains

The economy added 211,000 new *payroll jobs* in March, the 31st consecutive month with job gains (Fig. 1). Over 5.1 million new jobs have been added to payrolls in that period, and 2.1 million new jobs have been created in the last year alone (Fig. 2, next page). The *unemployment rate*, based on a survey of households, edged down to 4.7% in March, remaining below the averages of the 1960s, 1970s, 1980s, and 1990s and well below the near-term peak of 6.3% in June 2003.

Energy Prices Rise Again…

Last year was the third consecutive year of rising and volatile energy prices and those prices have again risen in recent weeks. Benchmark futures *prices of crude oil* set record dollar-value highs in recent weeks of around $75 a barrel. *Gasoline prices* have also risen, reflecting higher prices of crude oil and, at least partly, capacity constraints in refining of distillates which sometimes interrupts supplies. The national average price per gallon of regular unleaded gas rose above $2.90 in recent weeks and prices at the pump in some regions surpassed $3.00. When supplies get tight, prices rise to allocate a scarce resource to its most highly valued uses.

…Yet General Inflation Remains Contained

Increases in energy prices continue to push up overall *consumer price inflation,* but the energy price increases have not significantly "passed through" into higher inflation in prices of goods and services in general. Year-over-year inflation in the "core" consumer price index (CPI), which excludes volatile energy and food prices, remains low. Core CPI inflation was 2.10% in March, below the core inflation rate last year. Annual inflation in the core *personal consumption expenditure price index*, the Fed's preferred measure of consumer price inflation, remained below 2.00% in the first two months of this year. Inflation rates in core price indexes provide useful indicators of long-term inflation trends.

Federal Reserve is Expected to Raise Rates Again

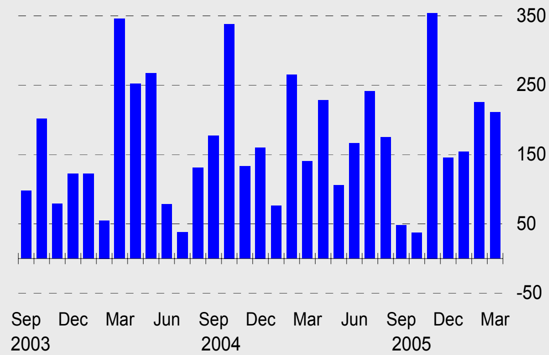
With robust economic growth and risks of energy price increases leading to higher general inflation, markets expect that the *Federal Reserve* will continue its recent course of monetary policy by increasing its target for overnight interest rates again by a quarter percent at its policymaking meeting scheduled for May 10. Market guesses about yet another quarter-point increase at the meeting on June 28 and 29 have been variable and "data dependent." The Fed has raised its target overnight rate from 1.00% to the current 4.75% in a sequence of quarter-point increases that began in June 2004.

Housing Market is Cooling

Both new and existing home sales have fallen, on net, from their peak highs of last summer and early autumn (Fig. 3). House prices, which have accelerated rapidly in the past several years, appear to be growing at slower rates. The median sales price of existing homes, for example, grew 7.4% on a year-over-year basis in March, down from a peak of almost 15.7% in August 2005.

Over 5.1 Million New Jobs in Past 31 Months Fig. 2

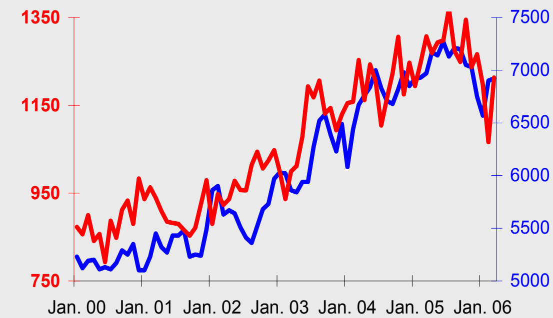
(Change in employment, in thousands)



Source: Bureau of Labor Statistics

Existing and New Home Sales Fig. 3

(Thousands)



Source: Haver Analytics and National Association of Realtors

Upcoming Indicators

Employment – The Bureau of Labor Statistics reports April's employment situation on *May 5.*

Federal Reserve – The Fed's next monetary policy meeting is scheduled for *May 10.*

Inflation – The Consumer Price Index for April is scheduled to be released on *May 17.*

GDP – The second look at GDP growth for the 1st quarter is scheduled for release on *May 25.*