



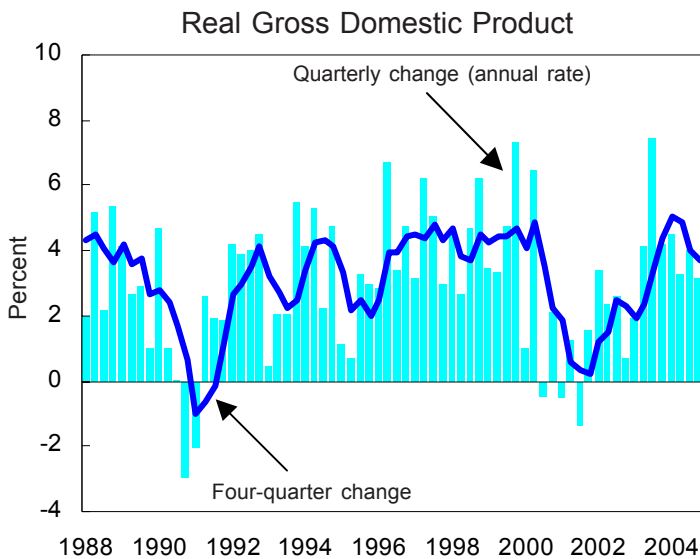
WEEKLY ECONOMIC DIGEST



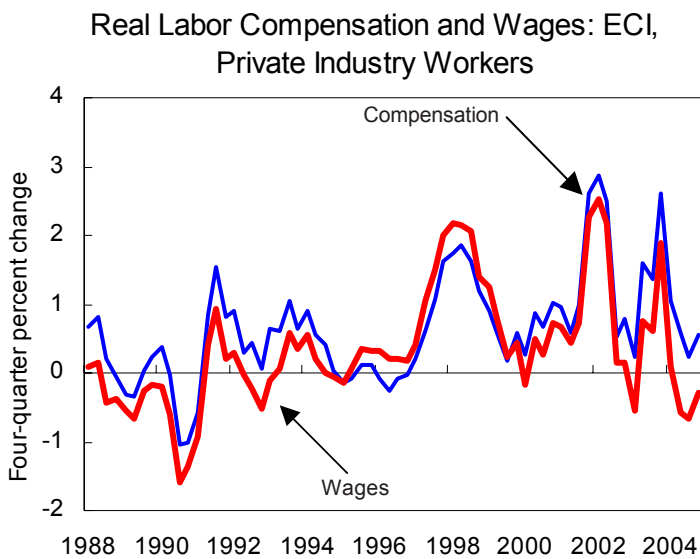
JOINT ECONOMIC COMMITTEE – DEMOCRATIC STAFF
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February 1, 2005

GDP Growth Slows, but Fed is Likely to Keep Raising Rates



Source: Bureau of Economic Analysis, U.S. Department of Commerce.



Sources: Bureau of Labor Statistics, U.S. Department of Labor and JEC staff calculations.

- **Output growth slowed in the fourth quarter.** Real (inflation-adjusted) gross domestic product (GDP) grew at a 3.1 percent annual rate after posting a 4 percent gain in the third quarter, according to advance estimates published by the Department of Commerce. Real GDP, the most comprehensive measure of domestic production, was 3.7 percent above its level at the end of 2003. In past recoveries, output growth like that seen in 2004 would have generated more jobs than were in fact generated last year, but strong growth in labor productivity (output per hour) meant that fewer workers could produce the same output.
- **A decline in exports slowed GDP growth.** Real consumption grew at a 4.6 percent annual rate, but some of that demand was met by imports (which do not contribute to GDP) rather than by domestic production. Also, exports of U.S. produced goods declined by 6.9 percent in the fourth quarter. That drop in exports stemmed from weakness in foreign economic activity that many analysts believe is temporary.
- **Growth in employment costs slowed at year's end.** Between October and December of last year, the employment cost index (ECI) for private industry workers rose at an annual rate of 2.8 percent, down slightly from 3.6 percent over the previous three months. The ECI includes non-wage compensation (benefits) as well as wages. From December 2003 to December 2004, the ECI rose by 3.8 percent. However, real (inflation-adjusted) total compensation rose by only 0.5 percent, and the wage component fell 0.3 percent.
- **The Fed is likely to keep raising rates.** The Federal Open Market Committee (FOMC) is expected to announce that it will raise its target for the federal funds rate by $\frac{1}{4}$ percentage point to $2\frac{1}{2}$ percent at the conclusion of its two-day policy meeting tomorrow. With real GDP growing somewhat faster than its long-run potential growth rate, the FOMC will probably stick to its self-described "measured" approach to raising rates.

The Economy at a Glance	Dec	Nov	Oct	Sep	2004 Qrt 4	2004 Qrt 3	2004 Qrt 2	2004 Qrt 1	2004	2003
Economic Activity										
Real GDP (% growth)	—	—	—	—	3.1	4.0	3.3	4.5	4.4	3.0
Industrial Production (% growth)	10.0	2.4	10.0	-3.5	4.1	2.7	4.3	5.6	4.1	0.0
Capacity Utilization (level, %)	79.2	78.6	78.5	78.0	78.8	78.2	77.9	77.3	78.0	75.5
Civilian Unemployment Rate (level, %)*	5.4	5.4	5.5	5.4	5.4	5.5	5.6	5.6	5.5	6.0
Housing Starts (thousands)	2004	1807	2065	1905	1959	1969	1920	1943	1948	1853
Real Disposable Personal Income (% growth)	9.4#	2.4	2.4	1.2	4.1#	2.0	2.8	2.4	3.1#	2.3
Retail Sales (% growth)	15.4	1.2	13.3	21.1	10.3	5.7	6.6	10.4	7.6	5.3
Personal Saving Rate (level, %)	0.1#	0.3	0.2	0.3	0.2#	0.5	1.3	1.0	0.8#	1.4
Inflation & Productivity										
CPI-U Inflation, all items (% growth)	-1.2	2.4	7.4	2.4	3.0	0.6	4.8	5.1	2.7	2.3
Core CPI-U Inflation (% growth)	2.4	2.4	2.4	3.7	2.0	1.8	2.3	2.9	1.8	1.5
Employment Cost Index (% growth)	—	—	—	—	2.8	3.6	4.1	4.5	3.7	4.1
Output per Hour (% growth)*	—	—	—	—	n.a.	1.8	3.9	3.7	n.a.	4.4
Financial Markets										
T-bill Rate, 3-month (level, %)	2.19	2.07	1.76	1.65	2.01	1.49	1.08	0.92	1.37	1.01
T-note Rate, 10-years (level, %)	4.23	4.19	4.10	4.13	4.17	4.30	4.60	4.02	4.27	4.01
Federal Funds Rate (level, %)	2.16	1.93	1.76	1.61	1.95	1.43	1.01	1.00	1.35	1.13
Dow Jones Industrial Avg (index level)	10673	10412	10002	10205	10362	10130	10289	10488	10317	8994

Sources: Bureau of Economic Analysis, U.S. Department of Commerce; Bureau of the Census, U.S. Department of Commerce; Bureau of Labor Statistics, U.S. Department of Labor; Board of Governors of the Federal Reserve System; Wall Street Journal; and Haver Analytics.

Notes: Except where otherwise noted, values in the table represent percentage growth measured at seasonally adjusted **annual** rates. Growth in retail sales includes food services. Core CPI-U inflation is the percentage change in the CPI-U excluding food and energy as reported by the Bureau of Labor Statistics. The Employment Cost Index is for workers in private industry. Productivity is output per hour for private nonagricultural establishments. The 3-month Treasury bill rate is the secondary market rate.

n.a. Denotes that data are not yet available.

* Subject to revision over the next week.

Adjusted by the JEC staff to exclude the temporary effects of Microsoft's special dividend payment in December.

Upcoming Economic Releases:

- **Federal Open Market Committee announcement on monetary policy** [Release: Wednesday, February 2]
- **Productivity and Costs, Fourth Quarter 2004 (Advance)** [Release: Thursday, February 3]
- **The Employment Situation: January 2005** [Release: Friday, February 4]

The employment release will reflect annual revisions to historical employment, unemployment, and labor force data and could raise the level of employment in 2004 by a modest amount.