Prefatory Note

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Please note that some material may have been redacted from this document if that material was received on a confidential basis. Redacted material is indicated by occasional gaps in the text or by gray boxes around non-text content. 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 optical 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.

Content last modified 5/20/2009.

Confidential (FR)   Class III FOMC

Part 2

September 10, 2003

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

The pace of economic expansion appears to be picking up, although the indicators have not been uniformly positive. Domestic final demand has strengthened appreciably in recent months, with solid gains in both household and business spending. But firms have continued to liquidate inventories and to shed workers. Core consumer price inflation has rebounded in the past few months from the extraordinarily low rates of earlier this year; even so, the twelve-month change in core CPI prices was 1-1/2 percent in July, about 3/4 percentage point less than the increase a year earlier.

Labor Market Developments

The labor market continued to deteriorate in August. Reflecting widespread losses, private nonfarm payroll employment fell 67,000 last month after similar declines in June and July. Only construction (+19,000) and health services (+25,000) enjoyed substantial job gains, while manufacturing (-44,000), transportation (-7,000), wholesale trade (-10,000), information (-16,000), and professional and business services (-28,000) posted sizable losses. Temporary help-supply services added only 7,000 jobs in August, and the July gain in that industry was revised down 30,000, to just 12,000.

The average workweek of production or nonsupervisory workers was unchanged last month at 33.6 hours, 0.1 hour below its second-quarter average.[1] With declining employment and a flat workweek, aggregate production-worker hours fell 0.1 percent in August, to a level 2.1 percent (annual rate) below the second-quarter average. However, hours worked by the self-employed—an especially volatile series—increased rapidly for the second month in a row after having plummeted in the second quarter.

In the household survey, the unemployment rate ticked down to 6.1 percent in August. After having hovered around 5-3/4 percent between the first quarter of 2002 and the first quarter of 2003, the jobless rate has exceeded 6 percent since April. Meanwhile, the labor force participation rate remained at 66.2 percent in August. The number of job losers unemployed less than five weeks as a percent of household employment edged down in August, suggesting that layoffs continue to abate from their elevated pace in the spring.

Indeed, the four-week moving average of initial claims for unemployment insurance has remained around of 400,000 since early August, while the four-week moving average of insured unemployment has crept down a bit since the beginning of the summer, although it remains above its level early in the year.

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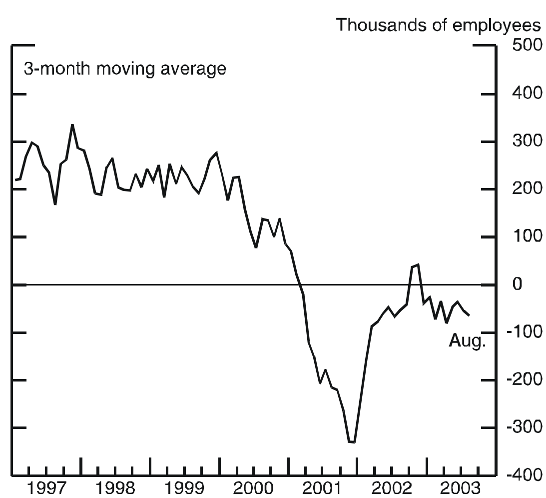
1. The Bureau of Labor Statistics (BLS) estimates that the mid-August blackout, which occurred during the reference week for the establishment survey, had only a small depressing effect on total production-worker hours.

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

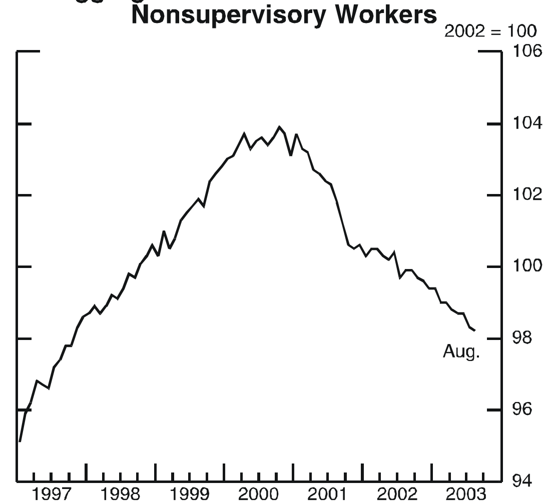
	2002	2003 Q1	2003 Q2	2003 June	2003 July	2003 Aug.
	-Average monthly change-					
Nonfarm payroll employment[1]	-39	-38	-60	-83	-49	-93
Private	-55	-35	-37	-75	-56	-67
Previous	*-55*	*-35*	*-35*	*-71*	*-34*	*n.a.*
Manufacturing	-57	-49	-61	-54	-59	-44
Construction	-4	-4	27	14	3	19
Wholesale trade	-7	-3	-8	-11	-12	-10
Retail trade	-6	-4	-10	-15	-2	-4
Transportation and utilities	-4	-6	-15	-17	-21	-7
Information	-14	-16	-7	-9	-10	-16
Financial activities	5	14	14	1	3	-1
Professional and Business services	-10	3	9	4	46	-28
Temporary Help Services	1	-8	24	30	12	7
Non-business services[2]	45	33	13	10	-3	25
Total government	16	-3	-24	-8	7	-26
Total employment (household survey)	31	303	130	251	-260	147
Memo:						
Aggregate hours of private production workers (percent change)[1,3]	-1.0	-1.7	-1.6	0.0	-0.4	-0.1
Average workweek (hours)[1]	33.9	33.8	33.7	33.7	33.6	33.6
Manufacturing (hours)	40.5	40.4	40.2	40.3	40.1	40.1

n.a. Not available.
Note. Average change from final month of preceding period to final month of period indicated.
1. Survey of establishments.
2. Non-business services comprises education and health, leisure and hospitality, and "other."
3. 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



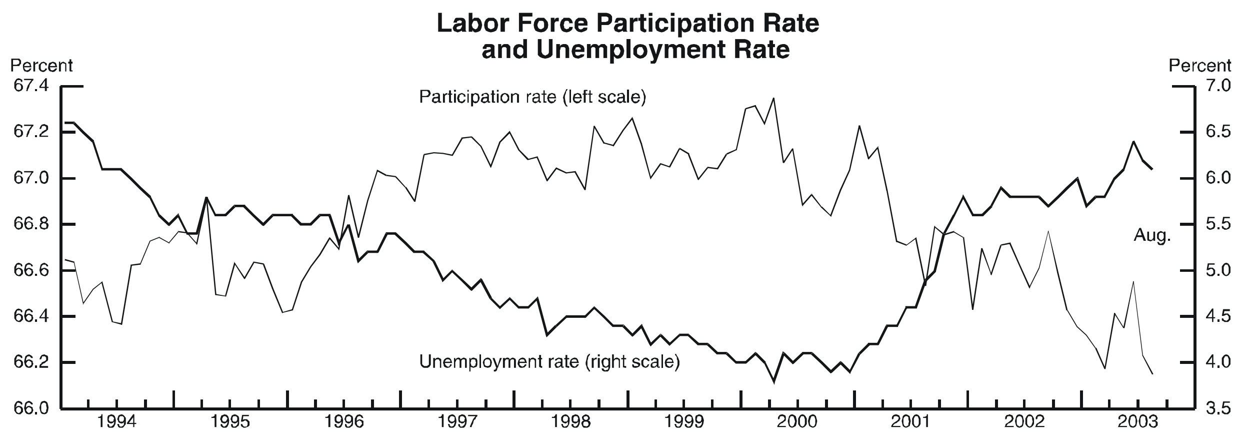
Aggregate Hours of Production or Nonsupervisory Workers

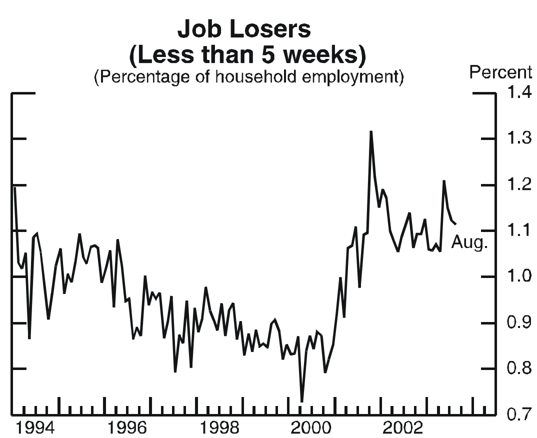


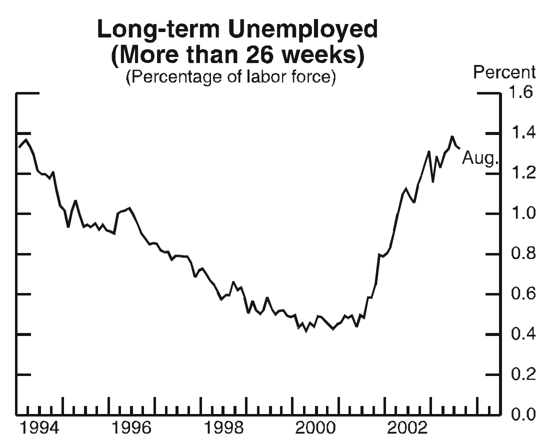
SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES

(Percent; based on seasonally adjusted data)

		2002	2003		2003		
	2002	Q4	Q1	Q2	June	July	Aug.
Civilian unemployment rate (16 years and older)	5.8	5.9	5.8	6.2	6.4	6.2	6.1
Teenagers	16.5	16.1	17.2	18.6	19.3	18.4	16.6
20-24 years old	9.7	9.9	9.2	10.4	10.7	10.3	10.3
Men, 25 years and older	4.7	4.9	4.9	5.3	5.5	5.2	5.3
Women, 25 years and older	4.6	4.6	4.4	4.6	4.7	4.7	4.6
Labor force participation rate	66.6	66.5	66.3	66.4	66.6	66.2	66.2
Teenagers	47.4	46.8	45.2	45.1	45.1	44.3	44.3
20-24 years old	76.4	75.8	75.5	75.9	76.2	75.4	75.3
Men, 25 years and older	75.9	75.6	75.3	75.6	75.6	75.4	75.5
Women, 25 years and older	59.4	59.4	59.6	59.8	59.9	59.6	59.6







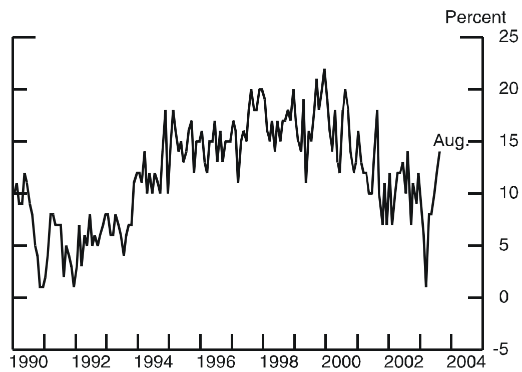
Labor Market Indicators

Unemployment Insurance

Layoff Announcements

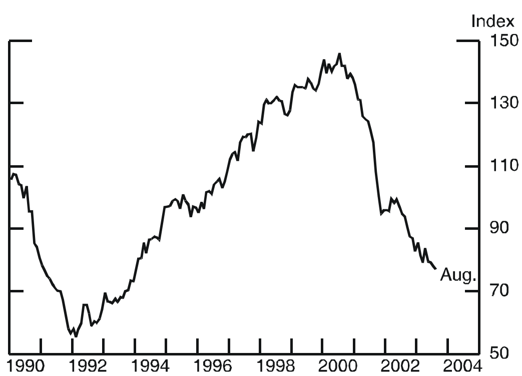
Note. Seasonally adjusted by FRB staff.
Source. Challenger, Gray and Christmas, Inc.

Small Business Hiring Plans



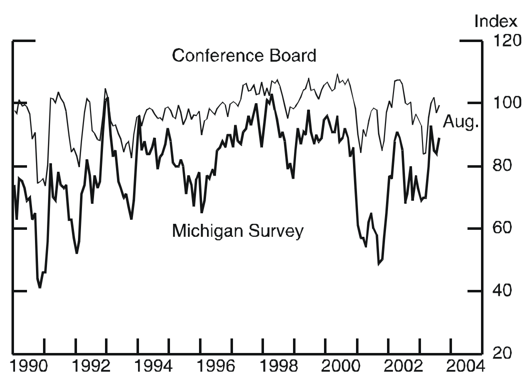
Note. Percent planning an increase in employment minus percent planning a reduction.
Source. National Federation of Independent Businesses.

Current Labor Market Conditions



Note. The proportion of households believing jobs are plentiful, minus the proportion believing jobs are hard to get, plus 100.
Source. Conference Board.

Expected Labor Market Conditions



Note. The proportion of households expecting labor market conditions to improve, minus the proportion expecting conditions to worsen, plus 100.

Similarly, layoff announcements compiled by the outplacement firm Challenger, Gray, and Christmas, Inc., and seasonally adjusted by FRB staff, fell in August to 73,000, the fourth straight monthly decline. Furthermore, the National Federation of Independent Businesses reported that small business hiring plans rose again last month.

Nonetheless, finding a job apparently remains difficult. The number of long-term unemployed as a percent of the labor force—though down a bit in August—remained close to its recent peak. Also, consumer perceptions of current labor market conditions as reported in the Conference Board survey continued to deteriorate last month, although the Conference Board and Michigan Survey measures of expected conditions stayed near the high end of their recent ranges.

According to the BLS, output per hour in the nonfarm business (NFB) sector increased at an annual rate of 6.8 percent in the second quarter, and we expect that figure to be revised up to 7.1 percent.[2] We estimate that labor productivity

Labor Productivity

(Percent change from preceding period at compound annual rate; based on seasonally adjusted rate)

			2002		2003	
	2001[1]	2002[1]	Q3	Q4	Q1	Q2
Total business	3.2	4.2	5.9	1.5	2.7	7.2
Nonfarm business	3.2	4.4	5.9	1.7	2.1	6.8
Previous	3.2	4.4	5.9	1.7	2.1	5.7
Manufacturing	2.9	5.1	6.7	-.4	4.0	3.7
Nonfinancial corporations[2]	4.2	4.4	3.1	3.8	4.3	8.1

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. Nonfinancial corporate sector includes all corporations doing business in the United States except banks, stock and commodity brokers, and finance and insurance companies; the sector accounts for about two-thirds of business employment.

2. The upward revision to productivity reflects our expectation that output in the second quarter will be revised up as a result of the data in the latest construction-put-in-place (CPIP) report. We now estimate that real GDP rose 3.3 percent at an annual rate, and output in the NFB sector rose 4.7 percent. The difference between these two output measures in the second quarter was unusually large and likely due, in part, to the heavy refinancing activity. The BEA treats refinancing as an intermediate input produced by the financial services sector and consumed by the housing sector. Thus, heavy refinancing acted to reduce net housing output in the second quarter. Because the housing sector is largely excluded from the NFB sector (and the financial services sector is included), the treatment of refinancing raised NFB output growth relative to GDP growth.

Selected Components of Industrial Production
(Percent change from preceding comparable period)

Component	Proportion 2002 (percent)	2002[1]	2003[2]		2003[3]		
			Q1	Q2	May	June	July
Total	**100.0**	**1.4**	**.3**	**-3.5**	**.1**	**.0**	**.5**
Previous	100.0	1.4	.3	-3.2	.1	.1	...
Manufacturing	84.7	1.0	-.6	-2.5	.2	.3	.2
Ex. motor veh. and parts	78.3	.1	-.8	-1.6	.3	.1	-.1
Ex. high-tech industries	71.6	-.5	-1.4	-2.6	.3	.1	-.2
Mining	6.3	-1.9	-2.7	.1	-.4	1.2	-.4
Utilities	9.0	7.7	10.3	-13.7	-.9	-3.3	3.9
Selected industries							
High technology	6.6	7.1	8.2	12.7	1.2	.7	.8
Computers	1.3	19.9	24.5	19.8	1.2	1.2	1.6
Communications equipment	2.3	-16.6	2.8	-3.9	-.4	-.7	-2.0
Semiconductors[4]	3.0	19.8	3.9	21.1	2.2	1.3	2.2
Motor vehicles and parts	6.5	10.9	1.6	-11.9	-1.1	1.7	2.9
Market groups excluding energy and selected industries							
Consumer goods	21.9	-1.3	-.2	-.8	.0	.4	-.6
Durables	3.5	.5	-2.2	-3.2	.7	-.3	.7
Nondurables	18.5	-1.6	.2	-.4	-.1	.5	-.9
Business equipment	7.8	-6.0	-1.9	-3.1	.4	.5	.5
Defense and space equipment	1.8	4.9	11.3	5.6	1.6	.6	1.5
Construction supplies	6.6	.8	-6.2	-1.5	.7	.0	.2
Business supplies	7.4	.3	-.7	-3.8	.8	.1	-.3
Materials	25.3	.9	-2.9	-4.8	-.1	-.3	-.2
Durables	13.6	.6	-3.9	-5.8	.3	-.2	.0
Nondurables	11.7	1.3	-1.7	-3.7	-.5	-.3	-.4

1. Fourth-quarter to fourth-quarter change.
2. Annual rate.
3. Monthly rate.
4. Includes related electronic components.
... Not applicable.

Capacity Utilization
(Percent of capacity)

Sector	1972-2002 average	1982 low	1990-91 low	2002	2003			
				Q4	Q1	Q2	June	July
Total industry	**81.3**	**70.8**	**78.6**	**75.3**	**75.2**	**74.3**	**74.2**	**74.5**
Manufacturing	80.2	68.6	77.2	73.5	73.2	72.6	72.7	72.8
High-tech industries	79.3	75.6	74.6	62.2	62.1	62.5	62.5	62.5
Excluding high-tech industries	80.2	68.1	77.3	75.0	74.7	74.1	74.2	74.3
Mining	86.9	78.6	83.3	85.1	84.4	84.3	84.9	84.6
Utilities	86.7	77.2	84.2	86.0	86.9	82.8	80.4	83.2

rose 4-1/4 percent over the four quarters ending in the second quarter of 2003, about 1 percentage point below the increase over the preceding four quarters but well above the average gains in the late 1990s. The latest Productivity and Cost release also included the first look at productivity in the nonfinancial corporate sector, which rose at an annual rate of 8.1 percent in the second quarter and 4.8 percent over the past year.

Industrial Production

Industrial production posted a solid increase in July and appears to have edged up further in August. Utilities made another positive contribution to total IP last month as the boost to electricity demand from the unusually warm weather more than offset the effects of the power outage. However, manufacturing output was restrained by an unexpected drop in motor vehicle assemblies, which fell to 11.7 million units at an annual rate in August. Outside of motor vehicles, output in manufacturing industries for which we have weekly physical product data—principally, iron and steel, crude oil and refinery products, appliances, meat products, and lumber and plywood—was about flat, in aggregate, in August. In putting together our estimate of IP for August, we are discounting much of the reported drop in hours of manufacturing production workers (1 percent using FRB seasonals) because it probably reflects the time lost temporarily due to the power outage during the survey reference week.[3] Using an estimate of hours that should be more representative of activity for the month as a whole, we think that manufacturing output was little changed.[4]

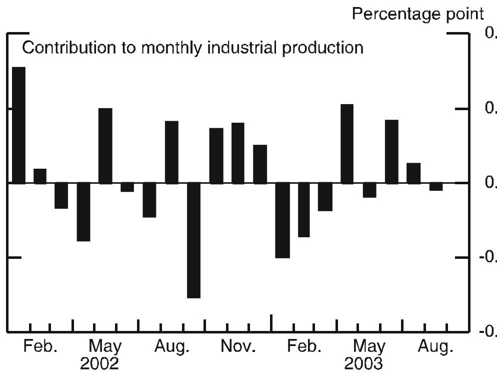
In July, developments in the high-tech industries remained uneven; output in the computer and semiconductor industries once again posted increases, while production of communications equipment continued to decline. However, forward-looking indicators for the high-tech sector now seem relatively upbeat. For example, Intel has significantly boosted its third-quarter revenue projection to a level that is consistent with a sharp acceleration in semiconductor

3. The drop in manufacturing hours using FRB seasonals is considerably larger than the 0.2 percent drop estimated by the BLS. The gap between the two measures of the change in hours is the result of differences in seasonal adjustment related to the timing of the July 4 holiday and reverses a discrepancy that cropped up in July.

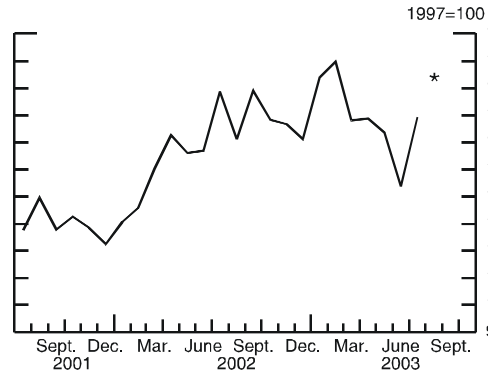
4. We think that the power outage had only a small negative effect on manufacturing production for August as a whole. Reports from the motor vehicle industry suggest that blackout-related losses were partly made up by the end of the month, while low rates of capacity utilization elsewhere likely allowed many firms to make up lost production within the month. Also, although some manufacturers with continuous processing such as steel and refineries probably experienced disruptions, the losses were apparently small relative to their normal month-to-month variations in output.

Indicators of Manufacturing Activity

Weekly Physical Product Data Except
Electricity Generation and Motor Vehicles

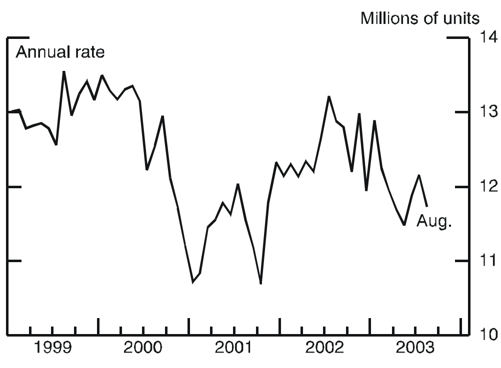


Electric Utilities Production

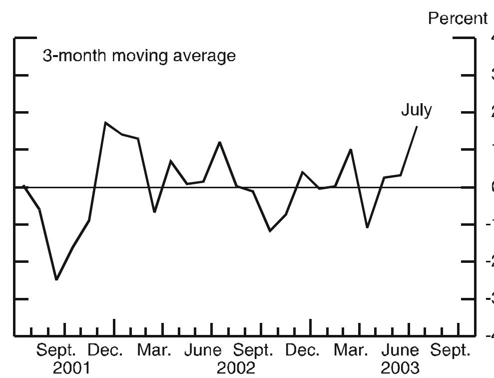


* August value; based on weekly data.

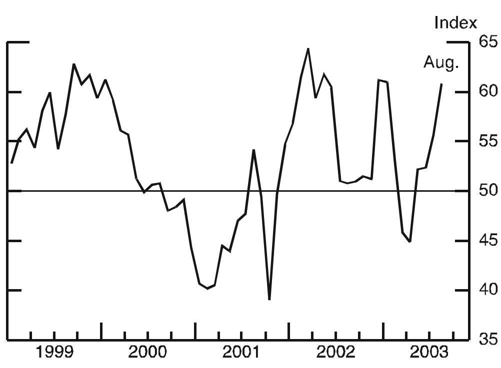
Motor Vehicle Assemblies



Change in Real Adjusted
Durable Goods Orders

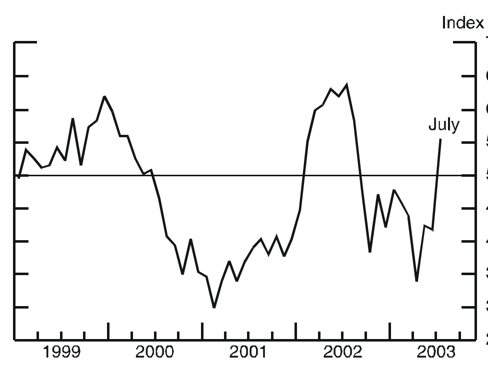


ISM New Orders Diffusion Index



Note. The diffusion index equals the percentage of respondents reporting greater levels of new orders, plus one-half the percentage of respondents reporting that new orders were unchanged.

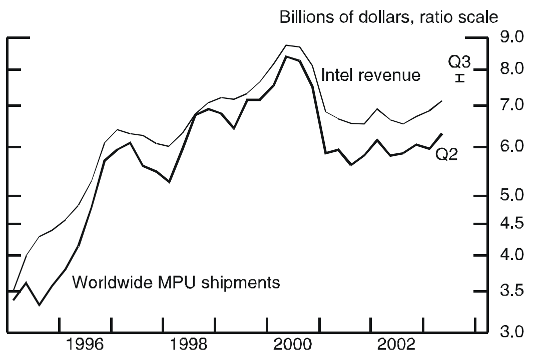
Industrial Production Diffusion Index



Note. The diffusion index equals the percentage of series that increased over three months plus one-half the percentage that were unchanged.

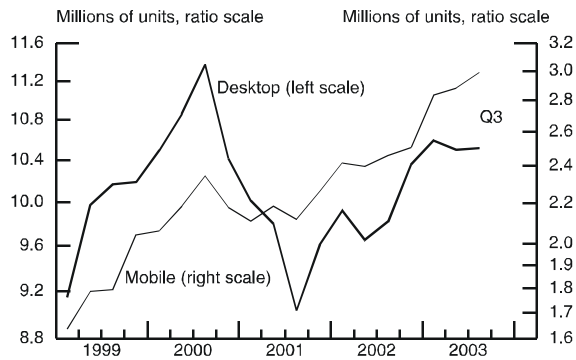
Indicators of High-Tech Manufacturing Activity

Microprocessor Unit (MPU) Shipments and Intel Revenue



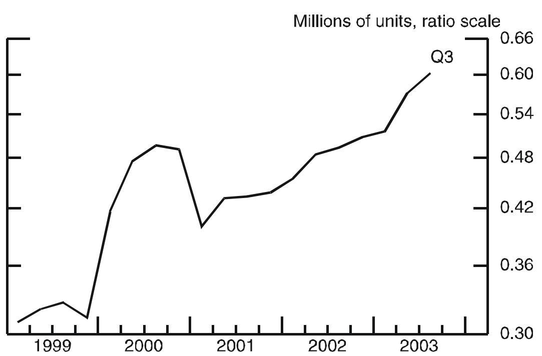
Note. Q3 is the range of Intel's guidance as of September 4, 2003.
Source. Intel and Semiconductor Industry Association.

U.S. Personal Computer Shipments



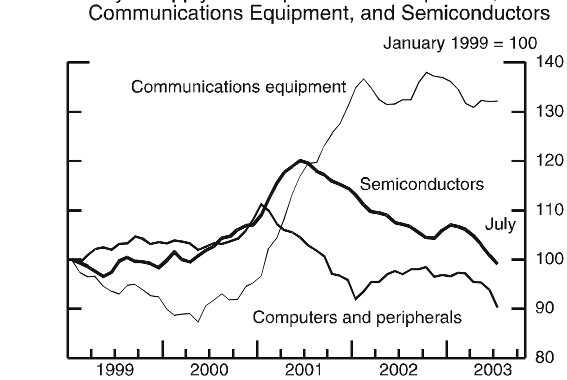
Note. FRB seasonals. Values for Q3 are Gartner forecasts.
Source. Gartner.

U.S. Server Shipments



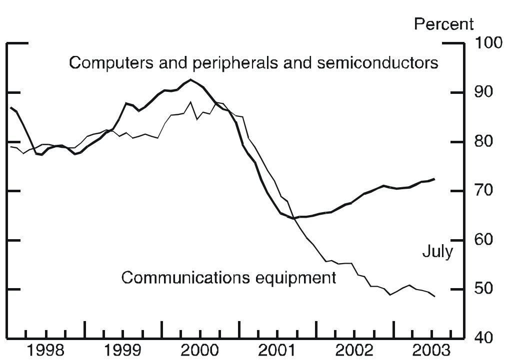
Note. FRB seasonals. Value for Q3 is a Gartner forecast.
Source. Gartner.

Days' Supply of Computers and Peripherals, Communications Equipment, and Semiconductors

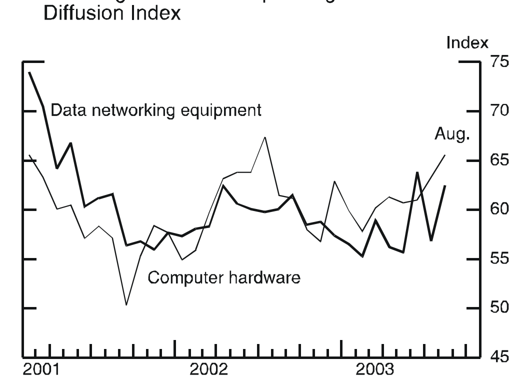


Source. Board staff's flow-of-goods system.

High-Tech Capacity Utilization Rates



CIO Magazine Future Spending Diffusion Index



Note. The diffusion index equals the percentage of respondents planning to increase future spending plus one-half the percentage of respondents planning to leave future spending unchanged. The average number of respondents per month from February 2001 to August 2003 was 273.
Source. CIO Magazine.

production.[5] Much of the pickup appears to be in the high-value microprocessors and memory chips used in personal computers, particularly mobile computers such as laptops. Unit shipments of servers, which are far fewer in number but of much greater value, increased 11 percent (not at an annual rate) in the second quarter, and Gartner, a research and advisory firm, expects an additional gain in the third quarter. In addition, the diffusion index compiled by *CIO Magazine* for future spending on computer hardware rose further in August; the diffusion index for data-networking equipment (such as routers, switches, and hubs) has been choppy recently, but it too has trended up over the past several months.

According to the Board staff's flow-of-goods system, days' supplies of computers and semiconductors are at relatively low levels; therefore, any pickup in demand for computing products should quickly translate into increased production. In addition, although the utilization rates in these industries have trended up since 2001, enough slack remains to easily accommodate a significant expansion of activity.[6] In contrast, because the days' supply for communications equipment remains elevated, stronger demand may not translate as readily into a rise in production.

The performance of the various IP market groups excluding high-tech products, energy, and motor vehicles and parts was mixed in July. The output of business equipment increased for a third consecutive month, and the output of defense and space equipment continued its recent upward trend. In contrast, the production of business and construction supplies changed little, and materials output continued a downward slide that has lasted for nearly a year. The production of consumer goods also dropped in July, but smoothing through the monthly volatility, this series has essentially moved sideways since late last year.

Indicators of near-term production point to a pickup in the industrial sector in the coming months. The staff's series on real adjusted durable goods orders has risen steadily in recent months, and the new orders diffusion index from the

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5. The midpoint of Intel's revenue guidance of September 4 is 8.8 percent (not an annual rate) above the company's actual second-quarter revenues and is a marked acceleration relative to the increase of 3 percent per quarter averaged during the preceding three quarters. In its public statements, the company has been hesitant to draw any conclusions about the imminence of a recovery in the high-tech sector.

6. The production of leading-edge semiconductor chips is an exception. According to the Semiconductor Industry Association, at least some of the plants that produce these chips are currently operating at high rates of utilization.

Institute for Supply Management has been above 50 since May. The new orders diffusion indexes provided in the various regional surveys generally paint a picture similar to that of the ISM and are consistent with faster growth in IP over the next couple of months.

New Orders for Durable Goods

(Percent change from preceding period except as noted; seasonally adjusted)

Component	Proportion, 2003: H1 (percent)	2003				
		Q1	Q2	May	June	July
Total orders	**100.0**	**0.7**	**-0.2**	**0.0**	**2.5**	**1.0**
Adjusted orders[1]	75.0	0.6	-0.8	2.0	1.5	1.1
Computers	4.0	-4.7	13.4	-2.0	3.4	0.5
Communication equipment	4.0	25.6	-8.9	-5.5	0.4	13.4
Other capital goods	24.0	2.0	0.3	2.7	1.9	-2.1
Other[2]	43.0	-1.4	-2.0	2.7	1.2	1.9
MEMO						
Real adjusted orders	. . .	1.0	-0.5	2.0	1.7	1.2
Excluding high tech	. . .	0.2	-1.2	1.5	1.9	0.5

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

Motor Vehicles

Sales of light motor vehicles jumped in August to an annual rate of 18.9 million units, more than 1-1/2 million units above the July pace. One factor contributing to the rise in sales was a further sweetening of incentives on 2003 model-year vehicles. Indeed, the average incentive per vehicle moved up another $170, to $2570. In addition, the tax cut boosted consumers' after-tax incomes. According to the Michigan Survey, car-buying attitudes slipped in August but remained relatively high. In the near term, both the continuation of heavy incentives on 2003 model-year vehicles and the introduction of several widely anticipated new models for 2004 should help bolster consumer demand.

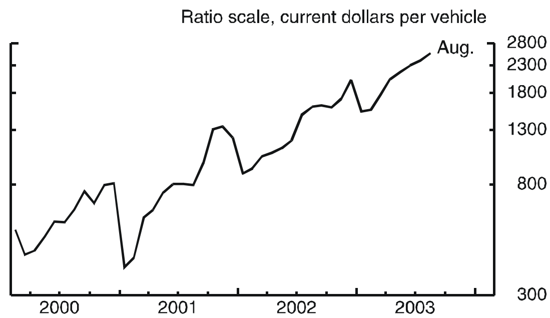
Business demand for motor vehicles appears to be firming, mainly because of stronger demand for trucks. Sales of both heavy and medium trucks have improved in recent months, and net orders have trended up as well. According to industry contacts, purchases of trucks may have been boosted by the partial expensing provisions of the latest tax bill. Fleet sales of light vehicles in August rose above July's low level, but so far this year they have tracked a bit below last year's pace.

Sales of Automobiles and Light Trucks
(Millions of units at an annual rate, FRB seasonals)

		2002	2003		2003		
	2002	Q4	Q1	Q2	June	July	Aug.
Total	16.7	16.5	15.8	16.2	16.3	17.2	18.9
Autos	8.1	7.9	7.7	7.4	7.6	7.8	8.2
Light trucks	8.6	8.6	8.1	8.8	8.8	9.4	10.6
North American[1]	13.5	13.3	12.5	12.9	13.0	13.9	15.4
Autos	5.9	5.7	5.5	5.4	5.5	5.8	6.1
Light trucks	7.6	7.6	6.9	7.5	7.5	8.1	9.3
Foreign-produced	3.3	3.2	3.4	3.3	3.3	3.3	3.5
Autos	2.2	2.2	2.2	2.0	2.0	2.0	2.2
Light trucks	1.1	1.1	1.2	1.3	1.3	1.3	1.4
Memo:							
Medium and heavy trucks	.40	.41	.37	.39	.39	.45	n.a.

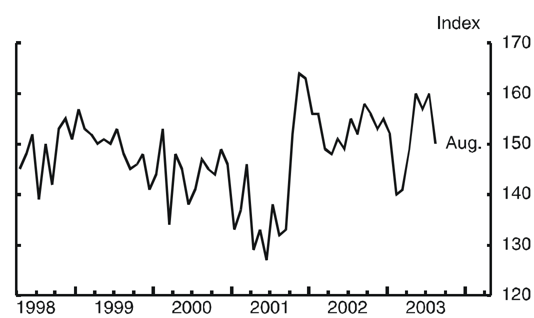
Note. Components may not sum to totals because of rounding. Data on sales of trucks and imported autos for the most recent month are preliminary and subject to revision.
1. Excludes some vehicles produced in Canada that are classified as imports by the industry.
n.a. Not available.

Average Value of Incentives on Light Vehicles

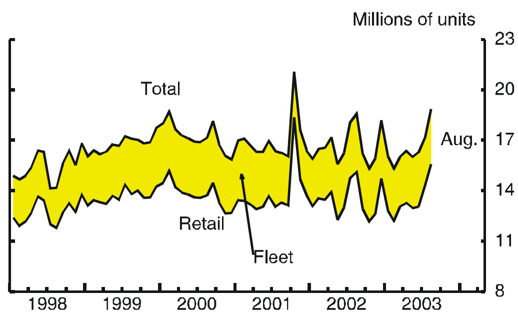


Note. Weighted average of customer cash rebate and interest rate reduction. Data are seasonally adjusted.
Source. J.D. Power and Associates.

Michigan Survey Index of Car-Buying Attitudes

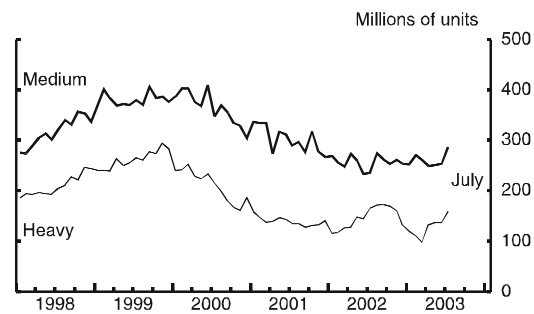


Fleet and Retail Sales of Light Vehicles



Note. Annual rate. FRB seasonals.

Sales of Medium and Heavy Trucks



Note. Annual rate. FRB seasonals.

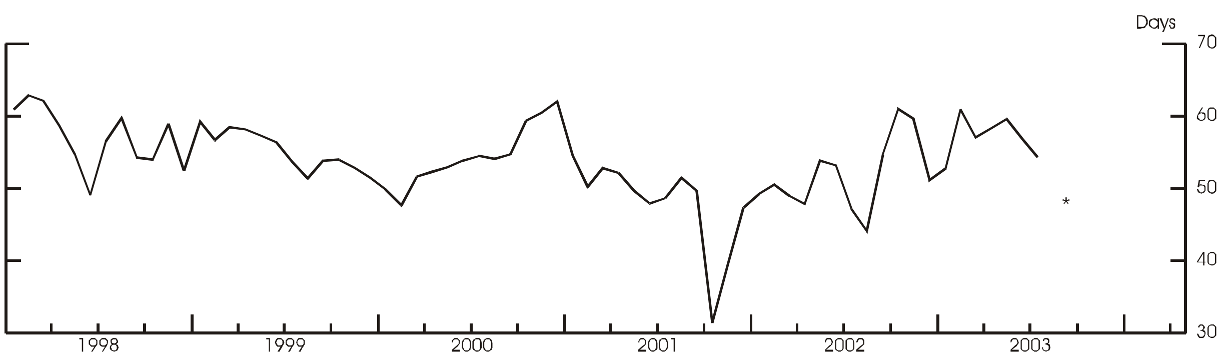
Production of Domestic Autos and Trucks

(Millions of units at an annual rate except as noted; FRB seasonal basis)

Item	2002	2003			2003			
	Q4	Q1	Q2	Q3[1]	May	June	July	Aug.
U.S. production	12.4	12.4	11.7	12.3	11.5	11.9	12.2	11.7
Autos	4.9	4.7	4.4	4.6	4.4	4.5	4.5	4.3
Trucks	7.5	7.7	7.3	7.7	7.1	7.4	7.7	7.4
Days' supply[2]	63	74	70	n.a.	71	70	65	55[e]
Inventories[3]	2.73	3.01	2.96	n.a.	2.97	2.96	2.95	2.76[e]

NOTE. Components may not sum to totals because of rounding.
1. Production rates reflect Ward's Communications' latest estimates for Q3.
2. Quarterly values calculated with end-of-period stocks and average reported sales; excludes medium and heavy trucks (classes 3-8).
3. End-of-period stocks; excludes medium and heavy trucks.
n.a. Not available
e Staff estimate

Days' Supply of Autos



* August value; based on staff estimates.

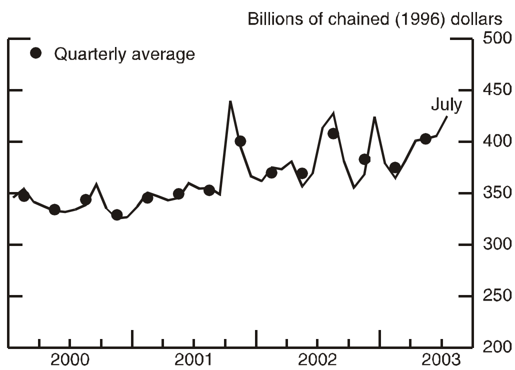
Days' Supply of Light Trucks

* August value; based on staff estimates.

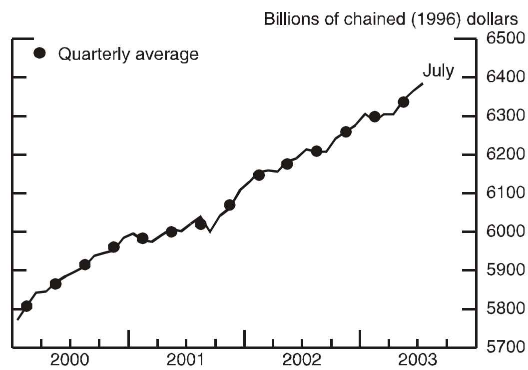
Real Personal Consumption Expenditures
(Percent change from the preceding period)

Expenditure	2002 Q4	2003 Q1	2003 Q2	2003 May	2003 June	2003 July
	Annual rate			Monthly rate		
Total real PCE	1.7	2.0	3.8	.6	.4	.6
Durable goods	-8.2	-2.0	24.1	1.1	1.3	2.4
Motor vehicles	-22.2	-8.0	33.5	.5	.7	4.8
Excluding motor vehicles	4.4	2.7	17.5	1.7	1.8	.5
Nondurable goods	5.1	6.1	1.1	.8	.5	.6
Energy	3.6	.7	-7.8	1.7	-.6	-.1
Other	5.2	6.7	2.1	.7	.6	.7
Services	2.2	.9	1.5	.3	.1	.2
Energy	22.8	-5.8	-12.8	.3	-2.1	3.8
Transportation	.5	.1	-3.4	.2	-.2	.0
Other	1.6	1.2	2.5	.4	.2	.1
Memo:						
Real disposable personal income	1.4	2.1	2.8	.5	.2	1.3

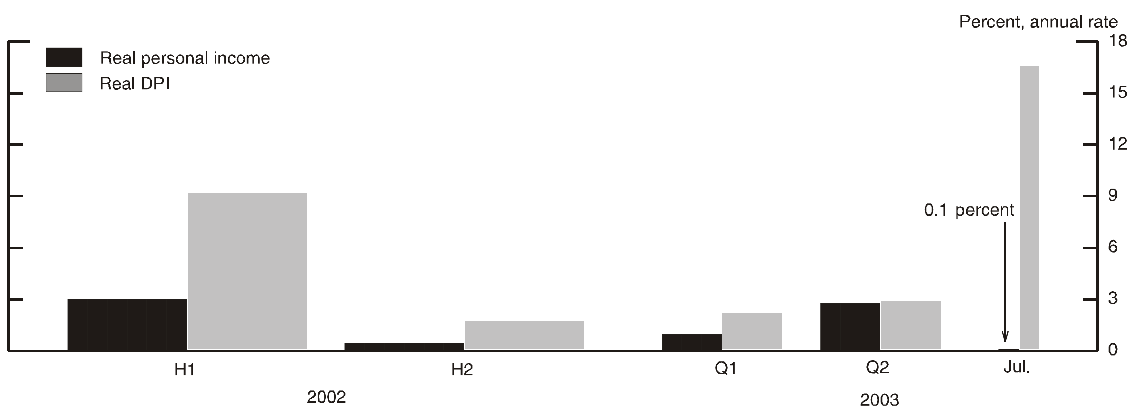
PCE Motor Vehicles



PCE Ex. Motor Vehicles



Change in Real Personal Income and Real DPI



Total motor vehicle production rose in July to 12.2 million units at an annual rate but fell to 11.7 million units in August. August's production rate was damped by a combination of plant closures for inventory control, power outages in the Northeast and Midwest, and start-up difficulties with new model-year vehicles. Automakers plan to make up much of this production loss and have raised September's assembly plans to 12.9 million units. As a result of the strong sales pace over the summer, inventories of automobiles and trucks have fallen significantly from their high levels in the first half of the year. With sales likely to fall back appreciably in September from the elevated August rate, automakers have scheduled assemblies in the fourth quarter at 11.7 million units.[7]

Consumer Spending

Consumer spending advanced briskly through July, and the indicators in hand point to another solid increase in August. Disposable income has been supported by the recent tax cuts, including both the reduction in withholding and the advance refunds of the child tax credit. In addition, consumer confidence remains well above the levels recorded earlier this year, and the stock market has continued to rise. However, the backup in interest rates since late June should exert some restraint on consumption going forward.

Real personal consumption expenditures climbed 0.6 percent in July after an upward-revised 0.4 percent gain in June. All major categories of outlays recorded increases in July. In August, weekly data on chain store sales are consistent with another appreciable increase in retail sales, and—as noted earlier—sales of light motor vehicles soared. Moreover, unusually hot weather likely left spending on energy services up for the month despite the blackout.

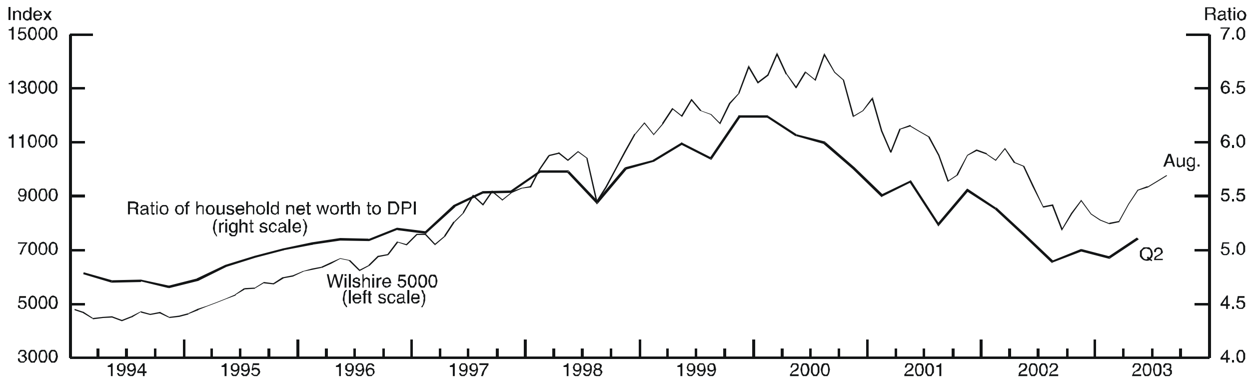
Real disposable income jumped 1.3 percent (monthly rate) in July because of a sharp reduction in tax payments; pre-tax income was essentially unchanged in real terms. With the second and third rounds of advance refunds reaching households in August, another sizable gain in disposable income seems likely. Because households spent only part of the additional July income, the personal saving rate moved up 0.7 percentage point, to 3.8 percent.

The Michigan Survey Research Center's index of consumer sentiment edged down in August, while the Conference Board's index rose a bit. Both measures of confidence stand well above their March lows but have moved little, on balance, in recent months. Looking back over the past year, however, the indexes have diverged noticeably, with the Michigan index rising a touch, on net, and the Conference Board index falling. This divergence is due primarily to

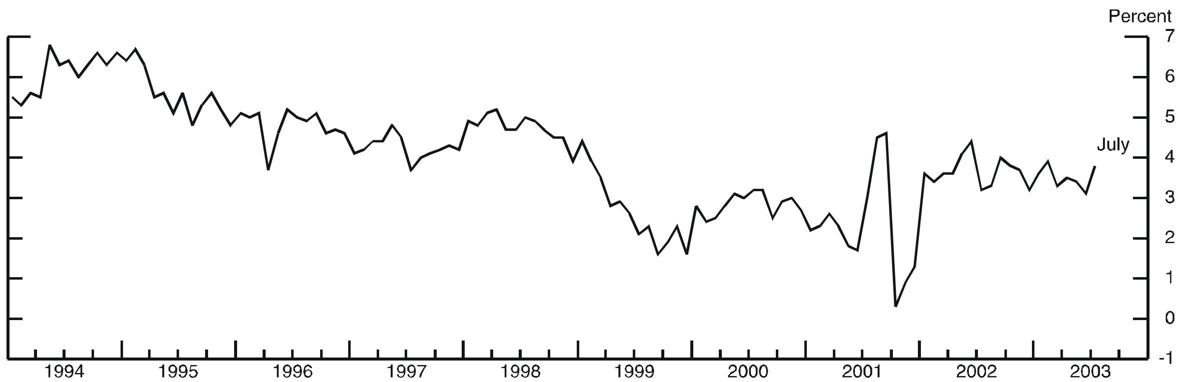
7. The UAW is reported to be close to concluding a simultaneous deal with all Big Three manufacturers.

Household Indicators

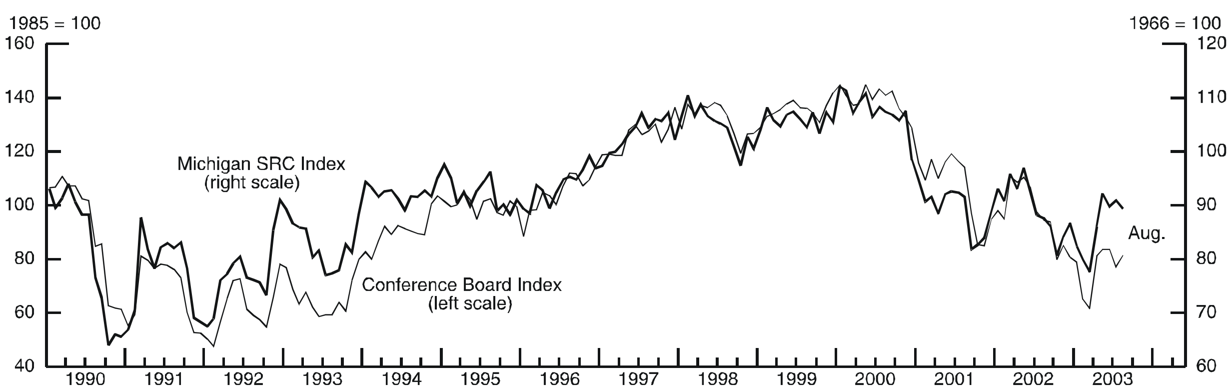
Household Net Worth and Wilshire 5000



Personal Saving Rate



Consumer Confidence



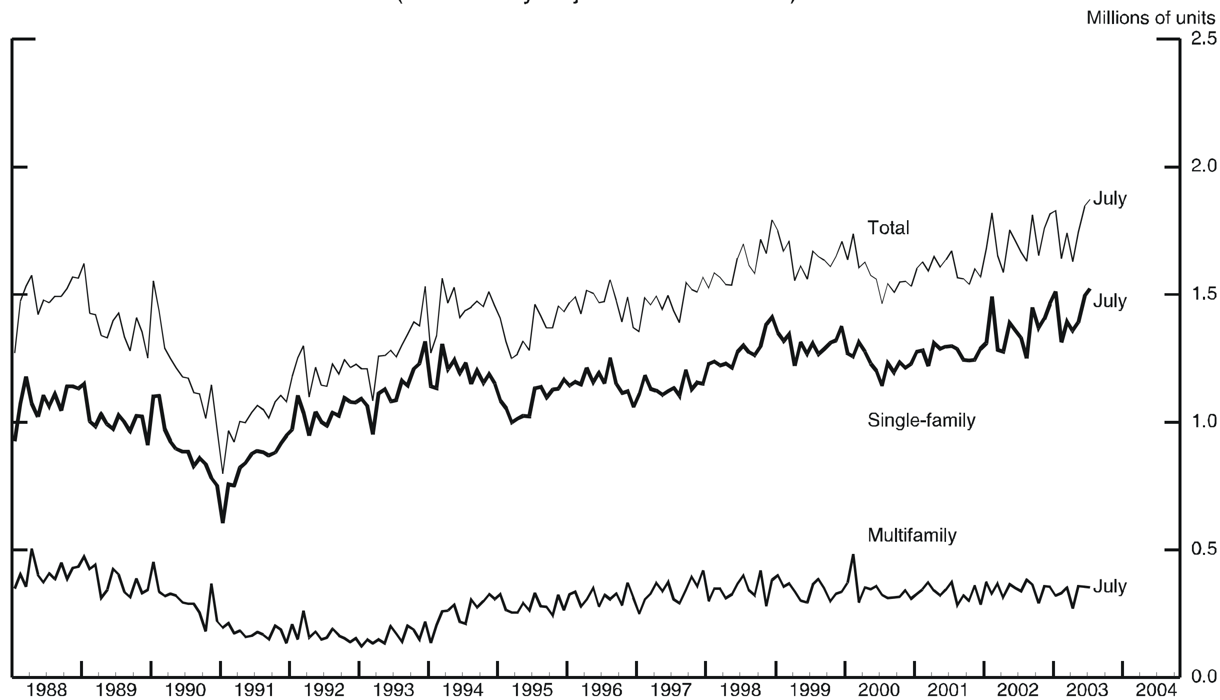
Private Housing Activity
(Millions of units; seasonally adjusted annual rate)

		2002	2003				
	2002	Q4	Q1	Q2[r]	May [r]	June[r]	July[p]
All units							
Starts	1.70	1.74	1.74	1.74	1.75	1.85	1.87
Permits	1.75	1.83	1.75	1.78	1.80	1.82	1.78
Single-family units							
Starts	1.36	1.41	1.41	1.41	1.39	1.49	1.52
Permits	1.33	1.40	1.35	1.37	1.35	1.43	1.42
Adjusted permits[1]	1.38	1.44	1.39	1.40	1.38	1.47	1.47
New home sales	0.97	1.03	0.98	1.10	1.11	1.20	1.17
Existing home sales	5.57	5.75	5.87	5.83	5.85	5.83	6.12
Multifamily units							
Starts	0.35	0.33	0.33	0.33	0.36	0.35	0.35
Permits	0.42	0.43	0.41	0.41	0.45	0.40	0.36
Mobile homes							
Shipments	0.17	0.15	0.14	0.13	0.13	0.13	n.a.

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

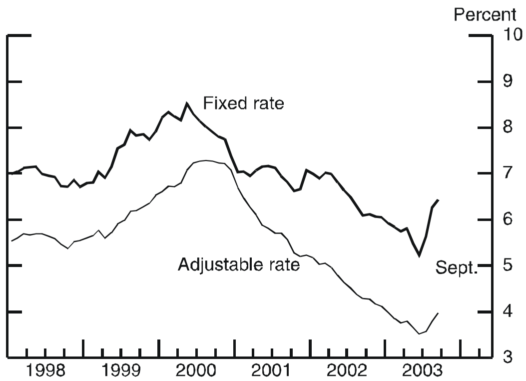
1. Adjusted permits equals permit issuance plus total starts outside of permit-issuing areas.

Private Housing Starts
(Seasonally adjusted annual rate)



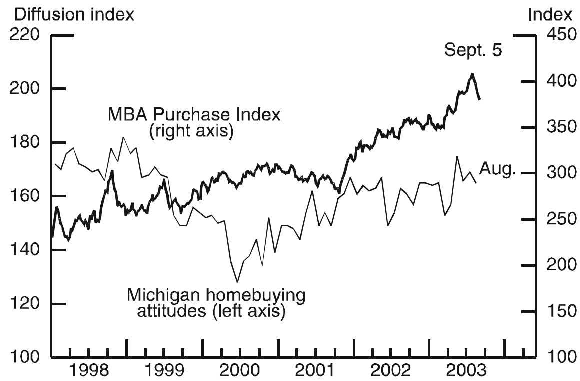
Indicators of Single-Family Housing

Mortgage Rates



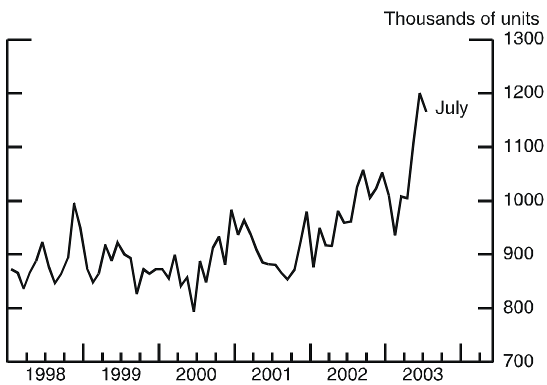
Note. Sept. figure is based on data through Sept. 5.
Source. Freddie Mac.

Homebuying Indicators



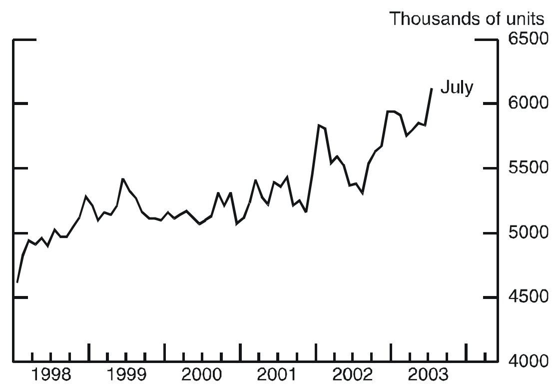
Note. MBA index is a 4-week moving average. Michigan Survey data are not seasonally adjusted.
Source. Mortgage Bankers Association and Michigan Survey.

New Home Sales



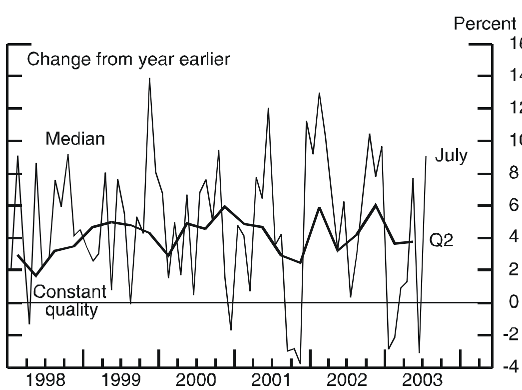
Source. Census Bureau.

Existing Home Sales



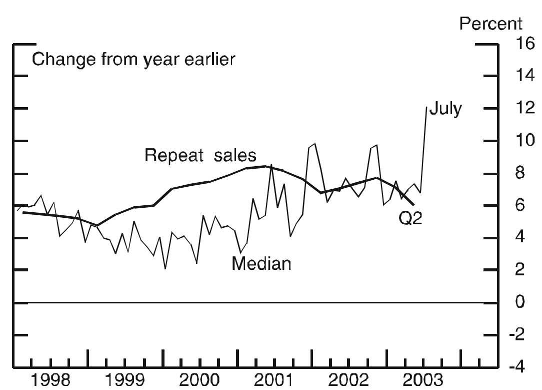
Source. National Association of Realtors.

Prices of New Homes



Source. Census Bureau.

Prices of Existing Homes



Source. National Association of Realtors and Freddie Mac.

the deterioration in the current-conditions component of the Conference Board measure, which incorporates questions about current business and labor-market conditions that are not included in the overall Michigan index.

Housing Markets

Housing construction and sales remained very strong in July. However, mortgage rates began to climb in late June. Shifts in housing activity typically lag movements in mortgage rates by a few months, and the effects of the run-up in rates should begin to show through to starts and sales soon.

In July, starts of single-family houses rose to an annual rate of 1.52 million units, the fastest pace in nearly twenty-five years, and permit issuance—adjusted for activity in areas where permits are not required—remained very strong at 1.47 million units. However, the ratio of starts to permits was atypically high, and, together with the escalating mortgage rates, suggests that single-family construction is likely to drop back some in coming months. Meanwhile, home sales were around record levels in July as new home sales fell only a little after having surged to an annual rate of 1.20 million units in June and existing home sales jumped to an annual rate of 6.1 million units.

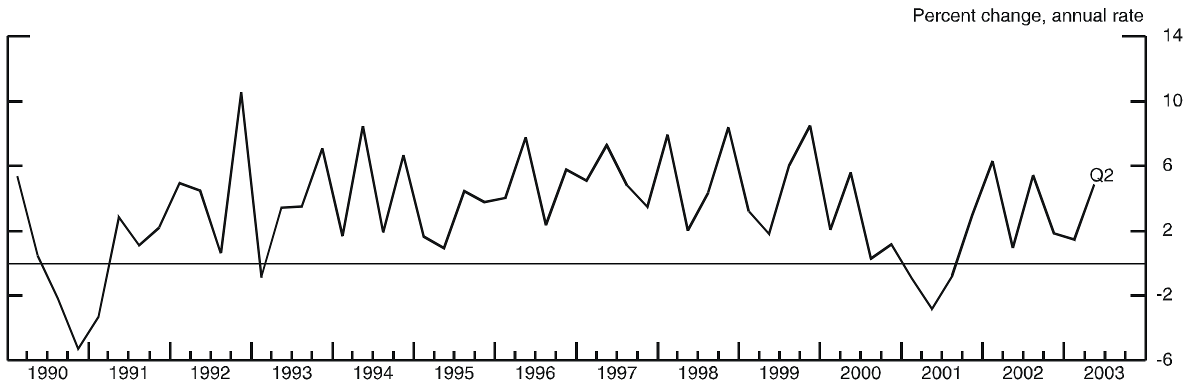
In the multifamily sector, starts remained at an annual rate of 350,000 units in July, a level in line with the average over the past year and a half. However, permit issuance for multifamily units fell nearly 10 percent, and the vacancy rate in the second quarter was a record high.

Other indicators of housing demand have generally remained robust, although some restraint from higher mortgage rates seems to be emerging. The four-week moving average of the Mortgage Bankers Association index of purchase applications declined 7 percent through early September from its high in late July. However, attitudes toward homebuying in the Michigan Survey were at roughly the same level in August as they had been in June, with nearly three-quarters of those who said it was a good time to buy mentioning low mortgage rates as a reason. Perhaps one sign of changing attitudes was an increase in the proportion of respondents citing a need to borrow in anticipation of rising mortgage rates.

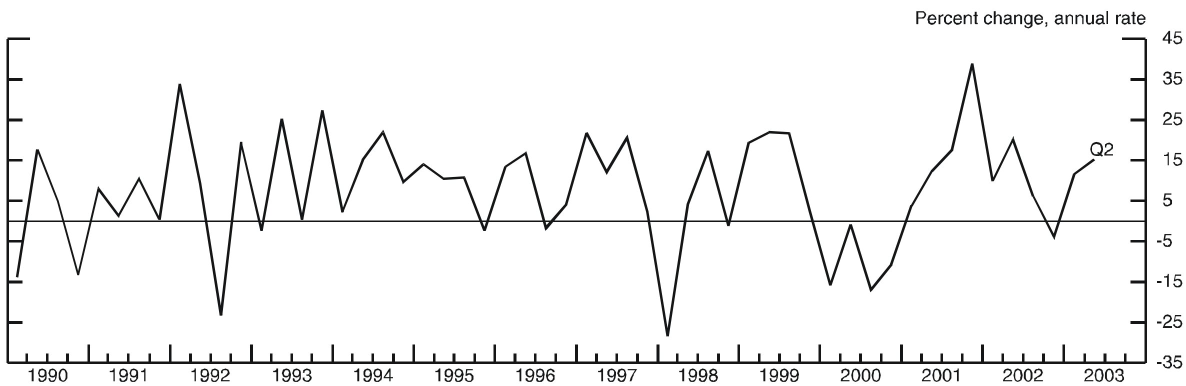
Available measures of house prices rose noticeably in July, with the median price of new homes up 9 percent from a year ago and the median price of existing homes up 12 percent. However, these series are erratic. Measures that are less affected by compositional changes, such as the quality-adjusted price of new homes and the repeat-sales price of existing homes, showed increases of 4 to 6 percent over the year ending in the second quarter; these increases, although substantial, were toward the lower end of their recent ranges.

Equipment and Software Investment Fundamentals

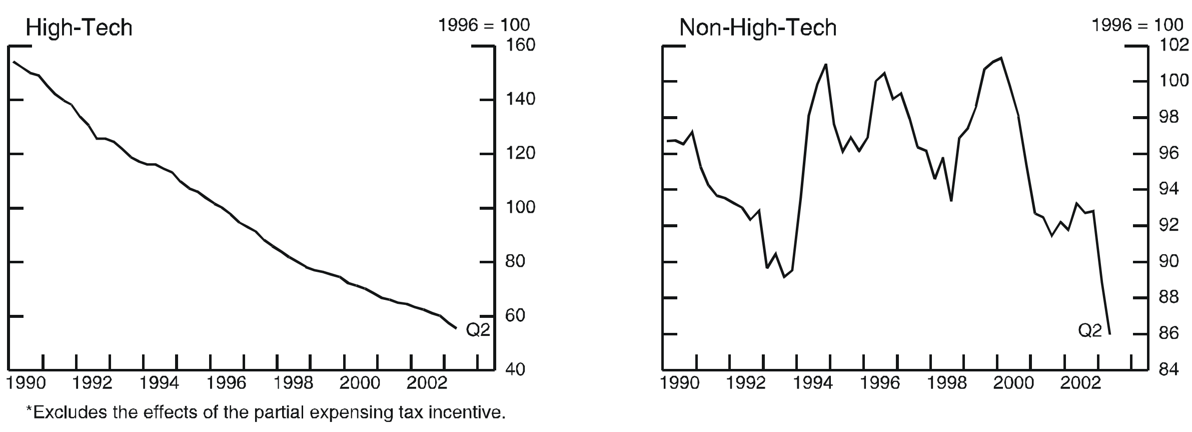
Real Business Output



Real Corporate Cash Flow



User Cost of Capital*



*Excludes the effects of the partial expensing tax incentive.

Equipment and Software

Real business outlays for equipment and software are currently estimated by the BEA to have increased at an annual rate of 8 percent in the second quarter, and the orders and shipments data for July suggest that this momentum carried over into the third quarter. The pickup in equipment and software spending appears to be broad-based and is consistent with the improving prospects for business output and the step-up in cash flow this year. Reports from the Beige Book and our business contacts, as well as revenue guidance by makers of high-tech equipment and software, have improved over the past month but are still shaded with caution.

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

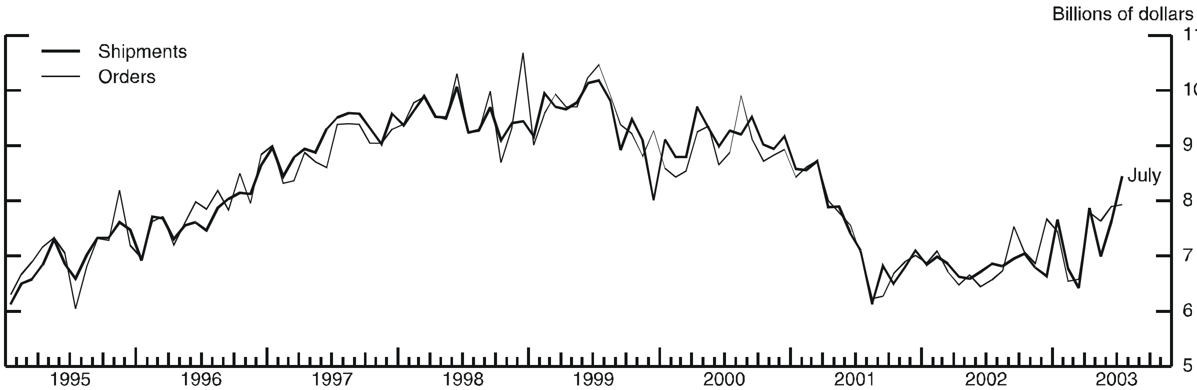
	2003		2003		
	Q1	Q2	May	June	July
	- Annual rate -		- - Monthly rate - -		
Shipments of nondefense capital goods	-5.1	5.7	-0.4	3.8	2.2
Excluding aircraft	-1.9	5.6	-0.9	2.8	2.5
Computers and peripherals	7.6	35.8	-11.2	9.1	10.6
Communications equipment	-3.5	-6.5	-0.9	16.4	-1.9
All other categories	-3.2	2.7	1.2	-0.1	1.7
Shipments of complete aircraft	-4.1	-41.5	5.3	49.0	0.9
Medium & heavy truck sales	-30.7	16.4	2.1	-0.2	13.4
Orders for nondefense capital goods	1.1	12.9	-0.9	3.6	0.8
Excluding aircraft	14.6	3.2	1.0	1.9	-0.0
Computers and peripherals	-17.5	65.1	-2.0	3.4	0.5
Communications equipment	148.9	-31.2	-5.5	0.4	13.4
All other categories	8.2	1.0	2.7	1.9	-2.1

In the high-tech sector, nominal shipments of computing equipment surged 10-1/2 percent (monthly rate) in July after a similar increase in June, and shipments of communications equipment declined only a bit after an extraordinary jump in June. Outside the high-tech sector, shipments moved up nearly 2 percent in July, with a rise in the machinery subcategory accounting for most of the increase. Looking forward, new orders for computers are trending up, in line with the trajectory of shipments, and bookings for communications equipment appear to have bottomed out. While new orders apart from high-tech slipped in July, they have increased, on balance, since the beginning of this year—a development that suggests ongoing gains in spending in this broad category.

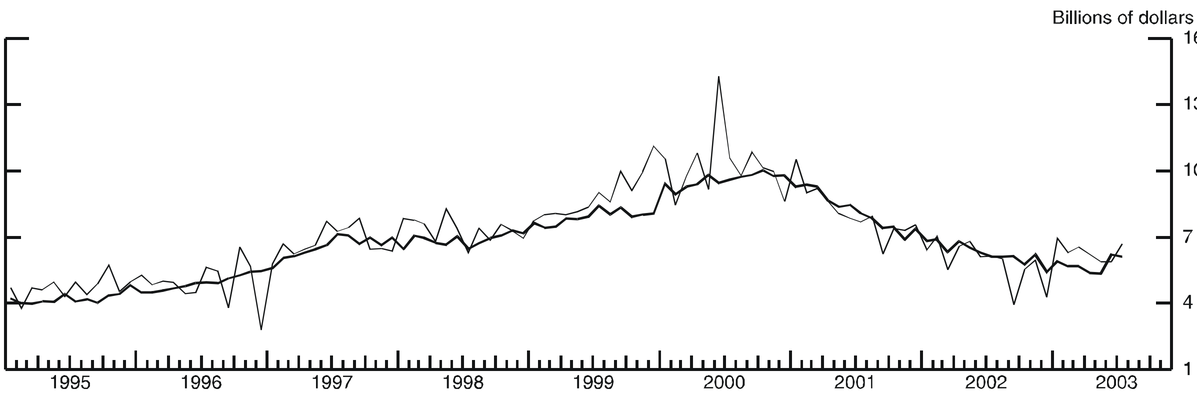
In the transportation sector, a sizable increase in spending on medium and heavy trucks appears to be under way this quarter, although fleet sales of light vehicles remain lackluster. Business spending on aircraft dropped substantially in the second quarter, but domestic shipments of aircraft leveled off in July.

Recent Data on Orders and Shipments of Nondefense Capital Goods

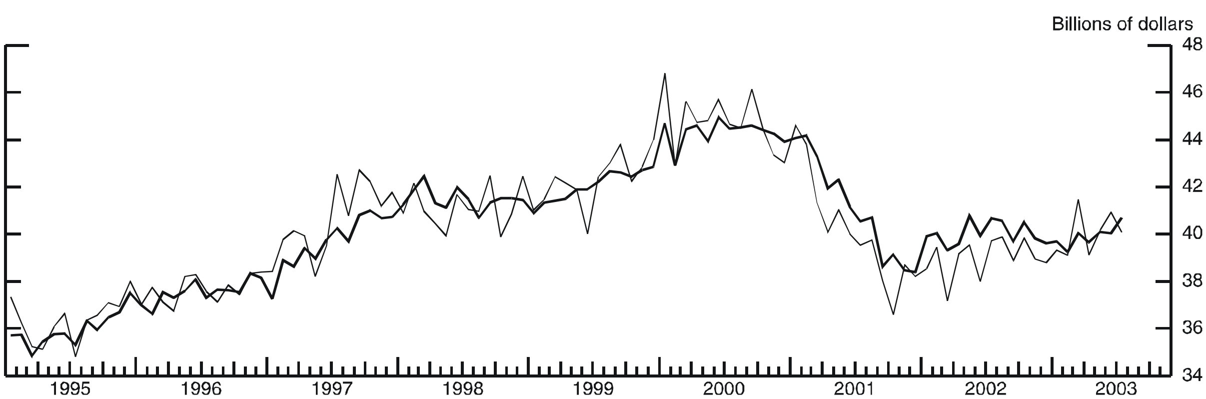
Computers and Peripherals



Communications Equipment

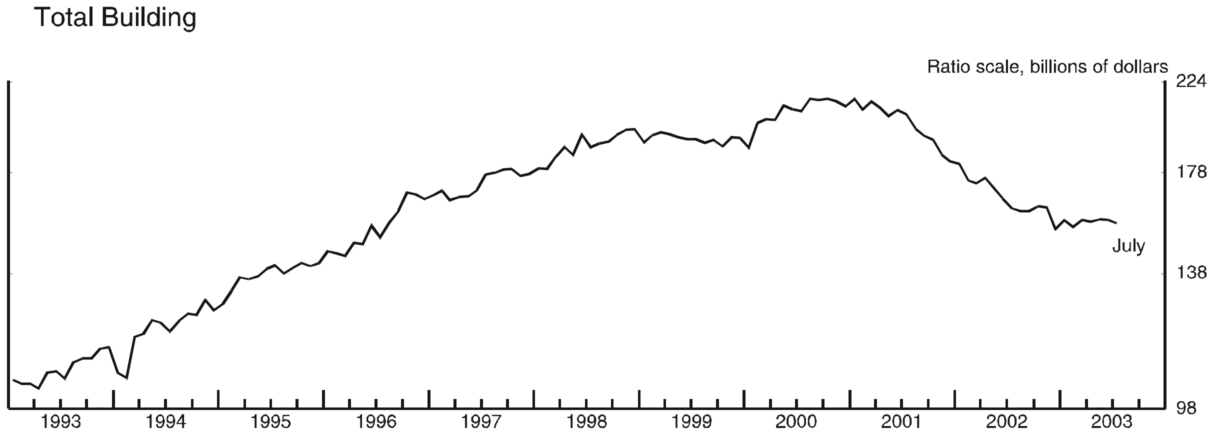


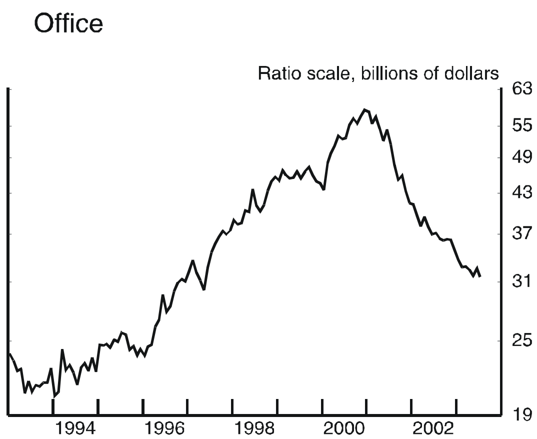
Other Equipment (Total Ex. Aircraft, Computers, and Communications)

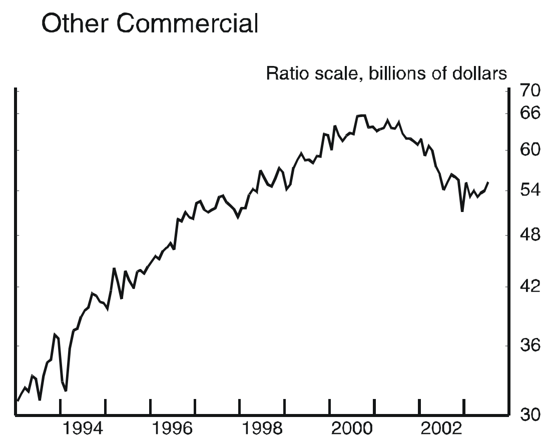


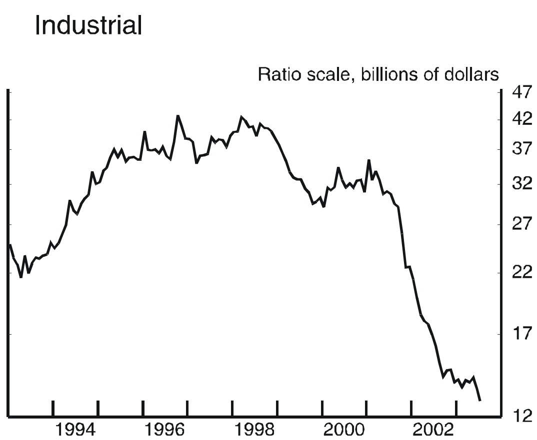
Nonresidential Construction

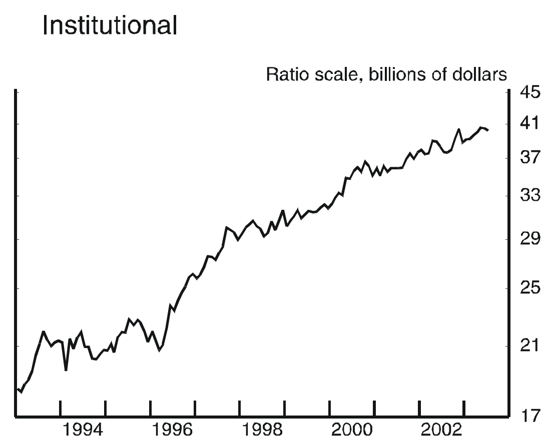
(Staff translation of CPIP data into traditional BEA categories; seasonally adjusted, annual rate)







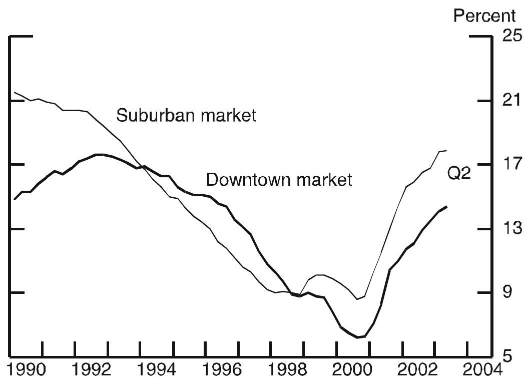




Indicators of Nonresidential Construction

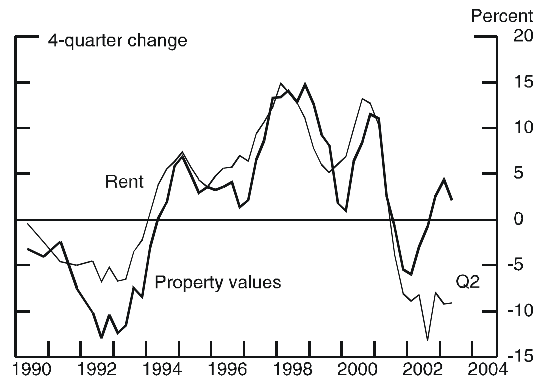
Office Buildings

Vacancy Rate



Source. CB Richard Ellis.

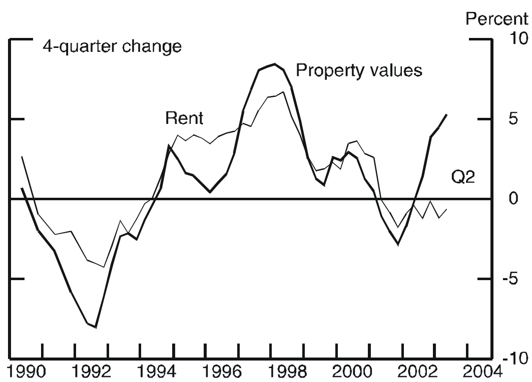
Property Values and Rent



Source. National Real Estate Index.

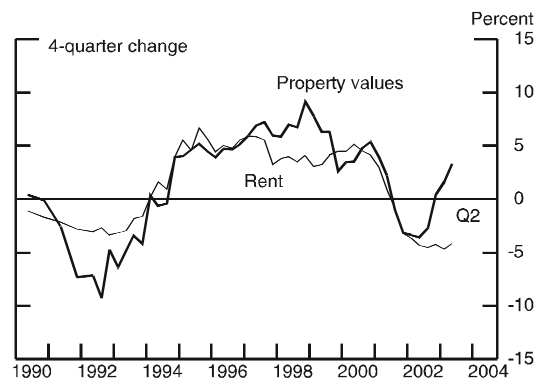
Other Commercial Buildings

Retail Property Values and Rent



Source. National Real Estate Index.

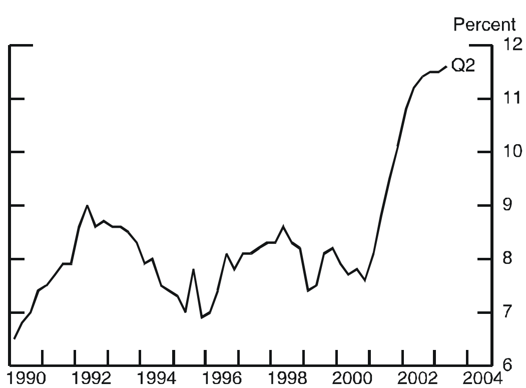
Warehouse Values and Rent



Source. National Real Estate Index.

Industrial

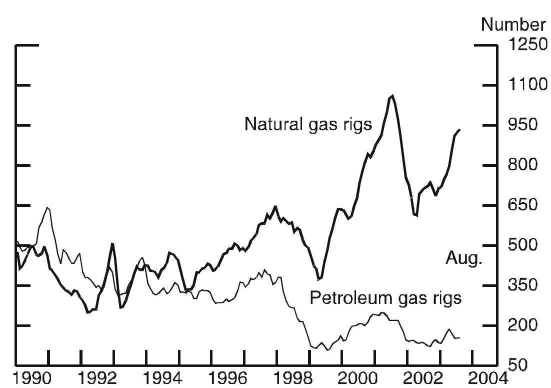
Vacancy Rate



Source. CB Richard Ellis.

Drilling Activity

Rigs in Operation



Note. August values are averages through August 29.
Source. DOE/Baker Hughes.

Nonresidential Construction

Nonresidential construction expenditures have remained very soft after having plummeted in 2001 and 2002. Although construction rose moderately in the second quarter, the increase was from an exceptionally low level and was reversed in July.[8] In the office sector, spending has declined in recent months, as the already-high vacancy rates continued to rise and rents continued to fall. Expenditures for industrial buildings, where the vacancy rate is also quite elevated, fell again in July, and spending for lodging facilities also dropped. Outlays for institutional construction, which comprise educational, religious and hospital structures, declined in July as well.

On a brighter note, nominal spending on construction of non-office commercial structures—which includes retail space and warehouses—has risen appreciably in recent months. Although rents on retail and warehouse properties remained below their year-earlier values in the second quarter, the four-quarter changes in property values moved further into positive territory. Expenditures for drilling and mining are also likely rising in the third quarter, but the rise is likely to be smaller than in the second quarter because of a more moderate increase in oil and gas drilling activity.

Business Inventories

Real nonfarm NIPA inventories excluding motor vehicles fell at an annual rate of $29 billion in the second quarter, and partial data for July suggest that the runoff has continued into the current quarter. The book value of manufacturing inventories declined at an annual rate of $28 billion in July, as stocks of nondurable goods edged down and stocks of durable goods, led by a large liquidation of aircraft, continued their long-running downward trend. Meanwhile, the book value of wholesale inventories excluding motor vehicles increased at an annual rate of $8 billion, owing to a large accumulation by wholesalers of drugs.

With sizable gains in manufacturing shipments, book-value inventory-shipments ratios moved down considerably in July; book-value inventory-sales ratios at wholesalers remained unchanged at a low level by historical standards.[9] In general, inventory stocks appear to be fairly lean across most categories of manufacturing and trade.

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8. Incorporating the revisions to spending in May and June from the latest CPIP release, we estimate that real outlays for nonresidential construction increased at an annual rate of 5-1/2 percent in the second quarter, compared with a 7 percent rise in the BEA's preliminary GDP estimate.

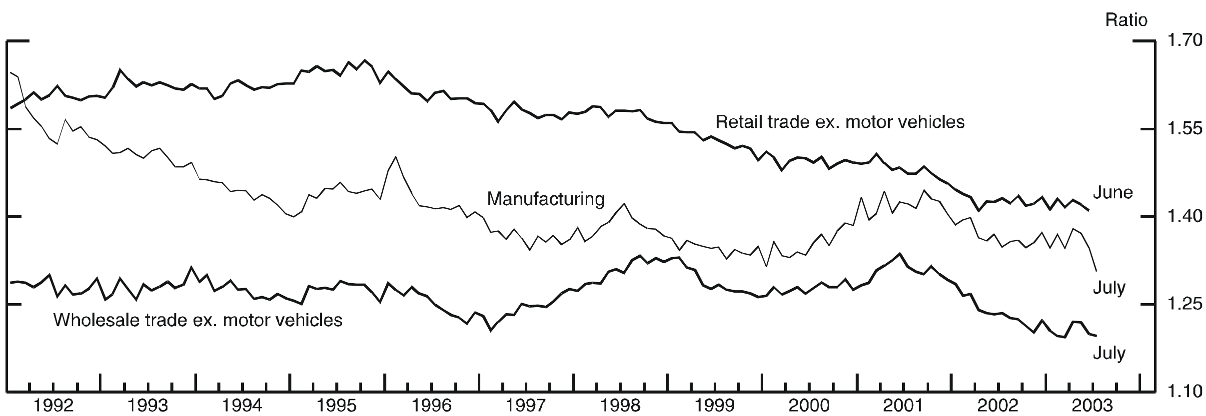
9. The Census Bureau recently released the annual revision to manufacturers' shipments, orders, and inventories. The new data include an upward revision to stocks in 2002, which taken together with small revisions to shipments, implies a shallower decline in the manufacturing inventory-shipments ratio in late 2001 and early 2002 than had previously been reported.

Changes in Manufacturing and Trade Inventories
(Billions of dollars, seasonally adjusted book value, annual rate)

Category	2002 Q4	2003 Q1	2003 Q2	2003 June	2003 July
Manufacturing and trade	43.7	55.7	-11.8	5.0	n.a.
Less wholesale and retail motor vehicles	15.1	23.4	-21.3	-11.1	n.a.
Manufacturing	2.4	4.0	-10.1	-16.6	-27.7
Less aircraft	1.5	5.0	-7.7	-8.5	-11.1
Merchant wholesalers	7.6	8.4	-8.1	-0.5	1.4
Less motor vehicles	4.2	6.8	-9.2	-5.4	7.8
Retail trade	33.8	43.4	6.4	22.1	n.a.
Automotive dealers	25.3	30.8	8.4	11.2	n.a.
Less automotive dealers	8.5	12.6	-2.1	10.9	n.a.

n.a. Not available.

Book-Value Inventories Relative to Shipments and Sales: Manufacturing and Trade



Inventory-Consumption Ratios, Flow-of-Goods System

The days' supply for total IP in the flow-of-goods system has been volatile but moving sideways, on balance, since the early part of 2002.[10] Excluding motor vehicles and parts, the inventory-consumption ratio has declined, on balance, since the end of 2001. The only industries with elevated days' supply levels are paper, communications equipment, and, to a lesser degree, electrical equipment. The days' supply for NIPA factory-value inventories has declined since the beginning of 2002. Excluding motor vehicles and parts, the flow-of-goods system and NIPA series have tracked reasonably well since then.

Federal Government Sector

The federal unified budget balance is being pushed further into deficit by increases in defense spending associated with Iraq and by diminished income tax receipts resulting from the Jobs and Growth Tax Relief Reconciliation Act (JGTRRA). Indeed, the deficit for the twelve months ending in July deepened to $336 billion, compared with $190 billion for the preceding twelve months. Meanwhile, the Congressional Budget Office (CBO) released new budget projections showing much larger deficits than it had anticipated last winter.

Federal receipts in July fell about 8 percent from the year-earlier level, a decrease that largely reflects the impact of the tax legislation enacted in late May. The decline in individual withheld and payroll taxes is consistent with new withholding tables in effect since late June, while the $4-1/2 billion increase in individual refunds matches the amount of the child-credit refund checks that were mailed out by the IRS on July 25. The remaining batches of checks were issued on August 1 and August 8.

Outlays, adjusted for financial transactions and payment-timing shifts, rose 8-1/2 percent in July over year-earlier levels. Increases were especially large for defense spending, which was 17 percent higher than it was in July 2002, and for Medicaid, which was boosted by the state-aid provision of the JGTRRA. Judging from the daily data on vendor payments, defense spending hit a lull in August and early September.

The Administration has announced that it will request an additional $87 billion in budget authority to help pay for activities in Iraq and Afghanistan. The

10. The Board staff's flow-of-goods system measures changes in inventories by tracking the flow of goods in the economy. The system divides the output from the staff's industrial production indexes into more than sixty different product categories. For each product category, the system estimates the supply of goods flowing into the economy–that is, domestic production plus imports. The system then estimates how much of the supply flows out, whether as final demand, including exports, or as inputs for other goods. The difference between the amount flowing in and the amount flowing out represents that change in inventories; we find inventory accumulation if inflows exceed outflows and inventory liquidation if outflows exceed inflows. The inventories are measured wherever held and valued at factory-gate prices.

Federal Government Outlays and Receipts

(Unified basis; billions of dollars)

Function or source	July 2002	July 2003	July Percent change	12 months ending in July 2002	12 months ending in July 2003	12 months ending in July Percent change
Outlays	163.6	177.8	8.7	2,007.0	2,130.0	6.1
Financial transactions[1]	-0.3	0.2	...	12.1	-1.8	...
Payment timing[2]	0.0	0.0	...	-0.9	-0.5	...
Adjusted outlays	163.9	177.6	8.4	1,995.9	2,132.4	6.8
Receipts	134.4	123.6	-8.1	1,817.1	1,794.1	-1.3
Payment timing	0.0	0.0	...	0.0	0.0	...
Adjusted receipts	134.4	123.6	-8.1	1,817.1	1,794.1	-1.3
Surplus/deficit(-)	-29.2	-54.2	...	-190.0	-335.9	...
	Selected components of adjusted outlays and receipts					
Adjusted outlays	163.9	177.6	8.4	1,995.9	2,132.4	6.8
Net interest	15.0	12.6	-16.4	176.2	157.7	-10.5
Non-interest	148.9	165.1	10.9	1,819.7	1,974.7	8.5
National defense	29.2	34.2	17.4	340.2	393.3	15.6
Social security	38.1	39.6	3.8	452.1	471.9	4.4
Medicare	20.8	21.7	4.5	231.5	246.9	6.7
Medicaid	12.6	14.8	17.6	145.1	157.7	8.7
Income security	25.2	25.8	2.2	302.0	334.2	10.7
Agriculture	0.1	1.0	992.5	28.0	22.8	-18.6
Other	22.9	28.0	22.0	320.8	347.9	8.4
Adjusted receipts	134.4	123.6	-8.1	1,817.1	1,794.1	-1.3
Individual income and payroll taxes	115.0	104.7	-9.0	1,502.3	1,479.6	-1.5
Withheld + FICA	113.5	107.8	-5.0	1,377.2	1,372.2	-0.4
Nonwithheld + SECA	5.0	4.7	-7.7	331.4	291.6	-12.0
Refunds (-)	3.5	7.8	121.5	206.3	184.2	-10.7
Corporate	1.7	2.6	57.1	128.2	130.6	1.9
Gross	6.8	6.0	-12.1	187.0	195.5	4.5
Refunds (-)	5.2	3.4	-34.5	58.9	64.8	10.1
Other	17.7	16.3	-8.1	186.6	183.8	-1.5
Adjusted surplus/deficit(-)	-29.5	-54.0	...	-178.8	-338.3	...

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

1. Financial transactions consist of deposit insurance, spectrum auctions, and sales of major assets.

2. 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.

CBO Budget Projections and Economic Assumptions

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Baseline Budget Projections[1] (fiscal years)	Billions of dollars										
Total surplus	-401	-480	-341	-225	-203	-197	-170	-145	-9	161	211
On-budget	-562	-644	-520	-425	-421	-434	-426	-417	-298	-143	-105
Off-budget	162	164	179	199	219	237	255	273	289	304	317
Economic Assumptions (calendar years)	Percent change, year over year										
Nominal GDP	3.7	5.3	5.4	5.7	5.4	5.3	5.1	5.0	4.8	4.9	4.9
Real GDP	2.2	3.8	3.5	3.3	3.2	3.0	2.9	2.7	2.6	2.6	2.6
CPI-U	2.3	1.9	2.4	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
	Percent, annual average										
Unemployment rate	6.2	6.2	5.7	5.4	5.3	5.2	5.2	5.2	5.2	5.2	5.2
Treasury yields											
Three-month	1.0	1.7	3.2	4.0	4.7	4.9	4.9	4.9	4.9	4.9	4.9
Ten-year	4.0	4.6	5.5	5.8	5.8	5.8	5.8	5.8	5.8	5.8	5.8

1. The on-budget surplus excludes the social security surplus and the Postal Service (which are off-budget). The baseline assumes that budget authority for discretionary programs grows with inflation after fiscal 2003. In addition, it assumes that no new mandatory spending or tax legislation is enacted.

Source. Congressional Budget Office, *The Budget and Economic Outlook: An Update* (August 2003).

requested amount exceeds the $79 billion provided by the defense supplemental enacted last April. Although details are sketchy, the new request likely will include about $66 billion for military and intelligence operations and $20 billion for reconstruction.

The CBO now expects the unified budget deficit to total $401 billion in fiscal 2003, and the monthly and daily data in hand are consistent with that estimate. The CBO projects a baseline federal budget deficit of $480 billion in fiscal 2004. It expects the budget to remain in the red through 2011, although the deficits are projected to shrink appreciably after next year and turn into small surpluses in 2012 and 2013.

A variety of conventions that the CBO uses in constructing its longer-term projections are important in shaping those estimates. For example, the CBO baseline projections assume that, on an inflation-adjusted basis, discretionary spending will continue at its current level in future years. The level of discretionary spending in 2003 includes $80 billion in supplemental appropriations, mainly for our activities in Iraq. As a result, the baseline effectively assumes that this year's funding for the war in Iraq will be renewed each year with adjustments for inflation. Nevertheless, baseline discretionary outlays over the 2004-13 period average 7 percent of GDP, less than the 7-1/2 percent average seen during the 1990s. At the same time, the baseline projections assume no changes to mandatory programs or tax laws currently in place. For example, the CBO assumes that tax provisions scheduled to expire between now and 2013 will actually do so; according to the CBO, extending the expiring provisions would add a cumulative $2 trillion to the deficit over this period, if not offset by other policy actions.

State and Local Government Sector

Real expenditures on consumption and investment by state and local governments were flat over the first half of the year and appear to have remained subdued in the third quarter. Outlays for construction projects edged down in July after having risen for three months.[11] Also, state and local employment fell 21,000 in August after an upward-revised increase of 11,000 in July. Virtually all of the movement in employment over the past two months has been at the local level, where non-educational payrolls have fallen in six out of the past seven months.

According to a new report from the National League of Cities, states reduced appropriations for aid to cities in fiscal 2004 by $2.3 billion (or about 9 percent)

11. The CPIP release for July contained sizable upward revisions to the figures for May and June, mainly for educational facilities and highways. After taking account of these revisions, we estimate that total real state and local spending was essentially unchanged in the second quarter, compared with the BEA's preliminary estimate of a decline of 0.7 percent (annual rate).

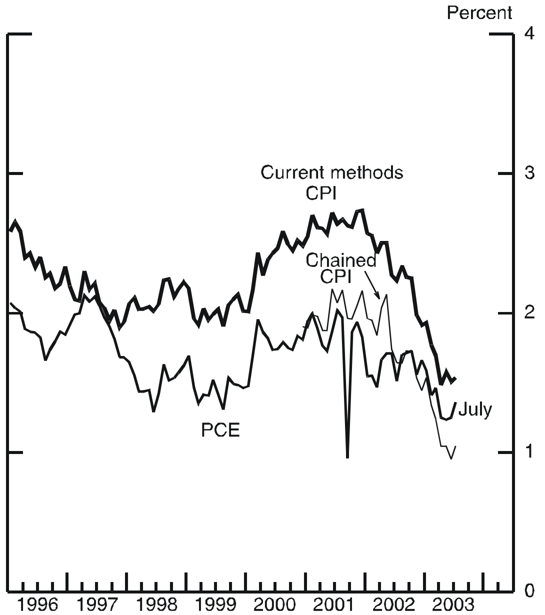
RECENT PRICE INDICATORS
(Percent)

	From 12 months earlier		From 3 months earlier		2003	
	July 2002	July 2003	Apr. 2003	July 2003	June	July
			-Annual rate-		-Monthly rate-	
CPI						
Total	1.5	2.1	2.4	1.3	0.2	0.2
Food	1.4	2.1	3.0	3.4	0.4	0.1
Energy	-5.2	9.0	24.8	-7.1	0.8	0.4
Ex. food and energy	2.2	1.5	0.4	1.9	0.0	0.2
Ex. tobacco	2.2	1.5	0.5	1.9	0.0	0.2
Core commodities	-1.3	-1.8	-1.7	-2.2	-0.1	-0.1
Core services	3.8	2.9	1.3	3.7	0.1	0.3
Current-methods total	1.5	2.1	2.4	1.3	0.2	0.2
Ex. food and energy	2.2	1.5	0.4	1.9	0.0	0.2
Ex. tobacco	2.2	1.6	0.5	1.9	0.0	0.2
Chained CPI (NSA)[1]	1.1	1.7	--	--	--	--
Ex. food and energy[1]	1.6	1.0	--	--	--	--
PCE Prices						
Total	1.2	1.8	2.2	1.3	0.2	0.2
Food	1.7	1.9	2.7	2.7	0.4	0.0
Energy	-5.4	10.4	26.3	-8.3	1.0	0.5
Ex. food and energy	1.5	1.4	0.9	1.7	0.1	0.2
Ex. tobacco	1.5	1.4	0.9	1.7	0.2	0.2
Core commodities	-1.6	-1.9	-2.0	-1.9	-0.1	0.0
Core services	2.9	2.7	2.0	3.2	0.2	0.3
Core market-based	1.2	0.8	0.2	1.2	0.1	0.2
Core nonmarket-based	2.7	3.5	3.3	3.2	0.4	0.1
PPI						
Total finished goods	-1.2	3.0	3.2	1.4	0.5	0.1
Food	-1.1	3.7	5.4	1.1	0.4	-0.2
Energy	-5.3	14.4	15.2	4.0	3.4	0.3
Ex. food and energy	-0.3	0.2	-0.3	0.8	-0.1	0.2
Ex. tobacco	-0.6	0.7	-0.1	0.8	-0.1	0.2
Core consumer goods	0.1	-0.1	-0.8	0.5	-0.1	0.1
Capital equipment	-0.9	0.7	0.3	1.2	-0.1	0.4
Intermediate materials	-1.5	4.4	7.5	-0.9	0.5	0.2
Ex. food and energy	-0.4	1.8	3.8	-0.6	0.0	-0.1
Crude materials	-6.2	24.5	-0.6	13.4	4.5	-2.9
Ex. food and energy	7.6	3.9	8.0	-2.2	0.6	0.8

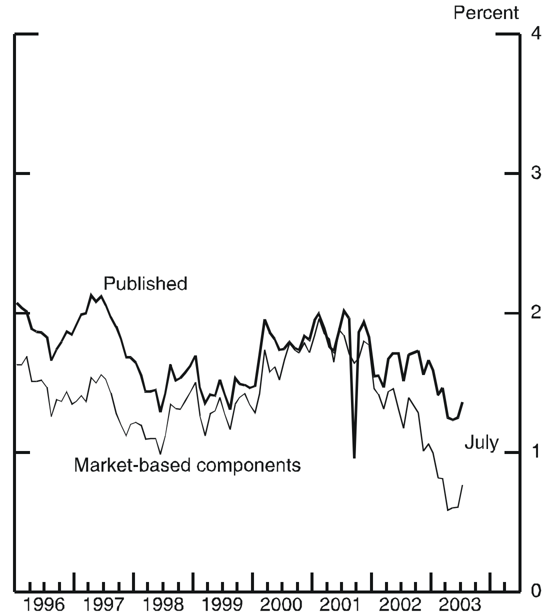
1. Higher frequency figures are not shown for data that are not seasonally adjusted.

Measures of Core Consumer Price Inflation
(12-month change)

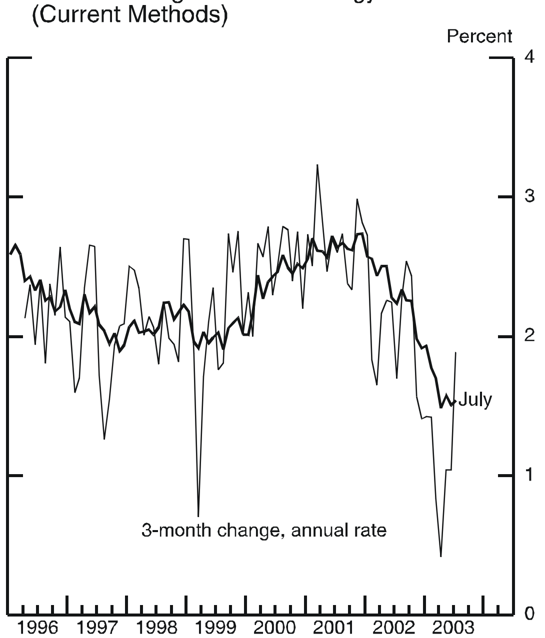
CPI and PCE excluding Food and Energy



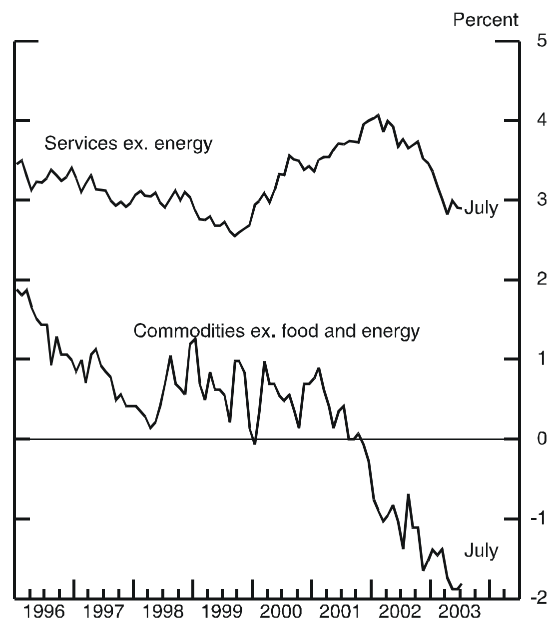
PCE excluding Food and Energy



CPI excluding Food and Energy
(Current Methods)



CPI Services and Commodities



in the aggregate. These are the first declines in at least a decade and included sizable reductions in aid in California, Massachusetts, Florida, and Minnesota. Historically, state aid has accounted for roughly 20 percent of cities' general revenue, with the remainder coming mainly from taxes and fees.

Prices and Labor Costs

Consumer prices have posted small increases, on net, since the spring after having been pushed up earlier in the year by the surge in energy prices. The overall CPI in July was 2.1 percent above its year-earlier level, an acceleration of 0.6 percentage point relative to the twelve-month change a year earlier. Core consumer prices rose somewhat faster over the three months ending in July, on average, than they had earlier in the year. Even so, the twelve-month change in most of these measures is considerably smaller than it was a year earlier.

Consumer energy prices rose 0.4 percent in July after June's 0.8 percent increase. The July rise was led by increases in prices for gasoline and heating oil that were only partly offset by declines in natural gas and electricity prices. Based on available survey data, we anticipate an even larger jump in gasoline prices in August, as supply disruptions—including a temporary pipeline shutdown in Arizona and maintenance problems at several refineries—have combined with strong demand and lean inventories to push up wholesale and retail margins. This pressure on retail prices should be short-lived, however: Wholesale gasoline prices have already moved most of the way back to levels more consistent with crude oil costs, and this should show through to retail prices in the next few weeks. Elsewhere, cooler-than-usual weather earlier this summer allowed rapid replenishment of natural gas inventories; although the unusually hot weather in July and August reduced the rate of accumulation, the remaining inventory gap is likely to be nearly closed by the start of winter.

The CPI for food rose 0.1 percent in July as price increases for meats, eggs, and fresh fruit were largely offset by declines for a number of other items. A ban on imports of beef from Canada (the result of concerns over mad cow disease) boosted beef prices and contributed significantly to the overall increase in food prices; however, this ban was partially lifted in August, and some imports likely resumed by the end of that month. In all, food prices rose 2.1 percent over the twelve months ending in July, 0.7 percentage point faster than the rate a year earlier.

Excluding food and energy, the CPI rose 0.2 percent in July after a 0.3 percent rise in May and no change in June. These readings are somewhat higher, on average, than the exceptionally low figures recorded earlier in the year, when core inflation was depressed by a number of transitory factors. As of July, the twelve-month change in the core CPI stood at 1.5 percent, down 0.7 percentage point relative to a year earlier.

SPOT PRICES OF SELECTED COMMODITIES
(Percent change except as noted)

	Current price (dollars)	2001	2002	Dec. 31 to Aug. 5[1]	Aug. 5[1] to Sept. 9	Memo: 52-week change to Sept. 9
Metals						
Copper (lb.)	0.860	-22.0	2.8	15.1	2.4	17.8
Steel scrap (ton)	128.667	-17.7	49.2	27.5	4.0	24.1
Aluminum, London (lb.)	0.643	-14.3	0.7	9.9	-4.0	5.9
Precious metals						
Gold (oz.)	382.250	1.2	24.7	1.0	9.7	19.8
Silver (oz.)	5.255	-3.5	3.0	4.0	5.5	14.7
Forest products[2]						
Lumber (m. bdft.)	346.000	25.0	-13.0	32.0	31.1	65.6
Plywood (m. sqft.)	520.000	3.2	-0.3	29.4	39.0	76.3
Petroleum						
Crude oil (barrel)	27.520	-16.3	65.8	-5.5	-8.9	-4.4
Gasoline (gal.)	0.951	-28.0	54.6	13.5	-1.1	21.4
Fuel oil (gal.)	0.753	-42.6	57.4	-3.1	-10.2	-3.4
Livestock						
Steers (cwt.)	84.000	-19.7	12.9	9.6	6.3	31.3
Hogs (cwt.)	39.500	-9.9	-18.9	35.0	-2.5	31.7
Broilers (lb.)	0.626	3.7	7.4	3.6	1.0	18.7
U.S. farm crops						
Corn (bu.)	2.315	-4.1	19.2	-11.1	13.5	-14.7
Wheat (bu.)	3.540	-8.9	30.4	-15.5	0.9	-32.2
Soybeans (bu.)	6.115	-13.4	35.6	-4.2	13.9	5.2
Cotton (lb.)	0.539	-45.7	53.8	9.0	3.4	40.9
Other foodstuffs						
Coffee (lb.)	0.590	-35.3	1.1	21.3	9.3	20.4
Memo:						
JOC Industrials	96.400	-17.1	16.2	8.7	5.7	18.9
JOC Metals	85.600	-17.0	9.5	12.4	0.5	13.5
CRB Futures	244.380	-16.3	23.0	0.1	4.1	7.3
CRB Spot Industrials	269.910	-14.6	14.4	5.9	2.5	11.9

Note. Changes are from the last week of the preceding year to the last week of the period indicated except as noted.
1. Week of the August Greenbook.
2. Reflects prices on the Friday before the date indicated.

Core commodities prices, which began to slide in 2001, decelerated 0.5 percentage point over the year ending in July. Prices of core services, led by a significant stepdown in the rate of increase of shelter costs, particularly owners' equivalent rent (OER), decelerated 0.9 percentage point. The reduction in OER inflation reflects, in part, a sharp acceleration in utilities prices; as these prices moderate, we expect some of this effect to unwind.[12] In addition, the initial wave of outsized tuition increases by state university systems was apparent in July's 1.0 percent rise in college tuition, and these increases should push core services prices higher in August and September.

Core PCE prices rose 0.2 percent in July following June's 0.1 percent increase. On a twelve-month change basis, core PCE inflation in July was 1.4 percent—essentially unchanged from the 1.5 percent increase posted over the preceding year. The stability of core PCE inflation relative to the sharp deceleration in the core CPI is largely the result of two factors. First, prices for the components of core PCE for which market-based prices do not exist—the so-called "nonmarket" portion of the index—accelerated 3/4 percentage point over this period.[13] Second, the twelve months ending in July saw a sharp deceleration in shelter rents, which receive a greater weight in the CPI. The core component of the chained CPI—which, like the PCE price index, employs a superlative aggregation formula that attempts to account for shifts in consumer expenditure patterns following relative price changes—rose 1.0 percent over the twelve months ending in July, compared with a year-earlier twelve-month change of 1.6 percent.

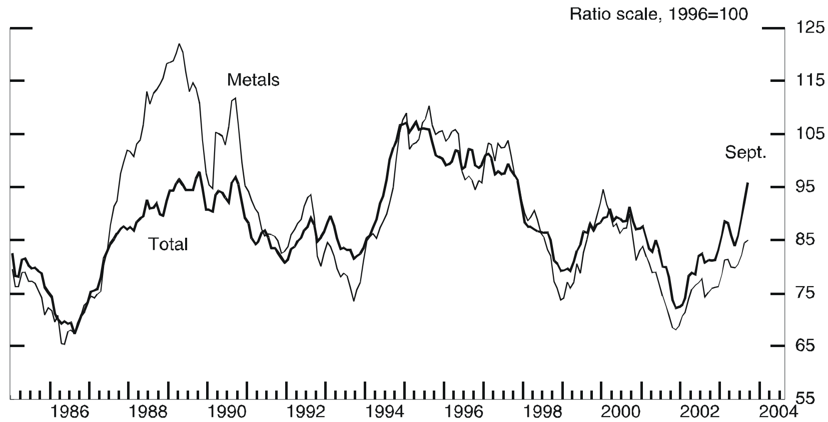
The PPI for capital equipment moved up 0.4 percent in July. After having fallen 0.9 percent over the preceding year, prices of capital equipment rose 0.7 percent in the twelve months ending in July; this acceleration was relatively widespread across categories of capital goods. At earlier stages of processing, the twelve-month change in the PPI for core intermediate goods stood at 1.8 percent in July, compared with a year-earlier decline of 0.4 percent; price increases for energy-intensive intermediate goods have been especially large over the past year. More recently, however, core intermediate prices have begun to edge lower. Spot commodity price indexes have moved higher on net since the August Greenbook: Continued price increases for plywood have helped push the *Journal of Commerce* index of industrial prices up 5-3/4 percent since early August, while the Commodity Research Bureau's measure of spot industrial

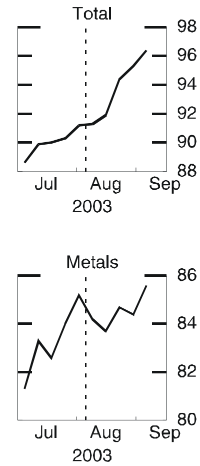
12. The BLS removes an estimate of landlord-provided utilities costs from the rent quotes that it uses to construct owners' equivalent rent. Hence, an acceleration in utilities prices will tend to lower OER relative to tenants' rent, all else equal.

13. Market-based core PCE price inflation declined 0.4 percentage point between July 2002 and July 2003, to 0.8 percent; this drop is larger than the decline seen in overall core PCE price inflation, but smaller than the decline in core CPI inflation.

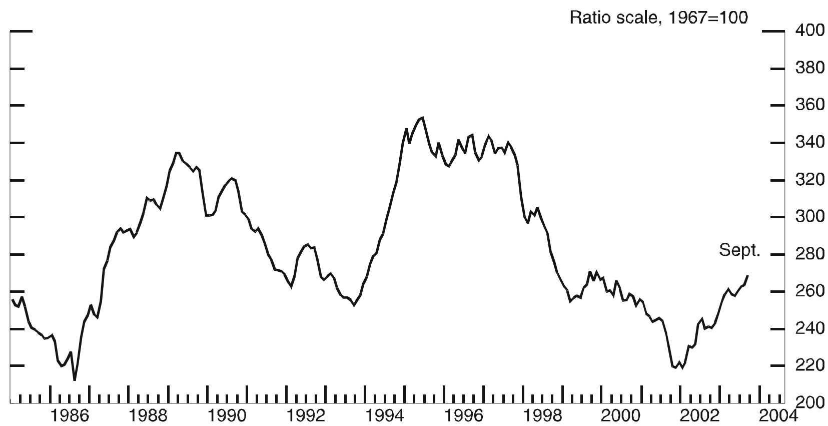
Commodity Price Measures

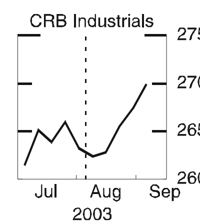
Journal of Commerce Index



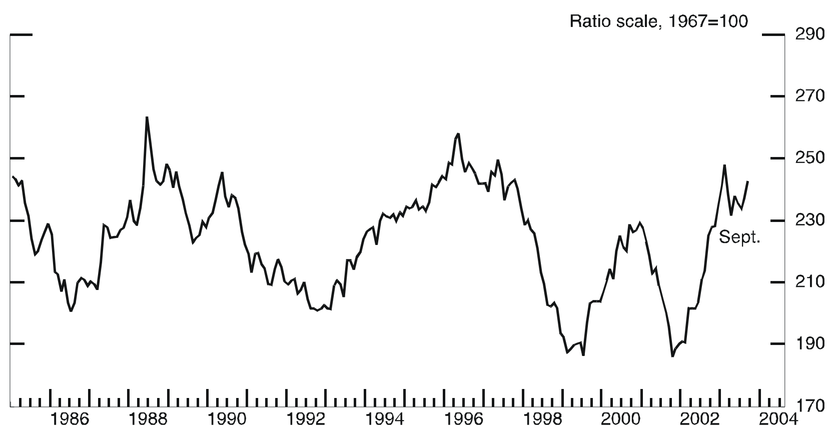


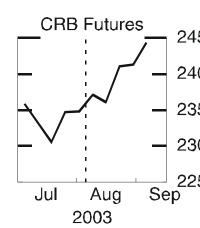
CRB Spot Industrials





CRB Futures





Note. Larger panels show monthly average of weekly data through last available week. Smaller panels show 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 Commodity Research Board (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.

BROAD MEASURES OF INFLATION
(4-quarter percent change)

	2000 Q2	2001 Q2	2002 Q2	2003 Q2
Product prices				
GDP chain price index	2.1	2.5	1.1	1.5
Less food and energy	2.0	2.0	1.5	1.2
Nonfarm business chain price index[1]	1.8	2.0	0.4	0.8
Expenditure prices				
Gross domestic purchases chain price index	2.5	2.3	0.9	1.6
Less food and energy	1.9	1.9	1.4	1.3
PCE chain price index	2.6	2.4	1.1	1.7
Less food and energy	1.8	1.8	1.7	1.2
PCE chain price index, market-based components	2.5	2.5	0.8	1.3
Less food and energy	1.6	1.8	1.4	0.6
CPI	3.3	3.4	1.3	2.2
Less food and energy	2.4	2.6	2.4	1.5
Chained CPI	n.a.	2.7	1.1	1.7
Less food and energy	n.a.	2.0	2.0	1.0
Median CPI	2.5	3.5	3.6	2.2
Trimmed mean CPI	2.4	2.8	2.2	1.9

1. Excluding housing.

SURVEYS OF (CPI) INFLATION EXPECTATIONS
(Percent)

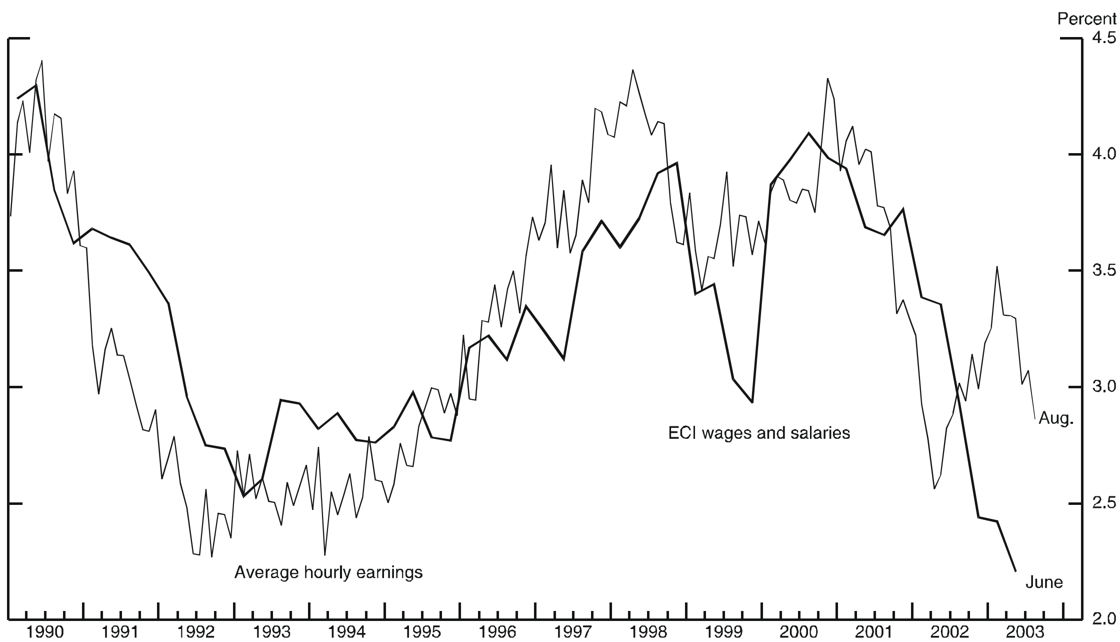
	Actual inflation[1]	University of Michigan: 1 year Mean[2]	University of Michigan: 1 year Median[2]	University of Michigan: 5 to 10 years Mean[3]	University of Michigan: 5 to 10 years Median[3]	Professional forecasters (10-year)[4]
2001-Q4	1.9	1.5	1.1	3.1	2.8	2.6
2002-Q1	1.3	2.6	2.2	3.1	2.8	2.5
Q2	1.3	3.1	2.7	3.4	2.9	2.5
Q3	1.6	2.8	2.6	3.2	2.7	2.5
Q4	2.2	2.7	2.5	3.3	2.8	2.5
2003-Q1	2.9	3.2	2.8	3.0	2.7	2.5
Q2	2.1	2.6	2.2	3.1	2.7	2.5
Q3						2.5
2003-Jan.	2.6	2.7	2.5	3.1	2.7	
Feb.	3.0	3.2	2.7	3.1	2.7	
Mar.	3.0	3.8	3.1	2.9	2.8	2.5
Apr.	2.2	2.7	2.4	3.1	2.7	
May	2.1	2.5	2.0	3.1	2.8	
June	2.1	2.5	2.1	3.0	2.7	2.5
July	2.1	2.3	1.7	3.2	2.7	
Aug.		2.8	2.5	3.0	2.7	
Sept.						2.5

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.

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

	12-month percent change			Percent change to Aug 2003 from month indicated		Percent change	
	Aug. 2001	Aug. 2002	Aug. 2003	Feb. 2003	May 2003	July 2003	Aug. 2003
	-Annual rate					- Monthly rate-	
Total private nonfarm	3.8	3.0	2.9	2.1	2.6	0.3	0.1
Manufacturing	3.4	3.2	2.9	1.9	2.6	0.1	0.3
Construction	2.8	2.8	2.3	1.6	0.8	0.0	0.2
Wholesale trade	2.5	1.6	2.2	1.7	2.6	0.2	0.1
Retail trade	3.9	3.4	2.1	1.4	2.0	0.3	0.1
Transportation and warehousing	1.3	3.0	3.4	1.4	2.0	0.6	-0.4
Information	3.9	1.2	6.0	5.4	4.8	0.7	0.3
Financial activities	4.3	4.3	6.4	7.5	9.0	1.0	0.2
Professional and business services	5.3	2.6	2.4	1.1	0.5	0.1	0.1
Education and health services	4.8	4.3	2.5	1.4	2.1	0.2	0.1
Leisure and hospitality	2.7	2.6	1.9	-0.2	1.4	0.1	0.0
Other services	4.3	3.4	1.4	-0.4	0.9	0.1	0.0

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



prices—which excludes forest products—has risen 2-1/2 percent over this period.

Like consumer price inflation, inflation as measured by most broad price indexes has been boosted over the past year by accelerating energy prices, while broader measures of core price inflation have generally moved a bit lower. In particular, GDP price inflation through the second quarter was 0.4 percentage point higher than a year earlier, while the corresponding core measure decelerated 0.3 percentage point.

As measured by the Michigan survey, median year-ahead expected inflation rebounded in August to 2.5 percent, well above the 1.7 percent reading for July and close to the average in the first quarter and in 2002. Median expected inflation over the next five to ten years remained at 2.7 percent and has changed little on net since the beginning of last year.

LABOR COSTS
(Percent change; annual rate; based on seasonally adjusted data)

			2002		2003		2002:Q2 to 2003:Q2
	2001[1]	2002[1]	Q3	Q4	Q1	Q2	
Compensation per hour							
Total business	2.9	2.8	2.1	1.6	4.8	4.3	3.2
Nonfarm business	2.7	2.8	2.0	1.6	4.1	3.8	2.9
Nonfinancial corporations[2]	2.4	3.3	2.7	2.8	5.2	3.9	3.6
Unit labor costs							
Total business	-.3	-1.4	-3.6	.1	2.0	-2.7	-1.1
Nonfarm business	-.5	-1.6	-3.7	-.1	2.0	-2.8	-1.2
Nonfinancial corporations[2]	-1.8	-1.0	-.5	-1.0	.9	-3.8	-1.1

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, finance and insurance companies; the sector accounts for about two-thirds of business employment.

We have received relatively little information on labor costs since the August Greenbook. As measured by the Productivity and Costs (P&C) data, the four-quarter change in nonfarm hourly compensation stood at 2.9 percent in the second quarter, about unchanged relative to a year earlier. In August, average hourly earnings of production or nonsupervisory workers on private nonfarm payrolls rose 0.1 percent following July's 0.3 percent increase. With the August figure, the twelve-month change in average hourly earnings stands at 2.9 percent, little changed from a year earlier.

Domestic Financial Developments

III-T-1

Selected Financial Market Quotations

(One-day quotes in percent except as noted)

Instrument	2001	2003			Change to Sept. 9 from selected dates (percentage points)		
	Sept. 10	May 5	Aug. 11	Sept. 9	2001 Sept. 10	2003 May 5	2003 Aug. 11
Short-term							
FOMC intended federal funds rate	3.50	1.25	1.00	1.00	-2.50	-.25	.00
Treasury bills [1]							
3-month	3.19	1.11	0.94	0.94	-2.25	-.17	.00
6-month	3.13	1.14	1.04	1.01	-2.12	-.13	-.03
Commercial paper (A1/P1 rates)							
1-month	3.42	1.21	1.04	1.02	-2.40	-.19	-.02
3-month	3.24	1.20	1.04	1.03	-2.21	-.17	-.01
Large negotiable CDs [1]							
1-month	3.46	1.26	1.07	1.07	-2.39	-.19	.00
3-month	3.26	1.24	1.07	1.08	-2.18	-.16	.01
6-month	3.24	1.22	1.12	1.13	-2.11	-.09	.01
Eurodollar deposits [2]							
1-month	3.41	1.25	1.05	1.06	-2.35	-.19	.01
3-month	3.26	1.21	1.07	1.08	-2.18	-.13	.01
Bank prime rate	6.50	4.25	4.00	4.00	-2.50	-.25	.00
Intermediate- and long-term							
U.S. Treasury[3]							
2-year	3.59	1.56	1.83	1.71	-1.88	.15	-.12
10-year	5.14	4.09	4.56	4.55	-.59	.46	-.01
30-year	5.55	4.97	5.46	5.40	-.15	.43	-.06
U.S. Treasury 10-year indexed note	3.28	2.18	2.31	2.22	-1.06	.04	-.09
Municipal revenue (Bond Buyer) [4]	5.25	5.09	5.42	5.41	.16	.32	-.01
Private instruments							
10-year swap	5.62	4.29	4.80	4.87	-.75	.58	.07
10-year FNMA[5]	5.68	4.39	4.96	4.95	-.73	.56	-.01
10-year AA [6]	6.30	4.83	5.24	5.27	-1.03	.44	.03
10-year BBB [6]	7.11	5.84	6.17	6.16	-.95	.32	-.01
High-yield [7]	12.72	9.54	9.69	9.06	-3.66	-.48	-.63
Home mortgages (FHLMC survey rate) [8]							
30-year fixed	6.89	5.70	6.34	6.44	-.45	.74	.10
1-year adjustable	5.64	3.74	3.80	3.98	-1.66	.24	.18

Stock exchange index	Record high		2003			Change to Sept. 9 from selected dates (percent)		
	Level	Date	May 5	Aug. 11	Sept. 9	Record high	2003 May 5	2003 Aug. 11
Dow-Jones Industrial	11,723	1-14-00	8,532	9,217	9,507	-18.90	11.44	3.14
S&P 500 Composite	1,527	3-24-00	927	981	1,023	-33.01	10.43	4.34
Nasdaq (OTC)	5,049	3-10-00	1,504	1,662	1,873	-62.89	24.56	12.75
Russell 2000	606	3-9-00	410	459	514	-15.27	25.32	11.82
Wilshire 5000	14,752	3-24-00	8,817	9,431	9,933	-32.67	12.65	5.32

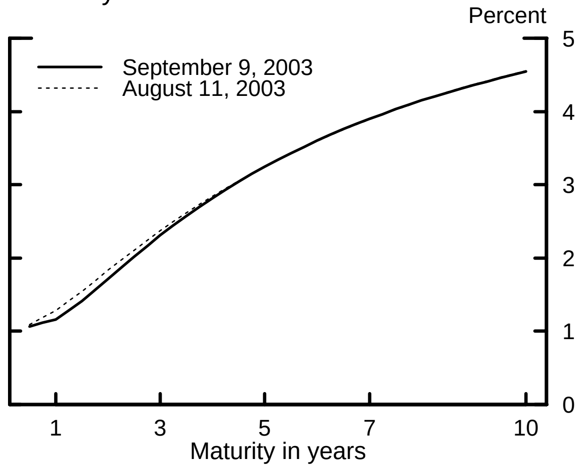
1. Secondary market.
2. Bid rates for eurodollar deposits collected around 9:30 a.m. Eastern time.
3. Derived from a smoothed Treasury yield curve estimated using off-the-run securities.
4. Most recent Thursday quote.
5. Constant maturity yields estimated from Fannie Mae domestic non-callable coupon securities.
6. Derived from smoothed corporate yield curves estimated using Merrill Lynch bond data.
7. Merrill Lynch Master II high-yield bond.
8. For week ending Friday previous to date shown.

NOTES:

September 10, 2001 is the day before the terrorist attacks.
May 5, 2003 is the day before the May FOMC meeting.
August 11, 2003 is the day before the most recent FOMC meeting.

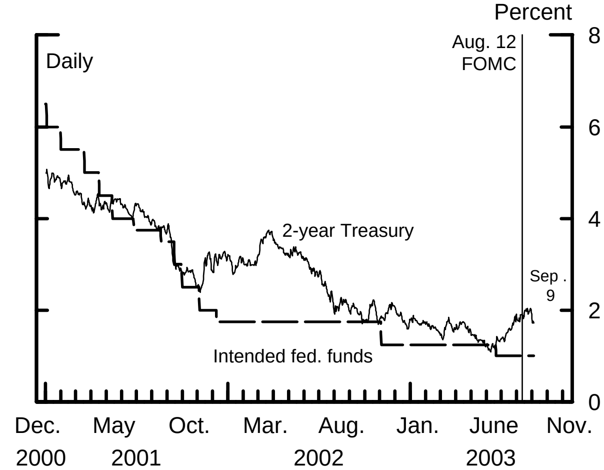
Selected Interest Rates

Treasury Yield Curve

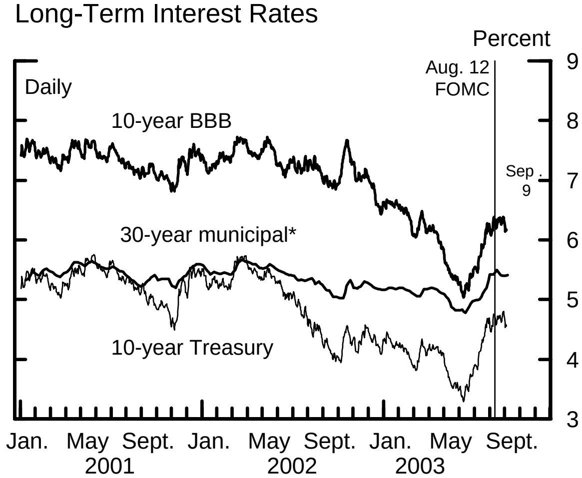


Note. Smoothed yield curve estimated using off-the-run Treasury coupon securities. Yields shown are those on notional par Treasury securities with semiannual payments.

Short-Term Interest Rates

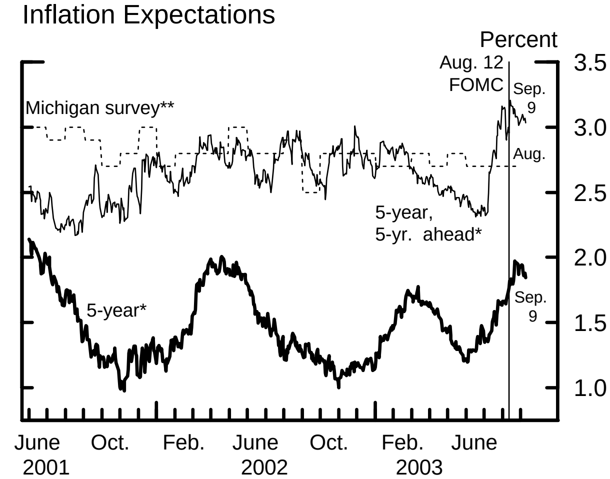


Long-Term Interest Rates



*Bond Buyer Revenue, weekly Thursday frequency.

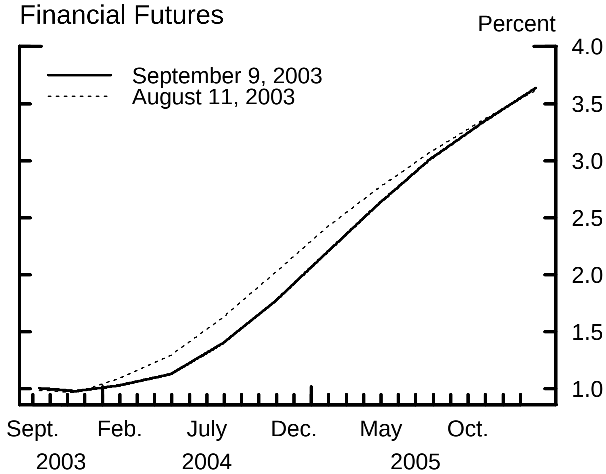
Inflation Expectations



*Estimates based upon smoothed nominal and inflation-indexed yield curves.

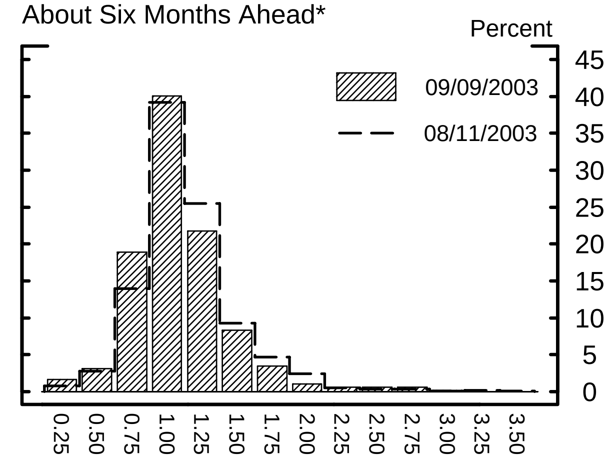
**Monthly median 5- to 10-year inflation expectations.

Expected Federal Funds Rates Estimated from Financial Futures



Note. Estimates from federal funds and eurodollar futures rates with an allowance for term premia and other adjustments.

Implied Distribution of Federal Funds Rate About Six Months Ahead*



*Based on the distribution of the three-month eurodollar rate five months ahead (adjusted for a risk premium), as implied by options on eurodollar futures contracts.

Domestic Financial Developments

Overview

During the first three weeks of the intermeeting period, market participants were heartened by a string of better-than-expected spending indicators, and they bid up Treasury yields and stock prices. More recently, though, disappointing labor market data and statements by Federal Reserve officials prompted a decline in yields, although equity prices continued to move higher. On balance, shorter-term Treasury yields have edged lower since the August FOMC meeting, while longer-term yields are about unchanged. Broad stock market indexes have risen about 4 to 5 percent. Share prices for technology companies and small firms have outperformed the broader indexes, and risk spreads on high-yield bonds have narrowed considerably. The expected path of the federal funds rate estimated from futures quotes suggests that market participants expect monetary policy to remain on hold well into next year, but they still anticipate a substantial increase in the federal funds rate over the second half of 2004 and 2005.

The rise in longer-term interest rates this summer has slowed bond issuance by businesses and mortgage refinancing by households, but it does not appear to have hampered the ability of either sector to finance desired spending. State and local governments have pared their refundings of higher-cost bonds but have continued to issue a substantial amount of debt overall, and federal borrowing has remained brisk.

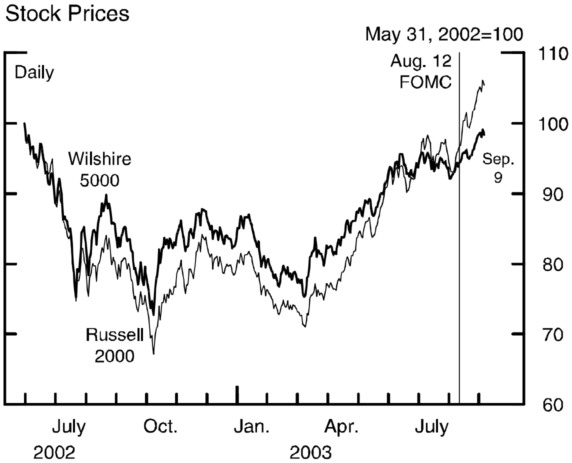
Policy Expectations and Interest Rates

The FOMC's decision to leave the federal funds rate target and its risks assessment unchanged at its August meeting was widely anticipated. However, the accompanying statement indicating that "policy accommodation can be maintained for a considerable period" prompted a decline in short-term Treasury yields and in eurodollar futures rates following the announcement. Over subsequent weeks, interest rates moved higher as investors responded to the generally positive spending data. But yields fell back toward the end of the period after labor market data proved disappointing and statements of Federal Reserve officials that suggested inflation pressures remained subdued.

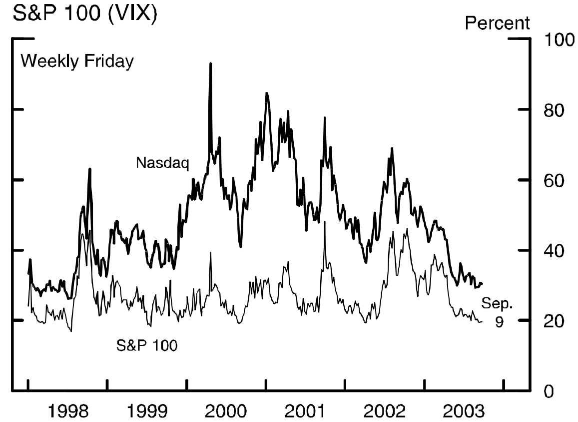
Market participants have pushed back the anticipated onset of policy tightening, leaving the expected level of the funds rate over the second half of 2004 about 25 basis points below the level expected at the time of the August FOMC meeting. Nonetheless, investors have not revised the cumulative amount of tightening that they anticipate by the end of 2005, when the funds rate is expected to reach about 3-1/2 percent. Reflecting these adjustments to the path

Stock Prices and Corporate Risk Spreads

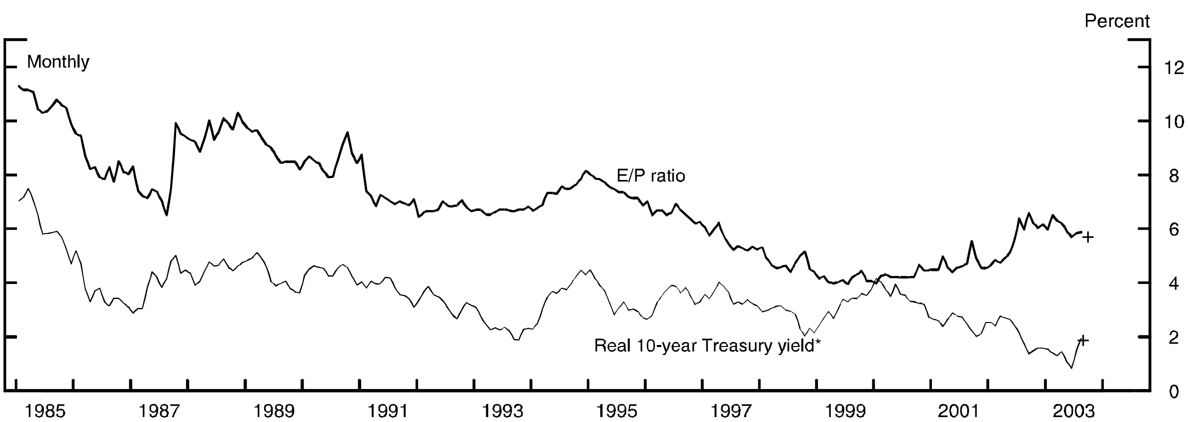
Stock Prices



Implied Volatility on Nasdaq 100 (VXN) and
S&P 100 (VIX)

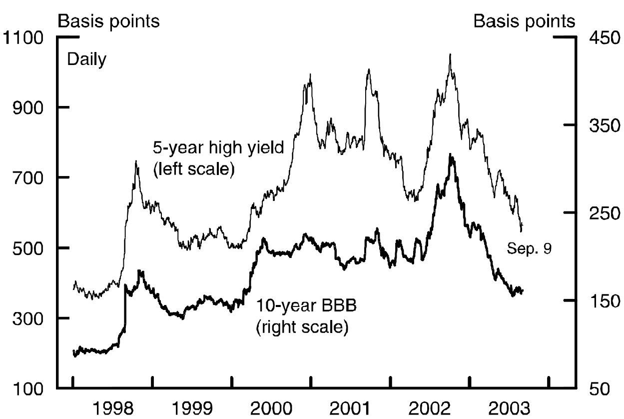


12-Month Forward Earnings-Price Ratio for S&P 500 and 10-Year Treasury

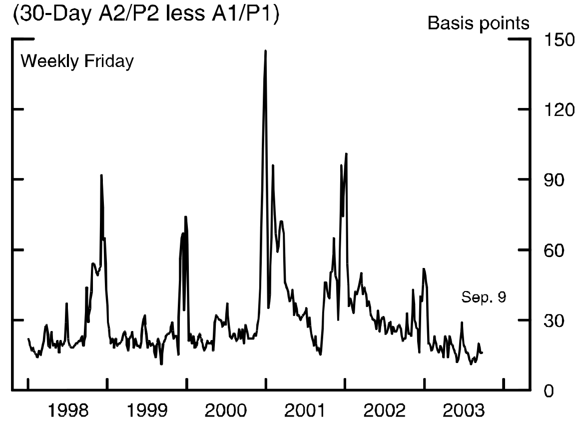


* 10-year Treasury yield minus Philadelphia Fed 10-year expected inflation.
+ Denotes the latest observation using daily interest rates and stock prices and latest earnings data from I/B/E/S.

Corporate Bond Spreads to Similar Maturity Treasury



Commercial Paper Quality Spread
(30-Day A2/P2 less A1/P1)



for short-term rates, two-year Treasury yields declined over the intermeeting period, while ten-year nominal yields were about unchanged.[1]

Inflation compensation, as measured by the spread of nominal yields to those of inflation-indexed securities, edged higher during the intermeeting period. The current levels of inflation compensation over the next five years and over the period from five to ten years ahead remained at or near the high end of their ranges of the past several years. Inflation expectations from the Michigan Survey were unchanged last month.

Stock Prices and Corporate Interest Rates

Broad equity price indexes rose about 4 to 5 percent over the intermeeting period on the more favorable outlooks for the economy and corporate profits. Small-cap and tech stocks outperformed the broad measures, as the Nasdaq and Russell 2000 gained about 12 percent, reaching their highest levels in nearly a year and a half. The implied volatility of equity prices varied in a low range over the intermeeting period, with that on the Nasdaq touching its lowest level since 1998. For the broad market, the twelve-month forward S&P 500 earnings-to-price ratio edged down, and its gap to the real 10-year Treasury yield—a rough measure of the equity premium—narrowed a bit. This measure now stands at about its average level over the decade prior to the run-up in stock prices in the late 1990s.

Yield spreads for investment-grade corporate bonds over Treasuries were about unchanged during the intermeeting period. In contrast, spreads for speculative-grade issuers, which may benefit more in the economic recovery, fell considerably, leaving them at their lowest levels since early 2000.

Business Finance

Bond issuance has shifted down of late as the opportunistic issuance in which many firms tapped markets to take advantage of low interest rates in May and June has ended. Issuance by investment-grade nonfinancial firms was sluggish in August, and although issuance of speculative bonds remains fairly robust, it dropped back last month from its extraordinary pace in the previous three months. The amount of short- and intermediate-term credit outstanding changed little on net in August; commercial paper edged up for the second month in a row, while C&I loans fell. The slower pace of net borrowing in the past two months likely does not indicate a softening in business spending plans, as the

1. Anecdotal reports suggest that the influence of mortgage hedging activities, which may have magnified movements in longer-term Treasury yields in July, waned over the intermeeting period. In addition, trading conditions in the Treasury market, which had been choppy at times in July, reportedly have largely returned to normal.

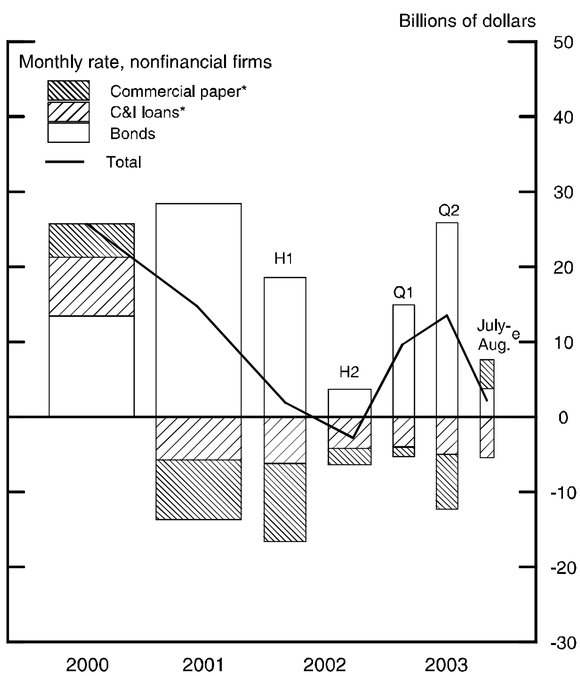
Business Finance

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

Type of security	2000	2001	2002 H1	2002 H2	2003 H1	2003 July	2003 Aug. e
Nonfinancial corporations							
Stocks [1]	9.9	6.5	7.4	2.9	2.8	3.3	1.7
Initial public offerings	4.4	2.1	1.2	0.3	0.0	1.0	0.0
Seasoned offerings	5.5	4.4	6.3	2.6	2.8	2.3	1.7
Bonds	22.6	39.1	31.4	18.0	36.6	29.0	17.8
Investment grade [2]	13.2	27.5	19.8	11.6	20.0	7.2	5.6
Speculative grade [2]	4.7	8.9	6.4	3.3	11.5	18.6	8.1
Other (sold abroad/unrated)	4.8	2.7	5.3	3.1	5.1	3.2	4.1
Memo							
Net issuance of commercial paper [3]	4.5	-8.0	-10.4	-2.2	-4.3	5.4	2.2
Change in C&I loans at commercial banks [3]	7.8	-5.7	-6.2	-4.2	-7.5	11.7	-4.6
Removing FIN 46 effects						*-6.5*	*-4.2*
Financial corporations							
Stocks [1]	1.4	4.2	4.2	3.8	6.0	9.6	4.0
Bonds [4]	57.9	80.2	89.8	83.9	106.3	92.1	79.2

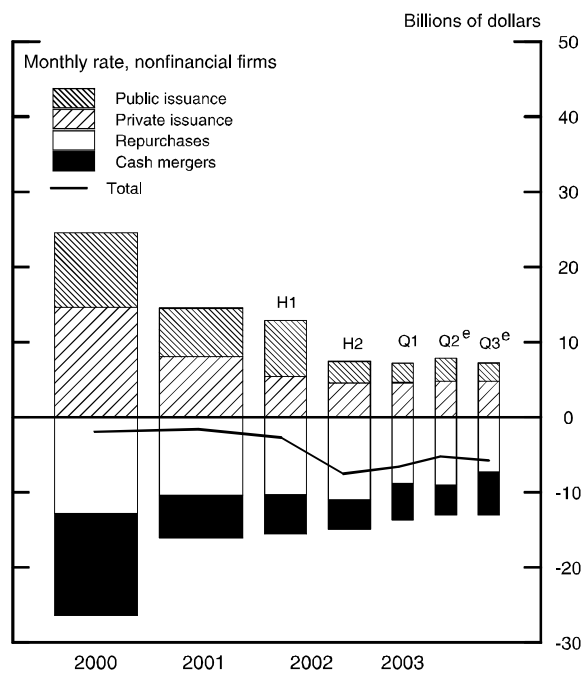
Note. Components may not sum to totals because of rounding. These data include bonds issued privately under Rule 144A. All other private placements are excluded. Total reflects gross proceeds rather than par value of original discount bonds.
1. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings.
2. Bonds sold in U.S. categorized according to Moody's bond ratings, or to Standard & Poor's if unrated by Moody's.
3. End-of-period basis, seasonally adjusted.
4. Excludes mortgage-backed and asset-backed bonds.
e Staff estimate.

Components of Net Debt Financing



* Seasonally adjusted.
e Staff estimate.

Components of Net Equity Issuance



e Staff estimate.

volume of funds raised in the second quarter appeared to have comfortably exceeded current spending needs.

Gross equity issuance was weak in August, but the recent significant rise in IPO filings suggests an increase in new offerings in the months ahead. In addition, although completions of cash-financed mergers have remained sluggish in recent months, announcements of new merger deals have steadily picked up. Announcements of new share repurchase programs slowed considerably in recent months, in part because of the elimination of preferential tax treatment for share buybacks. Even with the slower pace of repurchases, net equity issuance by nonfinancial firms is expected to remain negative this quarter.

Corporate Earnings and Credit Quality

Based on a full set of earnings reports, S&P 500 earnings increased 9 percent in the second quarter from a year earlier, handily beating analysts' expectations. NIPA economic profits before tax, a broader measure of profits, posted an even stronger increase. Analysts continue to expect a robust increase in S&P earnings growth in the second half of the year. In August, after several months of little net revision, they revised up their forecasts of S&P earnings for both 2003 and 2004—a bullish outlook given the usual pattern of downward adjustments.

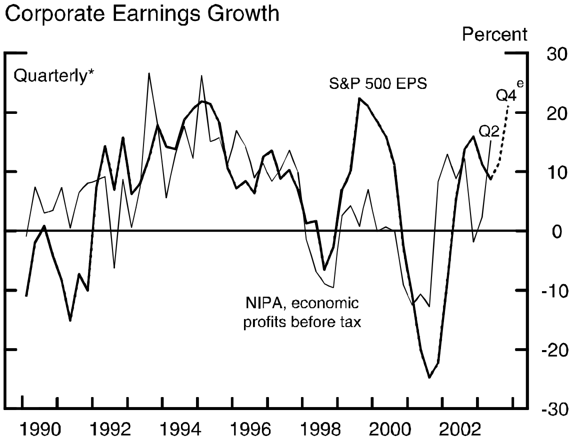
Measures of corporate credit quality have generally improved recently. The C&I loan delinquency rate declined further in the second quarter. The trailing six-month bond default rate was low in August and substantially below its peak at the end of last year. The recovery rate on defaulted bonds, however, continues to hover at the low levels of the past few years. The pace of bond downgrades in July and August was considerably less than in recent quarters, though upgrades remain sparse. In addition, the forecast of aggregate year-ahead default probability—based on the KMV model—fell in July, and rising equity prices and lower market volatility since then have likely pushed it down further.

Commercial Real Estate

Interest rates on high-grade CMBS have risen about in line with Treasury yields since the end of the second quarter, while those for lower-rated CMBS have increased by somewhat more. The limited data in hand indicate that higher interest rates likely have slowed the growth of commercial mortgage debt in the third quarter to about 7 percent at an annual rate. Spreads of AAA-rated CMBS yields over swap yields widened 12 basis points over the intermeeting period, while those on BBB-rated tranches widened 26 basis points. However, spreads remain relatively low, as is consistent with the still-subdued delinquency rates on commercial mortgages.

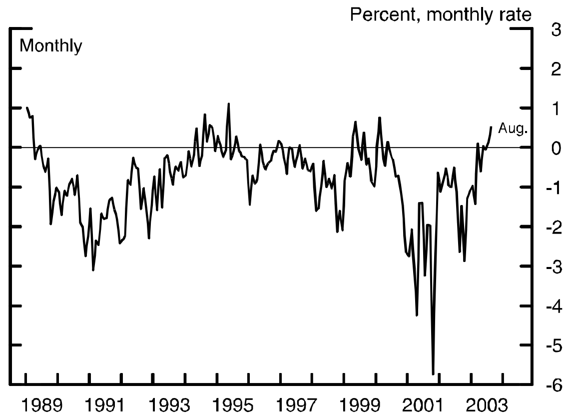
Corporate Credit Quality and Earnings

Corporate Earnings Growth



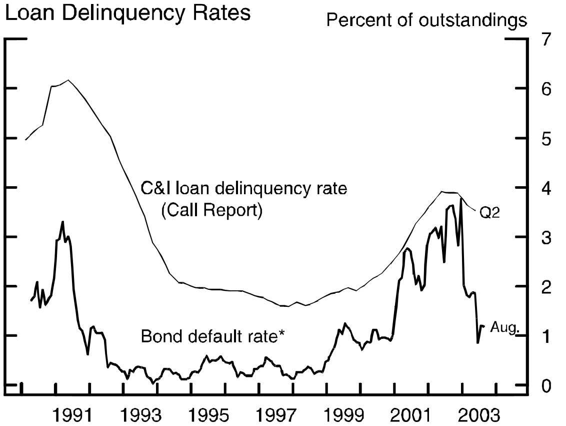
e Analysts' estimate as of August 29.
* Change from 4 quarters earlier.
Source. I/B/E/S for S&P 500 EPS.

S&P 500 EPS Revisions Index



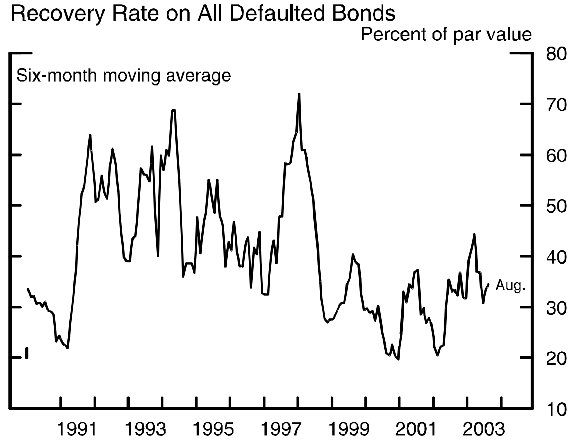
Note. Index is a weighted average of the percent change in the consensus forecasts of current-year and following-year EPS.

Bond Default and Loan Delinquency Rates



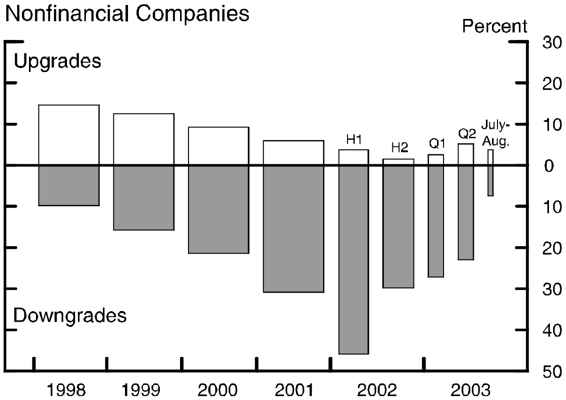
*6-month moving average, from Moody's Investors Service.

Recovery Rate on All Defaulted Bonds



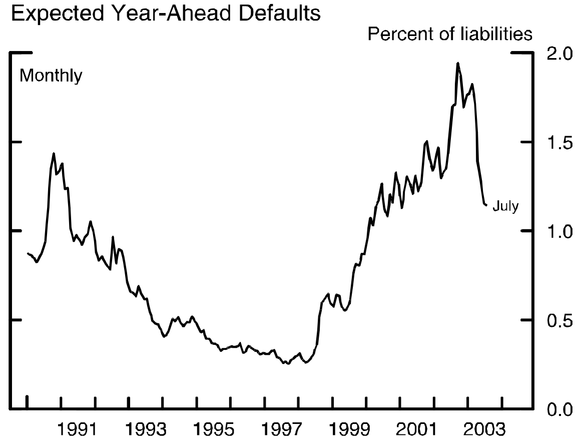
Note. Weighted-average market price at default.
Sources. Moody's Investors Service and Merrill Lynch.

Ratings Changes of Nonfinancial Companies



Note. Data are at an annual rate. Debt upgrades and downgrades as a percentage of par value of all bonds outstanding.
Source. Moody's Investors Service.

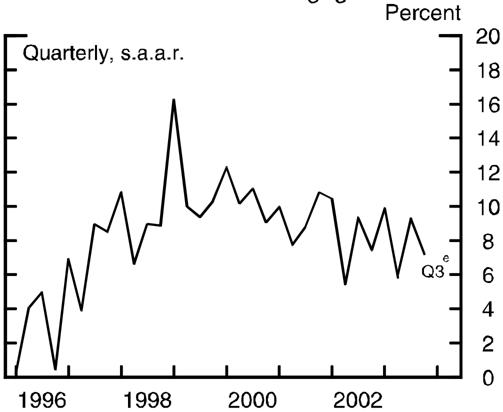
Expected Year-Ahead Defaults



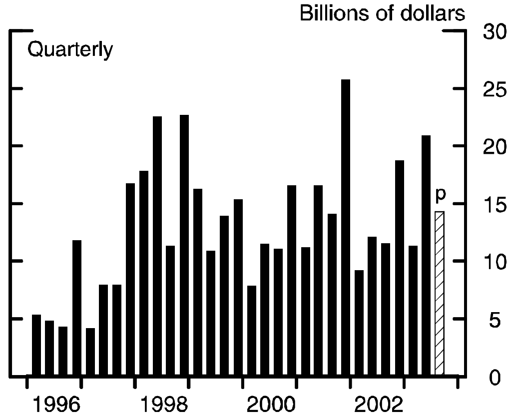
Note. Firm-level estimates of default weighted by firm liabilities as a percent of total liabilities.
Source. KMV Corporation.

Commercial Real Estate

Growth of Commercial Mortgage Debt

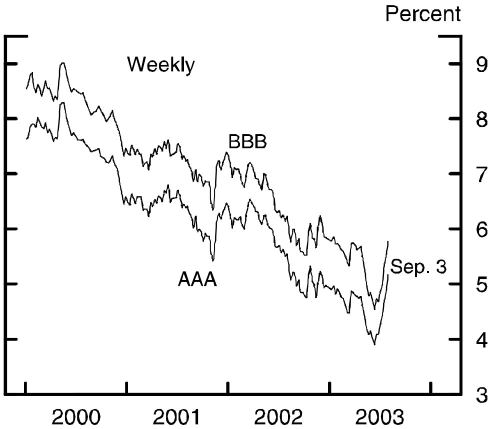


Gross Issuance of CMBS



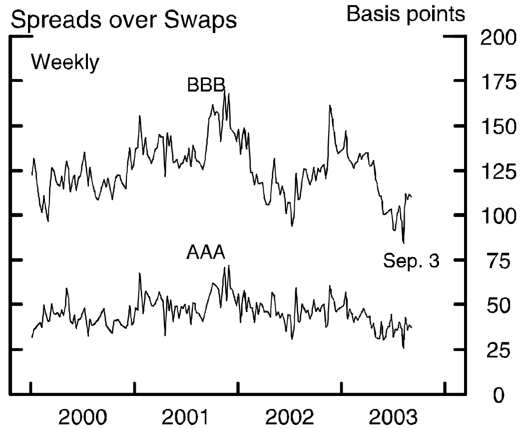
p Period to date at a quarterly rate.
Source. Commercial Mortgage Alert.

Investment-Grade CMBS Yields



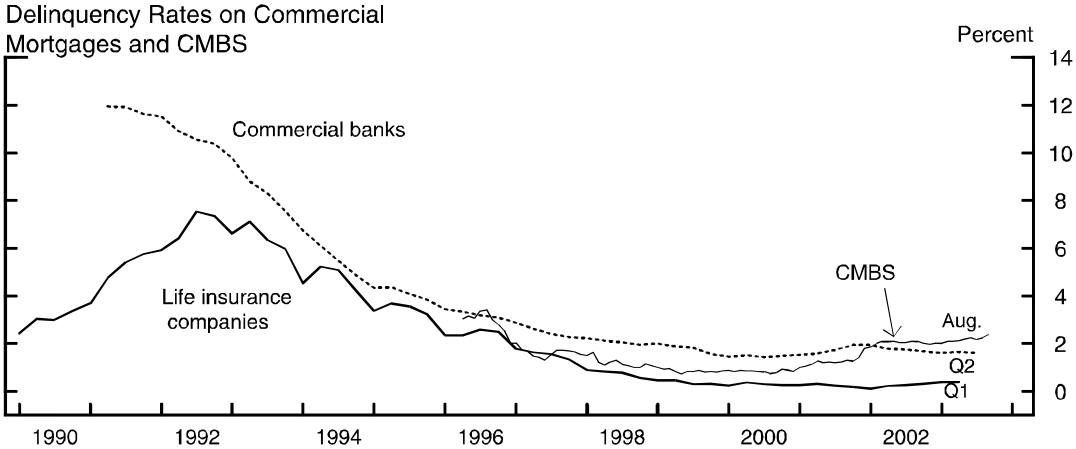
Source. Morgan Stanley.

Investment-Grade CMBS Spreads over Swaps



Source. Morgan Stanley.

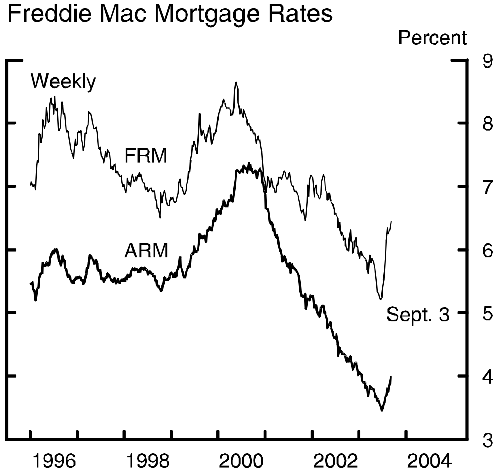
Delinquency Rates on Commercial Mortgages and CMBS



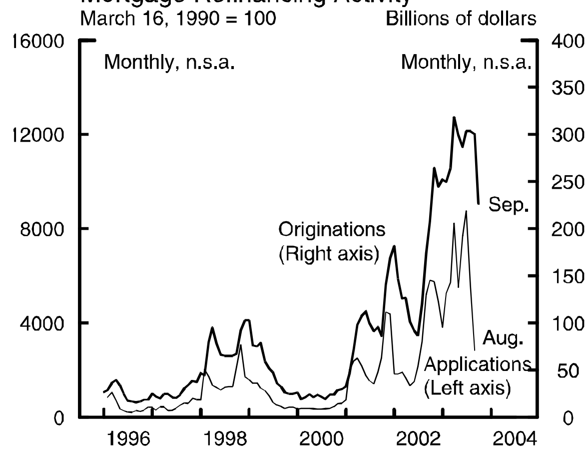
Source. Call Report, ACLI, Morgan Stanley.

Household Liabilities

Freddie Mac Mortgage Rates



Mortgage Refinancing Activity

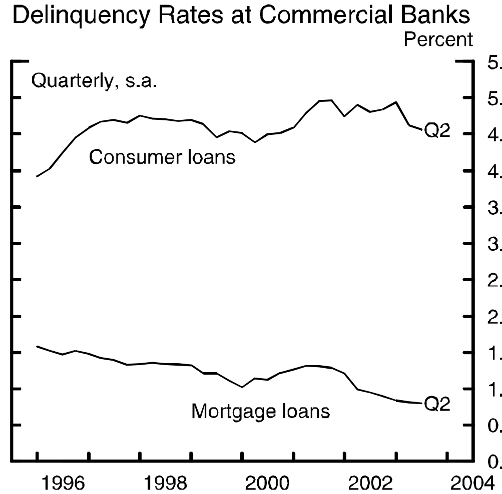


Source. Staff estimates.

Household Debt Growth

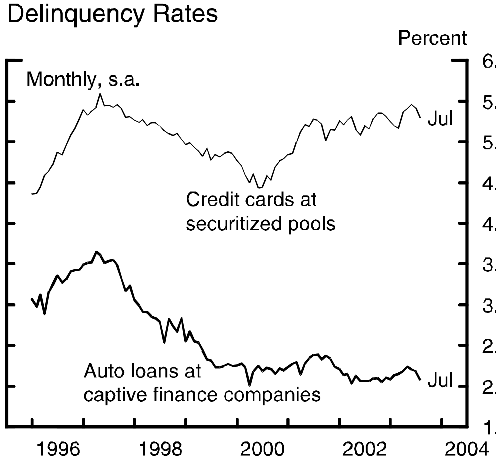
e Staff estimate.

Delinquency Rates at Commercial Banks



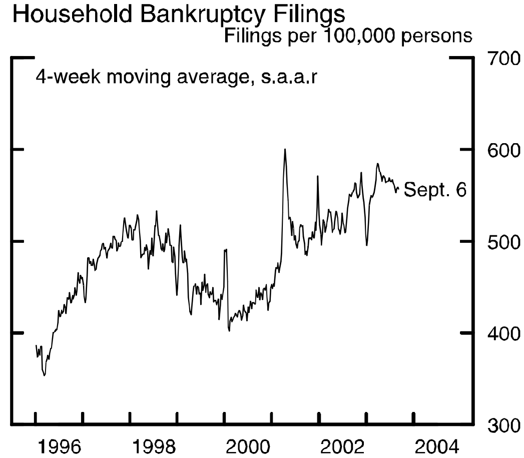
Source. Call Report.

Delinquency Rates



Source. Moody's, Federal Reserve.

Household Bankruptcy Filings



Source. Visa Bankruptcy Notification Service Statistics.

Household Finance
Interest rates on thirty-year fixed-rate mortgages remain more than 100 basis points above their mid-June lows. The rush of homeowners to complete mortgage refinancing in the face of rising rates kept originations high in August. However, the volume of refinancing applications has since fallen sharply, and purchase applications have weakened as well. These signs of softening point to a notable slowing of the growth of home mortgage debt this quarter from its rapid second-quarter pace of 14 percent at an annual rate.

Available data indicate that consumer credit has expanded moderately in the third quarter, similar to the pace earlier this year. The growth of consumer credit likely has been restrained as refinancing originations remained brisk through August and households continued to substitute mortgage debt for relatively high-cost consumer loans. In addition, some households may have paid down a portion of their consumer debt with the tax rebates they received this quarter.

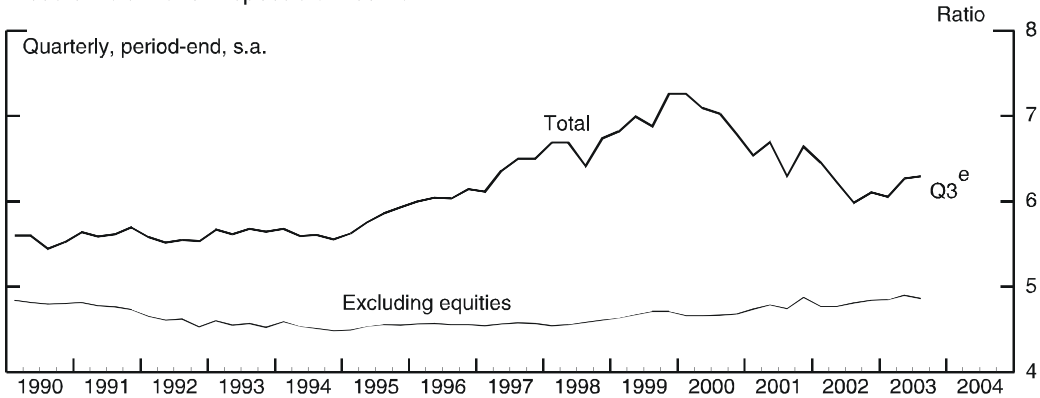
Household credit quality appears to have improved slightly on net in recent months. Delinquency rates on consumer loans and home mortgages at commercial banks fell a bit in the second quarter, and those on auto loans at the auto finance companies declined in July. While delinquency rates on credit cards in securitized pools and household bankruptcy filings have edged off in recent months, both remain high.

Given the large rise in equity prices so far this quarter, household net worth is on track to register a notable increase for the second consecutive quarter. Nonetheless, the boost to disposable income from this quarter's tax cuts will probably leave the ratio of net worth to disposable personal income about unchanged in the third quarter at a level just above its long-run average. In August, households continued to increase their holdings of domestic equity mutual funds, especially capital appreciation funds, which tend to hold shares of higher-risk companies. Meanwhile, they moved assets out of bond funds, which were experiencing capital losses as interest rates rose.

State and Local Government Finance
Gross municipal bond issuance—while down from the extraordinary pace in the second quarter—remained robust in August, boosted by an increase in short-term funding. The rise in longer-term rates in the summer appears to have damped new capital issuance, and issuance of advance refunding bonds slowed, owing in part to a dwindling pool of refundable bonds. Since the August FOMC meeting, municipal yields and muni-to-Treasury yield ratios are unchanged on net.

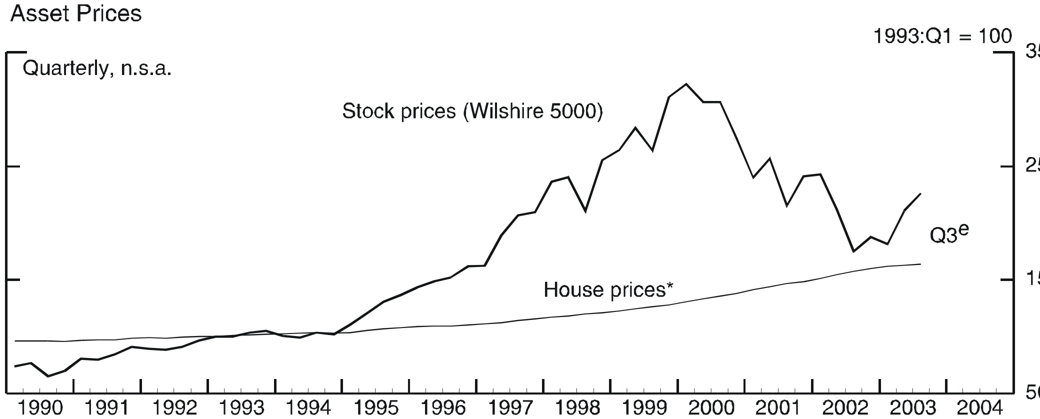
Household Assets

Assets Relative to Disposable Income



e Staff estimate.

Asset Prices



* Based on data through September 9.
* Source. Office of Federal Housing Enterprise Oversight (OFHEO).
e Staff estimate.

Net Flows into Long-Term Mutual Funds
(Billions of dollars, monthly rate)

	2001	2002	2003 H1	2003 July	2003 Aug. e	Assets July
Total long-term funds	**10.8**	**10.3**	**19.1**	**13.0**	**11.4**	**4,714**
Equity funds	**2.8**	**-2.2**	**5.8**	**18.0**	**23.6**	**3,126**
Domestic	4.6	-2.0	5.4	17.3	18.9	2,713
International	-1.8	-0.2	0.5	0.6	4.8	412
Hybrid funds	**0.7**	**0.7**	**2.0**	**3.3**	**-1.0**	**376**
Bond funds	**7.3**	**11.7**	**11.3**	**-8.3**	**-11.2**	**1,212**
High-yield	0.6	0.9	3.7	-0.7	0.2	136
Other taxable	5.7	9.5	7.1	-5.7	-9.0	747
Municipals	1.0	1.4	0.5	-1.9	-2.4	329

Note. Excludes reinvested dividends.
Source. Investment Company Institute.
e Staff estimates based on confidential ICI weekly data.

State and Local Government Finance

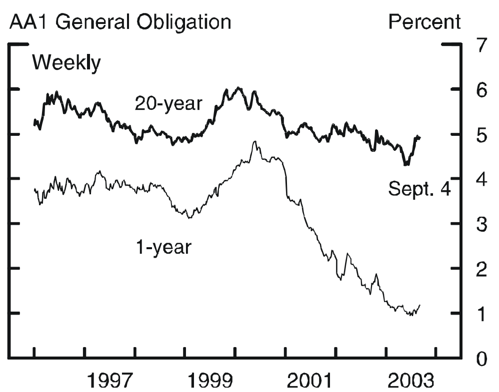
Gross Offerings of Municipal Securities

(Billions of dollars; monthly rate, not seasonally adjusted)

Type of security	2000	2001	2002	2003 Q1	2003 Q2	2003 July	2003 Aug.
Total	17.9	29.0	36.3	30.9	47.9	34.9	32.4
Long-term [1]	15.0	24.3	30.3	28.4	38.6	31.3	22.9
Refundings [2]	2.2	7.6	10.1	10.0	11.8	11.2	6.0
New capital	12.9	16.7	20.3	18.3	26.8	20.1	16.9
Short-term	2.8	4.7	6.0	2.6	9.3	3.5	9.5
Memo: Long-term taxable	0.7	1.4	1.7	1.8	5.9	1.8	0.7

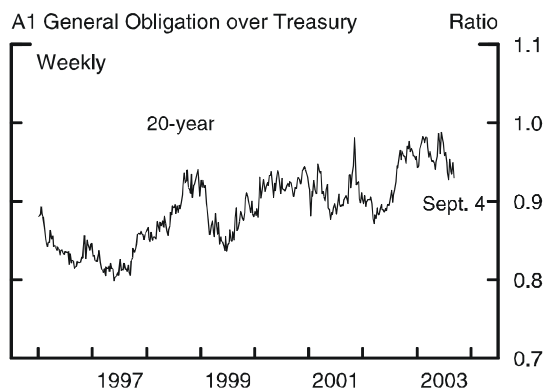
1. Includes issues for public and private purposes.
2. All issues that include any refunding bonds.

Municipal Bond Yields



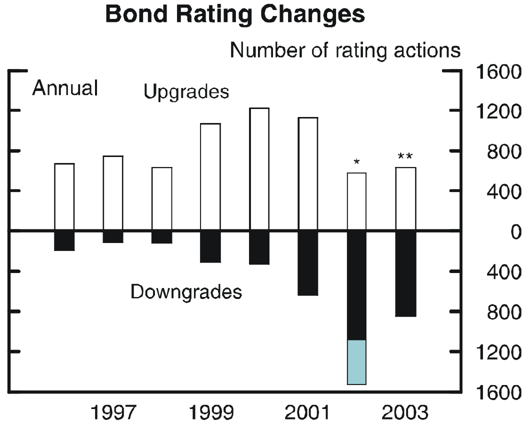
Source. Bloomberg.

Municipal Bond Ratios



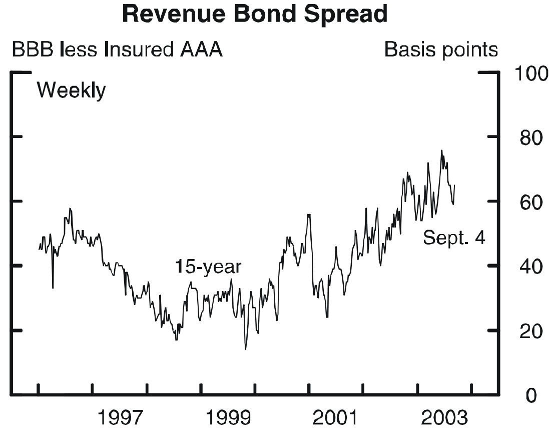
Source. Bond Buyer.

Bond Rating Changes



* Lightly shaded region shows a staff estimate of the number of downgrades related to downgrades of financial institutions that provided financial support for the bonds.
** Data through September 3 at an annual rate.
Source. S&P's Credit Week Municipal and Ratings Direct.

Revenue Bond Spread

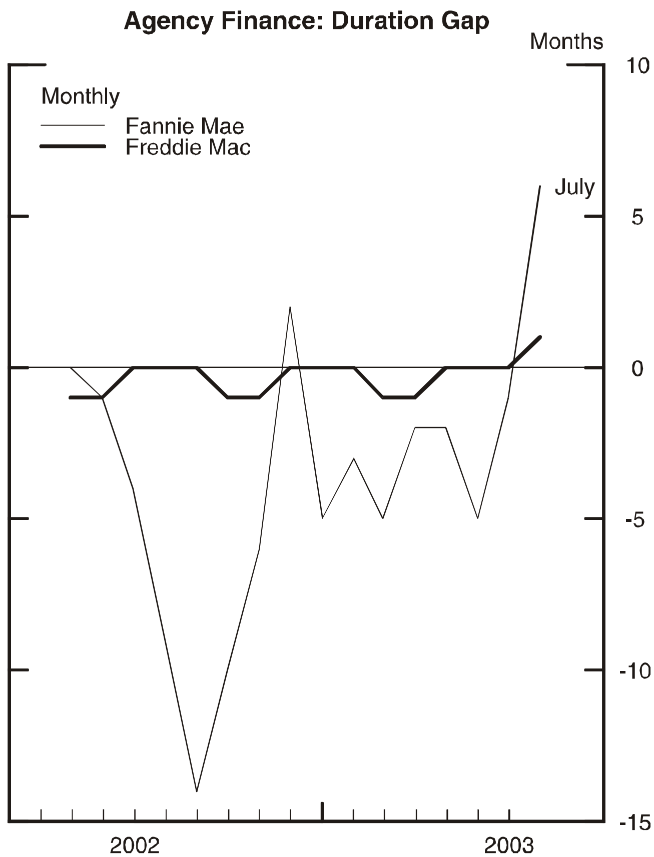


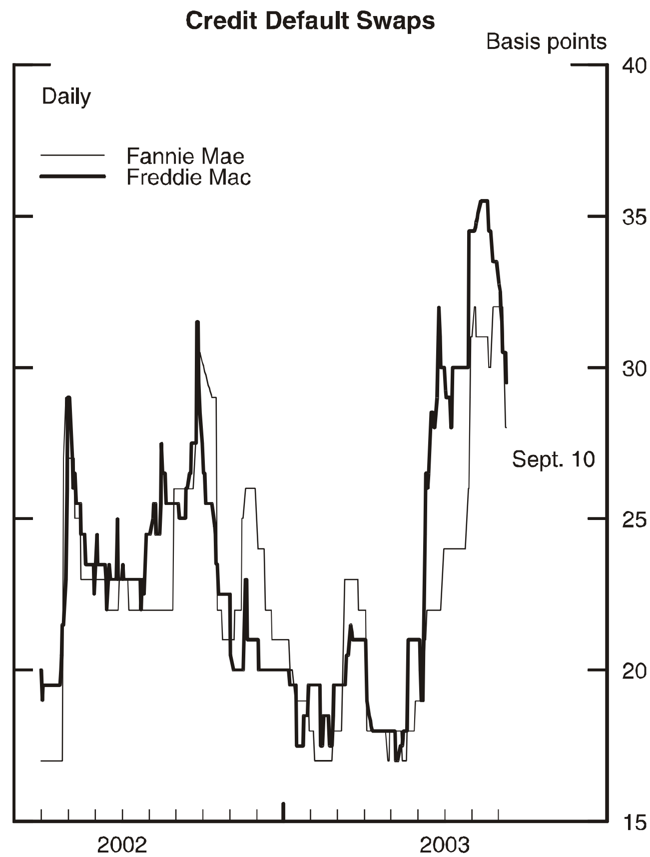
Source. Bloomberg.

Treasury Financing
(Billions of dollars)

Item	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 Jul.
Total surplus, deficit (−)	**-41.5**	**-107.8**	**-144.9**	**-16.6**	**-54.2**
Means of financing deficit					
Net borrowing	89.4	96.9	63.5	106.3	85.9
Nonmarketable	6.7	14.9	-50.5	45.9	52.4
Marketable	82.8	82.0	114.0	60.4	33.6
Bills	44.4	20.0	67.0	-27.2	8.6
Coupons[1]	38.4	62.0	47.0	87.6	25.0
Debt buybacks	0.0	0.0	0.0	0.0	0.0
Decrease in cash balance	-21.3	27.9	19.8	-16.8	-15.1
Other[2]	-26.7	-16.9	61.6	-73.0	-16.6
MEMO					
Cash balance, end of period	60.9	33.0	13.3	30.0	45.1

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.





The news about the credit quality of municipal issues has been mixed over the past several months. The number of municipal bond rating downgrades about matched the number of upgrades. However, some of the downgrades were large general-obligation issues from California and Illinois, so that the dollar volume of downgrades exceeded the dollar volume of upgrades by a wide margin. Spreads on general obligation bonds for these states had been rising as their fiscal conditions worsened, but they have not escalated recently, and spreads on revenue bonds were unchanged over the intermeeting period.

Treasury and Agency Finance
The Treasury is estimated to have continued its sizable net borrowing in August to finance the widening federal budget deficit. To address its current and prospective funding needs, the Treasury is returning to monthly issuance of five-year notes and, beginning this month, will regularly reopen ten-year notes issued at its mid-quarter refunding auctions.

Fannie Mae reported that the duration gap between its assets and liabilities over the month of July widened to an average of six months. Agency market participants have focused on Fannie Mae's duration gap as an indication of demand for hedging products, and the wider gap may have contributed to yield movements in the Treasury market around mid-summer and a widening in spreads on interest rate swaps. Continued management turmoil at Freddie Mac—most notably the recent removal of its CEO, which was demanded by the Office of Federal Housing Enterprise Oversight—has kept spreads on these GSE credit default swaps at or near their highest levels in more than a year. Market participants are awaiting testimony on the regulatory status of Fannie and Freddie by Treasury Secretary Snow, but reportedly most anticipate that only minor changes will be legislated.

Money and Bank Credit
M2 growth was boosted last month by another sizable increase in liquid deposits, owing to strong prepayments of mortgage-backed securities, which temporarily increased escrow accounts, and the August 14 power outage, which disrupted the disbursement of funds and left liquid deposits substantially elevated for a few days. Tax rebates distributed in late July and early August likely also contributed to M2 growth last month.

In July and August, bank lending remained fairly strong on net, bolstered by strong growth of real estate loans. In contrast, consumer loans were soft and C&I loans continued to contract. The run-off in business loans more likely reflects weak demand than tight supply. Indeed, preliminary results from the August Survey of Terms of Business Lending indicate that spreads on C&I loans at domestic banks have narrowed a bit this year but remain elevated.

Monetary Aggregates

(Based on seasonally adjusted data)

Aggregate or component	2002	2003 Q1	2003 Q2	2003 June	2003 July	2003 Aug. (p)	Level ($ billions) Aug. 03 (p)
Aggregate	Percent change (annual rate)[1]						
1. M2[2]	6.8	6.4	8.4	9.5	9.6	8.1	6,133
2. M3[3]	6.4	5.6	6.3	9.1	22.0	3.3	8,958
2a. Removing FIN 46 effects [4]					*10.7*	*3.3*	*8,875*
Components of M2 [5]							
3. Currency	8.2	7.6	6.0	1.3	-.6	5.4	649
4. Liquid deposits[6]	16.4	14.3	17.6	20.3	23.7	18.2	3,776
5. Small time deposits	-9.0	-6.9	-8.7	-11.7	-17.5	-17.0	831
6. Retail money market funds	-6.0	-10.0	-8.2	-7.9	-15.0	-9.0	869
Components of M3							
7. M3 minus M2[7]	5.5	3.9	1.8	8.2	49.5	-7.0	2,825
8. Large time deposits, net[8]	3.0	-2.6	1.5	-4.0	135.8	.0	896
8a. Removing FIN 46 effects [4]					*12.1*	*.0*	*813*
9. Institutional money market funds	2.2	-4.9	-14.7	20.3	42.1	-19.6	1,165
10. RPs	20.6	31.4	27.8	6.3	-57.9	-8.5	492
11. Eurodollars	7.0	19.2	32.0	-1.8	30.6	28.0	272
Memo							
12. Monetary base	7.2	7.6	5.9	3.4	.6	9.7	709
	Average monthly change (billions of dollars)[8]						
Selected managed liabilities at commercial banks							
13. Large time deposits, gross	1.8	1.5	-4.3	-5.2	84.2	-2.6	1,068
14. Net due to related foreign institutions	-3.2	6.8	-2.5	-20.1	16.3	-13.5	129
15. U.S. government deposits at commercial banks	-1.0	-4.2	.7	9.2	.4	-7.4	11

1. For the years shown, Q4 to Q4 percent change. For the quarters shown, based on quarterly averages.
2. Sum of currency, liquid deposits (demand, other checkable, savings), small time deposits, retail money market funds, and non-bank travelers checks.
3. Sum of M2, net large time deposits, institutional money market funds, RP liabilities of depository institutions, and eurodollars held by U.S. addressees.
4. Adjusted to remove estimated effects of consolidation related to FIN 46.
5. Non-bank travelers checks not listed.
6. Sum of demand deposits, other checkable deposits, and savings deposits.
7. Sum of large time deposits, institutional money market funds, RP liabilities of depository institutions, and eurodollars held by U.S. addressees.
8. Net of holdings of depository institutions, money market funds, U.S. government, and foreign banks and official institutions.
9. 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)

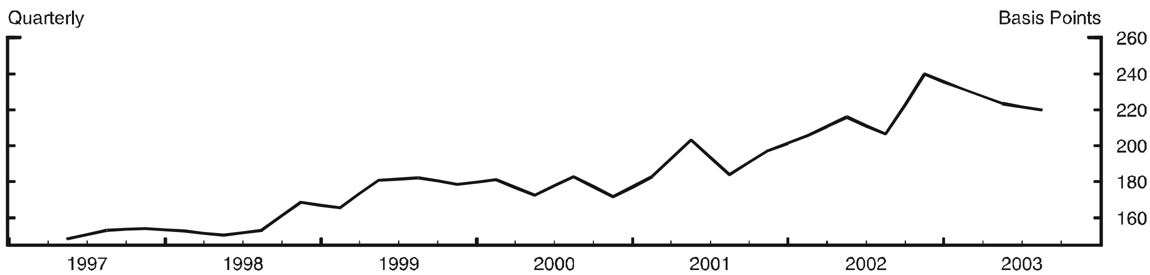
Type of credit	2002	Q1 2003	Q2[7] 2003	June[7] 2003	July 2003	Aug.[p] 2003	Level, Aug. 2003[p] ($ billions)
Total							
1. Adjusted[1]	**7.2**	**7.7**	**9.9**	**6.5**	**2.0**	**2.5**	**5,960**
2. Reported	7.3	8.2	11.0	10.8	7.6	-3.2	6,204
Securities							
3. Adjusted[1]	13.9	13.2	16.0	8.2	-10.3	-11.9	1,596
4. Reported	13.3	14.4	18.3	14.4	-29.9	-28.9	1,767
5. Treasury and agency	20.1	18.6	29.3	17.1	-38.4	-43.5	1,075
6. Other[2]	4.3	8.2	1.4	10.0	-15.8	-5.9	692
Loans[3]							
7. Total	5.0	5.6	8.0	9.3	23.8	7.4	4,437
7a. Removing FIN 46 effects[4]			*7.6*	*5.8*	*6.7*	*7.9*	
8. Business	-6.9	-5.1	-7.6	-16.6	4.4	-11.1	919
8a. Removing FIN 46 effects[4]			*-8.1*	*-20.7*	*-15.2*	*-10.7*	
9. Real estate	13.1	14.4	11.5	12.7	21.1	23.0	2,236
10. Home equity	36.6	28.1	28.1	32.2	20.1	21.7	253
11. Other	10.8	12.8	9.5	10.3	21.2	23.2	1,982
12. Consumer	5.5	2.7	-1.4	9.4	-0.2	1.8	593
13. Adjusted[5]	4.1	6.6	2.9	5.8	1.6	-3.9	957
14. Other[6]	1.6	-3.7	30.7	36.0	81.9	-12.2	689
14a. Removing FIN 46 effects[4]			*28.6*	*18.4*	*-3.9*	*-12.0*	

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. The conversion from a thrift to a commercial bank charter added approximately $37 billion to the assets and liabilities of domestically chartered commercial banks in the week ending May 8, 2002.

1. Adjusted to remove effects of mark-to-market accounting rules (FIN 39 and FIN 115), as well as the estimated effects of consolidation related to FIN 46.
2. Includes private mortgage-backed securities, securities of corporations, state and local governments, foreign governments, and any trading account assets that are not Treasury or agency securities, including revaluation gains on derivative contracts.
3. Excludes interbank loans.
4. Adjusted to remove estimated effects of consolidation related to FIN 46.
5. Includes an estimate of outstanding loans securitized by commercial banks.
6. Includes security loans and loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.
7. Banks implemented FIN 46 on July 1, but because of the staff's standard interpolation procedure for weekly bank credit series, this change also affected the levels and growth rates of bank credit and various components in June.

p Preliminary.

Weighted Average C&I Loan Rate Spreads at Domestic Banks*



* The spread over market interest rate on an instrument of comparable maturity.

International Developments

International Developments

U.S. International Transactions

Trade in Goods and Services

The U.S. international trade deficit in June was $39.5 billion, $2.0 billion smaller than in May (revised), as exports of goods and services increased and imports were unchanged. For the second quarter, the trade deficit was $491 billion at an annual rate, $4 billion larger than in the first quarter.

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

	2002	Annual rate 2002	Annual rate 2003		Monthly rate 2003		
		Q4	Q1	Q2	Apr.	May	June
Real NIPA[1]							
Net exports of G&S	-488.5	-532.2	-510.3	-543.6	...	...	...
Nominal BOP							
Net exports of G&S	-418.0	-464.5	-486.4	-490.7	-41.6	-41.5	-39.5
Goods, net	-482.9	-529.0	-544.1	-551.9	-46.4	-46.7	-45.0
Services, net	64.8	64.5	57.7	61.2	4.7	5.2	5.4

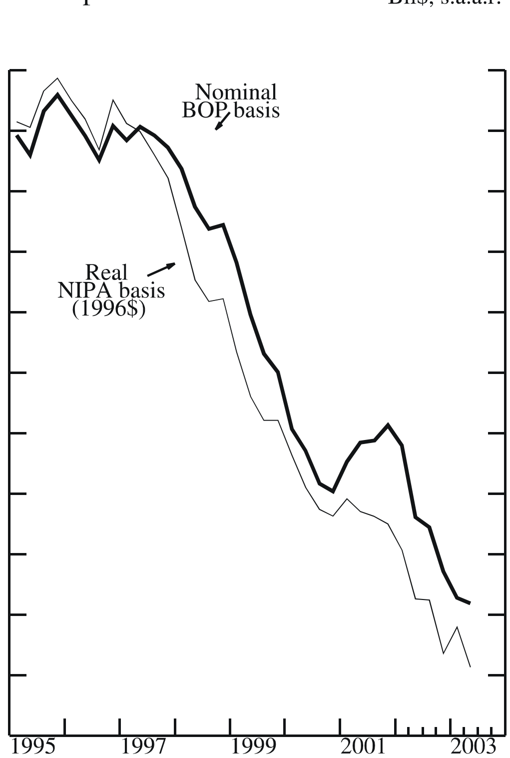
1. Billions of chained (1996) dollars.
Source: U.S. Department of Commerce, Bureaus of Economic Analysis and Census.
n.a. Not available. ... Not applicable.

The value of exports rose 2.4 percent in June, with increases in both goods and services. The moderate increase in exported goods was primarily in aircraft and consumer goods. Exports of services moved up strongly in June for the second consecutive month, largely from increasing receipts from international travel as worries related to terrorism, SARS, and the Iraq war appeared to wane. In the second quarter, the value of exported goods and services rose 1.1 percent at an annual rate. Exports of services were at about the same level in the second quarter as in the first quarter (the monthly trough occurred in April). Exports of goods rose slightly as increases in the value of semiconductors, consumer goods, and agricultural products were largely offset by declines in exported aircraft, computers, and industrial supplies.

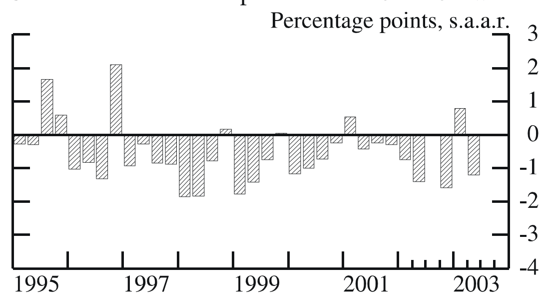
Imports of goods and services were at the same level in June as in May. Increases in the value of imported oil (mostly from higher prices), automotive products, and services (primarily from rising international travel) were offset by a sharp decline in the value of imported consumer goods and, to a lesser extent, industrial supplies. In the second quarter, imports of goods and services rose 1.9 percent at an annual rate. Despite rising monthly figures, imports of services were lower in the second quarter than in the first quarter. Increases in imports of

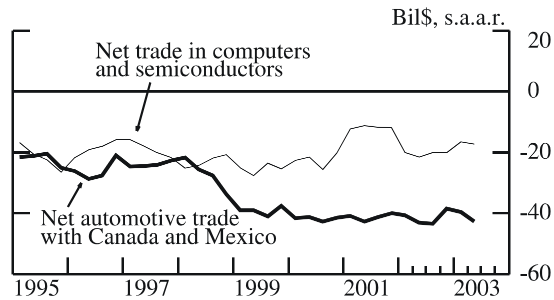
U.S. International Trade in Goods and Services

Net Exports

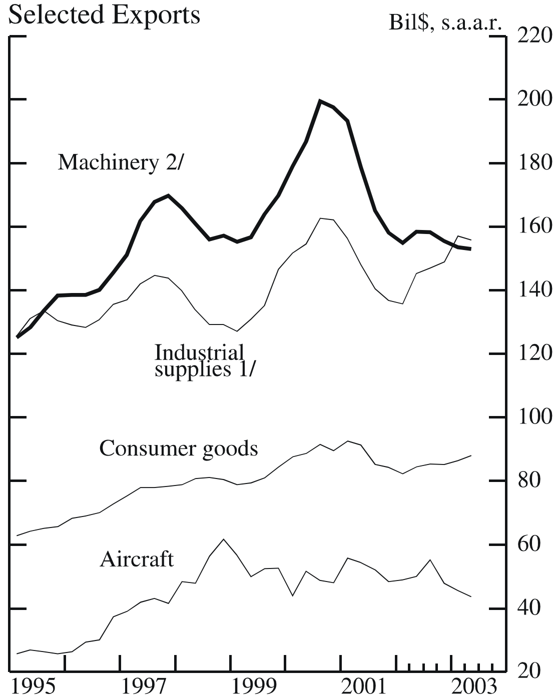


Contribution of Net Exports to Real GDP Growth



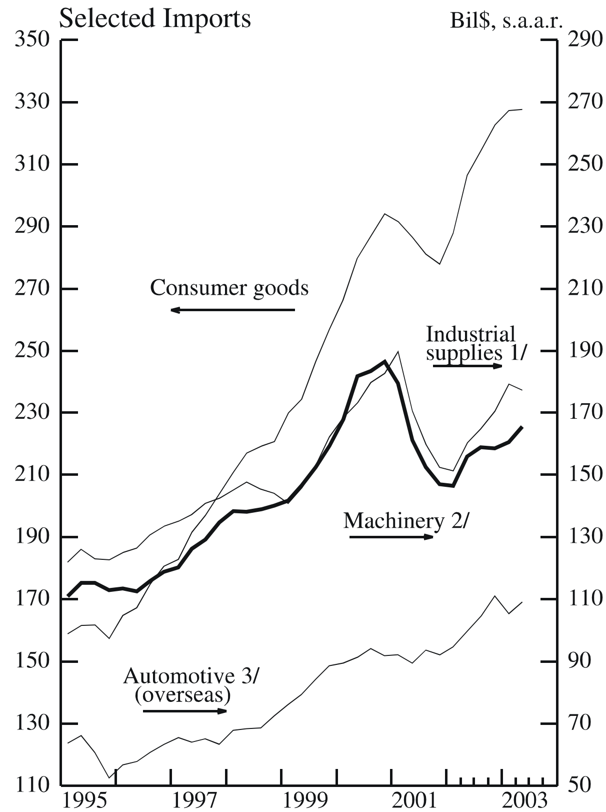


Selected Exports



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

Selected Imports



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]			
	2003		2003		2003		2003	
	Q1	Q2	May	June	Q1	Q2	May	June
Exports of G&S	**991.8**	**994.5**	**992.1**	**1015.5**	**7.2**	**2.7**	**16.2**	**23.3**
Goods exports	693.4	696.1	693.1	708.5	10.0	2.8	6.4	15.4
Gold	3.8	5.6	5.2	7.7	-0.1	1.8	1.4	2.5
Other goods	689.6	690.5	687.9	700.8	10.1	0.9	5.0	12.9
Aircraft & parts	45.6	43.7	41.6	46.8	-2.3	-1.9	-1.0	5.2
Computers & accessories	38.4	37.2	36.6	39.0	-0.5	-1.1	0.6	2.3
Semiconductors	42.8	45.3	45.5	45.4	2.4	2.4	0.6	-0.1
Other capital goods	156.2	155.7	156.0	158.4	-2.0	-0.5	3.3	2.4
Automotive	79.8	79.8	81.1	78.6	1.3	-0.1	1.4	-2.5
to Canada	46.7	45.2	46.8	44.4	1.7	-1.5	2.3	-2.4
to Mexico	13.1	14.4	15.0	14.2	-1.7	1.3	0.9	-0.7
to ROW	20.0	20.1	19.3	20.0	1.3	0.1	-1.8	0.7
Agricultural	56.9	57.5	56.5	58.8	2.0	0.6	-0.7	2.3
Ind supplies (ex. ag, gold)	157.1	155.9	155.9	155.1	8.2	-1.2	-0.8	-0.7
Consumer goods	86.5	88.0	86.1	91.9	1.3	1.5	0.1	5.8
All other goods	26.3	27.5	28.6	26.8	-0.3	1.2	0.8	-1.8
Services exports	298.4	298.4	299.0	306.9	-2.9	-0.0	9.8	8.0
Imports of G&S	**1478.1**	**1485.2**	**1489.9**	**1490.0**	**29.1**	**7.1**	**14.2**	**0.1**
Goods imports	1237.5	1248.1	1253.0	1248.1	25.1	10.6	9.9	-4.9
Petroleum	135.9	130.3	123.4	132.2	18.4	-5.6	-11.9	8.8
Gold	2.4	4.1	3.6	5.8	-0.6	1.7	0.7	2.2
Other goods	1099.1	1113.6	1126.0	1110.1	7.3	14.5	21.1	-15.9
Aircraft & parts	23.5	23.8	24.1	24.3	-2.8	0.3	1.0	0.2
Computers & accessories	73.2	75.2	75.7	74.9	-1.3	2.0	0.9	-0.8
Semiconductors	24.5	24.6	24.8	24.5	-0.3	0.1	0.2	-0.2
Other capital goods	162.5	168.1	169.1	169.0	2.4	5.6	2.7	-0.1
Automotive	204.6	211.6	213.5	218.7	-4.8	7.0	11.0	5.3
from Canada	59.2	59.6	59.6	62.1	1.8	0.4	2.6	2.5
from Mexico	40.1	42.8	44.1	43.2	-0.7	2.7	2.9	-0.9
from ROW	105.3	109.2	109.8	113.5	-5.9	4.0	5.5	3.7
Ind supplies (ex. oil, gold)	179.3	177.2	181.3	175.1	9.0	-2.1	5.9	-6.1
Consumer goods	327.3	327.6	332.5	318.0	4.7	0.2	0.3	-14.6
Foods, feeds, bev.	54.3	55.0	55.3	53.6	2.4	0.7	-0.7	-1.7
All other goods	49.9	50.5	49.7	51.9	-1.9	0.6	-0.2	2.3
Services imports	240.7	237.2	236.9	241.9	3.9	-3.5	4.3	5.0
Memo:								
Oil quantity (mb/d)	12.11	13.47	13.36	13.56	-0.38	1.36	-0.15	0.21
Oil import price ($/bbl)	30.74	26.46	25.30	26.69	4.98	-4.28	-2.14	1.39

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

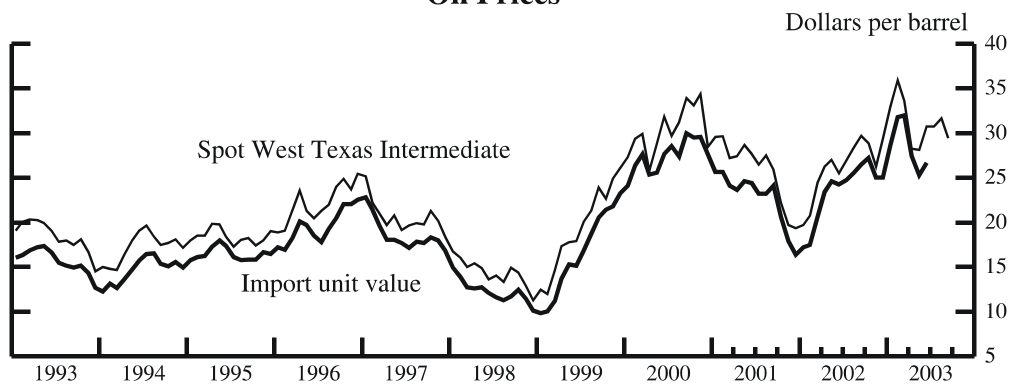
Prices of U.S. Imports and Exports

(Percentage change from previous period)

	Annual rates			Monthly rates		
	2002	2003		2003		
	Q4	Q1	Q2	May	June	July
	------------- BLS prices (2000 weights)-------------					
Merchandise imports	0.7	13.5	-9.4	-0.7	0.7	0.5
Oil	3.8	133.7	-55.3	-5.0	4.2	3.7
Non-oil	0.4	3.9	-1.0	-0.2	0.4	0.1
Core goods*	1.5	5.3	-0.4	-0.1	0.5	0.2
Cap. goods ex comp & semi	-0.8	2.1	1.5	0.0	0.5	0.1
Automotive products	1.2	-0.4	0.8	0.1	0.2	0.0
Consumer goods	-0.7	-0.3	0.3	0.0	0.3	-0.1
Foods, feeds, beverages	9.3	7.1	-0.3	-1.0	-0.4	0.9
Industrial supplies ex oil	5.8	25.3	-5.0	-0.6	1.7	0.6
Computers	-9.3	-5.7	-7.0	-0.9	-0.8	-1.1
Semiconductors	-4.6	-4.0	-2.3	-1.4	0.0	0.7
Merchandise exports	0.7	2.7	0.9	0.1	-0.2	-0.1
Core goods*	1.3	3.6	1.4	0.1	0.2	-0.1
Cap. goods ex comp & semi	0.5	0.9	0.1	0.0	0.2	0.0
Automotive products	1.3	0.7	0.1	-0.1	0.1	0.0
Consumer goods	0.4	-0.1	0.5	0.1	0.2	0.0
Agricultural products	8.2	0.2	5.9	2.5	-0.6	0.0
Industrial supples ex ag	1.5	12.4	3.4	-0.7	0.7	-0.3
Computers	-5.8	3.1	0.0	0.0	-0.3	0.0
Semiconductors	-2.8	-5.8	-5.9	-0.2	-4.4	0.0
Chain price index	---Prices in the NIPA accounts (1996 weights)---					
Imports of goods & services	0.9	11.7	-3.9	...	...	...
Non-oil merchandise	0.7	4.6	-0.8	...	...	...
Core goods*	1.5	5.5	-0.2	...	...	...
Exports of goods & services	0.9	3.9	0.8	...	...	...
Total merchandise	0.9	3.4	1.6	...	...	...
Core goods*	1.7	4.6	2.1	...	...	...

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

Oil Prices



goods were concentrated in capital equipment and automotive products. Declines were recorded in the quarterly value of imported oil (a drop in price outweighed an increase in quantity) and other industrial supplies. The value of imported consumer goods was about the same in the second quarter as in the first quarter, a notable change from the strong quarterly increases recorded for the past year.

Prices of Internationally Traded Goods

Non-oil imports. In July, the prices of U.S. imports of non-oil goods and of core goods increased 0.1 and 0.2 percent, respectively. Within core goods, the largest price changes were in industrial supplies and foods, feeds and beverages. After falling for the past three months, prices of foods, feeds and beverages rose 0.9 percent, driven by the prices for meat and fish. Higher prices for building materials and finished metals contributed to the 0.6 percent increase in the price of industrial supplies. In all other trade categories within core goods, prices were little changed. The prices of U.S. imports of computers continued to decline in July, but semiconductor prices rose.

Oil. The BLS price of imported oil rose 3.7 percent in July, following a revised 4.2 percent increase in June. The spot price of West Texas Intermediate (WTI) crude oil, however, was practically unchanged in July relative to June, averaging $30.76 per barrel. In August, the spot price edged up, averaging $31.59 per barrel, but has moved down somewhat in September, closing at $29.18 per barrel on September 8. The recent fall in the spot price may partly reflect the end of the summer driving season and the lack of significant supply disruptions from tropical storms. However, prices remain elevated owing to the slow return of Iraqi exports and low global oil inventories.

Exports. In July, the prices of U.S. exports of total goods and of core goods both fell 0.1 percent. Within core goods, industrial supplies was the only category that saw a price change, declining 0.3 percent. The largest decline was in the price of chemicals. The fall in prices of industrial supplies was the third decline seen over the past four months. The prices of U.S. exports of computers and semiconductors were unchanged in July.

U.S. International Financial Transactions

Foreign official inflows (line 1 of the Summary of U.S. International Transactions table) amounted to nearly $10 billion in July, a slowdown from the record pace recorded in the second quarter, but comparable to the average monthly inflows recorded over the last year-and-a-half. Inflows in July were particularly strong for Norway and China, and, to a lesser extent, Japan. For the first seven months of the year, foreign official inflows have amounted to $104 billion, exceeding the $94 billion inflow recorded for all of 2002. In August, data on official holdings at the Federal Reserve Bank of New York indicate a further increase of about $17 billion, primarily reflecting increases for China, Korea, and Japan.

Private inflows into U.S. securities (line 4) remained very strong at $50 billion in July, although down a bit from the record average monthly pace recorded in the second quarter. To date this year, private purchases of U.S. securities have amounted to $235 billion, putting these inflows on pace with the record inflows recorded for 2001 and 2002. Private foreign purchases of Treasury securities recorded their strongest month in seven years, and purchases of corporate bonds continued at the very strong pace of recent months. In contrast, purchases of agency debt were subdued in July following modest net sales in June, and private foreigners made small net sales of U.S. corporate equities compared with net purchases in recent months.

U.S. investors acquired $3 billion in foreign securities in July (line 5), as continued purchases of foreign equities were only partially offset by smaller sales of foreign bonds. While most transactions in foreign securities are recorded against major financial centers, over $9 billion of the roughly $12 billion in net purchases of foreign equities in June and July has been recorded against Japan.

Net capital flows through the banking sector (line 3) amounted to an inflow of $49 billion in July, primarily reflecting flows through affiliated foreign offices. These inter-bank funding flows tend to be volatile on a monthly basis; the inflow in July reversed a sizable net outflow in June.

Summary of U.S. International Transactions

(Billions of dollars, not seasonally adjusted except as noted)

	2001	2002	2002 Q3	2002 Q4	2003 Q1	2003 Q2	2003 June	2003 July
Official financial flows	**-.5**	**89.8**	**7.5**	**28.2**	**38.5**	**57.2**	**7.7**	**9.8**
1. Change in foreign official assets in the U.S. (increase, +)	4.4	93.5	8.9	29.0	38.5	57.3	8.1	9.8
a. G-10 countries	-8.4	30.7	1.8	6.0	27.0	27.8	4.7	6.1
b. OPEC countries	-3.1	-7.5	-1.4	.7	-7.5	1.1	.7	-.3
c. All other countries	15.9	70.3	8.4	22.4	19.0	28.4	2.6	4.0
2. Change in U.S. official reserve assets (decrease, +)	-4.9	-3.7	-1.4	-.8	.1	-.2	-.3	.0
Private financial flows	**416.1**	**438.2**	**163.7**	**124.4**	**74.2**	**n.a.**	**...**	**...**
Banks								
3. Change in net foreign positions of banking offices in the U.S.[1]	-6.2	99.0	65.7	52.6	-14.9	14.3	-22.2	49.3
Securities[2]								
4. Foreign net purchases of U.S. securities (+)	398.1	398.1	104.9	81.4	70.9	164.4	53.6	50.2
a. Treasury securities	-7.4	101.8	57.9	13.6	14.7	61.5	26.6	31.5
b. Agency bonds	81.8	78.0	21.8	15.4	-2.1	14.3	-4.1	1.9
c. Corporate and municipal bonds	201.8	160.3	17.2	39.9	60.4	67.4	20.9	24.6
d. Corporate stocks[3]	121.8	58.1	8.0	12.6	-2.1	21.2	10.2	-7.9
5. U.S. net acquisitions (-) of foreign securities	-85.1	15.3	21.4	-5.5	-27.3	3.2	4.6	-3.2
a. Bonds	24.6	33.5	8.8	7.5	7.3	20.8	10.9	2.1
b. Stock purchases	-62.7	-14.9	14.0	-13.0	-19.9	-17.1	-6.3	-5.3
c. Stock swaps[3]	-47.0	-3.2	-1.4	.0	-14.7	-.5	.0	.0
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-120.0	-137.8	-31.6	-31.7	-29.0	n.a.	...	...
7. Foreign direct investment in U.S.	151.6	39.6	14.2	15.3	25.8	n.a.	...	...
8. Foreign holdings of U.S. currency	23.8	21.5	2.6	7.2	4.9	n.a.	...	...
9. Other (inflow, +)[4]	53.9	2.4	-13.4	5.0	43.7	n.a.	...	...
U.S. current account balance (s.a.)	**-393.7**	**-480.9**	**-122.7**	**-128.6**	**-136.1**	**n.a.**	**...**	**...**
Capital account balance (s.a.)[5]	**-1.1**	**-1.3**	**-.4**	**-.4**	**-.3**	**n.a.**	**...**	**...**
Statistical discrepancy (s.a.)	**-20.8**	**-45.8**	**-48.1**	**-23.6**	**23.7**	**n.a.**	**...**	**...**

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

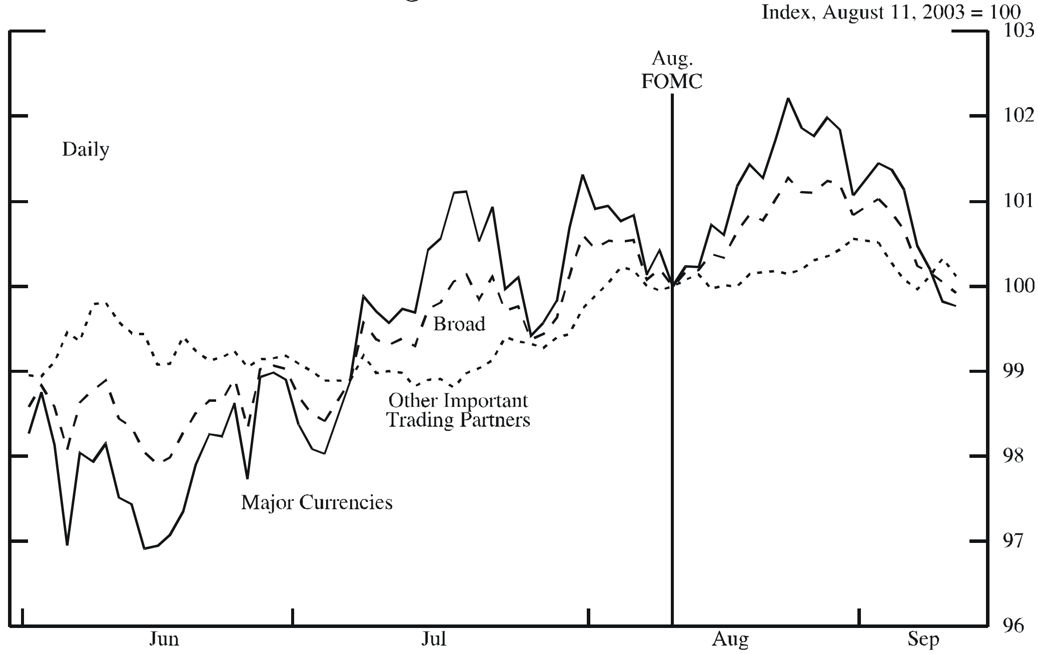
5. Consists of transactions in nonproduced nonfinancial assets and capital transfers.

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

Foreign Financial Markets

On balance, the broad nominal value of the dollar is little changed on a trade-weighted basis since the August FOMC meeting. Through the first three weeks of the intermeeting period, the dollar appreciated against most major foreign currencies, with the notable exception of the yen, amid growing optimism that U.S. economic growth would outpace that in most foreign industrial economies. These gains were reversed later in the period, however, in part following the much weaker-than-expected August U.S. labor market report. The dollar is also little changed, on balance, against the currencies of our other important trading partners.

Exchange Value of the Dollar



On net, the dollar appreciated 1¼ and 2 percent against the euro and Swiss franc, respectively, over the period. Euro-area economic data released during the period, while showing some signs of improvement, were viewed by market participants as somewhat less positive for growth than data released in the United States. News that French, German, and Italian GDP contracted in the second quarter contributed to this view, as it contrasted with the upward revision to U.S. second-quarter growth. Indeed, news of rising German consumer and business confidence, as well as improvements in the euro-zone manufacturing and services purchasing managers' indexes, elicited little net movement in foreign exchange rates, as the significance of these forward-looking indicators was weighed against more tangible evidence of current strength in the U.S. economy.

Financial Indicators in Major Industrial Countries

Country	Three-month rate Sep. 10 (Percent)	Three-month rate Percentage Point Change	Ten-year yield Sep. 10 (Percent)	Ten-year yield Percentage Point Change	Equities Percent Change
Canada	2.70	-.22	4.80	-.08	3.57
Japan	.08	.00	1.55	.66	12.43
Euro area	2.15	.02	4.27	.21	4.27
United Kingdom	3.59	.19	4.67	.26	2.29
Switzerland	.19	.00	2.76	.28	6.10
Australia	4.89	.04	5.51	-.01	2.67
United States	1.08	.01	4.36	-.02	3.95
Memo: Weighted-average foreign	1.81	-.05	4.11	.25	n.a.

NOTE. Change is from August 11 to September 10 (10 a.m. EDT).
n.a. Not available.

Meeting market expectations, the European Central Bank and Bank of England left their respective interest rate targets unchanged in decisions on September 4. While short-term interest rates in the United States and the euro area were little changed on balance—anchored by expectations that policymakers will leave rates unchanged in the near term—short-term rates in the United Kingdom increased about 20 basis points on net. A pickup in manufacturing and mortgage lending in the United Kingdom contributed to the upward shift in the expected path of short-term sterling rates. The dollar appreciated somewhat less against sterling, gaining about 1 percent on balance.

The dollar depreciated 1½ percent against the yen on net amid reportedly rising investor enthusiasm about Japanese growth prospects. Positive investor sentiment increased markedly early in the period, following news of stronger-than-expected growth in Q2 Japanese GDP, and was subsequently further supported by stronger-than-expected data on Japanese business activity and industrial production. The yen appreciated further in late August following a Ministry of Finance report which showed that the Japanese monetary authorities had not intervened in currency markets during the previous four weeks. Repeated large-scale intervention sales of yen for dollars by the Japanese monetary authorities late in the period were aimed at curbing the yen's appreciation.

Recent declines in inflation pressures and economic growth in Canada prompted markets to correctly anticipate a 25-basis-point rate cut by the Bank of Canada at its meeting on September 3. In the days following the policy announcement, the Canadian dollar appreciated as market participants noted that the accompanying statement was optimistic about future economic growth. On net, the dollar ended the period 1½ percent weaker against the Canadian dollar.
Optimism about global economic recovery reportedly prompted further equity price gains during the period. Net gains were the largest in Japan, where the Topix index rose over 12 percent. Gains in U.K. equity prices were somewhat less than those in U.S. markets, while euro-area share prices rose about 4 percent. Analysts noted that the recent retreat of the euro from multi-year highs attained earlier in the summer has helped support profit expectations for European export firms.

Benchmark government bond yields generally also rose in most foreign industrial economies, with Japan again registering the largest increases. On balance the yield on the benchmark Japanese government bond rose about 70 basis points, while European yields rose 20 to 30 basis points. European bond markets were substantially less volatile than U.S. markets over the intermeeting period, as they have been in recent months

The price of gold rose 6 percent on balance, briefly touching a seven-year high late in the intermeeting period. Prices of silver, platinum, and other precious metals also rose to multi-year highs. Market participants attributed these increases, in some part, to reports of heightened demand for gold from jewelry processors in East and South Asia.

The Mexican peso depreciated about 2½ percent against the dollar on balance over the intermeeting period. Receding inflation pressures have reportedly prompted expectations that the central bank of Mexico may loosen its monetary policy stance in the near term.

The Brazilian *real* appreciated 2¼ percent against the dollar over the period, while Brazilian share prices gained about 15 percent and Brazil's EMBI+ spread over comparable Treasury yields fell 130 basis points. Investors reportedly remain optimistic about Brazil's long-term prospects despite evidence of unexpected short-term weakness in the Brazilian economy. Contributing to the optimistic tone in markets, the central bank of Brazil lowered its policy rate 250 basis points on August 20, a bit more than markets had expected.

Financial Indicators in Latin America, Asia, and Russia

	Currency/ US dollar		Short-term Interest rates[1]		Dollar-denominated bond spread[2]		Equity prices
Economy	Sep. 10	Percent Change	Sep.9/10 (Percent)	Percentage Point Change	Sep.9/10 (Percent)	Percentage Point Change	Percent Change
Mexico	10.97	2.37	4.12	.22	2.08	-.12	5.11
Brazil	2.93	-2.30	20.30	-3.05	6.76	-1.31	14.75
Argentina	2.94	.69	n.a.	n.a.	48.24	-2.20	1.72
Chile	683.20	-2.69	3.04	.00	3.79	.03	3.92
China	8.28	.00	n.a.	n.a.	2.54	.08	-3.48
Korea	1170.00	-.85	4.06	-.04	...	...	8.92
Taiwan	34.00	-.99	1.18	.04	...	...	7.84
Singapore	1.75	-.28	.75	.00	...	...	1.33
Hong Kong	7.80	-.01	1.06	-.06	...	...	7.10
Malaysia	3.80	-.01	3.00	.00	2.79	.27	1.29
Thailand	40.37	-3.44	1.25	.00	.51	-.54	9.23
Indonesia	8420.00	-1.35	8.97	-.35	2.12	-.47	13.47
Philippines	54.85	.07	6.75	.56	3.91	-.08	4.40
Russia	30.63	.96	n.a.	n.a.	2.60	-.44	11.23

NOTE. Change is from August 11 to September 9/10.

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.

Investors in emerging Asian equity markets shared in the global market optimism, supported by evidence of increasing orders for electronics exports as well as the pickup in the U.S. economy. Share price gains in economies with a technology focus were pronounced, with markets in Hong Kong, Korea, and Taiwan up almost 10 percent.

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

Developments in Foreign Industrial Countries

Second-quarter national accounts show a mixed performance of real GDP growth for the major foreign industrial countries. GDP grew strongly in Japan, and growth picked up in the U.K. Canadian GDP contracted as the rate of inventory accumulation fell sharply, while euro-area GDP edged down, partly owing to disruptive strikes in Germany and France. With the exception of Japan, net exports made a negative contribution in all major foreign industrial countries. Limited data from the third quarter and some survey data indicate a firming of economic activity.

Twelve-month consumer-price inflation rates increased marginally in the latest data, on average, in response to higher energy prices and slight currency depreciations. Euro-area inflation moved back above 2 percent in August. Canadian inflation dropped sharply in July, while in the United Kingdom retail price inflation picked up slightly to nearly 3 percent. In Japan, deflation eased.

In **Japan**, real GDP rose a stronger-than-expected 3.9 percent (s.a.a.r.) during the second quarter, according to revised data. Business fixed investment provided the most support, expanding an eye-popping 20 percent. Private consumption advanced about 1½ percent. Net exports added almost 1 percentage point to growth, reflecting a rise in exports of roughly 3 percent and a fall in imports of about 6 percent. Service imports declined sharply as a result of a SARS-induced drop in foreign travel. Inventory decumulation created a drag on growth, subtracting slightly over ½ percentage point. Residential investment declined about 1¼ percent, and public investment also contracted.

Indicators for the third quarter suggest that economic activity continues to expand. Industrial production rose 0.5 percent in July from the previous month. Core machinery orders, a leading indicator of business fixed investment, were up about 0.5 percent in July from the second-quarter average. Real exports rose roughly 2 percent in July from the second-quarter average, boosted by strong demand from China, while imports jumped 6 percent. However, indicators point to a weak start to the third quarter for private consumption, with household expenditures dropping 3 percent in July from the second-quarter average. Household spending in July was reportedly depressed by an increase in the social security tax rate applied to summer bonuses and by unseasonably cool weather. New car registrations slipped in August.

Japanese Real GDP
(Percent change from previous period, except as noted, s.a.a.r.)

Component	2001[1]	2002[1]	2002		2003	
			Q3	Q4	Q1	Q2
GDP	-2.4	2.5	3.3	2.3	2.4	3.9
Total domestic demand	-1.8	1.5	4.3	.9	2.5	3.0
Consumption	1.4	1.4	2.7	.1	1.4	1.6
Private investment	-10.5	2.7	6.3	11.5	7.9	16.3
Public investment	-1.1	-5.9	-10.7	-9.6	-12.2	-7.2
Government consumption	2.3	1.4	3.1	.0	1.5	-.2
Inventories[2]	-.6	.3	1.7	-.7	.6	-.6
Exports	-11.0	17.7	.4	18.3	2.4	3.1
Imports	-7.1	8.8	10.9	5.8	2.6	-6.2
Net exports[2]	-.6	1.1	-.9	1.5	.0	.9

1. Q4/Q4.
2. Percentage point contribution to GDP growth, s.a.a.r.

Data suggest continued improvement in labor market conditions and an easing in deflation. In July, the unemployment rate held steady at 5.3 percent, down from a peak rate of 5.5 percent recorded early this year, and the job-offers-to-applicants ratio, a leading indicator of employment, rose slightly. Core consumer goods prices in the Tokyo area (which exclude fresh food but include energy) rose slightly in August from the previous month, but were down 0.3 percent from a year earlier. Wholesale prices for domestic goods fell 0.6 percent in August from a year earlier. The GDP deflator fell 2.5 percent in the second quarter from a year earlier.

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

Indicator	2002	2003					
	Q4	Q1	Q2	May	Jun.	Jul.	Aug.
Industrial production[1]	.4	.4	-.6	2.6	-1.2	.5	n.a.
All-industries index	-.3	.7	.1	.2	.9	n.a.	n.a.
Housing starts	1.7	.7	4.3	.6	8.7	-8.6	n.a.
Machinery orders[2]	-.1	5.8	3.4	6.5	2.4	-3.1	n.a.
Machinery shipments[3]	2.3	.2	1.5	3.6	-.9	-1.3	n.a.
New car registrations	1.0	1.4	-6.3	11.4	-6.1	.7	-.9
Unemployment rate[4]	5.4	5.4	5.4	5.4	5.3	5.3	n.a.
Job offers ratio[5]	.57	.6	.61	.61	.61	.62	n.a.
Business sentiment[6]	-28	-26	-26	...	...	...	...
CPI (Core, Tokyo area)[7]	-.7	-.7	-.4	-.4	-.4	-.4	-.3
Wholesale prices[7]	-1.4	-.9	-1	-1.1	-1.1	-.7	-.6

1. Mining and manufacturing.
2. Private sector, excluding ships and electric power.
3. Excluding ships and railway vehicles.
4. Percent.
5. Level of indicator.
6. Tankan survey, diffusion index.
7. Percent change from year earlier, n.s.a.

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

Euro-area real GDP fell 0.3 percent (s.a.a.r.) in the second quarter, the ninth straight quarter in which euro-area GDP growth has been below the 2-2½ percent estimated growth rate of potential GDP. Exports and investment both fell. Private consumption managed to grow slightly. Government expenditure contributed 0.6 percent to GDP growth. Growth in the second quarter was hampered by strikes in Germany and France. A large negative contribution from net exports combined with weak investment and consumption led GDP to fall in Germany, France, Italy, and the Netherlands.

Euro-Area Real GDP[1]
(Percent change from previous period, except as noted, s.a.a.r.)

Component	2001[2]	2002[2]	2002 Q3	2002 Q4	2003 Q1	2003 Q2
GDP	.8	1.1	.9	.2	.1	-.3
Total domestic demand	.1	.8	.8	1.3	2.1	.4
Consumption	1.4	.7	1.2	1.2	1.9	.3
Investment	-1.9	-1.8	.5	1.0	-4.7	-1.6
Government consumption	2.6	2.1	2.1	0.8	1.1	2.9
Inventories[3]	-.8	.3	-.5	.2	1.7	.0
Exports	-2.1	3.7	6.0	-1.7	-4.6	-1.8
Imports	-3.9	3.0	6.1	0.9	.3	.1
Net exports[3]	.6	.3	.1	-1.0	-1.9	-.7
Memo (GDP):						
France	.7	1.4	1.1	-.5	.7	-1.3
Germany	.5	.5	.6	-.2	-1	-.2
Italy	.7	.9	.6	1.5	-.5	-.4

1. Includes Greece as of 2001 Q1.
2. Q4/Q4.
3. Percentage point contribution to GDP growth, s.a.a.r.

While more direct indicators of economic activity are not available, survey measures of economic sentiment in the euro area improved markedly in recent months. The German IFO index of business sentiment rose for the fourth straight month in August, a strong indicator of the turning point for German manufacturing. The Belgian National Bank Survey (a leading indicator for production of intermediate goods) also increased in both July and August. Euro-area PMI for manufacturing rose further to 49.1 in August, ever closer to the 50 mark which is the benchmark for expansion. Country measures of consumer confidence also showed stability or improvement in August.

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

Indicator	2002 Q4	2003 Q1	2003 Q2	2003 May	2003 Jun.	2003 Jul.	2003 Aug.
Industrial production[1]	-.1	.0	-.8	-.9	-.1	n.a.	n.a.
Retail sales volume[2]	-.5	.7	.1	-.7	.0	n.a.	n.a.
Unemployment rate[3]	8.6	8.7	8.8	8.8	8.9	8.9	n.a.
Consumer confidence[4]	-14.0	-19.3	-19.3	-20.0	-19.0	-18.0	n.a.
Industrial confidence[4]	-10.0	-11.3	-12.7	-13.0	-13.0	-15.0	n.a.
Mfg. orders, Germany	.4	.3	-1.9	-2.6	2.1	-.3	n.a.
CPI[5]	2.3	2.3	2.0	1.9	2.0	1.9	2.1
Producer prices[5]	1.3	2.4	1.5	1.3	1.4	1.3	n.a.
M3[5]	6.9	8.0	8.4	8.5	8.4	8.5	n.a.

1. Excludes construction.
2. Excludes motor vehicles.
3. Percent. Euro area standardized to ILO definition. Includes Eurostat estimates in some cases.
4. Diffusion index based on European Commission surveys in individual countries.
5. Eurostat harmonized definition. Percent change from year earlier.
n.a. Not available.

Euro-area twelve-month consumer price inflation moved back above the ECB’s 2 percent ceiling in August, according to the flash estimate. Excluding energy and unprocessed food, however, inflation continued to fall to1.8 percent in July. Labor market conditions remain weak, with the unemployment rate stuck at a 3½ year high of 8.9 percent in July.

In the **United Kingdom**, second-quarter real GDP rose modestly, following a weak first quarter. Growth was supported by a bounce-back in consumption from a lackluster rate in the first quarter, and continued strength in government spending. These bright spots were offset by continued declines in investment and a sizable negative contribution from net exports, as exports plunged while imports rose. Inventories made a positive contribution to growth.

U.K. Real GDP
(Percent change from previous period, except as noted, s.a.a.r.)

Component	2001[1]	2002[1]	2002 Q3	2002 Q4	2003 Q1	2003 Q2
GDP	1.9	2.3	3.7	2.0	.4	1.4
Total domestic demand	2.3	3.8	4.4	7.6	-1.2	5.4
Consumption	4.3	3.4	3.2	4.1	.9	5.3
Investment	-5.0	1.4	-.7	1.3	-4.3	-1.9
Government consumption	4.6	1.6	1.2	3.6	10.4	4.5
Inventories[2]	-.4	1.0	2.3	4.2	-3.0	1.6
Exports	-4.6	-.7	-2.4	-14.7	8.9	-11.2
Imports	-2.5	3.7	.5	1.6	2.7	1.8
Net exports[2]	-.6	-1.7	-1.1	-5.9	-1.7	-4.6

1. Q4/Q4.
2. Percentage point contribution to GDP growth, s.a.a.r.

Indicators for the third quarter suggest continued recovery. The manufacturing sector is showing signs of firming, as output growth picked up in the sector in July, even as industrial production growth slowed because of a fall in electricity production. August's manufacturing PMI trended up, continuing to indicate expansion. Business confidence ticked up again in August. After surging in June, retail sales fell back slightly in July. Both of the leading surveys of retail sales cooled a little in August and consumer confidence has remained flat since rising in April. The services PMI rose again in August to its highest level since January 2001.

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

Indicator	2002	2003					
	Q4	Q1	Q2	May	Jun.	Jul.	Aug.
Industrial production	-.9	-.3	.2	-.1	.6	.3	n.a.
Retail sales volume[1]	1.6	.0	1.5	-.4	2.0	-.4	n.a.
Unemployment rate[2]							
Claims-based	3.1	3.1	3.1	3.1	3.1	3.1	n.a.
Labor force survey[3]	5.1	5.1	n.a.	5.0	n.a.	n.a.	n.a.
Business confidence[4]	3.0	-1.3	-6.3	-3.0	-6.0	-4.0	-3.0
Consumer confidence[5]	-3.0	-10.0	-6.7	-6.0	-6.0	-6.0	n.a.
Retail prices[6]	2.6	2.9	2.9	2.9	2.8	2.9	n.a.
Producer input prices[7]	1.4	4.9	1.2	1.4	1.4	2.2	2.9
Average earnings[7]	3.7	3.4	3.1	3.3	3.2	n.a.	n.a.

1. Excludes motor vehicles.
2. Percent
3. Three-month average centered on month shown.
4. Percentage of firms expecting output to increase in the next four months less percentage expecting output to decrease.
5. Average of the percentage balance from consumers' expectations of their financial situation, general economic situation, unemployment, and savings over the next 12 months.
6. Excluding mortgage interest payments. Percent change from year earlier.
7. Percent change from year earlier.
... Not applicable. n.a. Not available.

House price inflation is slowing, but only moderately. Prices rose around 17 percent in the twelve months ending in August, according to Nationwide, Britain's largest building society. Net mortgage lending continued to climb in July while consumer credit slowed. Mortgage equity withdrawals rose to 7.3 percent of net income in the first quarter.

The labor market continues to be tight as both the official claims-based and the labor force survey measures of the unemployment rate remain near record lows. Employment growth rose 0.8 percent in the twelve months ending in May. The twelve-month rate of retail price inflation (excluding mortgage interest payments) ticked up in July and remained above the Bank of England's 2½ percent target. The harmonized index of consumer prices (HICP) rose 1.3 percent in the twelve months ending in July.

In **Canada**, real GDP decreased 0.3 percent (s.a.a.r.) in the second quarter, after growing 2.6 percent in the first quarter. The outbreak of SARS in April, the discovery of mad cow disease in May, and the recent appreciation of the Canadian dollar all contributed to the fall in economic activity. Final domestic demand remained strong, advancing 2.9 percent, as consumption grew robustly despite SARS-related weakness in the travel, tourism, and accommodation sectors. Investment growth was supported by the continued strength of residential construction. GDP growth was depressed by a decrease in the rate of inventory accumulation and strong import growth.

Canadian Real GDP
(Percent change from previous period, except as noted, s.a.a.r.)

Component	2001[1]	2002[1]	2002		2003	
			Q3	Q4	Q1	Q2
GDP	1.4	3.5	2.7	1.6	2.6	-.3
Total domestic demand	.8	5.7	1.5	4.5	7.8	.1
Consumption	2.3	3.8	1.3	4.4	4.4	2.7
Investment	3.4	2.0	3.2	.1	6.6	2.7
Government consumption	3.5	2.8	4.2	2.4	2.4	3.6
Inventories[2]	-1.9	2.3	-.7	1.4	3.2	-2.6
Exports	-5.4	.7	8.5	-8.7	-6.7	2.2
Imports	-8.4	6.5	5.8	-1.4	3.8	5.6
Net exports[2]	.8	-2.0	1.3	-3.2	-4.2	-1.1

1. Q4/Q4.
2. Percentage point contribution to GDP growth, s.a.a.r.

Indicators for the third quarter have been mixed. Employment declined slightly in both July and August after increasing in the second quarter. The recent blackout in Ontario led to a record decline in hours worked in August, but is not thought to be responsible for the month's fall in employment. However, residential construction remained strong, with housing starts in August reaching their second-highest level since Canada's recent housing boom began in early 2002.

In July, the twelve-month rate of headline CPI inflation declined to 2.2 percent. The twelve-month rate of inflation has declined rapidly in recent months, largely on account of lower energy prices and the fading of a number of special factors, including an increase in tobacco taxes and a rapid rise in auto insurance premiums. Twelve-month core inflation, excluding food, energy prices, and indirect taxes, also continued to move down in July.

On September 3, the Bank of Canada cut its key policy rate, the overnight rate, 25 basis points to 2.75 percent, citing the rapid decline in core inflation and a number of recent adverse shocks to economic activity. The cut, in conjunction with another 25-basis-point reduction on July 15, brings the policy rate back to its beginning of year level.

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

Indicator	2002	2003					
	Q4	Q1	Q2	May	Jun.	Jul.	Aug.
GDP by industry	.4	.6	.0	.2	.1	n.a.	n.a.
Industrial production	-.3	.1	-1.8	-.4	-.8	n.a.	n.a.
New mfg. orders	-2.5	1.5	-5.1	-2.7	2.0	n.a.	n.a.
Retail sales	.8	-1.8	-.2	.5	.3	n.a.	n.a.
Employment	.8	.5	.1	-.1	.3	-.1	-.1
Unemployment rate[1]	7.5	7.4	7.7	7.8	7.7	7.8	8.0
Consumer prices[2]	3.8	4.5	2.8	2.9	2.6	2.2	n.a.
Core Consumer Prices[2,3]	3.0	3.2	2.4	2.5	2.0	1.7	n.a.
Consumer attitudes[4]	122.1	114.5	115.1	...	...	...	...
Business confidence[4]	136	131.4	109.9	...	...	...	...

1. Percent.
2. Percent change from year earlier, n.s.a.
3. Excluding food, energy, and indirect taxes.
4. Level of index, 1991 = 100.
n.a. Not available. ... Not applicable.

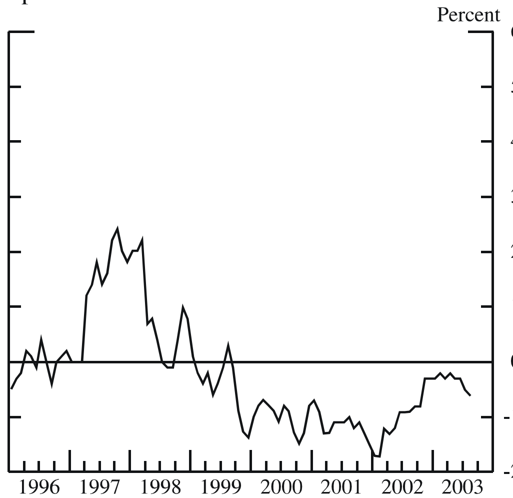
External Balances
(Billions of U.S. dollars, s.a.a.r.)

Country and balance	2002	2003				
	Q4	Q1	Q2	May	Jun.	Jul.
Japan						
Trade	84.9	73.3	77.2	77.5	73.8	75.9
Current account	102.2	117.3	131.3	159.6	113.4	149.4
Euro area						
Trade[1]	104.7	28.9	60.8	62.1	76.3	n.a.
Current account[1]	89.9	12.0	-20.6	5.5	44.8	n.a.
Germany						
Trade	127.9	125.8	136.6	148.2	136.3	n.a.
Current account[1]	87.0	41.9	40.1	42.8	38.2	n.a.
France						
Trade	1.1	.6	.3	.8	-.2	n.a.
Current account	4.6	3.7	1.1	5.4	2.0	n.a.
Italy						
Trade	5.2	1.3	n.a.	-4.0	n.a.	n.a.
Current account[1]	-15.8	-30.2	-35.7	-29.2	-44.4	n.a.
United Kingdom						
Trade	-83.9	-69.1	-71.1	-78.2	-89.0	-63.7
Current Account	-11.0	15.6	n.a.	...	...	...
Canada						
Trade	34.7	38.8	33.1	34.2	31.6	n.a.
Current Account	12.4	18.3	14.5	...	...	...

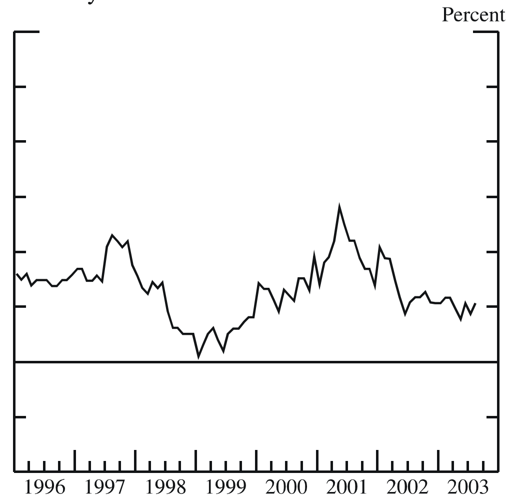
1. Not seasonally adjusted.
n.a. Not available. ... Not applicable.

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

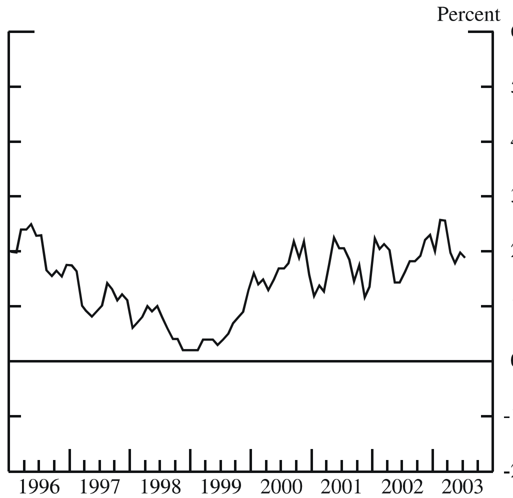
Japan



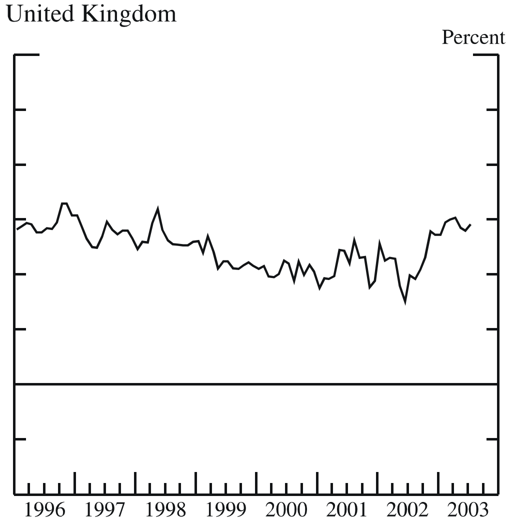
Germany



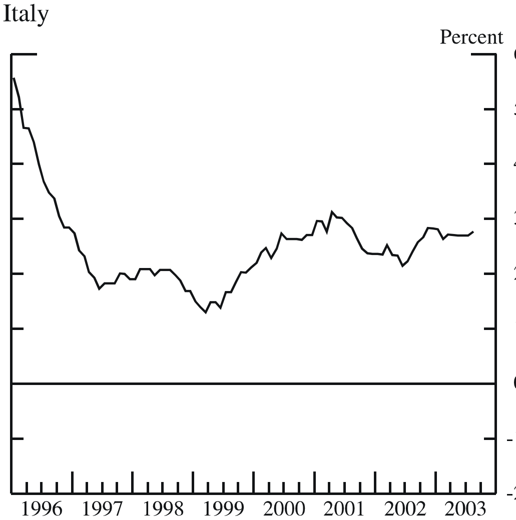
France



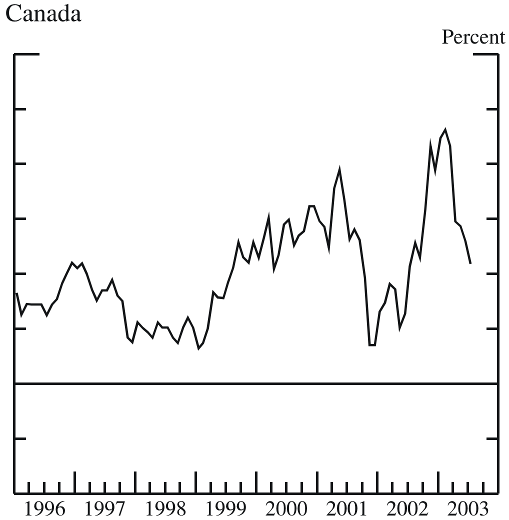
United Kingdom



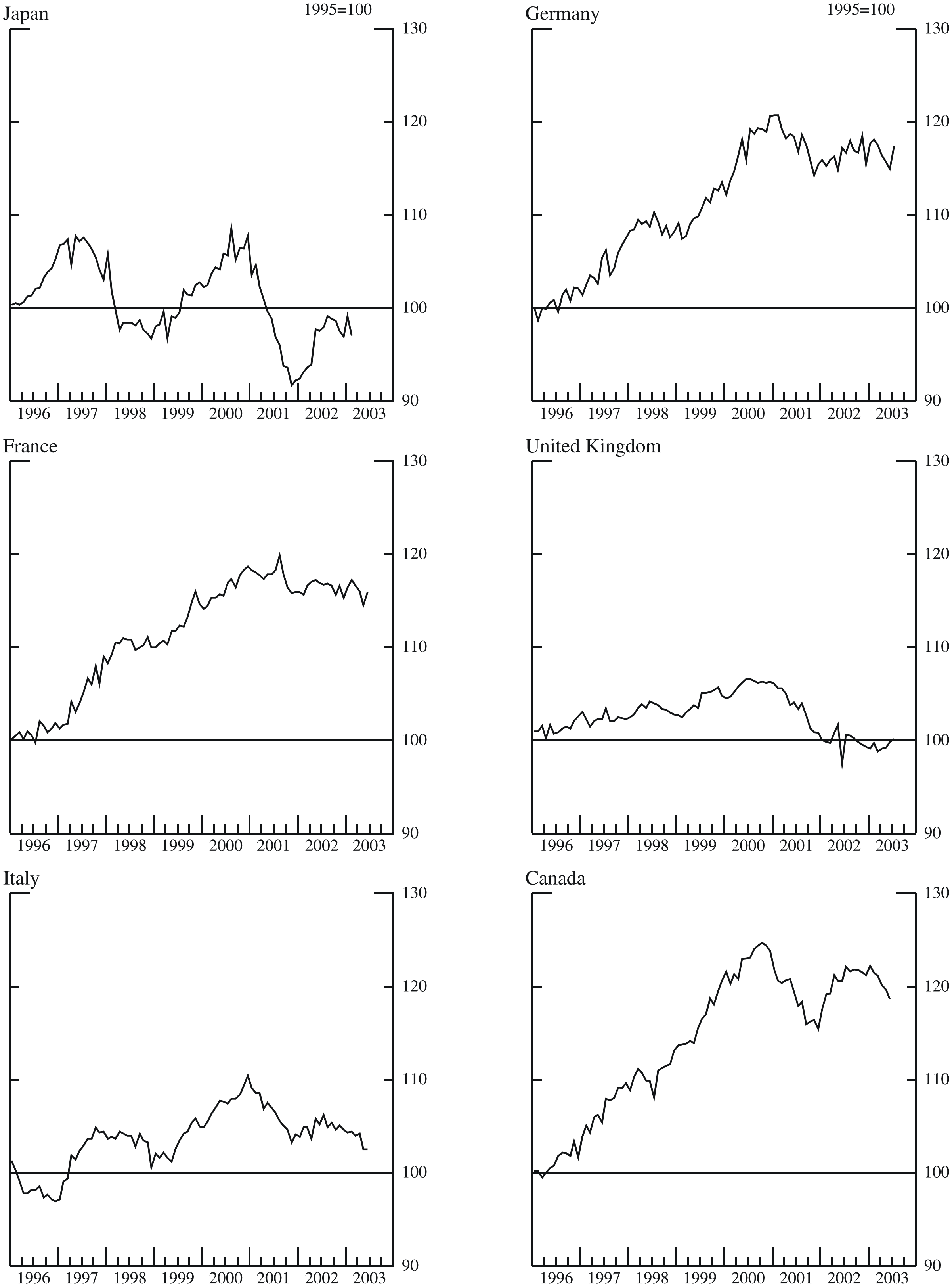
Italy



Canada



Industrial Production in Selected Industrial Countries



Economic Situation in Other Countries

In developing Asia, the negative economic effects of SARS became more apparent with the release of real GDP growth for the second quarter. Indicators for the third quarter suggest a strong rebound in most of the SARS-affected economies. However, economic conditions in Korea, a country not directly affected by SARS, have not improved substantially. Economic performance in Latin America has been mixed. While the Mexican and Argentine economies appear to be recovering, economic activity has continued to be weak in Brazil. Inflation has remained benign in most of the developing world.

In **China**, indications are that the economy is once again expanding at a very strong pace. Retail sales are growing rapidly and were above pre-SARS levels in July. Industrial production continues to expand briskly. Both exports and imports reached new highs in July and retraced only a part of the July increases in August. The trade balance has remained in surplus. Twelve-month consumer price inflation inched up a bit in July, and month-to-month inflation was positive for the first time since March, as the price-depressing effects of SARS waned.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	7.5	8.0	16.3	-2.9	...	...	...
Industrial production[2]	8.9	11.8	17.0	15.1	16.9	16.5	17.1
Consumer prices[2]	-.3	-.4	.5	.7	.3	.5	n.a.
Trade balance[3]	23.1	30.3	-7.2	12.5	13.1	5.8	19.2

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.

Foreign exchange reserves grew $10 billion in July and now exceed $350 billion. China’s central bank continues to attempt to sterilize these inflows. In addition, in August China’s central bank raised the legal reserve requirement for banks from 6 to 7 percent in order to slow the growth of private credit, which is now over 20 percent on a twelve-month basis. The central bank fears that some sectors of the economy, especially property and automobiles, may be experiencing a bubble.

In **Hong Kong**, real GDP plummeted 14 percent (s.a.a.r.) in the second quarter, much more than expected, as the negative economic effects of SARS were felt. Private consumption and services exports (which include tourism) both registered significant declines. The persistence of weakness beyond the second quarter was evident in July consumer price inflation figures, as price discounting by retailers and cuts in government-regulated utility rates led to a noticeable worsening of deflation. The trade deficit improved in July, owing largely to a big increase in re-exports (presumably exports from China, although the breakdown by country is not yet available).

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

Indicator	2001	2002	2003				
			Q1	Q2	May	June	July
Real GDP[1]	-1.3	5.2	-1.2	-14.0	...	...	...
Unemployment rate[2]	4.9	7.3	7.5	8.6	8.3	8.6	8.7
Consumer prices[3]	-3.7	-1.6	-.9	-2.5	-2.4	-3.1	-4.0
Trade balance[4]	-11.4	-7.7	-6.8	-6.8	-6.1	-7.7	-2.6

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.
... Not applicable.

In **Taiwan**, real GDP fell more than 8 percent (s.a.a.r.) in the second quarter due to the negative economic effects of SARS. Component details have not yet been released, but government statements indicated that private consumption fell considerably. However, recent data have been encouraging. Industrial production has picked up quite strongly in recent months, and all indications are that the high-tech industry is rapidly increasing output. Export growth has risen, and this has led to a considerable widening of the trade surplus. In addition, export orders data are reaching new highs, with orders for electronics products at levels not seen since the high-tech peak in late 2000. Consumer prices have fallen recently, largely due to the effects of SARS.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	-1.9	4.3	.0	-8.1	...	...	...
Unemployment rate[2]	4.6	5.2	5.2	5.2	5.2	5.0	n.a.
Industrial production	-7.3	6.4	-.2	-1.0	2.9	5.7	n.a.
Consumer prices[3]	-1.7	.8	-.2	-.1	-.6	-1.0	-.6
Trade balance[4]	15.6	18.1	16.5	16.2	15.6	20.1	18.8
Current account[5]	17.9	25.7	29.8	26.3	...	...	...

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.

Economic conditions in **Korea** have not improved substantially since the last Greenbook. Real GDP contracted about 3 percent (s.a.a.r.) in the second quarter, as geopolitical risks from North Korea's nuclear development, labor unrest, and the high level of household debt depressed private sector spending. Industrial production declined about 4 percent in July, mainly due to strikes in the auto sector, and the unemployment rate was unchanged at 3.6 percent. Consumer confidence indicators and retail sales were flat in July, suggesting continued weakness in consumer spending, and twelve-month consumer price inflation inched down a bit in August. However, consumer and business confidence indicators were up in August. And even though the trade surplus narrowed in July, due to rising imports, exports continued to grow.

On September 9, citing concerns that a much-awaited recovery had yet to take shape, the Bank of Korea held the overnight call rate unchanged at 3.75 percent.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	4.2	7.0	-1.6	-2.9	...	...	...
Industrial production	.4	8.3	.3	-.4	2.8	-3.9	n.a.
Unemployment rate[2]	3.8	3.1	3.1	3.4	3.6	3.6	n.a.
Consumer prices[3]	3.2	3.8	4.1	3.3	2.9	3.2	3.0
Trade balance[4]	13.5	14.2	9.4	19.3	26.6	19.8	n.a.
Current account[5]	8.2	6.1	-6.9	10.1	20.5	5.1	n.a.

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.

Economic indicators in the **ASEAN** region have been mixed since the last Greenbook. Indonesia and Malaysia posted robust growth in the second quarter. In Indonesia the expansion was widespread across all sectors, whereas in Malaysia healthy manufacturing growth offset slower growth in the service sector. In the Philippines, growth was marginal in the second quarter after contracting in the previous quarter, with the economy being held back by fiscal tightening and an agricultural sector suffering from prolonged drought. In Singapore a drastic contraction in the SARS-affected service sector dragged down the economy. There is little hard information available yet for the third quarter, but industrial production increased in July in both Singapore and Thailand. With the exception of Singapore, trade balances narrowed in July as imports rose faster than exports. Inflation remains benign, with Singapore again experiencing mild price increases.

ASEAN Economic Indicators: Growth
(Percent change from previous period, s.a., except as noted)

Indicator and country	2001	2002	2003				
			Q1	Q2	May	June	July
Real GDP[1]							
Indonesia	1.7	3.8	4.5	6.3	...	...	...
Malaysia	-.9	5.3	2.9	6.9	...	...	...
Philippines	3.6	5.7	-2.1	.3	...	...	...
Singapore	-6.0	3.0	1.4	-11.4	...	...	...
Thailand	2.2	6.4	6.3	n.a.	...	...	...
Industrial production[2]							
Indonesia[3]	.7	-1.1	1.1	-2.5	-2.1	-.9	n.a.
Malaysia	-4.1	4.6	2.1	4.0	4.7	-3.7	n.a.
Philippines	-5.7	-6.1	2.9	7.1	-2.9	8.5	n.a.
Singapore	-11.6	8.5	2.0	-4.0	-3.4	2.1	1.0
Thailand	1.3	8.5	4.1	3.0	-1.9	-3.2	2.5

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	2001	2002	2003				
			Q1	Q2	May	June	July
Indonesia	25.4	25.9	28.7	29.1	29.2	29.6	29.2
Malaysia	14.2	13.5	19.4	20.8	20.8	20.7	16.2
Philippines	-.9	-.2	-2.1	-1.2	-3.8	1.4	n.a.
Singapore	5.8	8.7	16.3	13.2	15.2	14.1	19.5
Thailand	2.5	3.4	5.7	5.8	4.1	7.6	4.2

n.a. Not available.

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

Country	2001[1]	2002[1]	2003				
			Q1	Q2	June	July	Aug.
Indonesia	12.5	10.0	7.7	7.0	6.6	5.8	6.4
Malaysia	1.2	1.7	1.3	.9	.8	1.0	n.a.
Philippines	4.1	2.6	2.9	3.0	3.4	3.4	3.0
Singapore	-.6	.4	.7	.2	-.3	.3	n.a.
Thailand	.8	1.6	2.0	1.8	1.7	1.8	2.2

1. December/December.
n.a. Not available

In **Mexico**, recent information suggests that the economy showed some recovery in the second quarter following a first-quarter contraction, although the improvement was uneven. Real GDP posted an annual rate gain of nearly 5 percent, with increases in agriculture and mining (including oil), and also in trade and financial services. However, industrial production declined in May and June and for the quarter on average. Exports also fell in the second quarter. Nevertheless, some positive indications appeared later in the quarter, as exports rose in June and were little changed in July. Retail sales also rose in June, and business confidence remained steady at a relatively favorable level through July. Twelve-month inflation has continued to fall and has reached the top of the one-percentage-point band around the 3 percent target for this year. Inflation expectations have also fallen.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	-1.4	2.0	-1.7	4.9	...	...	...
Overall economic activity	-.1	.9	.2	.4	.5	n.a.	n.a.
Industrial production	-3.3	-.2	.1	-.7	-.2	n.a.	n.a.
Unemployment rate[2]	2.5	2.7	2.7	3.0	3.4	3.5	n.a.
Consumer prices[3]	4.4	5.7	5.4	4.7	4.3	4.1	4.0
Trade balance[4]	-10.0	-7.9	-4.0	-7.5	-6.7	-7.6	n.a.
Imports[4]	168.4	168.7	169.0	168.5	169.4	170.0	n.a.
Exports[4]	158.4	160.8	165.0	161.0	162.7	162.4	n.a.
Current account[5]	-18.0	-14.0	-8.7	-5.9	...	...	...

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**, real GDP dropped 6.2 percent (s.a.a.r.) in the second quarter, as sharp declines in private consumption and investment more than offset positive growth in net exports. First-quarter GDP growth was also revised down from -0.2 percent to -2.3 percent. Only a sharp rebound in oil production kept industrial production growth positive in July. The weak economy kept inflationary pressures at bay: despite a rise in prices in July and August due to annual adjustments in utility rates, twelve-month inflation continued to decline. Brazil has continued to register sizeable trade surpluses, contributing to a small current account surplus. The weak economy and the decline in inflation led the central bank on August 20 to reduce its benchmark overnight interest rate, the Selic, for the third time this year, from 24.5 to 22 percent.

The Brazilian government met its second-quarter IMF program performance criteria, leading to a disbursement of $4 billion in early September (about $1.3 billion is due to the IMF over the third quarter). The government's pension and tax reform bills continued to make progress in the congress.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	-.9	3.2	-2.3	-6.2	...	...	...
Industrial production	1.6	2.4	-1.1	-2.5	-2.6	.4	n.a.
Unemployment rate[2]	12.4	12.5	11.1	12.1	12.6	12.7	n.a.
Consumer prices[3]	7.7	12.5	15.6	16.9	16.6	15.4	15.1
Trade balance[4]	2.7	13.1	17.0	23.6	24.8	22.8	26.4
Current account[5]	-23.2	-7.7	.3	1.6	5.7	8.9	n.a.

1. Annual rate. Annual figures are Q4/Q4.
2. Percent. Break in October 2001 as a result of change in methodology. Thus, 2001 is average for Q4 only.
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.

In **Argentina**, the incipient economic recovery continues. After three months of disappointing performance, industrial production rose 1.5 percent in July. Inflation has remained under control: in August the consumer price index rose 0.3 percent from the previous month, bringing the twelve-month inflation rate down to just under 5 percent. After significant appreciation in the first half of the year, the peso depreciated 1.3 percent against the dollar in August, and it now appears to have stabilized at just under 3 pesos per dollar.

Argentina’s IMF program, approved last January, expired at the end of August. Whereas fiscal and monetary targets agreed with the IMF have been met, the country had difficulties satisfying some of the program’s structural conditions. On September 9, Argentina failed to make a key $2.9 billion payment to the IMF, as a medium-term, three-year agreement with the Fund was not reached. However, negotiations are continuing. Some issues currently being negotiated include the size of the primary surplus, compensation to banks for actions undertaken by the government that damaged banks’ balance sheets, and utility rates. The Argentine authorities have indicated their desire to present a debt restructuring plan to private sector creditors in late September, assuming an IMF agreement will be in place by then. However, creditors are concerned that Argentina might present a take-it-or-leave-it offer.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	-10.3	-3.3	10.0	n.a.	...	...	...
Industrial production	-7.6	-10.7	7.7	.0	.2	1.5	n.a.
Unemployment rate[2]	18.1	20.4	16.4	16.4	...	...	...
Consumer prices[3]	-1.4	41.0	35.8	14.5	10.2	7.3	4.9
Trade balance[4]	7.5	16.7	15.7	19.1	18.6	18.3	n.a.
Current account[5]	-4.5	9.6	7.8	n.a.	...	...	...

1. Annual rate. Annual figures are Q4/Q4.
2. Percent, n.s.a. Data for Greater Buenos Aires. Data released semi-annually.
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 **Venezuela,** little new data have been released since the last Greenbook. July oil output remained at its second-quarter average, estimated to be at capacity, but still 15 percent below levels prevailing before the general strike at the end of last year. There have been no signs of a recovery in the non-oil sector. Unemployment remained around 18 percent in June. The government continues to maintain stringent capital controls to support the fixed-exchange rate regime introduced last January.

In late August, following months of political deadlock, the Supreme Court appointed members of an electoral council, strengthening prospects that President Chavez will face a recall election on November 20.

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

Indicator	2001	2002	2003				
			Q1	Q2	June	July	Aug.
Real GDP[1]	.9	-16.7	-52.4	n.a.	...	...	...
Unemployment rate[2]	13.4	16.0	19.4	18.4	17.8	n.a.	n.a.
Consumer prices[3]	12.3	31.2	35.5	34.2	34.2	31.8	30.4
Non-oil trade balance[4]	-12.2	-7.4	-2.5	n.a.	n.a.	n.a.	n.a.
Trade balance[4]	9.3	13.9	12.8	n.a.	n.a.	n.a.	n.a.
Current account[5]	3.9	7.7	7.8	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.