

Site w/
Record of
Speech

- Pleasure to be speaking w/ you tonight
- Several of my FRBB colleagues here who are Chartered Financial Analysts
- As it turns out - this is a watershed day - for NBER has called the stats on an end to 10 years of expansion today. Officially the U.S. economy is in a recession that will be dated from March of this year.

Current Economic Conditions in the U.S.

Depth.
Duration
Diffusion

- This chart pack completed prior to the action of the Business Cycle Dating Committee - so I talk about a downturn rather than be the first FOMC member to declare a recession.
- I want to use this talk to address three issues:
 - Where are we
 - ~~What~~ Sources of strength

- Uncertainties

Cathy E. Minehan

Federal Reserve Bank of Boston

November 2001

- Do a bit on the
region to conclude

So

Where are We?

The economy is contracting.

We're in a recession - how does the NBER determine this - lots of judgement used - but looking for depth, duration & diffusion - monthly data key so not so focused on GDP - std. definition of 2 qtrs. negative GDP - only time in headlight - for employment drops example only have one qtr. neg. now - don't use

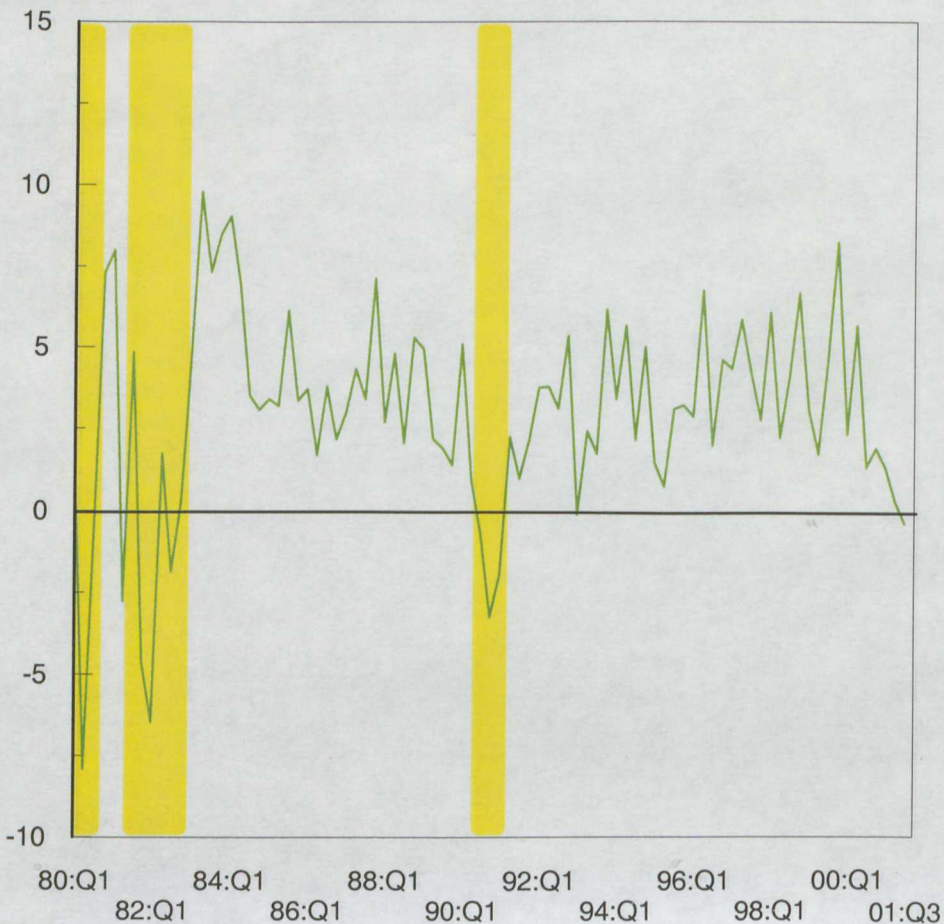
GDP Turns Negative

Qtrs. negative GDP - only time in headlight

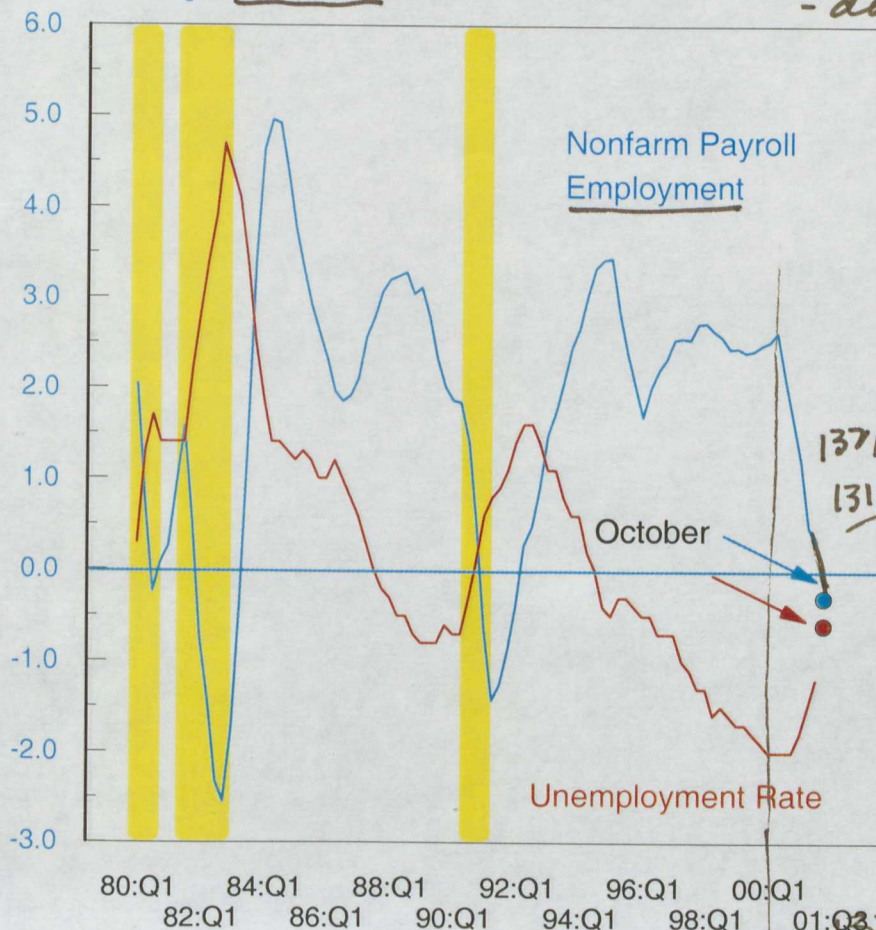
Employment Drops

example only have one qtr. neg. now - don't use

Annualized Percent Change, Previous Quarter



Percent Change, ^{quarterly data} Year-over-Year



Percent forecasts & lost for pattern vs. earlier recession 9.0

8.0 need

*1371659
131767
887*

Source: Bureau of Economic Analysis (GDP) and Bureau of Labor Statistics (employment and UR).

*137145
131767
0378*

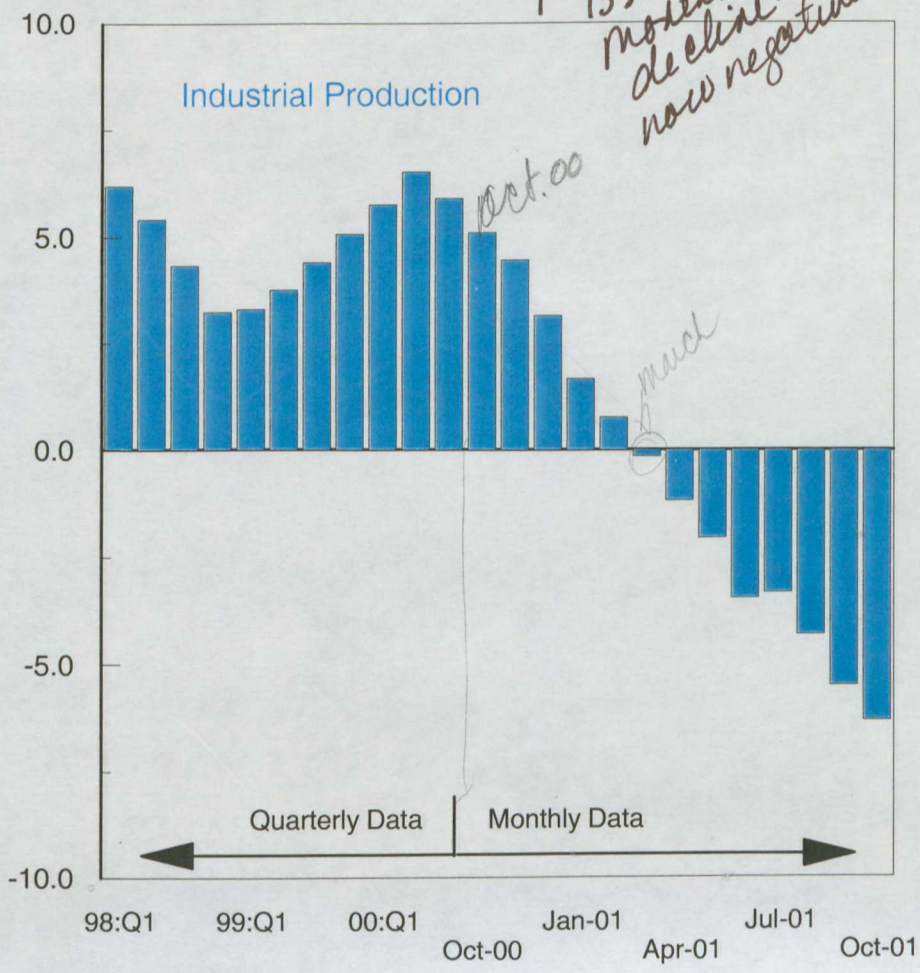
Key aspect to this recession - drop in business fixed investment. After years of double digit spending driven by Y2K and dot com fever, about a year ago, businesses, trapped by rising labor costs dropping profits stopped spending - and they particularly stopped spending on computer software

Business Investment Falls.

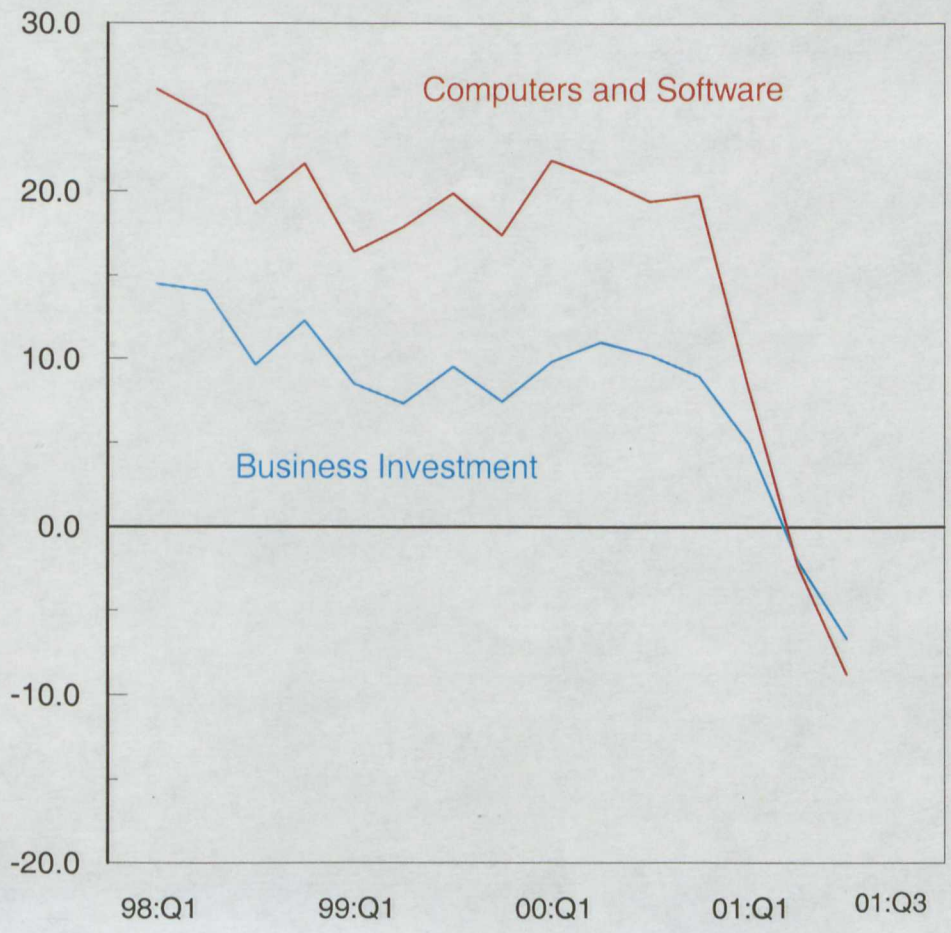
This much lower than usual pre-recession

can see the effects of this in industrial production
13 straight months of decline - now negative

Percent Change, Year-over-Year



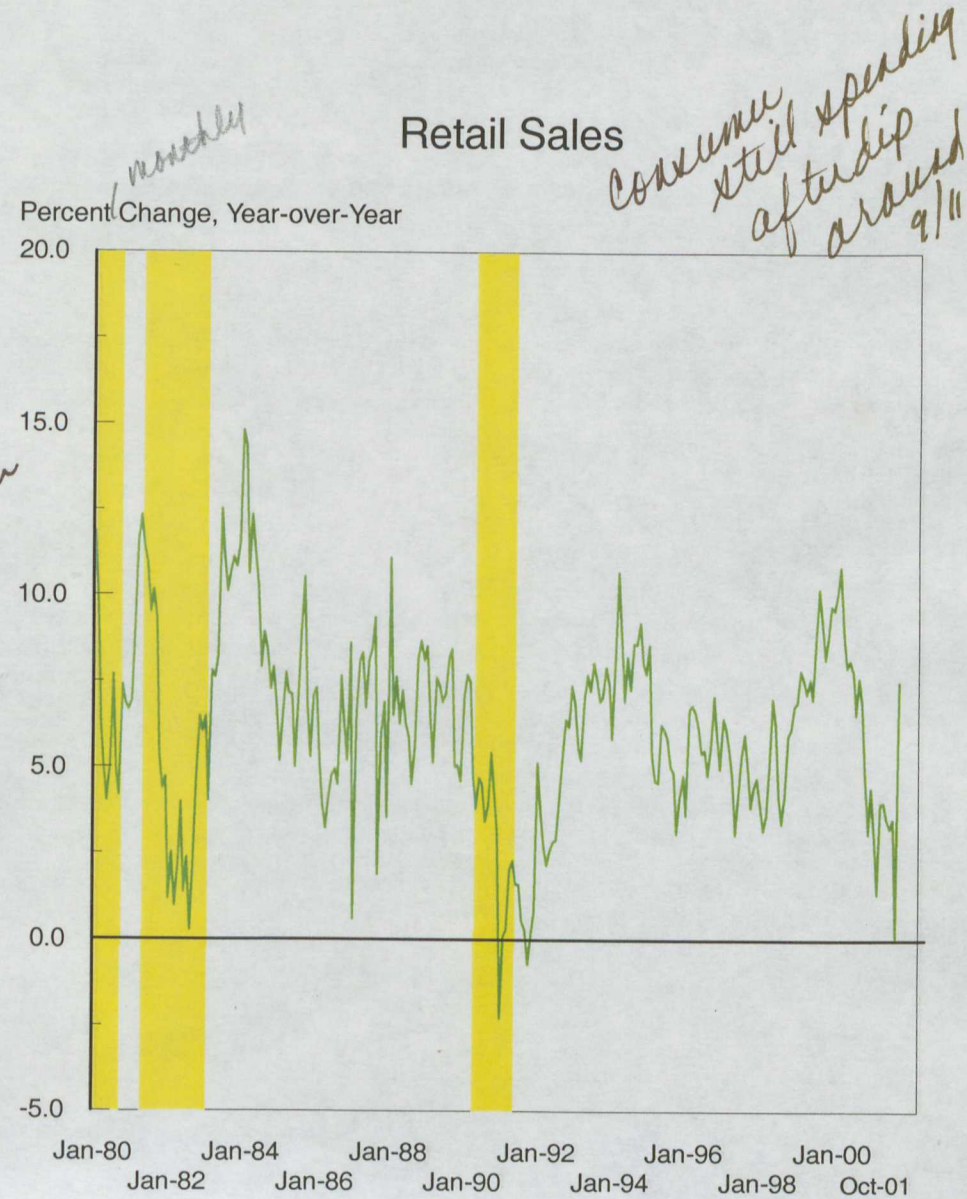
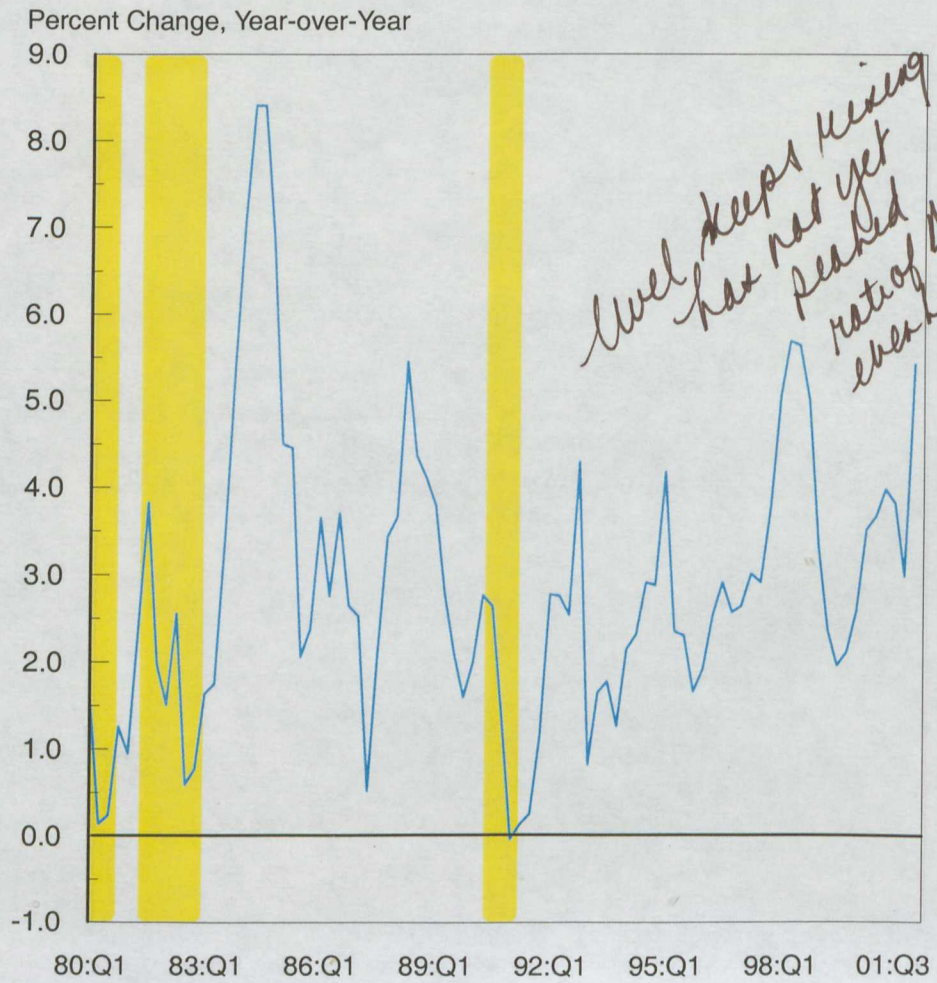
Percent Change, Year-over-Year



Source: Federal Reserve Board (production) and Bureau of Economic Analysis (investment).

But, there are some sources of strength - the consumer.

→ Here are areas that NBER looks at that has not yet peaked
 Real Disposable Personal Income



Source: Bureau of Economic Analysis (income) and Bureau of the Census (retail sales).

one recession in past was history Fed didn't cause

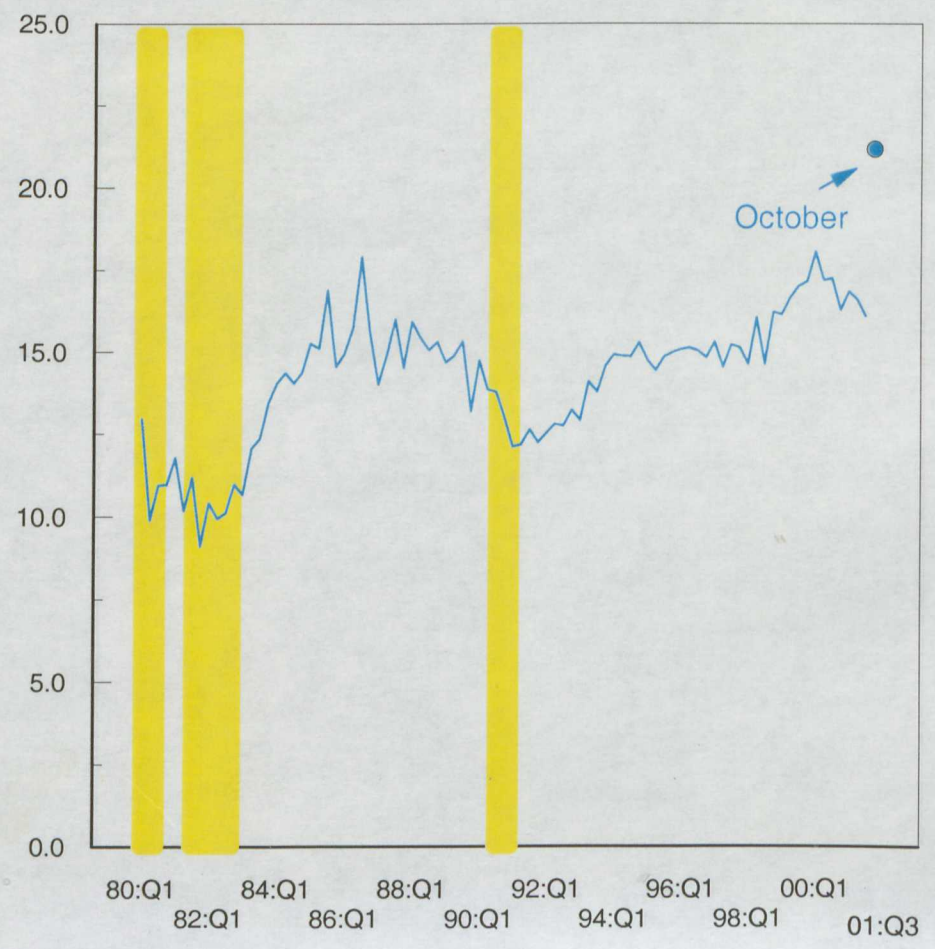
usually in a recession consumer interest sensitive sector is hardest hit - that's because Fed tightens to address inflation - this time we didn't because (turn)

And consumer willing to spend on big ticket items as well - some say only 0% financing and the lowest mortgage rates in some time make this possible - I say - couldn't tempt consumers to buy if they didn't have faith in the future -

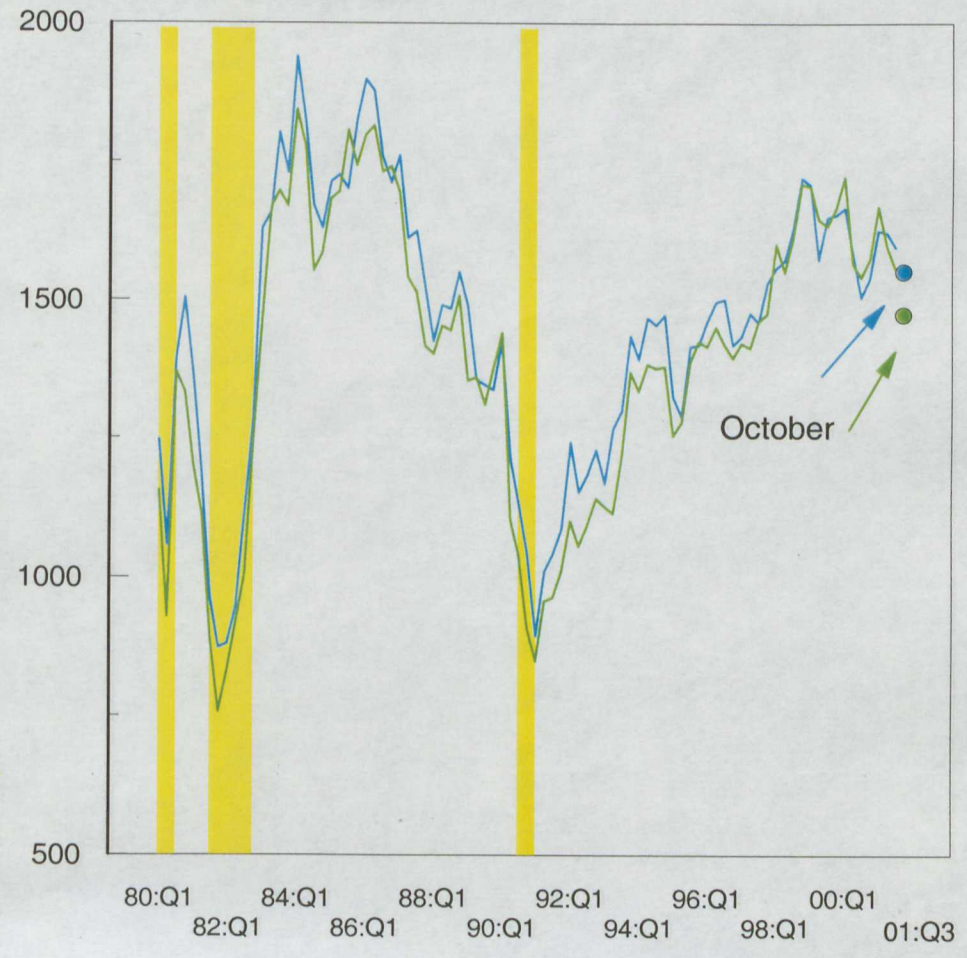
Auto and Light Truck Sales

Housing Starts and Building Permits

Millions of Units at Annual Rates



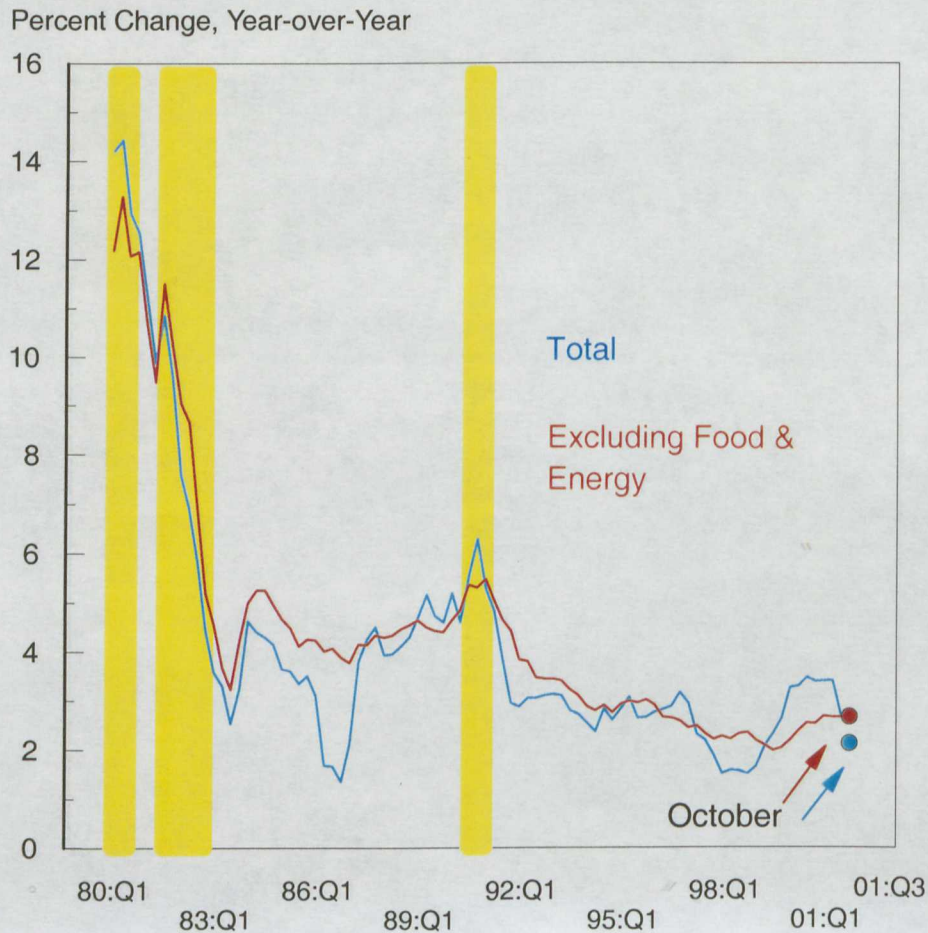
Thousand of Units at Annual Rates



Source: Bureau of Economic Analysis (autos) and Bureau of the Census (housing).

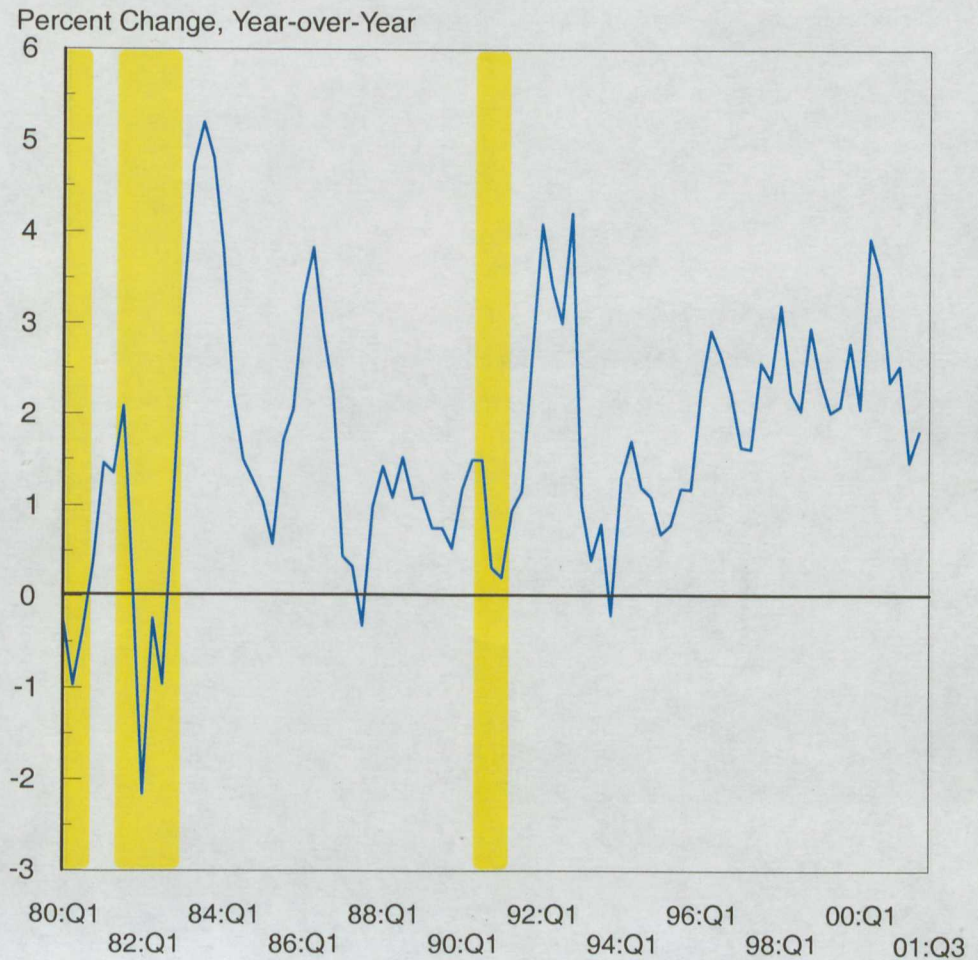
Inflation is not an issue. - *certainly a concern rather issue - thus, without hitting consumers not hit hard, spending continues, prices*

Consumer Price Index



Productivity is remarkably strong. *cyclical vs structural*

Output per Hour

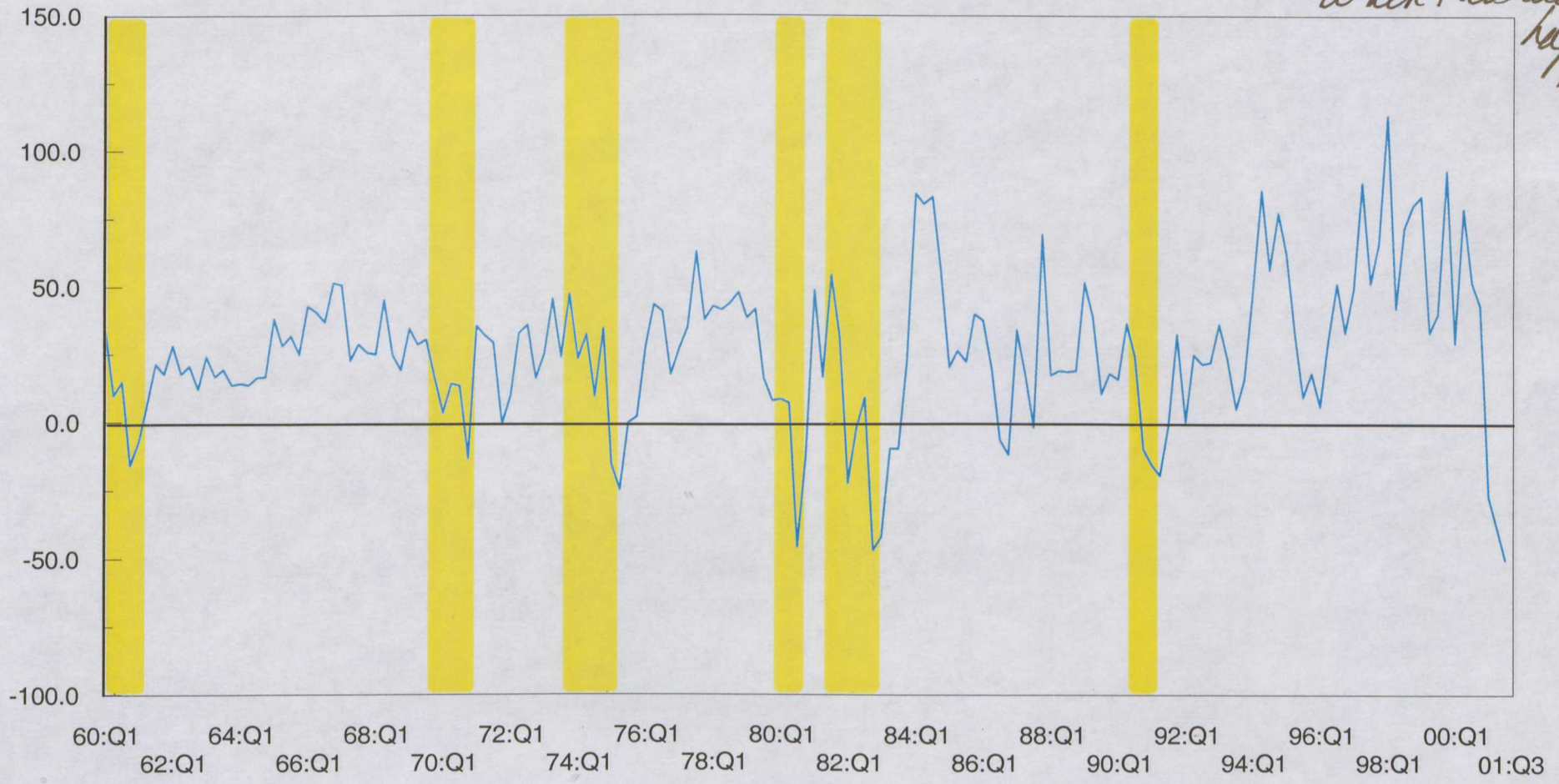


Inventories could add to future growth. *Here's an area where we really look as if in recession territory - inventories drawn down by just about record amounts in real terms - at some point have to start building inventories again - that will lead to ^{spec. production} growth -*

Change in Real Business Inventories

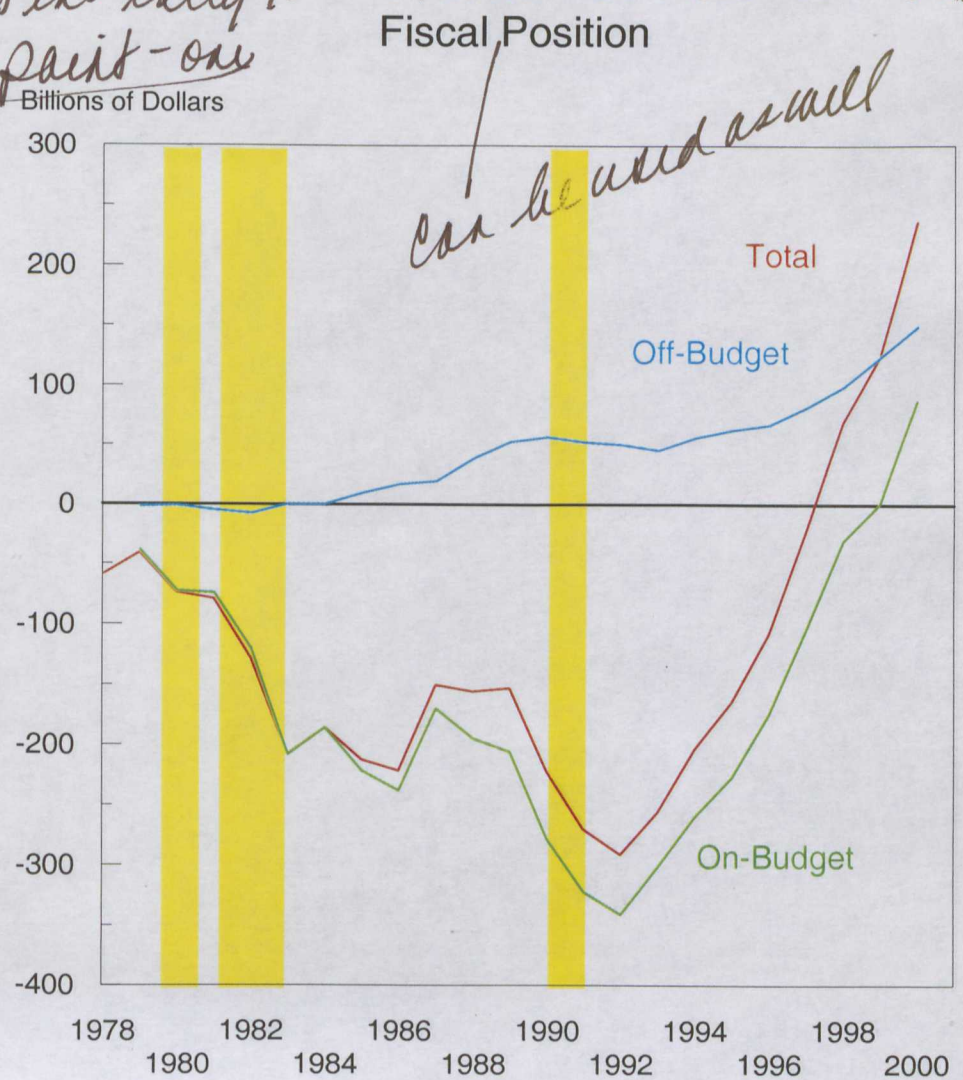
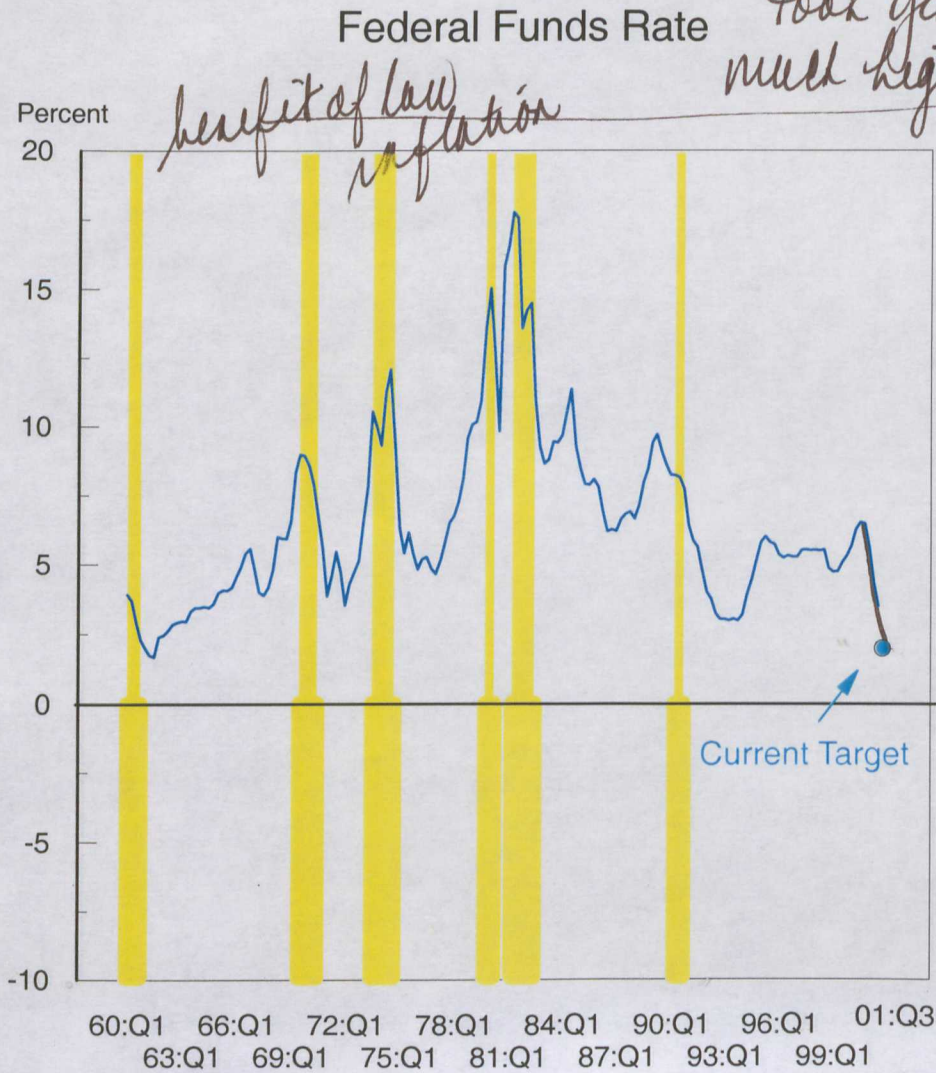
only question is when this will happen

Billions of Dollars (Chained 1996)



Source: Bureau of Economic Analysis.

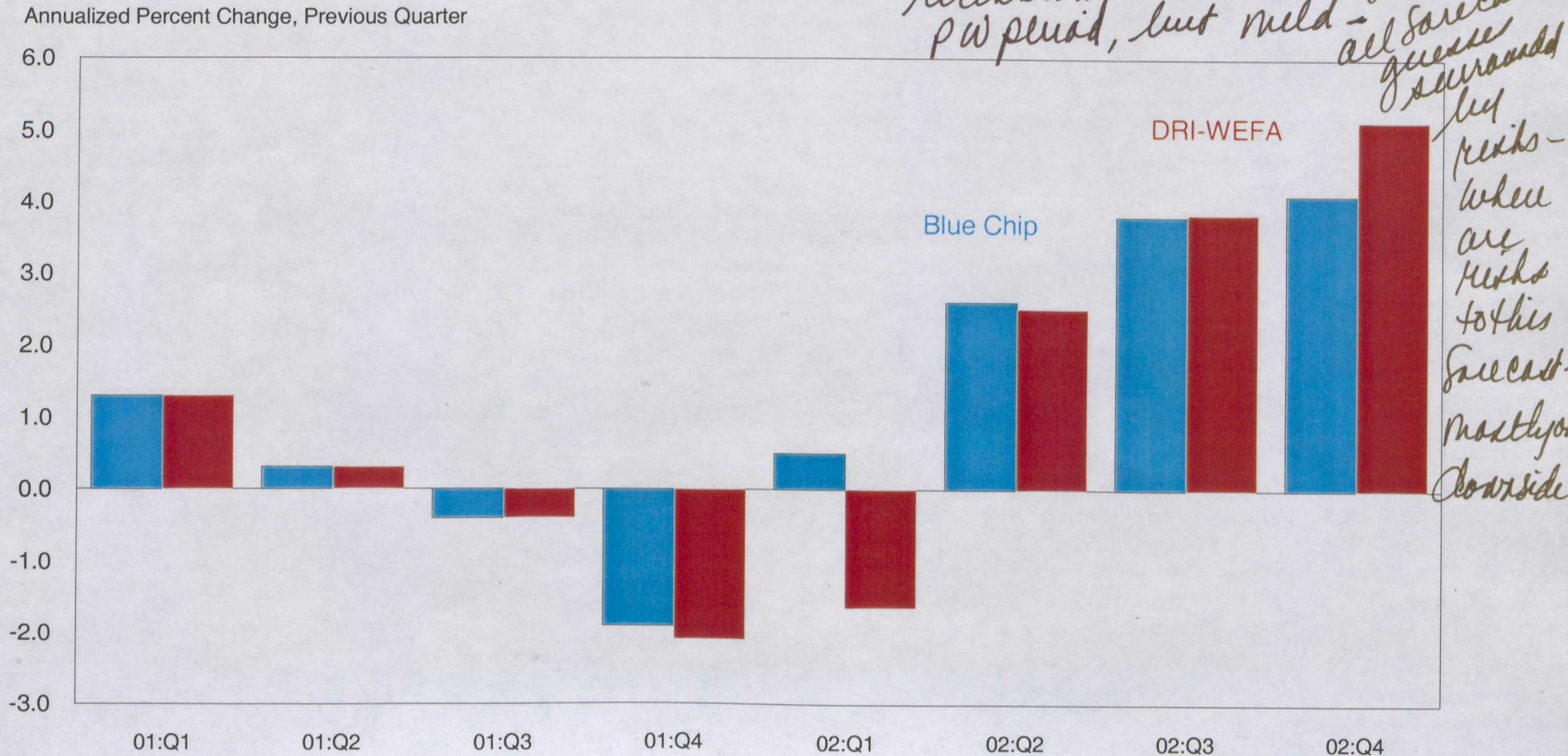
Policy response has been aimed at making that turnaround happen sooner rather than later. 4.5 percentage point ease in Monetary and fiscal policy response. Federal funds rate in last 10 months - ~~quicker than~~ started before the recession began - unusual and mixed factor - hard to see on the chart but took years in early 90's to move that much even for much higher point - one



As a result, most forecasts see a shallow, short downturn.

now should note that with recession now dated at March 2001, by April 2001 will be 11 months old - so if DRI might recession, about average for PW period, but mild - all forecasts guess around 1% but

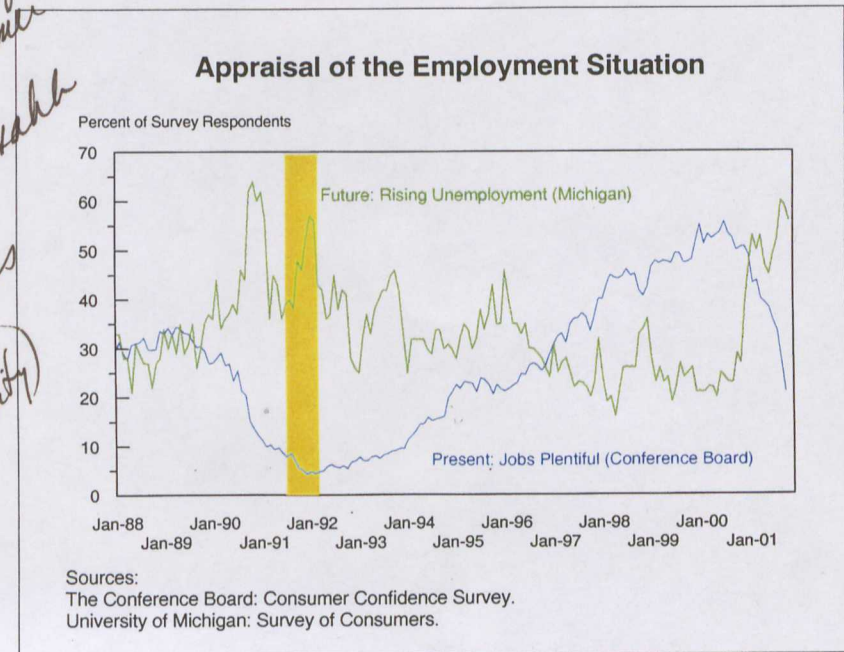
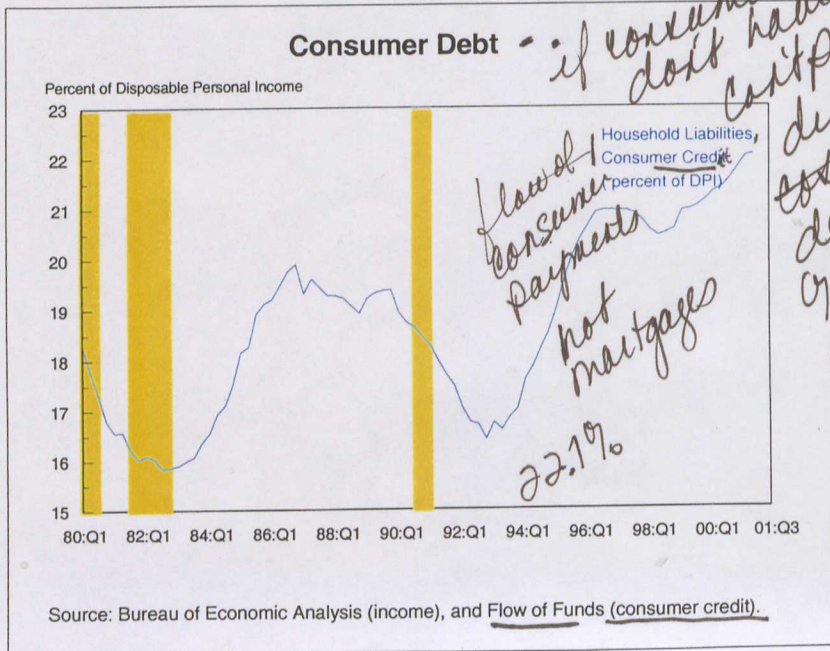
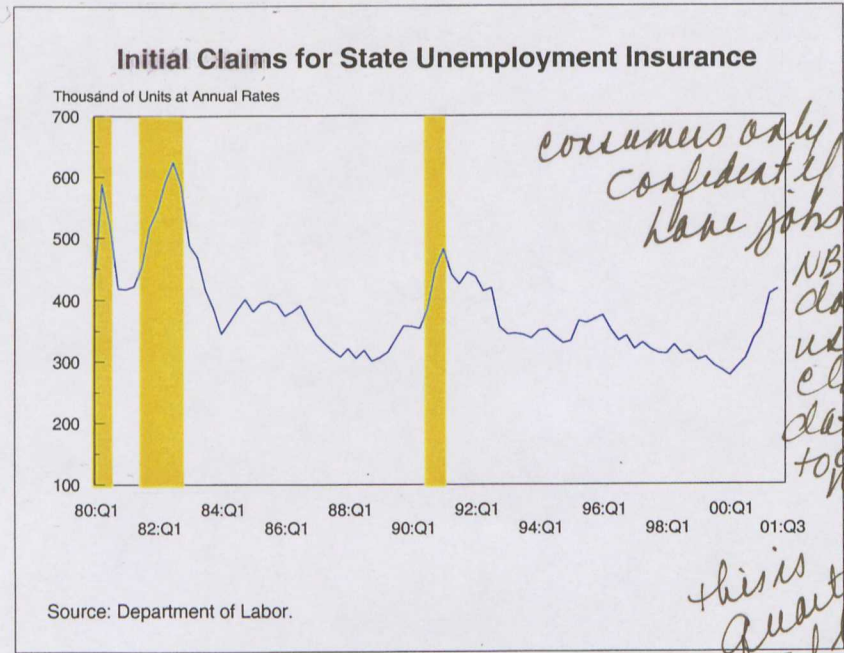
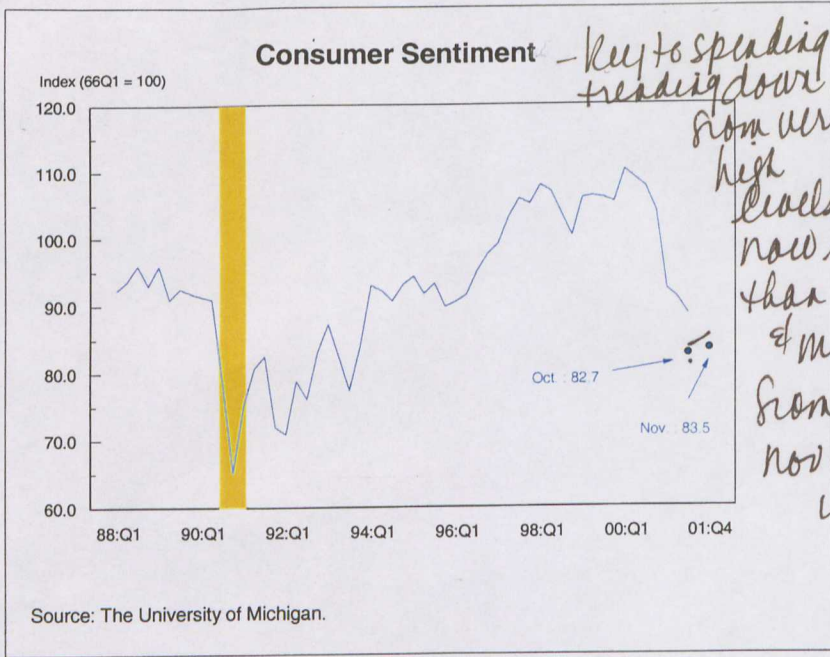
Forecasts of GDP Growth



but peaks - where are peaks to this forecast - mostly downside

Source: Blue Chip Economic Indicators (November 10th) and DRI-WEFA (November 8th).

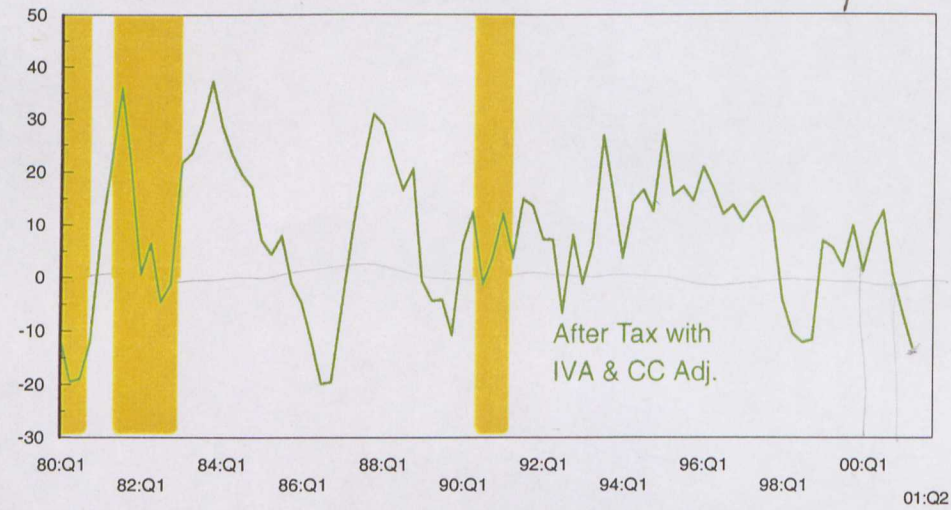
But uncertainties abound.



Business prospects unsettled as well.

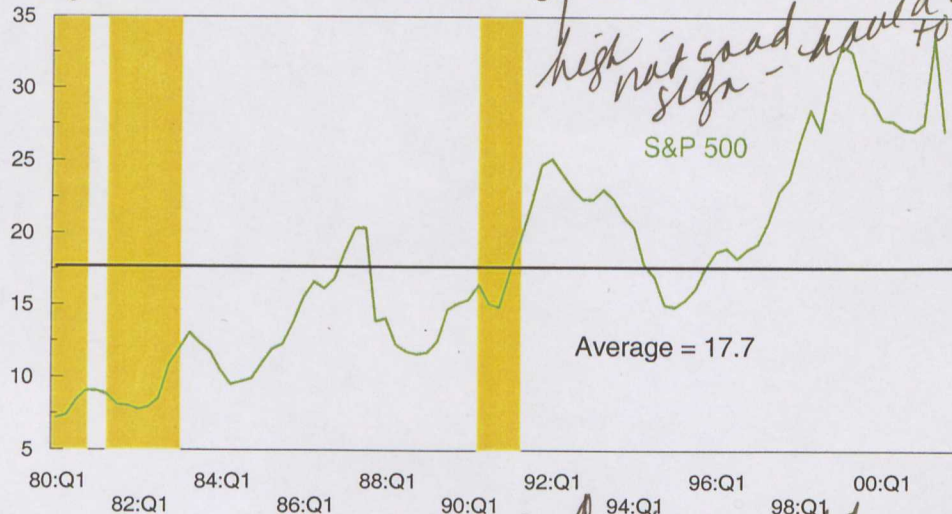
And businesses may have run down their inventories, but questionable how soon they will start spending - corporate profit growth trending down, negative for most of the yr - 15% + 5 1/4

Percent Change, Year-over-Year Corporate Profits



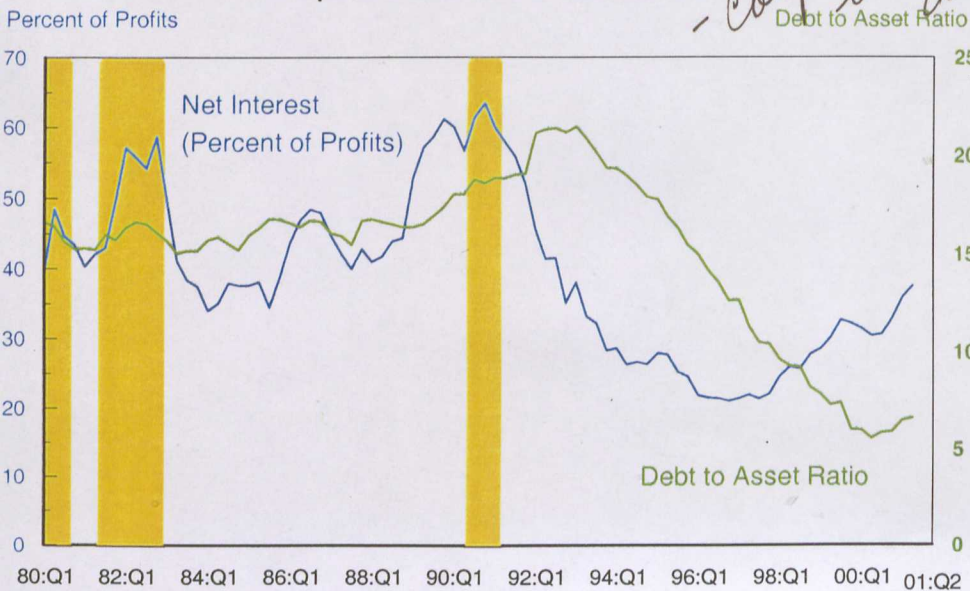
Note: IVA & CC Adj. = Inventory valuation and capital consumption adjustments.
Source: Bureau of Economic Analysis.

Ratio Price Earnings Ratio



Source: Standard and Poor's

Corporate Debt and Net Interest



Source: Bureau of Economic Analysis (income), and Flow of Funds (business liabilities).

corporations increasing debt & cash flow disappear - this is leverage of profits - going to interest

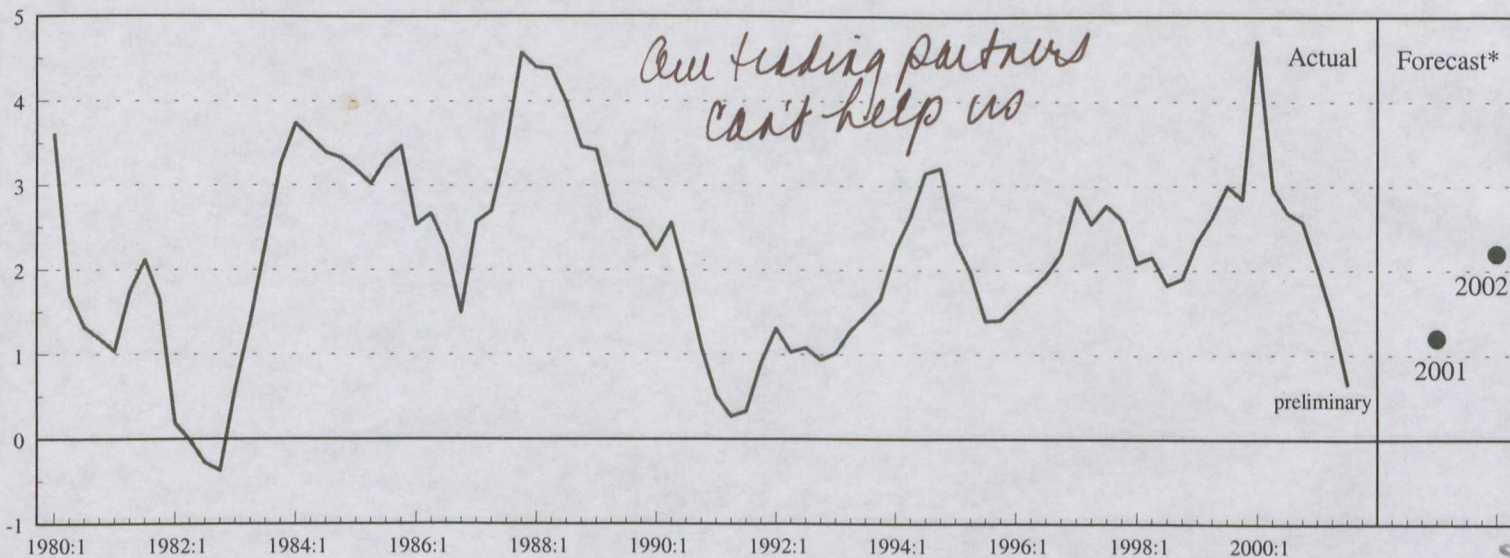
Selected Fixed Income Spreads from the 10 Year Treasury



Source: JP Morgan, Bloomberg, FAME, Federal Reserve Board of Governors.

Trade-Weighted GDP Growth for Top Ten U.S. Export Partners

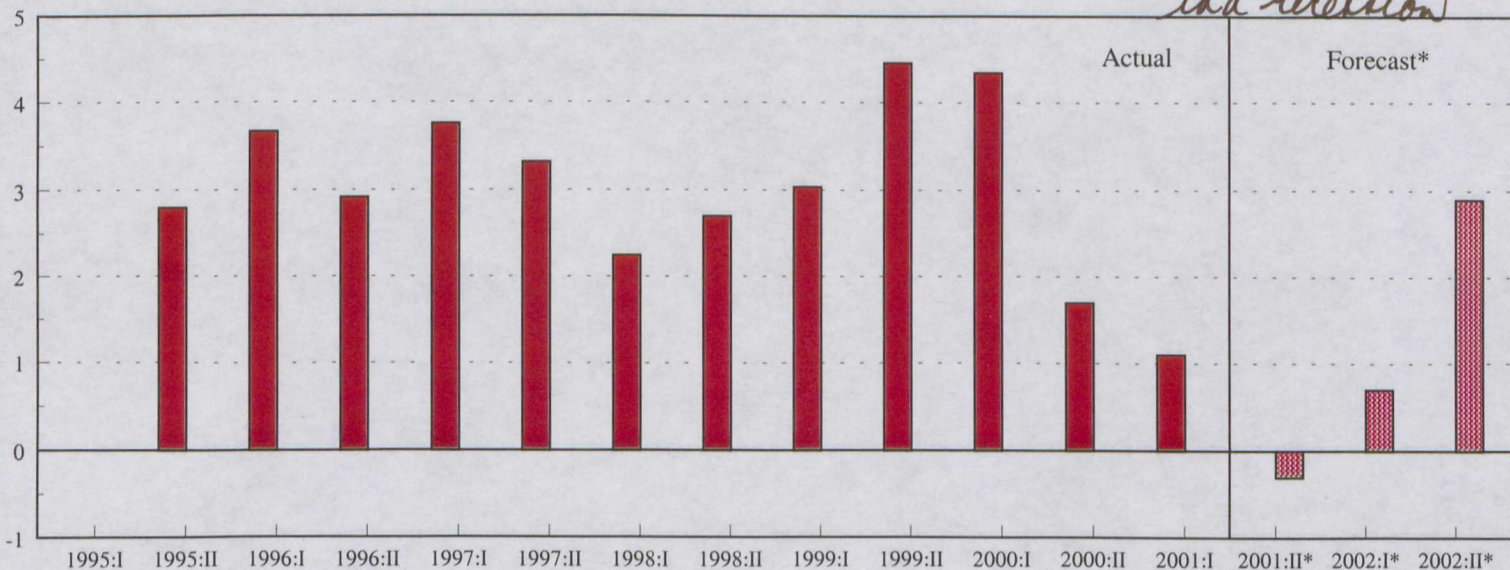
% change from previous quarter at annual rate; forecast from previous year



% change from previous half-year at annual rate

Total OECD GDP Growth

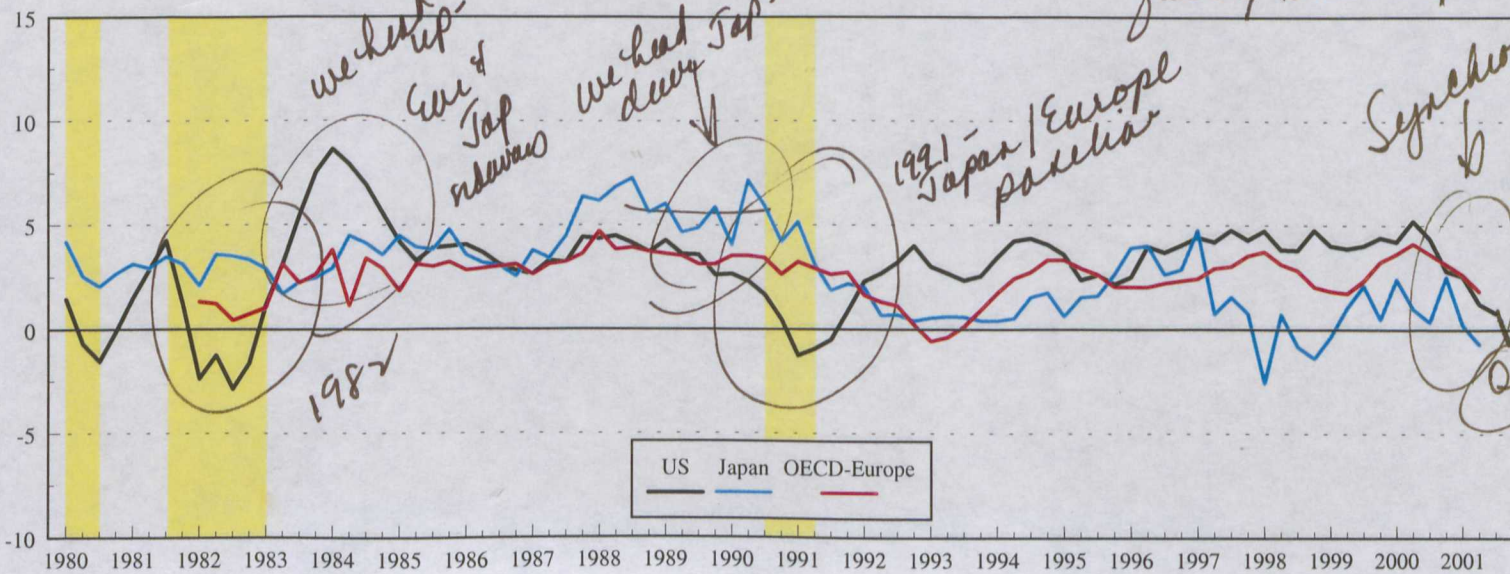
- whole world now in a recession



Year-over-year percent change

Real GDP Growth in Selected Regions

- fairly unusual



* Forecast (from Blue Chip for top ten U.S. export partners; from OECD for OECD members).

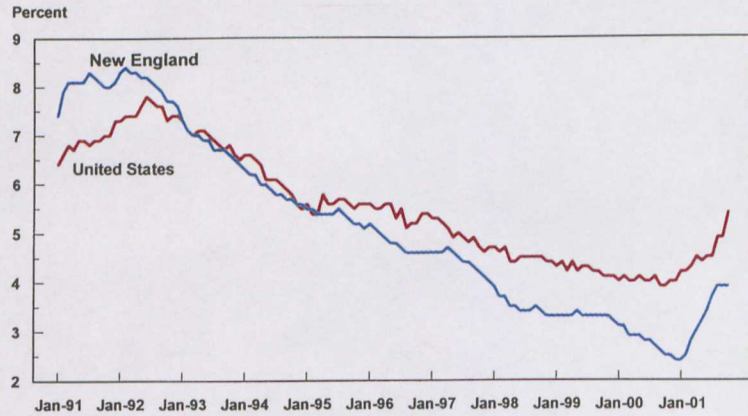
Sources: OECD Main Economic Indicators; Blue Chip; U.S. Bureau of Economic Analysis; Standard and Poor's DRI.

and the rest of the world won't help.

In Sum:

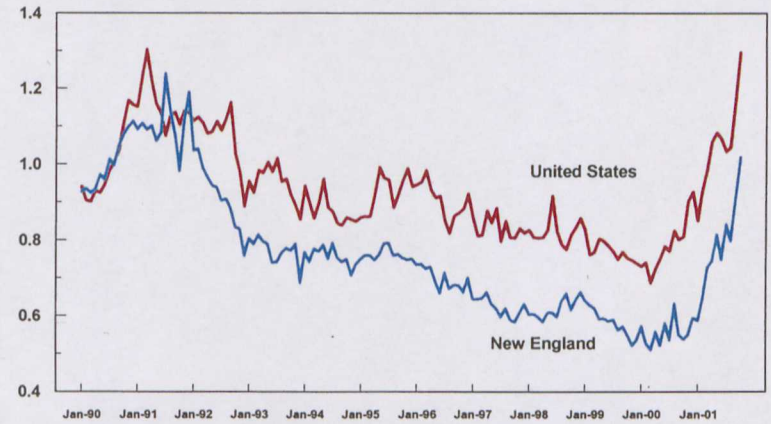
- Downturn will deepen in late 2001, ^{and continue into} early 2002.
- Best guess: shallow and short.
- Lots of downside risks.
- Region will follow national path.

Unemployment Rates



Note: Data beginning January 1994 reflect the redesigned CPS survey and are not strictly comparable to data for 1993 and earlier years.
Source: U.S. Bureau of Labor Statistics.

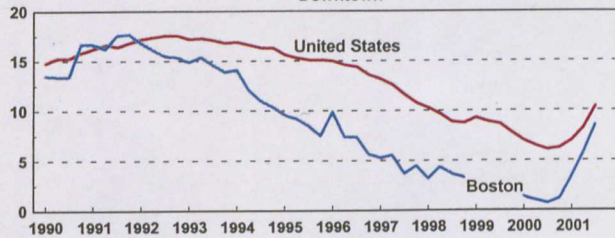
Initial Claims for Unemployment Insurance (Index 1990 = 1)



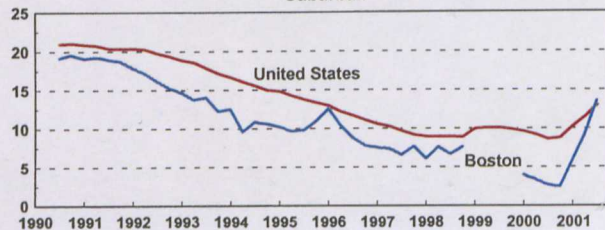
Source: U.S. Employment and Training Administration

Office Vacancy Rates

Downtown

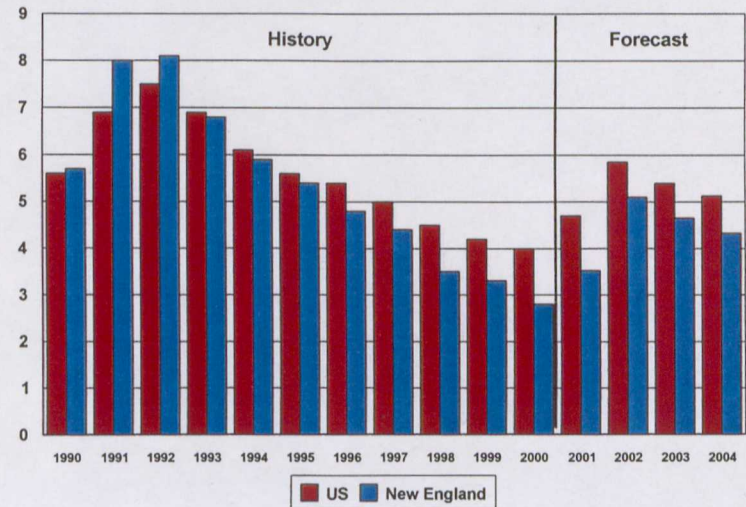


Suburban



Source: CB Richard Ellis.

NEEP Forecast of Unemployment Rates



Source: The New England Economic Project.