



# JOINT ECONOMIC COMMITTEE

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## ECONOMIC VITAL SIGNS: MARCH 2006

Economic activity has increased for seventeen consecutive quarters. In 2005, the economy grew at an annual rate of 3.5%. Job creation has maintained its healthy growth rate through February 2006. Since August of 2003, the economy has added 5 million non-farm payroll jobs.

### Economic Indicators

- Economy grew at a 3.5% rate in 2005
- Employment
  - 243,000 payroll jobs were added in Feb.
  - 4.8% unemployment rate in Feb.
  - 2.1 million payroll jobs added since Feb. 05
- Fixed nonresidential investment rose 5.4% in Q4
- Manufacturing production increased 0.7% in Jan.
- Real disposable personal income increased 2.2% from January 05 to January 06
- Inflation from January 05 to January 06
  - 3.1% increase in prices for PCE
  - 1.8% increase excluding energy & food
- Interest rates in February
  - Home mortgage rates averaged 6.25%
  - The prime rate stood at 7.5%

### REAL GDP

The Commerce Department reported that real gross domestic product (GDP) – the inflation-adjusted measure of current output of goods and services produced by labor and property located in the U.S. – increased 1.6% in the fourth quarter. The deceleration in real GDP growth in the fourth quarter from 4.1% in the third quarter can be largely attributed to a hurricane-related deceleration in personal consumption expenditures as well as a deceleration in fixed investment and national defense expenditures.

Real GDP increased at an annual rate of 3.5% in 2005. This increase in economic activity compares favorably to the 30-year annual average increase of 3.1%.

### EMPLOYMENT

In February, the economy created 243,000 non-farm payroll jobs. The unemployment rate stood at 4.8%. Over the last year, the economy added 2.1 million non-farm payroll jobs. This is an impressive showing considering that net national job growth was at a virtual standstill in September and October due to the effects of the hurricanes.

### INDUSTRIAL PRODUCTION

According to the Federal Reserve, manufacturing production increased 0.7% in January, following a gain of 0.5% in December. From January 2005 to January 2006, manufacturing production rose 4.5%. Manufacturing and mining production rose in January, but as a result of the decline in utility output due to unseasonably warm weather, the broader measure of industrial activity, called industrial production, decreased slightly.

The Commerce Department reported that new orders for manufacturing industries, excluding transportation equipment, increased 1.6% in January. The headline aggregate statistic for new manufacturing orders (that includes transportation equipment) registered a decrease due to a large drop in orders for transportation equipment. Transportation equipment orders can fluctuate dramatically because new aircraft orders are often valued in the tens of billions of dollars.

The Institute for Supply Management reported that both the manufacturing and non-manufacturing sectors expanded in February.

## PERSONAL CONSUMPTION AND INCOME

The August and September hurricanes disrupted the growth of real personal consumption expenditures (PCE). The drop in spending after the hurricanes, and the volatility of energy prices that affects how real PCE is calculated, account for most of the erratic behavior of the month-to-month real PCE statistic. It appears that real PCE has returned to trend, as the accompanying graph shows. From January 2005 to January 2006, real PCE increased 3.6%.

Principally due to the effects of the hurricanes, there have also been erratic swings in the components of personal income. However, from January 2005 to January 2006, real disposable personal income increased 2.2%.

### INTEREST RATES

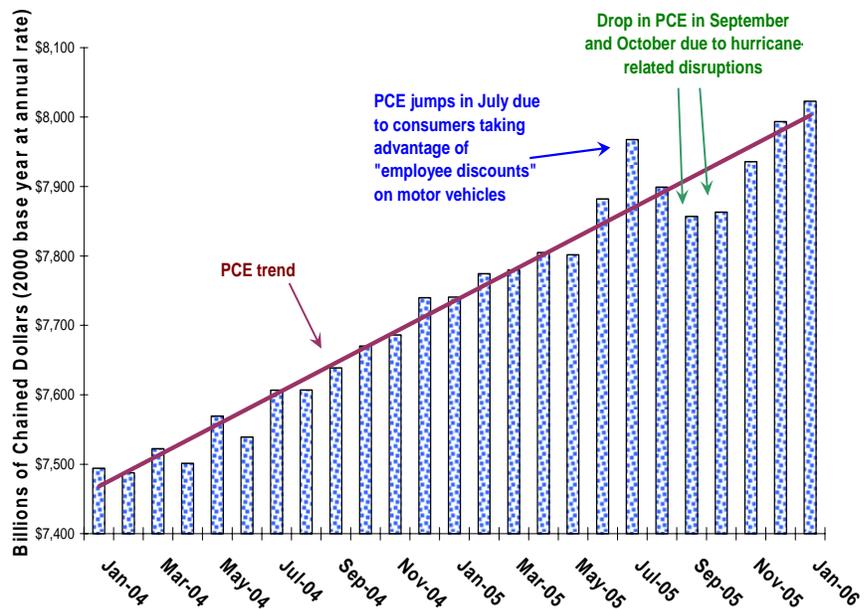
On January 31, the Federal Reserve raised the federal funds rate to 4.5%. The prime rate, moving in lockstep, increased to 7.5%.

From October of 2005 through February, long-term Treasury interest rates were relatively stable. The rate on 10-year Treasury notes moved from an October average of 4.46% to 4.57% in February. The standard 30-year mortgage rate also edged up from an average of 6.07% in October to an average of 6.25% in February.

### INVESTMENT

Fixed nonresidential investment spending decelerated from 8.5% in the third quarter to 5.4% in the fourth quarter of 2005. New orders for non-defense capital goods, excluding volatile orders for aircraft, continued to be positive, increasing 2.9% in the fourth quarter. In January 2006, new

## Real Personal Consumption Expenditures



orders for non-defense capital goods, excluding aircraft, increased 7.5% compared to January 2005.

### INFLATION

Core inflation, or the increase in the level of prices that excludes volatile energy and food prices, remains low. Over the twelve-month period ending January 2006, the core personal consumption expenditures price index increased by 1.8%. The PCE index that includes food and energy prices increased by 3.1%. The core Consumer Price Index that excludes food and energy prices rose 2.1% for the twelve-month period ending February 2006.

### CLOSING THOUGHTS

The economy continues to create jobs at a solid rate and has shown itself to be resilient to significant shocks. There is no indication that higher energy costs have passed through to the general price level for the economy as a whole. The Federal Reserve's assessment of the economy in its recent Monetary Policy Report to the Congress is upbeat: "The U.S. economy should continue to perform well in 2006 and 2007."