



# JOINT ECONOMIC COMMITTEE

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## RECENT ECONOMIC DEVELOPMENTS

### Strong Economic Momentum

The unemployment rate continues to fall, manufacturing growth is recovering, and stock prices continue to rally. The decline in the value of the dollar and faster growth abroad should further boost export growth and trim the trade deficit. The pace of housing activity has cooled, but remains extremely robust. Forecasters see strong growth and accelerating job gains ahead.

#### Highlights

- The unemployment rate fell to 5.7% in December (Figure 1).
- Following the remarkable 8.2% annualized growth in gross domestic product in the 3<sup>rd</sup> quarter of 2003, forecasters see robust growth of over 4% in the 4<sup>th</sup> quarter and continued strong growth throughout 2004.
- The U.S. dollar continues to fall against other major currencies, especially the euro.
- Retail sales were healthy during the holiday season.

#### Unemployment Rate Below Previous Peaks 1

(Civilian unemployment rate, SA)



#### The Unemployment Rate Fell but Job Gains Slowed in December

The *unemployment rate* fell to 5.7% in December, far below its summer peak of 6.3%. Both initial and continuing *jobless claims* for unemployment insurance have declined substantially since early May, indicating improving labor market conditions. Over the past five months, *payroll employment* increased by 278,000 jobs, with 1,000 workers added to payrolls in December. The *survey of households*, used to calculate the unemployment rate, shows even stronger job gains in the past five months – 786,000 – continuing the large discrepancies between the two employment surveys.

#### Business Recovery has Solid Momentum

*Industrial production* posted solid gains over the past four months. Further evidence of recovery in manufacturing comes from the *Institute for Supply Management's (ISM) manufacturing index* (Figure 2), which now stands at 66, the highest value in 20 years. The index plunged well below 50 during 2000, indicating an industry in contraction. Since April 2003, however, the index has shot up, indicating strengthening expansion. The ISM index of service sector activity, well above 50, also indicates expansion in services. U.S. businesses and their stockholders enjoyed increased profit growth over the past two quarters. Higher profits along with increased expensing and bonus depreciation from the May 2003 tax relief have helped fuel growth in business investment spending.

#### Retail Sales Stay Strong

There was healthy growth in retail sales during last year's holiday season. Both total sales and non-auto sales were up 6.7% in December 2003 from a year earlier, reflecting continued strong consumer spending and rising consumer confidence.

### Stock Markets Continue to Rally

*Stock indexes* broke their three-year slide with robust gains last year. Since mid-March of last year, stock market wealth has increased by more than \$3 trillion. In 2003 the Dow Jones industrial average gained 25%, the NASDAQ gained 50%, and the Standard & Poor's 500 was up 26%. Gains have continued. So far this year the Dow is up by about 1.25%, the NASDAQ by 5.4%, and the Standard & Poor's by around 1.7%.

### Home Sales Soften, But Remain Strong

*Existing home sales* slipped for the second straight month in November and *new home sales* have been edging down since July. Home sales remain very strong, however, thanks to low mortgage rates. New home sales, for example, ran 6% higher last year than in 2002.

### Energy Costs are Elevated

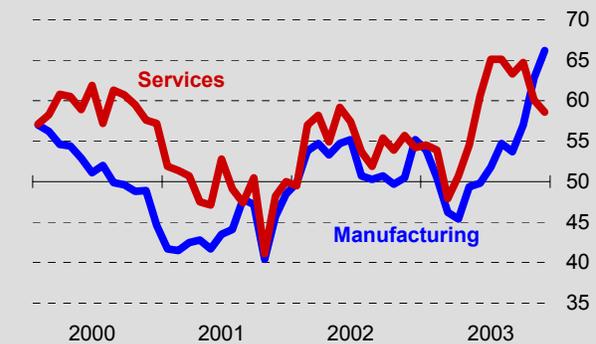
Oil prices are up, hitting \$35 a barrel for the first time since last winter, because of a weakening dollar and fears that U.S. weather will strain the currently low crude oil stocks. OPEC members are reluctant to increase production to moderate prices because oil is sold for dollars and a weaker dollar reduces the purchasing power of their oil revenue. Natural gas prices have increased sharply since late November, partly due to declining North American production and cold weather. Persistently high energy costs could dampen future economic growth.

### International Developments

The *dollar* (Figure 3) fell by close to 3% against the yen since the start of December and over 7% against the euro, hitting all-time lows against the euro. In 2003, the dollar fell 10% against the yen and 17% against the dollar. A weaker dollar makes U.S. exports less expensive in world markets and U.S. imports more expensive. The *trade deficit* narrowed in November as exports rose and imports fell, reflecting adjustments to the weak dollar.

### Business Activity Continues to Increase

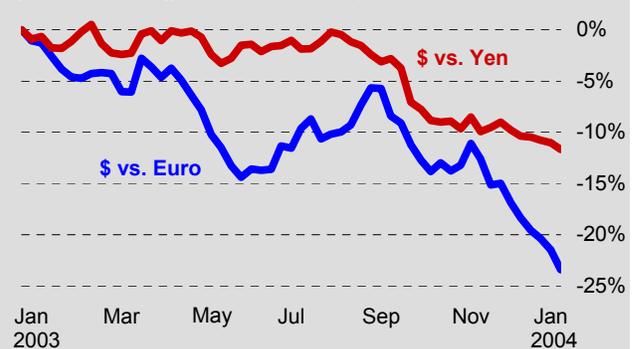
(Reading of 50+ indicates sector expansion)



Source: Institute for Supply Management

### The Dollar Continues to Fall

(Percent change since Jan 2003)



Source: Bureau of Economic Analysis

### Upcoming Indicators

**Federal Reserve** – The Fed's Open Market Committee meets on *January 28* to decide on short-term interest rates. No change in the Fed's target interest rate is expected.

**GDP** – The first estimate of fourth-quarter gross domestic product will be reported on *January 30*. The Blue Chip consensus forecast is for 4.3% growth.

**Employment** – Employment data for January are due *February 6, 2004*, while weekly jobless claims are reported *each Thursday*.