



JOINT ECONOMIC COMMITTEE

CHAIRMAN ROBERT F. BENNETT

RECENT ECONOMIC DEVELOPMENTS

APRIL 29, 2003

Mixed Economic Signals Continue

The economy posted tepid growth in the first quarter. Consumer spending growth slowed, business investment declined, and job losses continued. Rapid developments in Iraq and fickle winter weather have made it difficult to discern underlying economic trends. A key uncertainty is whether positive developments, like declining oil prices and increasing consumer confidence, will provide a sustained lift to the economy. Another uncertainty is future tax policy; many forecasters see a pickup in growth assuming enactment of significant tax relief.

First Quarter GDP:

The “advance” estimate of **Gross Domestic Product** for the first quarter showed sluggish annualized growth of 1.6 percent. Contributions to growth came from consumer spending, residential housing, government spending, and international trade. Weighing negatively on growth were declines in business inventories, lower business investment in equipment and software, and weak investment in commercial and industrial real estate.

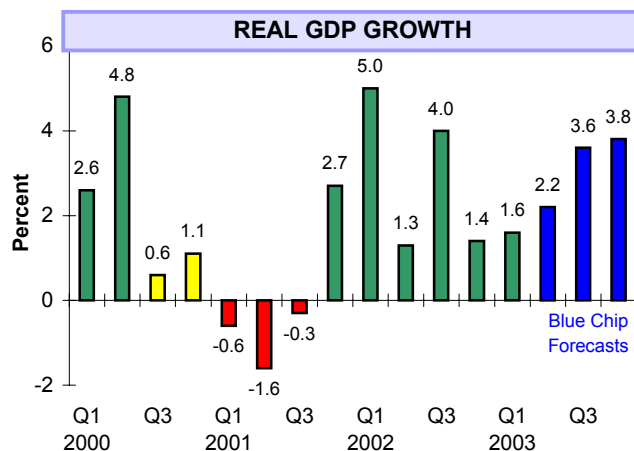
Positive Signals:

Energy Prices have declined significantly, with further declines expected. Oil futures prices signal expected declines below \$25 per barrel by year’s end, a retreat from recent highs above \$35.

Stock Prices have advanced as tensions in the Middle East have subsided and reports of **Corporate Profits** have turned rosier.

Personal Income grew steadily for the eighth consecutive month in March. Consumption also posted healthy growth, and the savings rate edged down to 3.6 percent. Many expect that lower energy prices and future tax relief will help sustain after-tax income and consumer spending growth.

Retail Sales showed strong growth in March, offsetting weather-related losses in February.



Sources: Bureau of Economic Analysis, Blue Chip Economic Indicators

Durable Goods Orders for both defense and non-defense goods also showed strong, broad-based growth in March.

Assisted by low mortgage rates, **Housing Markets** remain robust.

Consumer Confidence shot up in April as the Iraq situation improved, but still remains low.

Signals of Weakness:

Capacity Utilization—use of existing factories and equipment—fell in February and March. March’s utilization rate of 74.8 percent is well below the long-run average of 80 to 81 percent. Excess capacity is a factor behind business reluctance to spend on new factories and equipment.

Industrial Production—manufacturing, mining, and utility output—also fell in February and March.

Payroll Employment has continued to decline; employers shed 108,000 jobs in March and 357,000 in February, with job losses spread across most sectors of the economy. The **Unemployment Rate**, which comes from a different survey, remained at 5.8 percent in March. The unemployment rate has remained relatively flat, despite declines in payroll employment, because some workers have left the labor force and because of increases in self-employment. Unemployment insurance claims have been increasing and are above 400,000, indicating a flat or contracting labor market.

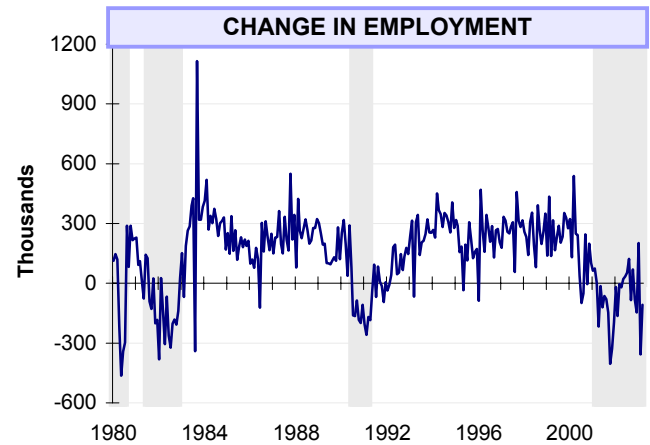
Other Developments:

Inflation spiked up on higher energy prices, but otherwise seems contained. The **Consumer Price Index** and the **Producer Price Index** both advanced significantly in March, but the “core” rates excluding food and energy continue to show little inflationary pressure.

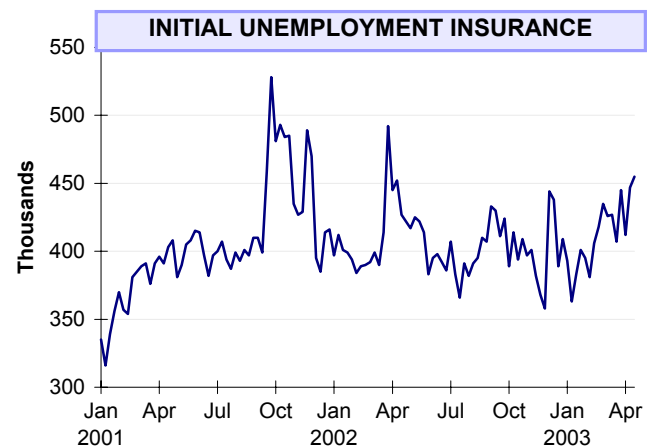
The **Federal Reserve** meets on May 6th to determine short-term interest rates, which remain low. Futures markets assign virtually no chance of a change in rates in May, and only a very small chance through the beginning of autumn. **Interest Rates** facing many businesses remain high relative to rates on relatively less risky Treasury securities.

The **Trade Deficit** edged down in February, as exports grew and imports fell. Global weakness has constrained U.S. growth for years. Despite expectations of recovery, the world economy stalled in 2002 and hasn’t shown signs of a major pickup.

The **IMF**, **OECD**, and **Blue Chip Economic Indicators** have each released recent forecasts showing subnormal growth in 2003, especially the first half, and increases toward more normal growth rates through 2004. Risks to the outlooks include a continued unwinding of the 1990s stock price bubble, global financial imbalances, security concerns, weakness in Japan and Germany, fragile emerging market economies, and SARS.



Source: Bureau of Labor Statistics, nonfarm payroll, seasonally adjusted



Source: Employment Training Administration, seasonally adjusted

A source of strength in the **Blue Chip Consensus Forecast** of U.S. growth is an assumption by many forecasters that significant **Tax Relief** will add to growth in the second half of this year and beyond.

Looking Ahead to May:

- May 1: Productivity for Q1. Strong productivity growth has helped sustain the recovery.
- May 2: April Employment report. Hiring has been noticeably absent in the recovery. While the data come from different sources, recent increases in unemployment claims suggest that the unemployment rate could edge up in April.
- May 6: Federal Reserve meeting. An interest rate change is unlikely, but the Fed’s risk assessment could change.
- May 28: Durable Goods Orders. Looking at orders excluding defense and aircraft will give an indication of whether business investment is rebounding.