

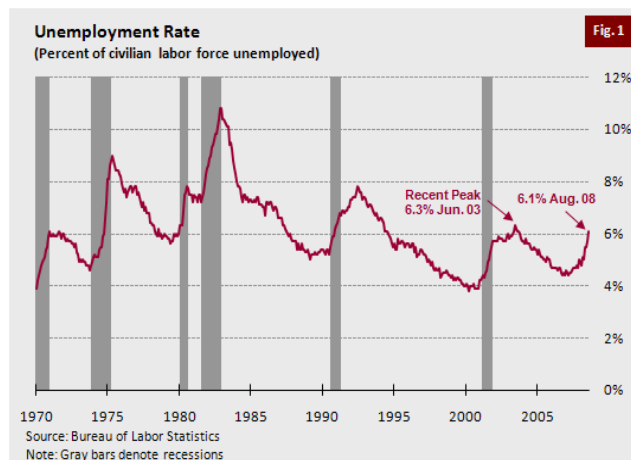
SEPTEMBER 9, 2008

Unemployment and GDP Growth Up; Employment Down; Fannie and Freddie Seized

The unemployment rate rose to 6.1% in August, from 5.7% in July and 5.5% in May and June. Payroll employment declined for the 8th consecutive month in August, by 84,000 jobs. Despite weakness in labor markets, revised data on the inflation-adjusted (real) gross domestic product (GDP) show that growth accelerated in the 2nd quarter. Annualized 2nd-quarter GDP growth was 3.3%, up from 0.9% in the 1st quarter and an annualized 0.2% decline in the 4th quarter of 2007. Growth in the 2nd quarter may have benefited from stimulus-payment effects on consumer spending, but was unambiguously boosted by international trade: net exports contributed 3.1 percentage points to overall 2nd-quarter growth. Residential investment declines continued to weigh on growth. In light of the continued adjustments in the housing sector and financial markets, Treasury placed mortgage giants Fannie Mae and Freddie Mac in conservatorship, giving management control to their regulator, the Federal Housing Finance Agency (FHFA).

Highlights

- The *unemployment rate* rose to 6.1% in August, from 5.7% in July and 5.5% in June and in May (Fig.1).
- Non-farm *payroll employment* declined by 84,000 in August, the 8th consecutive monthly decline (Fig. 2, next page).
- GDP growth in the 2nd quarter was revised up to 3.3%, buoyed by net exports (Fig. 3, next page).
- *Home prices* continue to decline (Fig. 4, next page).
- Treasury placed the Government Sponsored Enterprises *Fannie Mae and Freddie Mac* in FHFA conservatorship, and pledged as much as \$200 billion to the companies.



Unemployment Rises to 6.1%; Eight Consecutive Months of Payroll Job Declines

The *unemployment rate* rose to 6.1% in August, from 5.7% in July and 5.5% in June and May (Fig. 1). *Payroll employment* fell by 84,000 jobs in August (Fig. 2, next page), the 8th consecutive monthly decline; over those eight months, there has been a decline of 605,000 payroll jobs. Reflecting adjustments in the housing sector, employment in the construction industry declined by 8,000 in August and has declined by 564,000 jobs since its recent peak in September 2006.

3.3% Real GDP Growth in the 2nd Quarter

GDP growth was 3.3% in the 2nd quarter and 0.9% in the 1st quarter (Fig. 3, next page). The increase in 2nd quarter GDP primarily reflected consumer spending (up 1.7%—perhaps buoyed by stimulus payments), federal government spending (up 6.8%), state and local government spending (up 2.2%), non-residential structures investment (up 13.7%), and exports (up 13.2%). Imports—a subtraction in calculating GDP—declined by 7.6%. Partly offsetting the factors contributing positively to growth were a decline in residential investment (down 15.7%), the change in inventory investment (which subtracted 1.44 percentage points from the 2nd-quarter change in real GDP), and equipment and software spending (down 3.2%). Residential investment has declined for 10 straight quarters, reducing growth in that period by an average 0.96 percentage point. Over the same period, exports added to growth by an average 1.08 percentage points.

Housing Market Adjustments Continue

On a year-over-year basis, *existing and new home sales* have not risen since November 2005. The inventory of unsold new homes remains elevated at 10 months, above the long-term average of 6 months. There is hope that levels of sales have stabilized, though it is premature to declare a trend. *Home prices* have been falling for at least the past two quarters on a year-over-year basis (some measures show declines beginning in the second half of 2006). *Mortgage delinquency and foreclosure rates* have risen markedly, especially for sub-prime adjustable-rate mortgages, since the beginning of 2006.

Inflation Up; Energy and Commodity Prices Have Eased

Inflation in the core consumer price index (CPI), which excludes volatile energy and food prices, was 2.5% in July, an increase from the near-term low of 2.1% in August 2007. Inflation in the overall CPI was 5.5% in July, up significantly from a 2.9% average last year and a near-term low of 1.9% in August 2007. Part of the recent acceleration in CPI inflation reflects rapid energy price increases: year-over-year inflation in the CPI energy component averaged 20.4% this year through July and was 29.3% in July, in contrast to average growth of 5.8% in 2007. Growth in the price of a barrel of West Texas Intermediate crude averaged close to 80% in the first eight months of this year, though the spot price has fallen in recent trading weeks from over \$145 to below \$110. Gasoline prices have also retreated, from record highs above \$4.16 per gallon in the weeks ending July 7 and July 14 to \$3.70 in the week ending September 8. Commodity prices generally, too, have eased recently: growth in the All Commodities Spot Price Index from the Commodity Research Bureau was 9.8% in August, down from an average 17.6% in the first eight months of this year and an average 19.3% in 2007.

Fed Expected to Hold Short-Term Rates Steady

Markets expect the Fed to keep its target overnight interest rate steady at 2.0% at its monetary policy meeting on September 16. The expectation for continued policy ease reflects ongoing adjustments in housing and financial markets along with concern about economic weakness. However, the Fed continues to note upside risks to inflation.

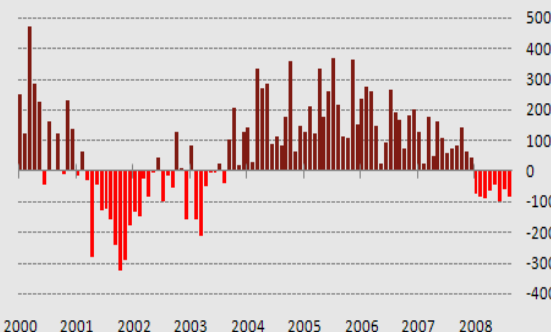
Treasury Places Fannie and Freddie in Conservatorship

The Treasury Department announced plans on September 7 to put Government Sponsored Enterprises Fannie Mae and Freddie Mac under conservatorship, giving management control to their regulator, the FHFA. Treasury will acquire \$1 billion of preferred shares in each company and pledged to provide as much as \$200 billion to the companies as they deal with losses from mortgage defaults. More details on the conservatorship are in the Joint Economic Committee's September 9 report titled "Fannie Mae and Freddie Mac Placed in FHFA Conservatorship."

Payroll Employment Since 2000

(Change in employment, in thousands)

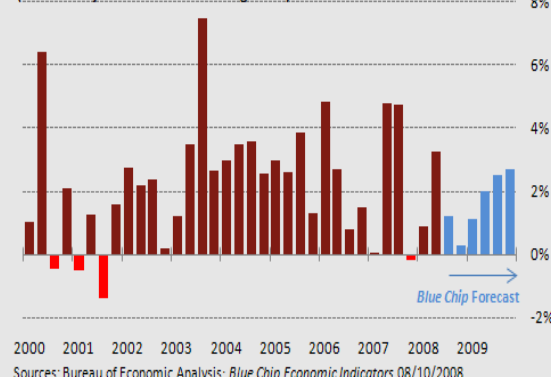
Fig. 2



Economic Growth Since 2000

(Inflation-adjusted annualized GDP growth)

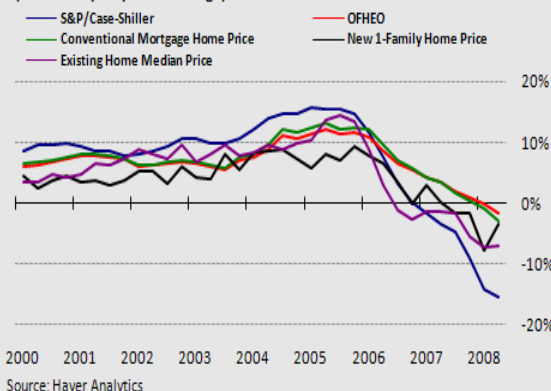
Fig. 3



Home Prices

(Year-over-year percent change)

Fig. 4



Upcoming Indicators

Federal Reserve – The Fed's next policy meeting is scheduled for *September 16*.

Inflation – The Consumer Price Index for August is scheduled for release on *September 16*.

GDP – The final estimate of 2nd quarter GDP growth is scheduled for release on *September 26*.

Employment – The Bureau of Labor Statistics reports September's employment situation on *October 3*.