JOINT ECONOMIC COMMITTEE

CHAIRMAN ROBERT F. BENNETT

RECENT ECONOMIC DEVELOPMENTS

APRIL 6, 2004

A Surge in Job Growth

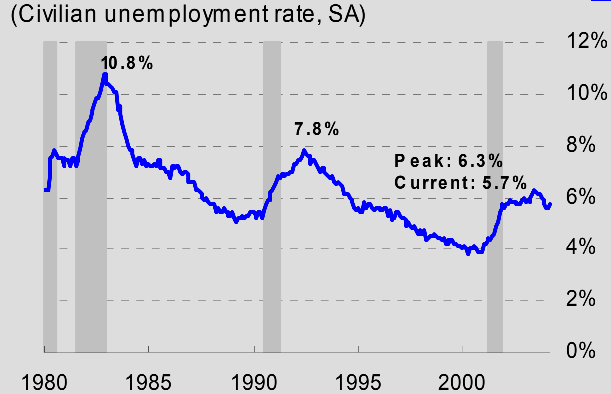
Employment growth surged in March as the economy continues its brisk expansion. Activity in manufacturing and service industries remains strong, profits and cash flows continue to improve, business confidence and spending have been on the rise, and job growth is accelerating. Households continue to benefit from tax relief and low interest rates. Short-term interest rates were kept at multi-decade lows by the Federal Reserve in light of very low inflation. Rapid increases this year in energy and industrial commodity prices have not inflated prices of most producer or consumer goods. Forecasters see rapid, sustained growth of GDP this year and continued job growth.

Highlights

- Payroll employment increased by 308,000 jobs in March. The unemployment rate edged up to 5.7% (Figure 1).
- The final estimate of 4th quarter GDP kept growth at a robust 4.1% annual rate. Blue Chip forecasts are for GDP to grow 4.7% in 2004, the highest in 20 years.
- Corporate profits grew at a 7.2% annual pace in the 4th quarter. Growth in profits has been very strong in the past three quarters.

Unemployment Rate Below Previous Peaks 1

(Civilian unemployment rate, SA)



Source: Bureau of Labor Statistics   Gray bars denote recessions

Job Gains Accelerated in March

Payroll employment rose by 308,000 jobs in March, the seventh straight month of job gains and the largest monthly gain in four years. The past seven months added 759,000 jobs to U.S. payrolls. Manufacturing payrolls were unchanged in March, following 43 months of job losses. The *unemployment rate* edged up to 5.7% in March from 5.6%, but remains well below its recent peak of 6.3% last June. The *household survey*, used to calculate the unemployment rate, showed slight job losses in March, but job gains of 978,000 over the last seven months. The four-week moving averages of *initial and continuing jobless claims*, "tracking polls" that smooth out week-to-week fluctuations, have fallen well below last summer's levels and to a new post-recession low.

Business Investment and Profits Continue to Grow

Profits from current production increased 18.3% in 2003, following an increase of 17.4% in 2002. Strong growth in profits increases tax revenue and helps fuel growth in hiring and investment. After years of declines, business investment rebounded in the past three quarters; annualized growth in business investment averaged close to 14% in the last half of 2003 (Figure 2, next page).

Business Activity Remains Strong

The *Institute for Supply Management's (ISM) index of manufacturing activity* has been above 60 for five months, indicating vigorous expansion. Expansion in services is also vigorous. The *ISM services index* was above 60 in March for the seventh time in the last nine months.

Energy and Raw Commodity Prices are Elevated

Energy and many other commodity prices have risen sharply this year (Figure 3). *Gasoline prices* have risen to multi-year dollar highs and are expected to stay high through the summer driving season. Crude *steel prices* have risen because of increases in prices of steelmaking materials, and coke shortages have restrained some production. Reflecting China's appetite for raw materials, overseas *shipping rates* have also risen substantially this year.

Crude oil prices hit a 13-year peak of over $38 per barrel in mid-March, but have recently retreated to around $36. *OPEC* agreed to reduce its output target, but many doubt whether members will comply, as futures markets see lower oil prices by the end of the year. *Natural gas prices* remain elevated despite the end of the high-demand winter heating season.

The Federal Reserve Keeps Policy Steady

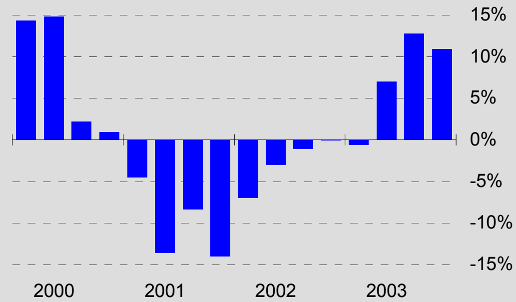
Increases in raw material and energy prices have not passed through to prices of most consumer or producer goods. Given low overall inflation, the *Federal Reserve* remains "patient" in removing its policy of accommodating economic growth through low interest rates. The Fed kept its target short-term interest rate at a 45-year low of 1% at its March meeting.

March Erases Earlier Stock Gains

Declines in major stock market indexes in March took away gains registered earlier this year. The *Dow, Nasdaq,* and *Standard & Poor's (S&P) 500* indexes fell in March because of concerns about terrorism after the bombing in Spain and weak employment data at the time. The *10-year Treasury note* yield also fell in March to below 4%, but has since risen following the report of March's strong job gains. Last year, the Dow rose 25%, the S&P 500 rose 26%, and the Nasdaq was up 50%. Those equity gains and increased housing wealth have helped push overall household wealth up to a record high.

Business Investment Rebounding 2

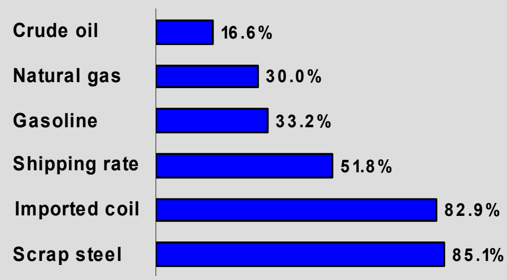
(Non-residential fixed investment, SAAR)



Source: Bureau of Economic Analysis

Some Prices Have Accelerated 3

Percent change since October 2003



Source: Bloomberg LP

Upcoming Indicators

GDP – The first look at GDP growth for the 1st quarter arrives *April 29*. Forecasts are for annualized growth above 4%.

Employment – The Bureau of Labor Statistics reports April's employment situation on *May 7*. Jobless claims data arrive every Thursday.

Inflation – The Producer Price Index is scheduled to be released *April 8*, and the Consumer Price Index follows on *April 14*. The data should show a continuation of very low inflation.

Federal Reserve – The Fed meets *May 4* to decide about short-term interest rates. No change in policy is expected.