

Prefatory Note

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Part 2

October 24, 2007

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

October 24, 2007

Recent Developments

Domestic Nonfinancial Developments

Domestic Nonfinancial Developments

Overall economic activity appears to have advanced at a solid pace in the third quarter. Despite the turbulence in credit markets and the further deterioration in the housing market, consumer outlays picked up after posting a weak showing in the second quarter, and business outlays for both equipment and structures seem to have remained reasonably strong. In particular, consumer goods spending was well maintained in August and September, and orders and shipments for capital goods trended up through August. The one notable locus of weakness was in residential investment, where the ongoing slump intensified, at least partly because of problems in nonconforming mortgage markets. In the labor market, private payroll growth decelerated from its first-half pace. After registering elevated rates during the first half of the year, top-line inflation eased over the past several months because of falling energy prices; core inflation continued to be moderate.

Labor Market Developments

Employment decelerated in the third quarter. Private payrolls increased at an average monthly rate of 74,000, about 40,000 per month less than in the first half of the year. Employment in residential construction, manufacturing, and industries related to mortgage lending continued to decline, whereas most service industries added jobs at a moderate pace. With employment growth slowing and the workweek flat, aggregate hours of private production and nonsupervisory workers increased at an annual rate of 1.2 percent in the third quarter, down from the 2.1 pace recorded in the previous quarter.¹

On balance, other indicators of labor demand do not suggest as much softening as is indicated by the payroll survey. The pace of layoffs appears to have held steady thus far, according to such indicators as initial claims for unemployment insurance, layoffs as reported in the JOLT survey, layoff announcements as compiled from press reports, and the short-term job losers rate from the household survey. Indicators of hiring—hires as reported in the JOLT survey and hiring plans in surveys by Manpower and the National Federation of Independent Businesses (NFIB)—have stepped down recently but remain

¹ With the September employment report, the Bureau of Labor Statistics announced its preliminary estimate of the annual benchmark revision that will be published with the January 2008 employment report. For March 2007, the preliminary benchmark revision for total private employment is -217,000 (-0.2 percentage point). By industry, the largest downward revisions are expected in manufacturing, leisure and hospitality, and financial activities. Construction employment is expected to be virtually unrevised (-8,000). Thus, the surprising resilience of reported payrolls in the construction sector in the face of the sharp downturn in residential construction activity is not expected to be revised away by the upcoming benchmark. The downward revision to private employment growth implies that, to a first approximation, productivity growth over the four quarters ending in 2007:Q1 will be revised up 0.2 percentage point, to about 0.6 percent.

Changes in Employment

(Thousands of employees; seasonally adjusted)

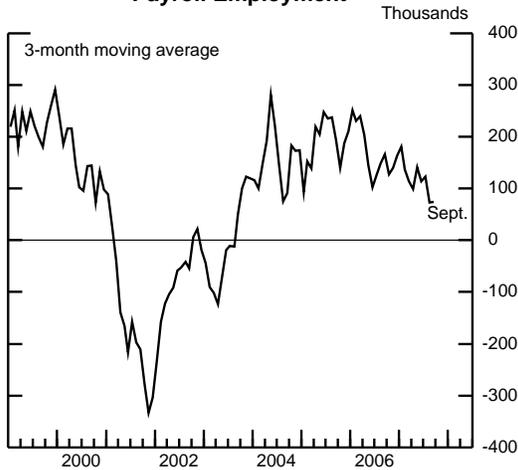
Measure and sector	2006	2007					
		Q1	Q2	Q3	July	Aug.	Sept.
	Average monthly change			Monthly change			
Nonfarm payroll employment (establishment survey)	189	142	126	97	93	89	110
Private	169	115	114	74	117	32	73
Natural resources and mining	5	3	2	2	5	3	-1
Manufacturing	-7	-14	-13	-22	-4	-45	-18
Construction	11	3	-9	-17	-16	-22	-14
Wholesale trade	11	2	15	7	9	5	7
Retail trade	-3	27	-7	3	7	9	-5
Transportation and utilities	9	2	1	8	9	4	11
Information	2	4	2	2	-2	-3	11
Financial activities	16	2	5	-4	16	-14	-14
Professional and business services	42	14	17	21	25	18	21
Temporary help services	-1	-7	-11	-13	-10	-10	-20
Nonbusiness services ¹	83	71	100	74	69	77	75
Total government	20	28	12	23	-24	57	37
Total employment (household survey)	262	109	-38	39	-30	-316	463
Memo:							
Aggregate hours of private production workers (percent change) ²	2.5	1.1	2.1	1.2	-.1	.1	.1
Average workweek (hours) ³	33.8	33.8	33.8	33.8	33.8	33.8	33.8
Manufacturing (hours)	41.1	41.0	41.2	41.4	41.3	41.4	41.4

1. Nonbusiness services comprises education and health, leisure and hospitality, and "other."

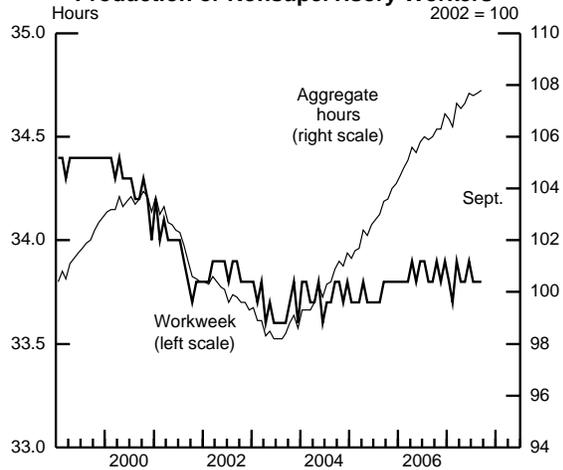
2. Establishment survey. Annual data are percent changes from Q4 to Q4. Quarterly data are percent changes from preceding quarter at an annual rate. Monthly data are percent changes from preceding month.

3. Establishment survey.

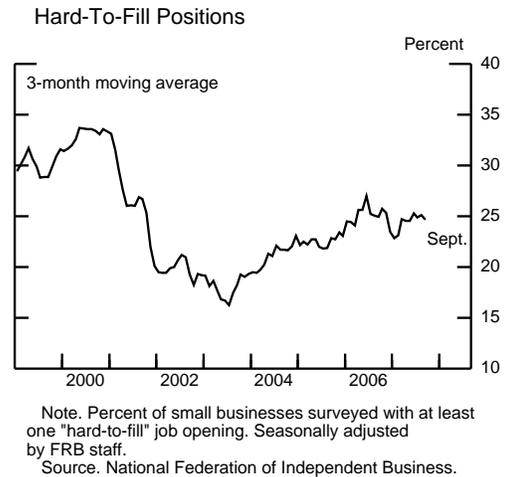
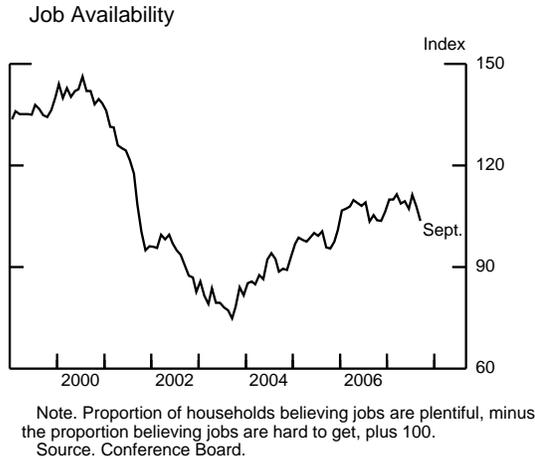
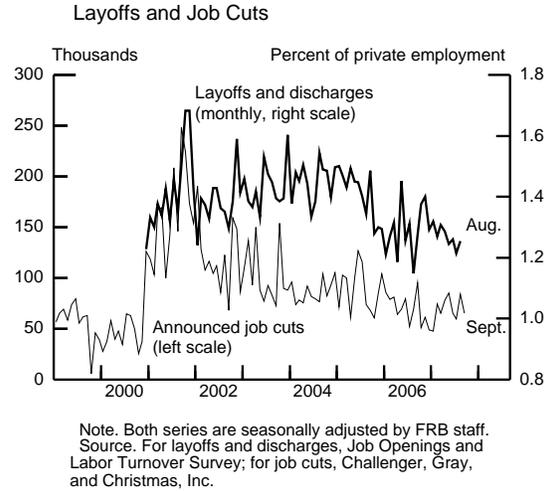
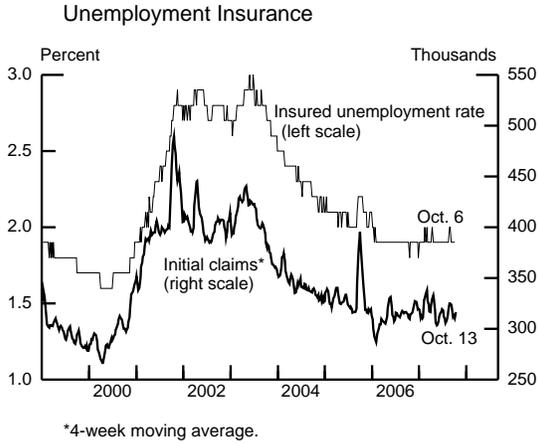
Changes in Private Payroll Employment



Aggregate Hours and Workweek of Production or Nonsupervisory Workers



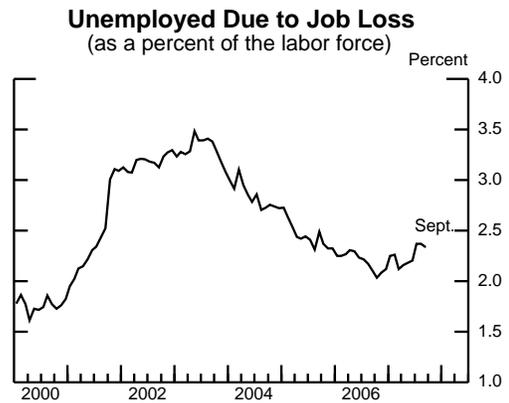
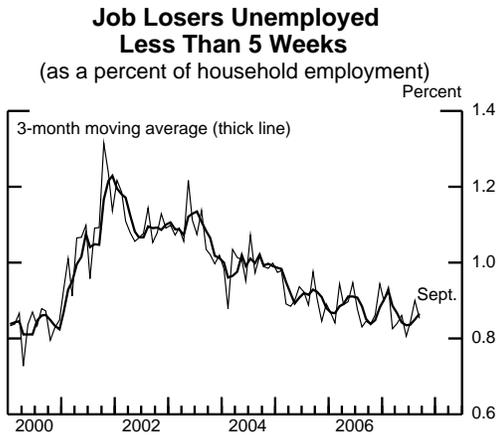
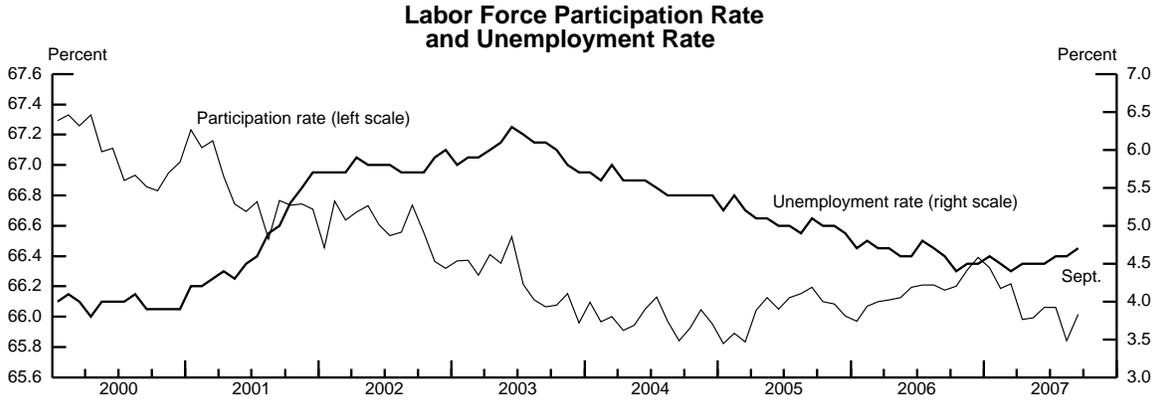
Labor Market Indicators



Selected Unemployment and Labor Force Participation Rates

(Percent; seasonally adjusted)

Rate and group	2006	2007					
		Q1	Q2	Q3	July	Aug.	Sept.
<i>Civilian unemployment rate</i>							
Total	4.6	4.5	4.5	4.7	4.6	4.6	4.7
Teenagers	15.4	14.8	15.6	15.7	15.2	16.1	16.0
20-24 years old	8.2	7.7	7.7	8.5	8.5	8.3	8.9
Men, 25 years and older	3.5	3.6	3.5	3.6	3.6	3.6	3.6
Women, 25 years and older	3.7	3.5	3.5	3.7	3.7	3.7	3.6
<i>Labor force participation rate</i>							
Total	66.2	66.2	66.0	66.0	66.1	65.8	66.0
Teenagers	43.6	42.2	41.5	40.7	41.2	39.7	41.2
20-24 years old	74.6	75.1	74.2	74.5	74.6	74.0	75.0
Men, 25 years and older	75.5	75.7	75.6	75.5	75.6	75.5	75.5
Women, 25 years and older	59.6	59.6	59.6	59.8	59.8	59.8	59.8



Selected Components of Industrial Production
(Percent change from preceding comparable period)

Component	Proportion 2006 (percent)	2006 ¹	2007		2007		
			Q2	Q3	July	Aug.	Sept.
			Annual rate		Monthly rate		
Total	100.0	3.5	3.5	4.0	.6	.0	.1
Previous	100.0	3.5	3.5	...	.5	.2	...
Manufacturing	81.9	3.4	4.3	4.0	.8	-4	.1
Ex. motor veh. and parts	76.3	3.9	3.7	4.2	.8	-3	.3
Ex. high-tech industries	71.5	2.5	2.9	2.7	.6	-4	.3
Mining	8.6	8.0	.1	3.6	1.0	-6	.2
Utilities	9.6	.3	-1.0	5.0	-9	4.6	-1
<i>Selected industries</i>							
Energy	20.5	4.0	-1.4	5.4	.1	2.0	.1
High technology	4.8	24.6	16.6	28.2	3.5	1.0	.4
Computers	1.2	12.1	39.4	12.9	.3	.6	.9
Communications equipment	1.1	14.8	8.3	13.6	1.0	1.7	.8
Semiconductors ²	2.6	34.8	9.5	45.2	6.4	.9	-1
Motor vehicles and parts	5.5	-3.8	13.3	.4	.7	-1.6	-3.3
<i>Total ex. selected industries</i>	69.1	2.4	3.2	2.4	.6	-4	.3
Consumer goods	20.9	1.8	1.8	1.6	.7	-6	.1
Durables	4.0	-1.9	4.1	2.0	.3	-5	-1
Nondurables	16.9	2.7	1.2	1.4	.7	-6	.1
Business equipment	7.8	10.2	4.4	6.3	1.4	-7	.6
Defense and space equipment	1.7	2.0	-2.4	4.9	.1	-2	.3
Construction supplies	4.5	-2.2	5.6	1.9	-2	-2	-2
Business supplies	7.9	1.0	1.2	-1	.0	-3	.5
Materials	26.1	2.3	4.6	2.5	.6	-4	.4
Durables	14.5	2.0	6.1	4.4	.9	-3	.4
Nondurables	11.6	2.6	2.7	.2	.3	-5	.3

1. From fourth quarter of preceding year to fourth quarter of year shown.

2. Includes related electronic components.

... Not applicable.

Capacity Utilization
(Percent of capacity)

Sector	1972- 2006 average	1994- 95 high	2001- 02 low	2007				
				Q1	Q2	Q3	Aug.	Sept.
Total industry	81.0	85.1	73.6	81.3	81.7	82.1	82.1	82.1
Manufacturing	79.8	84.6	71.6	79.8	80.3	80.6	80.5	80.4
Ex. motor veh. and parts	79.9	84.3	71.4	80.3	80.5	80.9	80.7	80.8
Mining	87.4	88.9	84.8	90.0	89.9	90.7	90.4	90.6
Utilities	86.7	93.7	83.8	86.4	85.8	86.6	88.0	87.8
<i>Stage-of-process groups</i>								
Crude	86.5	89.5	82.0	88.7	89.2	90.0	89.7	90.3
Primary and semifinished	82.2	88.2	74.6	82.2	82.2	82.7	82.9	82.7
Finished	77.8	80.5	70.0	78.0	78.6	78.9	78.7	78.6

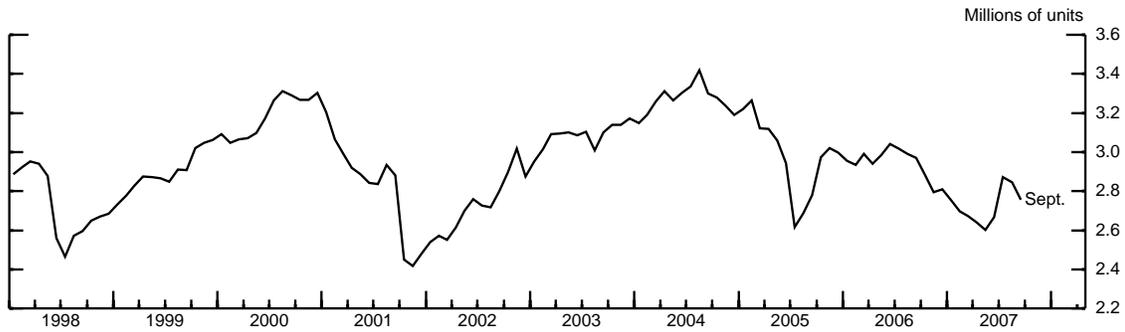
Production of Domestic Light Vehicles
(Millions of units at an annual rate except as noted)

Item	2007							
	Q1	Q2	Q3	Q4	Sept.	Oct.	Nov.	Dec.
U.S. production ¹	10.2	10.8	10.6	10.1	10.1	10.0	10.4	9.9
Autos	4.0	3.9	3.9	3.6	3.6	3.7	3.7	3.4
Light trucks	6.3	6.9	6.7	6.5	6.5	6.2	6.7	6.5
Days' supply ²	65	67	69	n.a.	68	n.a.	n.a.	n.a.
Autos	60	55	60	n.a.	59	n.a.	n.a.	n.a.
Light trucks	69	75	75	n.a.	74	n.a.	n.a.	n.a.
Inventories ³	2.67	2.67	2.76	n.a.	2.76	n.a.	n.a.	n.a.
Autos	1.00	.95	.99	n.a.	.99	n.a.	n.a.	n.a.
Light trucks	1.67	1.72	1.76	n.a.	1.76	n.a.	n.a.	n.a.
Memo: U.S. production, total motor vehicles ⁴	10.6	11.1	10.9	10.4	10.4	10.2	10.7	10.2

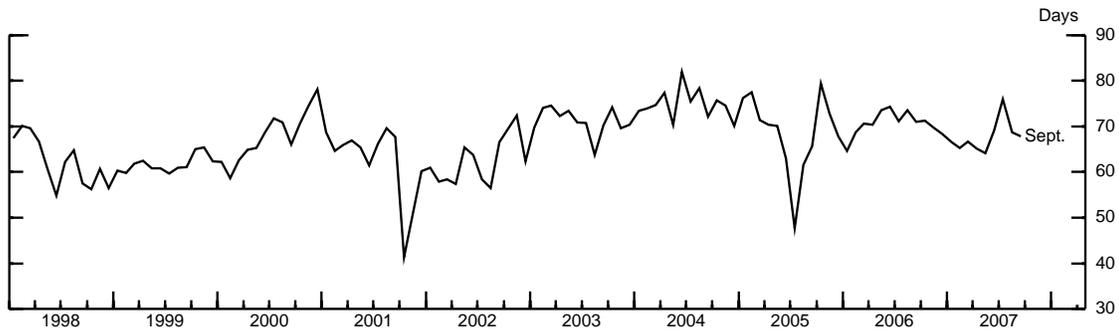
Note. FRB seasonals. Components may not sum to totals because of rounding.

1. Production rates in the fourth quarter reflect the latest industry schedules.
 2. Quarterly values are calculated with end-of-period stocks and average reported sales.
 3. End-of-period stocks.
 4. Includes medium and heavy trucks.
- n.a. Not available.

Inventories of Light Vehicles



Days' Supply of Light Vehicles



at healthy levels. Measures of labor market tightness—the share of firms reporting to the NFIB that they had a hard-to-fill position and households’ assessments of job availability according to the Conference Board—suggest that little has changed in the balance between supply and demand since the beginning of 2007.

In the household survey, the unemployment rate ticked up 0.1 percentage point in September to 4.7 percent, and the labor force participation rate bounced back to 66.0 percent following a drop in August. The movements in the participation rate in August and September were probably due to the late date of the August survey this year—late enough for a larger-than-normal number of students to have already headed back to school.

Industrial Production

After solid advances in June and July, industrial production (IP) changed little in August and September. Manufacturing output fell back 0.4 percent in August and edged up 0.1 percent in September but, on the strength of large increases in June and July, rose at an annual rate of about 4 percent for the third quarter as a whole. This advance was about the same as in the second quarter, as greater strength in high-technology industries offset weakness in motor vehicles and parts. Overall, manufacturing production appears poised for modest gains in the near term, although the decline in homebuilding will continue to be a drag on output of construction supplies and products.

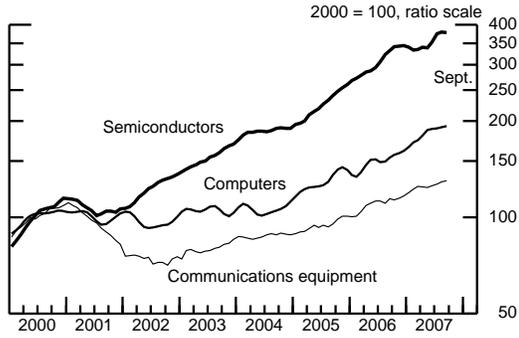
In September, production of light motor vehicles tumbled 600,000 units to an annual rate of 10.1 million units. About half of the decline reflected losses from a two-day strike at General Motors.² For the third quarter as a whole, light vehicle production averaged 10.6 million units (annual rate), down a bit from the second-quarter pace but still well above the assembly rates recorded earlier this year. Inventories of light vehicles fell sharply in September, but inventories appear to remain above desired levels at Chrysler and Ford. Plans for the fourth quarter call for assemblies at a rate of 10.1 million units. Elsewhere in transportation equipment, Boeing recently announced it would delay by six months its initial deliveries of the 787 Dreamliner, which should damp production during the first half of 2008.

High-technology output decelerated in August and September, but overall the third quarter came in with an above-average gain of nearly 30 percent at an annual rate. The first half of 2007 witnessed a surge in computer production resulting from demand for

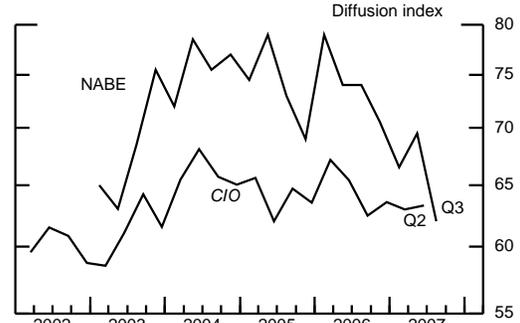
² The staff estimates that GM lost 310,000 units (annual rate) in September because of the strike. The brief strike at Chrysler appears to have had no significant effect on production.

Indicators of High-Tech Manufacturing Activity

Industrial Production in the High-Tech Sector

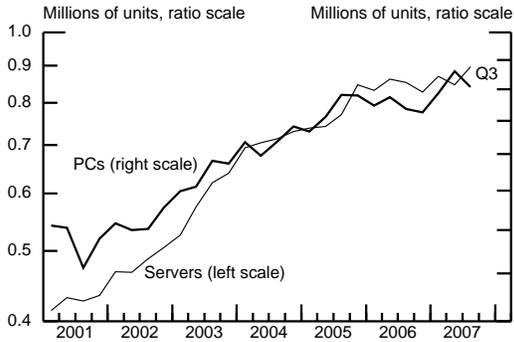


Surveys of High-Tech Spending Plans



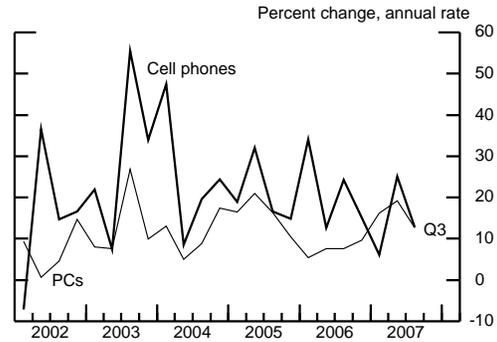
Note. Indexes are based on responses to survey questions about whether firms plan to increase or decrease their spending on various categories of high-tech goods in the next 12 months.
Source. C/O magazine and NABE Industry Survey.

U.S. Personal Computer and Server Sales



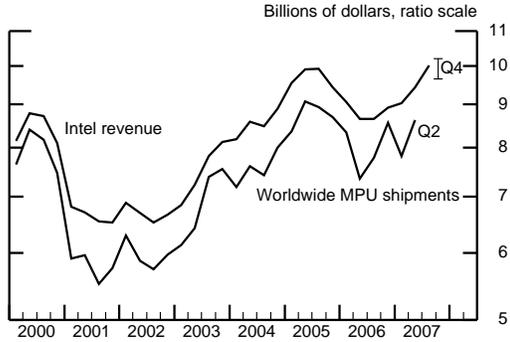
Note. FRB seasonals.
Source. Gartner.

Worldwide Unit Sales of Personal Computers and of Cell Phones



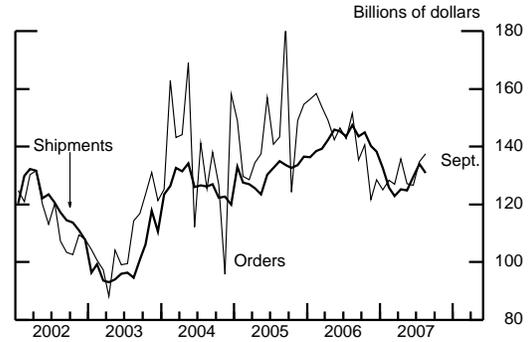
Note. FRB seasonals. Q3 worldwide cell phone sales is based upon Q3 reports from Nokia and Sony Ericsson.
Source. Gartner.

MPU Shipments and Intel Revenue



Note. FRB seasonals. Q4 Intel revenue is the range of the company's guidance as of October 16, 2007.
Source. Intel and Semiconductor Industry Association.

IPC Circuit Board Orders and Shipments



Note. US and Canadian bare and loaded circuit board shipments.

high-end servers and computers capable of running Microsoft's newest operating system. In the third quarter, preliminary data from Gartner indicate that unit sales of servers increased, but unit sales of personal computers fell slightly, held back by lower consumer demand. Output of communications equipment continued to rise at a healthy pace in September.

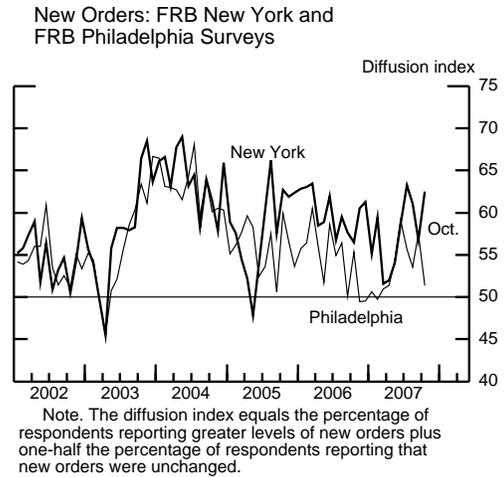
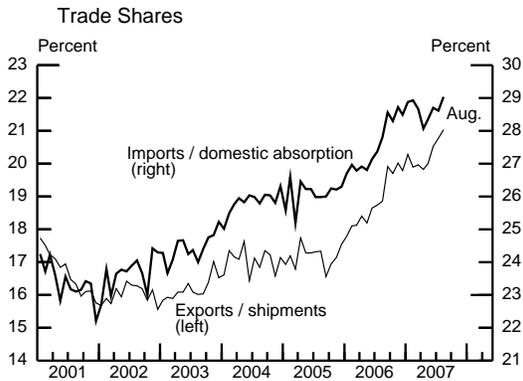
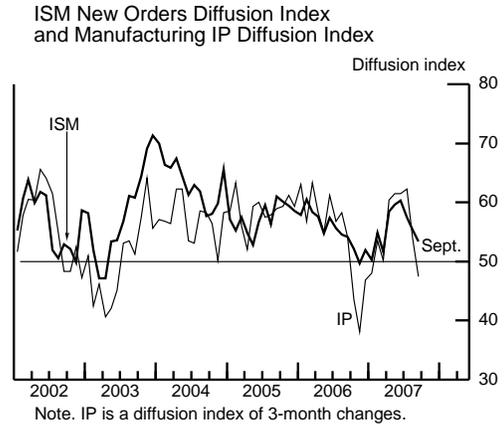
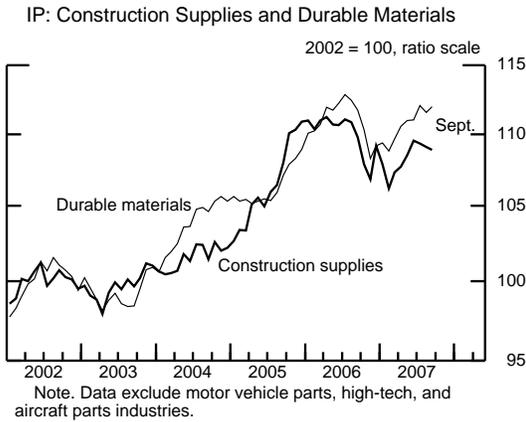
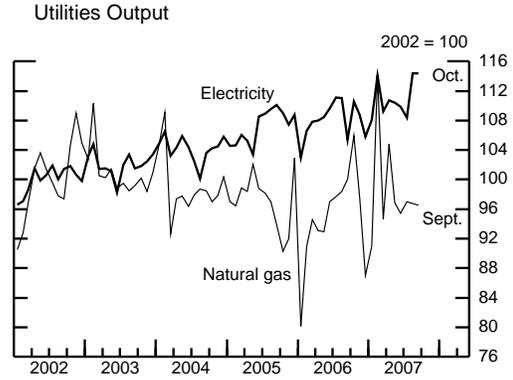
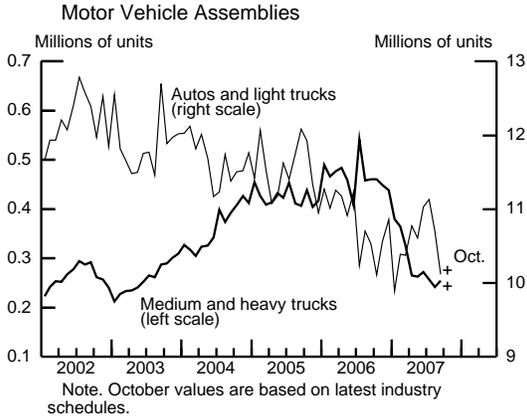
After a surge in June and July, semiconductor production decelerated in August and edged down in September, as downstream demand at manufacturers of PCs and cell phones slowed. Intel's revenue guidance dipped for the fourth quarter, consistent with a slight pullback in the output of MPUs. Meanwhile, domestic production of circuit boards has risen in recent months, and the book-to-bill ratio for this industry has been above 1 for most of the year, pointing to further gains in production of high-end equipment in coming months. Among other near-term indicators, the National Association for Business Economics (NABE) survey of business plans for spending on high-tech equipment over the next 12 months deteriorated in the third quarter, suggesting that future capital spending plans for high-technology products may be damped some by the current financial stress, especially in the finance, insurance, and real estate category.³

Excluding the production of energy, motor vehicles and parts, and high-tech products, manufacturing output rose 0.3 percent in September, nearly reversing a drop in August. Increases in production of medical equipment and business supplies were particularly strong in September. In contrast, the index for construction supplies declined for the third consecutive month, after increasing briskly during the second quarter when the output of products associated with nonresidential construction posted large increases. The recent weakness in construction supplies was widespread and likely driven by the ongoing plunge in residential investment. Production of both durable and nondurable materials rose in September, but the level of production was little changed from July.

Looking forward, a subdued pace of motor vehicle assemblies and the ongoing contraction in residential construction will likely prove a drag on the output of a variety of materials-related industries, such as primary metals, plastics, and rubber products. Some weakness is already evident, as the three-month IP diffusion index has moved down for two consecutive months. The Institute for Supply Management (ISM) new orders diffusion index also moved down in September, and the New York and Philadelphia Federal Reserve Banks' new orders indexes were mixed in October. All three indexes, however, remain consistent with continued modest gains in the near term.

³ *CIO* magazine's Tech Poll, which provided information on IT spending projections, was discontinued in October.

Indicators of Industrial Activity



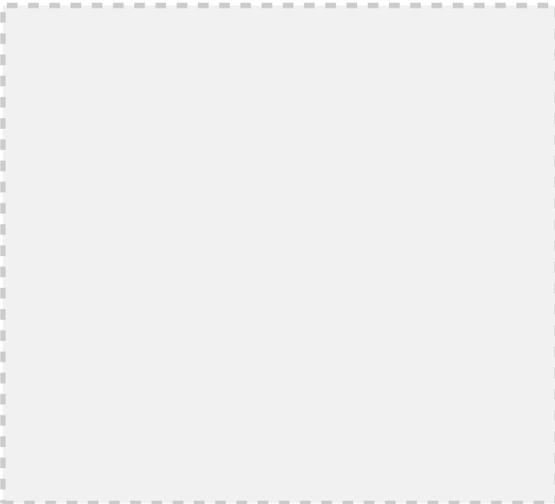
Sales of Light Vehicles
(Millions of units at an annual rate; FRB seasonals)

Category	2006	2007					
		Q1	Q2	Q3	July	Aug.	Sept.
Total	16.5	16.4	16.0	15.9	15.2	16.2	16.2
Autos	7.8	7.6	7.7	7.3	7.2	7.4	7.5
Light trucks	8.7	8.9	8.4	8.5	8.0	8.8	8.7
North American ¹	12.8	12.6	12.3	12.3	11.6	12.7	12.5
Autos	5.4	5.1	5.3	5.1	4.9	5.1	5.2
Light trucks	7.4	7.4	7.0	7.2	6.7	7.6	7.3
Foreign-produced	3.7	3.9	3.8	3.6	3.6	3.5	3.7
Autos	2.3	2.4	2.4	2.3	2.3	2.2	2.3
Light trucks	1.3	1.4	1.4	1.3	1.3	1.3	1.4
Memo: Detroit Three domestic market share (percent) ²	53.7	52.1	51.8	50.4	48.3	51.9	50.8

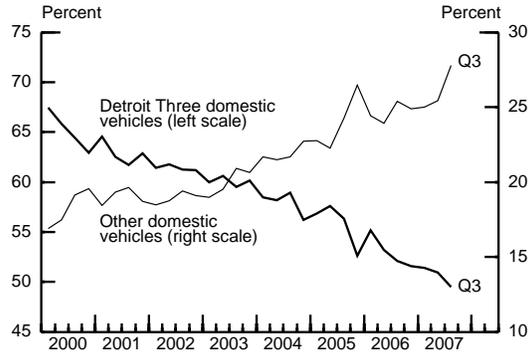
Note. Components may not sum to totals because of rounding.

1. Excludes some vehicles produced in Canada that are classified as imports by the industry.
2. Domestic market share excludes sales of foreign brands affiliated with the Detroit Three.

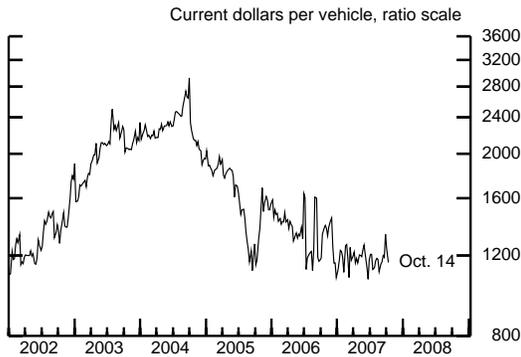
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Market Share

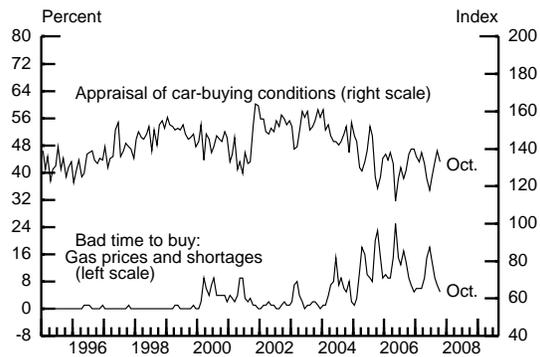


Average Value of Incentives on Light Vehicles



Note. Weighted average of customer cash rebate and the present value of interest rate reduction. Data are seasonally adjusted.
Source. J.D. Power and Associates.

Car-Buying Attitudes



Source. Reuters/University of Michigan Survey.

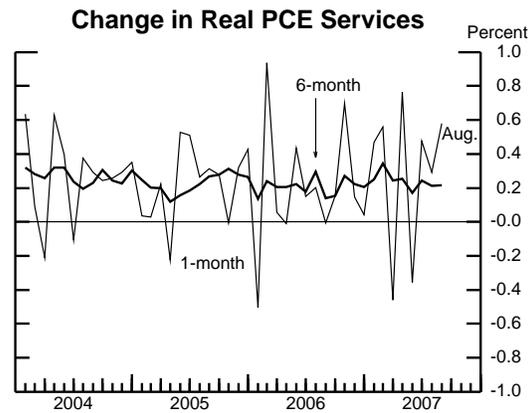
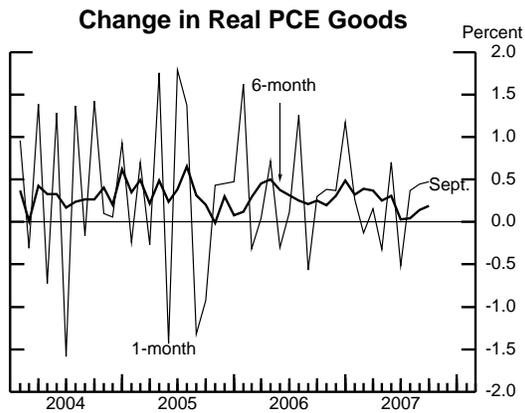
Retail and Food Services Sales

(Percent change from preceding period; seasonally adjusted current dollars)

Category	2007					
	Q1	Q2	Q3	July	Aug.	Sept.
	Annual rate			Monthly rate		
Total sales	6.3	5.4	4.0	.6	.3	.6
Retail control ¹	7.7	8.0	4.6	.7	-.3	.5
Ex. sales at gasoline stations	5.5	5.4	5.8	.8	.0	.3
Memo:						
Real PCE control ²	4.0	.3	4.5	.8	.2	.3

1. Total sales less outlays at building material and supply stores and automobile and other motor vehicle dealers.

2. Total goods spending excluding autos and trucks. The values for July and August are staff estimates. The values for September and Q3 are staff forecasts.



Note. The values for July and August are staff estimates. The value for September is a staff forecast.

Personal Saving Rate



Foreign demand has continued to support manufacturing output, and the ratio of exports to shipments remained on its upward trajectory in August. Last, few inventory overhangs are apparent, and the inventory-shipments ratio derived from the staff's flow-of-goods system continues to trend downward.

Motor Vehicles

After having slowed in June and July, demand for motor vehicles has rebounded more recently despite little change in overall incentive spending; automobiles and light trucks sold at an annual rate of 16.2 million units in both August and September. Over the first 20 days of October, unit sales of the major Japanese nameplates—which represent more than one-third of total sales—were running only a bit below their brisk September rate. To date, the recent turbulence in credit markets does not appear to be disrupting motor vehicle financing or sales.

The Reuters/Michigan index of car-buying conditions moved down in early October but remains well above the recent lows that were seen from May through July, when households were particularly concerned about gasoline prices.

Consumer Spending

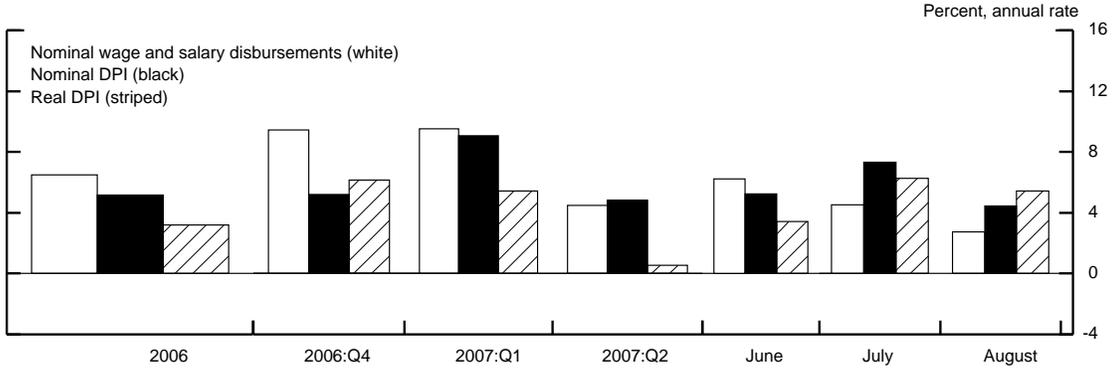
Consumer spending has been well maintained over the past few months. In addition to the aforementioned improvement in motor vehicle sales in August and September, real spending on other goods posted solid gains in both months. Real outlays for consumer services rose a strong 0.6 percent in August (the latest available data), in part because of an estimated rise in spending on brokerage services and a weather-induced jump in energy services; services spending likely moderated in September as the weather turned more seasonable. All told, we estimate that total real PCE increased at an annual rate of about 3¼ percent in the third quarter.

Gains in real income were robust over the summer, the result of solid increases in nominal wages and salaries and very low headline inflation. Furthermore, the latest readings on average hourly earnings and prices point to strong gains in real wages and salaries in September.

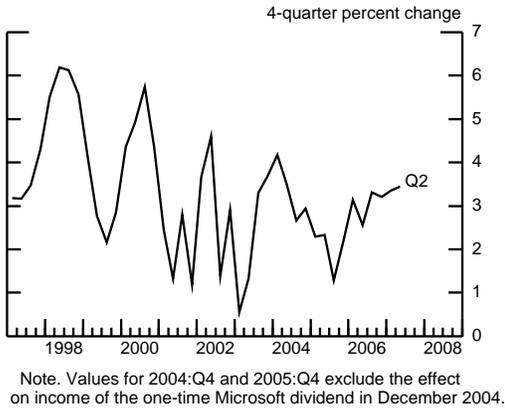
Other factors affecting consumer spending have been mixed. The recent drop in short-term interest rates should help boost spending by bolstering households' expectations for future economic growth and perhaps by lowering borrowing costs, and the stock market has risen, on balance, since August. However, house prices have continued to decelerate, and the turmoil in financial markets that began in August is likely exerting some restraint on consumer spending; since mid-summer, standards on consumer and mortgage credit

Fundamentals of Household Spending

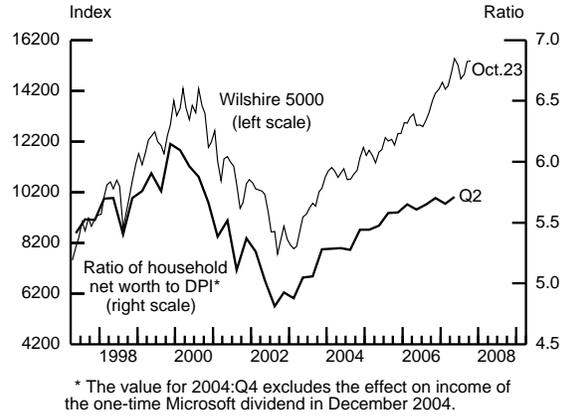
Changes in Nominal Wages and Salaries, Nominal DPI, and Real DPI



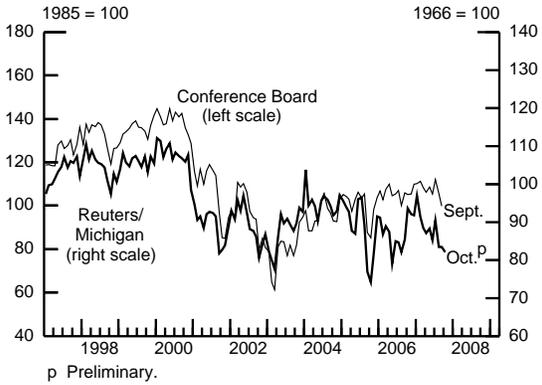
Change in Real DPI



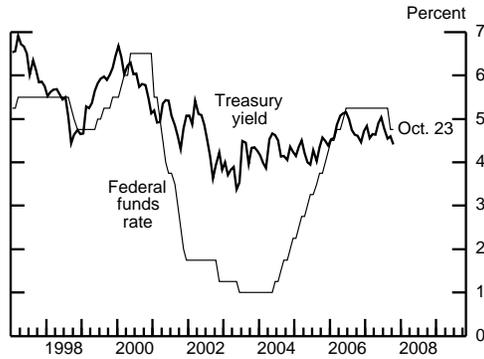
Household Net Worth and Wilshire 5000



Consumer Confidence



Federal Funds Rate and 10-Year Treasury Yield



have tightened. In addition, consumer confidence, as measured by both the Reuters/Michigan and the Conference Board surveys, is down relative to readings from July despite the recent goods news on inflation, the labor market, and stock prices.

With real income having risen somewhat more slowly than real PCE in August, the saving rate edged down to 0.7 percent. More generally, however, the saving rate has been rising from the low levels of the summer of 2006.

Housing

As was anticipated, the housing downturn appears to be deepening. Sales of existing single-family homes dropped a cumulative 12½ percent during August and September, and new home sales slid 8¼ percent in August (not at annual rates). The deterioration in nonprime mortgage markets and the higher rates and tighter lending conditions for prime-rate jumbo loans have exacerbated the worsening conditions in housing markets. Nonprime mortgage originations (which include the subprime and alt-A categories) have slowed to a trickle since mid-summer, and, although spreads between rates for prime-rate jumbo and conforming thirty-year fixed-rate mortgages have narrowed a bit in recent weeks, they are still 40 basis points wider than the 25 basis point spread that prevailed on average since 2001. Moreover, even though rates for thirty-year fixed-rate conforming mortgages have moved down of late, they are still about 20 basis points above their average level over the first four months of this year.

Other indicators point to a further slowing in housing demand in the near term. The index of pending sales agreements—which tends to lead sales of single-family existing homes by one to two months—slid 6½ percent in August on the heels of July’s decline of 11 percent.⁴ In these two months, pending sales were down in all regions of the country, with the largest cumulative declines in the West and Northeast—regions where average home prices are higher and where nonconforming mortgages tend to be more prevalent.

⁴ On a contrary note, the four-week moving average of the Mortgage Bankers Association’s mortgage purchase index (not shown) still stands well above its mid-April level. However, this net increase is likely misleading for two reasons. First, the purchase index does not sample loan applications taken by mortgage brokers, who issue the overwhelming majority of nonprime loans. Second, the index measures mortgage applications rather than approvals; because mortgage lending standards have tightened this year for many borrowers, a smaller proportion of these applications are likely to have been approved than previously, and some borrowers may be applying to more lenders for a given loan.

Private Housing Activity

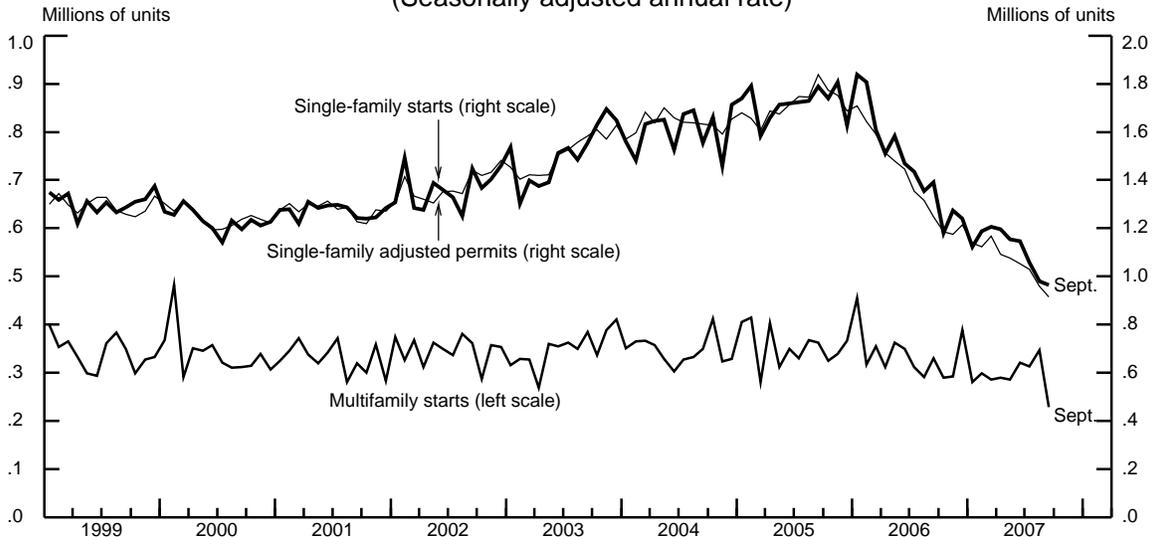
(Millions of units, seasonally adjusted; annual rate except as noted)

Sector	2006	2007					
		Q1	Q2	Q3	July	Aug.	Sept.
<i>All units</i>							
Starts	1.80	1.46	1.46	1.30	1.37	1.33	1.19
Permits	1.84	1.56	1.46	1.31	1.39	1.32	1.23
<i>Single-family units</i>							
Starts	1.47	1.17	1.17	1.00	1.06	.98	.96
Permits	1.38	1.12	1.05	.94	1.01	.93	.87
Adjusted permits ¹	1.41	1.14	1.07	.97	1.03	.96	.92
Permit backlog ²	.133	.132	.116	.112	.115	.115	.112
<i>New homes</i>							
Sales	1.05	.85	.87	n.a.	.87	.80	n.a.
Months' supply ³	6.36	7.64	7.53	n.a.	7.43	7.98	n.a.
<i>Existing homes</i>							
Sales	5.68	5.63	5.15	4.72	5.00	4.79	4.38
Months' supply ³	6.35	7.12	8.34	9.26	8.75	8.95	10.07
<i>Multifamily units</i>							
Starts	.336	.288	.298	.296	.313	.347	.228
Permits	.461	.440	.411	.375	.381	.388	.358
Permit backlog ²	.062	.076	.081	.076	.081	.077	.076
<i>Mobile homes</i>							
Shipments	.117	.094	.099	n.a.	.099	.097	n.a.
<i>Condos and co-ops</i>							
Existing home sales	.801	.790	.767	.700	.750	.690	.660

1. Adjusted permits equal permit issuance plus total starts outside of permit-issuing areas.
 2. Number outstanding at end of period. Excludes permits that have expired or have been canceled, abandoned, or revoked. Not at an annual rate.
 3. At current sales rate; expressed as the ratio of seasonally adjusted inventories to seasonally adjusted sales. Quarterly and annual figures are averages of monthly figures.
- n.a. Not available.

Private Housing Starts and Permits

(Seasonally adjusted annual rate)



Note. Adjusted permits equal permit issuance plus total starts outside of permit-issuing areas.

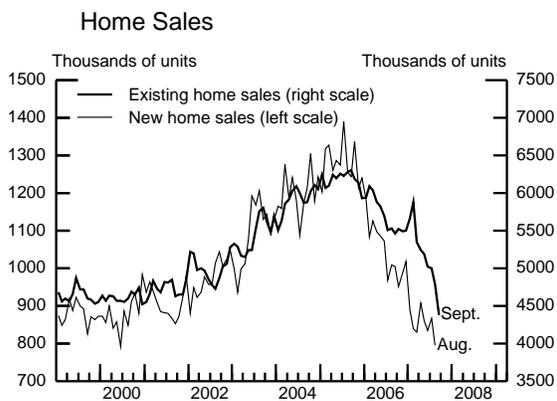
Indeed, anecdotes from many builders suggest that a lack of buyer confidence will significantly restrain new housing demand for the rest of this year.

After having held production roughly steady over the first half of this year, homebuilders are once again making significant cuts. In September, single-family housing starts moved down another 1¾ percent, to an annual rate of 963,000 units, after declining a cumulative 15 percent during July and August. Meanwhile, adjusted single-family permit issuance—generally a useful indicator of future starts—continued along the steep downward trajectory that began about two years ago. Yet, because of sagging sales, builders are making only limited progress at paring down their bloated inventories. In August, the months' supply of unsold new homes remained at about 8 months, approximately 65 percent above the upper end of the fairly tight range it had occupied between 1997 and the summer of 2005.

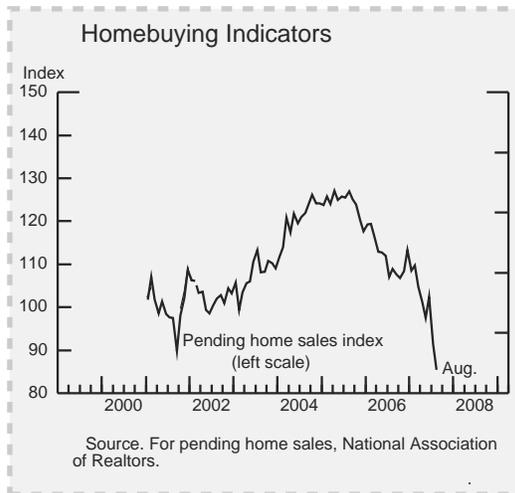
. Multifamily starts declined sharply in September, but the third-quarter reading remained within the fairly narrow range in which this series has fluctuated over the past ten years.

Little new information on house prices has become available since the time of the September Greenbook. The latest-available reading for the purchase-only version of the repeat-sales price index calculated by the Office of Federal Housing Enterprise Oversight (OFHEO) shows that prices were 2¾ percent higher in the second quarter than a year earlier, well below the 8¼ percent increase posted over the preceding four-quarter period. The ten-city version of the Case-Shiller repeat-sales price index—which is more heavily concentrated in urban areas that had seen larger appreciations in earlier years—shows an outright decline of 4½ percent over the twelve-month period ending in July. The average price of existing homes sold—which is available on a more timely basis than these other

Indicators of Single-Family Housing



Source. For existing homes, National Association of Realtors; for new homes, Census Bureau.



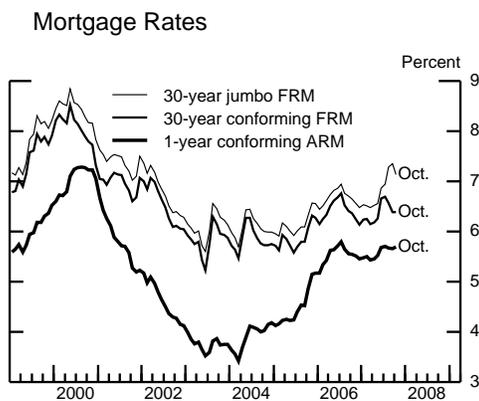
Source. For pending home sales, National Association of Realtors.

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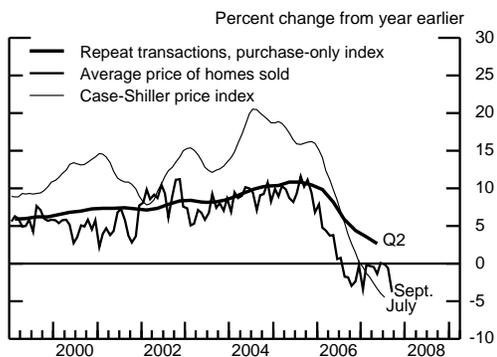


Note. Months' supply is calculated using the 3-month moving average of sales.
Source. for months' supply, Census Bureau.



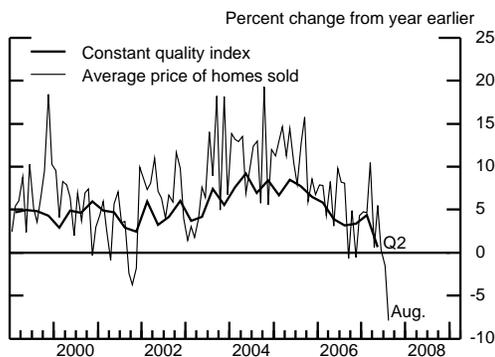
Note. The Oct. readings are for data through Oct. 17, 2007.
Source. Conforming rates are from Freddie Mac. The jumbo rate is the sum of the 30-year conforming FRM rate and the jumbo conforming spread from bankrate.com.

Prices of Existing Homes



Note. The Case-Shiller price index is the 10-city index.
Source. For repeat transactions, OFHEO; for average price, National Association of Realtors; for Case-Shiller, Chicago Mercantile Exchange.

Prices of New Homes



Note. Average price values have been adjusted by Board staff to take into account new sampling procedures adopted in 2005.
Source. Census Bureau.

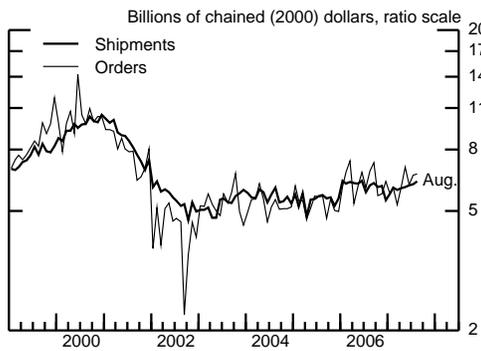
Orders and Shipments of Nondefense Capital Goods

(Percent change; seasonally adjusted current dollars)

Category	2007				
	Q1	Q2	June	July	Aug.
	Annual rate		Monthly rate		
Shipments	-8.8	9.7	-.5	1.0	.8
Excluding aircraft	-11.1	9.6	-.8	.0	1.0
Computers and peripherals	16.2	11.9	-7.6	-15.1	9.5
Communications equipment	2.4	12.6	.8	1.0	1.9
All other categories	-14.7	9.0	-.2	1.5	.1
Orders	-18.5	34.2	6.3	4.8	-12.1
Excluding aircraft	-16.2	13.0	-.2	.9	-.5
Computers and peripherals	13.2	7.5	-4.5	-12.1	8.1
Communications equipment	-13.0	64.2	-12.8	7.6	1.1
All other categories	-19.0	9.6	1.8	1.7	-1.5
Memo: Shipments of complete aircraft ¹	46.2	40.2	44.5	42.5	51.3

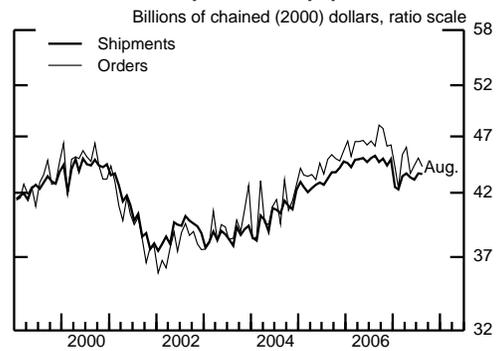
1. From Census Bureau, Current Industrial Reports; billions of dollars, annual rate.

Communications Equipment



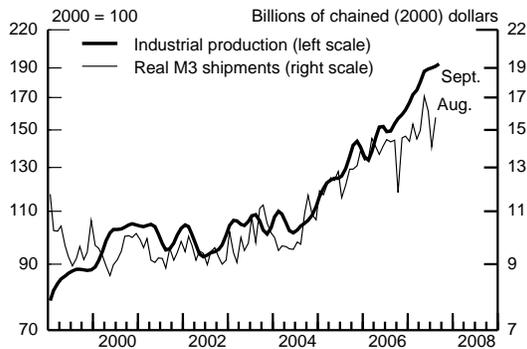
Note. Shipments and orders are deflated by a price index that is derived from the BEA's quality-adjusted price indexes and uses the PPI for communications equipment for monthly interpolation.

Non-High-Tech, Nontransportation Equipment



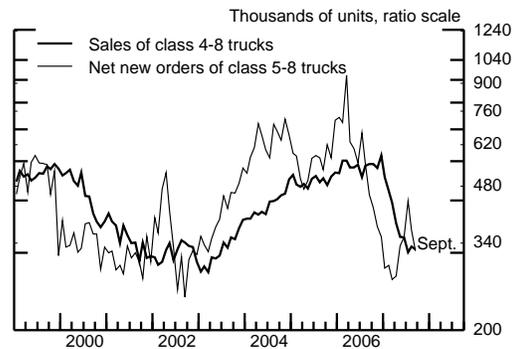
Note. Shipments and orders are deflated by the staff price indexes for the individual equipment types included in this category. Indexes are derived from the BEA's quality-adjusted price indexes.

Computers and Peripherals



Note. Ratio scales. Shipments are deflated by the staff price index for computers and peripheral equipment, which is derived from the BEA's quality-adjusted price indexes.

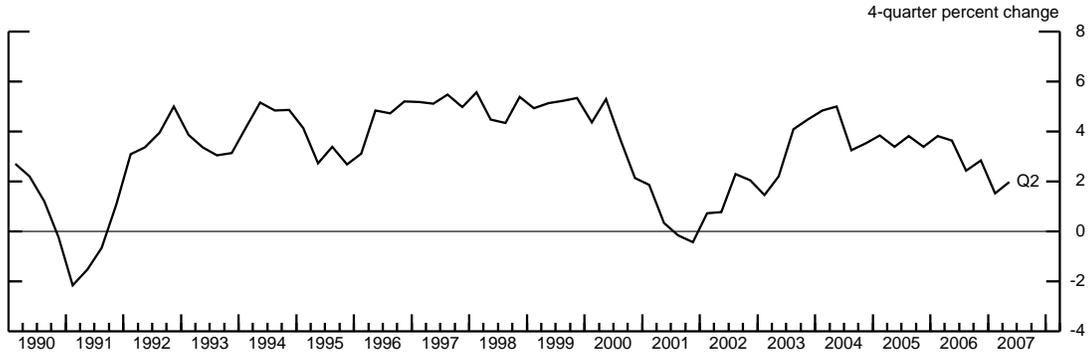
Medium and Heavy Trucks



Note. Annual rate, FRB seasonals. Source. For sales, Ward's Communications; for orders, ACT Research.

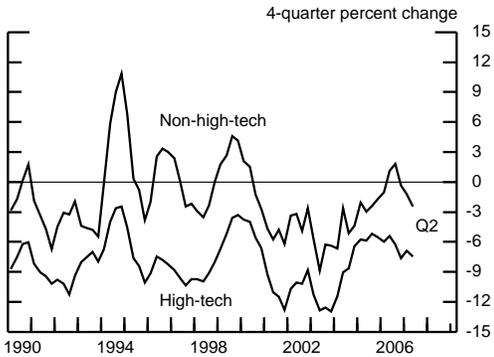
Fundamentals of Equipment and Software Investment

Real Business Output



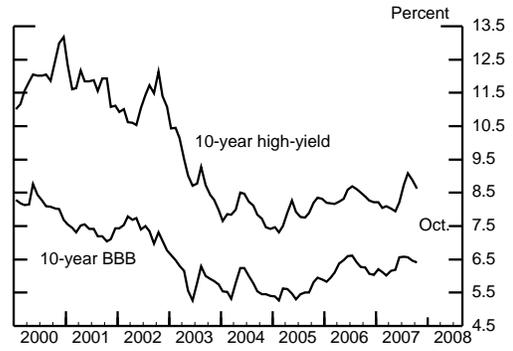
Source. Bureau of Economic Analysis.

User Cost of Capital



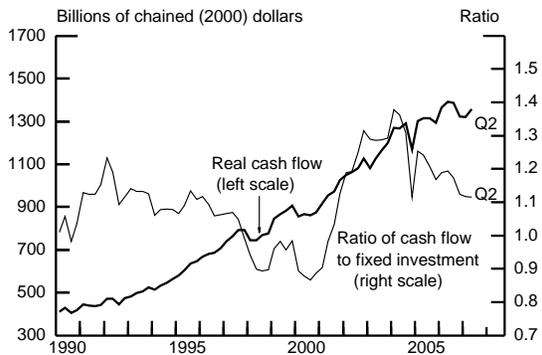
Source. Staff calculation.

Corporate Bond Yields



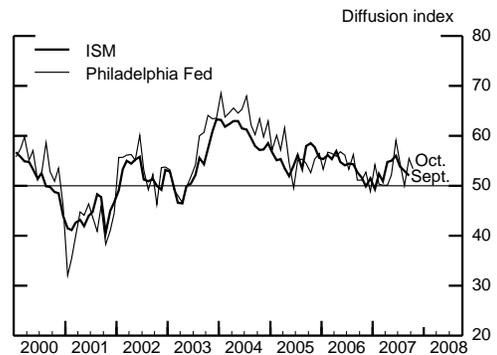
Note. Monthly averages based on Merrill Lynch bond data; Values for October are averages through Oct. 22.

Corporate Cash Flow



Note. Cash flow and fixed investment for the corporate business sector. Source. Bureau of Economic Analysis; FRB flow of funds accounts.

Surveys of Business Conditions



Source. Manufacturing ISM Report on Business; Philadelphia Fed Business Outlook Survey.

measures but often reflects shifts in the mix of homes sold—fell in September relative to year-earlier readings. Average new-home prices had held up fairly well through much of the current downturn, but they plunged in August relative to their year-earlier level. The decline is consistent with mounting anecdotal evidence that many large homebuilders are resorting to price discounts, rather than nonprice incentives, to bolster sales and unload inventory.

Equipment and Software

Real spending on equipment and software (E&S) appears to have increased at a solid pace in the third quarter. Orders and shipments of nondefense capital goods excluding aircraft increased, on average, over July and August. In addition, the drag from falling business purchases of motor vehicles has dissipated. However, anecdotal evidence suggests that this summer's financial market turbulence may be restraining spending in some industries.

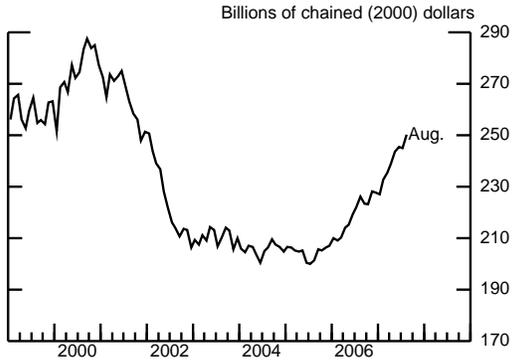
The fundamental determinants of business investment have been mixed. Business output has decelerated over the past year. However, the user cost of capital continued to trend down through the second quarter, and corporate cash flow remained at an elevated level relative to corporate fixed investment. In the summer, financing costs increased amid the turmoil in corporate credit markets, especially for lower-grade borrowers, but these costs receded somewhat in early September. Surveys of business conditions, such as the ISM and Philadelphia Fed manufacturing diffusion indexes and the NABE survey, remain consistent with further near-term gains in spending. However, according to firms contacted by Reserve Banks as part of their Beige Book inquiries, about 20 percent of businesses have revised down their plans for capital spending over the next six to twelve months—and about 7 percent have revised up their capital spending plans—in response to the recent changes in financial conditions. Based on our own discussions with industry contacts and on the third-quarter NABE survey, some of this revision to spending plans appears to be at financial firms, which purchase a good deal of high-tech equipment.

Business spending for the broad category of equipment outside of high-tech and transportation likely increased at a solid rate in the third quarter. Although shipments were flat and orders declined in August, the robust gains in the preceding month left the average value of shipments and orders in the first two months of the third quarter above the second-quarter average.

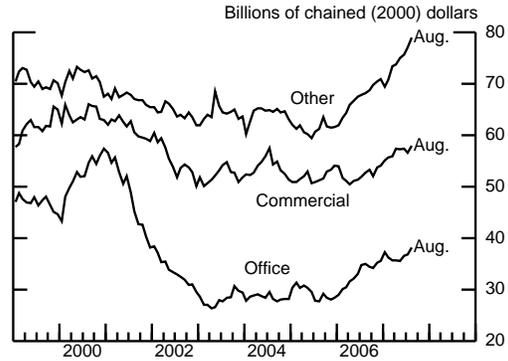
Nonresidential Construction and Indicators

(All spending series are seasonally adjusted at an annual rate; nominal CPIP deflated by BEA prices through Q2 and by staff projection thereafter)

Total Structures

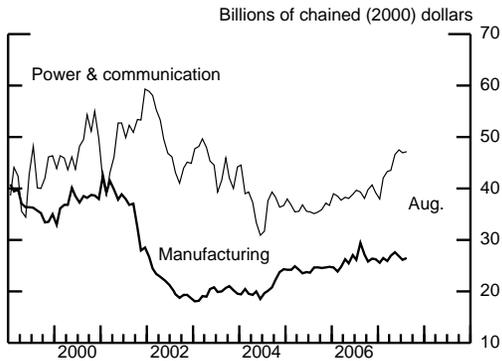


Office, Commercial, and Other

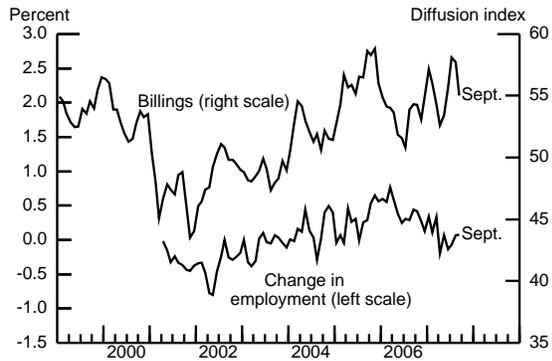


Note. Other includes religious, educational, lodging, amusement and recreation, transportation, and health-care facilities.

Manufacturing and Power & Communication

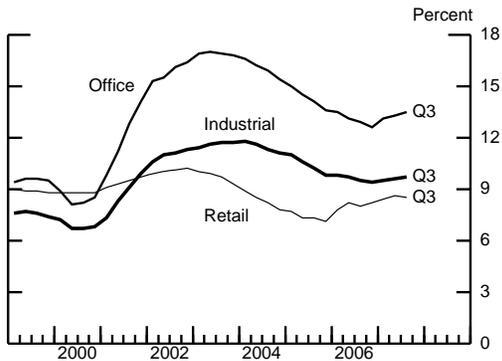


Architectural Billings and Nonresidential Construction Employment



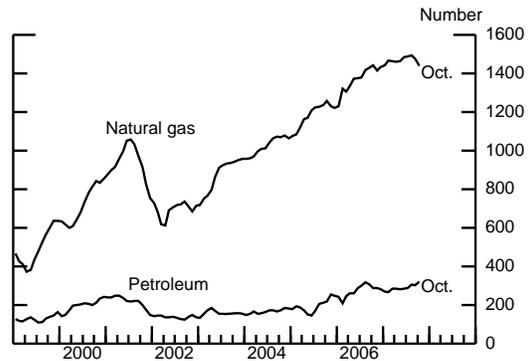
Note. Both series are 3-month moving averages. Employment includes industrial, commercial, and specialty trade construction. Source. For billings, American Institute of Architects; for employment, Bureau of Labor Statistics.

Vacancy Rates



Note. Industrial space includes both manufacturing structures and warehouses. Source. Torto Wheaton Research.

Drilling Rigs in Operation



Note. The October readings are based on data through October 19, 2007. Source. DOE/Baker Hughes.

In the high-tech sector, real business spending on computers and peripherals appears to have risen at a moderate pace in the third quarter. Although industrial production of computers slowed in the third quarter, output for the business market appears to have posted a solid gain. In contrast, business outlays on communications equipment likely rose at a subpar pace in the third quarter, as the fraction of shipments going overseas seems to have risen.

After tumbling sharply over the first half of this year, sales of medium and heavy trucks leveled off in the third quarter at an average annual rate of about 325,000 units per month. The earlier weakness was largely due to payback for purchases pulled forward by the change in engine emissions standards for heavy trucks, but this payback appears to have run its course, and the current levels likely reflect a lower underlying pace of demand.

. Domestic outlays on aircraft have likely stepped down somewhat in the third quarter, with sales to foreign airlines accounting for a higher share of domestic aircraft shipments.

Nonresidential Construction

Available data through August show that nonresidential building activity has remained vigorous on the heels of the sizzling 20 percent (annual rate) spending gain posted in the second quarter. The nonfinancial fundamentals for this sector remain solid, with vacancy rates remaining below their cyclical peaks despite having edged up in recent quarters. Although the recent turbulence in commercial credit markets has somewhat clouded the outlook, anecdotes from general contractors through early October suggest that these developments have done little to slow the pace of commercial construction thus far. That said, the three-month moving average of the architectural billings index—which is reasonably well correlated with construction spending six months hence—has come down noticeably in recent months, hinting that financial turmoil may be hindering construction plans to some extent.

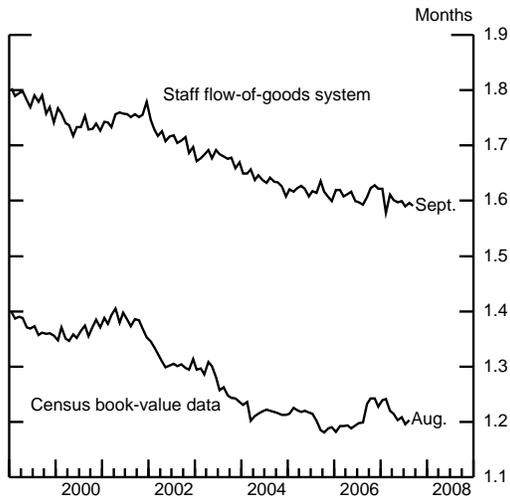
Activity in the drilling and mining sector remains at a high level but does not seem to be increasing as rapidly as previously. Available data through early October show that the number of rigs drilling for natural gas or crude oil has moved up little, on balance, so far this year after four years of robust increases. Measures of footage drilled from the Department of Energy through September (not shown) show modest gains in recent

Nonfarm Inventory Investment
(Billions of dollars; seasonally adjusted annual rate)

Measure and sector	2006	2007				
	Q4	Q1	Q2	June	July	Aug.
<i>Real inventory investment (chained 2000 dollars)</i>						
Total nonfarm business	13.6	-5.8	1.3	n.a.	n.a.	n.a.
Motor vehicles	-16.8	-14.7	-9.6	n.a.	n.a.	n.a.
Nonfarm ex. motor vehicles	30.4	8.9	10.9	n.a.	n.a.	n.a.
Manufacturing and trade ex. wholesale and retail motor vehicles and parts						
Manufacturing	-1.8	-5.0	-4.2	-8.4	-3.9^e	n.a.
Wholesale trade ex. motor vehicles & parts	5.3	4.3	6.5	2.0	13.3 ^e	n.a.
Retail trade ex. motor vehicles & parts	11.3	1.8	8.5	6.1	.7 ^e	n.a.
<i>Book-value inventory investment (current dollars)</i>						
Manufacturing and trade ex. wholesale and retail motor vehicles and parts	39.4	33.9	60.7	35.2	26.0	-13.1
Manufacturing	7.3	4.8	21.6	13.7	7.2	-6.3
Wholesale trade ex. motor vehicles & parts	17.5	22.0	20.6	10.3	13.6	-7.2
Retail trade ex. motor vehicles & parts	14.6	7.2	18.4	11.2	5.2	.4

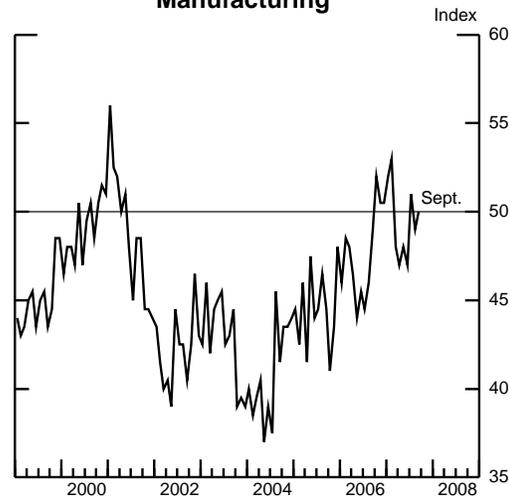
^e Staff estimate of real inventory investment based on revised book-value data.
n.a. Not available.
Source. For real inventory investment, BEA; for book-value data, Census Bureau.

Inventory Ratios ex. Motor Vehicles



Note. Flow-of-goods system covers total industry ex. motor vehicles and parts, and inventories are relative to consumption. Census data cover manufacturing and trade ex. motor vehicles and parts, and inventories are relative to sales.

ISM Customer Inventories: Manufacturing



Note. A number above 50 indicates inventories are "too high."

months.⁶ Looking forward, anecdotes in the Beige Book have improved somewhat of late but suggest that chronic shortages of equipment and key services are boosting costs and restraining new activity. Incentives for further expansion of natural gas drilling—which has propelled much of the recent growth in this sector—also seem to have been damped by lower prices and persistently elevated inventories of natural gas.

Business Inventories

Real nonfarm inventory investment excluding motor vehicles increased at a moderate annual rate of \$11 billion in the second quarter, and the book-value data in hand suggest a small liquidation over the first two months of the third quarter. The ratio of book-value inventories to sales in the manufacturing and trade sector excluding motor vehicles in August remained at a level well below the elevated values seen around the turn of the year. Information from the staff's flow-of-goods system suggests that months' supply of inventories excluding motor vehicles has been little changed for several months. Purchasing managers, on average, viewed the level of their customer's inventories as about right in September, as the ISM customers' inventories index ticked up to 50.

Federal Government Sector

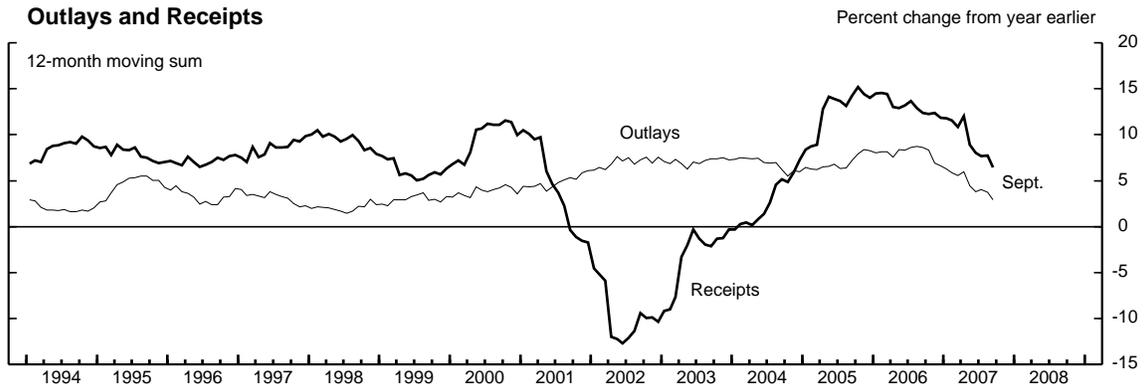
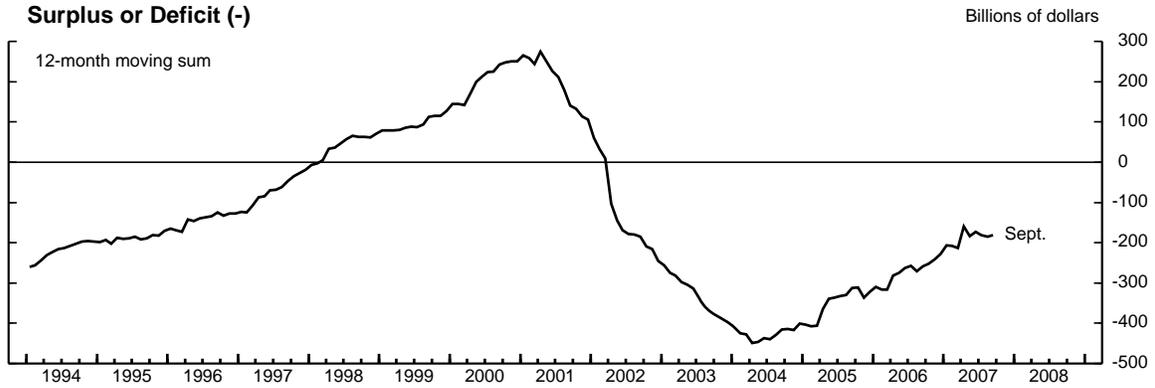
The federal unified budget deficit, which shrunk noticeably early in fiscal year 2007, has leveled off over the past six months as the rate of growth of receipts has slowed markedly. The Treasury reported an unadjusted deficit of \$163 billion for fiscal 2007, which ended in September. The deficit adjusted for payment timing shifts and financial transactions was \$181 billion, or approximately 1¼ percent of GDP, down from 2 percent of GDP a year earlier.⁷

Receipts in the third quarter increased just 3¼ percent relative to their year-earlier level, about half the pace seen for the fiscal year as a whole. The slowdown was mostly due to a decline of 12 percent in corporate income tax collections relative to their level a year earlier, probably reflecting weaker gains in profits as well as volatility in the timing of payments. By contrast, withheld income and payroll taxes in the third quarter rose 6½ percent above their year-earlier level, close to the rate of increase for the fiscal year as a whole.

⁶ The BEA reported that spending on drilling and mining structures jumped at an annual rate of 49 percent in the second quarter, an estimate that is difficult to reconcile with the data cited above for the number of rigs in operation and footage drilled. Our analysis of the historical data suggests that unexplained increases in the level of spending of this nature tend to be reversed, in fairly short order, over subsequent quarters.

⁷ The adjusted measure is larger than the unadjusted one primarily because it excludes the proceeds from sales of the electromagnetic spectrum, which held down the actual (unadjusted) deficit.

Federal Government Budget
 (Unified basis; adjusted for payment-timing shifts and financial transactions; data from Monthly Treasury Statement)



Recent Federal Outlays and Receipts
 (Billions of dollars except as noted)

Function or source	July-September			12 months ending in September		
	2006	2007	Percent change	2006	2007	Percent change
Outlays						
Outlays	656.0	684.1	4.3	2,671.9	2,749.1	2.9
Net interest	57.1	60.6	6.2	226.6	237.9	5.0
National defense	134.7	146.2	8.5	524.4	562.9	7.3
Major transfers ¹	346.0	367.8	6.3	1,428.9	1,517.6	6.2
Other	116.0	108.6	-6.4	461.1	411.0	-10.9
Receipts						
Receipts	602.9	622.3	3.2	2,412.7	2,567.7	6.4
Individual income and payroll taxes	443.6	474.9	7.1	1,836.4	1,987.5	8.2
Corporate income taxes	102.7	90.7	-11.7	353.9	370.2	4.6
Other	56.6	56.7	.2	222.3	209.9	-5.6
Surplus or deficit (-)	-53.1	-61.8	...	-259.2	-181.4	...
Memo:						
Unadjusted surplus or deficit (-)	-41.7	-41.9	...	-248.2	-162.8	...

1. Includes Social Security, Medicare, Medicaid, and income security programs.

... Not applicable.

Outlays (adjusted for payment timing shifts and financial transactions) rose 4¼ percent in the third quarter compared with their year-earlier level. Defense spending increased a brisk 8½ percent relative to the same period a year earlier. These data suggest that real NIPA defense purchases in the third quarter will be substantially above their second quarter level. Outlays for the major transfer programs posted an increase of 6¼ percent from a year ago, in line with the pace seen over the fiscal year. For the fiscal year as a whole, total outlays increased only 3 percent (year over year), the slowest pace since the late 1990s, as payments for certain programs (disaster relief expenditures, agriculture subsidy payments, and student loan subsidies) that were temporarily elevated in fiscal 2006 returned to more normal levels in 2007.

Little progress has been made in completing the fiscal 2008 budget. A continuing resolution is funding the federal government through November 16 while the Congress continues to work on the annual appropriations bills. The House has passed all twelve regular appropriations bills, and the Senate has passed seven that cover 90 percent of discretionary spending, but none of them have yet been enacted.

State and Local Government Sector

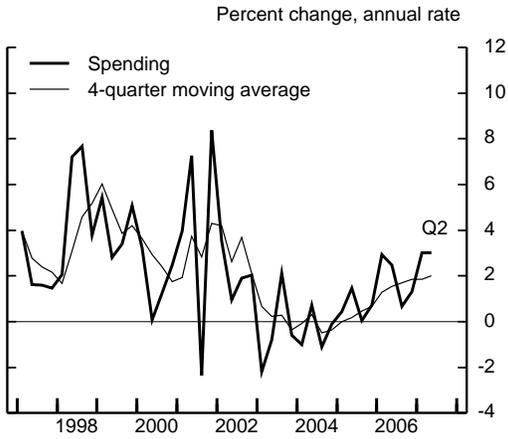
The incoming data point to a moderate increase in real state and local purchases in the third quarter. As we had thought likely, the most recent labor market report contained sizable upward revisions to the previously published figures for state and local employment in July and August, and employment increased sharply in September.⁸ As a result, employment is now estimated to have risen 23,000 per month, on average, over the three months ending in September, similar to the pace recorded over the first half of the year. Meanwhile, real construction spending appears to have moved up further in July and August (the latest available data) after increasing substantially in the first half.

On the whole, state and local revenue flows have held up reasonably well of late, although recent gains have been much smaller than those recorded over the preceding two years. According to the Census Bureau's *Quarterly Summary of State and Local Government Tax Revenue*, state revenues during the year ending in June—fiscal year 2007 for most states—were 5 percent above their year-earlier level; individual and corporate income taxes posted solid—albeit unspectacular—gains over this period, and

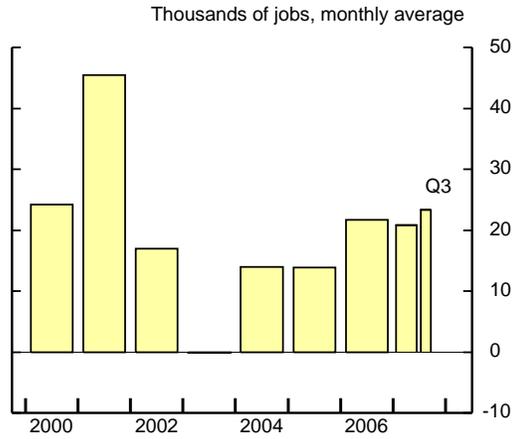
⁸ Most of the upward revision was in local education employment, which had previously been reported to have declined a startling 82,000 between June and August, but was revised up to show a small increase, on net, over the two months. As the BLS noted in the Acting Commissioner's statement on October 5, initial estimates of employment in local education typically are based upon a smaller percentage of survey responses than in other sectors, which can make estimation problematic in months when school sessions begin and end.

State and Local Indicators

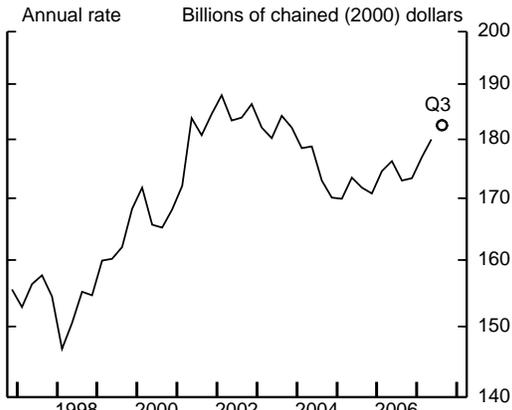
Real Spending on Consumption & Investment



Net Change in Employment

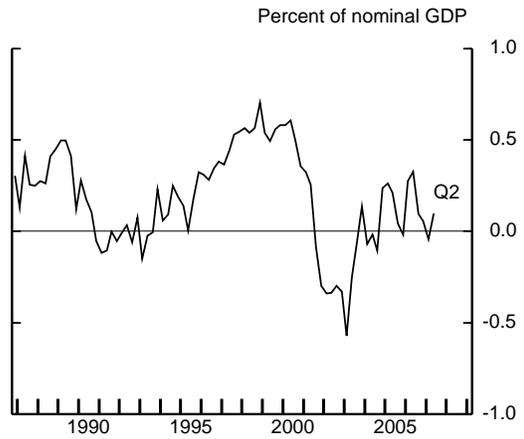


Real Construction

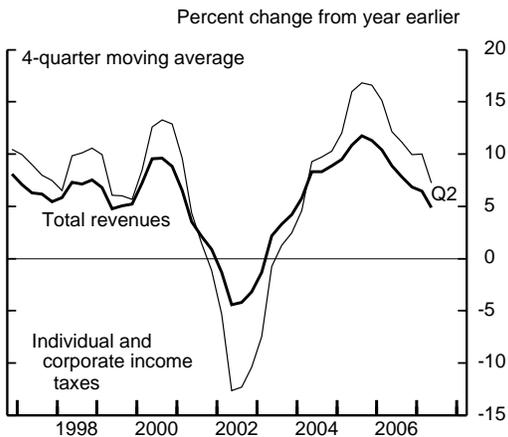


Note. Nominal CIPPI deflated by BEA prices through Q2 and by a staff projection thereafter. Q3 is the average for July and August.

Net Saving

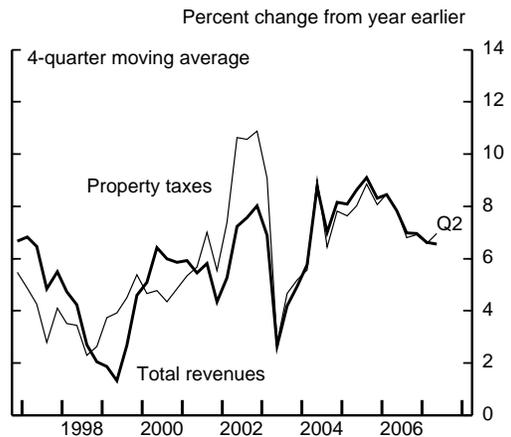


State Revenues



Source. Census Bureau.

Local Revenues



Source. Census Bureau.

Price Measures
(Percent change)

Measures	12-month change		3-month change		1-month change	
	Sept. 2006	Sept. 2007	Annual rate		Monthly rate	
			June 2007	Sept. 2007	Aug. 2007	Sept. 2007
<i>CPI</i>						
Total	2.1	2.8	5.2	1.0	-1	.3
Food	2.5	4.5	5.1	4.9	.4	.5
Energy	-4.3	5.3	32.9	-14.8	-3.2	.3
Ex. food and energy	2.9	2.1	2.3	2.5	.2	.2
Core goods	.5	-.8	-1.2	.3	.0	.0
Core services	3.9	3.3	3.6	3.3	.2	.3
Shelter	4.3	3.5	4.1	2.9	.1	.3
Other services	3.3	3.0	3.2	3.7	.3	.3
Chained CPI (n.s.a.) ¹	1.8	2.3	...	...	...	...
Ex. food and energy ¹	2.6	1.7	...	...	...	...
<i>PCE prices²</i>						
Total	2.0	2.3	3.7	.9	-1	.2
Food and beverages	2.5	4.2	4.6	4.5	.4	.4
Energy	-4.6	5.5	34.8	-15.3	-3.3	.3
Ex. food and energy	2.4	1.7	1.5	1.6	.1	.2
Core goods	.2	-1.1	-1.8	-.7	-.2	.0
Core services	3.4	2.9	2.8	2.5	.2	.3
Shelter	4.2	3.3	3.1	2.9	.2	.3
Other services	3.1	2.7	2.7	2.4	.2	.2
Core market-based	2.2	1.6	1.2	1.7	.1	.2
Core non-market-based	3.6	2.2	2.6	1.2	.1	.1
<i>PPI</i>						
Total finished goods	.9	4.4	6.0	1.4	-1.4	1.1
Food	2.2	5.7	-2.1	4.7	-.2	1.5
Energy	-1.8	10.6	27.5	-1.5	-6.6	4.1
Ex. food and energy	1.3	2.0	2.5	1.5	.2	.1
Core consumer goods	1.2	2.3	2.6	2.4	.2	.2
Capital equipment	1.5	1.6	2.2	.3	.1	-.1
Intermediate materials	4.7	4.2	10.7	-.7	-1.2	.4
Ex. food and energy	7.2	1.7	7.4	-.5	-.5	.1
Crude materials	-8.2	11.4	12.4	-6.6	-3.0	.1
Ex. food and energy	20.7	13.9	.0	12.4	1.3	1.6

1. Higher-frequency figures are not applicable for data that are not seasonally adjusted.

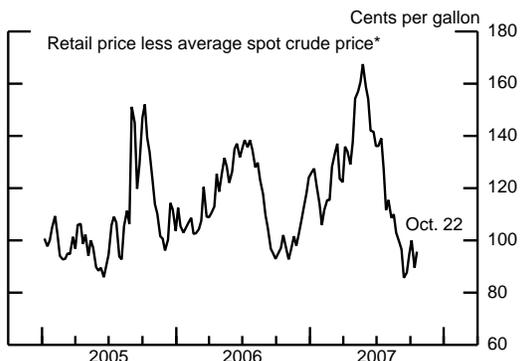
2. PCE prices in September 2007 are staff estimates.

... Not applicable.

Energy and Food Price Indicators

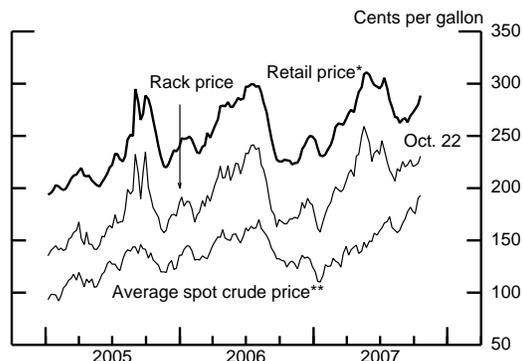
(Data from Energy Information Administration except as noted)

Total Gasoline Margin



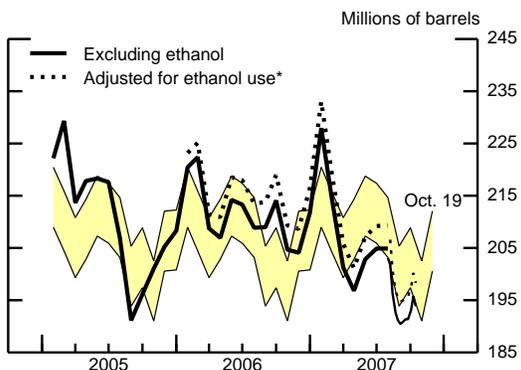
* Regular grade seasonally adjusted by FRB staff, less average spot crude price: 60% WTI, 40% Maya heavy crude.

Gasoline Price Decomposition



* Regular grade seasonally adjusted by FRB staff.
** 60% WTI, 40% Maya heavy crude.

Gasoline Inventories



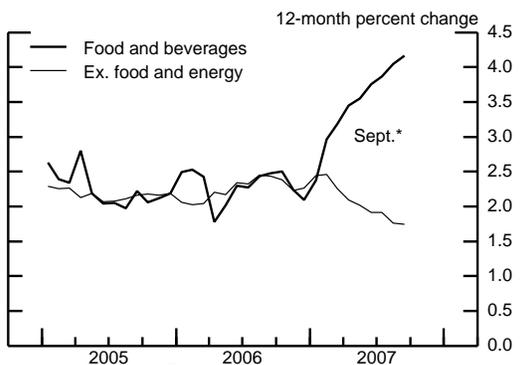
Note. Shaded region is average historical range as calculated by DOE. Monthly data through July 2007, weekly data thereafter, as indicated by line weights.
* Adjustment for approximate amount of fuel ethanol to be blended with RBOB component of inventories; estimated by FRB staff.

Ethanol Prices



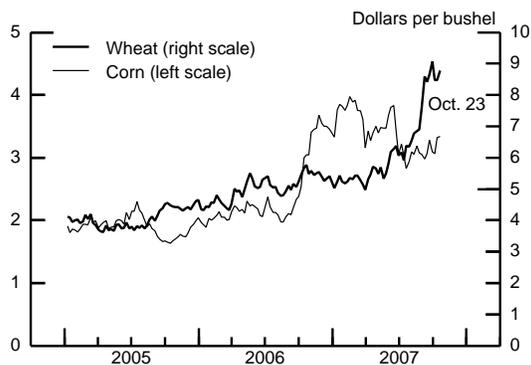
Source: Chicago Board of Trade.

PCE Food Prices



Source: Bureau of Economic Analysis.
*Staff estimate.

Spot Agricultural Commodity Prices



Source: Commodity Research Bureau.

sales tax collections rose just 4 percent, held down in part by softness in purchases of building materials and supplies and other housing-related items. At the local level, revenues rose 6½ percent during the year ending in June as property taxes apparently continued to be bolstered by the lagged effects of earlier increases in real estate values.

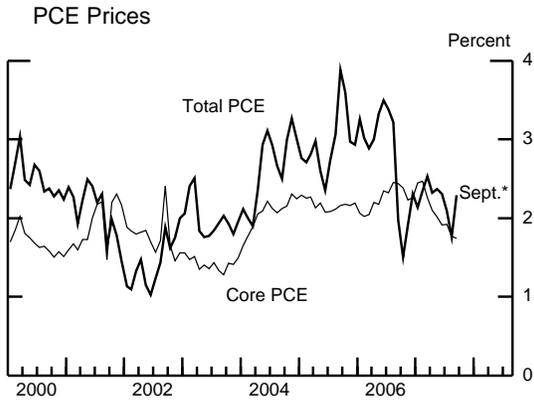
Prices

After having risen rapidly in the first half of the year, headline consumer prices decelerated considerably this summer, largely due to a fall in energy prices. In September, the overall CPI increased 0.3 percent after almost no change in July and August. These readings brought the annual rate of increase in the headline CPI down to 1 percent over the three months ending in September, well below the 5 percent rate posted in the first half of the year. Core consumer price inflation continued to be moderate in August and September and, on a twelve-month change basis, is down noticeably from a year earlier. Survey measures of inflation expectations edged down in September and early October; however, measures based on TIPS have edged up a bit over this period.

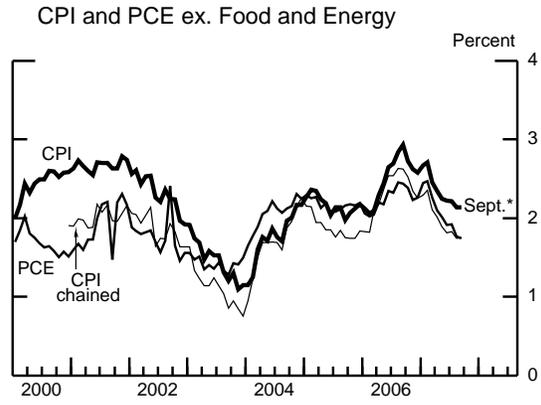
Energy prices increased 0.3 percent in September after having fallen in each of the previous three months. Gasoline prices increased only slightly in September, despite a jump in crude oil costs, and appear to have risen only modestly so far in October as well. As a result, the margin between the retail price of gasoline and crude oil costs, which had reached record highs last spring, has declined to relatively low levels in recent weeks, even though inventories remain near the low end of their normal range.

Consumer food prices posted further sizable increases in August and September and continue to run well above the change in core prices. These elevated rates of inflation in food prices reflect, in part, the ongoing pass-through of high corn prices, which have been boosted by the strong demand for ethanol. Retail prices for chicken and milk have continued to rise appreciably in recent months, and egg prices have soared. In contrast, beef prices have leveled out, and pork prices have turned down. In addition, rising prices for other grains, most noticeably wheat and soybeans—the output of which was reduced by adverse weather and the shift in acreage to corn production—have shown through to higher retail prices for products such as cereal and bakery products. Finally, other price increases—notably for food away from home—have remained elevated. In spot markets for crops, corn prices have moved up somewhat since the September Greenbook but remain well below their peak reached earlier this year, whereas prices for wheat appear to have stabilized in recent weeks near their record high. Spot prices for steers and chickens

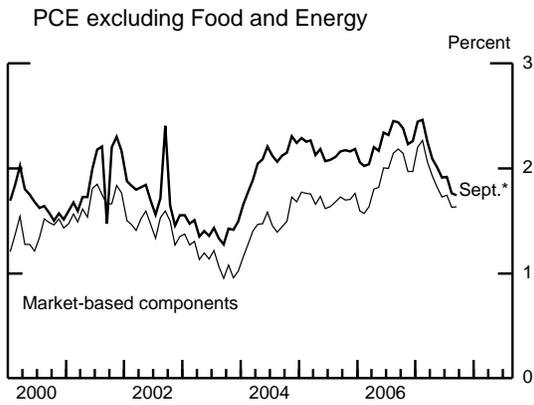
Consumer Prices (12-month change except as noted)



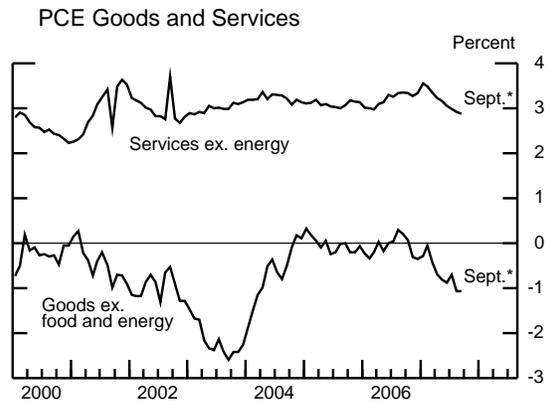
* Staff estimate.



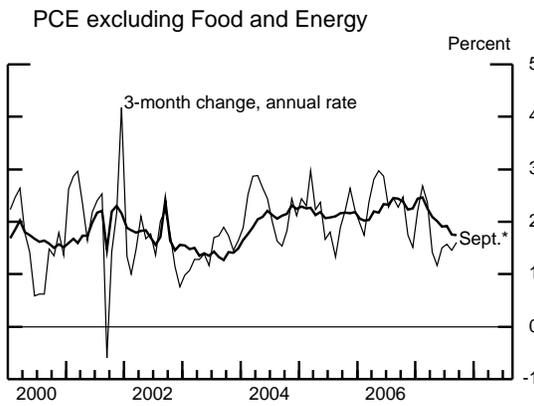
* PCE for September is a staff estimate.



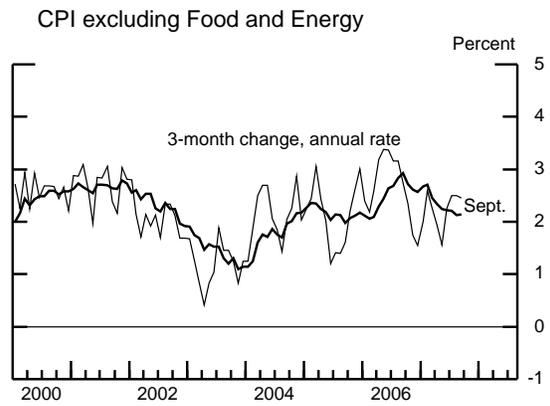
* Staff estimate.



* Staff estimate.



* Staff estimate.



have moved down a bit since the September Greenbook, whereas hog prices have dropped sharply.

In September, the CPI excluding food and energy rose 0.2 percent for the fourth consecutive month. On the basis of the CPI and PPI data, we estimate that core PCE prices also rose 0.2 percent in September, following smaller increases in each of the previous six months.

Over the last six months, core PCE price inflation (at a 1.6 percent rate) has been running well below core CPI inflation (at a 2.4 percent rate). In contrast, both core price indexes had increased at a 1.9 percent annual rate over the previous six-month period. The $\frac{3}{4}$ percentage point gap between core CPI inflation and core PCE inflation over the most recent six months is unusually large, and we continue to view the recent low readings on PCE price inflation as partly transitory. The recent relative softness in PCE price inflation reflects, in part, below-average rates of nonmarket price inflation; because these price changes tend to be mean reverting, we expect this factor to diminish over time. Beyond that, differences in the weights used in the two indexes have contributed to the divergent movements, as has the fact that the PPI measures of medical services prices used in the PCE price index have increased by much less than have the equivalent CPI measures. Large gaps between the CPI and PCE measures of core inflation typically do not persist; however, outside of the nonmarket segment, history does not provide a strong indication of which measure will move to narrow the gap.

Measures of Core Consumer Price Inflation (Percent change)

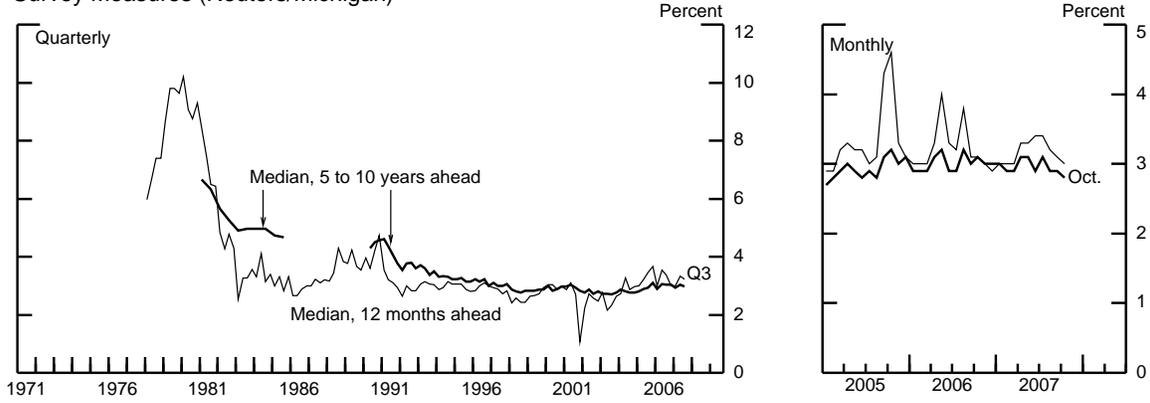
Category	Twelve-month change		Six-month change, annual rate	
	Sept. 2006	Sept. 2007	Mar. 2007	Sept. 2007
CPI ex. food and energy	2.9	2.1	1.9	2.4
PCE ex. food and energy ¹	2.4	1.7	1.9	1.6
Gap	.5	.4	.0	.8

1. PCE prices in Sept. 2007 are staff estimates.

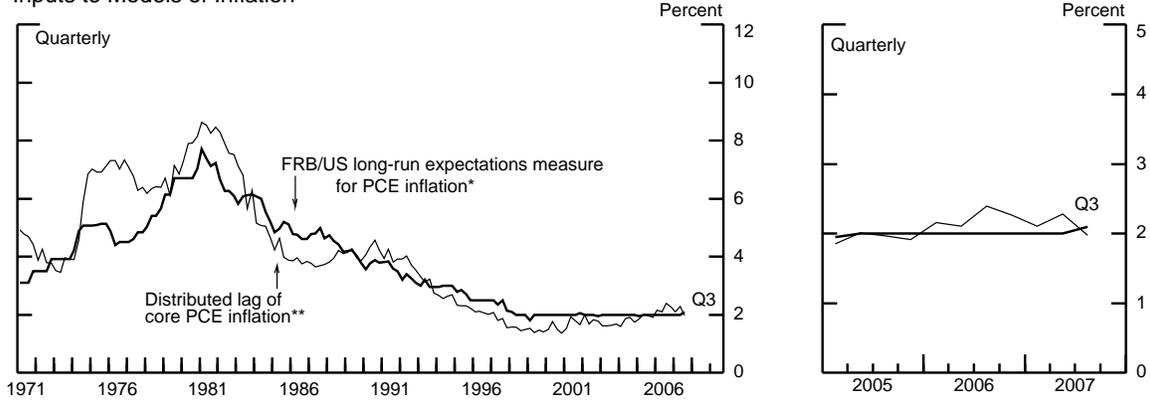
Taking a longer view, both the core CPI and core PCE indexes have decelerated over the most recent twelve months compared with the similar period twelve months earlier. As already noted, below-average increases in the nonmarket components of PCE have held down core PCE inflation this year, but market-based core PCE prices have decelerated markedly over the past year as well. Core goods prices have fallen about 1 percent over the past year after rising little over the preceding year (with noticeable decelerations in

Measures of Expected Inflation

Survey Measures (Reuters/Michigan)



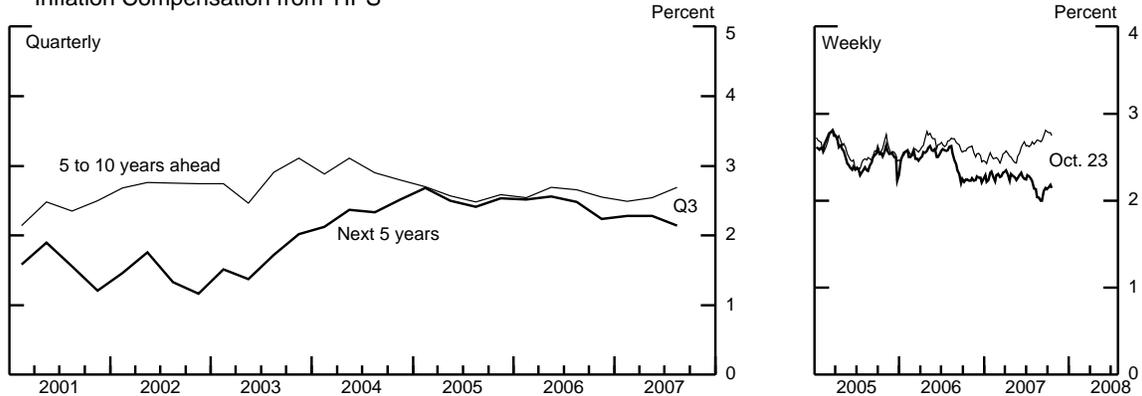
Inputs to Models of Inflation



*For 2007 forward, the median projection for PCE inflation over the next 10 years from the Survey of Professional Forecasters (SPF); for 1991 to 2006, the equivalent SPF projection for the CPI; for 1981 to 1991, a related survey for the CPI conducted by Richard Hoey; and for the period preceding 1981, a model-based estimate constructed by Board staff. The survey data before 2007 are adjusted down 0.5 percentage point to put the CPI projections approximately on a PCE basis.

**Derived from one of the reduced-form Phillips curves used by Board staff.

Inflation Compensation from TIPS



Note. Based on a comparison of an estimated TIPS yield curve with an estimated nominal off-the-run Treasury yield curve, with an adjustment for the indexation-lag effect.

the prices of apparel, prescription drugs, and motor vehicles). In addition, increases in owners' equivalent rent have slowed noticeably over the past year, whereas rent inflation has remained about the same as a year earlier.

Recent readings of inflation expectations have been mixed. According to the Reuters/Michigan survey in early October, the median expectation for year-ahead inflation inched down to 3 percent—the same as its level at the turn of the year—and the median expectation over the next five to ten years edged down to 2.8 percent, the lowest level since August 2005. Meanwhile, five-year inflation compensation as derived from TIPS has remained relatively subdued, and forward inflation compensation five to ten years ahead has remained at the high end of the range in which it has been observed in recent years.

Price movements for goods at earlier stages of processing have been mixed in recent months. The PPI for core intermediate materials edged up in September after decreasing 0.5 percent in August, bringing September's twelve-month change in core intermediate materials prices to 1.7 percent, down considerably from the rise of 7.2 percent posted over the year-earlier period. This step-down reflects (in part) the continued deceleration in prices for a wide variety of energy-intensive goods, such as industrial chemicals and plastics, as well as a significant deceleration in the price of construction materials—some of which are also energy intensive—such as metal products, asphalt shingles, gypsum, cement, and paints. In addition, lumber and plywood spot prices have dropped noticeably since the September Greenbook.

Commodity prices have moved up further since the September PPI pricing date (which occurred around the time of the September Greenbook). The *Journal of Commerce* index of industrial materials has risen about 2.8 percent since mid-September, and the Commodity Research Bureau's index of industrial spot prices is up about 4.2 percent, both reflecting, in part, large price increases for a variety of metals.

Labor Costs

The only timely information we have received on wages since the last Greenbook is the September reading for average hourly earnings of production or nonsupervisory workers. With the increase of 0.4 percent in September, average hourly earnings were up 4.1 percent over the twelve months ending in September, the same increase as a year earlier.

Broad Measures of Inflation
(Percent change, Q2 to Q2)

Measure	2004	2005	2006	2007
<i>Product prices</i>				
GDP price index	2.9	3.0	3.5	2.7
Less food and energy	2.7	3.1	3.3	2.5
Nonfarm business chain price index	2.2	3.2	3.5	1.9
<i>Expenditure prices</i>				
Gross domestic purchases price index	3.1	3.4	3.8	2.5
Less food and energy	2.7	3.0	3.1	2.3
PCE price index	2.8	2.6	3.3	2.3
Less food and energy	2.1	2.1	2.2	2.0
PCE price index, market-based components	2.4	2.4	3.2	2.2
Less food and energy	1.5	1.7	1.9	1.8
CPI	2.8	2.9	4.0	2.7
Less food and energy	1.8	2.2	2.4	2.3
Chained CPI	2.7	2.6	3.4	2.3
Less food and energy	1.7	1.9	2.4	1.9
Median CPI	2.2	2.3	2.9	3.0
Trimmed mean CPI	2.1	2.2	2.7	2.6
Trimmed mean PCE	2.3	2.3	2.7	2.4

Surveys of Inflation Expectations
(Percent)

Period	Actual CPI inflation ¹	Reuters/Michigan Survey				Professional forecasters (10 years) ⁴	
		1 year ²		5 to 10 years ³		CPI	PCE
		Mean	Median	Mean	Median		
2005:Q4	3.7	4.6	3.7	3.5	3.1	2.5	...
2006:Q1	3.6	3.7	3.0	3.3	2.9	2.5	...
Q2	4.0	4.5	3.5	3.6	3.1	2.5	...
Q3	3.3	4.0	3.4	3.3	3.0	2.5	...
Q4	1.9	3.5	3.0	3.5	3.0	2.5	...
2007:Q1	2.4	3.6	3.0	3.4	2.9	2.4	2.0
Q2	2.7	4.2	3.3	3.5	3.0	2.4	2.0
Q3	2.4	4.1	3.2	3.5	3.0	2.4	2.1
2007:June	2.7	4.2	3.4	3.3	2.9	...	...
July	2.4	4.2	3.4	3.6	3.1	...	...
Aug.	2.0	4.0	3.2	3.4	2.9	2.4	2.1
Sept.	2.8	4.0	3.1	3.4	2.9	...	...
Oct.	n.a.	3.5	3.0	3.0	2.8	...	...

1. Percent change from the same period in the preceding year.

2. Responses to the question, By about what percent do you expect prices to go up, on average, during the next 12 months?

3. Responses to the question, By about what percent per year do you expect prices to go up, on average, during the next 5 to 10 years?

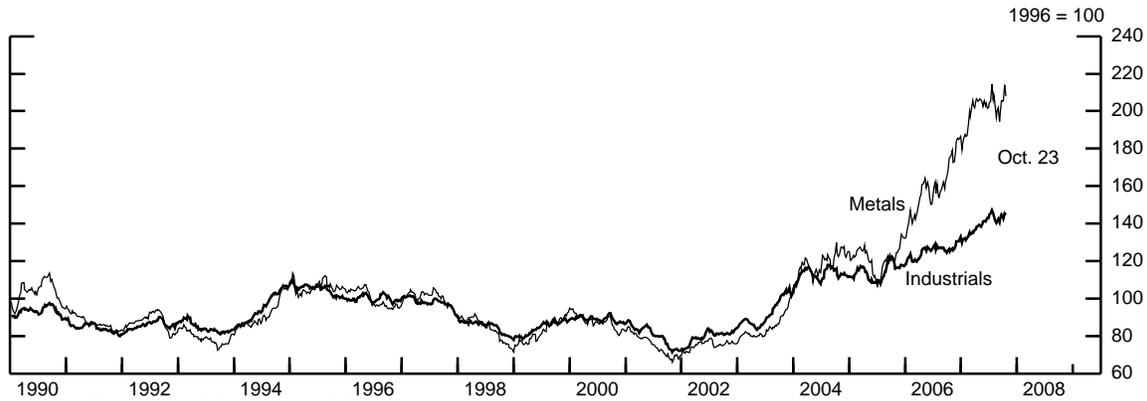
4. Median CPI and PCE price projections compiled by the Federal Reserve Bank of Philadelphia.

... Not applicable.

n.a. Not available.

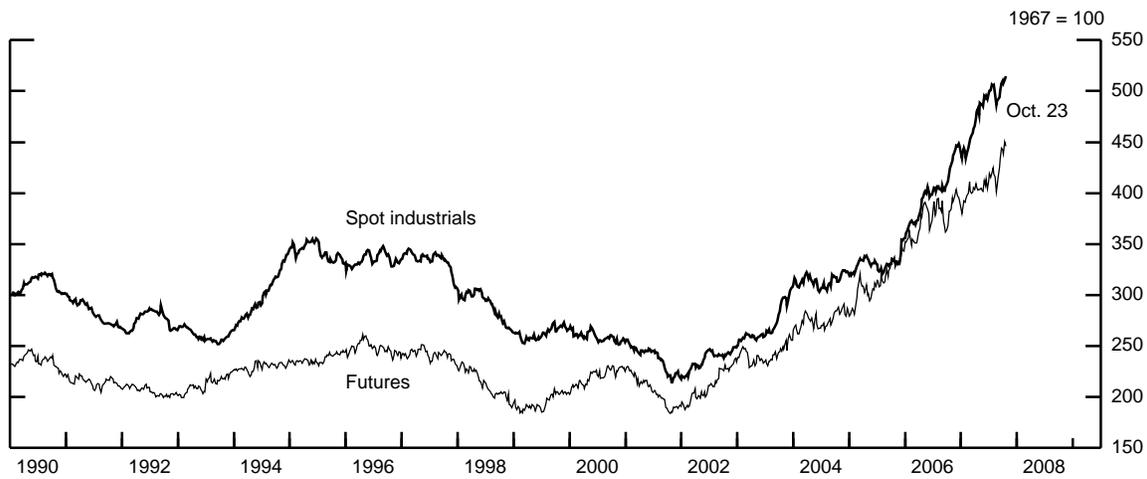
Commodity Price Indexes

Journal of Commerce



Note. The *Journal of Commerce* (JOC) industrial price index is based almost entirely on industrial commodities, with a small weight given to energy commodities. Copyright for *Journal of Commerce* data is held by CIBCR, 1994.

Commodity Research Bureau



Note. The Commodity Research Bureau (CRB) spot industrials index consists entirely of industrial commodities, excluding energy. The CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities, and precious metals.

Selected Commodity Price Indexes (Percent change)

Index	2006 ¹	12/19/06 to 9/11/07 ²	9/11/07 ² to 10/23/07	52-week change to 10/23/07
JOC industrials	11.0	7.9	2.8	15.6
JOC metals	38.9	5.1	7.1	18.7
CRB spot industrials	26.9	10.2	4.2	21.3
CRB spot foodstuffs	13.0	19.7	-.8	20.7
CRB futures	15.0	7.6	4.9	16.6

1. From the last week of the preceding year to the last week of the year indicated.

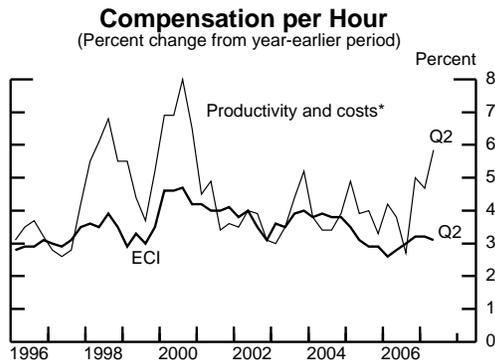
2. September 11, 2007, is the Tuesday preceding publication of the September Greenbook.

Hourly Compensation and Unit Labor Costs

(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

Category	2005:Q2 to 2006:Q2	2006:Q2 to 2007:Q2 ^e	2006		2007	
			Q3	Q4	Q1	Q2 ^e
<i>Compensation per hour</i> Nonfarm business	3.8	5.8	1.3	12.2	5.9	4.3
<i>Unit labor costs</i> Nonfarm business	2.2	5.1	2.9	10.3	5.2	2.2

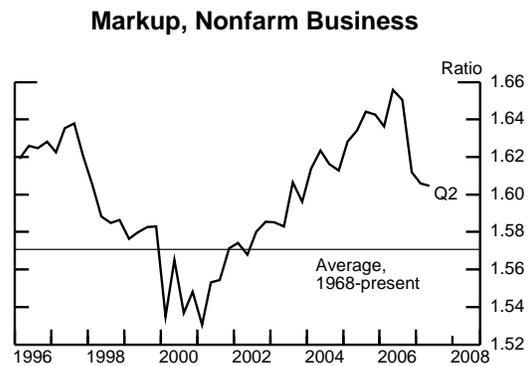
e Staff estimate.



* Value for 2007:Q2 is a staff estimate.



Note. Value for 2007:Q2 is a staff estimate.



Note. The markup is the ratio of output price to unit labor costs. Value for 2007:Q2 is a staff estimate.

Domestic Financial Developments

III-T-1
Selected Financial Market Quotations
(One-day quotes in percent except as noted)

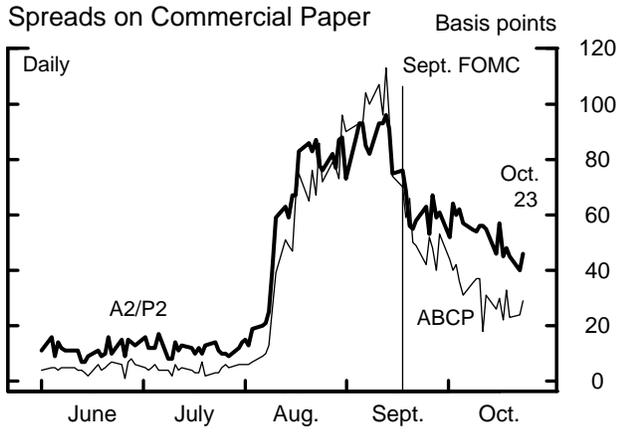
Instrument	2004	2006	2007		Change to Oct. 23 from selected dates (percentage points)		
	June 28	June 29	Sept. 17	Oct. 23	2004 June 28	2006 June 29	2007 Sept. 17
<i>Short-term</i>							
FOMC intended federal funds rate	1.00	5.25	5.25	4.75	3.75	-.50	-.50
Treasury bills ¹							
3-month	1.36	4.88	4.05	3.88	2.52	-1.00	-.17
6-month	1.74	5.06	4.15	3.97	2.23	-1.09	-.18
Commercial paper (A1/P1 rates) ²							
1-month	1.28	5.27	5.23	4.72	3.44	-.55	-.51
3-month	1.45	5.37	5.25	4.82	3.37	-.55	-.43
Large negotiable CDs ¹							
3-month	1.53	5.47	5.52	5.02	3.49	-.45	-.50
6-month	1.82	5.59	5.36	4.88	3.06	-.71	-.48
Eurodollar deposits ³							
1-month	1.29	5.33	5.55	4.90	3.61	-.43	-.65
3-month	1.51	5.49	5.60	5.09	3.58	-.40	-.51
Bank prime rate	4.00	8.25	8.25	7.75	3.75	-.50	-.50
<i>Intermediate- and long-term</i>							
U.S. Treasury ⁴							
2-year	2.88	5.26	4.12	3.84	.96	-1.42	-.28
5-year	3.97	5.15	4.18	4.03	.06	-1.12	-.15
10-year	4.90	5.28	4.58	4.52	-.38	-.76	-.06
U.S. Treasury indexed notes ⁵							
5-year	1.60	2.51	2.04	1.90	.30	-.61	-.14
10-year	2.26	2.61	2.15	2.11	-.15	-.50	-.04
Municipal general obligations (Bond Buyer) ⁶	5.01	4.71	4.46	4.39	-.62	-.32	-.07
Private instruments							
10-year swap	5.21	5.81	5.17	5.05	-.16	-.76	-.12
10-year FNMA ⁷	5.38	5.59	5.01	4.91	-.47	-.68	-.10
10-year AA ⁸	5.60	6.20	6.05	5.86	.26	-.34	-.19
10-year BBB ⁸	6.25	6.74	6.46	6.26	.01	-.48	-.20
10-year high yield ⁸	8.41	8.74	8.95	8.67	.26	-.07	-.28
Home mortgages (FHLMC survey rate) ⁹							
30-year fixed	6.21	6.78	6.34	6.40	.19	-.38	.06
1-year adjustable	4.19	5.82	5.65	5.76	1.57	-.06	.11

Stock exchange index	Record high		2006	2007		Change to Oct. 23 from selected dates (percent)		
	Level	Date	June 29	Sept. 17	Oct. 23	Record high	2006 June 29	2007 Sept. 17
Dow Jones Industrial	14,165	10-9-07	11,191	13,403	13,676	-3.45	22.21	2.04
S&P 500 Composite	1,565	10-9-07	1,273	1,477	1,520	-2.91	19.38	2.91
Nasdaq	5,049	3-10-00	2,174	2,582	2,799	-44.55	28.74	8.43
Russell 2000	856	7-13-07	714	776	819	-4.35	14.59	5.51
Wilshire 5000	15,807	10-9-07	12,846	14,839	15,386	-2.66	19.78	3.69

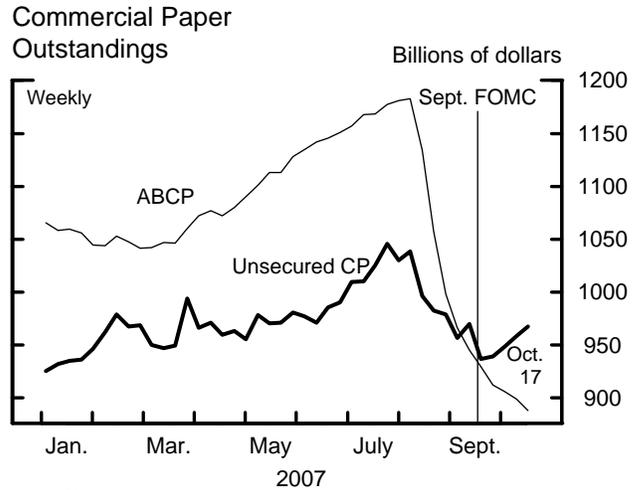
1. Secondary market.
2. Financial commercial paper.
3. Bid rates for Eurodollar deposits collected around 9:30 a.m. eastern time.
4. Derived from a smoothed Treasury yield curve estimated using off-the-run securities.
5. Derived from a smoothed Treasury yield curve estimated using all outstanding securities and adjusted for the carry effect.
6. Most recent Thursday quote.
7. Constant-maturity yields estimated from Fannie Mae domestic noncallable coupon securities.
8. Derived from smoothed corporate yield curves estimated using Merrill Lynch bond data.
9. Home mortgage rates for October 23, 2007, are for the week ending October 18, 2007.

NOTES:
June 28, 2004, is the day before the most recent policy tightening began.
June 29, 2006, is the day the most recent policy tightening ended.
September 17, 2007, is the day before the most recent FOMC announcement.

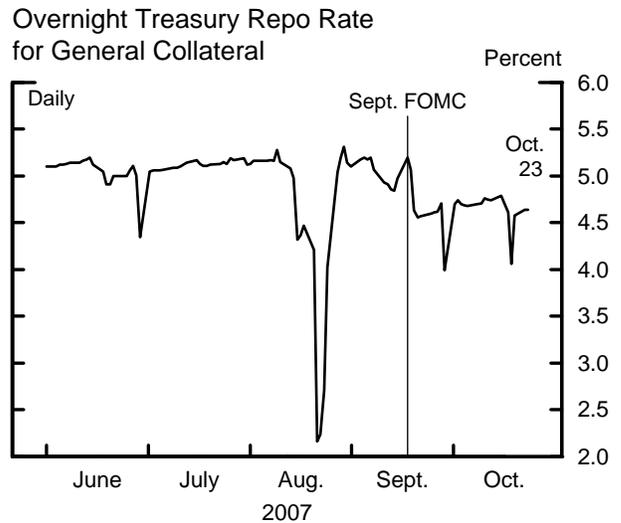
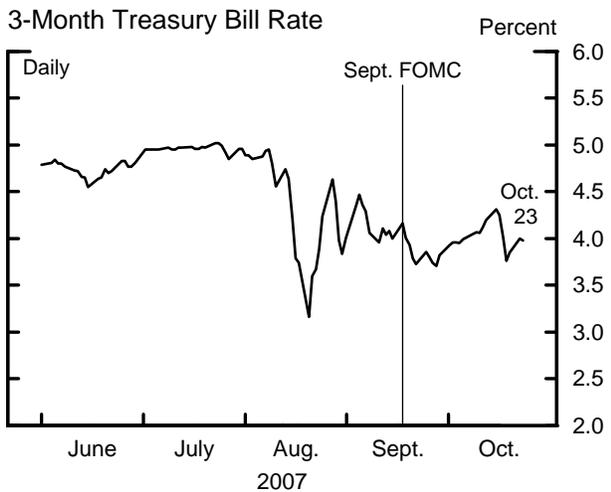
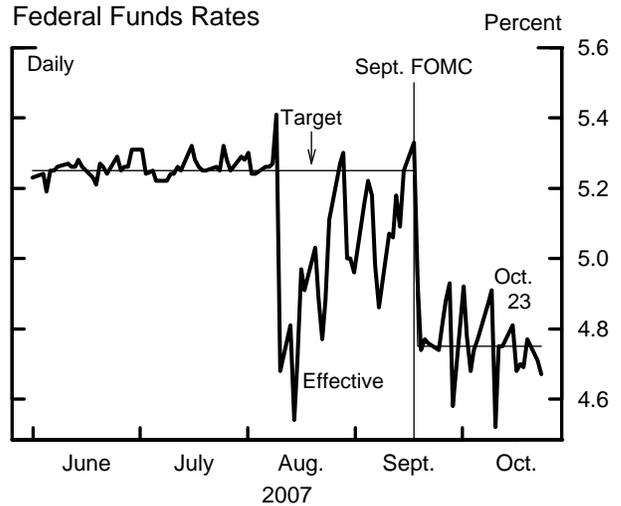
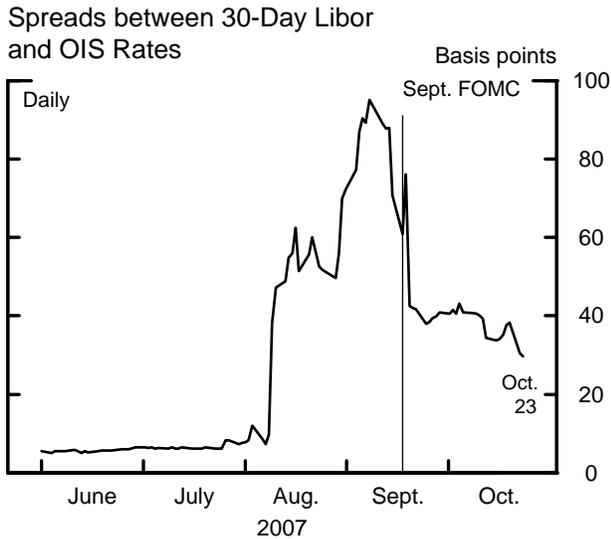
III-C-1
Short-Term Funding and Interbank Markets



Note. The ABCP spread is the AA ABCP rate minus the AA financial rate. The A2/P2 spread is the A2/P2 nonfinancial rate minus the AA nonfinancial rate.



Note. Seasonally adjusted; weeks ending Wednesdays.



Domestic Financial Developments

Overview

The functioning of short-term funding markets improved somewhat early in the intermeeting period, but conditions in these markets remained strained. Credit spreads declined in the commercial paper and term interbank funding markets but stayed well above longer-term norms, and liquidity in the Treasury bill market was still reportedly poor at times. The expected path for monetary policy moved lower after the FOMC's announcement of a 50 basis point easing at its September meeting, as many investors were surprised by the magnitude of the reduction in the target rate. The anticipated policy path beyond the middle of next year moved down a bit further, on net, over the remainder of the intermeeting period, in response to heightened concerns about economic growth. Two-year Treasury yields declined roughly in line with the lower expected policy path, and yields on ten-year Treasuries were little changed, on net.

Stock prices jumped early in the intermeeting period in response to the cut in the target federal funds rate and some favorable economic news, but dropped back in recent weeks, leaving broad indexes up 3 to 4 percent on net. Corporate bond spreads narrowed somewhat, leaving private yields a little lower. Nonfinancial bond issuance was quite strong, including a marked pickup in speculative-grade offerings. C&I loans continued to soar, as some banks had to retain LBO loans that they had planned to syndicate. The credit quality of most households remained strong, but delinquency rates on subprime mortgages climbed further. Securitization of nonconforming mortgages remained limited, and spreads on jumbo mortgages stayed high. According to responses from the October Senior Loan Officer Opinion Survey, banks have tightened their standards and terms on a range of loan categories over the past three months.

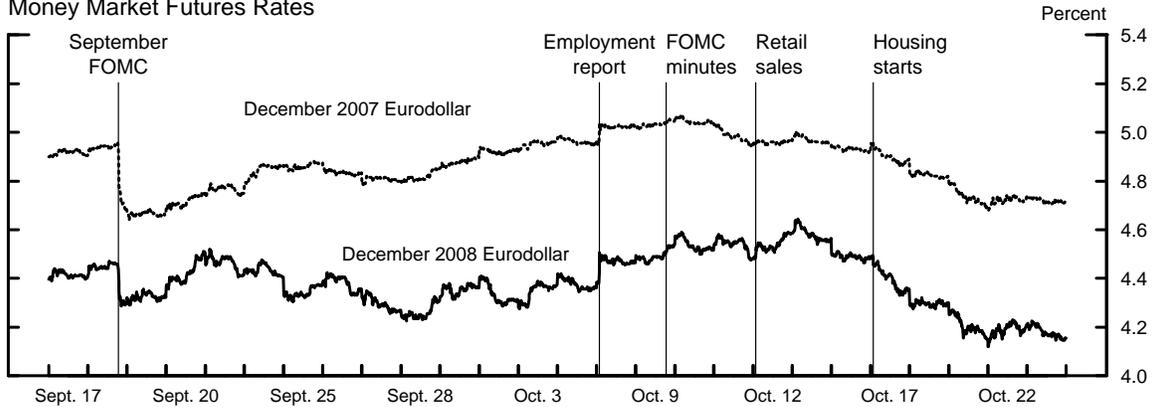
Money Market Functioning

The functioning of money markets improved early in the intermeeting period, but some strains remain evident. Spreads on asset-backed commercial paper (ABCP) over comparably-rated unsecured financial paper continued to decline from their peaks in late August and early September, with the spreads on paper issued by multi-seller conduits, which typically have full liquidity support from banks, falling the most. Spreads on nonfinancial unsecured paper also declined over the intermeeting period. Outstandings of unsecured paper, which fell in August and September, turned up in October, and the runoff of ABCP slowed somewhat.

However, some ABCP conduits, particularly structured investment vehicles (SIVs), continue to face severe funding constraints. Two SIV programs defaulted late in the

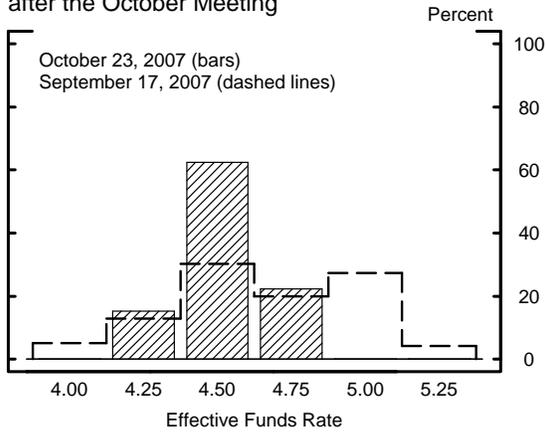
Policy Expectations and Treasury Yields

Money Market Futures Rates



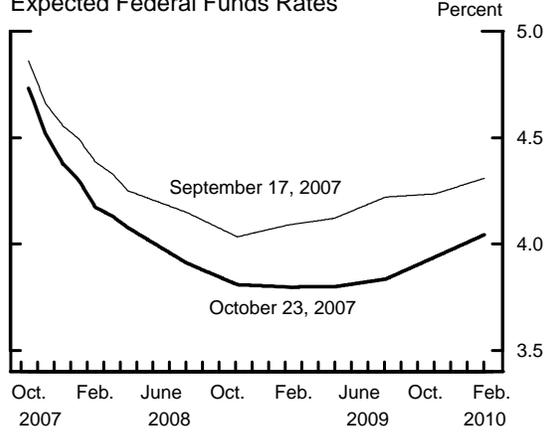
Note. 5-minute intervals. 8:00 a.m. to 4:00 p.m. No adjustments for term premiums.

Probability Density for Federal Funds Rate after the October Meeting



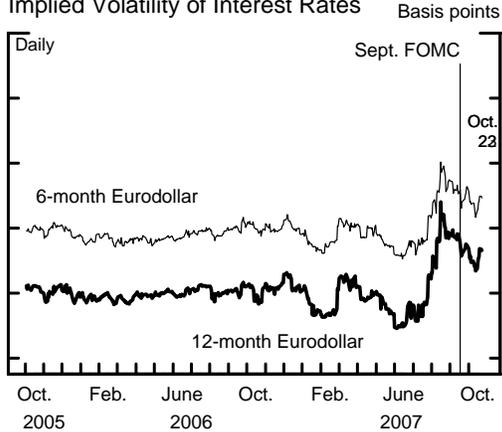
Note. Derived from options on the November 2007 federal funds futures contract, with a term premium adjustment.

Expected Federal Funds Rates

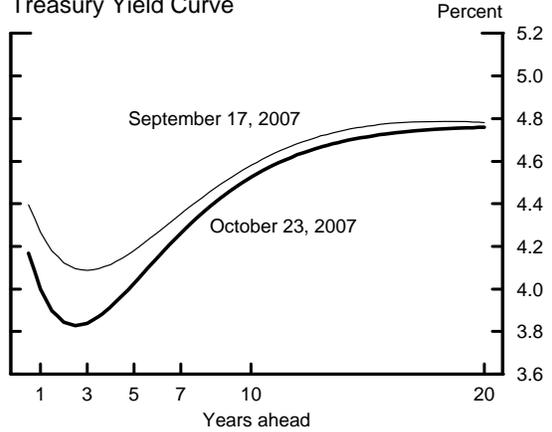


Note. Estimates from federal funds and Eurodollar futures.

Implied Volatility of Interest Rates



Treasury Yield Curve



Note. Smoothed yield curve estimated from off-the-run Treasury coupon securities.

intermeeting period, and a proposal by a consortium of large banks to create a Master Liquidity Enhanced Conduit that would purchase selected assets of some ABCP programs as a means of avoiding asset “fire sales” met with mixed reviews from other market participants.

Interbank funding markets showed some improvement, with the spread between thirty-day libor and comparable-maturity overnight index swaps declining markedly after the September FOMC announcement. The spread edged down a bit further, on net, in subsequent weeks but remained atypically high, reflecting elevated premiums for liquidity and counterparty risk. The effective federal funds rate, which had traded well below the target at times before the September meeting, has averaged close to the new target since then but has remained relatively volatile. Liquidity conditions in the Treasury bill market improved early in the intermeeting period but were still strained, with bid-asked spreads staying above the levels prevailing before August. Rates on three-month bills declined 17 basis points, on net, amid substantial volatility that was likely exacerbated by a paydown of Treasury bills. Overnight repo rates also displayed heightened volatility on some days.

Policy Expectations and Interest Rates

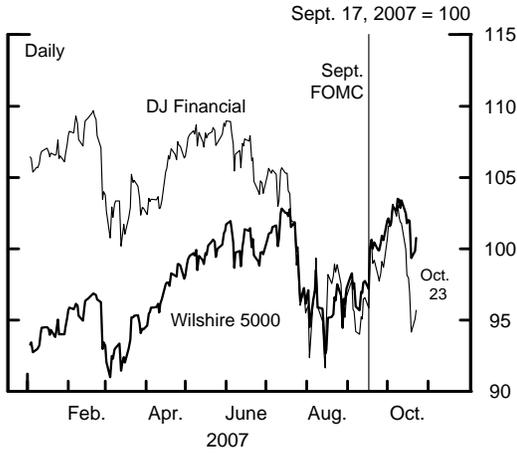
The expected path for monetary policy dropped after the September FOMC announcement of a 50 basis point cut in the target federal funds rate. Policy expectations firmed somewhat over the next three weeks, particularly in response to a better-than-expected employment report. However, disappointing news about activity in the housing sector and a resurgence of concerns about mortgage and other credit markets pushed policy expectations back down late in the intermeeting period.

Investors now see high odds that the FOMC will further reduce the target federal funds rate at the October meeting, most likely by 25 basis points. Looking further ahead, futures markets quotes imply an expected federal funds rate of 3.8 percent by the end of 2008—about 25 basis points below where it stood just before the September meeting. Uncertainty about monetary policy, as measured by implied volatilities derived from options on Eurodollar futures contracts, declined a bit further, on net, over the intermeeting period from the very high levels reached in August. These options also indicate that the distribution of future policy rates remains skewed to the downside.

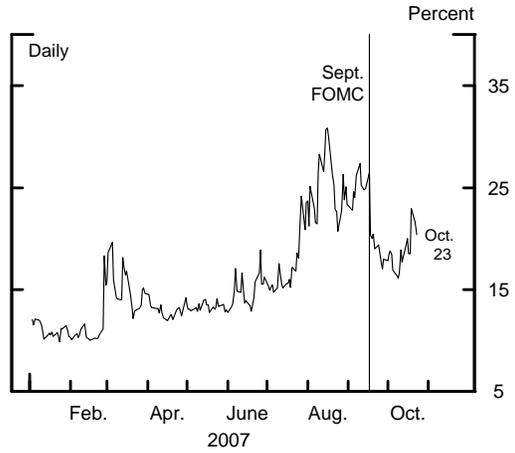
Yields on two-year nominal Treasury coupon securities fell 28 basis points, broadly in line with the decline in policy expectations, and ten-year Treasury yields declined just

Corporate Yields, Risk Spreads, and Stock Prices

Selected Stock Price Indexes



Implied Volatility on S&P 500 (VIX)

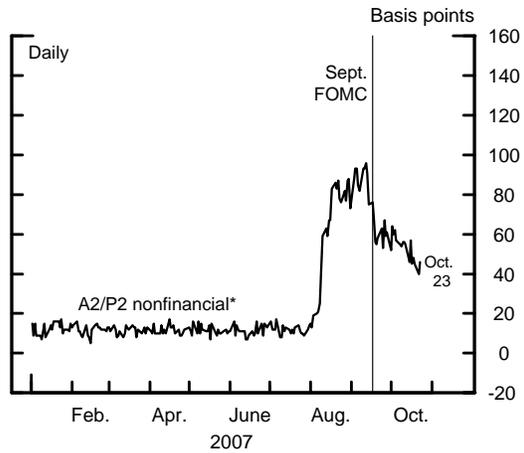


Ratio of Trend Earnings to Price for S&P 500 and Long-Run Treasury Yield



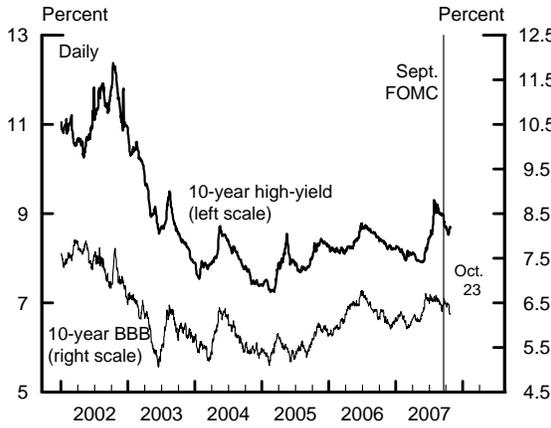
1986 1989 1992 1995 1998 2001 2004 2007
 * Trend earnings are estimated using analysts' forecasts of year-ahead earnings from I/B/E/S.
 + Denotes the latest observation using daily interest rates and stock prices and latest earnings data from I/B/E/S.

30-Day Commercial Paper Spreads



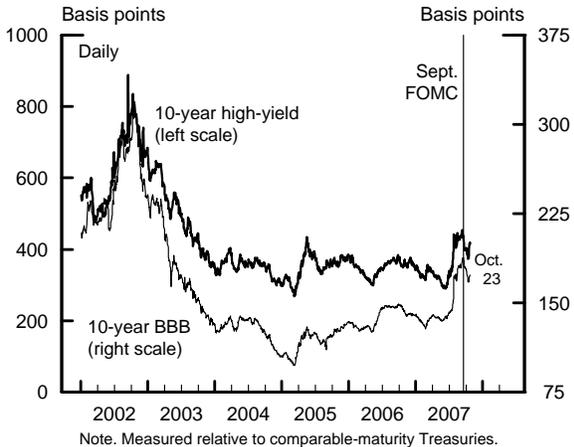
* A2/P2 nonfinancial rate minus AA nonfinancial rate.

Corporate Bond Yields



Note. Yields from smoothed yield curves based on Merrill Lynch bond data.

Corporate Bond Spreads



Note. Measured relative to comparable-maturity Treasuries.

6 basis points. Inflation compensation based on TIPS quotes was little changed despite much higher oil prices.

Stock Prices, Corporate Yields, and Risk Spreads

Broad equity indexes rose about 3 to 4 percent, on net, over the intermeeting period. Stock prices surged on the heels of the cut in the target federal funds rate and rose further following the October employment report. However, mixed news in third-quarter earnings reports and renewed concerns about the consequences of weakness in housing markets weighed on share prices more recently. Stocks of financial firms continued to be particularly volatile, first boosted by diminished concerns about downside risks from financial market turmoil, but then dragged back down by disappointing third-quarter reports from many bank holding companies that were adversely affected by writedowns of leveraged loans and mortgage-related assets. Options-implied volatility of returns on the S&P 500 dropped sharply after the September FOMC announcement but has since drifted back up and is well above its range in the first half of the year. The spread between the twelve-month forward trend earnings-price ratio for S&P 500 firms and a real long-run Treasury yield—a rough gauge of the equity risk premium—was little changed.

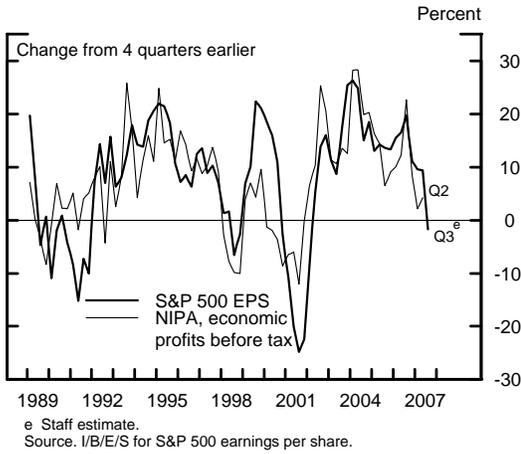
Over the intermeeting period, corporate bond yields declined, leaving spreads on investment- and speculative-grade corporate bonds down about 15 and 20 basis points respectively. These spreads are still near their recent highs but roughly in line with their averages over the past decade. In the market for nonfinancial commercial paper, the thirty-day A2/P2 quality spread narrowed to about 45 basis points.

Corporate Earnings and Credit Quality

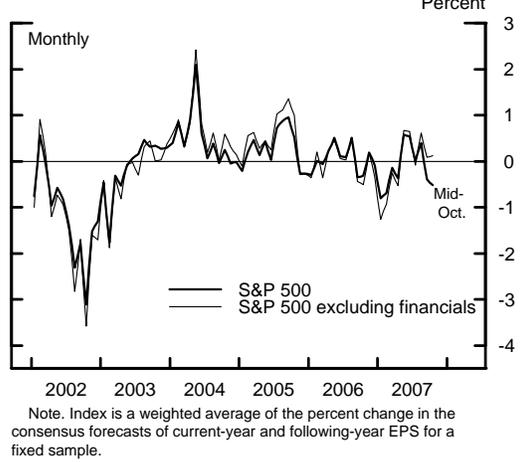
On the basis of nearly 200 reports in hand and analysts' estimates for the rest, it appears that earnings per share for S&P 500 firms in the third quarter were a bit lower than a year earlier—a sharp deceleration from the 10 percent increase registered in the second quarter. The falloff in the third quarter is mostly attributable to the financial sector, where earnings appear to have dropped about 15 percent from year-earlier levels. In contrast, nonfinancial firms are estimated to have logged four-quarter gains of nearly 5 percent. Substantial markdowns of forecasts for financial firms' current-year profits pulled revisions to expected earnings for the S&P 500 into negative territory in September and October. Even so, analyst forecasts remain surprisingly optimistic, with year-over-year growth now projected to bounce back to nearly 10 percent in the fourth quarter and beyond.

Corporate Earnings and Credit Quality

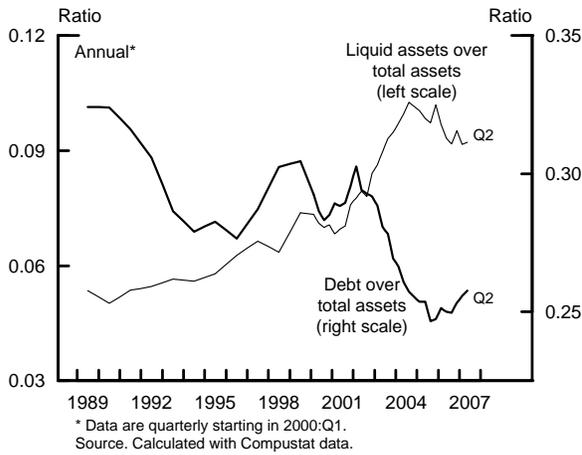
Corporate Earnings Growth



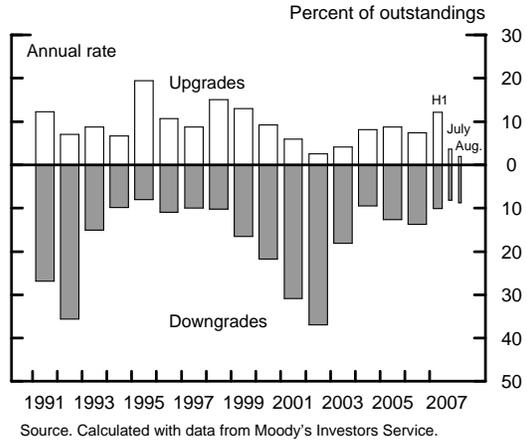
Revisions to Expected S&P 500 Earnings



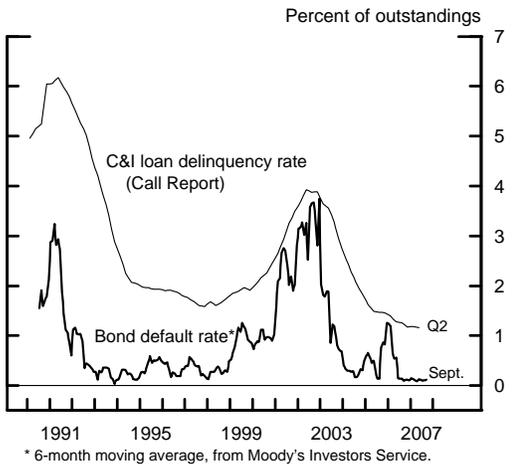
Financial Ratios for Nonfinancial Corporations



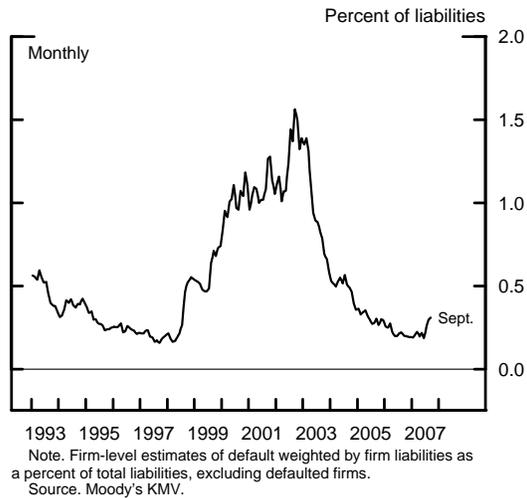
Bond Ratings Changes of Nonfinancial Companies



Selected Default and Delinquency Rates



Expected Year-Ahead Defaults



The credit quality of nonfinancial corporations appears to have remained strong through September. In the second quarter, nonfinancial corporate leverage increased slightly but remained near the low end of its range over the past twenty years, and the sector's balance-sheet liquidity remained high by historical standards. Rating downgrades on corporate bonds continued to be modest through August, and the six-month trailing bond default rate stayed near zero in September. KMV's aggregate year-ahead expected default rate, which had increased somewhat in August, inched up a bit further last month.

Business Finance

Gross bond issuance by investment-grade nonfinancial corporations remained strong in September and continued apace into October. Speculative-grade bond issuance, though still sluggish in September, picked up markedly in October, and a couple of offerings to finance leveraged buyouts (LBOs) cleared the market for the first time since late June. Even so, the backlog of LBO-related deals remains very large. Outstanding nonfinancial commercial paper dipped again in September but edged up in the first half of this month. Meanwhile, C&I loans continued to soar, in part as banks retained on their books loans that they had intended to syndicate. Responses from the October Senior Loan Officer Opinion Survey indicate that a significant number of banks have tightened standards and terms on loans to businesses over the past three months, consistent with the shift in risk pricing in the bond market. Overall, net debt financing was robust in September and appears to have picked up a bit in October.

Gross public equity issuance by nonfinancial corporations was light in September but has strengthened a bit this month. We estimate that equity retirements posted another record in the third quarter, as repurchases remained robust and cash-financed mergers and acquisitions soared. A sizable volume of LBOs, a component of cash mergers, was completed in the third quarter, but almost no new large LBO deals have been announced since early July. In contrast, the pace of announcements of small- and middle-market M&A deals has continued to be quite robust.

Commercial Real Estate

Spreads on BBB-rated commercial-mortgage-backed securities (CMBS) over comparable-maturity Treasuries remained elevated over the intermeeting period, reportedly reflecting ongoing concerns among investors and rating agencies about high levels of leverage on recently securitized commercial mortgages, as well as persistent worries about structured financial products in general. The increase in CMBS yields

Business Finance

Gross Issuance of Securities by U.S. Corporations

(Billions of dollars; monthly rates, not seasonally adjusted)

Type of security	2003	2004	2005	2006	2007			
					H1	Q3	Sept.	Oct. ^P
<i>Nonfinancial corporations</i>								
Stocks ¹	3.7	5.4	4.6	4.7	5.5	4.1	2.6	3.7
Initial public offerings	.4	1.6	1.7	1.8	1.7	1.2	.3	1.9
Seasoned offerings	3.3	3.8	2.8	2.9	3.9	2.9	2.3	1.8
Bonds ²	31.6	22.7	19.1	29.8	37.9	26.1	33.6	50.0
Investment grade	15.9	8.2	8.4	13.0	14.2	19.5	22.6	18.0
Speculative grade	11.3	9.7	6.4	8.0	15.4	3.4	4.0	15.0
Other (sold abroad/unrated)	4.3	4.9	4.3	8.8	8.3	3.1	6.9	17.0
<i>Memo</i>								
Net issuance of commercial paper ³	-3.4	1.5	-.4	3.9	1.2	-4.1	-7.8	2.2
Change in C&I loans at commercial banks ^{3,4}	-7.7	3.2	10.0	12.9	11.5	36.6	43.5	n.a.
<i>Financial corporations</i>								
Stocks ¹	6.6	6.9	5.0	5.3	9.3	3.4	3.9	3.0
Bonds ²	111.1	139.3	176.3	187.7	207.0	126.2	117.1	100.0

Note. Components may not sum to totals because of rounding.

1. Excludes private placements and equity-for-equity swaps that occur in restructurings.

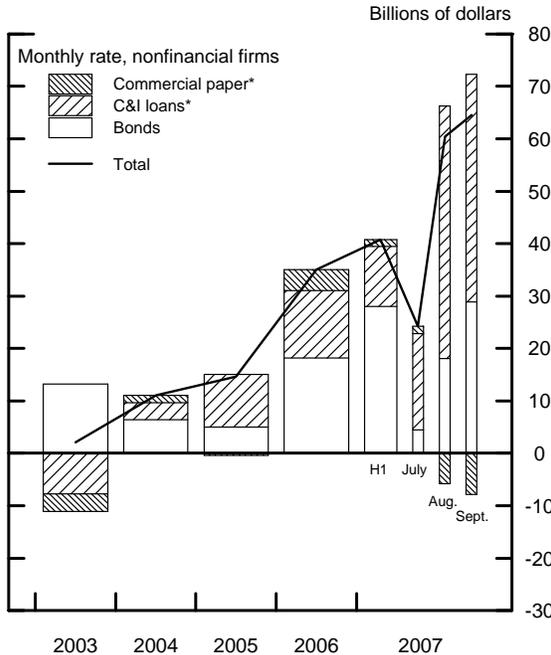
2. Data include regular and 144a private placements. Bond totals reflect gross proceeds rather than par value of original discount bonds. Bonds are categorized according to Moody's bond ratings or to Standard & Poor's if unrated by Moody's.

3. End-of-period basis, seasonally adjusted.

4. Adjusted commercial bank credit data.

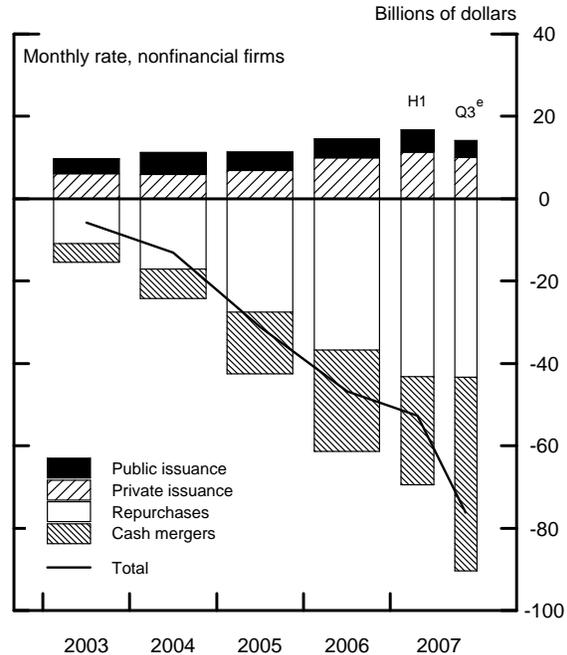
p Preliminary.

Selected Components of Net Debt Financing



* Seasonally adjusted, period-end basis.

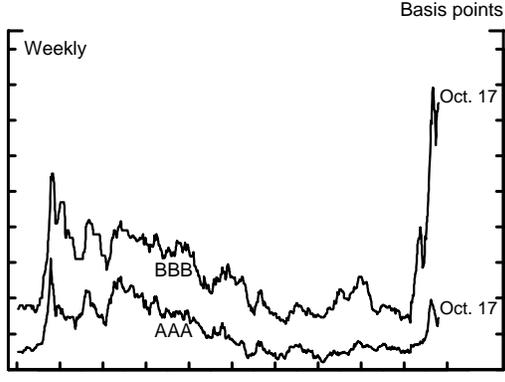
Components of Net Equity Issuance



e Staff estimate.

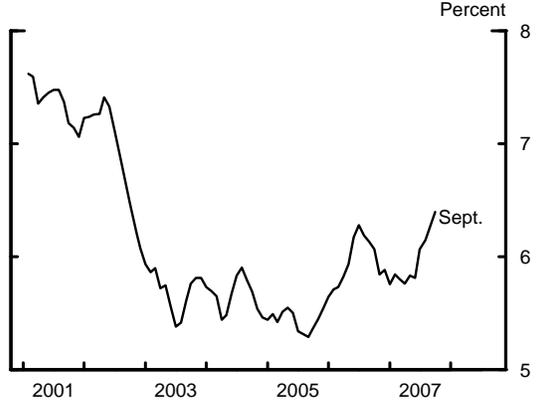
Commercial Real Estate

Investment-Grade CMBS Spreads



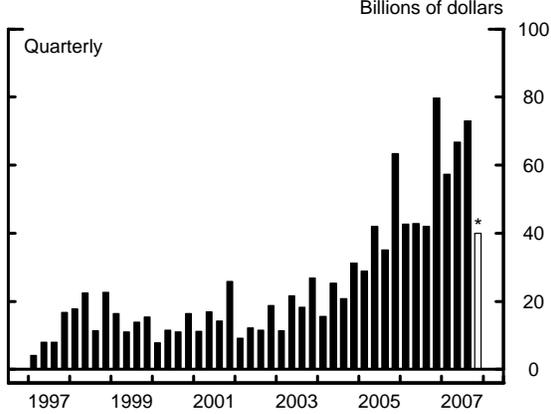
Note. Measured relative to the 10-year Treasury yield.
Source. Morgan Stanley.

Interest Rate on Securitized Mortgages



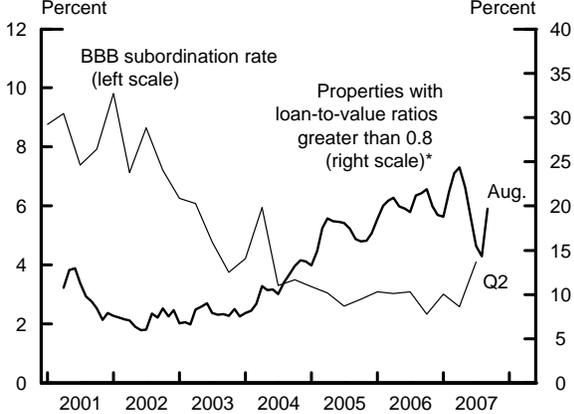
Source. Real Capital Analytics.

Gross Issuance of CMBS



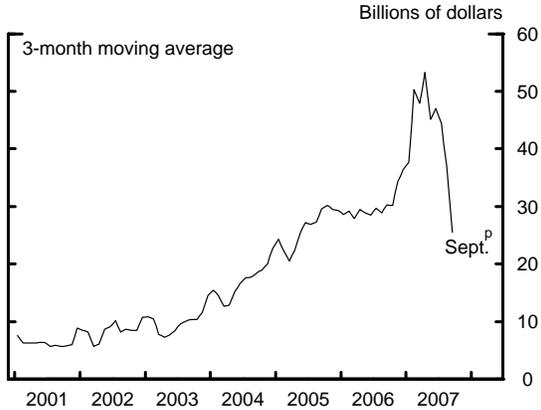
Source. Commercial Mortgage Alert.

Leverage on Newly Securitized Mortgages



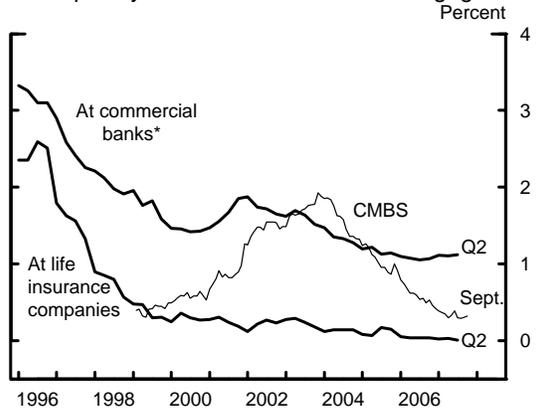
Source. Real Capital Analytics, Commercial Mortgage Alert.

Sales of Commercial Real Estate



^p Preliminary
Source. Real Capital Analytics.

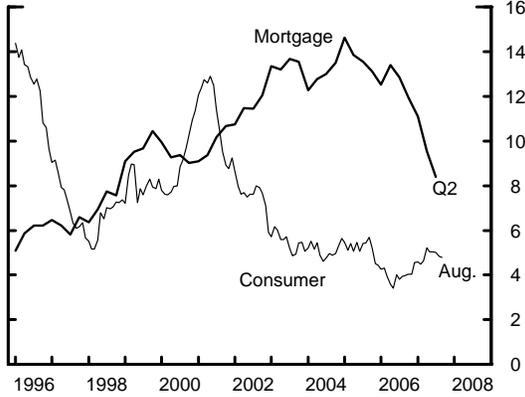
Delinquency Rates on Commercial Mortgages



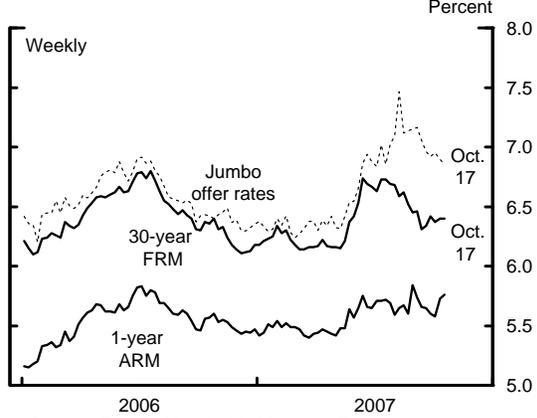
* Excluding construction, land development, and multifamily loans.
Source. Citigroup, Call Report, ACLI.

Household Liabilities

Mortgage Debt and Consumer Credit
Percent change from year earlier

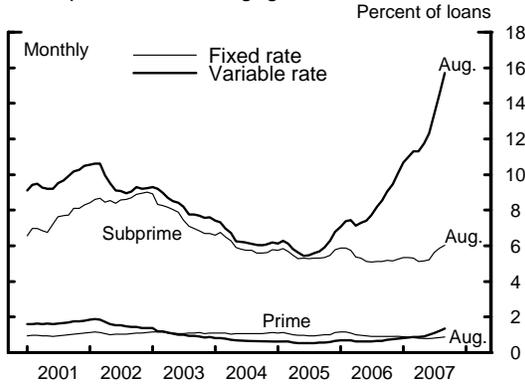


Mortgage Rates for Prime Borrowers



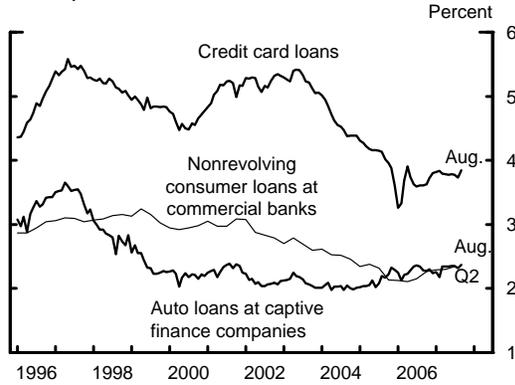
Source: Freddie Mac, Inside Mortgage Finance.

Delinquencies on Mortgages



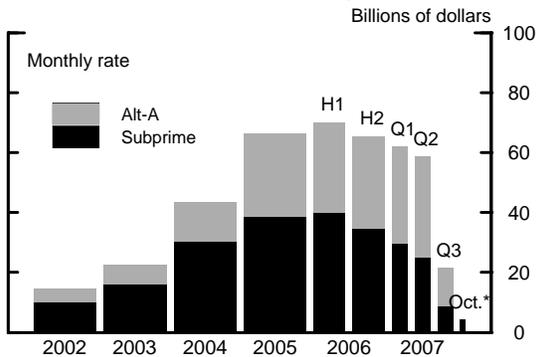
Note: Percent of loans 90 or more days past due or in foreclosure. Prime includes near-prime mortgages.
Source: First American LoanPerformance.

Delinquencies on Consumer Loans



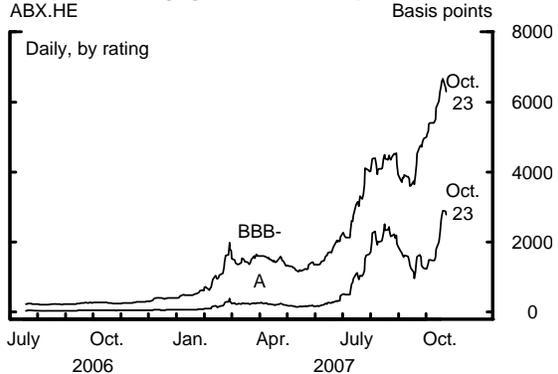
Source: For credit cards, Moody's; for nonrevolving, Call Report; for auto loans, Federal Reserve.

Gross Issuance of Alt-A and Subprime MBS



* Month to date at a monthly rate. Alt-A not yet available.
Source: Inside Mortgage Finance MBS database.

Subprime Mortgage CDS Index Spreads



Note: Measured relative to libor. Each index corresponds to pools of mortgages securitized in 2006:H1.
Source: JP Morgan.

pushed up interest rates on commercial mortgages originated for securitization to their highest levels since late 2002.

Issuance of CMBS was robust in the third quarter, primarily because of a backlog of loans that were originated earlier this year. However, originations data and the issuance calendar point to a marked slowing of CMBS offerings in the fourth quarter, likely reflecting both the higher cost of capital in recent months and tighter underwriting standards. CMBS issuers have gradually responded to concerns of investors and rating agencies by reducing leverage and increasing credit support in newly issued pools.

Although delinquency rates on commercial mortgages have shown no signs of increasing from their recent low levels, the volume of real estate transactions continues to fall from record highs in the first half of the year, led by a sharp decline in LBOs of REITs, as buyers that had depended on high leverage are withdrawing from the market. Alternate sources of financing such as commercial banks and insurance companies, which historically have had more conservative underwriting standards, picked up market share as CMBS-financed lending contracted.

Household Finance

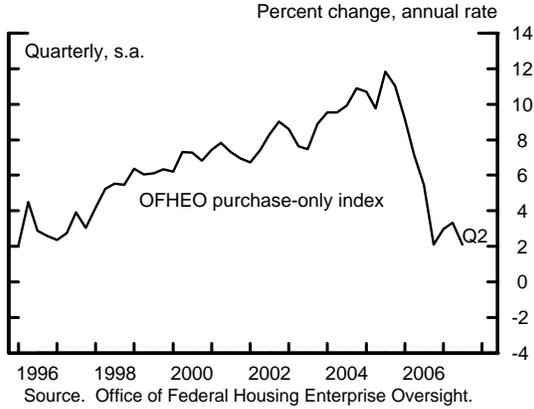
On a year-over-year basis, growth of home mortgage debt slowed in the second quarter, in line with the sharp deceleration in house prices and the drop in home sales. Consumer credit continued to expand moderately through August.

Over the intermeeting period, interest rates on fixed-rate and variable-rate conforming mortgages for prime borrowers increased 6 and 11 basis points respectively. The spread between interest rates offered on jumbo fixed-rate prime mortgages and those on conforming thirty-year loans—our best indicator of pricing in the jumbo market—moved down 17 basis points but remained well above the levels seen earlier this year. Notably, results from the October Senior Loan Officer Opinion Survey indicate that substantial fractions of respondents had tightened standards on prime, as well as nontraditional and subprime, mortgages over the past three months.

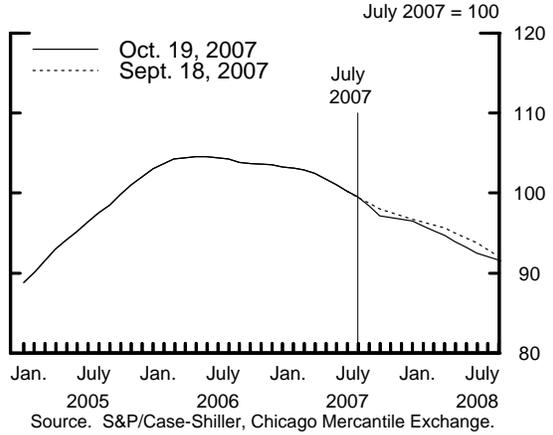
The variable-rate subprime mortgage delinquency rate rose sharply again in August, reaching almost 16 percent. Delinquency rates on subprime fixed-rate mortgages ticked up again in August, but rates on prime mortgages stayed low. Delinquency rates on most consumer loans have also remained at low levels. Nonetheless, a sizable share of

Household Assets

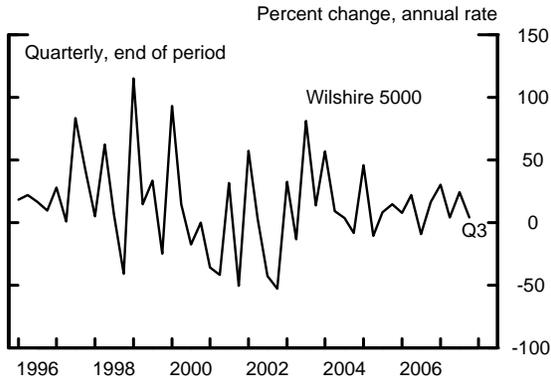
House Prices



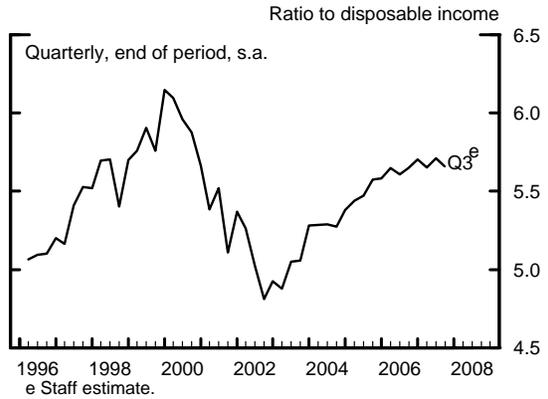
S&P/Case-Shiller House Price Futures



Stock Prices



Net Worth



Net Flows into Mutual Funds (Billions of dollars, monthly rate)

Fund type	2006	2007		2007			Assets Aug.
		Q1	Q2	July	Aug.	Sept. ^e	
Total long-term funds	18.8	39.5	24.2	17.4	-16.4	23.7	8,719
Equity funds	13.1	21.2	8.1	11.6	-12.3	10.8	6,415
Domestic	0.8	6.5	-3.9	-3.4	-14.0	-2.6	4,866
International	12.3	14.7	12.0	14.9	1.7	13.4	1,549
Hybrid funds	0.6	3.3	1.9	1.9	-0.1	1.3	693
Bond funds	5.1	15.0	14.1	3.9	-4.0	11.6	1,611
High-yield	-0.2	0.7	-0.2	-1.7	-1.5	1.4	156
Other taxable	4.0	11.4	12.5	5.5	-1.4	8.7	1,083
Municipals	1.3	2.9	1.8	0.2	-1.2	1.5	373
Money funds	27.4	18.2	39.1	45.4	174.0	91.4	2,778

Note. Excludes reinvested dividends.

^e Staff estimate based on confidential weekly data.

Source. Investment Company Institute.

surveyed banks reported tightening standards for consumer installment loans over the past three months.

Issuance of mortgage-backed securities (MBS) for subprime and Alt-A pools was limited in the third quarter, as underwriters experienced severe difficulties placing these securities with investors. The limited data for October suggest that credit conditions for nonprime MBS remained very tight. Subprime mortgage credit default swap (CDS) index spreads—as measured by the ABX—widened further, and Standard and Poor’s downgraded a large number of securities backed by Alt-A and subprime residential mortgages. In contrast, issuance of credit card and auto asset-backed securities (ABS) was relatively robust in the third quarter and in October.

Available monthly indicators suggest that house prices remained sluggish nationwide in the third quarter. According to futures quotes on the S&P/Case-Shiller indexes, market participants expect a further decline of home prices in ten of the largest metropolitan markets in coming months.

The ratio of household net worth to disposable income likely inched down in the third quarter, held down by soft house prices and stock prices that were roughly flat on net. Long-term mutual funds, which registered net redemptions in August, had solid net inflows into all major fund categories in September, a pattern that continued into October. Assets in money market funds—including both retail and institutional funds—grew rapidly again in September, but the inflow fell well short of August’s record-setting figure.

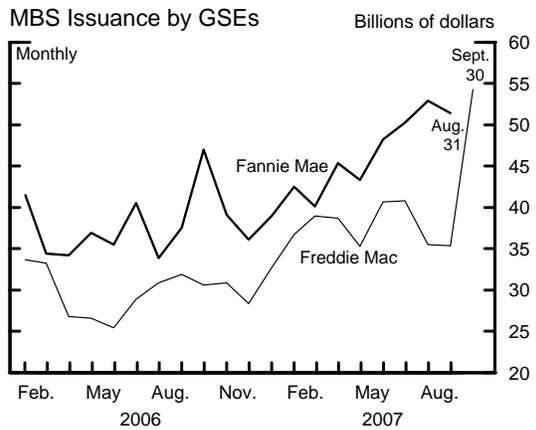
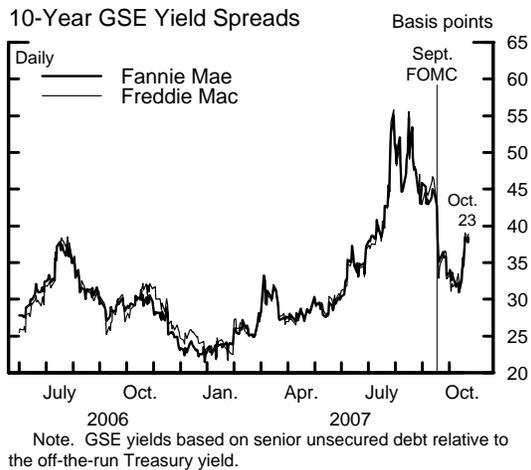
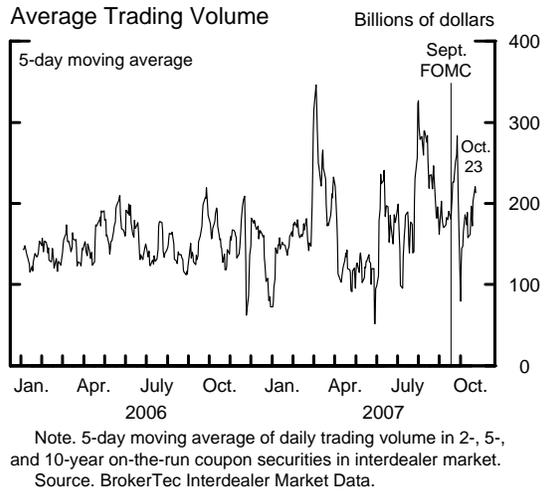
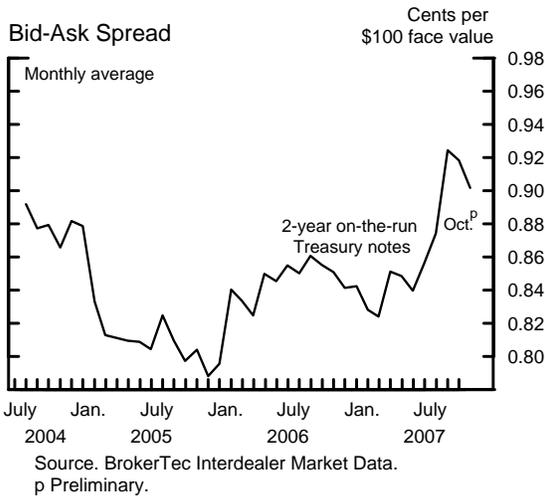
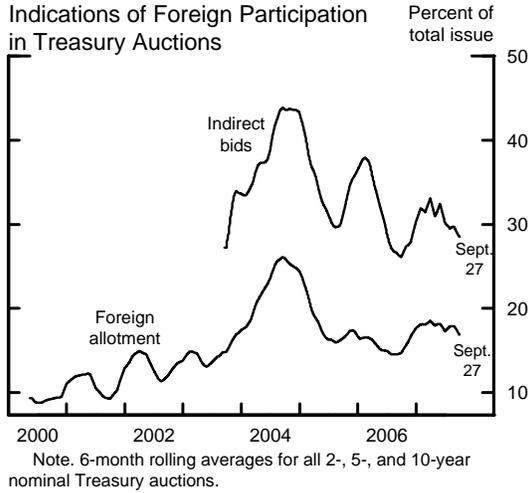
Treasury and Agency Finance

The Treasury conducted auctions of two- and five-year nominal coupon securities and five- and ten-year TIPS over the intermeeting period, and the auctions were generally well received by investors. Liquidity in secondary markets for intermediate and longer-term Treasuries improved somewhat over the intermeeting period, as bid-asked spreads for coupon securities retreated from recent highs. Liquidity premiums for on-the-run two- and ten-year securities were little changed. Spreads on agency debt yields over those on comparable-maturity Treasuries declined slightly on net.

State and Local Government Finance

Gross issuance of long-term municipal bonds for new capital projects, which had dipped somewhat in August, bounced back in September. Advance refundings, however,

Treasury and Agency Finance



State and Local Government Finance

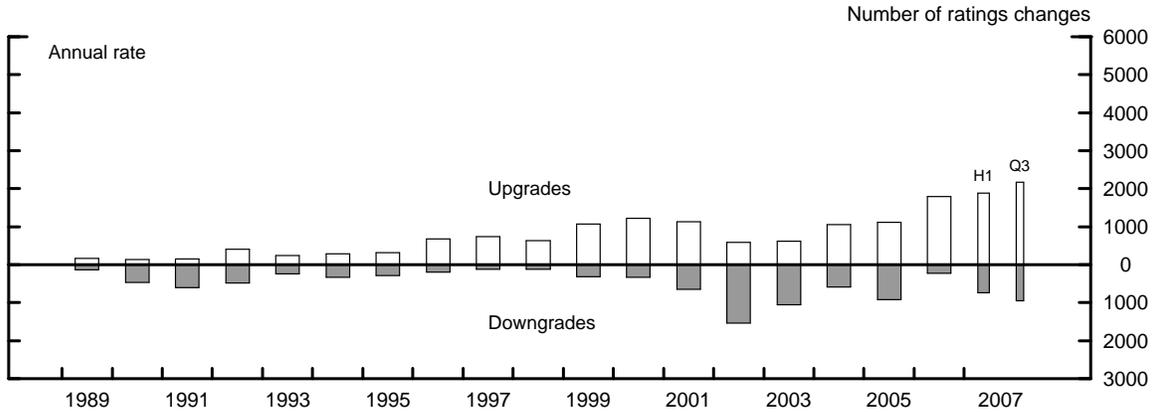
Gross Offerings of Municipal Securities

(Billions of dollars; monthly rate, not seasonally adjusted)

Type of security	2003	2004	2005	2006	2007			
					H1	July	Aug.	Sept.
Total	37.9	34.7	38.4	36.1	41.7	34.5	36.3	37.4
Long-term ¹	32.0	29.8	34.1	32.5	38.4	31.4	27.8	32.1
Refundings ²	10.0	10.8	15.6	10.6	16.3	8.2	7.3	7.3
New capital	22.1	19.0	18.6	21.9	22.0	23.2	20.5	24.8
Short-term	5.8	4.9	4.2	3.7	3.4	3.1	8.5	5.3
Memo: Long-term taxable	3.5	2.0	2.1	2.5	2.1	2.5	1.3	5.1

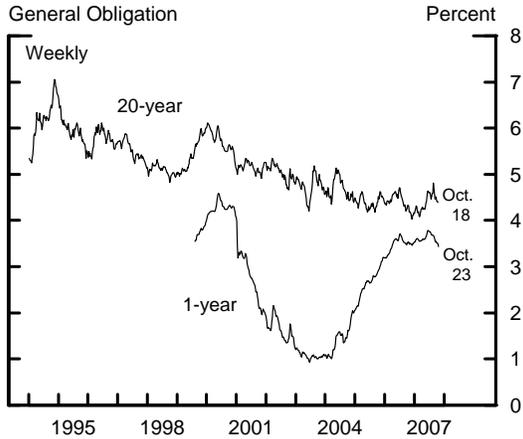
- 1. Includes issues for public and private purposes.
- 2. All issues that include any refunding bonds.

Ratings Changes



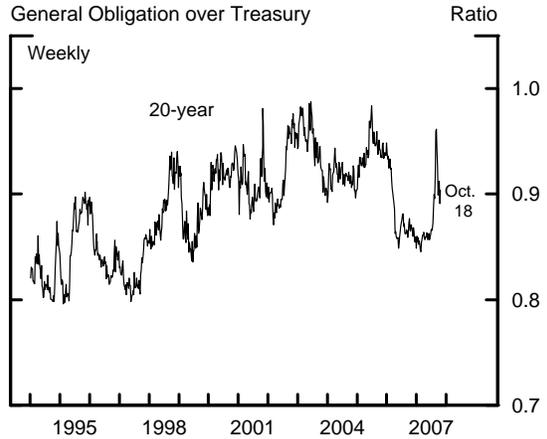
Source: S&P's Credit Week Municipal and Ratings Direct.

Municipal Bond Yields



Source: Municipal Market Advisors and Bond Buyer.

Municipal Bond Yield Ratio



Source: Bond Buyer.

M2 Monetary Aggregate
(Based on seasonally adjusted data)

Aggregate and components	Percent change (annual rate) ¹						Level (billions of dollars), Oct. (e)
	2005	2006	2007				
			H1	Q3	Sept.	Oct. (e)	
M2	4.2	4.9	7.0	5.1	5.2	5.6	7,405
Components ²							
Currency	3.5	3.6	1.9	2.4	2.7	6.3	764
Liquid deposits ³	2.0	.7	6.9	2.7	-1.3	3.0	4,483
Small time deposits	19.4	18.5	4.1	.4	10.4	8.3	1,204
Retail money market funds	.0	12.9	16.3	26.6	32.8	14.3	948
Memo:							
Institutional money market funds	4.8	15.9	20.4	40.0	76.7	51.0	1,769
Monetary base	3.5	3.2	1.9	2.5	-3.5	6.2	827

1. For years, Q4 to Q4; for quarters and months, calculated from corresponding average levels.

2. Nonbank traveler's checks are not listed.

3. Sum of demand deposits, other checkable deposits, and savings deposits.

e Estimated.

remained below their pace over the first half of the year, and short-term issuance slowed, following its typical seasonal pattern.

Indicators of municipal-bond credit quality have improved of late. The number of rating upgrades significantly outpaced downgrades in the third quarter. Also, the ratio of municipal bond yields to those on comparable-maturity Treasuries has retraced most of the jump in August, as concerns about the possible exposure of municipal bond insurers to mortgage-related losses diminished.

Money and Bank Credit

M2 grew at an average annual rate of 5½ percent in September and October, about half the pace in August. Small time deposits grew apace, as banks apparently offered attractive rates to help fund their expanding loan portfolios. Assets in retail money market funds rose rapidly. In the third quarter, the velocity of M2 resumed the decline that began about a year ago.

Commercial bank credit grew vigorously again in September, as C&I loans expanded at an annual rate of 44 percent, the fastest monthly pace in more than thirty years. The surge in C&I loans occurred primarily at large banks and banks affiliated with securities firms—institutions that likely retained on their books loans that had been intended for syndication. That said, C&I loan growth at smaller banks was solid as well. Most other loan categories also expanded briskly in September, but non-home-equity mortgage loans were about flat after adjusting for thrift acquisitions by banks. Bank credit continued to surge in the first two weeks of October, driven by C&I lending and acquisitions of securities. The hefty increase in bank credit comes despite indications, from the October Senior Loan Officer Opinion Survey, that banks had tightened standards and terms for C&I loans, commercial mortgages, prime and nonprime mortgages, and consumer loans over the past three months.

Commercial Bank Credit

(Percent change, annual rate, except as noted; seasonally adjusted)

Type of credit	2005	2006	H1 2007	Q3 2007	July 2007	Aug. 2007	Sept. 2007	Level ¹ Sept. 2007
Total	10.5	9.8	9.1	11.9	11.7	16.8	16.1	8,598
<i>Loans</i> ²								
Total	11.6	11.2	9.6	12.0	11.2	19.5	18.6	6,484
To businesses								
Commercial and industrial	13.5	16.4	9.6	24.1	19.5	31.6	44.0	1,336
Commercial real estate	17.1	13.9	11.3	8.1	7.6	7.2	9.8	1,555
To households								
Residential real estate	11.9	7.6	7.8	4.6	6.2	1.7	9.0	1,858
Revolving home equity	13.3	1.4	1.8	6.4	7.1	9.2	11.2	467
Other	11.4	10.0	9.9	3.9	5.8	-8	8.3	1,391
Consumer	3.1	5.9	6.4	10.4	11.9	4.0	11.0	782
Originated ³	.7	6.9	5.1	10.2	15.6	9.0	9.0	1,175
Other ⁴	8.3	12.3	13.3	18.6	16.0	74.4	23.2	953
<i>Securities</i>								
Total	7.5	5.9	7.6	11.8	13.1	8.8	8.4	2,114
Treasury and agency	2.4	1.3	-3.1	4.4	13.8	-.2	-23.0	1,162
Other ⁵	17.5	13.8	23.9	21.7	12.1	20.7	48.9	952

Note. Yearly annual rates are Q4 to Q4; quarterly and monthly annual rates use corresponding average levels. Data have been adjusted to remove the effects of mark-to-market accounting rules (FIN 39 and FAS 115), the consolidation of certain variable interest entities (FIN 46), the adoption of fair value accounting (FAS 159), and the effects of sizable thrift-to-bank and bank-to-thrift structure activity in October 2006 and March 2007 respectively. Data also account for breaks caused by reclassifications.

1. Billions of dollars. Pro rata averages of weekly (Wednesday) levels.

2. Excludes interbank loans.

3. Includes an estimate of outstanding loans securitized by commercial banks.

4. Includes security loans and loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.

5. Includes private mortgage-backed securities, securities of corporations, state and local governments, foreign governments, and any trading account assets that are not Treasury or agency securities, including revaluation gains on derivative contracts.

Appendix

Senior Loan Officer Opinion Survey on Bank Lending Practices

The October 2007 Senior Loan Officer Opinion Survey on Bank Lending Practices addressed changes in the supply of, and demand for, bank loans to businesses and households over the past three months.¹ Special questions in the survey queried banks about changes in their lending policies for backup lines of credit for commercial paper programs and prime nonconforming residential mortgage loans. As in the past two surveys, banks were asked separately about changes in credit standards and demand for prime, nontraditional, and subprime residential mortgages. This appendix is based on responses from fifty domestic banks and twenty foreign banking institutions.

In the October survey, domestic and foreign institutions reported having tightened their lending standards and terms on commercial and industrial (C&I) loans over the previous three months. Both domestic and foreign institutions also reported a tightening of lending standards on commercial real estate loans. On net, domestic banks indicated that demand for C&I loans had weakened over the survey period, whereas foreign institutions reported that demand for these loans was little changed. Both domestic and foreign institutions noted weaker demand for commercial real estate loans over the past three months. In the household sector, domestic banks reported, on net, tighter lending standards and terms on consumer loans other than credit card loans, as well as tighter lending standards on prime, nontraditional, and subprime residential mortgages over the survey period. Lending standards on credit card loans were, by contrast, little changed. Demand for residential mortgages and consumer loans of all types had reportedly weakened, on net, over the past three months.

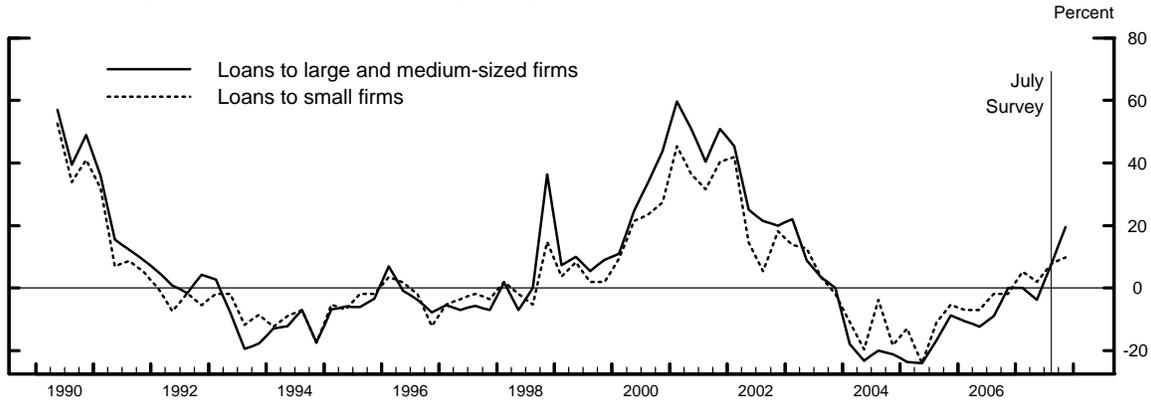
Business Lending

Questions on C&I lending. In the October survey, one-fifth of domestic institutions, on balance, reported that they had tightened their lending standards on C&I loans to large and middle-market firms over the past three months relative to the previous three months. While the net fraction of domestic respondents reporting tighter lending standards over the survey period was only somewhat higher than in the July survey, the fraction of domestic institutions that reportedly increased spreads of loan rates over their cost of funds increased sharply in the October survey, to about one-third. Domestic respondents also reported having tightened several price-related terms on C&I loans to large and middle-market firms over the survey period: Significant net fractions of banks indicated that they had increased the cost of credit lines and premiums charged on loans to riskier borrowers. One-fifth of domestic banks, on net, reported more stringent covenants on loans to large and middle-market firms—the first net tightening of such covenants in a few years.

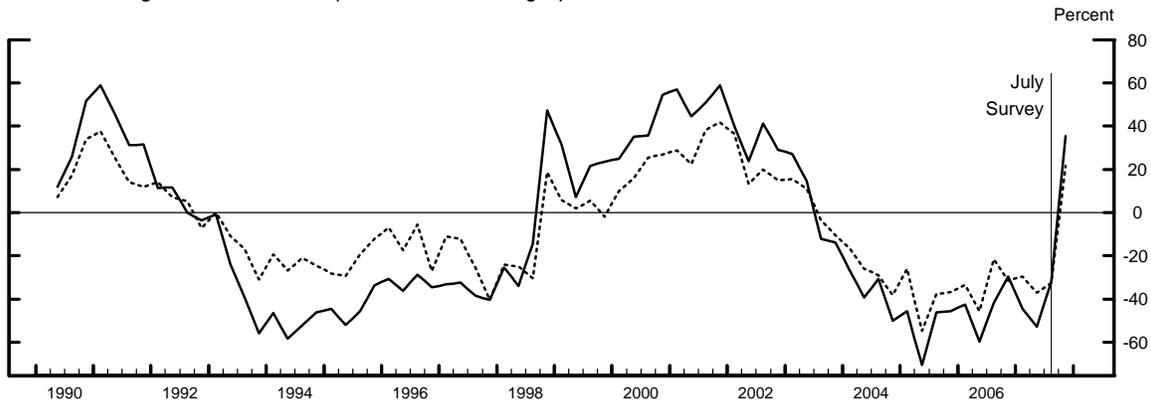
¹ Banks received the survey in early October, and their responses were due October 18.

Measures of Supply and Demand for C&I Loans, by Size of Firm Seeking Loan

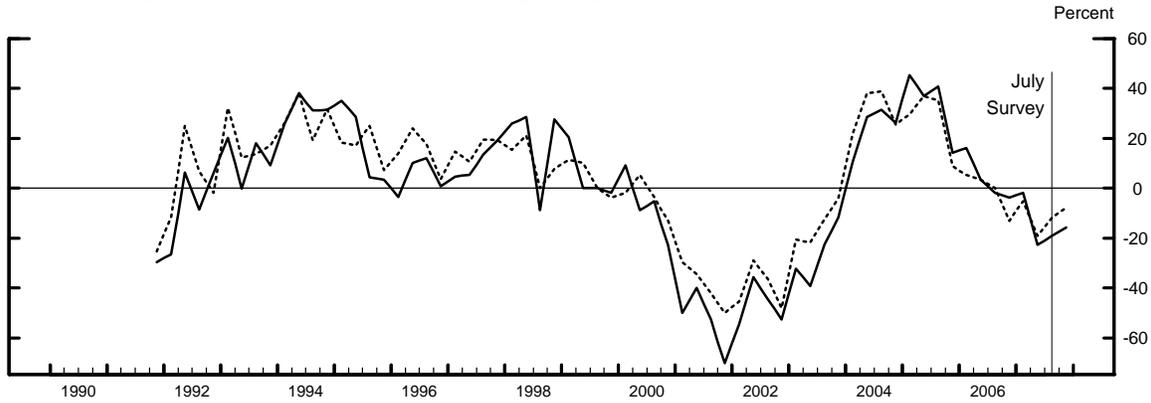
Net Percentage of Domestic Respondents Tightening Standards for C&I Loans



Net Percentage of Domestic Respondents Increasing Spreads of Loan Rates over Banks' Costs of Funds



Net Percentage of Domestic Respondents Reporting Stronger Demand for C&I Loans



Smaller net fractions of domestic banks reported that they had tightened their C&I lending policies for small firms over the past three months. On net, one-tenth of respondents—a fraction similar to that in the July survey—reported tightening their lending standards on C&I loans to small firms, and one-fifth of domestic institutions reported charging higher loan rate spreads on such loans.

Compared with domestic banks, larger net fractions of U.S. branches and agencies of foreign banks reportedly tightened their lending standards and terms on C&I loans over the past three months. About one-third of foreign respondents—up from one-eighth in the July survey—indicated that they had tightened their lending standards on C&I loans. About two-thirds of respondents reportedly widened spreads of loan rates over their cost of funds, and a similar net fraction indicated that they had increased the cost of credit lines and raised premiums charged on loans to riskier business borrowers.

Almost all domestic banks and U.S. branches and agencies of foreign banks that reported having tightened their lending standards and terms on C&I loans pointed to a less favorable economic outlook as a reason for having done so. Large majorities of both domestic and foreign respondents also cited decreased liquidity in the secondary market and reduced tolerance for risk as reasons for a move toward more-stringent lending policies. By contrast, relatively few respondents indicated that concerns about their banks' capital ratios had contributed to the tightening of lending standards and terms.

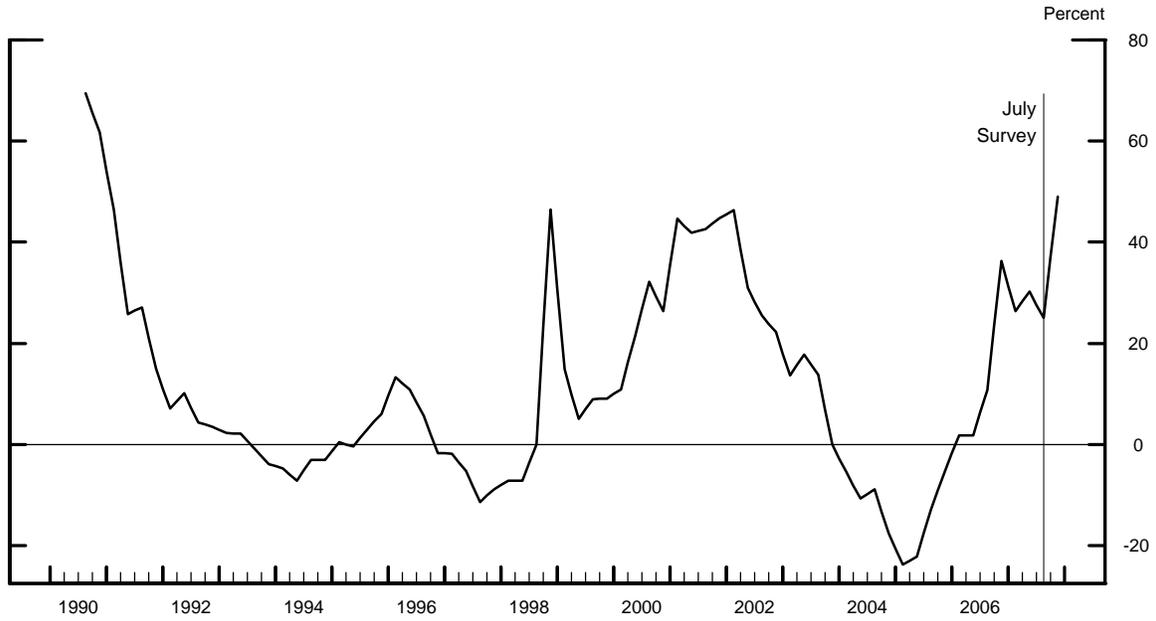
The net fractions of domestic respondents that reported a weakening of demand for C&I loans from large and middle-market firms as well as small firms over the past three months were a bit smaller than in the July survey. About one-eighth of domestic respondents noted weaker C&I loan demand from large and middle-market firms, and one-tenth of banks indicated weaker demand from small firms. The demand for C&I loans at foreign institutions was reportedly unchanged, on net, over the past three months. Regarding future business, about 20 percent of domestic respondents and 10 percent of foreign respondents reported that the number of inquiries from potential business borrowers had decreased relative to the previous three months.

Special questions on commercial paper backup lines of credit. According to the October survey, both domestic and to an even greater extent foreign institutions had tightened, on net, their lending standards and terms for providing backup lines of credit for commercial paper programs over the past three months.² About half of the domestic and two-thirds of the foreign

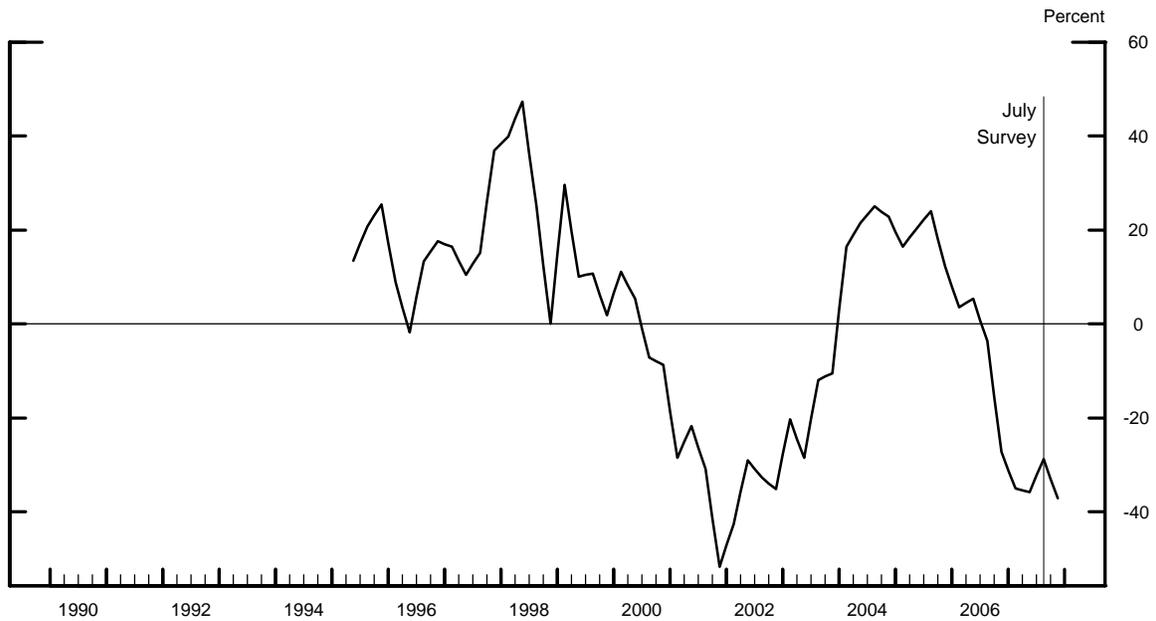
² The number of domestic respondents to this set of special questions varied from sixteen to twenty-six, depending on the question. According to Call Reports, these institutions accounted for between 35 percent and 48 percent of C&I loans on the books of all domestic commercial banks as of June 30, 2007. The number of foreign respondents varied from fourteen to seventeen; these institutions accounted for between 40 percent and 54 percent of C&I loans on the books of all U.S. branches and agencies of foreign banks as of June 30, 2007.

Measures of Supply and Demand for Commercial Real Estate Loans

Net Percentage of Domestic Respondents Tightening Standards for Commercial Real Estate Loans



Net Percentage of Domestic Respondents Reporting Stronger Demand for Commercial Real Estate Loans



respondents reported a tightening of lending standards and terms on backup credit lines for single-seller, multi-seller, and other types of asset-backed commercial paper programs. Furthermore, about 25 percent of domestic and 60 percent of foreign respondents reported that they had tightened lending standards and terms on credit lines for unsecured A2/P2-rated commercial paper programs; less than 10 percent of domestic and about 40 percent of foreign respondents indicated that they had instituted more-stringent lending policies on credit lines for A1/P1-rated commercial paper programs.

Questions on commercial real estate lending. The net fraction of domestic banks that reported having tightened their lending standards for commercial real estate loans over the past three months increased notably, to 50 percent, relative to the July survey. The net fraction of foreign institutions that reported tightening their lending standards on such loans was, at about 40 percent, little changed compared with the July survey. Regarding demand, approximately 38 percent of domestic and foreign institutions—up from about 25 percent in the July survey—reported that demand for commercial real estate loans had weakened over the survey period.

Lending to Households

Questions on residential real estate lending. In the October survey, significant numbers of domestic respondents reported that they had tightened their lending standards on prime, nontraditional, and subprime residential mortgages over the past three months; the remaining respondents indicated that their lending standards had remained basically unchanged. About 45 percent of respondents indicated that they had tightened their lending standards on prime mortgages, compared with only about 15 percent that reported having done so in the July survey.³ Of the thirty-eight banks that originated nontraditional residential loans, about 65 percent—up from around 40 percent in the July survey—reported a tightening of their lending standards on such loans over the past three months.⁴ Finally, five of the eight banks that originated subprime mortgage loans noted that they had tightened their lending standards on such loans, a slightly larger proportion than in the July survey.⁵

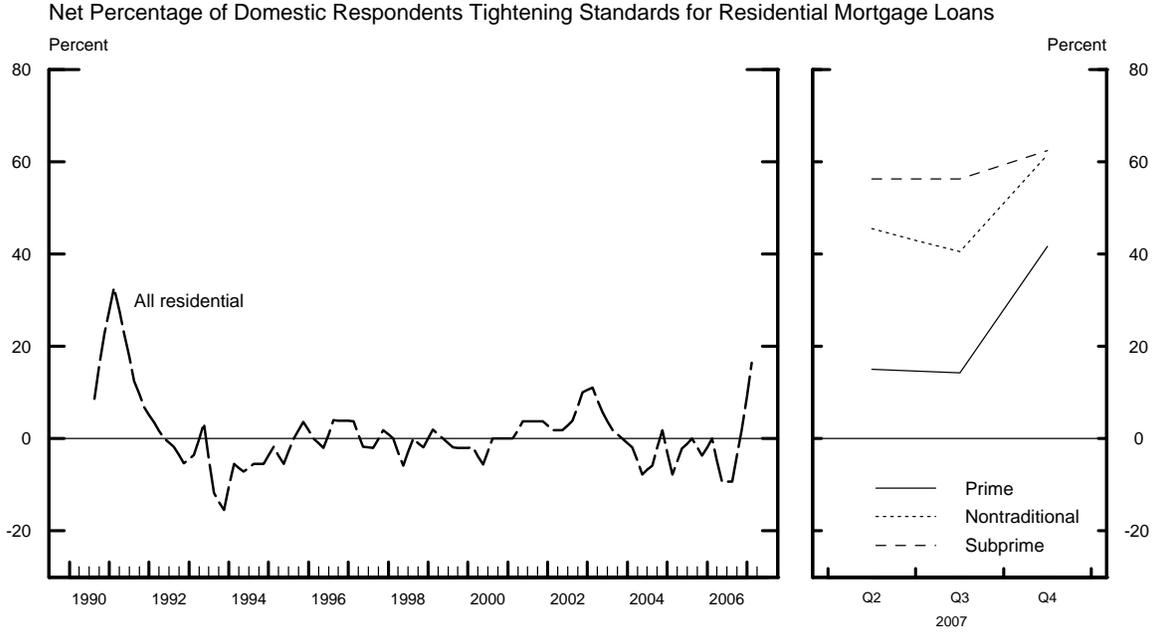
About half of the domestic respondents, on net, indicated that demand for prime, nontraditional, and subprime residential mortgages had weakened further over the past three months. The net fractions reporting weaker demand for prime and nontraditional mortgage loans increased

³ Forty-seven institutions reported that they had originated prime residential mortgages. According to Call Reports, these forty-seven banks accounted for about 73 percent of residential real estate loans on the books of all commercial banks as of June 30, 2007.

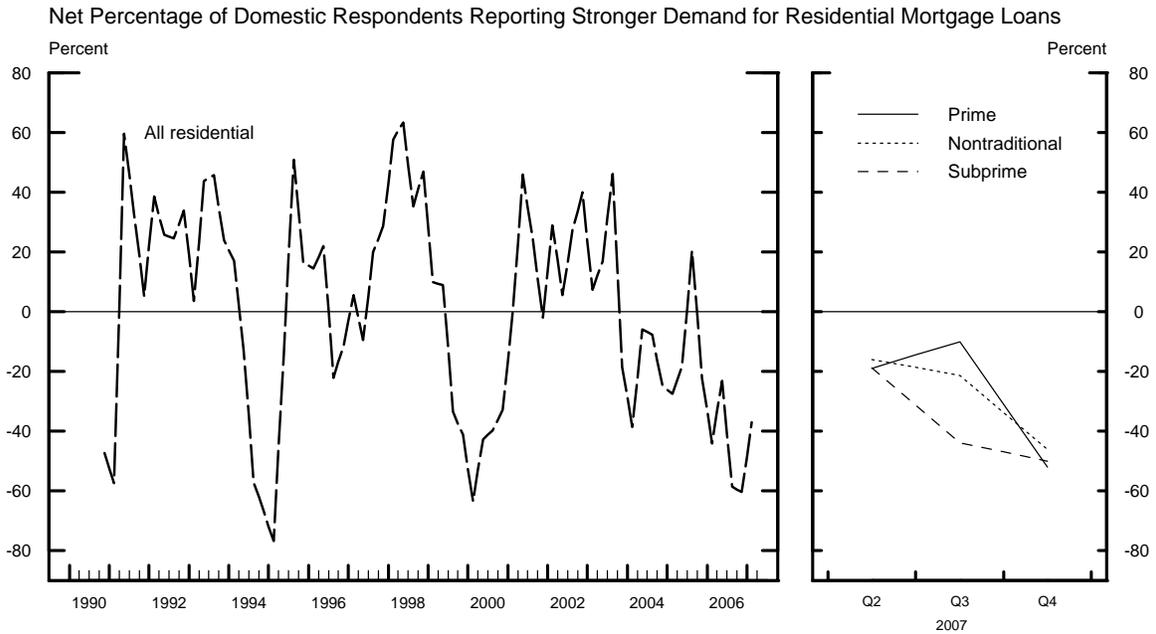
⁴ According to Call Reports, these thirty-eight institutions accounted for about 71 percent of residential real estate loans on the books of all commercial banks as of June 30, 2007.

⁵ According to Call Reports, these eight institutions accounted for about 47 percent of residential real estate loans on the books of all commercial banks as of June 30, 2007.

Measures of Supply and Demand for Residential Mortgage Loans



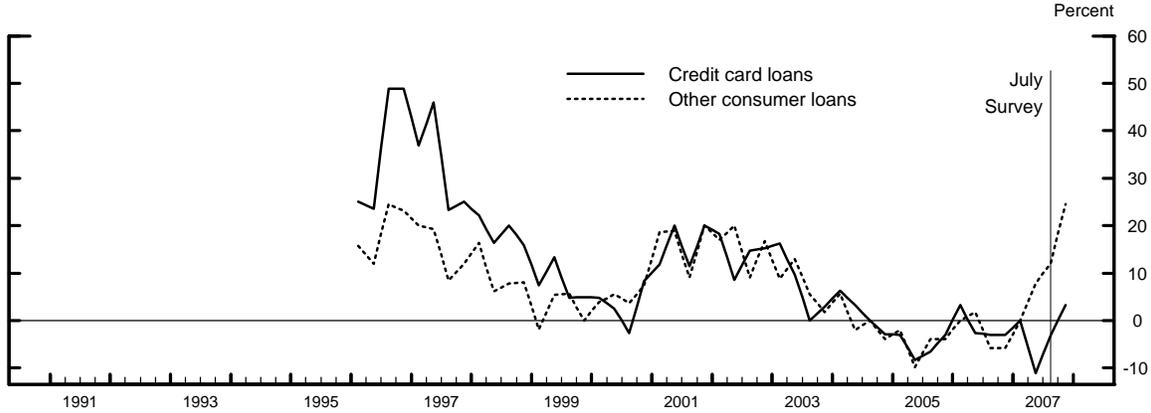
Note. For data starting in 2007:Q2, changes in standards for prime, nontraditional, and subprime mortgage loans are reported separately.



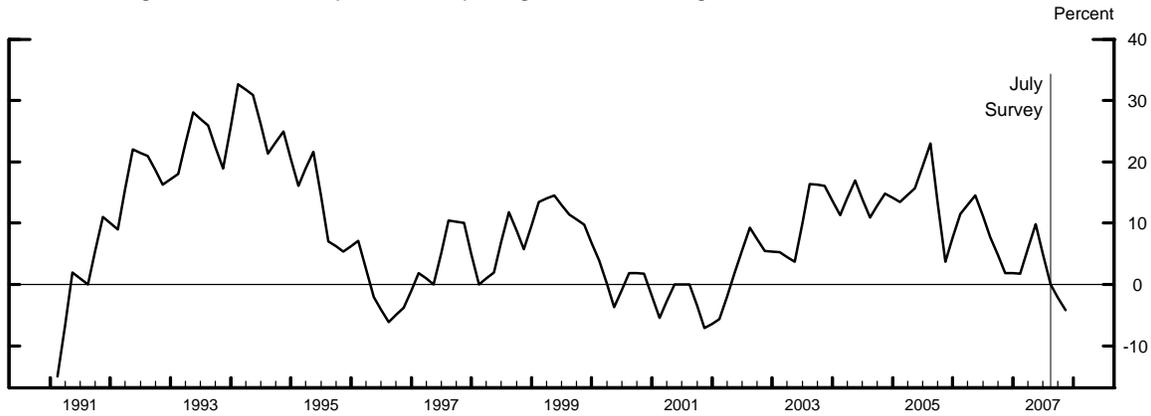
Note. For data starting in 2007:Q2, changes in demand for prime, nontraditional, and subprime mortgage loans are reported separately.

Measures of Supply and Demand for Consumer Loans

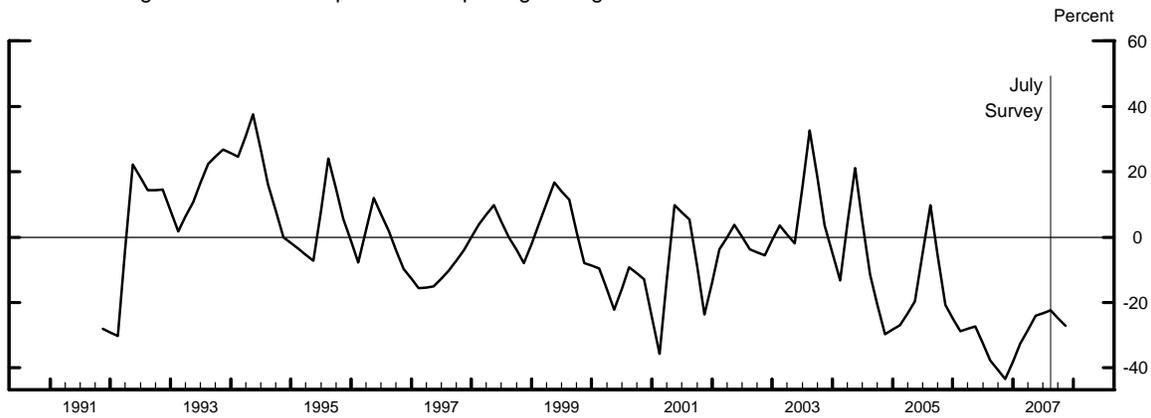
Net Percentage of Domestic Respondents Tightening Standards for Consumer Loans



Net Percentage of Domestic Respondents Reporting Increased Willingness to Make Consumer Installment Loans



Net Percentage of Domestic Respondents Reporting Stronger Demand for Consumer Loans



noticeably compared with the July survey, whereas the net fraction reporting weaker demand for subprime loans was only a little larger than in July.

Special questions on prime jumbo mortgage loans. On net, about 45 percent of domestic respondents indicated that the volume of their banks' originations for prime residential mortgage loans that were above the conforming loan limit had declined over the survey period.⁶ Regarding securitizations of such loans, about 40 percent of respondents reported that the share of new prime jumbo mortgage originations that was securitized over the past three months had declined relative to the previous survey period; the remaining respondents indicated that there had been no substantial change in the share of such securitizations. Domestic banks reportedly tightened several lending terms on prime jumbo loans over the past three months. In particular, significant fractions of respondents reported that they had increased loan fees and spreads of mortgage loan rates over their cost of funds and that they are requiring more-stringent income and asset documentation as well as higher minimum downpayments.

Questions on other consumer lending. One-fourth of domestic banks—up from about 10 percent in the July survey—reported that they had tightened their lending standards on consumer loans other than credit cards over the past three months. Moderate net fractions of banks also indicated that they had tightened lending terms on such loans; in particular, they reduced the extent to which such loans were granted to customers who did not meet credit-scoring thresholds and increased minimum credit scores and spreads of loan rates over their cost of funds. A few banks indicated a diminished willingness to make consumer installment loans relative to three months earlier. Lending standards and terms on credit card loans were reportedly little changed, on balance, over the past three months, although one-tenth of respondents reported that they had widened spreads of loan rates over their cost of funds on such loans.

Last Page of Domestic Financial Developments

⁶ The number of domestic respondents to this set of special questions varied from twenty-eight to forty-five depending on the question. According to Call Reports, these institutions accounted for between 60 percent and 71 percent of residential real estate loans on the books of all commercial banks as of June 30, 2007.

International Developments

International Developments

U.S. International Transactions

Trade in Goods and Services

The U.S. international trade deficit narrowed to \$57.6 billion in August from \$59 billion in July. The narrowing of the deficit reflected both higher exports and lower imports.

Trade in Goods and Services

	2006	Annual rate			Monthly rate		
		2007			2007		
		Q1	Q2	Q3 ^e	June	July	Aug.
Percent change							
<i>Nominal BOP</i>							
Exports	13.3	4.9	14.9	20.0	1.3	2.7	.4
Imports	4.7	3.8	10.1	11.3	.8	1.7	-.4
<i>Real NIPA</i>							
Exports	9.3	1.1	7.5	n.a.	...	...	...
Imports	3.7	3.9	-2.7	n.a.	...	...	...
Billions of dollars							
<i>Nominal BOP</i>							
Net exports	-758.5	-710.3	-710.7	-699.5	-59.4	-59.0	-57.6
Goods, net	-838.3	-803.5	-816.9	-806.1	-68.4	-67.8	-66.6
Services, net	79.7	93.1	106.1	106.6	9.0	8.8	9.0

e. BOP data are two months at an annual rate.

Source. U.S. Department of Commerce, Bureaus of Economic Analysis and Census.

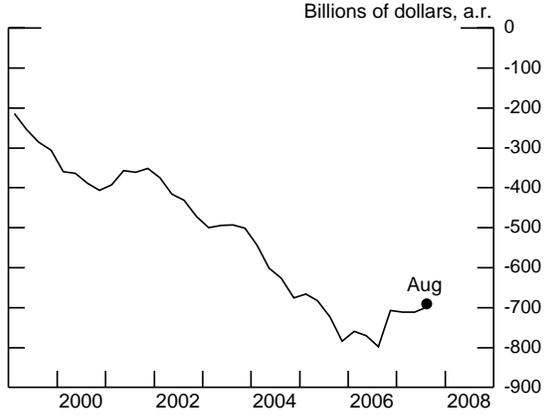
n.a. Not available. ... Not applicable.

In August, the value of exports of goods and services increased 0.4 percent following a 2.7 percent increase in July. The August increase was split between higher exports of services and exports of goods. Goods exports were boosted by a jump in exports of agricultural products and gold, which more than offset a decline in exports of other goods. Exports of automotive products fell back sharply following a surge in July. Exports of capital goods contracted slightly, led by a drop in exports of aircraft. Exports of semiconductors declined, whereas exports of computers were flat.

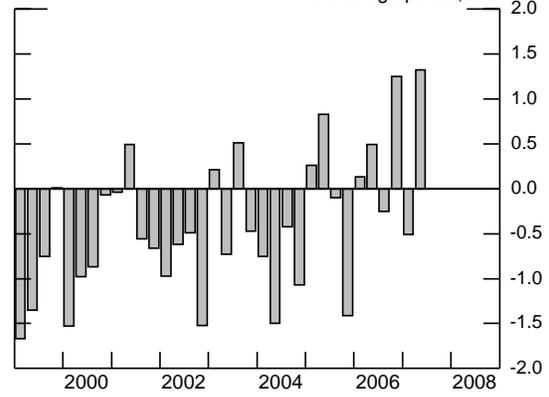
The average value of exports in July and August increased 20 percent (a.r.) from the second quarter. Almost all major categories of exports recorded large increases, with exports of aircraft, automobiles, machinery, industrial supplies, and agricultural goods exhibiting particular strength. In contrast, exports of semiconductors declined.

U.S. International Trade in Goods and Services (Quarterly)

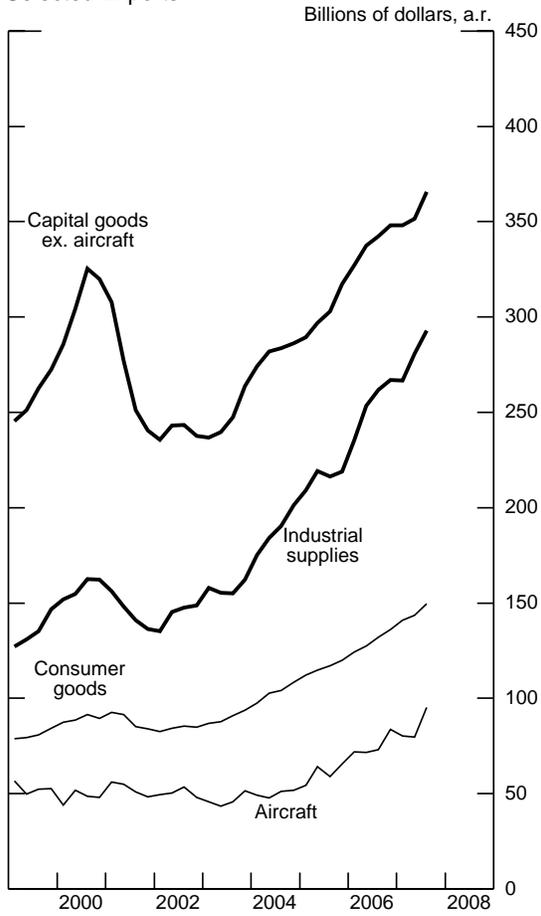
Trade Balance



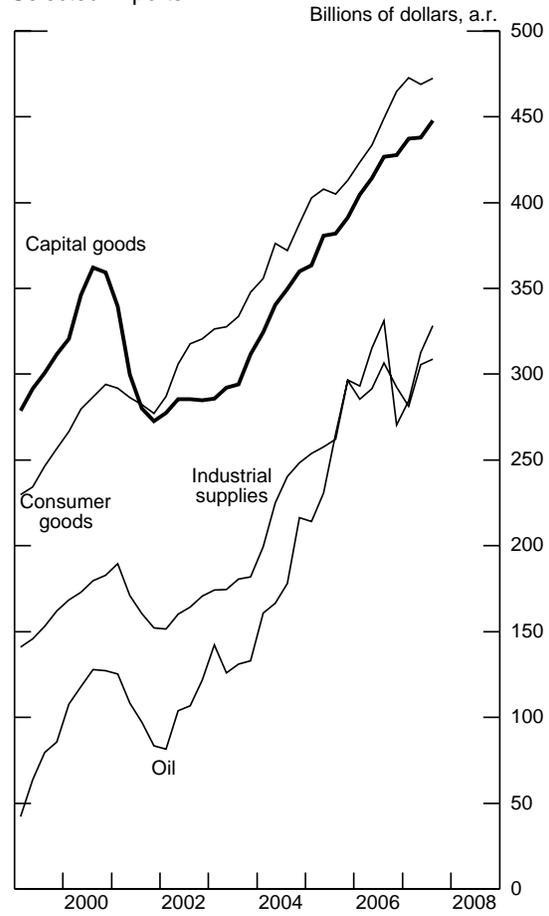
Contribution of Net Exports to Real GDP Growth



Selected Exports



Selected Imports



U.S. Exports and Imports of Goods and Services
(Billions of dollars, a.r., BOP basis)

	Levels				Change ¹			
	2007		2007		2007		2007	
	Q2	Q3 ^e	July	Aug.	Q2	Q3 ^e	July	Aug.
Exports of G&S	1582.8	1656.5	1652.9	1660.0	54.1	73.7	43.7	7.2
Goods exports	1117.4	1185.4	1183.3	1187.5	36.9	68.1	43.8	4.2
Gold	16.5	14.6	12.0	17.3	5.9	-1.9	-5.8	5.3
Other goods	1100.9	1170.8	1171.4	1170.2	31.0	69.9	49.6	-1.1
Capital goods	431.2	461.0	462.3	459.7	3.1	29.8	22.7	-2.6
Aircraft & parts	79.5	95.2	97.7	92.8	-.8	15.7	14.7	-4.9
Computers & accessories	41.9	43.5	43.3	43.8	-3.4	1.7	.7	.5
Semiconductors	49.8	47.5	48.2	46.8	-.4	-2.3	-3.8	-1.4
Other capital goods	260.0	274.7	273.1	276.3	7.8	14.7	10.9	3.2
Automotive	118.0	130.4	136.1	124.7	6.5	12.3	17.3	-11.4
Ind. supplies (ex. ag., gold)	280.7	292.9	292.2	293.6	14.0	12.2	.9	1.4
Consumer goods	143.5	149.6	148.5	150.7	2.6	6.1	6.1	2.2
Agricultural	87.1	96.4	90.8	102.0	7.8	9.3	3.1	11.2
All other goods	40.3	40.6	41.6	39.6	-3.1	.3	.0	-1.9
Services exports	465.4	471.0	469.5	472.5	17.2	5.6	-.1	3.0
Imports of G&S	2293.5	2356.0	2360.9	2351.1	54.6	62.5	38.5	-9.8
Goods imports	1934.2	1991.5	1996.6	1986.4	50.3	57.3	36.4	-10.1
Oil	312.6	328.3	327.1	329.6	29.2	15.8	8.2	2.5
Gold	9.8	10.7	12.1	9.3	1.9	.9	6.5	-2.8
Other goods	1611.9	1652.5	1657.4	1647.6	19.2	40.6	21.7	-9.8
Capital goods	437.9	447.9	445.9	449.9	.4	10.0	-.2	4.0
Aircraft & parts	34.3	34.7	34.4	35.1	1.5	.4	-3.4	.7
Computers & accessories	102.8	99.3	96.8	101.8	-5.7	-3.5	-7.2	5.0
Semiconductors	26.0	26.5	25.3	27.7	-1.0	.4	-.3	2.4
Other capital goods	274.8	287.4	289.5	285.3	5.6	12.6	10.7	-4.2
Automotive	252.3	268.8	271.1	266.5	-1.1	16.5	13.1	-4.5
Ind. supplies (ex. oil, gold)	305.5	308.8	313.4	304.2	24.2	3.4	2.7	-9.2
Consumer goods	468.8	472.3	473.5	471.1	-4.2	3.5	2.6	-2.4
Foods, feeds, bev.	80.3	83.7	83.3	84.1	.2	3.3	2.5	.8
All other goods	67.1	71.0	70.2	71.7	-.4	3.9	1.0	1.6
Services imports	359.3	364.5	364.3	364.6	4.3	5.2	2.1	.3
<i>Memo:</i>								
Oil quantity (mb/d)	13.41	12.84	12.90	12.78	-.91	-.57	-.38	-.12
Oil import price (\$/bbl)	63.82	70.01	69.41	70.61	9.48	6.20	3.69	1.20

1. Change from previous quarter or month. e. Average of two months.

Source. U.S. Department of Commerce, Bureaus of Economic Analysis and Census.

The value of imported goods and services fell 0.4 percent in August after increasing 1.7 percent in July. The decline reflected lower imports of goods, as imports of services were flat. Higher imports of oil and capital goods, particularly computers and semiconductors, were more than offset by lower imports of non-oil industrial supplies, automotive products, and consumer goods. A large decline in imports of natural gas, largely reflecting lower prices, contributed to the decline in non-oil industrial supplies, while weaker imports of pharmaceuticals helped hold back consumer goods.

The average value of imports in July and August increased 1 1/4 percent (a.r.) from the second quarter. All major categories of imports increased over the period, with imports of automotive products, oil, and capital goods making the largest contributions to the increase.

Prices of Internationally Traded Goods

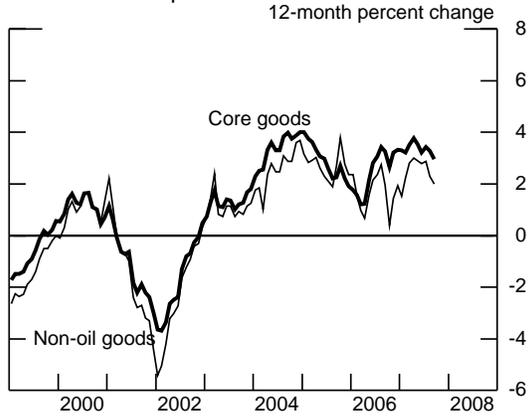
Non-oil imports. In September, prices of U.S. imports of core goods fell 0.1 percent, the first decline since February. Lower prices for industrial supplies, particularly metals, were behind the decline. For the third consecutive month, prices for imported foods rose sharply, increasing 1.2 percent. Prices for imported finished goods rose 0.2 percent for the fourth straight month. After increasing in August, prices for imported computers and semiconductors both fell in September. Prices for imported natural gas fell 4.2 percent in September, following a 12.6 percent decline in August.

The average level of imported core goods prices in the third quarter was 3 percent at an annual rate above the second-quarter level. Prices for material-intensive goods were up 4 3/4 percent, lifted by higher prices for foods, whereas prices for finished goods increased 2 1/2 percent. Prices for semiconductors were up 3 3/4 percent after a steep second-quarter decline of 16 1/4 percent. In the third quarter, prices for imported natural gas fell 52 percent at an annual rate.

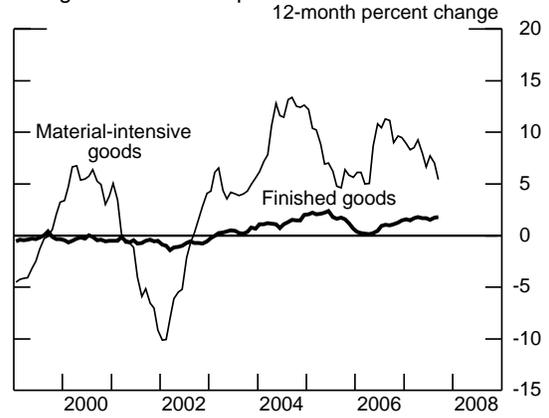
Oil. The BLS price index of imported oil rose 5.4 percent in September, following a 1.1 percent decrease in August, since January, the price of imported oil has increased about 40 percent. The spot price of West Texas Intermediate (WTI) crude oil increased 10 percent in September to average about \$80 per barrel for the month as a whole. In October, the spot price of WTI crude oil surged, peaking at \$89.48 on October 18. The spot price has subsequently edged down, closing at \$86.48 on October 23. Support for the high level of oil prices appears to have come in part from concerns about the level of inventories, both in the United States and abroad, going into the high-demand winter

Prices of U.S. Imports and Exports

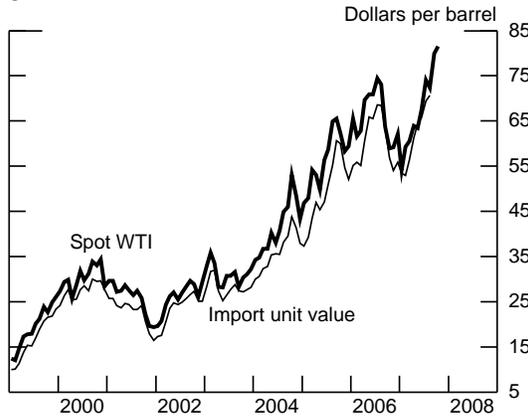
Merchandise Imports



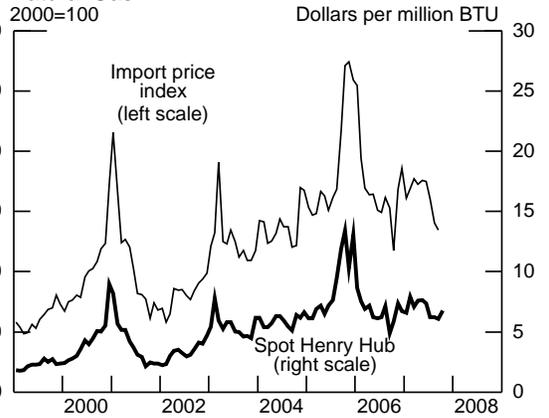
Categories of Core Imports



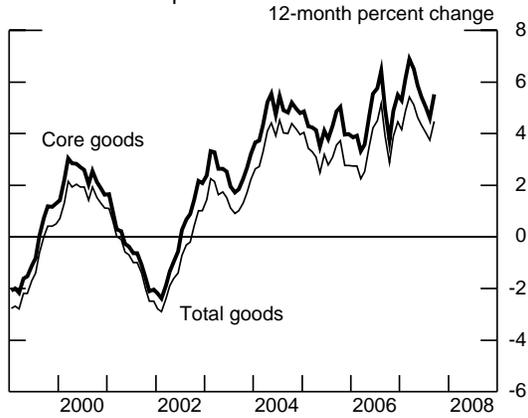
Oil



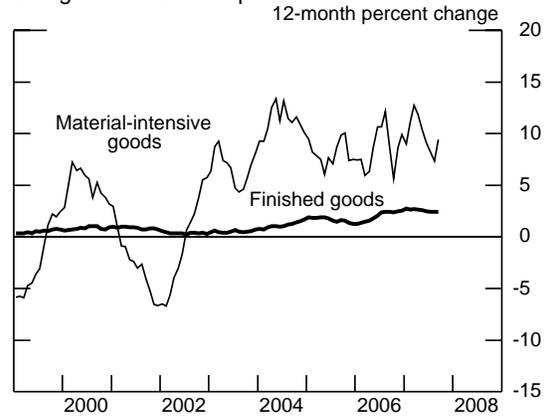
Natural Gas



Merchandise Exports



Categories of Core Exports



Prices of U.S. Imports and Exports
(Percentage change from previous period)

	Annual rate			Monthly rate		
	2007			2007		
	Q1	Q2	Q3	July	Aug.	Sept.
	----- BLS prices -----					
Merchandise imports	1.8	15.2	10.3	1.3	-.3	1.0
Oil	-3.2	89.0	54.3	6.0	-1.1	5.4
Non-oil	2.6	3.8	1.4	.1	-.1	-.2
Core goods ¹	3.4	4.6	3.1	.2	.2	-.1
Finished goods	1.8	1.4	2.4	.2	.2	.2
Cap. goods ex. comp. & semi.	3.1	3.1	4.1	.4	.3	.1
Automotive products	.3	.9	1.5	.1	.2	.2
Consumer goods	1.9	.4	1.9	.2	.2	.2
Material-intensive goods	6.4	12.3	4.7	.3	.2	-.5
Foods, feeds, beverages	9.8	8.4	10.7	1.3	.5	1.2
Industrial supplies ex. fuels	3.8	13.3	3.3	.0	.2	-1.1
Computers	-9.5	-7.7	-.9	.2	.2	-.2
Semiconductors	-6.8	-16.2	3.7	.5	.2	-.4
Natural gas	33.6	13.0	-52.0	-8.1	-12.6	-4.2
Merchandise exports	7.2	6.1	2.8	.1	.2	.3
Core goods ²	9.3	7.3	3.1	.1	.3	.4
Finished goods	3.6	2.4	1.9	.2	.1	.1
Cap. goods ex. comp. & semi.	4.4	2.7	2.5	.3	.2	.2
Automotive products	1.7	.9	.8	.1	.0	.1
Consumer goods	3.4	3.2	2.0	.3	.1	.0
Material-intensive goods	17.0	13.7	4.4	-.1	.4	.8
Agricultural products	27.8	7.0	24.0	1.6	1.1	4.1
Industrial supplies ex. ag.	14.1	16.4	-.3	-.7	.2	-.2
Computers	-12.8	-11.1	-4.2	-.6	-.3	-.1
Semiconductors	-.8	4.2	.6	.0	-.1	.1
	----- NIPA prices -----					
Chain price index						
Imports of goods & services	1.0	11.9	n.a.	...	...	...
Non-oil merchandise	2.1	2.7	n.a.	...	...	...
Core goods ¹	2.7	3.6	n.a.	...	...	...
Exports of goods & services	3.6	5.3	n.a.	...	...	...
Total merchandise	3.5	5.1	n.a.	...	...	...
Core goods ²	6.0	7.4	n.a.	...	...	...

1. Excludes computers, semiconductors, and natural gas.

2. Excludes computers and semiconductors.

n.a. Not available. ... Not applicable.

months. These concerns were exacerbated by threats of a Turkish invasion into Iraq, which could disrupt oil supplies from the region. In addition, market participants appear highly skeptical that OPEC will act to alleviate near-term tightness in the oil market.

Exports. Prices of U.S. exports of core goods rose 0.4 percent in September. After three months of large increases, prices for agricultural exports jumped 4.1 percent in September. Higher prices for corn, wheat, and soybeans accounted for much of the increase. Prices for nonagricultural industrial supplies fell 0.2 percent, as lower prices for chemicals, copper, and aluminum offset higher prices for fuel and steel-making materials. Prices for exported finished goods rose 0.1 percent in September, a rate similar to that observed in August. Prices for exported computers fell 0.1 percent, whereas prices for semiconductors moved up.

The average level of exported core goods prices in the third quarter was 3 percent at an annual rate above the second-quarter level. In the third quarter, prices for agricultural products were up 24 percent, whereas prices for nonagricultural industrial supplies were little changed. Prices for finished goods rose 2 percent, reflecting higher prices for consumer goods and capital goods excluding computers and semiconductors. After sharp price declines in the first half of 2007, the rate of deflation for computer export prices slowed in the third quarter.

U.S. International Financial Transactions

This summer's financial market turmoil had a noticeable effect on U.S. financial flows in August. Foreign private purchases of U.S. Treasury securities spiked up to a record \$45 billion in an apparent "flight to safety" (line 4a of the Summary of U.S. International Transactions table). These large purchases of U.S. Treasuries in August were more than offset by exceptionally large sales of other U.S. securities. Private foreigners sold \$39 billion in corporate stocks (line 4d), and foreign demand for U.S. debt was also weak, with foreign residents selling, on net, \$12 billion of corporate and municipal bonds (line 4c) and \$5 billion of agency bonds (line 4b). We note that the reductions in private foreigners' holdings of bonds coincided with unusually low issuance of U.S. corporate bonds during the third quarter, about half the pace of issuance recorded in the first half of the year. On balance, foreign investors sold \$11 billion of U.S. securities in August (line 4). With the exception of agency bonds, these securities flows are unprecedented and are in sharp contrast to recent trends (top panels of the chart on Private Security Flows).

Flows from foreign official investors also deviated from past patterns. Foreign official investors recorded an outflow of \$18 billion in August, compared to an inflow of \$46 billion in July (line 1). Declines in U.S. holdings by foreign official investors are unusual (the last one was in April 2003), and the magnitude of the decline in August was large (top-left panel of the chart on Foreign Official Financial Flows).

U.S. transactions in foreign securities appear to have been less affected by the turmoil. After a relatively weak July, U.S. acquisitions of foreign securities picked up to \$36 billion in August (line 5), bringing the average for the two months back to near its pace of the first half of the year (bottom-left panel of the chart on Private Security Flows).

Monthly data for the banking sector (line 3) show a record net outflow of \$100 billion during August, compared with a net inflow of \$58 billion during July. Much of this swing can be attributed to the market turmoil, as the spread between the repo and Treasury rates shifted up markedly during the last week of August and nearly two-thirds of the outflow was associated with a reduction in U.S. bank borrowings from foreigners via RPs.

Combining all the monthly recorded flows, for both official and private transactions, yields a net outflow of \$165 billion for August. However, this figure does not include direct-investment flows, which are recorded only quarterly. Also, data on U.S. residents' holdings of foreign short-term securities, such as foreign commercial paper, are only available quarterly; a reduction in U.S. holdings of these securities represents a financial inflow (included in line 10) that would help close the apparent gap between the current account and the flows that finance it. Further, the relative stability of the dollar in August suggests that the net demand for U.S. assets (from both domestic and foreign investors) did not decline appreciably, although the composition of that demand shifted from what has prevailed in recent months.

Summary of U.S. International Transactions
(Billions of dollars, not seasonally adjusted except as noted)

	2005	2006	2006		2007			
			Q3	Q4	Q1	Q2	Jul	Aug
Official financial flows	272.0	445.2	109.6	87.5	149.4	71.7	45.8	-18.3
1. Change in foreign official assets in the U.S. (increase, +)	257.9	442.8	108.6	86.1	149.4	71.7	45.7	-18.2
a. G-10 countries + ECB	12.8	21.4	6.6	10.0	9.1	6.2	6.7	-2.7
b. OPEC	14.0	44.2	13.1	-7.8	11.2	0.4	-0.4	2.5
c. All other countries	231.1	377.3	88.9	83.9	125.2	69.1	39.4	-17.9
2. Change in U.S. official reserve assets (decrease, +)	14.1	2.4	1.0	1.4	-0.1	0.0	0.1	-0.1
Private financial flows	505.3	388.0	145.4	137.7	32.6	79.2	...	...
Banks								
3. Change in net foreign positions of banking offices in the U.S. ¹	15.4	126.4	54.2	22.1	-15.4	19.2	57.8	-99.8
Securities²								
4. Foreign net purchases (+) of U.S. securities	573.9	562.6	126.3	170.1	172.3	245.2	-1.7	-10.7
a. Treasury securities	133.7	-24.9	-15.9	32.8	46.4	0.7	1.5	45.2
b. Agency bonds	37.0	22.5	0.3	-6.1	-32.0	29.0	-11.7	-5.0
c. Corporate and municipal bonds	311.2	416.1	106.0	114.6	114.2	110.2	-9.9	-11.9
d. Corporate stocks ³	92.0	148.8	35.9	28.8	43.7	105.4	18.4	-39.0
5. U.S. net acquisitions (-) of foreign securities	-197.0	-291.2	-52.9	-119.3	-86.1	-81.9	-7.3	-36.2
a. Bonds	-53.1	-152.1	-44.8	-53.4	-41.6	-41.1	0.2	-22.3
b. Stock purchases	-139.9	-120.3	-8.0	-53.5	-40.3	-40.8	-7.5	-13.9
c. Stock swaps ³	-4.0	-18.8	0.0	-12.4	-4.2	0.0	0.0	0.0
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	7.7	-235.4	-49.0	-66.1	-81.4	-71.5	...	...
7. Foreign direct investment in the U.S.	109.0	180.6	43.0	45.6	11.9	73.6	...	...
8. Net derivatives (inflow, +)	n.a.	28.8	15.1	-1.1	14.8	-1.0	...	...
9. Foreign acquisitions of U.S. currency	19.0	12.6	1.1	8.4	-1.6	3.3	...	...
10. Other (inflow, +) ⁴	-22.6	3.7	7.4	78.1	18.1	-107.6	...	...
U.S. current account balance (s.a.)	-754.8	-811.5	-217.3	-187.9	-197.1	-190.8	...	...
Capital account balance (s.a.)⁵	-4.1	-3.9	-0.5	-0.6	-0.6	-0.6	...	...
Statistical discrepancy (s.a.)	-18.5	-17.8	-37.1	-36.6	15.7	40.4	...	...

Note. Data in lines 1 through 5 differ in timing and coverage from the balance of payments data published by the Department of Commerce. Details may not sum to totals because of rounding.

1. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements). Includes changes in custody liabilities other than U.S. Treasury bills.

2. Includes commissions on securities transactions and therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. Includes (4d) or represents (5c) stocks acquired through non-market means such as mergers and reincorporations.

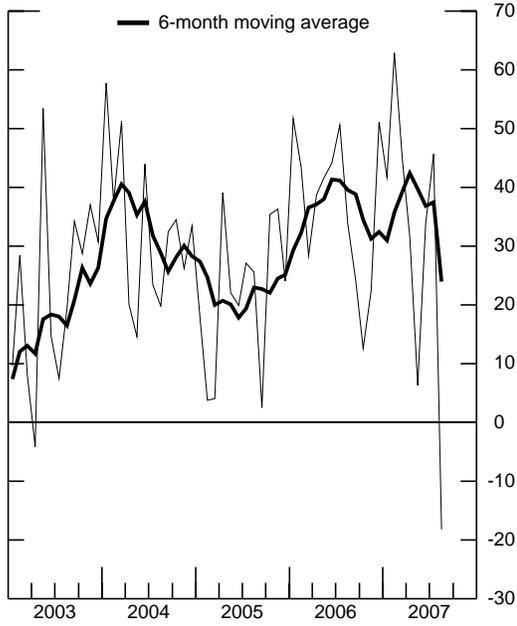
4. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business.

5. Consists of transactions in nonproduced nonfinancial assets and capital transfers.

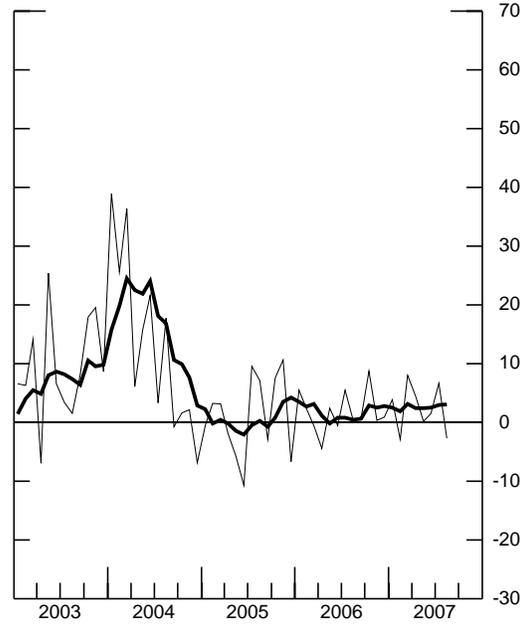
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Foreign Official Financial Flows Through August 2007 (increase, +)
 (\$ Billions, monthly, not seasonally adjusted)

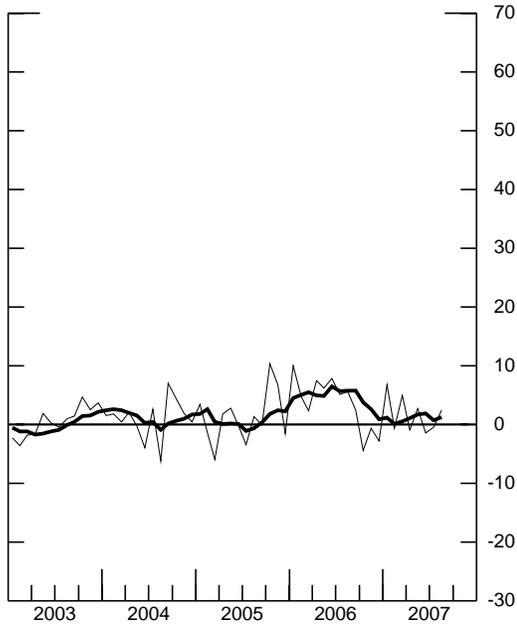
Total



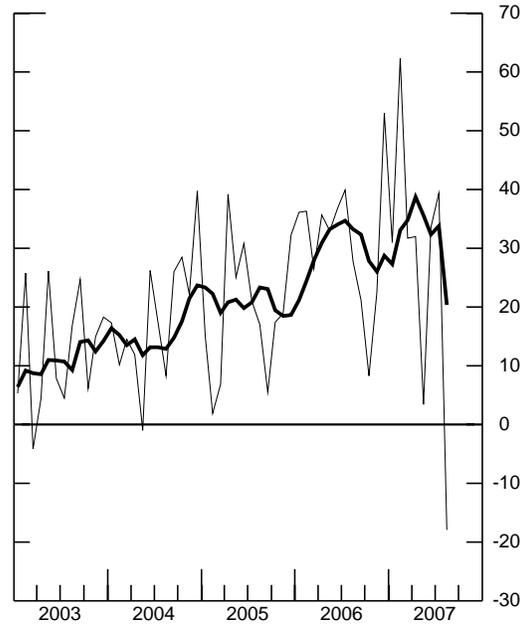
G-10 + ECB



OPEC

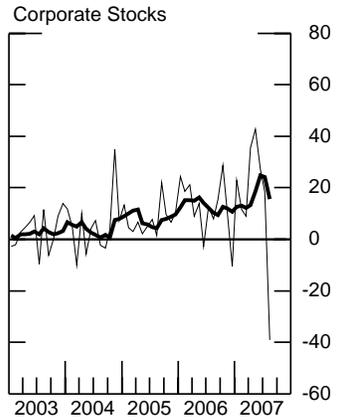
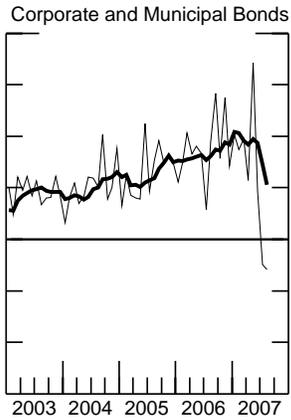
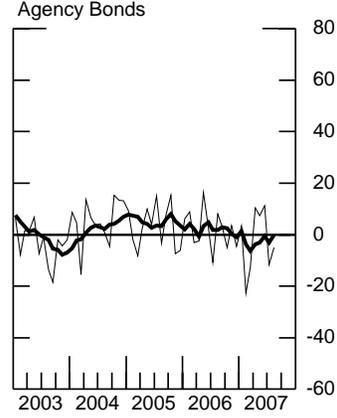
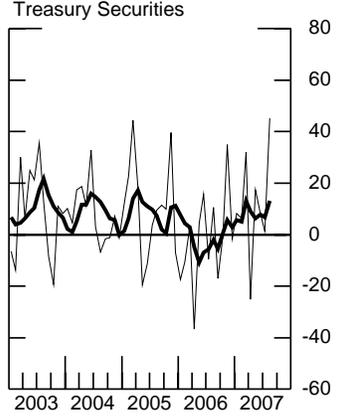
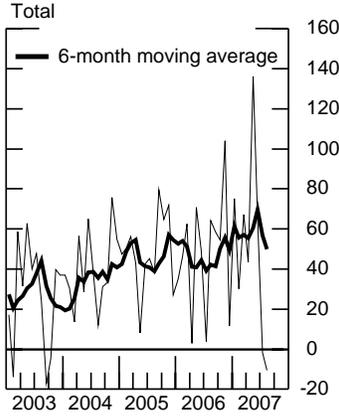


All other countries

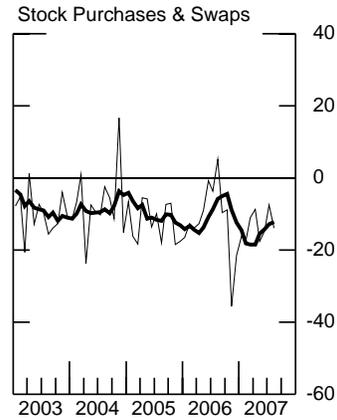
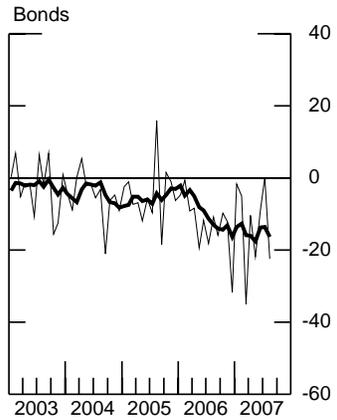
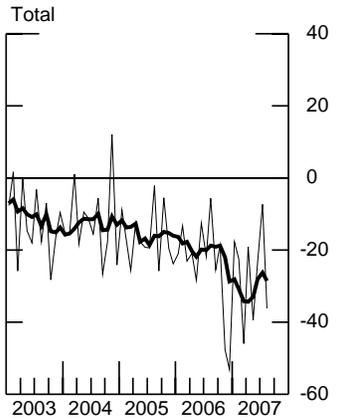


Private Securities Flows Through August 2007
 (\$ Billions, monthly, not seasonally adjusted)

Foreign Net Purchases (+) of U.S. Securities



U.S. Net Acquisitions (-) of Foreign Securities



Foreign Financial Markets

Following the larger-than-expected cut in the federal funds target announced on September 18, equity prices rose across the globe and risk spreads and implied volatilities on a wide range of assets declined. These movements continued for several weeks after the FOMC meeting. Although equity markets gave back some of their gains and risk spreads rose late in the period in response to weak US housing data and disappointing bank earnings reports, market conditions improved on net over the intermeeting period.

Conditions in European interbank money markets, which had been severely strained since early August, improved substantially at the shortest maturities over the period, although improvements for longer maturities were more modest. The amount of outstanding asset-backed commercial paper issued in Europe declined sharply until early October but has since stabilized. In an attempt to alleviate the stress in euro money markets, the European Central Bank continued to provide large amounts of euro liquidity, particularly early in the intermeeting period. The Bank of England also injected short-term liquidity and allowed banks greater flexibility in meeting target balances. The Bank's repeated offers to depositary institutions of three-month funds at a penalty rate of 6.75 percent were shunned, however, as three-month sterling market interest rates remained below the penalty rate.

The trade-weighted exchange value of the dollar against the major foreign currencies fell $3\frac{1}{4}$ percent over the intermeeting period, and the dollar declined $1\frac{3}{4}$ percent against the currencies of our other important trading partners. The dollar depreciated 5 percent against the Canadian dollar, with the exchange rate crossing parity for the first time since 1976; the Canadian currency was likely supported by better-than-expected Canadian employment data and rising crude oil and metals prices. The dollar depreciated $2\frac{1}{2}$ percent versus the euro and sterling over the period, but only $1\frac{1}{4}$ percent against the yen, reportedly as some investors reestablished yen-funded carry-trade positions. Consistent with this interpretation, the dollar depreciated 7 percent against the Australian dollar and 6 percent versus the New Zealand dollar, currencies often favored in yen carry-trades. Major European indexes and the Nikkei index rose about 4 percent on balance, even after declines late in the period. Ten-year European sovereign yields declined a few basis points on net, but Japan's ten-year benchmark yield rose 5 basis points. As the yields on corresponding ten-year inflation-indexed bonds registered movements that were close to those of the nominal bonds, inflation expectations appeared to be little changed in these economies.

Financial markets in emerging economies were also buoyed in the weeks following the September FOMC meeting. The Mexican peso and Brazilian *real* appreciated 2½ and 5½ percent, respectively, against the dollar, and Mexican and Brazilian stock indexes rose 8 and 15 percent over the intermeeting period. Most currencies in emerging Asia appreciated 1 to 4 percent against the dollar. The renminbi's spot exchange value against the dollar appreciated ½ percent over the period, but the one-year forward exchange value of the Chinese currency rose 2½ percent; it now prices in a 6½ percent appreciation against the dollar in twelve months. Chinese stock prices rose 8 percent over the period, but Hong Kong equity prices surged 20 percent. Equity indexes in Korea, Taiwan, and Thailand rose 5 to 8 percent.

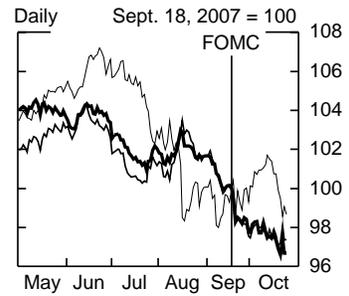
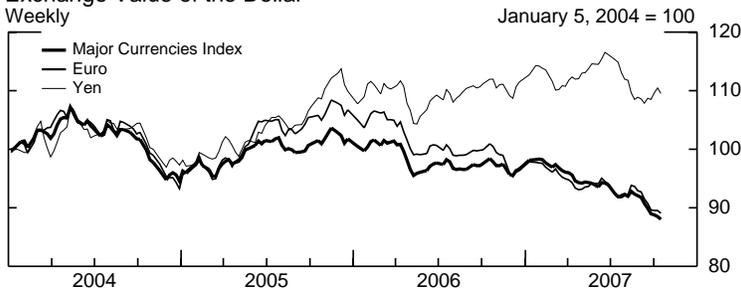
. The Desk did not intervene during the period for the accounts of the System or the Treasury.

Exchange Value of the Dollar and Stock Market Indexes

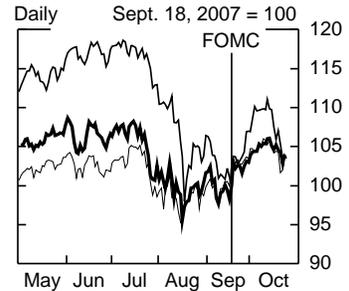
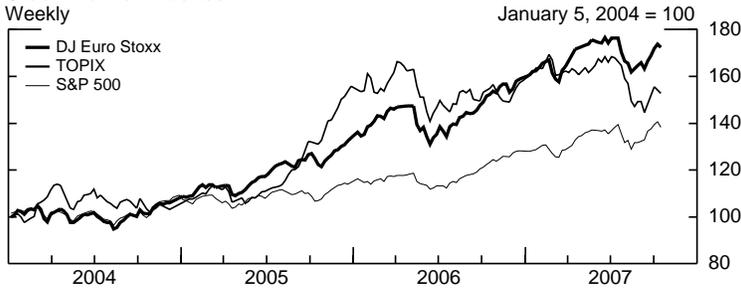
	Latest	Percent change since September FOMC
<i>Exchange rates*</i>		
Euro (\$/euro)	1.4243	-2.6
Yen (¥/\$)	114.2	-1.3
Sterling (\$/£)	2.0482	-2.5
Canadian dollar (C\$/\\$)	0.9694	-5.3
<i>Nominal dollar indexes*</i>		
Broad index	99.5	-2.5
Major currencies index	73.6	-3.3
OITP index	128.0	-1.7
<i>Stock market indexes</i>		
DJ Euro Stoxx	422.8	3.7
TOPIX	1563.9	3.5
FTSE 100	6531.0	3.9
S&P 500	1519.6	2.9

* Positive percent change denotes appreciation of U.S. dollar.

Exchange Value of the Dollar
Weekly



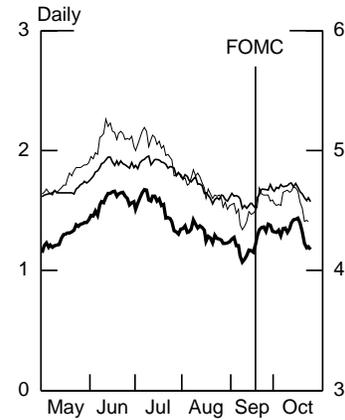
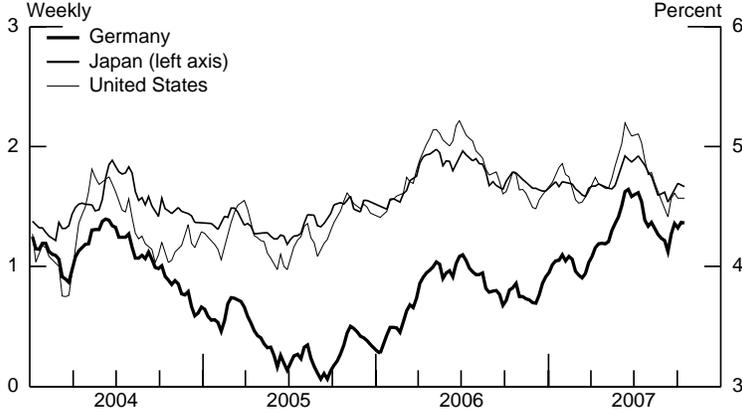
Stock Market Indexes
Weekly



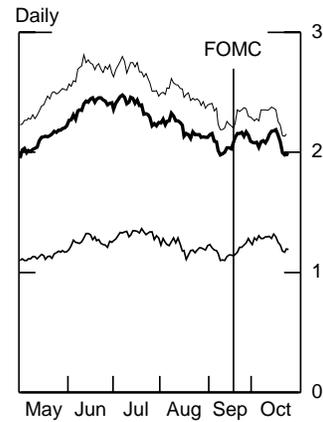
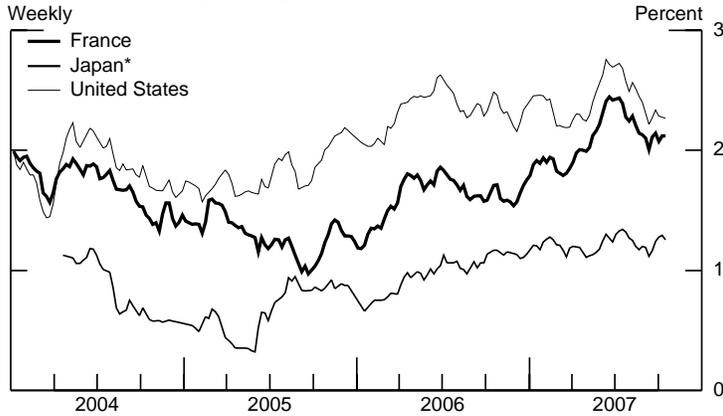
Industrial Countries: Nominal and Real Interest Rates

	3-month LIBOR		10-year nominal		10-year indexed		Percent
	Latest	Change since September FOMC	Latest	Change since September FOMC	Latest	Change since September FOMC	
Germany	4.62	-0.11	4.18	-0.04	2.03	-0.06	
Japan	0.92	-0.07	1.57	0.05	1.19	0.06	
United Kingdom	6.28	-0.47	4.88	-0.07	1.71	-0.05	
Canada	4.93	-0.37	4.30	-0.02	...	...
United States	5.07	-0.53	4.41	-0.07	2.15	-0.07	

Nominal 10-Year Government Bond Yields



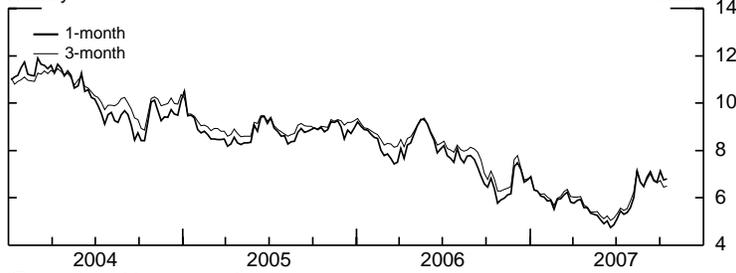
Inflation-Indexed 10-Year Government Bond Yields



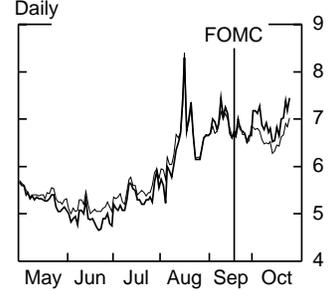
*Japan first issued inflation-indexed debt in March 2004.

Measures of Market Volatility

Dollar-Euro Options-Implied Volatility*
Weekly



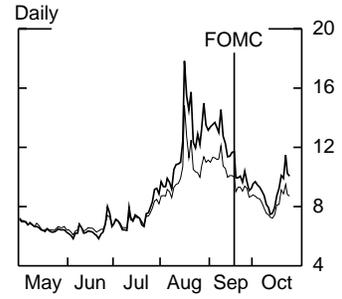
*Derived from at-the-money options.



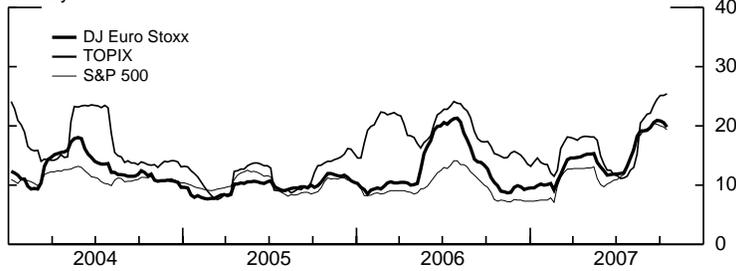
Yen-Dollar Options-Implied Volatility*
Weekly



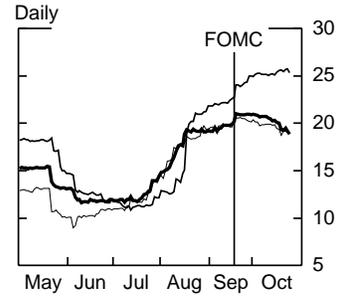
*Derived from at-the-money options.



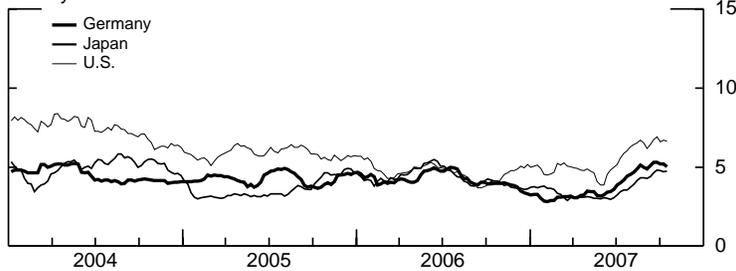
Realized Stock Market Volatility*
Weekly



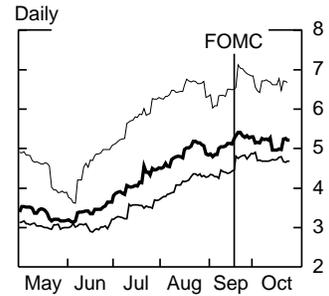
*Annualized standard deviation of 60-day window of daily returns.



Realized 10-Year Bond Volatility*
Weekly



*Annualized standard deviation of 60-day window of daily returns.

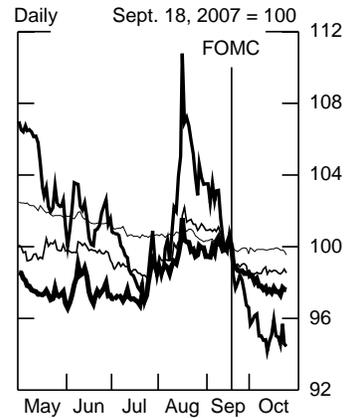
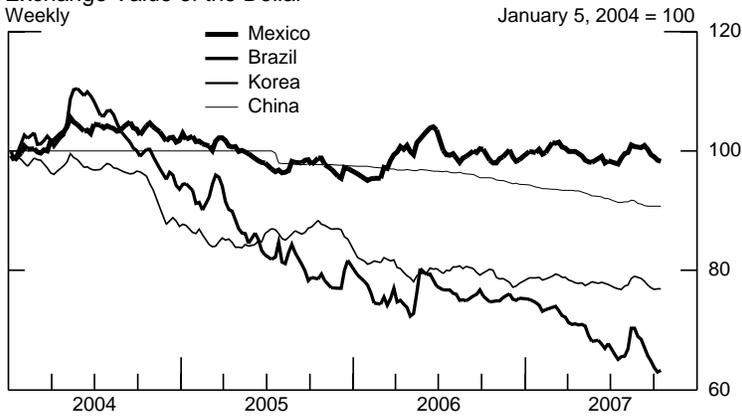


Emerging Markets: Exchange Rates and Stock Market Indexes

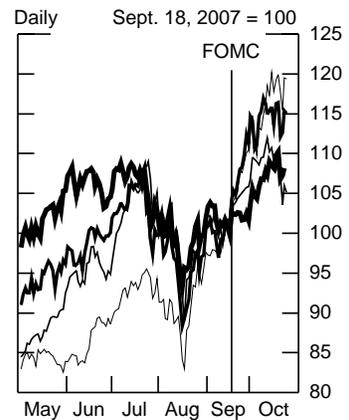
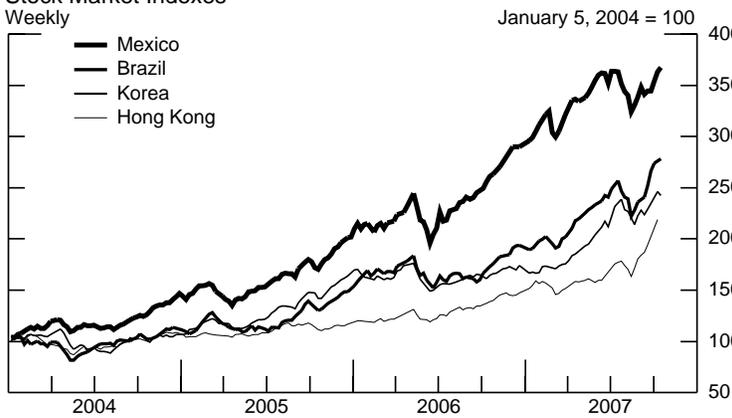
	Exchange value of the dollar		Stock market index	
	Latest	Percent change since September FOMC*	Latest	Percent change since September FOMC
Mexico	10.8250	-2.4	32229	8.2
Brazil	1.7950	-5.6	62513	15.0
Venezuela	2145.80	0.1	37105	-4.3
China	7.4870	-0.5	5843	7.7
Hong Kong	7.7513	-0.5	29334	19.4
Korea	916.2	-1.5	1933	5.2
Taiwan	32.57	-1.6	9443	6.1
Singapore	1.4608	-3.7	1010	5.6
Thailand	31.56	-1.0	866	7.9

* Positive percent change denotes appreciation of U.S. dollar.

Exchange Value of the Dollar
Weekly



Stock Market Indexes
Weekly



Emerging Markets: Short-Term Interest Rates and Dollar-Denominated Bond Spreads

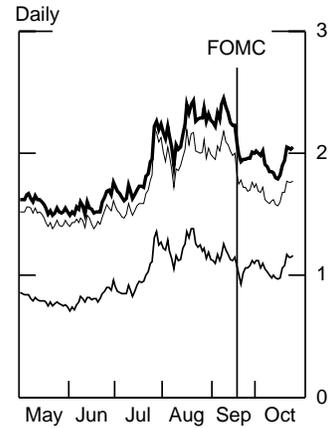
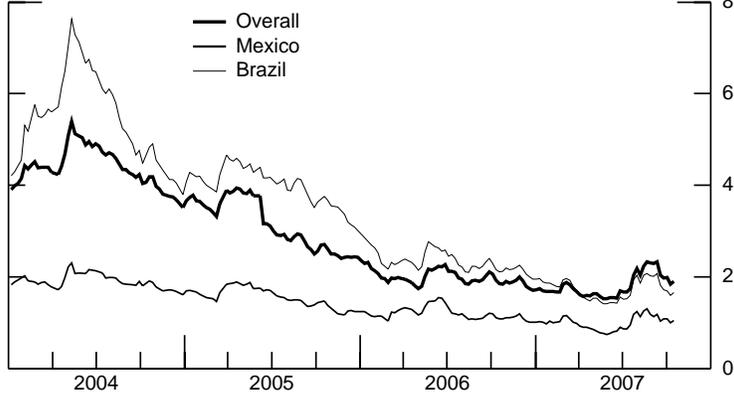
	Short-term interest rates*		Dollar-denominated bond spreads**	
	Latest	Change since September FOMC	Latest	Change since September FOMC
Mexico	7.25	0.05	1.16	0.01
Brazil	11.35	0.30	1.77	-0.23
Argentina	12.50	-1.06	3.88	-0.52
China	...	...	0.95	0.05
Korea	5.15	0.05	...	...
Taiwan	2.48	0.05	...	...
Singapore	3.50	0.00	...	...
Hong Kong	4.83	-0.05	...	...

*One month interest rate except 1-week rate for Korea. No reliable short-term interest rate exists for China.

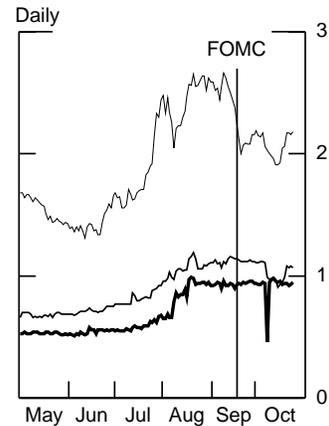
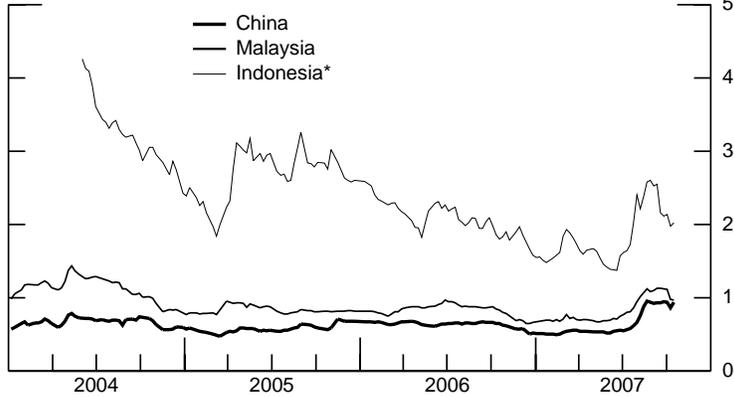
**EMBI+ or EMBI Global Spreads over similar-maturity U.S. Treasuries.

... Korea, Taiwan, Singapore, and Hong Kong have no outstanding dollar-denominated sovereign bonds.

EMBI+ Spreads
Weekly



EMBI Global Spreads
Weekly



*Begins May 2004.

Developments in Advanced Foreign Economies

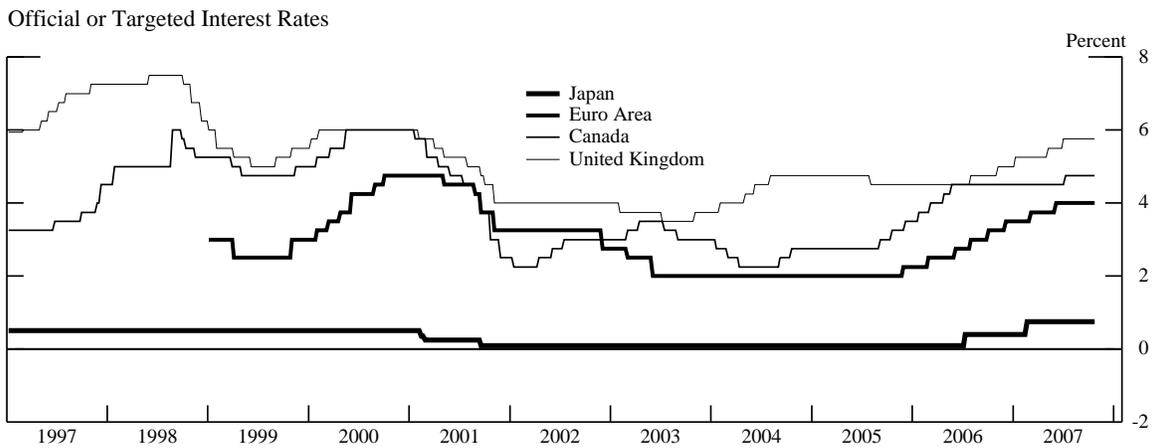
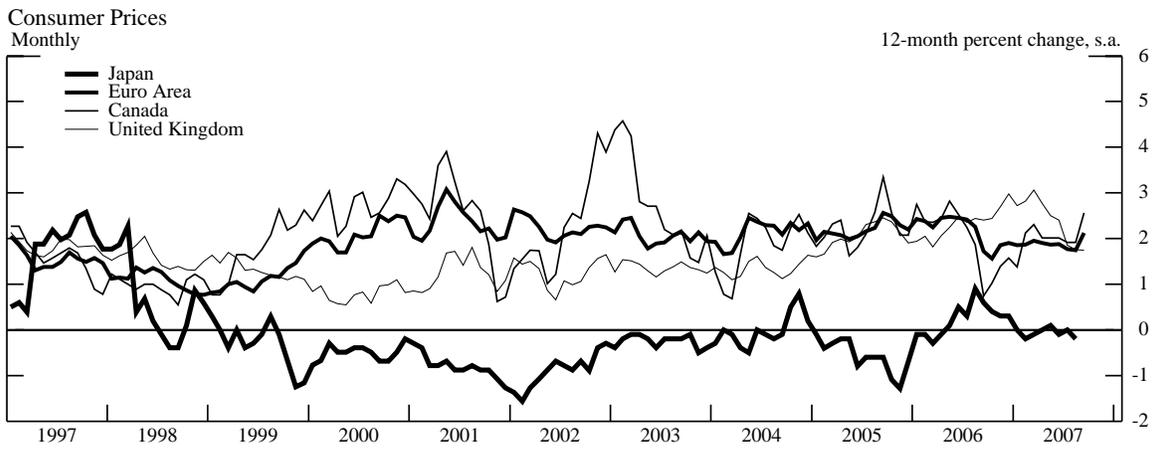
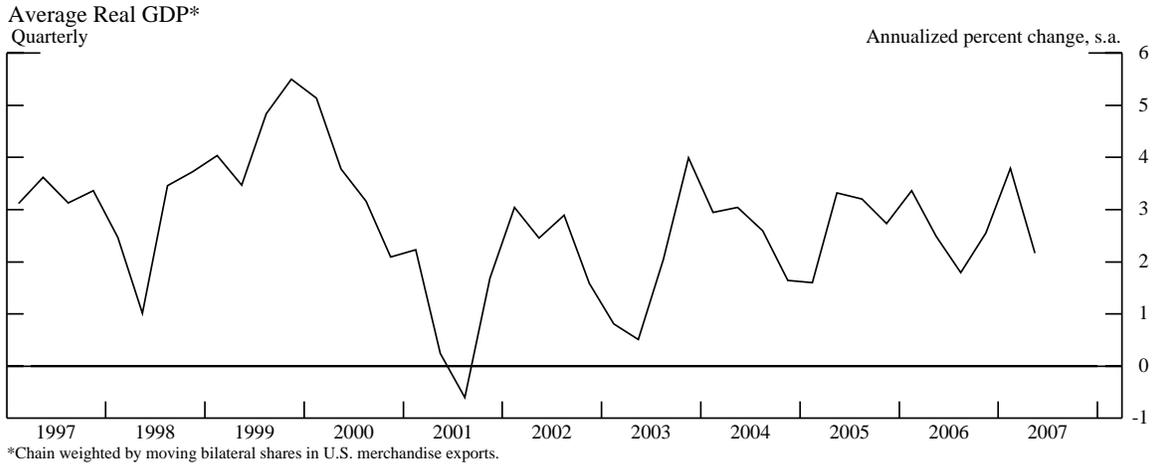
Third-quarter indicators of economic activity for the advanced foreign economies have been solid on balance. In the euro area, production and sales rebounded in the third quarter from their second-quarter levels. However, recent surveys, including the movements on balance in the purchasing manager's index (PMI) for the service sector, point to a notable slowing in activity. Likewise, the preliminary estimate of third-quarter growth in U.K. real GDP (based mostly on the first two months of the quarter) was 3.3 percent, though recent surveys suggest that growth slowed only slightly in September. Recent Canadian data have been mixed, with relatively strong employment growth and some weakness in retail sales. In contrast, Japanese retail sales and exports rebounded in August, and the Tankan survey for October seems to lend credence to the view that the second quarter's sharp contraction in investment was temporary.

To date the decline in some surveys in the euro area in the last couple months is one sign of a potential effect of the recent turmoil in financial markets. In addition, credit standards at euro area banks have tightened for both households and businesses in the third quarter. Mortgage lending has also slowed in the United Kingdom, and lenders reported that they had reduced corporate credit availability in the third quarter.

The four-quarter rate of headline inflation in Canada and the euro area rose to 2.5 percent and 2.1 percent, respectively, in September. However, core inflation remained contained—edging down in Canada and staying the same in the euro area—and the quarterly rate of headline inflation moved lower in the third quarter. The inflation rate edged down in the United Kingdom since the last Greenbook, and prices in Japan continued to fall slightly.

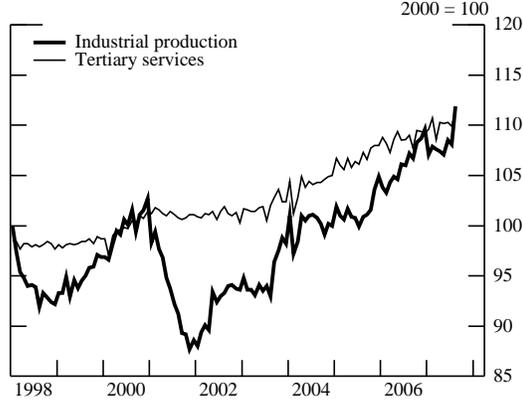
In **Japan**, the October Tankan survey continued to portray an economy that is expanding moderately, with the headline index of economic sentiment among large manufacturers remaining unchanged from June and high by historical standards. On the other hand, perceptions of the economy held by small manufacturing firms and all sizes of non-manufacturing firms have worsened since June. The survey also pointed to robust capital spending plans by large- and medium-sized firms, which supports the Bank of Japan's view that the fall in capital expenditures in the second quarter is likely to be temporary. The survey indicated an across-the-board improvement in the sales outlook and that firms continued to see the labor market and resource utilization as relatively tight.

Advanced Foreign Economies

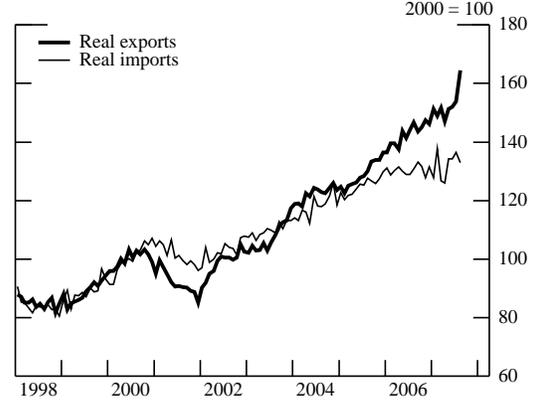


Japan

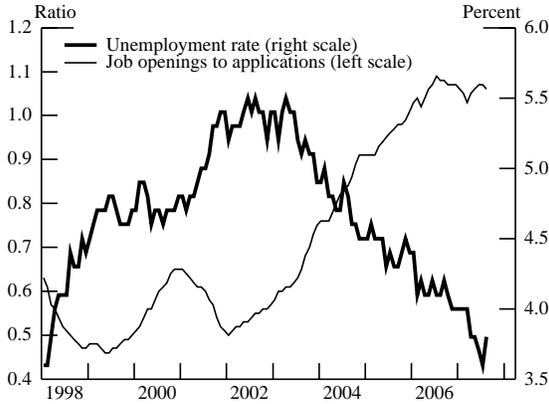
Economic Activity



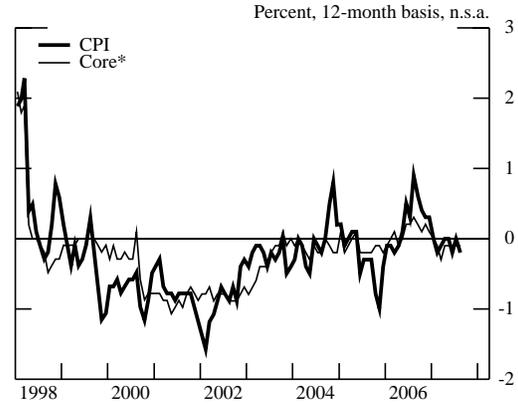
Real Trade



Labor Market



Consumer Price Inflation



*Excludes fresh food.

Economic Indicators

(Percent change from previous period except as noted, s.a.)

Indicator	2007			2007			
	Q1	Q2	Q3	June	July	Aug.	Sept.
Housing starts	-4.6	1.2	n.a.	17.3	-30.1	-23.0	n.a.
Machinery orders ¹	-0.7	-2.3	n.a.	-10.4	17.0	-7.7	n.a.
Household expenditures	1.0	-0.1	n.a.	-0.2	-1.2	0.4	n.a.
New car registrations	-1.5	-2.5	1.8	-1.7	-2.5	11.5	-6.7
Business sentiment ²	8.0	7.0	4.0	...	...	...	...
Wholesale prices ³	2.0	2.4	2.0	2.4	2.3	2.0	1.7

1. Private sector, excluding ships and electric power.

2. Tankan survey, diffusion index. Level.

3. Percent change from year earlier, n.s.a.

n.a. Not available. ... Not applicable.

Economic indicators for August have also been relatively positive. Industrial production rebounded strongly from the decline in July, as automakers recovered from the production disruption caused by the Niigata earthquake on July 16. Retail sales and real household expenditures also bounced back some from recent declines over the previous two months. Net exports continued to rise in the third quarter, supported by strong export growth to Asia and Europe. However, housing starts tumbled in August, as stricter rules regarding the approvals of construction plans were adopted by the government earlier this summer.

The labor market remains strong, with the unemployment rate rising slightly to 3.8 percent in August from the nine-year low registered in July. The job offers-to-applicants ratio (the number of officially posted job openings relative to the number of officially registered job seekers) edged down to 1.06, still close to a fifteen-year high. Earnings growth moved further into negative territory, however, as total cash earnings (which include bonuses) fell 0.8 percent from a year earlier.

The nationwide core consumer price index (excluding fresh food only) fell 0.1 percent in August from a year earlier, the seventh consecutive month of decline. Moreover, the core CPI for Tokyo, a leading indicator of prices, also declined 0.1 percent from a year earlier in September.

Former Cabinet Secretary Yasuo Fukuda was elected Prime Minister on September 25, following the resignation of former Prime Minister Shinzo Abe. Mr. Fukuda stated the need to continue the reforms initiated under Prime Minister Koizumi, but also mentioned the need to pay more attention to regional income disparities.

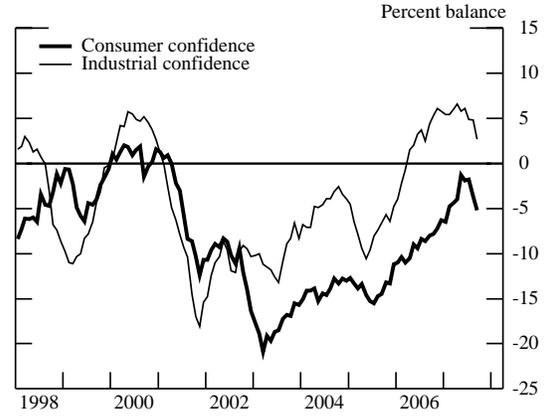
Readings of activity in the **euro area** have been strong on average in the third quarter, though more recent figures indicate some slowing. Average retail sales for July and August retail sales were up 0.6 percent relative to the second quarter, the strongest gain in the past year. However, the monthly pace of sales has slowed over the past three months. Household spending has been supported by a favorable job market: the unemployment rate remained at a record-low 6.9 percent in August, down nearly one percentage point from a year earlier. Euro-area industrial production (excluding construction) rose in August; the July/August average was up a strong 1.7 percent relative to the second quarter. Production strength was broad-based across capital goods, intermediate goods, and consumer goods.

Euro Area

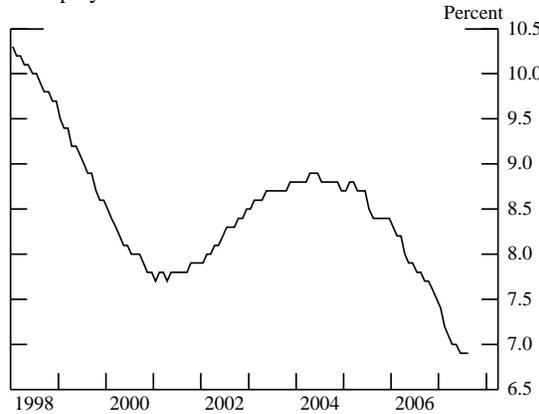
Nominal Exports and Imports



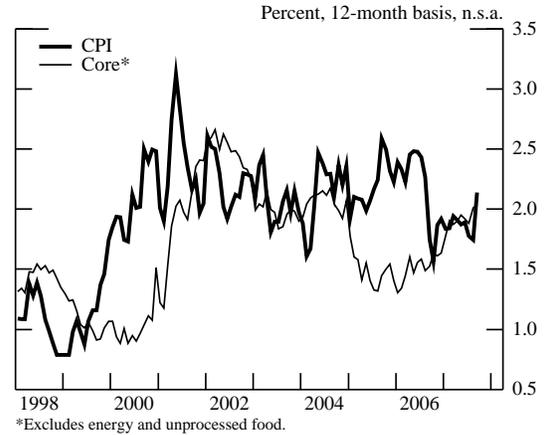
Economic Sentiment



Unemployment Rate



Consumer Price Inflation



Economic Indicators
(Percent change from previous period except as noted, s.a.)

Indicator	2006	2007		2007			
	Q4	Q1	Q2	May	June	July	Aug.
Industrial production ¹	0.7	1.1	0.5	1.1	-0.0	0.7	1.2
Retail sales volume ²	0.4	0.1	0.2	-0.7	0.7	0.4	0.0
New car registrations	3.5	-2.1	0.4	4.3	1.4	-1.7	-0.1
Employment	0.4	0.6	0.5	...	...	...	...
Producer prices ³	4.1	3.0	2.4	2.4	2.3	1.8	1.8
M3 ³	9.9	11.0	10.9	10.6	10.9	11.7	11.6

1. Excludes construction.
 2. Excludes motor vehicles.
 3. Eurostat harmonized definition. Percent change from year earlier, s.a.
 n.a. Not available. ... Not applicable.

Surveys of activity and confidence measures weakened considerably in September and October. The euro-area manufacturing PMI dropped in September and, more sharply, in October (according to the flash estimate). The services PMI registered in September its largest one-month decline since the series started in 1998, although nearly half of that decline was reversed in the flash October data. The financial services sector was particularly hard hit in September, where firms commonly cited the recent credit tightening and resulting financial uncertainty as the main causes of reduced business activity. The German services PMI showed a particularly sharp decline, consistent with German banks having faced especially large difficulties recently. September economic sentiment tumbled more than in any month since October 2001. Although overall industrial confidence remains well above its long-run average, the components measuring the trend of recent production and production expectations fell. Consumer confidence declined substantially for the second month in a row; confidence in the retail trade sector posted its largest monthly drop since 1995.

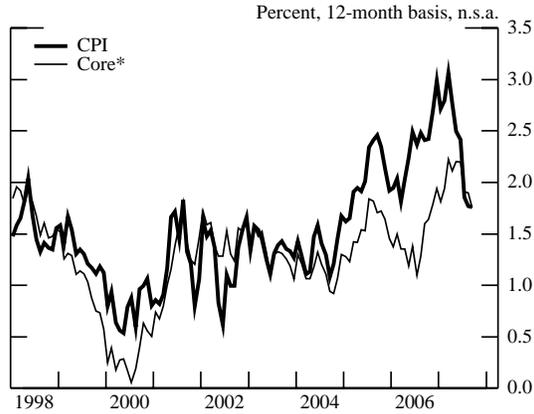
The ECB's survey of euro-area bank lending indicated sharply tighter credit standards in the third quarter. The percent balance of euro-area banks reporting a net tightening of credit standards for loans to enterprises was 31 percent in the third quarter, versus a net easing of 3 percent in the second quarter. The percent balance of euro-area banks reporting a net tightening of credit standards for housing loans to households switched to 12 percent in the third quarter from a net easing of 1 percent in the second quarter. Banks indicated that the recent tensions in the credit markets have hampered their access to wholesale funding over the past three months.

Twelve-month euro-area inflation rose to 2.1 percent in September, according to the preliminary estimate. The increase was widely anticipated by analysts and mostly represents a base effect: the removal of the monthly change for September 2006, when energy prices declined sharply, from the twelve-month calculation.

In the **United Kingdom**, real output grew 3.3 percent (a.r.) in the third quarter according to the preliminary estimate. Activities within the business services and finance sector expanded 6.8 percent, nearly matching a four-year high achieved in the previous quarter. The economic expansion was also supported by strong retail sales, which grew 7 percent (a.r.) in third quarter as many retailers slashed prices to lower inventories. The PMIs for services and manufacturing, which are derived from surveys conducted mainly after the run on Northern Rock, both slid a touch in September but continue to indicate moderate

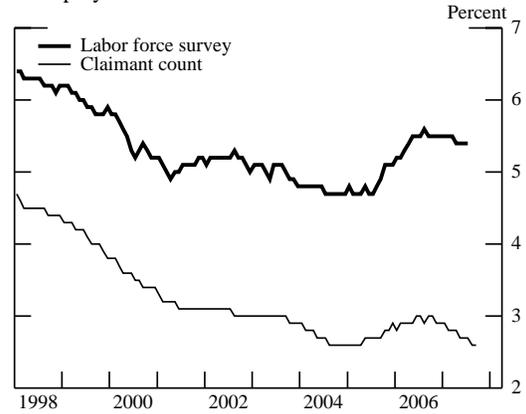
United Kingdom

Consumer Price Inflation

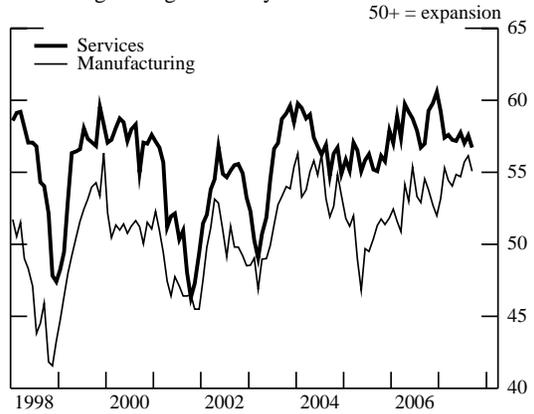


*Excludes energy and unprocessed food.

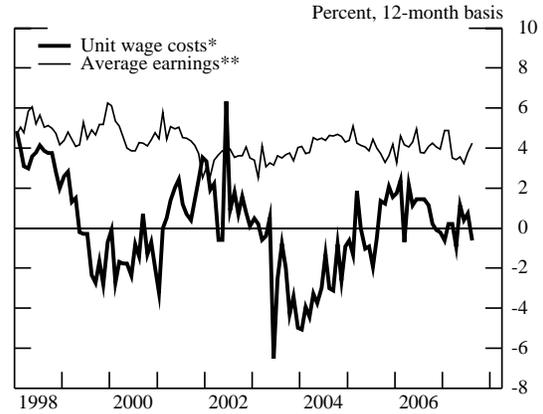
Unemployment Rates



Purchasing Managers Survey



Labor Costs



*Manufacturing industries.

**Whole economy, including bonuses.

Economic Indicators

(Percent change from previous period except as noted, s.a.)

Indicator	2007			2007			
	Q1	Q2	Q3	July	Aug.	Sept.	Oct.
Real GDP	3.2	3.3	3.3	...	...	...	...
PMI Services ¹	58.1	57.4	57.1	57.0	57.6	56.7	n.a.
Industrial production	-0.1	0.7	n.a.	-0.1	0.1	n.a.	n.a.
Business confidence ²	20.3	20.3	13.3	10.0	13.0	17.0	10.0
Consumer confidence ²	-6.2	-4.2	-2.5	-2.8	-2.1	-2.7	n.a.
Trade balance ³	-24.2	-22.8	n.a.	-9.4	-8.3	n.a.	n.a.

1. 50+ indicates expansion.

2. Percent balance. 3. Level in billions of US Dollars.

n.a. Not available. ... Not applicable.

expansion. Consumer confidence weakened slightly in August, and business confidence fell back to its July level in October.

Some indicators suggest that credit standards in the mortgage market may have tightened in the third quarter. Gross mortgage lending was up only 2.5 percent on a twelve-month basis in September, its slowest pace in two years. The number of mortgage loans approved reached a thirty-month low in August. Moreover, the underlying trend of house price inflation has moderated, especially outside London and the south-east region, after flirting with a double-digit rate for over a year.

Activity in the labor market continued at a solid pace, and wage pressure remained contained. The claimant count measure of the unemployment rate was unchanged at a thirty-year low of 2.6 percent in September. The Labor Force Survey measure was also unchanged at 5.4 percent in July. Average earnings including bonuses rose 4.2 percent in the twelve months ending in August, but unit wage costs in the manufacturing sector declined 0.6 percent over the same period.

The twelve-month rate of headline inflation was unchanged in September at 1.8 percent, after ticking down in August. Inflation was held down by the phasing in of lower utility prices that were announced earlier this year and by lower price rises for clothing and footwear items. Food price inflation picked up, however, with particularly large rises in the price of dairy products. Core inflation, which excludes unprocessed food and energy, ticked down to 1.8 percent.

In **Canada**, recent data have been mixed. Monthly GDP growth in July was 1.9 percent (s.a.a.r.), slightly below market expectations. GDP growth at this rate for the rest of the quarter would put third-quarter growth at around 2.3 percent, well below its second-quarter pace. Goods-producing industries showed a 1 percent decline, while output in the service-producing industries rose 3.3 percent. Sales through August indicate some weakness in third-quarter consumption, though both retail sales and motor vehicle sales rose in August after declining during the previous two months. Real shipments from manufacturing industries showed unusual volatility in July and August, giving no solid indication of direction. On net, shipments remain below their May level. Housing starts surged in September; however, single-unit starts fell a little.

Real imports rose sharply in July before falling back somewhat in August. As with shipments data, the unusual monthly pattern appears to owe primarily to the automotive

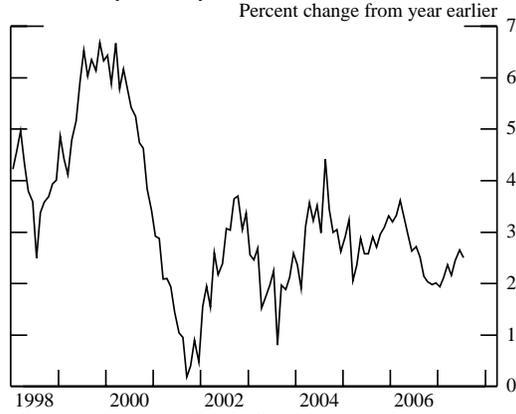
sector. Imports of automotive products jumped 16.4 percent in July and fell 6.9 percent in August. Real exports exhibited a similar, but more muted, pattern. On net, Canada's nominal trade surplus in August was well below its June level, implying a large negative contribution to third-quarter GDP growth.

Employment rose by a solid 51 thousand jobs in September. However, gains in employment were concentrated in the public sector, while private sector employment growth was muted. From January to September, private and public sector employment increased by 43 thousand and 141 thousand jobs, respectively, compared with 247 thousand and 17 thousand jobs over the same period in 2006.

In September, the twelve-month rate of consumer price inflation jumped 0.7 percentage point to 2.6 percent. The acceleration in inflation was mainly attributable to the twelve-month increase in gas prices; the rise in gas prices in September was only 0.8 percent. Core inflation, which excludes the eight most volatile components and the effects of changes in indirect taxes, edged down further in September to 2 percent. Average hourly wages increased 4.2 percent over the twelve months ending in September. This rate is the largest increase since the start of the series in 1997.

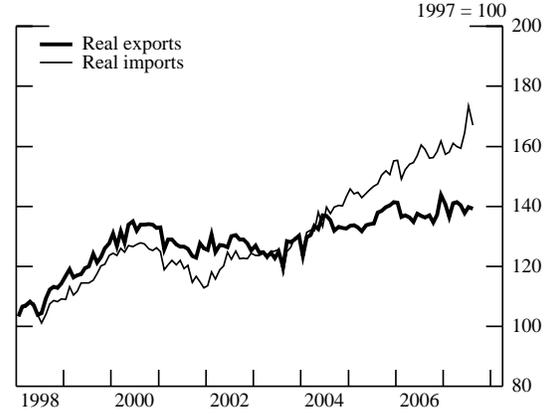
Canada

Real GDP by Industry*

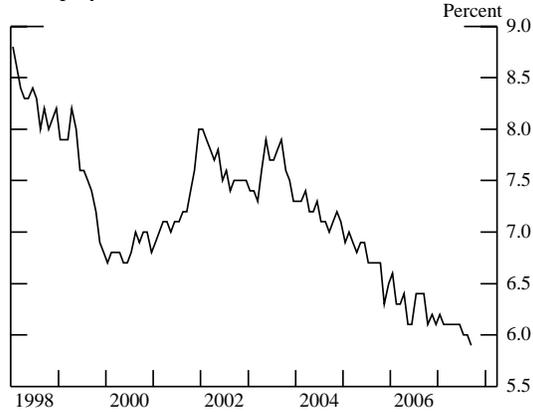


*Constructed from various Statistics Canada surveys and supplements the quarterly income and expenditure-based estimates.

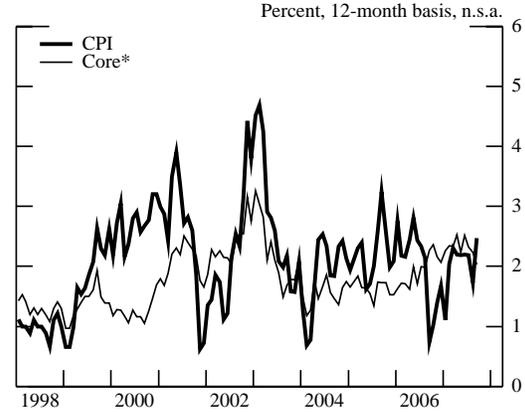
Real Trade



Unemployment Rate



Consumer Price Inflation



*Excludes 8 most volatile components and the effects of changes in indirect taxes.

Economic Indicators

(Percent change from previous period except as noted, s.a.)

Indicator	2007			2007			
	Q1	Q2	Q3	June	July	Aug.	Sept.
Industrial production	0.8	0.5	n.a.	0.3	-0.2	n.a.	n.a.
New manufacturing orders	0.4	0.4	n.a.	-2.5	5.5	n.a.	n.a.
Retail sales	1.1	2.6	n.a.	-0.7	-0.8	1.4	n.a.
Employment	1.0	0.3	0.4	0.2	0.1	0.1	0.3
Consumer attitudes ¹	98.3	96.6	n.a.	...	...	...	...
Business confidence ¹	102.1	106.7	n.a.	...	...	...	...

1. 2002=100.

n.a. Not available. ... Not applicable.

Economic Situation in Other Countries

Recent economic information, mostly through August, shows no signs that the turmoil in financial markets has had a significant negative impact on real economic activity in emerging market economies. Activity appears to have remained robust in emerging Asia, although down from its elevated second-quarter pace, when growth in several countries was at double-digit levels. Mexican economic indicators point to moderate growth in the third quarter. In South America, activity has been strong, boosted by high commodities prices and, in Argentina and Venezuela, by expansionary macro policies. Food prices continued to be a major source of inflationary pressures in the emerging market economies. Chinese authorities took several steps that were aimed at quelling rising prices.

In **China**, incoming data point to some moderation of activity. The trade surplus narrowed in the third quarter to \$265 billion from \$280 billion (a.r.) in the second quarter; export growth picked up a bit, but the increase in import growth was more substantial. Industrial production has also decelerated in recent months. Chinese authorities announced a new set of measures in early October to cool the country's real estate market, including raising minimum down payment requirements for purchases of second homes and commercial property.

Inflation moderated a touch in September, with the 12-month increase in the headline CPI falling to about 6 percent from 6½ percent in August. With money growth still elevated at about 18½ percent for the twelve months ending in September, authorities remain concerned about underlying inflation pressures, prompting them to take several steps to control prices. First, the central bank raised benchmark bank lending rates in mid-September and reserve requirement ratios in mid-October. Second, in mid-September, the government announced a freeze on prices that it controls (land, transport, utilities, and fuel) for the rest of the year. However, food prices, which are not administered, were the source of the recent runup in consumer prices. Third, the authorities announced that they will release some grain reserves and also decrease import duties on certain grains to stabilize food prices. The measures aimed at releasing grain price pressures, which were generally anticipated, should have some effect in curbing inflation.

In late September, China formally launched its long-anticipated sovereign wealth fund. The fund will reportedly be given \$200 billion of the country's \$1.4 trillion international

reserves to make overseas investments. Officials have stated that that the wealth fund would aim to maximize returns while taking acceptable risks.

China's 17th Party Congress occurred in mid-October. This is a five-yearly meeting that establishes the new leadership and party line in major policy areas. The political report of the Party Congress reiterated the policy priorities of market reform and openness and endorsed some limited progress on "inner-party democracy." At the conclusion of the meeting, the Party Congress announced the 25 members of the new Politburo (the "political bureau" that oversees the Communist Party) and the 9 members of that select group who will form the powerful Standing Committee of the Politburo. There are 10 new members in the Politburo and 4 new members in the Standing Committee. President Hu Jintao was reappointed for another five-year term, as was Premier Wen Jiabao. Two of the younger new members of the Standing Committee, Mr. Xi Jinping (Party chief of Shanghai) and Mr. Li Keqiang (Party chief of Lianoning) are being billed as successors to the presidency and the premiership in 2012. The leadership reshuffle is generally viewed as consolidating the authority of President Hu.

Chinese Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	10.0	10.4	14.7	n.a.	...	...	...
Industrial production	17.2	14.3	8.1	n.a.	-1.8	.8	n.a.
Consumer prices ²	1.5	2.7	3.6	6.1	5.6	6.4	6.1
Merch. trade balance ³	102.0	177.5	280.5	264.5	261.1	249.9	282.3

1. Annual rate. Quarterly data estimated by staff from reported four-quarter growth rates. Annual data are Q4/Q4.

2. Percent change from year-earlier period, except annual data, which are Dec./Dec.

3. Billions of U.S. dollars, annual rate. Imports are c.i.f.

n.a. Not available. ... Not applicable.

In Hong Kong, indicators of economic activity in the third quarter show the economy carried forward momentum from the second quarter, when real GDP jumped 8.2 percent. In July and August, retail sales volume was up 12 percent versus a year earlier, compared with around 7½ percent in the first half of the year, boosted by an increase in tourism. Twelve-month inflation remained well under 2 percent in the third quarter. In his annual policy address in October, Hong Kong Chief Executive Donald Tseng announced that salary and profit tax rates would be reduced gradually over the next few years.

Hong Kong Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	7.8	7.2	8.2	n.a.	...	...	...
Unemployment rate ²	5.7	4.8	4.2	4.1	4.1	4.2	4.1
Consumer prices ³	1.4	2.3	1.3	1.6	1.6	1.6	1.6
Merch. trade balance ⁴	-10.5	-17.9	-18.8	n.a.	-21.3	-36.5	n.a.

1. Annual rate. Annual data are Q4/Q4.

2. Percent. Monthly data are averages of the current and previous two months.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

n.a. Not available. ... Not applicable.

In **Taiwan**, economic indicators remained largely positive during the third quarter, particularly with respect to external demand, following strong GDP growth in the second quarter. The trade surplus increased in the third quarter to its highest level since 2005, with exports rising nearly 4 percent at a quarterly rate and imports up less. Industrial production rebounded in September from a contraction in August, and was up on average in the third quarter. Consumer price inflation picked up in September, due largely to a sharp increase in food prices related to recent typhoons. In response, the central bank raised its official discount rate $\frac{1}{8}$ percentage point in September to $3\frac{1}{4}$ percent.

Taiwan Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	6.5	4.0	7.6	n.a.	...	...	...
Unemployment rate ²	4.1	3.9	3.9	3.9	3.9	3.9	3.9
Industrial production	4.6	5.0	6.5	2.8	-1.2	-1.6	3.2
Consumer prices ³	2.2	.7	.3	1.4	-.3	1.6	3.1
Merch. trade balance ⁴	7.8	11.6	11.5	18.3	.5	30.4	23.9
Current account ⁵	16.0	24.7	19.9	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

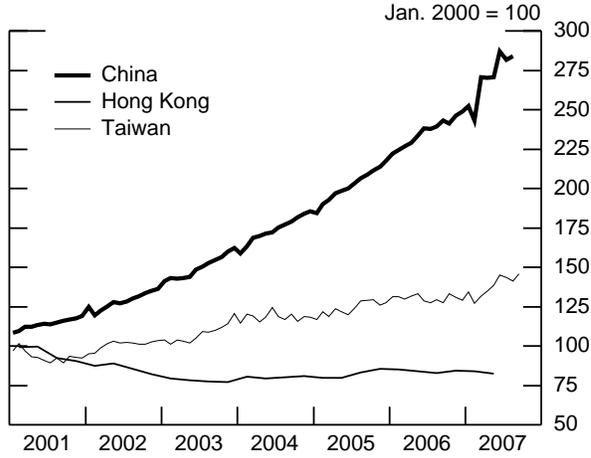
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

5. Billions of U.S. dollars, n.s.a., annual rate.

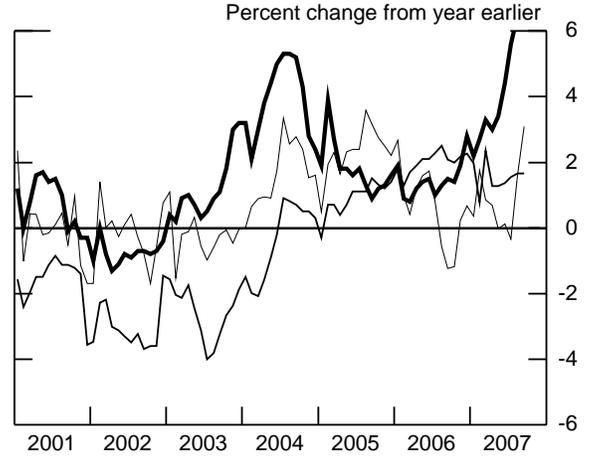
n.a. Not available. ... Not applicable.

China, Hong Kong, and Taiwan

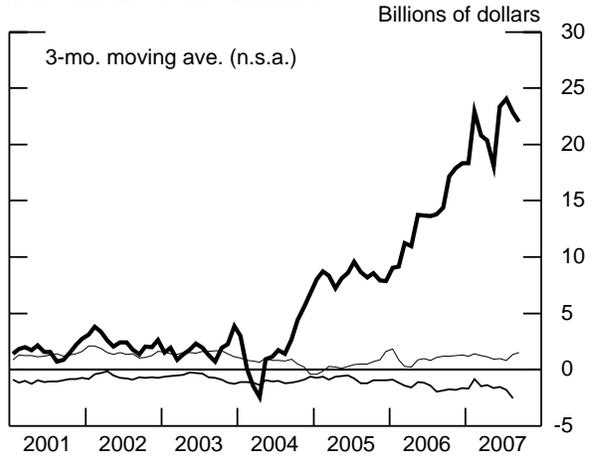
Industrial Production



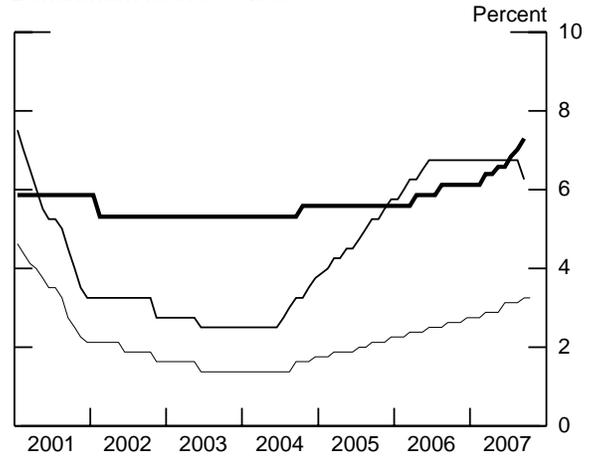
Consumer Prices



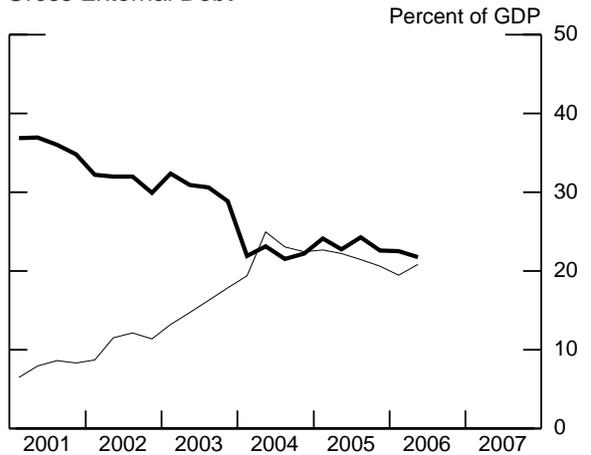
Merchandise Trade Balances



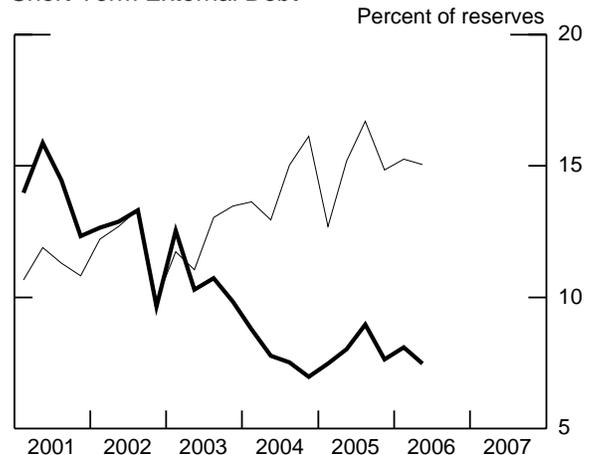
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



Recent data from **South Korea** suggest that activity remained strong in the third quarter. Average industrial production for July and August was up 4 percent from the second quarter. Indicators for consumer and business confidence were strong in the third quarter, and the unemployment rate continued to decline. The merchandise trade surplus edged higher, contributing to noticeable widening of the current account surplus. Twelve-month consumer price inflation moderated to 2.3 percent in the third quarter, below the central bank's 2.5 to 3.5 percent target range. Although Bank of Korea left the policy rate unchanged at 5 percent at its October 11 meeting following two consecutive 25-basis point increases, it remains concerned about the recent growth in lending, notably to small and medium sized enterprises.

Korean Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	5.7	4.0	7.4	n.a.	...	...	...
Industrial production	5.8	10.8	4.4	n.a.	2.0	.8	n.a.
Unemployment rate ²	3.7	3.4	3.3	3.3	3.4	3.2	3.2
Consumer prices ³	2.6	2.1	2.5	2.3	2.5	2.0	2.3
Merch. trade balance ⁴	32.7	29.2	25.2	n.a.	26.5	55.4	n.a.
Current account ⁵	15.0	6.1	.1	n.a.	18.6	7.3	n.a.

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Singapore**, economic activity continued to expand at a strong pace in the third quarter. According to the advance unofficial estimates, real GDP grew 6.4 percent (s.a.a.r) from the previous quarter. Average industrial production rose 13 percent in July and August from the second-quarter average despite a contraction in August, as production in the volatile biomedical sector surged and electronics production recovered. Anecdotes indicate that strong activity in construction and services also contributed to the third-quarter performance. The trade surplus remained high in the third quarter. In recent months, twelve-month consumer price inflation has been rising, owing not only to a 2 percentage point increase in the Goods and Services Tax (GST) in July, but also to tighter economic conditions. Concerns over rising inflation prompted the Monetary Authority of Singapore to announce that it will allow a more appreciated path for the currency at its October 10 meeting.

Singapore Economic Indicators
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	8.2	6.5	14.4	n.a.	...	...	...
Industrial production	9.5	11.9	4.9	n.a.	26.3	-13.7	n.a.
Unemployment rate ²	3.1	2.7	2.3	n.a.	...	...	...
Consumer prices ³	1.3	.8	1.0	2.7	2.6	2.9	2.7
Merch. trade balance ⁴	29.6	33.1	36.9	41.5	47.5	40.2	36.8

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

n.a. Not available. ... Not applicable.

In **India**, economic indicators point to a bit of slowing from the rapid pace in the second quarter. Average industrial production for July and August was slightly below the second-quarter level, and indicators show declines in auto and electricity output in September. After narrowing in July, the trade deficit widened sharply in August reflecting stable exports along with a jump in oil imports. Inflation indicators have been mixed. Twelve-month CPI inflation ticked up in August while inflation of the more closely watched wholesale price index decelerated further in September. Neither consumer nor wholesale prices reflect rising oil prices, as ceilings on consumer fuel prices have not been adjusted since early this year, when they were lowered.

Strong capital inflows have put increasing pressure on the Indian rupee, prompting the central bank to undertake substantial intervention operations and loosen restrictions on capital outflows. In mid-October, the Indian government also announced plans to restrict capital flows from unregulated overseas investments into the Indian stock market, effective October 25. International reserves in October reached nearly \$250 billion, 30 percent of 2006 GDP in 2006.

Indian Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	9.3	8.7	9.9	n.a.	...	...	...
Industrial production	7.9	10.5	2.3	n.a.	-2.7	3.8	n.a.
Consumer prices ²	5.6	6.5	6.0	n.a.	5.5	6.3	n.a.
Wholesale prices ²	4.4	5.7	5.4	4.0	4.7	4.1	3.3
Merch. trade balance ³	-43.9	-54.4	-76.0	n.a.	-63.8	-82.7	n.a.
Current account ⁴	-7.8	-9.4	-18.8	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent change from year-earlier period, except annual data, which are Dec./Dec.

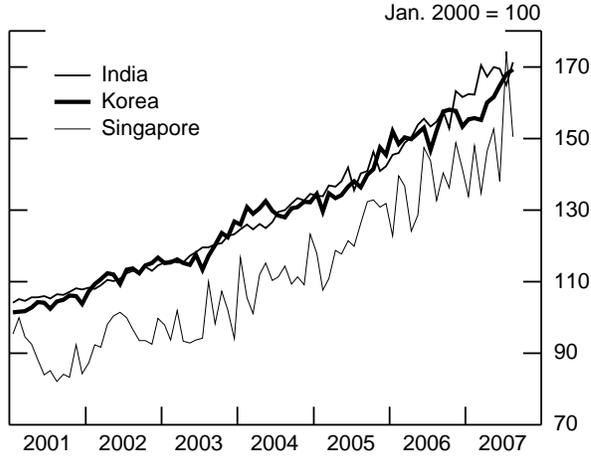
3. Billions of U.S. dollars, annual rate.

4. Billions of U.S. dollars, n.s.a., annual rate.

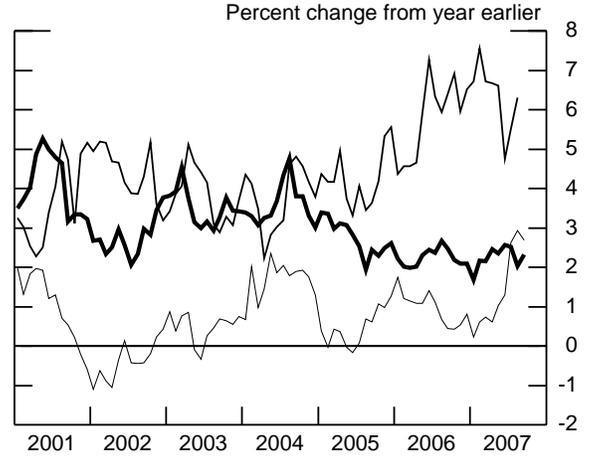
n.a. Not available. ... Not applicable.

India, Korea, and Singapore

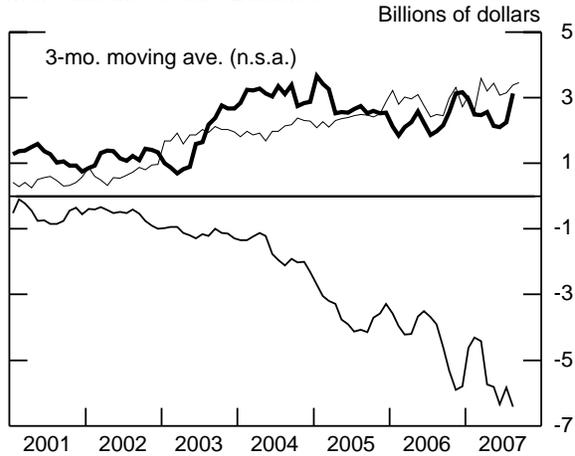
Industrial Production



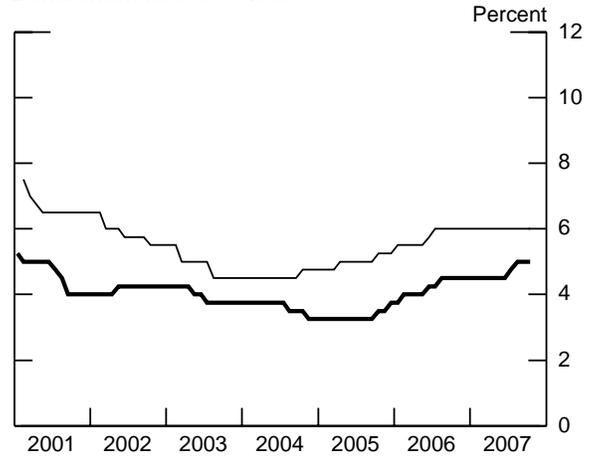
Consumer Prices



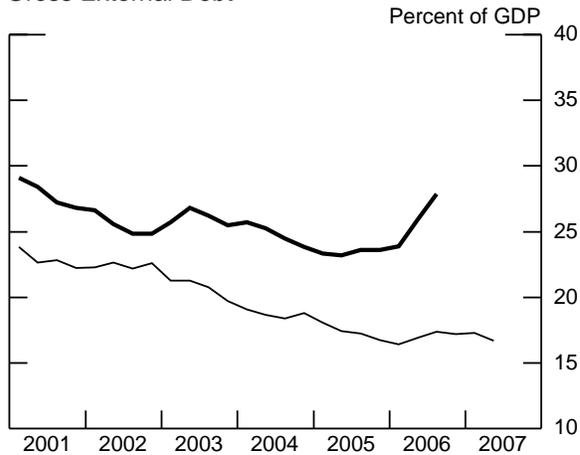
Merchandise Trade Balances



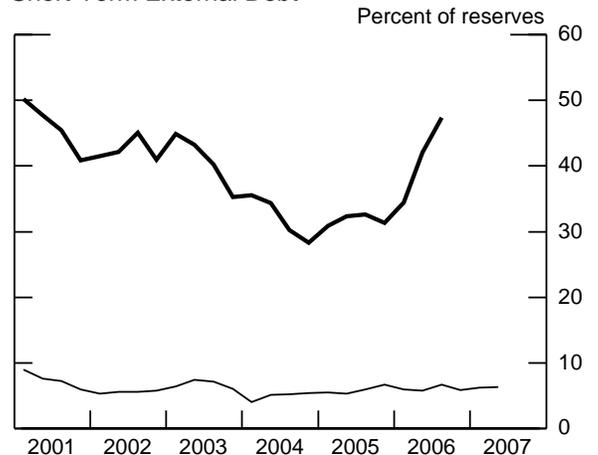
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



Data from the **ASEAN-4** indicate that economic growth in the region may have slowed from its strong pace in the second quarter. Industrial production data were mixed; average production over July-August declined from the second-quarter level in Indonesia, but was up in Malaysia, Thailand, and the Philippines. Trade surpluses in Indonesia, Malaysia, and Thailand narrowed slightly through the first two months of the third quarter. Consumer price inflation picked up in Indonesia, Malaysia, and the Philippines during the third quarter, in part owing to food price pressures. In Thailand, food prices also caused inflation in September to rise above 2 percent for the first time since early this year, but inflation for the quarter as a whole fell as rapid appreciation of the baht helped dampen import prices. On October 4, the Philippine central bank cut rates by 25 basis points to 5.75 percent.

ASEAN-4 Economic Indicators: Growth
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Jun.	Jul.	Aug.
<i>Real GDP¹</i>							
Indonesia	4.9	6.0	3.0	6.4	...	...	...
Malaysia	5.7	5.8	5.9	6.2	...	...	...
Philippines	5.6	5.5	10.6	7.1	...	...	...
Thailand	4.3	4.2	4.9	5.2	...	...	...
<i>Industrial production²</i>							
Indonesia ³	1.3	-1.6	-.1	2.7	-2.0	1.1	-4.3
Malaysia	4.0	4.9	-2.3	3.1	-.1	-.5	-.7
Philippines	2.2	-9.9	-7.4	3.7	1.5	3.0	.0
Thailand	9.1	7.4	1.7	1.4	-1.1	2.2	3.7

1. Annual rate. Annual data are Q4/Q4.
2. Annual data are annual averages.
3. Staff estimate.
- ... Not applicable.

ASEAN-4 Economic Indicators: Merchandise Trade Balance
(Billions of U.S. dollars, s.a.a.r.)

Indicator	2005	2006	2007				
			Q1	Q2	Jun.	Jul.	Aug.
Indonesia	28.0	39.7	43.1	40.8	40.2	43.5	35.4
Malaysia	26.4	29.5	24.3	28.5	34.2	32.2	24.2
Philippines	-6.2	-4.4	.9	-1.1	-4.9	-10.0	n.a.
Thailand	-8.5	1.0	16.2	13.0	18.1	2.6	10.7

n.a. Not available.

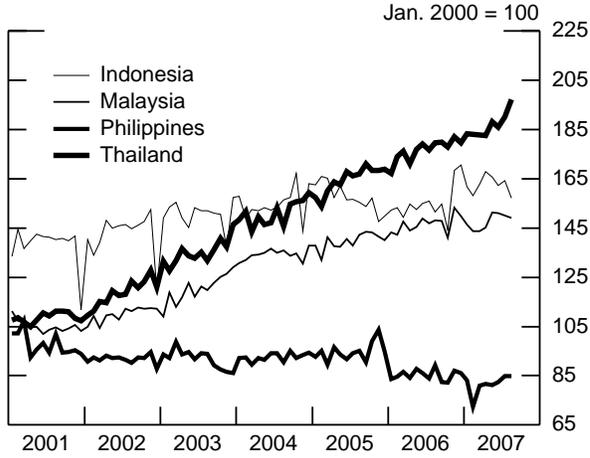
ASEAN-4 Economic Indicators: CPI Inflation
(Percent change from year earlier, except as noted)

Indicator	2005 ¹	2006 ¹	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Indonesia	17.0	6.7	6.0	6.4	6.0	6.6	6.7
Malaysia	3.3	3.1	1.5	1.8	1.6	1.9	1.8
Philippines	6.7	4.3	2.4	2.5	2.6	2.4	2.7
Thailand	5.8	3.5	1.9	1.6	1.7	1.1	2.1

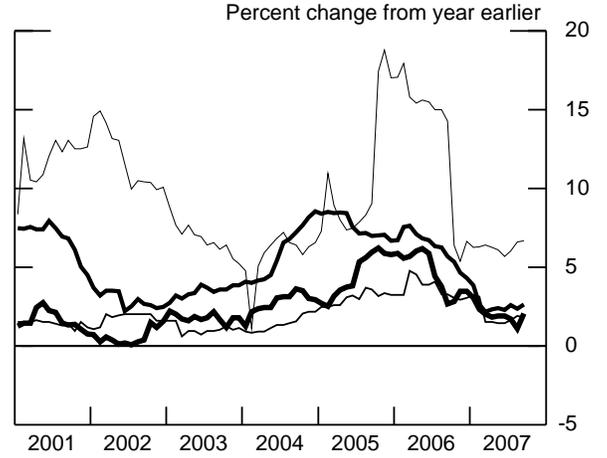
1. Dec./Dec.

ASEAN-4

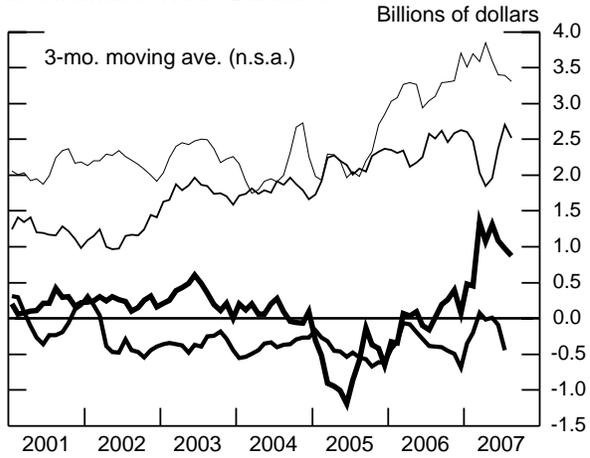
Industrial Production



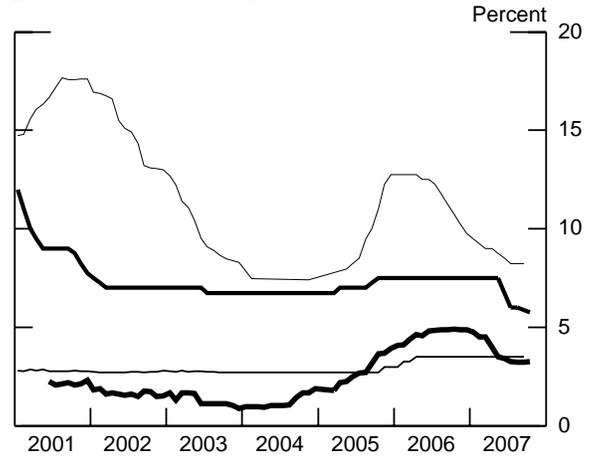
Consumer Prices



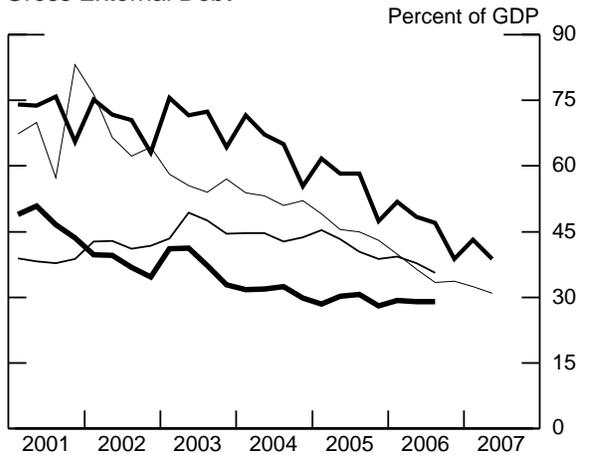
Merchandise Trade Balances



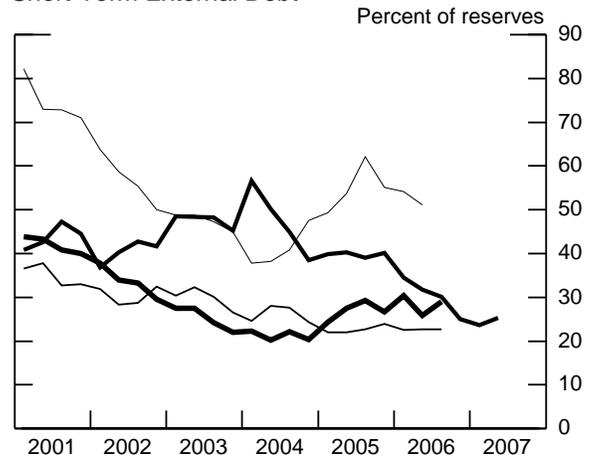
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



In **Mexico**, recent indicators point to moderate growth in the third quarter. Average industrial production in July and August was up 1.3 percent from the second-quarter average. The manufacturing and construction sectors, areas of weakness earlier this year, continued to recover. Oil production was down in the third quarter, however. In mid-September, Mexico's Congress approved President Felipe Calderon's plan to overhaul tax laws, the most significant economic reform in a decade. The central provision of the tax bill is the establishment of a minimum corporate tax. The fiscal overhaul is likely to significantly increase Mexico's tax revenues in the long run and thus ameliorate the government's dependence on oil revenues.

Twelve-month headline inflation remained high at 3.8 percent in September, boosted by increases in prices of dairy products and tomatoes. However, September marks the first month in the past year in which twelve-month headline inflation was within the Bank of Mexico's 2-to-4 percent inflation target range. As in its previous monthly meetings since April, the central bank at its late-September meeting kept its benchmark rate, the overnight lending rate, steady at 7¼ percent because it expects inflation to remain within the target range.

Mexican Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	2.5	4.3	5.3	n.a.	...	...	...
Overall economic activity	3.1	4.9	1.4	n.a.	1.0	n.a.	n.a.
Industrial production	2.1	5.0	1.3	n.a.	.3	.8	n.a.
Unemployment rate ²	3.6	3.6	3.7	3.6	3.6	3.6	3.6
Consumer prices ³	3.3	4.1	4.0	4.0	4.1	4.0	3.8
Merch. trade balance ⁴	-7.6	-6.1	-15.2	-11.7	-11.6	-12.3	-11.2
Merchandise imports ⁴	221.8	256.1	281.3	292.6	288.4	291.4	297.9
Merchandise exports ⁴	214.2	250.0	266.1	280.8	276.8	279.0	286.6
Current account ⁵	-4.6	-1.6	-3.9	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent; counts as unemployed those working one hour a week or less.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Brazil**, data releases suggest that activity continued to expand in the third quarter. August industrial production more than recovered from its July decline and was at a record high. The trade surplus narrowed in the third quarter, as nominal exports were stable while nominal import growth continued to be strong. Real capital goods imports in July were up nearly 50 percent on a twelve-month basis. Twelve-month headline consumer price inflation held steady at 4.3 percent in September, as pressures from food prices abated, and core inflation remained at 3.6 percent on a twelve-month basis.

On October 17, the central bank held its policy rate steady at 11¼ percent, in response to concerns about food price and domestic demand-side inflationary pressures. The government announced that it is considering a sovereign wealth fund to manage a small part of the central bank's \$160 billion in international reserves. The sovereign wealth fund would be focused on ensuring adequate liquidity and security rather than seeking high returns.

Brazilian Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	3.1	4.7	3.2	n.a.	...	...	...
Industrial production	3.1	2.8	2.6	n.a.	-4	1.3	n.a.
Unemployment rate ²	9.8	10.0	9.6	n.a.	9.4	9.3	n.a.
Consumer prices ³	5.7	3.3	3.4	4.2	3.9	4.3	4.3
Merch. trade balance ⁴	44.8	46.1	48.5	32.4	27.5	32.3	37.5
Current account ⁵	14.0	13.6	11.3	4.1	-9.5	16.1	5.7

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

Price index is IPCA.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Argentina**, indications are that activity continued to be strong in the third quarter. The Index of Economic Activity (a monthly proxy of GDP) was up 2.2 percent on average in July and August from the second quarter. Reported twelve-month consumer price inflation remained elevated in September at 8.6 percent, fueled by an increase in food prices. (There continue to be allegations that Argentine authorities are tampering with the consumer price data.) Credit conditions in Argentina have tightened considerably since July, despite the injection of liquidity by the central bank and pressure on banks by

the government to reduce rates. Ahead of the October 28 presidential election, Cristina Fernández de Kirchner, President Kirchner's wife, has a commanding lead.

Argentine Economic Indicators
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	8.8	8.7	8.8	n.a.	...	...	...
Industrial production	8.0	8.3	2.0	n.a.	-2.6	7.2	n.a.
Unemployment rate ²	11.6	10.2	8.5	n.a.	...	...	...
Consumer prices ³	12.1	9.7	8.9	8.7	8.7	8.7	8.6
Merch. trade balance ⁴	11.7	12.3	13.1	n.a.	4.2	6.1	n.a.
Current account ⁵	5.7	8.1	8.9	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent; n.s.a.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In Venezuela, macroeconomic policies continued to be very expansionary ahead of the December referendum on a new constitution that would further centralize power with the executive and allow unlimited terms in office for Chavez. Monthly consumer price inflation in September was 1.4 percent, bringing twelve-month inflation to 15.3 percent, despite price controls and cuts in the value-added tax earlier this year.

In September, in an attempt to support the currency, the government issued the third so-called Bond of the South, which consisted of the sale of roughly \$0.6 billion of its holdings of Argentine government dollar-denominated bonds and the sale of about \$0.6 billion in Venezuelan government dollar-indexed bonds. The dollar-linked bonds are attractive because the government allows investors to purchase them using bolivares at the official exchange rate, which is considerably higher than the exchange rate in the parallel market. Nevertheless, the parallel market bolivar has continued to depreciate sharply since August and stood at 5,940 VEN per dollar on October 23, versus the official exchange rate of 2,144 VEN per dollar.

Venezuelan Economic Indicators
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	10.9	11.8	9.5	n.a.	...	...	...
Unemployment rate ²	12.2	10.0	8.2	8.5	8.8	8.5	8.1
Consumer prices ³	14.4	17.0	19.5	16.1	17.2	15.9	15.3
Non-oil trade balance ⁴	-14.3	-22.7	n.a.	n.a.	...	...	...
Merch. trade balance ⁴	31.8	33.0	22.2	n.a.	...	...	...
Current account ⁵	25.5	27.2	20.5	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

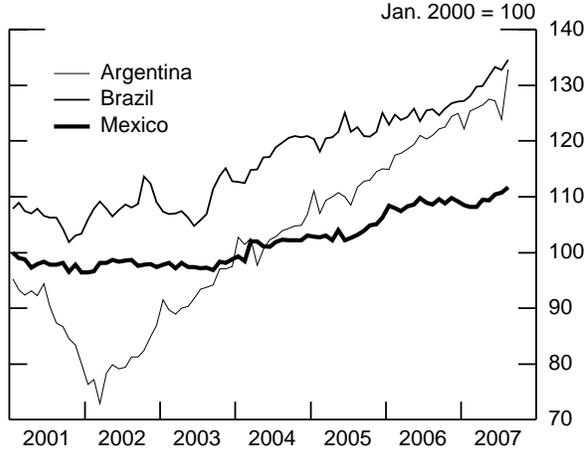
4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

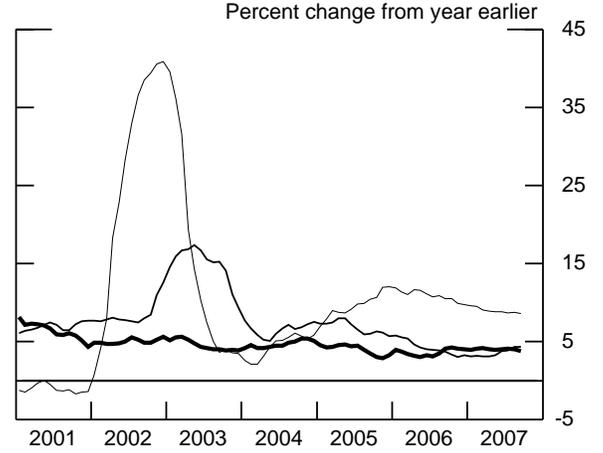
n.a. Not available. . . . Not applicable.

Latin America

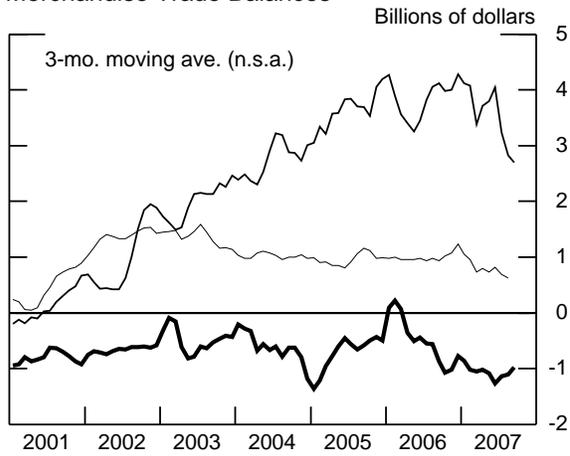
Industrial Production



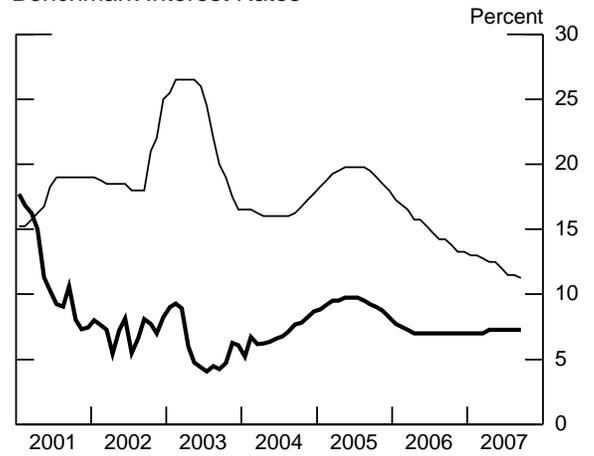
Consumer Prices



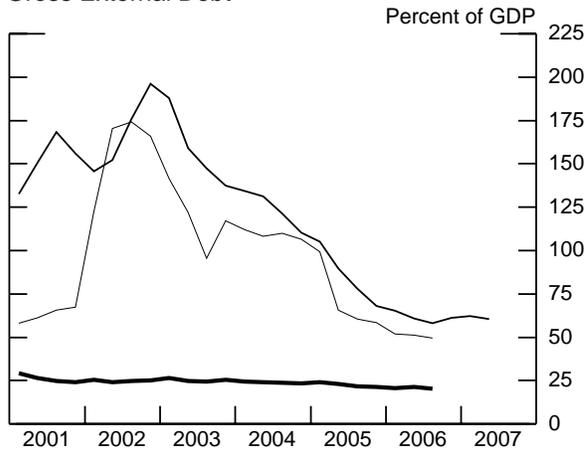
Merchandise Trade Balances



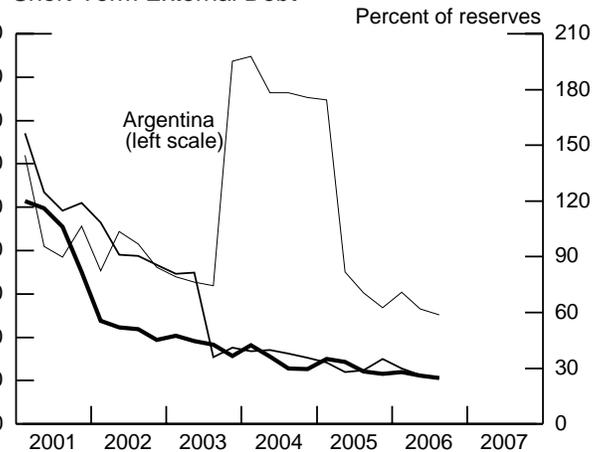
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



In **Turkey**, industrial production increased 2.4 percent in August, fueled by strength in the machinery and equipment sector. Twelve-month consumer price inflation declined to 7.1 percent in September, still above the Central Bank's year-end target range of 4 percent +/- 2 percent. At its September and October meetings, the Central Bank cut its benchmark overnight borrowing and lending rates by a cumulative $\frac{3}{4}$ percentage point and one percentage point to $16\frac{3}{4}$ and $21\frac{1}{2}$ percent, respectively. The Monetary Policy Committee indicated that the lagged effects of previous monetary tightening coupled with weakening external demand will continue to support the disinflation process.

Turkish Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q2	Q3	Jul.	Aug.	Sep.
Real GDP ¹	7.4	6.1	3.9	n.a.	...	...	...
Industrial production	5.4	5.9	.1	n.a.	-.3	2.4	n.a.
Consumer prices ²	7.7	9.7	9.5	7.1	6.9	7.4	7.1
Merch. trade balance ³	-43.3	-53.8	-60.7	n.a.	-71.5	-64.8	n.a.
Current account ⁴	-22.6	-32.9	-41.2	n.a.	-27.6	-17.1	n.a.
Unemployment rate ⁵	10.2	9.8	n.a.	n.a.	...	...	...

1. Percent change from year-earlier period. Annual data are annual averages.

2. Percent change from year-earlier period, except annual data, which are Dec./Dec.

3. Billions of U.S. dollars, annual rate. Imports are c.i.f.

4. Billions of U.S. dollars, n.s.a., annual rate.

5. Percent

n.a. Not available. ... Not applicable.