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Part 2

June 20, 2001

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

June 20, 2001

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Domestic Nonfinancial Developments

Domestic Nonfinancial Developments

Overview

Although real GDP appears likely to eke out a small gain in the second quarter, the pace of activity across the various sectors continues to be highly uneven. Generous incentives from automakers have helped to prevent a sharper drop-off in vehicle sales, and overall real PCE appears to be headed for a small increase this quarter. Construction activity remains solid in the residential sector—supported by favorable mortgage rates—and increased investment in mining and drilling and in utilities is providing a lift to spending on nonresidential structures. In contrast, business spending on equipment and software appears headed for another dismal quarter, and inventory imbalances persist. As a result, firms in manufacturing and related industries have continued to shed workers, and factory output will fall sharply again in the second quarter. Energy prices may be cresting, and core inflation has slowed after the hefty first-quarter increases.

Employment and Productivity

Labor demand has weakened further in recent months. In May, employment declined for the second straight month, and the aggregate hours of production workers were flat. Although the unemployment rate ticked down 0.1 percentage point in May, we view this as only a pause in the general uptrend that began last November.

Private nonfarm payroll employment declined 32,000 in May following a drop of more than 200,000 in April.¹ Last month's decline was again concentrated in manufacturing and related industries, but employment in the service-producing sector also increased well below trend, suggesting that the economic slowdown has spread to sectors beyond manufacturing.

Within manufacturing, job losses were widespread in May, and the three-month diffusion index of factory employment change fell to its lowest level since March 1991. Since reaching its most recent peak in July 2000, the manufacturing sector has shed 675,000 jobs, almost three-fourths of which have been lost since the start of this year. Wholesale trade, an industry that is closely linked to manufacturing, lost 13,000 jobs per month in April and May after having posted little change in employment during the first quarter. Employment

1. As is its usual practice with the release of the May data, the BLS introduced its comprehensive benchmark of the payroll survey to unemployment insurance records along with revisions to establishment classification, bias adjustment factors, and seasonal adjustment factors. In addition, the BLS introduced probability-based sample estimates and birth/death estimates for the manufacturing, mining, and construction industries. The benchmark raised the level of not seasonally adjusted total nonfarm payroll employment by 432,000 in March 2000, with the April 2001 level revised up by a similar amount. Although the monthly pattern of employment changes over the past year was altered somewhat, the new data still show a sharp deceleration in employment beginning in the fourth quarter of last year.

CHANGES IN EMPLOYMENT
(Thousands of employees; based on seasonally adjusted data)

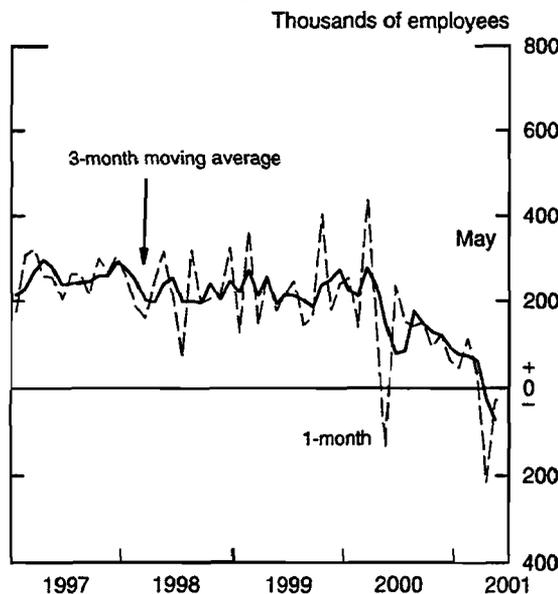
	2000		2001	2001		
	H1	H2	Q1	Mar.	Apr.	May
	--Average monthly change--					
Nonfarm payroll employment ¹	267	66	96	59	-182	-19
Previous	268	39	124	-53	-223	
Private	178	121	63	28	-217	-32
Mining	1	1	3	2	3	4
Manufacturing	5	-29	-78	-76	-113	-124
Construction	16	21	46	49	-78	31
Transportation and utilities	13	16	6	4	-8	12
Retail trade	31	21	17	-15	61	-5
Wholesale trade	9	8	-1	2	-12	-14
Finance, insurance, real estate	-7	7	12	9	8	22
Services	110	76	57	53	-78	42
Help supply services	15	-19	-37	-46	-92	1
Total government	90	-54	32	31	35	13
Total employment (household survey)	114	109	-19	-35	-426	-251
Nonagricultural	116	115	19	-62	-456	-252
Memo:						
Aggregate hours of private production workers (percent change) ^{1,2}	2.1	0.2	1.0	0.2	-0.3	0.0
Average workweek (hours) ¹	34.5	34.3	34.3	34.3	34.2	34.3
Manufacturing (hours)	41.8	41.3	41.0	41.0	41.0	40.8

Note. Average change from final month of preceding period to final month of period indicated.

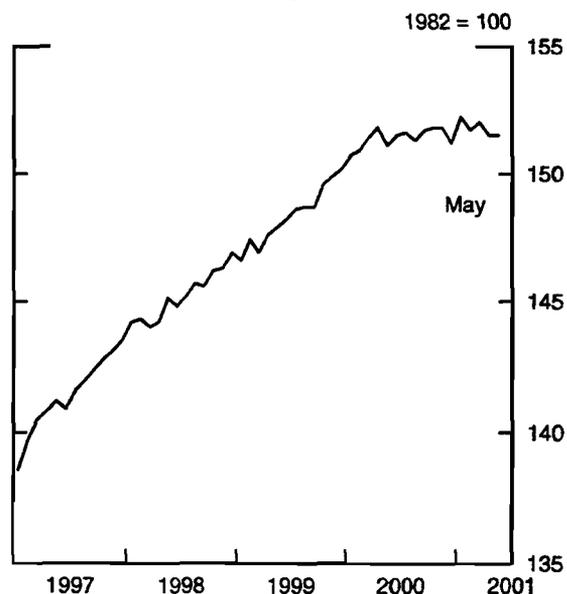
1. Survey of establishments.

2. 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.

Private Payroll Employment Growth
(Strike-adjusted data)



Aggregate Hours of Production or
Nonsupervisory Workers



in help supply services, which also is related to manufacturing activity, was flat in May after having fallen an average of 50,000 per month in the first four months of the year. Discussions with industry contacts suggest that employment in this industry has not yet stabilized, and declines may be spreading beyond workers with light industrial jobs to the clerical, office, and financial occupations.

Excluding help supply, the services industry added 41,000 jobs in May—less than half the average monthly gain in 2000—following an increase of only 14,000 in April. The weakness in services was concentrated in leisure-related and business-related services industries, which are traditionally more cyclically sensitive.

On the brighter side, hiring last month was brisk in finance, insurance, and real estate, reflecting continued strength in housing-related businesses—mortgage banking and real estate firms. Moreover, construction industry employment jumped 31,000 in May, reversing nearly half its April decline. Buoyed by the high level of activity in both residential and nonresidential building, job gains in construction have held up well in recent months, averaging 18,000 per month since the start of the year, identical to the average monthly increase over 2000 as a whole.

Aggregate weekly hours of production or nonsupervisory workers on nonfarm private payrolls were flat in May, as declines in employment were offset by an increase in the average workweek. But this comes on the heels of a 0.3 percent drop in April, and, thus, hours are very likely to post a decline for the second quarter as a whole. In manufacturing, the weakness in May was accompanied by another 0.2 hour drop in the factory workweek to 40.8 hours. The manufacturing workweek is now a full hour lower than it was last July.

In the household survey, the unemployment rate edged down 0.1 percentage point in May to 4.4 percent. However, we suspect that an early survey week in May contributed to a decline in unemployment of young workers, which held down the overall unemployment rate slightly.² Short-term job losers as a percent of household employment (a rough proxy for the layoff rate) remained at 1.1 percent in May, the highest level since 1996. Even with the small decline in May, the unemployment rate stands 0.5 percentage point above the recent low of 3.9 percent reached in September and October 2000.

2. The seasonal flow of college students into the labor market at this time of year is typically large. Because of the early timing of the survey week, fewer students may have entered the labor market by the time of the survey than is usual.

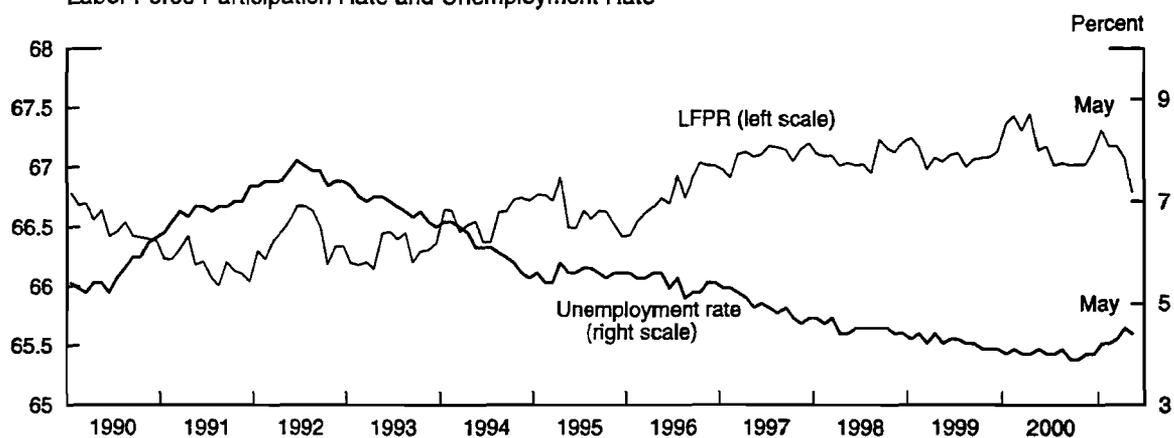
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SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES
(Percent; based on seasonally adjusted data, as published)

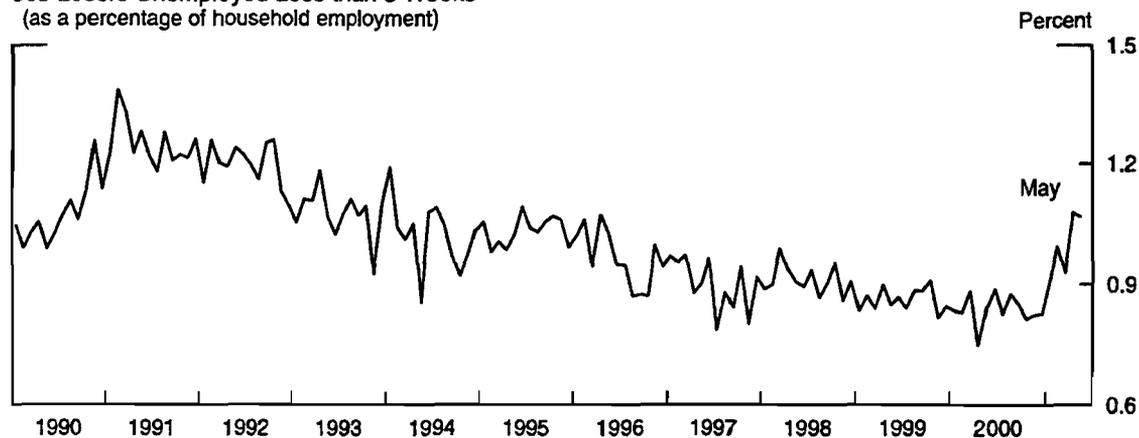
	1999	2000	2001 Q1	Mar.	2001 Apr.	May
Civilian unemployment rate (16 years and older)	4.2	4.0	4.2	4.3	4.5	4.4
Teenagers	13.9	13.1	13.7	13.8	14.2	13.6
20-24 years old	7.5	7.1	7.4	7.8	8.3	7.9
Men, 25 years and older	3.0	2.8	3.1	3.2	3.5	3.3
Women, 25 years and older	3.3	3.2	3.3	3.2	3.3	3.4
Labor force participation rate	67.1	67.2	67.2	67.2	67.1	66.8
Teenagers	52.0	52.2	51.3	50.9	50.1	48.6
20-24 years old	77.6	77.9	78.2	77.8	77.5	76.3
Men, 25 years and older	76.1	76.0	75.9	75.9	76.0	75.9
Women, 25 years and older	59.5	59.7	59.9	60.0	59.7	59.7
Memo: Potential worker rate ¹	7.2	6.9	7.1	7.2	7.4	7.3

1. The potential worker rate equals the number of civilian unemployed plus those who are not in the labor force and want a job as a percent of the civilian labor force plus those who are not in the labor force and want a job.

Labor Force Participation Rate and Unemployment Rate



Job Losers Unemployed Less than 5 Weeks
(as a percentage of household employment)



Other data also suggest that the labor market continued to soften in May. The four-week moving average of initial unemployment insurance claims moved up further to 425,000 in early June, a level not seen since 1992. Moreover, insured unemployment reached nearly 3 million, its highest level in more than seven years. Fewer employers surveyed by the Bureau of National Affairs reported difficulty hiring workers in April and May, suggesting that labor demand eased further; and while employers surveyed by the National Federation of Independent Businesses have reported no change in hiring difficulties in the past three months, the index remains well below the levels reached last fall. Households' assessments of current labor market conditions, as measured in the Conference Board survey, deteriorated somewhat further in May but remained at relatively favorable levels, and expectations of employment conditions improved slightly. Looking ahead, surveys conducted by Manpower and the National Federation of Independent Businesses suggest that employers plan to cut their hiring further in coming months.

The BLS now reports that productivity of all persons working in the nonfarm business sector fell at an annual rate of 1.2 percent in the first quarter of 2001.³ However, this measure of productivity was depressed in the first quarter by a surge in the volatile self-employed component of hours worked. The output per hour of employees, who account for more than 90 percent of all hours, was essentially flat in the first quarter. In the three quarters since the economic slowdown began in 2000:Q3, the productivity of all persons has increased at an

Labor Output per Hour

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

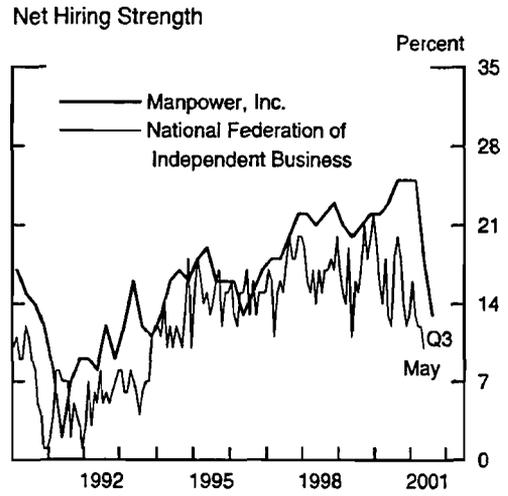
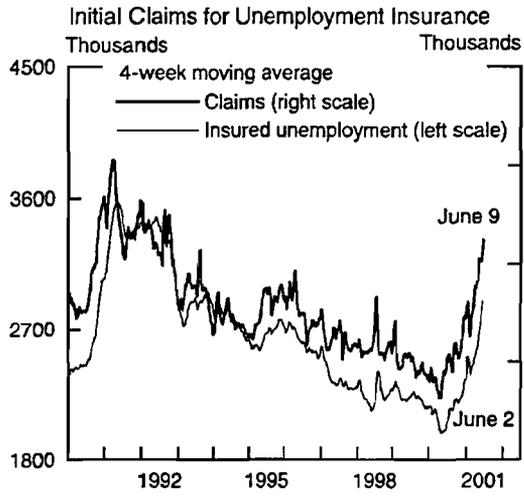
Sector	1999 ¹	2000 ¹	2000			2001
			Q2	Q3	Q4	Q1
Nonfarm business	3.8	3.3	6.3	3.0	2.0	-1.2
Nonfarm business (employees)	3.2	2.9	5.4	2.5	1.3	0.1
Nonfinancial corporations ²	4.0	3.3	5.6	4.4	0.3	-0.1

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.

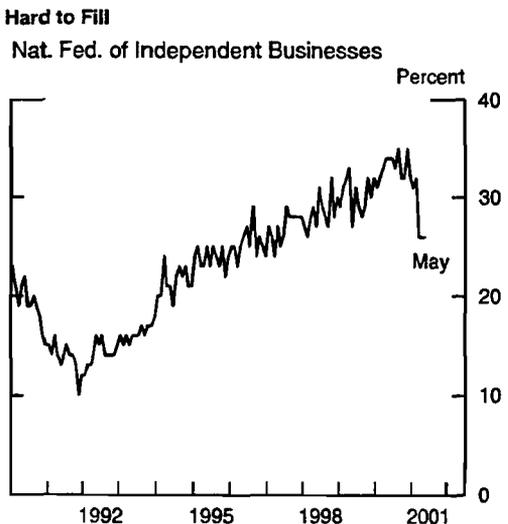
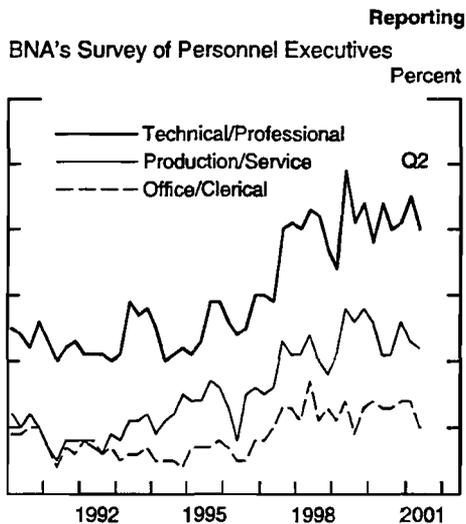
2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, and finance and insurance companies; the sector accounts for about two-thirds of business employment.

3. This estimate does not take into account the recent benchmark revisions to employment, which were released on June 1. These revisions, along with the annual revisions to the NIPAs, will be incorporated into the productivity and cost estimates released in August.

Labor Market Indicators



Note. Percent planning an increase in employment minus percent planning a reduction.



annual rate of 1.3 percent, far below the average 5.5 percent rate over the preceding three quarters. This sharp deceleration is roughly consistent with the typical relationship between productivity and output, suggesting that the bulk of the deceleration has been cyclical rather than structural.

The initial estimate of productivity in the nonfinancial corporate sector for the first quarter of 2001 showed that it edged down at an annual rate of 0.1 percent. Over the three quarters ended 2001:Q1, output per hour at nonfinancial corporations rose at an annual rate of 1.5 percent, down from the 4.8 percent rate posted in the preceding three quarters.

Production and Inventories

Industrial production and manufacturers' inventories. The contraction of the industrial sector has continued at a rapid pace. Total industrial production fell 0.8 percent in May after a 0.6 percent decline in April. Manufacturing production fell sharply again in both April and May, and lower electricity generation led to a decrease in the output of utilities over this period as well. Mining output also retreated in April and May after having posted strong gains in the first quarter. Reflecting these widespread losses in production, the diffusion index of three-month percent changes in IP declined to 33.3 percent last month, only a shade above the previous low in the first quarter of 1991.

Manufacturing output fell 0.7 percent in May, but excluding motor vehicles and parts, factory production was down 0.9 percent; indeed, the motor vehicle industry was one of few sectors that picked up in May. Assemblies rose to an annual rate of 11.8 million units, nearly a million units above the average assembly pace in the first quarter. Elsewhere in manufacturing, large production declines occurred at makers of consumer nondurable goods, business equipment, and materials in May. With output declines widespread, the overall factory operating rate sank to 76 percent—its lowest level since 1983.

The high-tech sector remains in the doldrums. The output of high-tech industries decreased for a fifth consecutive month in May: Production of semiconductors moved down 1.1 percent, and output of both office and computer equipment and communications equipment dropped noticeably. At 70.3 percent in May, capacity utilization for high-tech manufacturing industries has fallen 20 percentage points since its peak last summer. With the orders situation for semiconductors and the downstream industries remaining weak, further production cutbacks in high-tech seem likely. This interpretation is consistent with a recent industry status report from the Semiconductor Industry Association (SIA), which indicated that excess inventories of semiconductors remain a concern despite having improved somewhat in the first quarter. More recently, data from a monthly Dataquest survey of large semiconductor buyers indicated that actual days' supply remained well above its target in May. On a

SELECTED COMPONENTS OF INDUSTRIAL PRODUCTION
(Percent change from preceding comparable period)

	Proportion 2000	2000		2001		2001	
		Q3	Q4	Q1	Mar.	Apr.	May
		----Annual rate-----			--Monthly rate---		
Total	100.0	3.5	-.9	-6.7	-.2	-.6	-.8
Manufacturing	87.8	3.7	-1.6	-7.9	-.5	-.6	-.7
Ex. motor veh. and parts	82.1	4.9	.1	-6.5	-.9	-.6	-.9
Ex. high-tech industries	72.7	-.6	-2.8	-6.7	-.8	-.5	-.9
Mining	6.3	2.8	-1.5	6.2	1.4	-.2	-.4
Utilities	5.9	1.0	9.3	-2.4	1.0	-1.0	-1.8
Selected industries							
High technology	9.4	56.9	25.2	-5.7	-1.3	-1.8	-1.2
Computers	2.7	51.9	24.8	-3.5	-.4	-.4	-.6
Communication equipment	2.0	41.6	30.2	-1.4	-.9	-2.3	-1.9
Semiconductors ²	4.7	66.4	23.3	-9.0	-2.0	-2.4	-1.1
Motor vehicles and parts	5.7	-11.2	-23.6	-27.2	6.1	-.7	2.4
Aircraft and parts	2.2	11.6	5.1	-5.8	.1	.0	-.1
Market groups, excluding energy and selected industries							
Consumer goods	22.5	-.3	-1.7	-.2	-.4	-.7	-1.1
Durables	3.5	-9.5	-5.0	-4.8	-.4	-.7	-.6
Nondurables	19.0	1.6	-1.0	.6	-.4	-.6	-1.2
Business equipment	8.4	4.6	4.0	-7.3	.0	-1.5	-1.0
Construction supplies	6.1	-1.1	-4.7	-3.0	.5	-1.0	-.3
Materials	24.2	-3.1	-7.3	-11.5	-1.5	.1	-.9
Durables	15.9	-.6	-7.1	-9.5	-1.0	-.5	-.8
Nondurables	8.3	-7.6	-7.7	-15.1	-2.4	1.2	-1.2

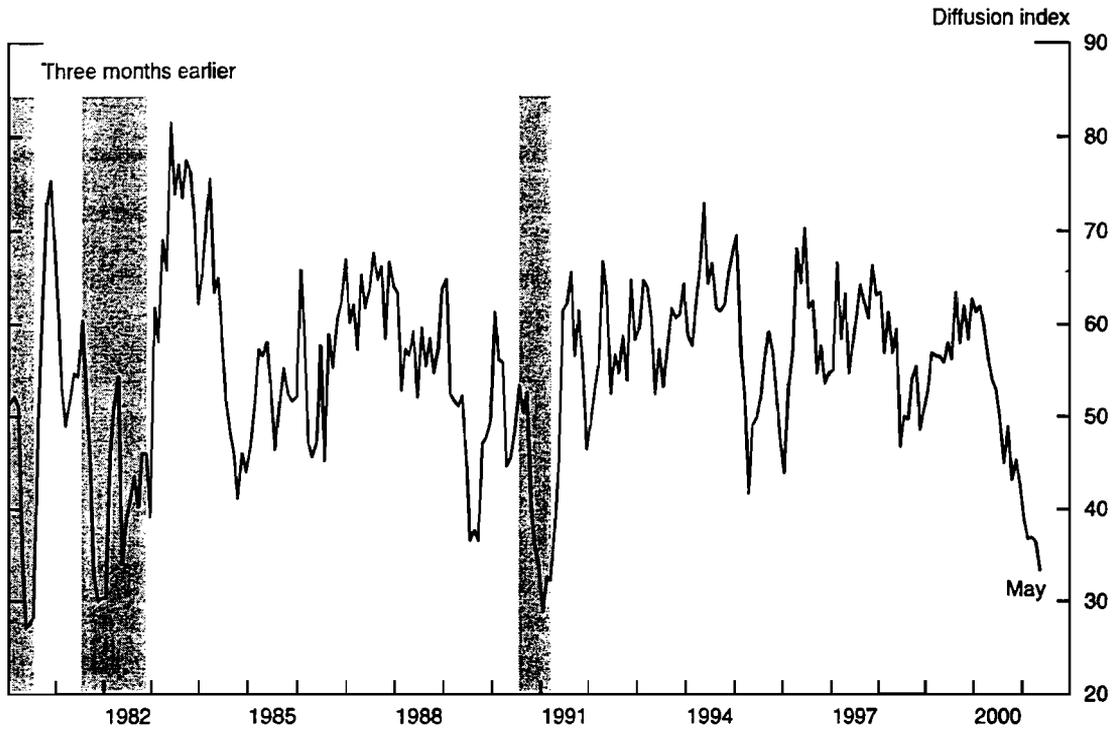
1. From the final quarter of the previous period to the final quarter of the period indicated.

2. Includes related electronic components.

CAPACITY UTILIZATION
(Percent of capacity)

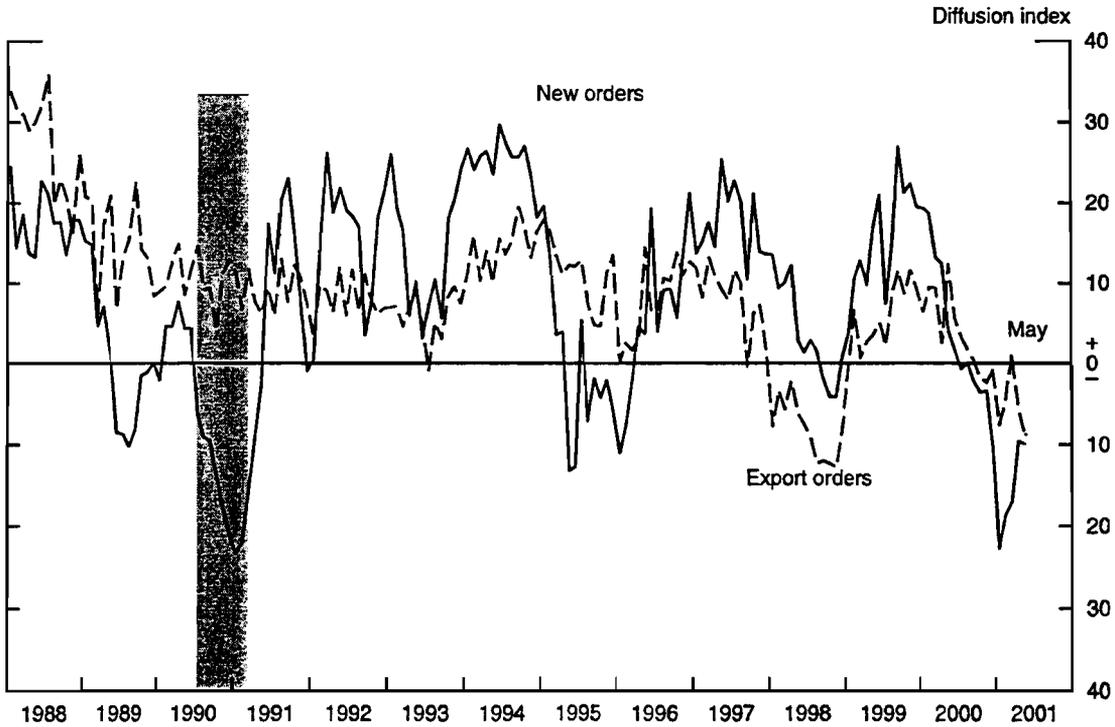
	1967-2000	1988-89	1990-91	2000		2001	2001	
	Avg.	High	Low	Q3	Q4	Q1	Apr.	May
Manufacturing	81.1	85.7	76.6	81.7	80.3	77.9	76.7	76.0
High-tech industries	80.4	81.9	72.4	89.1	85.1	77.4	72.2	70.3
Excluding high-tech	81.2	86.1	76.8	80.6	79.5	77.6	77.0	76.4

Diffusion Index of Industrial Production



Note. The diffusion index is calculated as the percentage of the number of series that increased from three months earlier plus one-half the percentage that were unchanged.

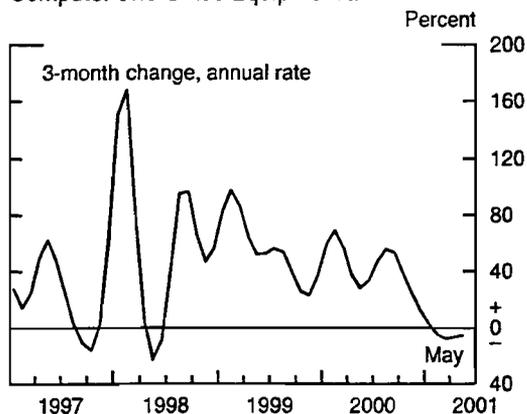
Indicators of Future Production: NAPM



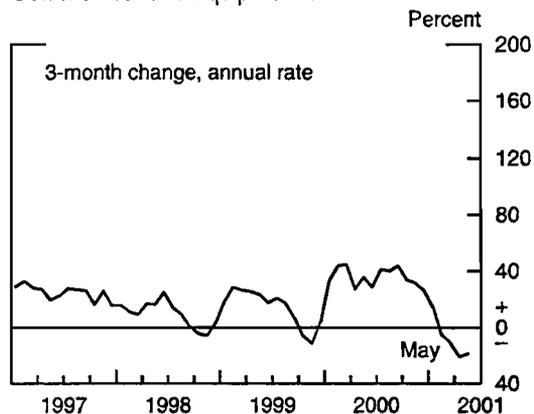
Note. The NAPM diffusion indexes are calculated as the difference between the percentage of respondents reporting an increase and those reporting a decrease in orders, seasonally adjusted.

Measures of Activity in High-Tech Industry

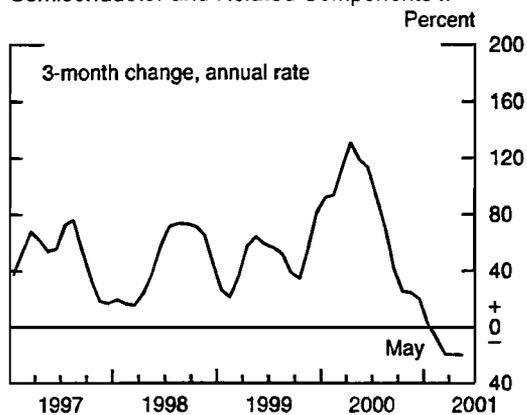
Computer and Office Equipment IP



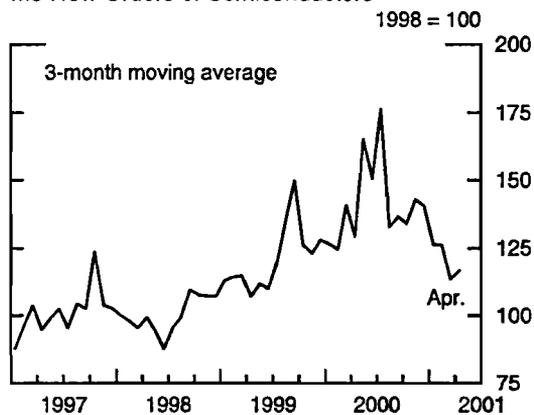
Communications Equipment IP



Semiconductor and Related Components IP

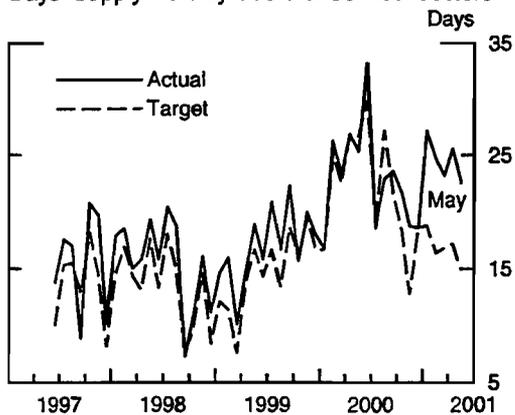


M3 New Orders of Semiconductors



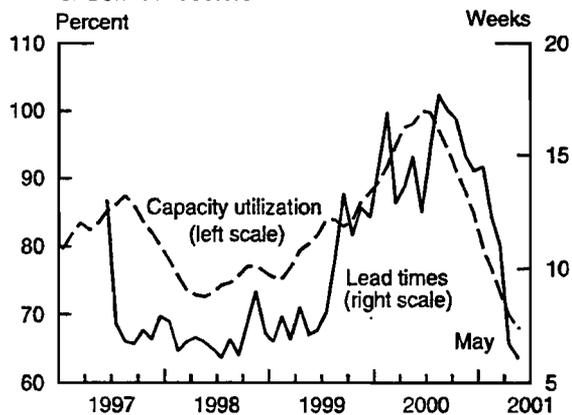
Note. Includes related components.

Days' Supply Held by Users of Semiconductors



Source. Dataquest survey of large semiconductor buyers.

Lead Times and Capacity Utilization of Semiconductors



Source. Dataquest survey of large semiconductor buyers.

somewhat brighter note, the SIA report also indicated that the computer sector has returned to “replenishment ordering.”

Overall, the book value of manufacturing inventories increased at an annual rate of \$4.6 billion in April following the \$11.9 billion liquidation posted in the first quarter. Inventories at motor vehicle manufacturers (which mainly include work in progress and materials and supplies) rose at a \$6.4 billion annual rate. Outside of motor vehicles, stocks were little changed in April. Nonetheless, shipments were down sharply, and the inventory-to-shipments ratios in most categories increased. Ratios appear to be especially high at producers of various types of construction supplies, computers and electronic equipment, primary metals, fabricated metals, chemicals, textiles, and apparel.

Partly reflecting the lingering inventory overhangs in many industries, indicators of near-term activity for manufacturing point to further cuts in output. The three-month moving average of real adjusted durable goods orders fell for a ninth consecutive month in April, the latest month for which these data are available. The new orders indexes in the NAPM survey and the Philadelphia Survey of Business suggested that orders continued to decline in May, although the levels of both indexes were notably higher than the troughs in January.

New Orders for Durable Goods
(Percent change from preceding period; seasonally adjusted)

Component	Share, 2000:H2	2000	2001			
		Q4	Q1	Feb.	Mar.	Apr.
Total orders	100.0	-1.8	-7.0	3.9	1.9	-4.9
Adjusted orders ¹	73.0	-2.1	-5.6	-.2	-.7	-4.3
Computers	6.0	1.6	-8.9	-3.4	-1.5	-5.6
Communications equipment	5.0	-6.8	-10.1	-20.8	1.2	-4.7
Semiconductors and related devices	4.0	2.8	-19.2	91.4	-9.4	-34.8
Other capital goods	18.0	-2.5	3.0	-12.2	-2.7	7.2
Other ²	40.0	-2.4	-6.9	3.8	1.3	-6.1
Memo:						
Real adjusted orders	...	-1.4	-4.2	.4	-.1	-4.3
Excluding high tech	...	-9.2	-13.4	-3.1	.8	-2.6

1. Orders excluding defense capital goods, nondefense aircraft, and motor vehicle parts.

2. Includes primary metals, most fabricated metals, most stone, clay, and glass products, household appliances, scientific instruments, and miscellaneous durable goods.

... Not applicable.

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars; annual rate except as noted;
based on seasonally adjusted Census book value)

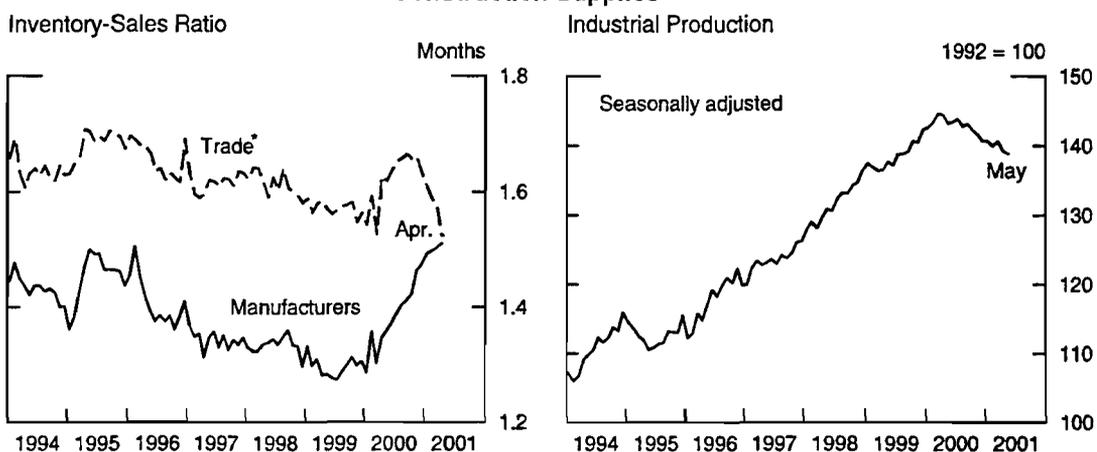
Category	2000		2001	2001		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Manufacturing and trade	46.5	45.7	-24.0	-40.5	-58.0	4.2
Less wholesale and retail motor vehicles	40.0	36.5	-10.0	-17.1	-43.3	3.0
Manufacturing	18.2	17.2	-11.9	-11.4	-45.3	4.6
Less aircraft	19.4	17.1	-10.1	-5.8	-42.3	3.6
Merchant wholesalers	8.6	9.4	-5.0	-8.2	3.4	10.2
Less motor vehicles	12.0	7.0	-2.4	-7.8	3.8	6.4
Retail trade	19.6	19.1	-7.2	-20.9	-16.1	-10.6
Automotive dealers	9.8	6.8	-11.5	-23.0	-14.3	-2.6
Less automotive dealers	9.8	12.3	4.3	2.1	-1.8	-8.0

SELECTED INVENTORY-SALES RATIOS IN MANUFACTURING AND TRADE
(Months' supply, based on seasonally adjusted Census book value)

Category	2000		2001	2001		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Manufacturing and trade	1.40	1.42	1.43	1.43	1.43	1.44
Less wholesale and retail motor vehicles	1.36	1.37	1.39	1.38	1.39	1.40
Manufacturing	1.34	1.36	1.38	1.39	1.38	1.42
Primary metals	1.70	1.83	1.81	1.84	1.81	1.87
Steel	2.19	2.41	2.29	2.34	2.29	2.38
Machinery	2.00	2.04	2.05	2.02	2.05	2.09
Computer and Electronic	1.21	1.25	1.41	1.41	1.41	1.51
Electrical equipment	1.37	1.37	1.41	1.41	1.41	1.43
Transportation equipmen	1.40	1.50	1.43	1.53	1.43	1.55
Motor vehicles	.58	.62	.59	.64	.59	.64
Aircraft	4.00	4.33	3.90	3.88	3.90	4.32
Fabricated metals	1.64	1.67	1.72	1.72	1.72	1.74
Textiles	1.81	1.87	1.77	1.75	1.77	1.77
Paper	1.16	1.18	1.18	1.18	1.18	1.19
Chemicals	1.39	1.39	1.41	1.40	1.41	1.44
Petroleum	.69	.67	.71	.69	.71	.69
Rubber and plastics	1.22	1.25	1.25	1.25	1.25	1.27
Merchant wholesalers	1.30	1.30	1.31	1.29	1.31	1.31
Less motor vehicles	1.27	1.27	1.29	1.27	1.29	1.29
Durable goods	1.61	1.63	1.63	1.62	1.63	1.64
Nondurable goods	.96	.95	.98	.95	.98	.98
Retail trade	1.59	1.62	1.60	1.59	1.60	1.57
Less automotive dealers	1.49	1.51	1.50	1.50	1.50	1.48
Automotive dealers	1.86	1.92	1.86	1.86	1.86	1.81
General merchandise	1.90	1.93	1.96	1.91	1.96	1.90
Apparel	2.42	2.47	2.43	2.41	2.43	2.38
Food	.85	.84	.85	.85	.85	.86

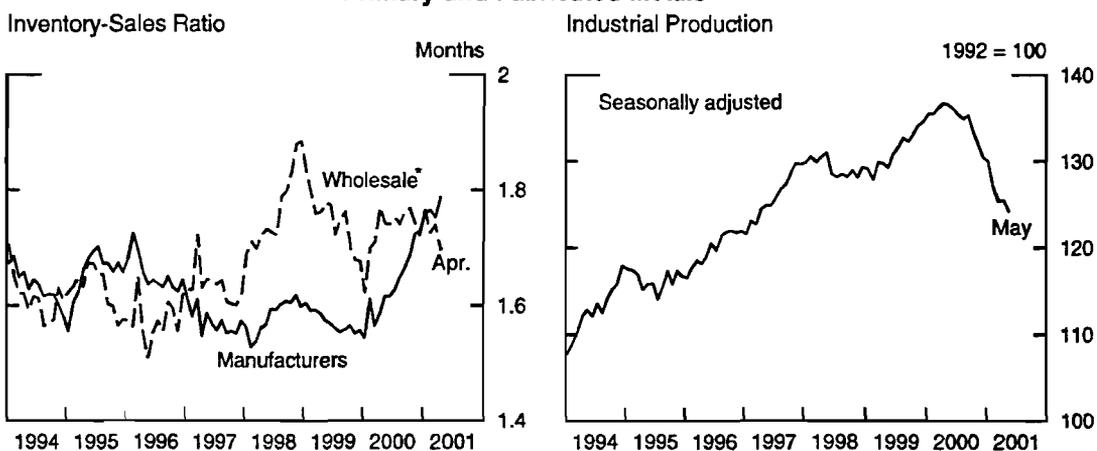
Inventory-Sales Ratios and Industrial Production in Selected Industries

Construction Supplies



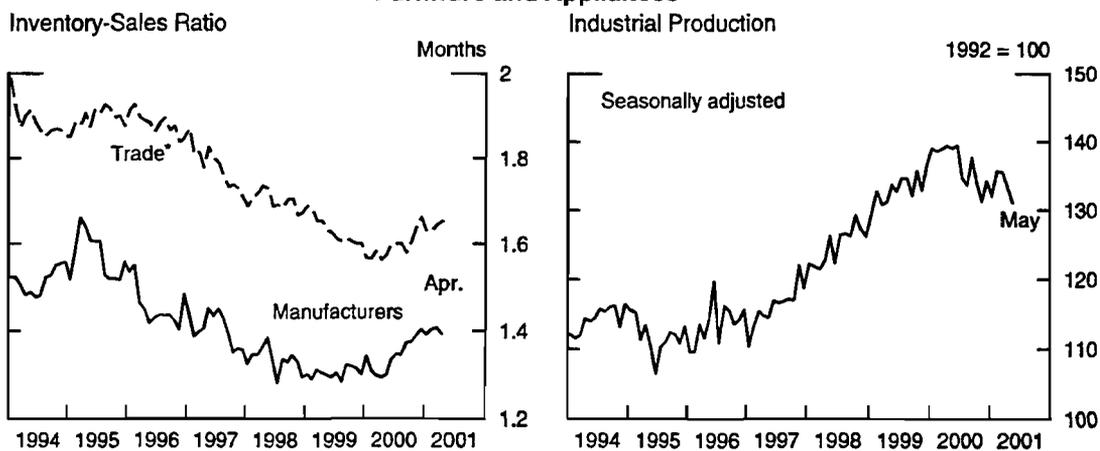
* Retail building materials group of stores and wholesale lumber and construction materials.

Primary and Fabricated Metals



* Wholesale metals and minerals, excluding petroleum.

Furniture and Appliances

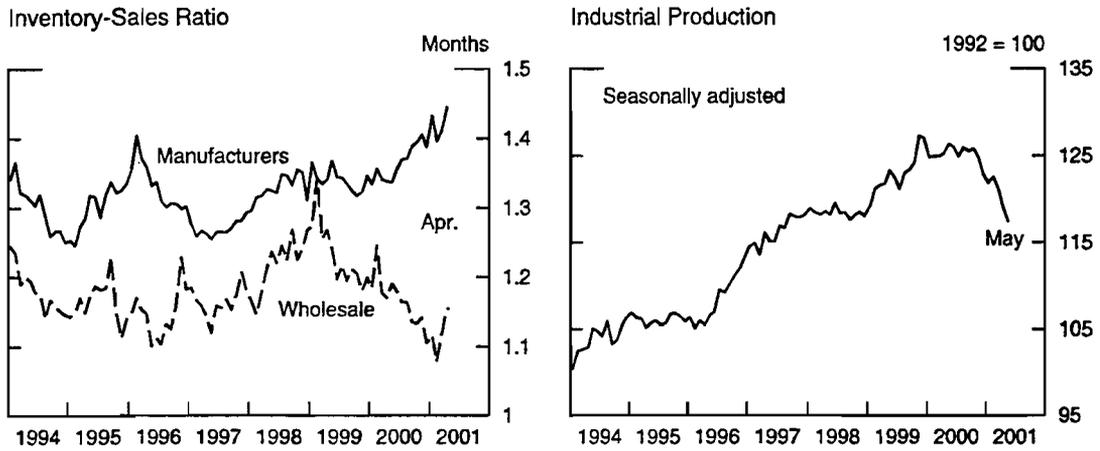


* Retail furniture group of stores and wholesale furniture and home furnishings.

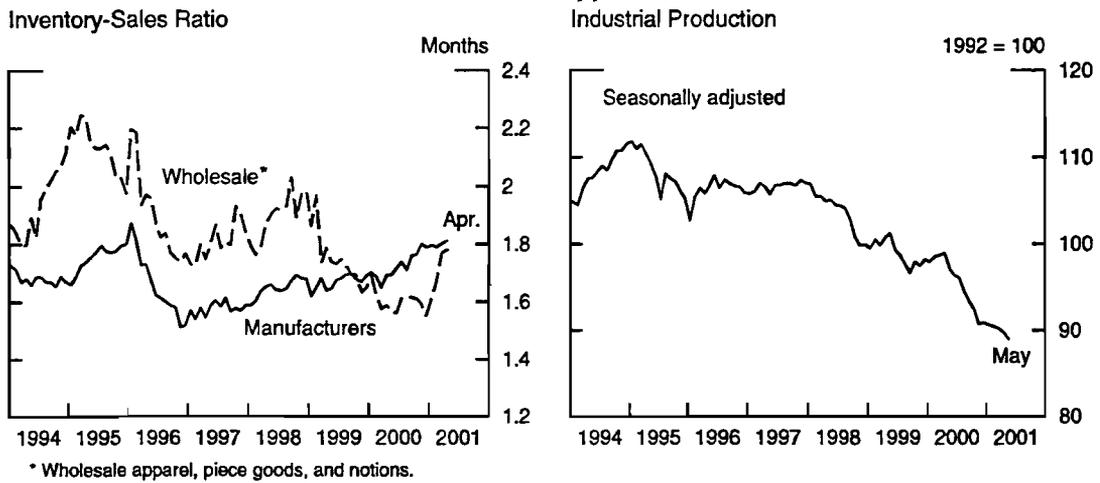
Note. Inventory-sales ratios calculated at book value.

Inventory-Sales Ratios and Industrial Production in Selected Industries

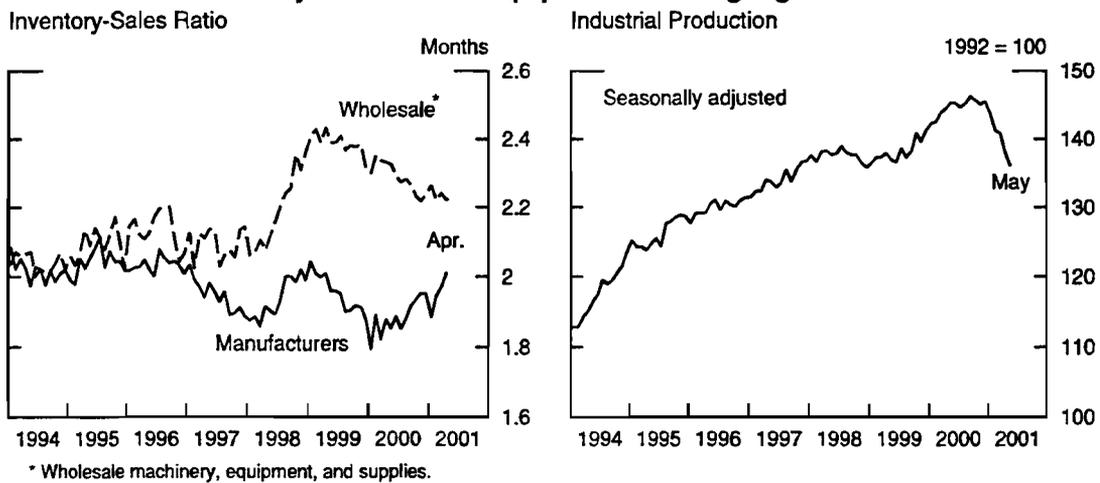
Chemicals and Products



Textiles and Apparel



Machinery and Electrical Equipment Excluding High-Tech



Note. Inventory-sales ratios calculated at book value.

Aggregate inventories. Inventories held by firms outside of manufacturing seem to be in somewhat better shape on balance. The book value of wholesale inventories excluding motor vehicles rose at an annual rate of \$6.4 billion in April, and the overall inventory-sales ratio for this sector was unchanged. Inventories held by distributors of computer equipment and electrical goods rose noticeably in April, and with sales down in both categories, stock-to-sales ratios climbed from already elevated levels. For other wholesalers, inventory-sales ratios have moved up a little in recent months but remain well below the levels of late 1998.

In the retail sector (excluding automotive dealers) , the book value of inventories dropped at an annual rate of \$8 billion in April, compared with a \$4.3 billion increase in the first quarter. The liquidation was led by sizable runoffs at clothing and accessory stores and at general merchandisers. Sales moved up in these two categories in April, and inventory-sales ratios dropped appreciably. Retailers in other categories registered only small inventory changes in April, and in general, retailers' inventory-sales ratios have remained relatively stable over the past year after having trended downward during the latter half of the 1990s. All told, the book value of manufacturing and trade inventories (excluding motor vehicles) increased at an annual rate of \$3 billion in April following the \$10 billion (annual rate) liquidation recorded in the first quarter.⁵

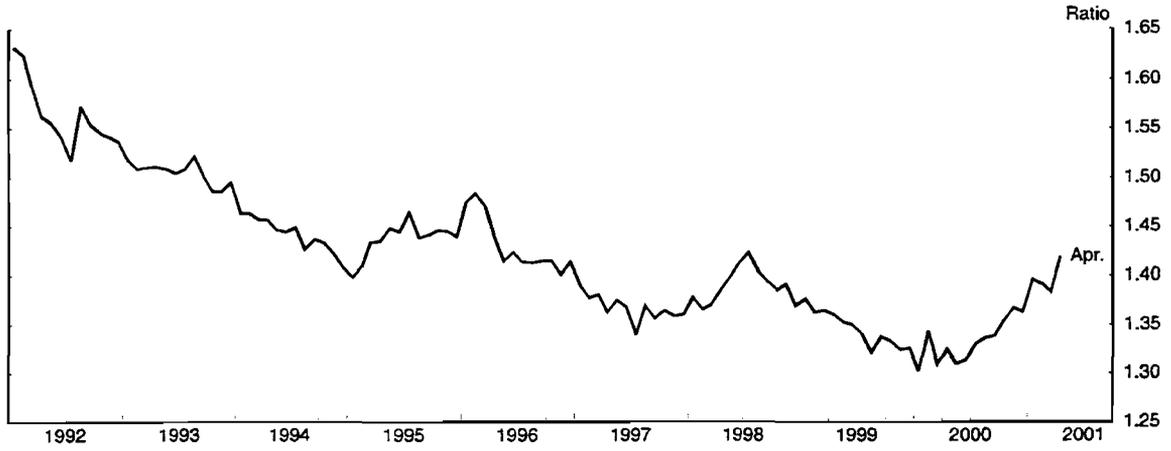
Motor vehicle sales and production. Sales of new light vehicles in May came in at a hefty rate of 16.5 million units—unchanged from April and off just 500,000 units from the robust pace of the first quarter. Despite rising gasoline prices, the Big Three automakers saw their sales of light trucks pick up from the soft April pace, reflecting a strong consumer response to a late-month boost in pricing and financing incentives at GM. Nevertheless, GM, Ford, and DaimlerChrysler had a combined share of the light vehicle market of just 64 percent in May—only slightly above the record-low of 63 percent reported last December.

On balance, the fundamentals affecting consumers' purchases of motor vehicles look mixed in the near term. On the one hand, we expect that producers will continue to offer attractive pricing schemes. Indeed, new vehicle prices as measured in the CPI edged down further in May, and incentives on light trucks by GM and Ford in June reportedly will be at least as high as those the month

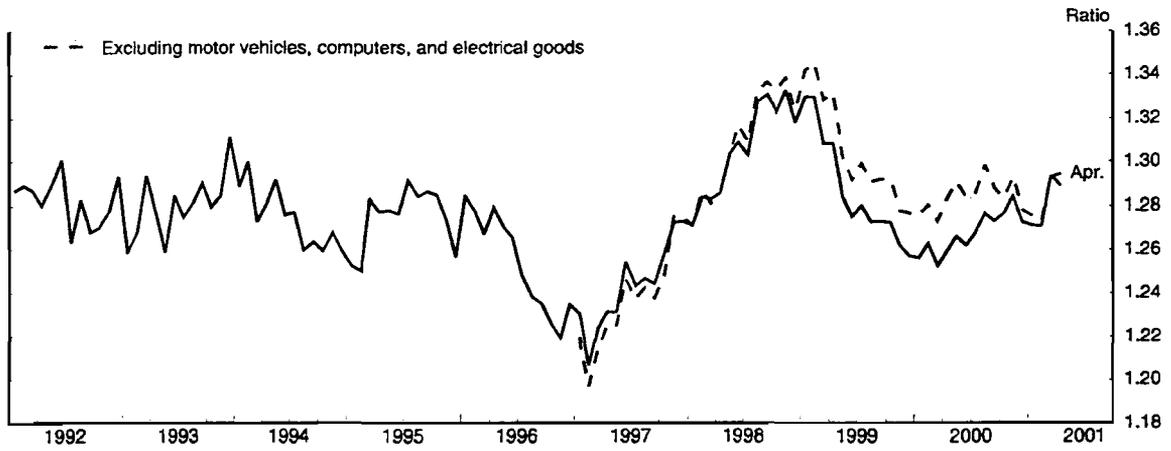
5. The Census Bureau has begun reporting these inventory data according to the North American Industrial Classification System (NAICS). Although the definitions of many of the sub-categories have changed, the aggregate inventory data are little affected by the changes in definition.

Inventory-Sales Ratios

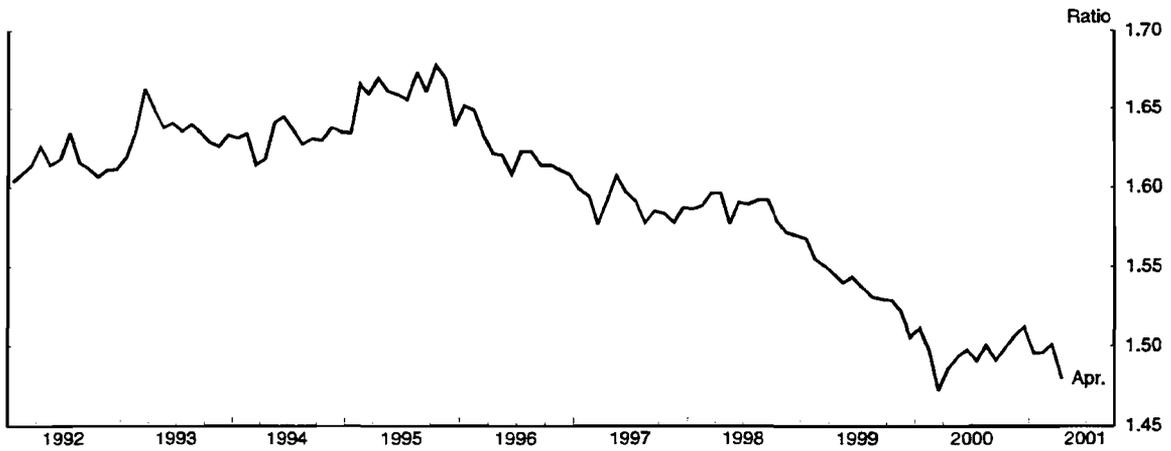
Manufacturing



Wholesale Trade Excluding Motor Vehicles



Retail Trade Excluding Motor Vehicles



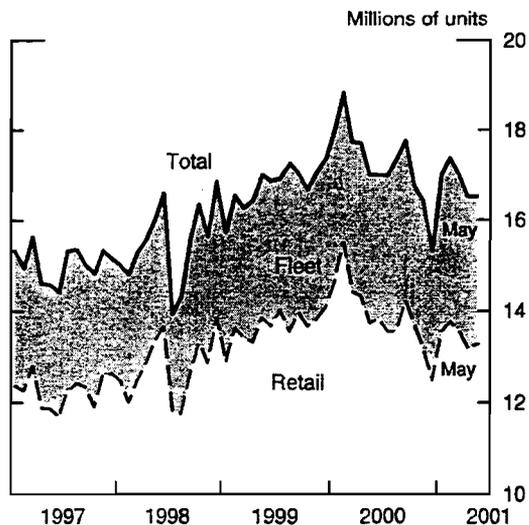
SALES OF AUTOMOBILES AND LIGHT TRUCKS
(Millions of units at an annual rate, FRB seasonals)

	1999	2000	2000		2001	2001		
			Q3	Q4	Q1	Mar.	Apr.	May
Total ¹	16.8	17.2	17.4	16.3	17.0	17.0	16.5	16.5
Autos	8.7	8.8	8.8	8.3	8.7	8.4	8.5	8.4
Light trucks	8.1	8.4	8.6	7.9	8.3	8.6	8.0	8.1
North American ²	14.3	14.4	14.5	13.4	14.1	14.1	13.4	13.5
Autos	7.0	6.8	6.8	6.3	6.7	6.4	6.4	6.4
Big Three	4.9	4.7	4.5	4.2	4.5	4.3	4.1	4.1
Transplants	2.1	2.2	2.3	2.1	2.1	2.1	2.2	2.2
Light trucks	7.3	7.6	7.7	7.1	7.4	7.7	7.0	7.2
Big Three	6.6	6.6	6.7	6.0	6.4	6.6	6.0	6.2
Transplants	.8	1.0	1.0	1.0	1.0	1.1	1.0	1.0
Foreign-produced	2.5	2.9	2.8	2.9	2.9	2.9	3.1	3.0
Autos	1.7	2.0	2.0	2.0	2.0	2.0	2.2	2.0
Light trucks	.8	.8	.8	.8	.9	.9	.9	.9
Memo:								
Total, as reported	16.8	17.2	17.4	16.2	17.1	17.0	16.5	16.5

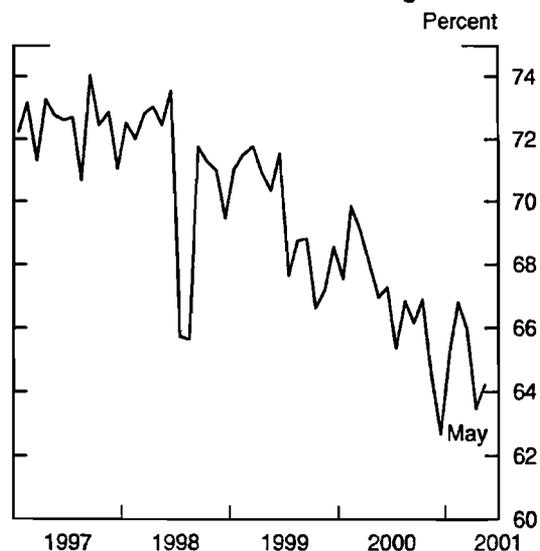
Note. Components may not sum to totals because of rounding. Data on sales of trucks and imported autos for the most recent month are preliminary and subject to revision.

1. Excludes the estimated effect of automakers' changes in reporting periods.
2. Excludes some vehicles produced in Canada that are classified as imports by the industry.

Fleet and Retail Sales of Light Vehicles
(Annual rate; FRB seasonals)



Combined Market Share for the Big Three



Note. Staff estimates based on confidential data.

Production of Domestic Autos and Trucks
(Millions of units at an annual rate except as noted; FRB seasonal basis)

Item	2001			2001				
	Q1	Q2 ¹	Q3 ¹	Feb.	Mar.	Apr.	May	June ¹
U.S. production	10.9	11.5	11.8	10.8	11.4	11.5	11.8	11.3
Autos	5.0	5.0	5.0	4.9	5.1	5.1	5.1	5.0
Trucks	6.0	6.5	6.8	6.0	6.4	6.5	6.7	6.3
Days' supply ²	60.7	n.a.	n.a.	60.9	61.1	62.7	62.4	n.a.
Autos	49.8	n.a.	n.a.	49.3	52.0	50.0	49.1	n.a.
Light trucks ³	70.5	n.a.	n.a.	71.9	68.8	74.2	74.2	n.a.
Inventories ⁴	2.80	n.a.	n.a.	2.87	2.80	2.74	2.75	n.a.

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

1. Production rates reflect manufacturers' schedules for June and Q3.

2. Quarterly average calculated using end-of-period stocks and average reported sales.

3. Excludes medium and heavy (classes 3-8) trucks.

4. End-of-period stocks; excludes medium and heavy (class 3-8) trucks.

n.a. Not available.

before.⁶ On the other hand, a softening labor market and negative wealth effects point to a further downshift in sales in coming months. In addition, the increases in gasoline prices so far this year could produce a small drag on overall motor vehicle demand, and car-buying attitudes in the University of Michigan survey of consumer sentiment declined in early June.

The overhang of motor vehicle inventories that developed late last year was largely worked off by the end of the first quarter. Currently, auto stocks largely appear to be at comfortable levels. However, as a result of the increases in light truck production in April and May, inventory imbalances have re-emerged in that segment of the market. Days' supply of light trucks was 74 in May—above the dealers' desired range of 65 to 70. Current production schedules call for motor vehicle output to step up from an annual rate of 11.5 million units in the second quarter to an 11.8 million unit rate in 2001:Q3. However, most industry analysts expect sales of domestically produced vehicles to weaken further next quarter, and assemblies may well come in below scheduled levels.⁷

6. With prices for new vehicles falling, prices for used cars and trucks have declined in recent months as well.

7. Reducing output at this time of the year is not difficult because factory downtime for summer vacations can be extended. In addition, start-up problems are not uncommon when new models are introduced.

Consumer Spending and Personal Income

After having increased at an annual rate of about 2-3/4 percent in the previous two quarters, the pace of consumer spending appears to have decelerated further in the current quarter. Real purchases of consumer goods excluding motor vehicles continued to increase in April and May, though at a slower pace than earlier in the year. Moreover, real purchases of energy services will likely be little changed in the second quarter after falling sharply in the first quarter. Offsetting some of this weakness, outlays for non-energy services registered a noticeable increase in April (the latest available data), led by gains in airline travel, medical care, personal business services, and recreational services.

In May, nominal sales in the retail control group of stores, which excludes automotive dealers and building materials and supply stores, increased 0.4 percent following a slightly upward-revised gain in April of 0.8 percent.⁸ Sales were off sharply at general merchandise and clothing and accessory stores in May. Nevertheless, many other retailers reported large increases in nominal expenditures, including furniture outlets, health and personal care stores, sporting goods, hobby, book and music stores, and food services (eating and drinking establishments). Nominal outlays also rose at gasoline stations, but this increase likely reflected higher prices at the pump last month. Physical product data from the Energy Department indicate that real gasoline purchases declined in May. Factoring in price changes, we estimate that retail control increased 0.1 percent in real terms in May following an increase of 0.6 percent in April.

Recently legislated tax reductions should provide some stimulus to consumption later this year, although the timing and magnitude of the likely response is uncertain. But other fundamentals for the household sector are rather soft. Real disposable personal income has been rising only slowly this spring, and the recent uptrend in the unemployment rate raises the possibility that households could become cautious about purchasing more discretionary items. Although the ratio of household net worth relative to disposable income will likely increase in the second quarter, the sizable drag on spending from earlier declines in wealth remains.

Overall, the Michigan Survey Research Center (SRC) and Conference Board surveys indicate that consumer sentiment has essentially moved sideways at levels near their historical averages since January, after having dropped sharply toward the end of 2000. Meanwhile, labor market expectations in both surveys

8. The Advance Monthly Retail Trade Survey for May applied the NAICS to the establishment-level data for the first time. Neither the changes in the industry classifications nor the other data revisions associated with the Census Bureau's usual annual benchmarking procedures led to any significant changes to the pattern of annual sales growth in the retail control group between 1992 and 2000 or to its recent monthly movements.

RETAIL SALES
(Percent change; seasonally adjusted)

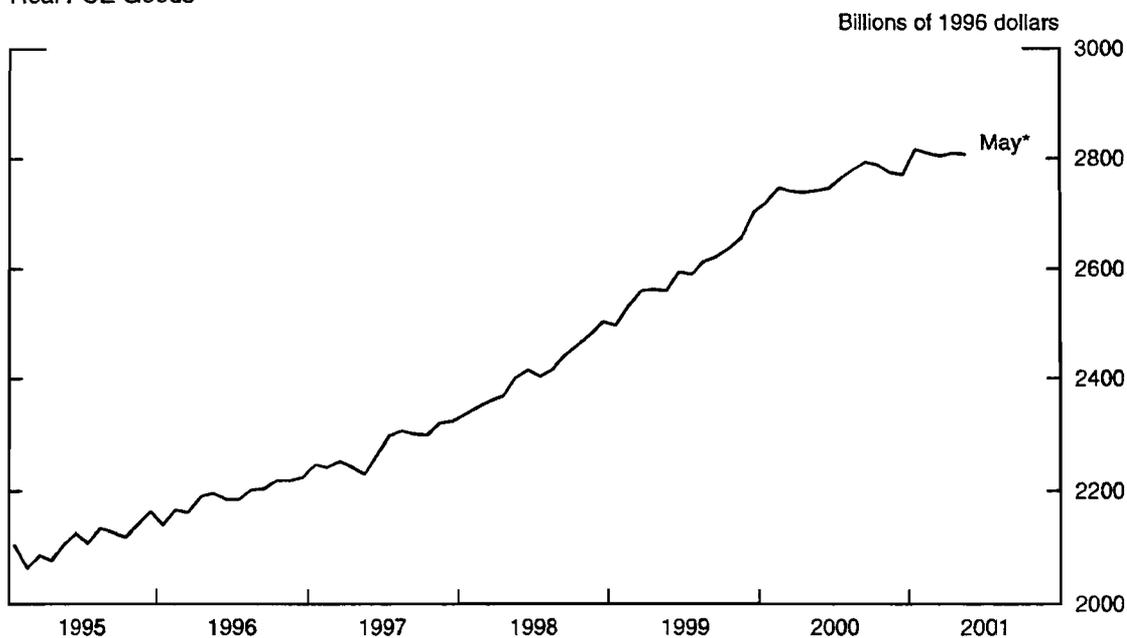
	2000		2001	2001		
	Q3	Q4	Q1	Mar.	Apr.	May
Total retail trade and food services	1.1	.1	1.3	-.4	1.4	.1
Previous estimate				-.3	1.1	
Retail control ¹	1.2	.3	1.0	-.4	.8	.4
Previous estimate				-.4	.7	
Furniture and home furnishings	.0	-2.2	1.7	-.4	-.2	1.2
Electronics and appliances	-.1	-.5	-1.8	-.8	-.6	-.1
Clothing and accessories	1.1	1.3	1.6	-2.0	.6	-1.0
Food and beverage stores	.4	1.0	.9	-.1	.0	.6
General merchandise	1.6	-.1	1.0	-1.4	2.6	-1.3
Gasoline stations	2.1	.0	-1.1	-1.9	4.2	1.4
Health & personal care	2.7	1.7	2.7	.6	-.1	1.1
Nonstore retailers ²	1.3	1.1	-1.5	-.9	-.6	.5
Other retailers ³	.8	-.6	3.0	2.1	-.6	2.2

1. Total retail sales less sales at building materials and supply stores and automobile and other motor vehicle dealers.

2. Includes electronic shopping and mail order houses.

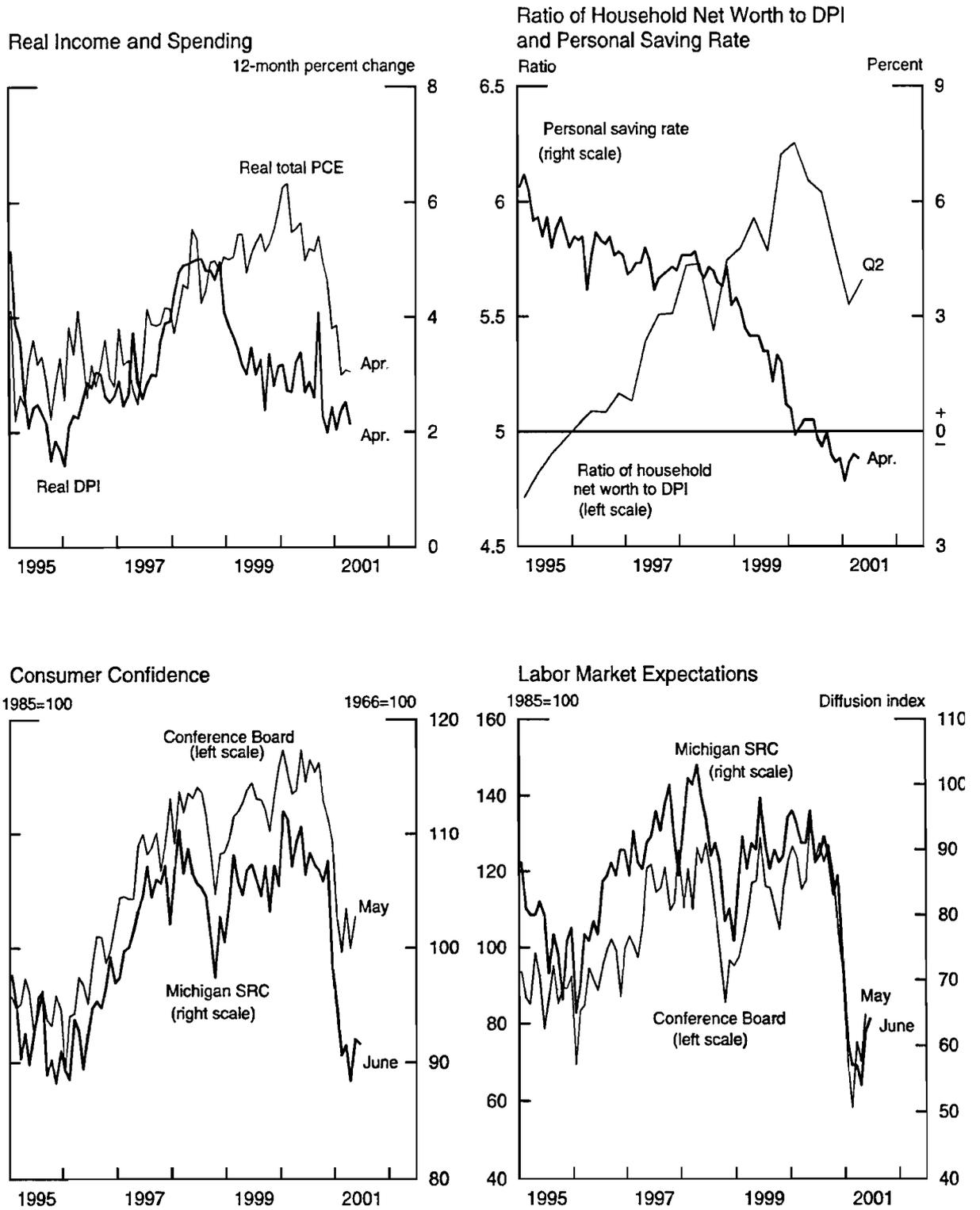
3. Includes miscellaneous retailers and sporting goods, hobby, book and music stores.

Real PCE Goods



*Staff estimates from March through May.

Household Indicators



Private Housing Activity

(Millions of units; seasonally adjusted annual rate)

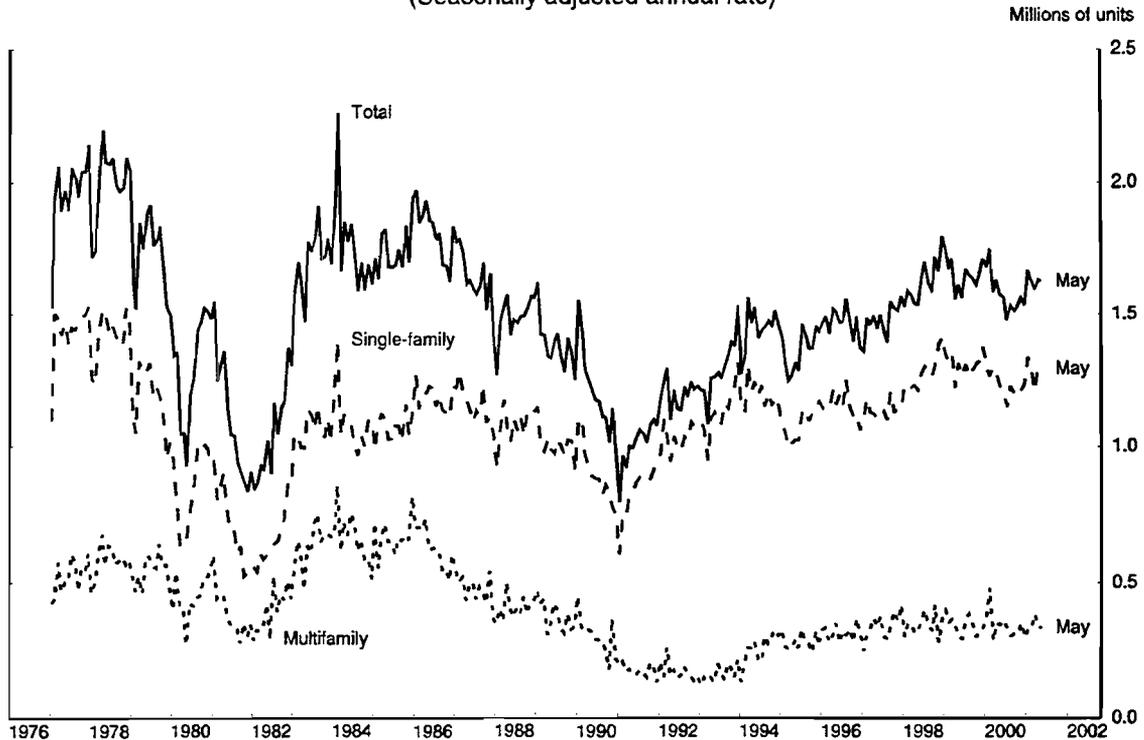
	2000			2001			
	2000	Q3	Q4	Q1 ^r	Mar. ^r	Apr. ^r	May ^p
<i>All units</i>							
Starts	1.57	1.51	1.54	1.63	1.59	1.63	1.62
Permits	1.59	1.54	1.58	1.67	1.63	1.59	1.62
<i>Single-family units</i>							
Starts	1.23	1.19	1.22	1.28	1.21	1.29	1.29
Permits	1.20	1.16	1.20	1.24	1.21	1.22	1.20
Adjusted permits ¹	1.25	1.21	1.23	1.28	1.25	1.26	1.25
New home sales	0.88	0.87	0.94	0.96	0.99	0.89	n.a.
Existing home sales	5.11	5.07	5.10	5.27	5.43	5.20	n.a.
<i>Multifamily units</i>							
Starts	0.34	0.31	0.32	0.35	0.38	0.34	0.33
Permits	0.39	0.38	0.38	0.43	0.42	0.37	0.42
<i>Mobile homes</i>							
Shipments	0.25	0.24	0.20	0.17	0.18	0.18	n.a.

1. Adjusted permits equals permit issuance plus total starts outside of permit-issuing areas.

p Preliminary. r Revised. n.a. Not available.

Total Private Building

(Seasonally adjusted annual rate)



have improved slightly, on balance, so far this year after having deteriorated dramatically at the end of last year.

Housing Markets

Housing activity remained brisk in April and May. Low mortgage rates have supported housing in recent months even as a weakening labor market and sluggish personal income growth have acted to restrain it.

At an annual rate of 1.62 million units in May, total housing starts were little changed from the pace in April.⁹ The April-May average was in line with activity in the first quarter and was well above that seen last year. Single-family housing starts were about unchanged in May at an annual rate of 1.29 million units but were a bit above adjusted permits, suggesting that this starts figure slightly overstates the underlying pace of activity. Multifamily starts edged down almost imperceptibly in May.

Although the rate on thirty-year fixed-rate mortgages has moved up since March to just over 7 percent, rates are still quite low by historical standards. In addition, ARM rates have been falling fairly steadily since late last year, and the spread between one-year ARMs and thirty-year fixed-rate mortgages widened from about 40 basis points in January to 132 basis points in mid-June.¹⁰

Sales of both new and existing single-family homes fell in April following near-record levels for each in March.¹¹ The April drop was more noticeable for new home sales; sales of existing homes have remained within a fairly narrow band since 1999. Looking ahead, more recent indicators of housing demand continued to paint, on balance, a relatively upbeat picture. The Michigan Survey's measure of households' perceptions of homebuying conditions jumped again in early June, reflecting in part respondents' favorable views on mortgage rates. And mortgage applications for home purchases continued to move higher through mid-June.

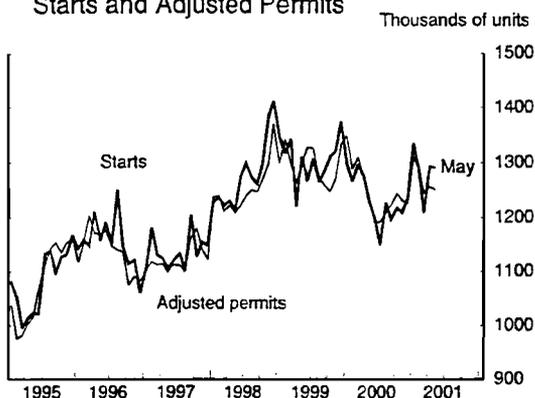
9. The starts data were revised since January 1999 to incorporate changes in the way the Census Bureau adjusts for late reports, undercoverage, and nonresponses. The revisions lowered the level of single-family starts 2.5 percent and raised the level of multifamily starts 1.8 percent, on average, over this period.

10. Although the ARM spread has widened sharply in recent months, the ARM share of mortgage originations has declined from 14 percent in January to 10 percent in April. However, because the ARM share is constructed from mortgages that closed in a given month, it tends to lag the ARM spread, which is calculated from the mortgage rates recorded for that month.

11. The new home sales data were also revised to incorporate changes in the way the Census Bureau adjusts for late reports, undercoverage, and nonresponses. These revisions affect the historical data starting in January 1999: The level of new home sales was revised down 3 percent, on average, since then.

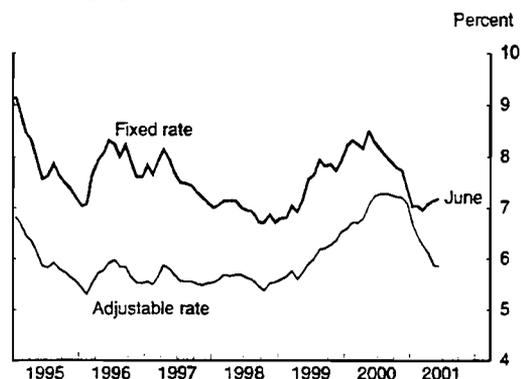
Indicators of Single-Family Housing

Starts and Adjusted Permits



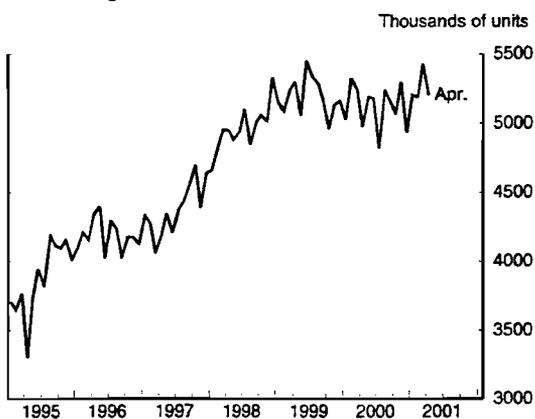
Source: Census Bureau. Adjusted permits calculated by staff.

Mortgage Rates



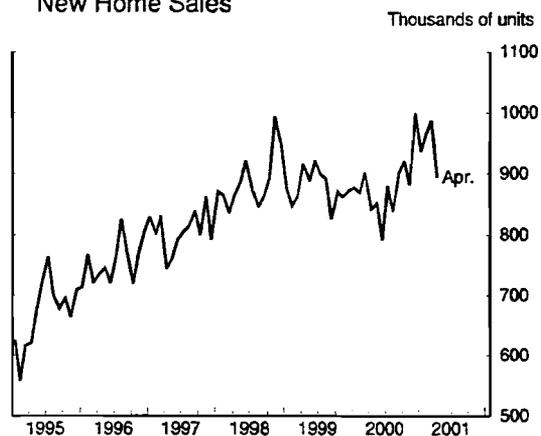
Note: The June reading is an average of weekly data through June 15.
Source: Freddie Mac.

Existing Home Sales



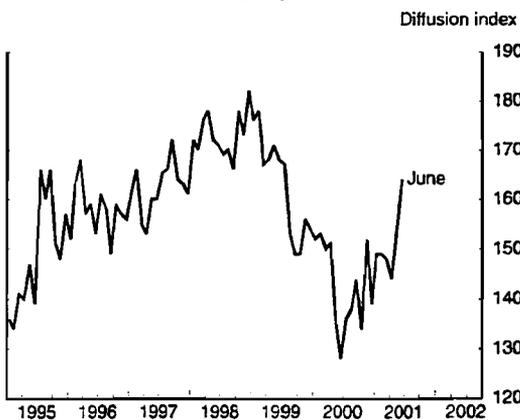
Source: National Association of Realtors.

New Home Sales



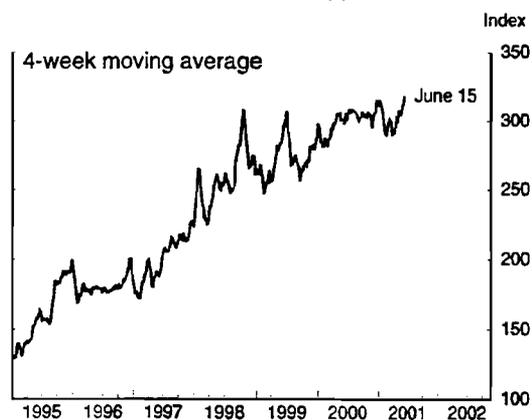
Source: Census Bureau.

Perceived Homebuying Conditions



Source: Michigan Survey, not seasonally adjusted.

MBA Index of Purchase Applications



Business Fixed Investment

Equipment and software. Real expenditures on equipment and software continued to fall early in the second quarter, a reflection of anemic growth in output, declines in corporate cash flow, and continued uncertainty about the pace of sales going forward.

The near-term outlook for spending on high-tech equipment continues to be decidedly pessimistic. Nominal shipments of computing equipment dropped 3.9 percent in April (not at an annual rate) following a 9 percent decline in the first quarter.¹² In addition, anecdotal reports suggest that businesses are lengthening the replacement cycle for personal computers and software, likely in response to weak fundamentals.¹³ Shipments of communications equipment slumped 9 percent in April after having fallen 13.6 percent in the first quarter. Bookings also decreased sharply in April; since last June, orders have plummeted 45 percent (not at an annual rate), and the level of new orders for communications equipment in April was below shipments for the third consecutive month, suggesting that shipments may have further to fall in coming months.

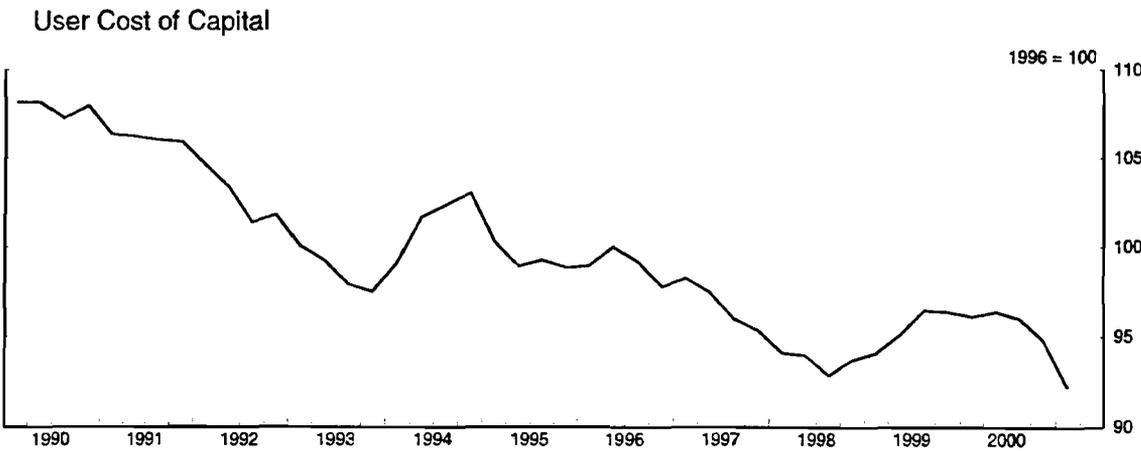
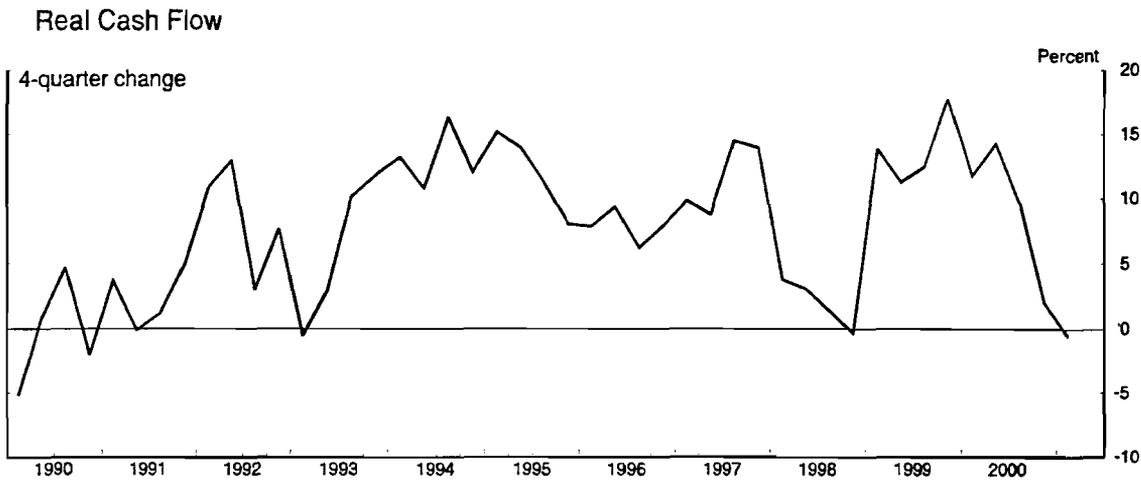
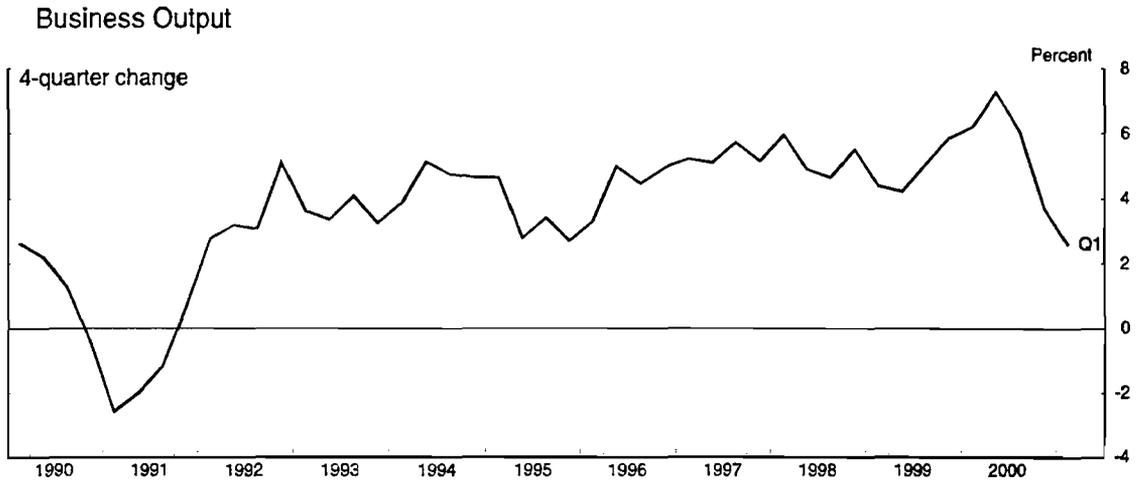
Business expenditures for aircraft are likely to be little changed in the second quarter. Although shipments of aircraft declined 9.2 percent in April, the decrease appears to reflect, in part, a drop in exported planes. In addition, more recent delivery data (provided by Boeing) point to a rebound in shipments in May. Regarding business spending on motor vehicles, fleet sales dropped in both April and May, and further declines are anticipated in June. The overall slowing in business conditions likely is contributing to softer sales, but the weakness in the second quarter mainly represents a payback from the acceleration in automobile deliveries to fleet customers that occurred in the first quarter. Although sales of medium and heavy trucks in May retraced most of the sharp decline in April, sales so far this quarter are still running well below their first-quarter pace, and new orders for medium and heavy trucks in May remained extremely weak.

Outside of the high-tech and transportation sectors, nominal shipments of nondefense capital goods fell 2.3 percent in April after having edged up 0.7 percent in the first quarter. The weakness in this category has been

12. With the release of the most recent orders and shipments data, the Census Bureau began reporting these data according to the NAICS. The definitions of computers and nondefense communications equipment were unchanged, but the definition of total nondefense capital goods was altered to include data on photographic equipment; electromedical, measuring, and controlling devices; and heavy-duty trucks. These category changes have no implications for the BEA's construction of equipment and software investment.

13. Personal computers constitute about 67 percent of business spending on computers.

Equipment Investment Fundamentals



Note. Equipment excluding high-tech and transportation.

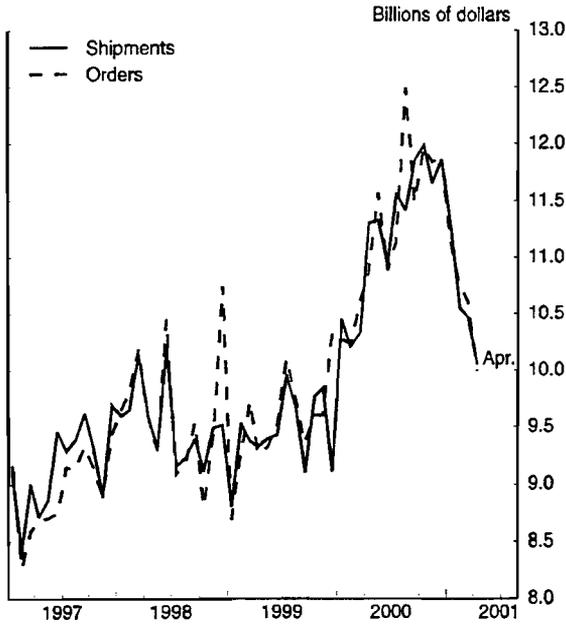
BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period;
based on seasonally adjusted data, in current dollars)

	2000		2001	2001		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
<u>Equipment and software</u>						
Shipments of nondefense capital goods	.5	.1	-2.6	.2	-1.0	-5.0
Excluding aircraft	1.4	.6	-3.0	-2.4	-.3	-3.4
Computers and related equipment	3.8	1.9	-9.0	-6.2	-.9	-3.9
Communications equipment	.5	-.2	-13.6	-.7	.1	-9.0
All other categories	1.0	.4	.7	-1.8	-.3	-2.3
Shipments of complete aircraft	-5.9	-16.0	17.4	47.2	-22.5	-9.2
Medium & heavy truck sales (units)	-11.4	-11.3	-1.5	-3.6	-.2	-12.4
Orders for nondefense capital goods	.1	-.4	-8.6	.3	.5	-4.6
Excluding aircraft	-1.1	-1.7	-3.9	-4.6	-3.0	-2.0
Computers and related equipment	5.4	1.6	-8.9	-3.4	-1.5	-5.6
Communications equipment	-11.2	-6.8	-10.1	-20.8	1.2	-4.7
All other categories	-.3	-1.5	-1.3	-1.7	-4.0	-.7
<u>Nonresidential structures</u>						
Construction put in place, buildings	2.2	1.2	4.7	-1.1	3.3	-.9
Office	4.2	5.5	2.9	-2.1	5.3	-2.5
Other commercial	-1.1	-1.4	8.4	2.2	1.7	-.1
Institutional	4.2	.2	2.0	-3.0	2.9	.4
Industrial	5.1	4.8	5.5	-4.3	4.4	-.8
Lodging and miscellaneous	-.8	-5.6	2.4	1.9	1.7	-1.3
Rotary drilling rigs in use ¹	10.2	7.4	13.9	6.1	2.7	4.4

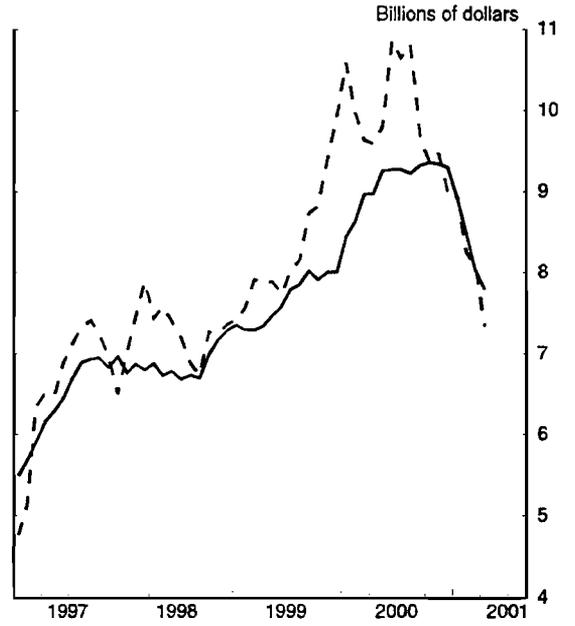
1. Percent change of number of rigs in use, seasonally adjusted.

Recent Data on Orders and Shipments
(3-month moving average)

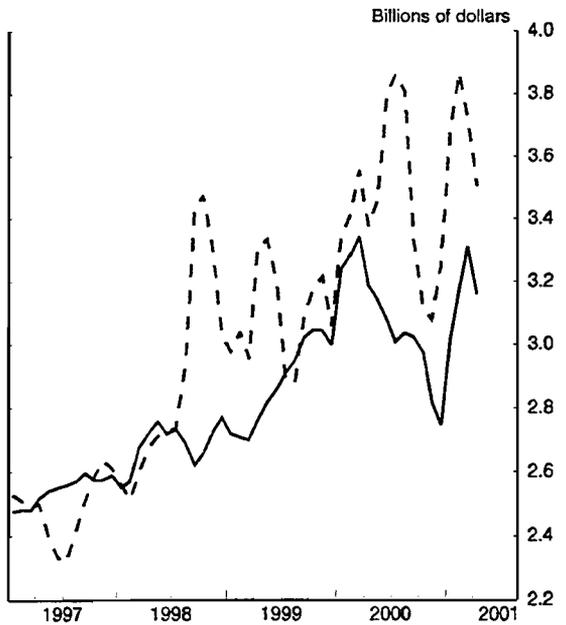
Computers and Related Equipment



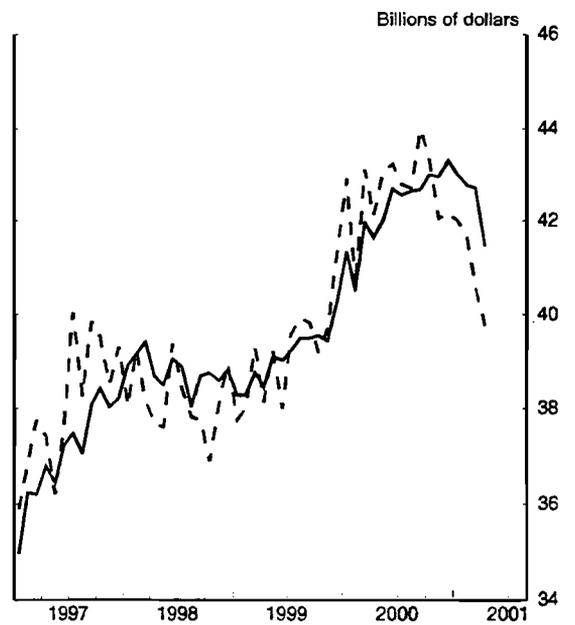
Communications Equipment



Turbines and Power Transmission Equipment



Other Equipment



Note. Excluding aircraft, computers, communications and turbines and power transmission equipment.

widespread, with only the turbines and power transmission equipment category showing any strength. Excluding this grouping, orders fell 2 percent in April. The level of new orders stayed well below the level of shipments in April, and the backlog of unfilled orders fell sharply.

Nonresidential construction. Data through April showed that spending in the nonresidential construction sector remained robust even as vacancy rates have moved up a bit and rents are rising more slowly. Although the deterioration of these fundamentals suggests that building construction may be becoming less profitable, financing conditions have remained generally favorable. Seemingly, investors have determined that, at least for now, the risks of lending for commercial construction have not increased significantly.

Spending on nonresidential building construction ticked down slightly in April after having advanced rapidly in the first quarter. The recent strength has been evident in all the major sectors. In particular, outlays for industrial structures remain high despite falling manufacturing employment and output—supported in part by construction of private electric power plants and facilities for cogeneration of power by industrial companies. Outside of building construction, indicators for drilling and exploration expenditures (primarily for natural gas) have remained strong.

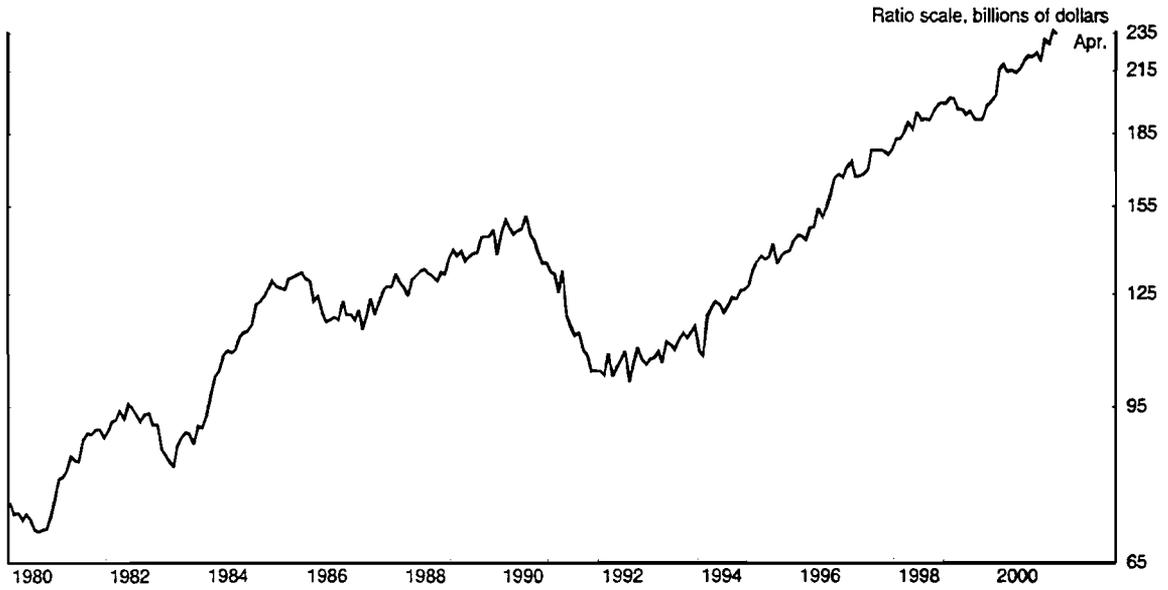
The signs that the profitability of building construction is eroding have surfaced in a number of market segments. In the office sector, the appreciation of property values and rents moderated, and vacancy rates popped up in the first quarter. Increases in retail-property rents have also slowed a bit in recent quarters, and property values changed little over the past year. Year-over-year growth in warehouse-property values was up sharply from last year's negative readings, but this series has been unusually erratic recently, and rent gains for warehouses have continued to drop back. In the industrial sector, the vacancy rate moved up in the first quarter, suggesting that the sharp declines in capacity utilization associated with the slowdown in manufacturing activity have begun to affect this sector.

For the most part, financial markets have taken the recent deterioration of these indicators in stride. The available monthly data suggest that issuance of commercial-mortgage-backed securities (CMBS) will likely increase in the second quarter from an already robust first-quarter pace. Although rates paid by borrowers on CMBS have moved up a bit in recent months, spreads relative to the ten-year swap rate have been about flat, suggesting that investors' views of the risk of lending for commercial construction have not deteriorated. That said, the delinquency rate on CMBS has moved up a bit, on balance, in recent months, although the most recent reading for April was still at a low level.

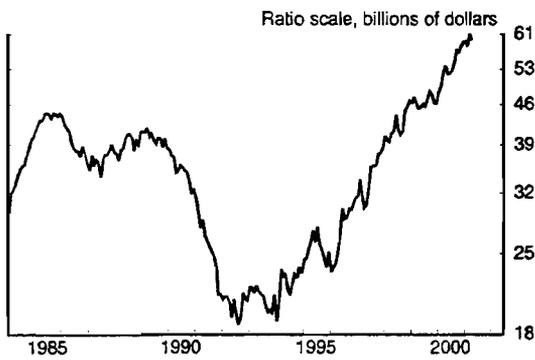
Nonresidential Construction

(Seasonally adjusted, annual rate)

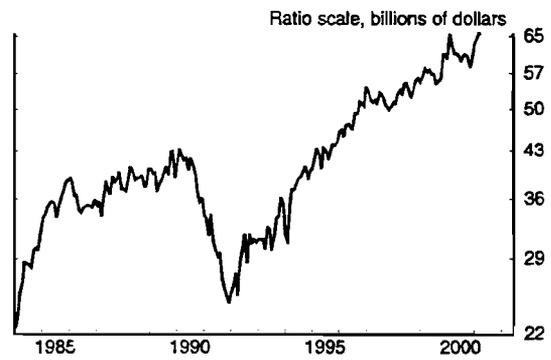
Total Building



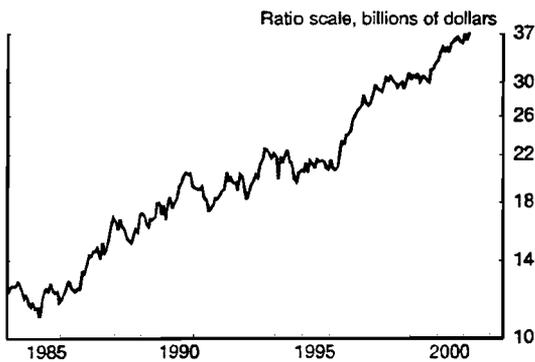
Office



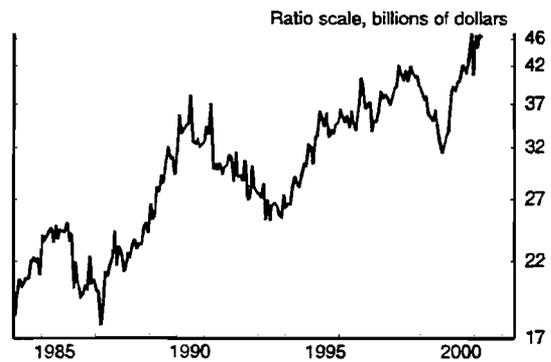
Other Commercial



Institutional

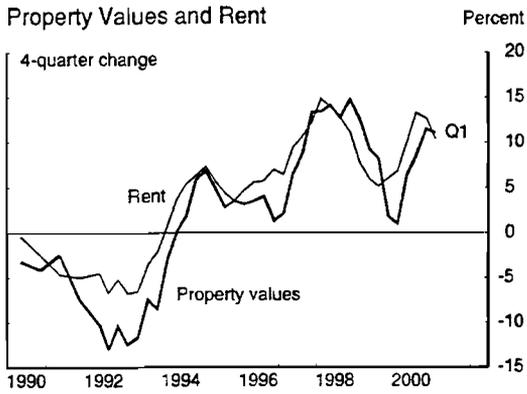


Industrial

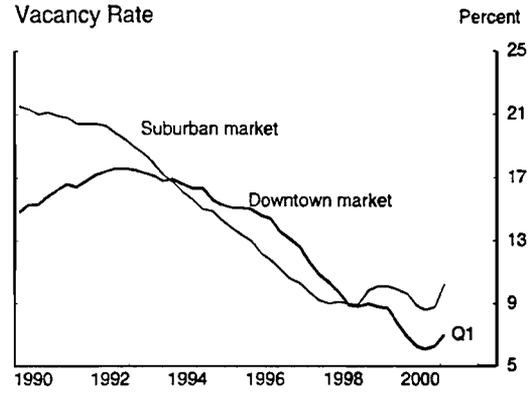


Indicators of Nonresidential Construction

Office Buildings

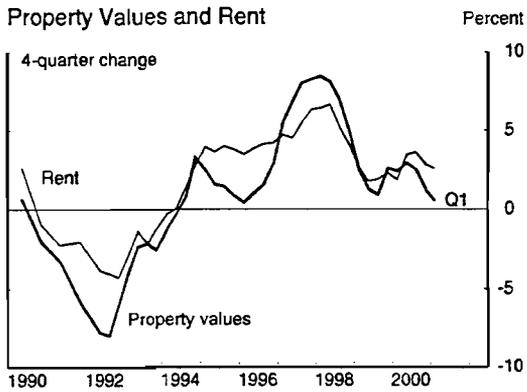


Source. National Real Estate Index.



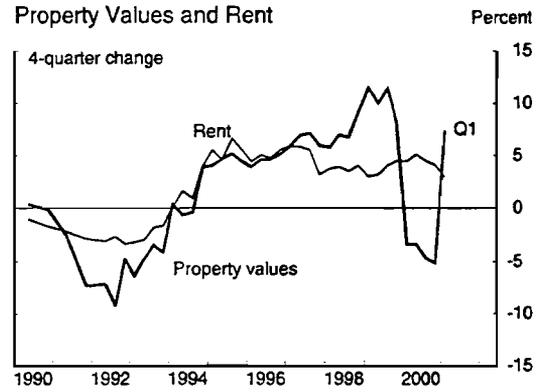
Source. CB Richard Ellis.

Retail Space



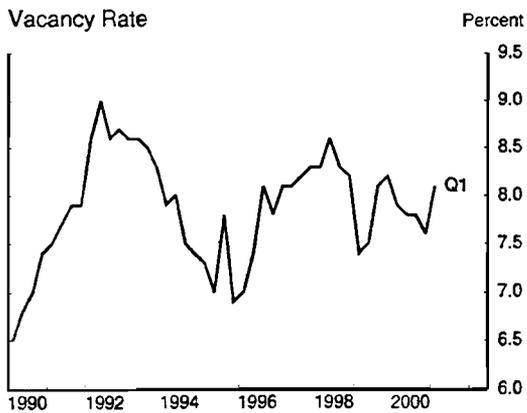
Source. National Real Estate Index.

Warehouses

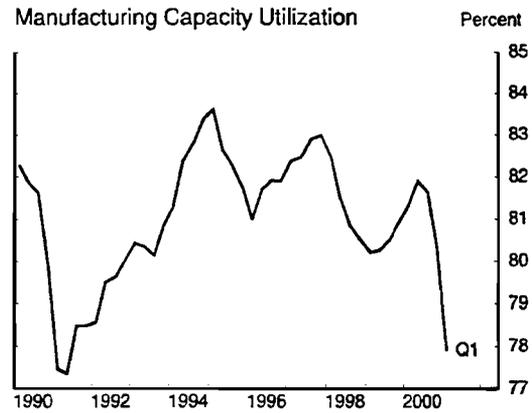


Source. National Real Estate Index.

Industrial

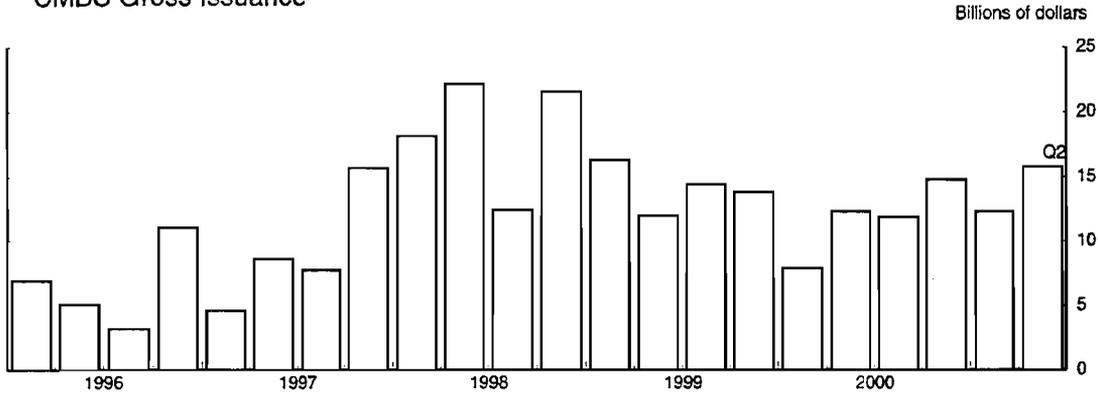


Source. CB Richard Ellis.



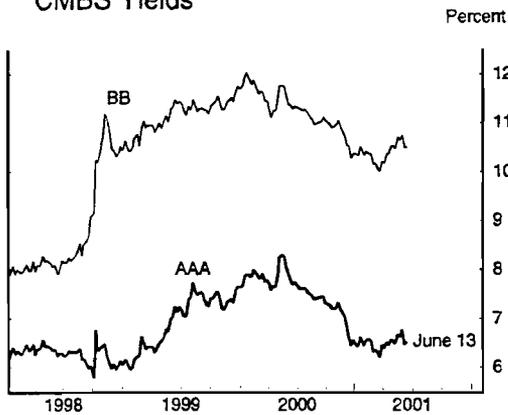
Commercial Mortgage Markets

CMBS Gross Issuance



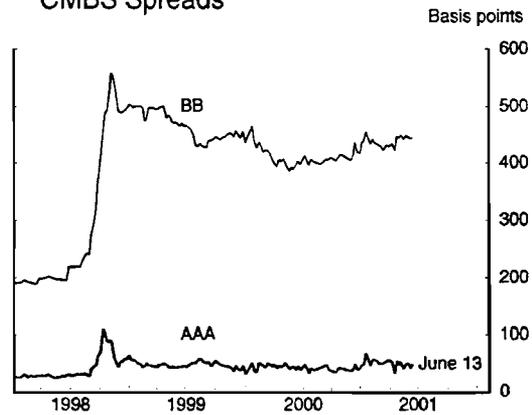
Note. 2001:Q2 data are for period to date. Excludes Fannie Mae and Freddie Mac securities and all CMBS backed by mortgages on foreign properties.
Source. Commercial Mortgage Alert.

CMBS Yields



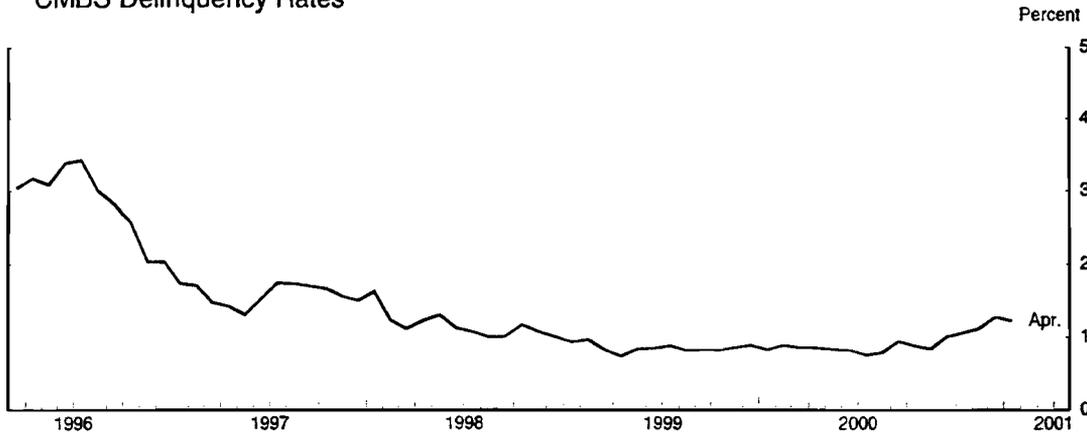
Source. Morgan Stanley.

CMBS Spreads



Note. Rate on CMBS minus 10-year swap rate.
Source. Morgan Stanley.

CMBS Delinquency Rates



Source. Morgan Stanley.

Government Sector

Federal. According to Treasury data, the federal government ran a surplus of \$137 billion over the first eight months of fiscal year 2001 (FY2001)—\$16 billion more than during the same period of FY2000. Although receipts have continued to increase more rapidly than outlays so far this fiscal year, they have, nevertheless, decelerated sharply for the fiscal year-to-date, reflecting the slowdown in economic activity; receipts are up 4-1/2 percent relative to the first eight months of FY2000 compared with a 12 percent advance in the preceding year. The gains in receipts from individual taxes have continued to be robust, owing primarily to a surge in non-withheld receipts collected during the April-May filing season. However, net corporate receipts during April and May dropped significantly from the same period last year, reflecting continued weakness in corporate profits. (Daily Treasury data indicate that corporate payments for the first half of June were again noticeably below last year.)

Revenue Loss from Tax Cut (Billions of dollars, fiscal years)

Revenue loss	2001	2002	2001-11
Rate reductions	-40	-55	-875
10 percent bracket	-38	-33	-421
Other rates	-2	-21	-421
Miscellaneous	0	0	-33
Other reductions	-1	-15	-474
Child credit	-1	-9	-172
Marriage penalty	0	0	-63
Education	0	-2	-29
Estate and gift	0	-0	-138
Pension and IRA	0	-2	-50
Alternative minimum tax	0	-2	-14
Miscellaneous	0	-0	-8
Corporate timing shift	-33	33	0
Total	-74	-38	-1,349

Source. Joint Committee on Taxation

President Bush recently signed the Economic Growth and Tax Relief Reconciliation Act of 2001, which provides fiscal stimulus in the near term; according to estimates from the Joint Committee on Taxation (JCT), the new law will reduce tax collections by \$1.35 trillion over the 2001-2011 period. The act includes reductions in personal income tax rates, expansion of the child credit, marriage penalty relief, education provisions, elimination of the estate

FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis; billions of dollars)

	April-May			FY-to-date ending in May		
	2000	2001	Percent change	2000	2001	Percent change
Outlays	285.3	295.1	3.5	1197.8	1240.9	3.6
Deposit insurance	-0.6	-0.3	...	-2.6	-1.4	...
Spectrum auction	0.0	0.0	...	0.0	-1.0	...
Sale of major assets	0.0	0.0	...	0.0	0.0	...
Other	285.9	295.4	3.3	1200.5	1243.3	3.6
Receipts	441.2	457.0	3.6	1318.5	1378.0	4.5
Surplus	155.9	161.9	...	120.7	137.1	13.6
Outlays excluding deposit insurance, spectrum auction, and sale of major assets are adjusted for payment timing shifts ¹						
Outlays	297.1	307.2	3.4	1200.4	1250.4	4.2
National defense	47.4	50.8	7.0	192.1	201.3	4.8
Net interest	40.7	36.2	-11.2	155.7	146.3	-6.0
Social security	69.1	72.4	4.7	267.7	283.8	6.0
Medicare	34.5	39.2	13.5	130.5	140.8	7.9
Medicaid	19.1	21.9	14.7	76.5	84.7	10.7
Other health	5.9	7.9	34.6	23.7	27.8	17.5
Income security	39.5	44.0	11.4	174.6	186.7	6.9
Agriculture	1.8	2.0	9.5	28.0	22.1	-21.1
Other	39.0	32.9	-15.8	151.6	156.8	3.4
Receipts	441.2	457.0	3.6	1318.5	1378.0	4.5
Individual income and payroll taxes	361.4	386.9	7.0	1071.6	1141.2	6.5
Withheld + FICA	220.1	231.9	5.3	918.7	972.3	5.8
Nonwithheld + SECA	194.2	216.8	11.6	276.0	305.7	10.8
Refunds (-)	53.0	61.8	16.7	123.1	136.8	11.1
Corporate	33.5	28.8	-13.8	113.6	110.3	-3.0
Gross	37.7	33.1	-12.0	134.4	136.0	1.2
Refunds (-)	4.2	4.3	1.9	20.8	25.7	23.9
Other	46.3	41.3	-10.8	133.3	126.6	-5.0
Surplus	144.0	149.8	...	118.1	127.7	8.1

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

1. A shift in payment timing occurs when the first of the month falls on a weekend or holiday, or when the first three days of a month are nonworking days. Outlays for defense, social security, Medicare, income security, and "other" have been adjusted to account for these shifts.

... Not applicable.

tax, pension and IRA provisions, and temporary relief from the alternative minimum tax.¹⁴

The tax rate reductions will lead to substantially lower revenues in fiscal years 2001 and 2002. Tax rates above the 15 percent bracket are reduced by 1/2 percentage point in 2001 and an additional 1/2 percentage point in 2002. In addition, beginning in 2002, the bottom of the 15 percent bracket is replaced by a new 10 percent bracket, applicable to the first \$12,000 of taxable income for joint filers. In 2001, a rebate on 2000 income taxes will be paid in lieu of the new 10 percent bracket; these rebates are estimated to total \$38 billion and will be paid in the third quarter.¹⁵

In order to provide a cushion for additional spending contemplated in the fiscal year 2002 budget resolution, the tax law also shifts \$33 billion in corporate payments from fiscal year 2001 into fiscal year 2002.¹⁶ Including this timing change, the tax cut is expected to reduce revenues by \$74 billion in fiscal year 2001 and \$38 billion in fiscal year 2002.

State and local governments. Data in hand point to continued solid growth in real spending by state and local governments. Real construction spending jumped another 1 percent in April, the sixth consecutive monthly increase. In addition, employment was up on average 25,000 per month in April and May. While this is below the rapid advance in the first quarter, hiring remains quite strong by historical standards.

Legislatures in forty-seven states have been working on their annual or biennial general fund budgets this spring, and most will likely have them finalized by the end of their fiscal years.¹⁷ Growth in state tax collections, measured by the Rockefeller Institute relative to the same quarter a year earlier, averaged 4.5 percent in the fourth quarter of 2000 and the first quarter of 2001.¹⁸ These rates are the lowest for two consecutive quarters since 1992. Partly as a result, a number of states have had to wrestle with downward revisions to their revenue forecasts. For some states, such as Oregon, Colorado, Pennsylvania, and Maryland, weaker projected revenues have meant a smaller expected surplus for

14. The tax law is examined in detail in a memo to the FOMC by Glenn Follette dated June 1, 2001.

15. The rebate will be calculated based on the tax savings that the 10 percent bracket would have provided had it been in place during 2000; thus, single filers will receive up to \$300, heads of household up to \$500, and joint filers up to \$600.

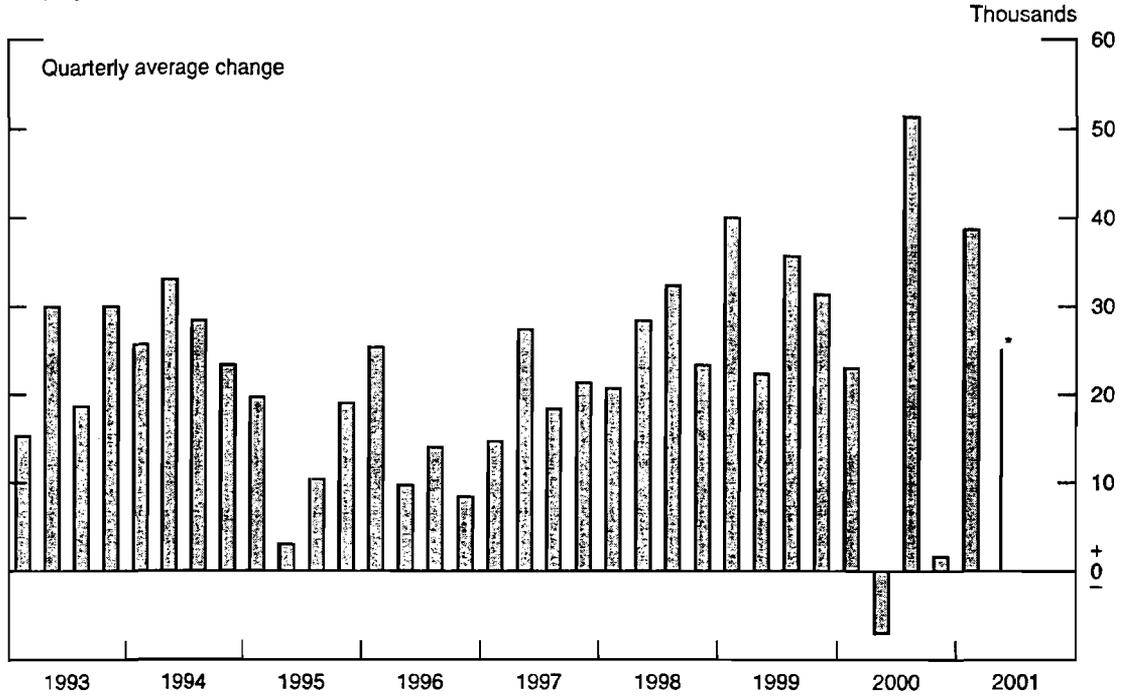
16. The \$33 billion figure is a JCT estimate. Given the weakness in corporate receipts, however, we estimate that the figure will turn out to be closer to \$28 billion.

17. All but four states end their fiscal year on June 30. Twenty-one are on a two-year budget cycle, with most writing their budgets in odd-numbered years.

18. The NIPAs do not show separate data on tax receipts between collections from states and collections from local governments.

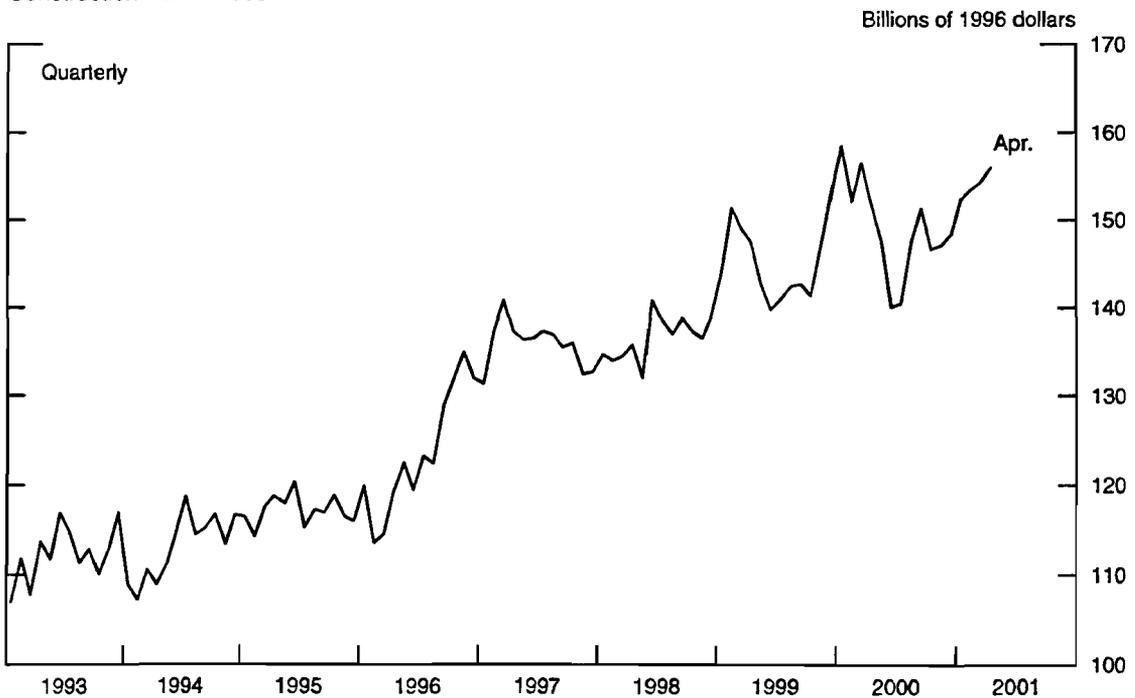
State and Local Employment and Construction

Employment



* Average of employment data for April and May 2001.

Construction Put in Place



next year; however, to avoid projecting deficits, other states have had to use a variety of strategies including funds transfers, reductions in planned spending, and some increases in fees.

Prices and Labor Costs

Core consumer price inflation seems to have cooled somewhat in recent months after coming in on the high side earlier in the year. The core CPI edged up 0.1 percentage point in May and is up 2.5 percent over the past twelve months, an acceleration of only 0.1 percentage point from the preceding year. The overall consumer price index rose 0.4 percent in May, boosted by a further surge in energy prices, and has risen 3.6 percent over the past twelve months. However, energy prices may now have peaked.

After moderating a bit toward the end of the first quarter, retail energy prices rose substantially in April and May, with the largest increases among motor fuels. In the first half of April, inventories of gasoline were about 5 percent below the normal range for the season, and several domestic refineries were not operating because of either maintenance or breakdowns. However, since then, stocks have been replenished by resumed refinery production and a surge in imports. Stocks of the gasoline additive MTBE have been rebuilt as well, easing concerns that supply might not be sufficient for refiners to produce enough summer-blend reformulated gasoline.¹⁹ With inventories having recovered impressively, both wholesale and retail gasoline prices have retreated in recent weeks. Futures quotes point to further declines in spot gasoline prices in coming months, as the risk of supply disruptions during the driving season diminishes.

A similar, rapid replenishment of inventories has helped pull down natural gas prices. On April 1, inventories of natural gas were 35 percent below normal, but since then, gas has been injected into storage caverns at the fastest rate seen in the twenty-five years that the Department of Energy has kept records. By late May, the American Gas Association and the Department of Energy estimated that inventories had recovered to the normal level for the season. Weather has been somewhat milder than usual over the past two months, but the bulk of the increase in inventories results from the production and consumption response to higher gas prices over the past year. Industrial gas usage is down about 3 percent from last year, and electricity producers have cut consumption of gas by about the same percentage. At the same time, the higher natural gas prices have encouraged more exploration, and gas output so far this year is running about 2 percent above year-earlier levels. The sharp rebuilding of gas

19. Near the start of the summer, however, stocks of another additive—ethanol—appeared quite low, pointing to risks for Midwestern areas that use ethanol to produce their reformulated gasoline.

RECENT PRICE INDICATORS
(Percent)

	From 12 months earlier		2000	2001	2001	
	May 2000	May 2001 ¹	Q4	Q1	Apr.	May ¹
					-Annual rate-	-Monthly rate-
<u>CPI</u>						
Total	3.2	3.6	2.9	4.2	0.3	0.4
Core	2.4	2.5	2.4	3.2	0.2	0.1
ex tobacco	2.3	2.5	2.4	3.1	0.1	0.1
Core commodities	0.7	0.1	1.1	1.1	0.0	-0.4
ex tobacco	-0.0	-0.2	1.1	0.8	-0.3	-0.4
Core services	3.6	3.8	3.4	4.0	0.4	0.4
Current-methods	3.2	3.6	2.9	4.2	0.3	0.4
Core	2.4	2.5	2.3	3.1	0.2	0.1
ex tobacco	2.2	2.4	2.4	3.1	0.1	0.1
<u>PCE Prices</u>						
Total	2.3	2.4	1.9	3.2	0.3	0.2
Core	1.7	1.7	1.6	2.6	0.2	0.0
ex tobacco	1.5	1.6	1.6	2.6	0.1	0.0
Core commodities	-0.2	-0.7	0.3	0.3	-0.1	-0.4
ex tobacco	-0.9	-1.0	0.3	0.0	-0.3	-0.3
Core services	2.5	2.7	2.1	3.6	0.3	0.2
Core market prices	1.6	1.7	1.7	2.2	0.2	0.0
Core nonmarket prices	1.9	1.4	1.1	4.4	0.3	0.0
<u>PPI</u>						
Total finished goods	3.7	3.8	4.1	5.5	0.3	0.1
Core	1.4	1.6	1.3	1.6	0.2	0.2
ex tobacco	1.1	0.9	1.1	0.4	0.2	-0.1
Core consumer goods	1.8	2.1	1.7	2.3	0.2	0.4
ex tobacco	1.2	1.0	1.4	0.3	0.2	0.0
Capital equipment	0.7	0.8	0.7	0.6	0.3	-0.1
Core intermediate materials	3.2	0.6	-0.4	1.0	-0.1	0.1
Core crude materials	13.2	-12.0	-7.6	-9.0	-2.6	-0.2

1. PCE Prices for May are staff estimates.

inventories has led to a drop in spot and near-futures prices of natural gas since April.²⁰ At this point, markets are showing little concern about a shortfall this coming winter.

Electricity markets remain fairly calm outside of California, and nationwide generating capacity has risen 4-1/2 percent over the past twelve months. However, California still faces the prospect of blackouts and wholesale price increases on the hottest days of this summer. Nonetheless, upward pressures on electricity prices there have eased markedly in the past month or so. Since April, California's seasonally adjusted retail demand for electricity has fallen in response to higher prices, and natural gas input costs to electricity generators have also eased. As a result, the disparity between retail prices and input costs has narrowed substantially, reducing (but by no means eliminating) the prospect of further residential rate increases.

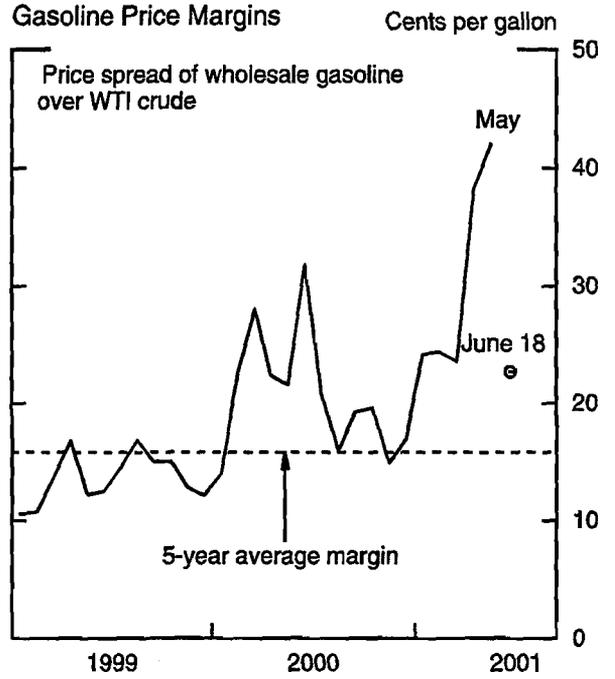
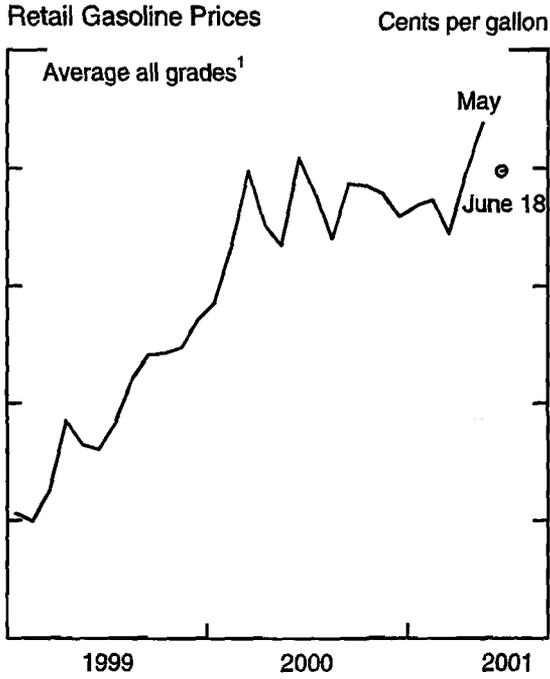
Consumer food prices rose 0.3 percent in May and have increased 3.1 percent over the past twelve months, an acceleration of about 1 percentage point from the previous year. The erratic index for fruits and vegetables declined last month, and the index for meats, poultry, fish, and eggs, which had increased more than 0.7 percent on average each month in 2001, rose just 0.1 percent in May. But prices for other foods were up 0.5 percent, largely reflecting increases for dairy products and fats and oils.

The small increase in the CPI excluding food and energy items in May left the three-month change for these items at 2.2 percent at an annual rate, well below the spike that occurred early this year. The CPI for core commodities fell 0.4 percent in May, with motor vehicle prices edging down further and with price declines for apparel and other goods likely reflecting weak demand. Over the past twelve months, core goods prices have risen 0.1 percent—a deceleration of about 1/2 percentage point from the previous twelve-month period. In contrast, prices for non-energy services have accelerated notably over the past year, and the index for these items rose another 0.3 percent in May. Over the twelve months ended in May, prices for non-energy services have increased 3.6 percent, about 1/2 percentage point more than in the previous twelve-month period. Prices for shelter rents rose 0.4 percent in May, and these prices have increased 3.7 percent over the past twelve months, a pickup of 0.6 percentage point relative to the preceding year. Prices for medical services have accelerated a similar amount over the past year.

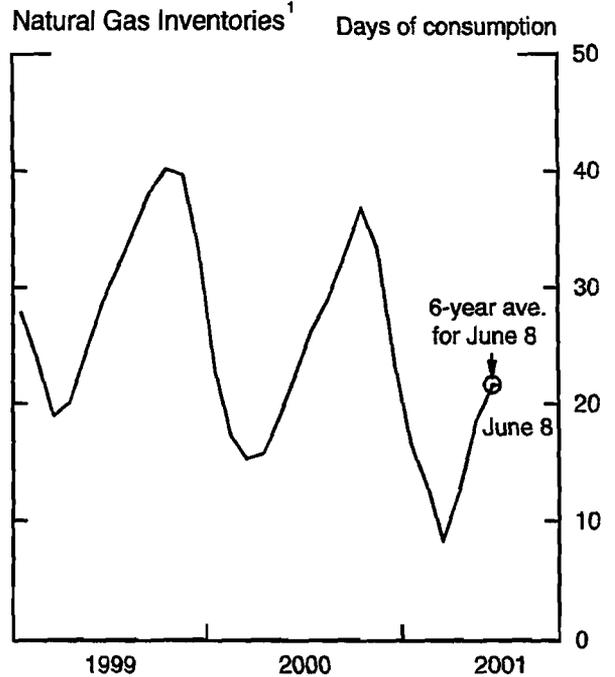
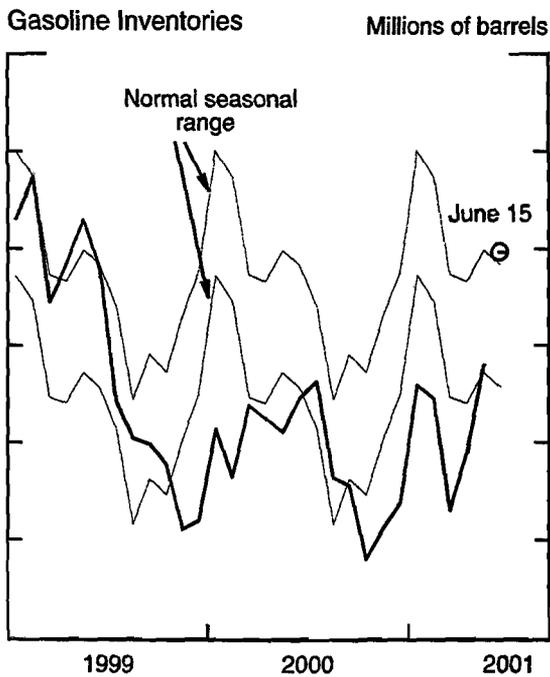
As with the CPI, core PCE prices picked up in the first quarter but posted a more moderate reading in April. The information in the May CPI points to a

20. California spot prices of natural gas remain quite high relative to the rest of the country, but even these prices have come down sharply in recent weeks.

Gasoline and Natural Gas Developments



1. Prices adjusted using CPI seasonal factors

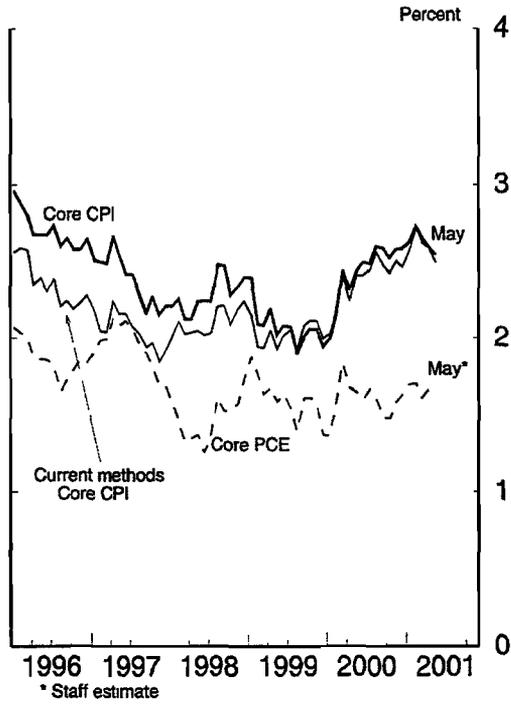


1. Working gas in storage divided by U.S. D.O.E. projection of 2000/2001 average daily winter consumption

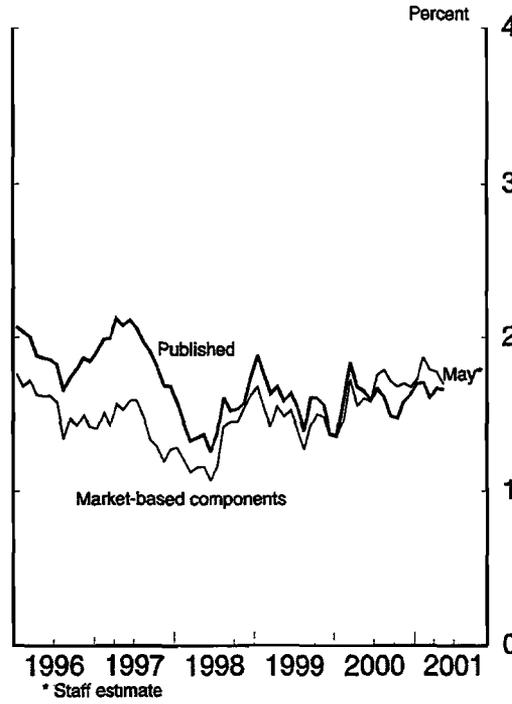
Source. U.S. Department of Energy.

Measures of Core Consumer Price Inflation (12-month change except as noted)

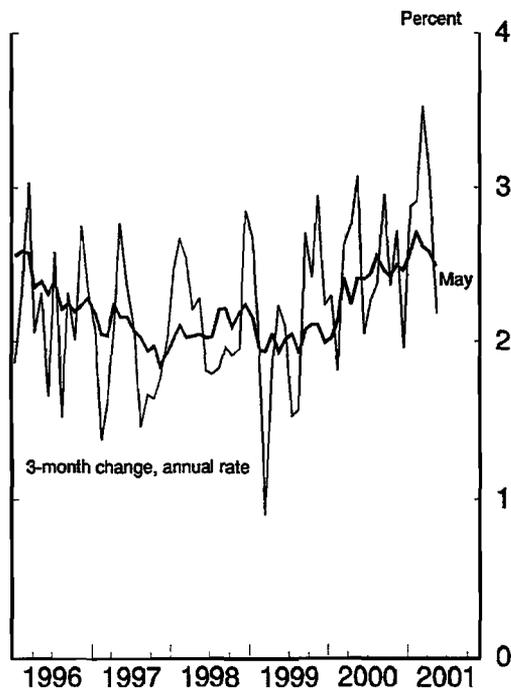
CPI and PCE Excluding Food and Energy



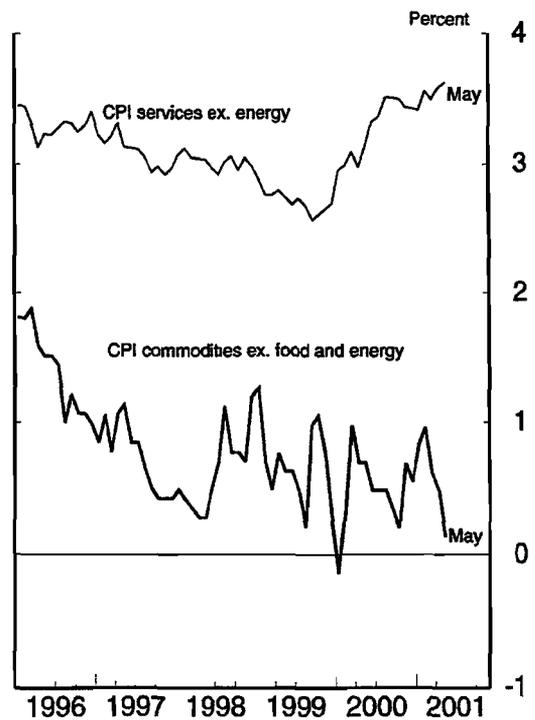
PCE Excluding Food and Energy



CPI Excluding Food and Energy
(Current Methods)



CPI Services and Commodities



SPOT PRICES OF SELECTED COMMODITIES

	Current price (dollars)	-----Percent change ¹ -----				Memo: Year earlier to date
		1999	2000	Dec. 26 to May 08 ²	May 08 ² to June 19	
Metals						
Copper (lb.)	0.770	26.1	3.4	-9.9	-6.1	-11.5
Steel scrap (ton)	78.667	61.5	-32.7	-2.5	2.2	-19.5
Aluminum, London (lb.)	0.665	27.7	-0.8	1.7	-7.5	-4.4
Precious metals						
Gold (oz.)	273.400	-1.6	-5.7	-3.3	3.1	-4.5
Silver (oz.)	4.440	5.5	-10.9	-7.3	2.5	-12.0
Forest products³						
Lumber (m. bdft.)	310.000	8.3	-44.6	64.4	4.7	17.0
Plywood (m. sqft.)	345.000	-3.2	-8.2	17.9	4.5	15.0
Petroleum						
Crude oil (barrel)	26.490	163.3	-13.0	25.2	-4.8	-7.2
Gasoline (gal.)	0.751	132.9	5.2	31.2	-22.0	-20.2
Fuel oil (gal.)	0.770	140.7	34.4	-21.5	3.4	1.3
Livestock						
Steers (cwt.)	72.790	15.7	13.2	-1.9	-3.6	3.6
Hogs (cwt.)	53.250	194.0	7.1	36.4	3.4	4.4
Broilers (lb.)	0.595	-4.0	-13.7	12.6	6.2	4.2
U.S. farm crops						
Corn (bu.)	1.760	-10.2	10.1	-12.8	-2.8	-1.4
Wheat (bu.)	3.278	-17.4	31.9	-2.5	-3.5	11.6
Soybeans (bu.)	4.635	-17.6	10.8	-11.0	5.9	-4.1
Cotton (lb.)	0.361	-20.9	27.0	-30.5	-11.5	-34.8
Other foodstuffs						
Coffee (lb.)	0.558	5.1	-43.1	21.3	-32.4	-36.8
Memo:						
JOC Industrials	82.300	11.0	-1.5	-2.4	-2.8	-7.7
JOC Metals	76.400	26.3	-10.3	-5.2	-3.4	-12.5
CRB Futures	208.470	7.8	12.1	-6.2	-2.9	-7.1
CRB Spot	244.550	-0.1	-3.5	-5.1	0.4	-6.0

1. Changes, if not specified, are from the last week of the preceding year to the last week of the period indicated.

2. Week of the May Greenbook.

3. Reflects prices on the Friday before the date indicated.

flat May reading for core PCE prices and suggests that the twelve-month change will remain around 1-3/4 percent.

Prices for capital goods as measured by the producer price index edged down in May, leaving the twelve-month change at 0.8 percent, about the same as a year ago. Prices for computers plummeted in the first quarter as demand dried up in the high-tech sector, but prices look to have firmed a little in the last couple of months. In all, computer prices have declined 17.2 percent over the twelve months to May, about the same as the decline over the previous year.

At earlier stages of processing, the producer price index for core intermediate materials rose 0.6 percent in the twelve months ended in May, a marked slowdown from the 3.2 percent jump over the previous twelve months. And the PPI for core crude materials edged down further in May after having dropped sharply earlier in the year. Indexes of industrial materials prices (such as the Commodity Research Bureau and *Journal of Commerce* commodity price indexes) also generally have moved down since the last Greenbook. One exception is the price of lumber, which has risen substantially, on net, since the start of April. Lumber distributors reportedly had run off their stocks earlier in the year in anticipation of a possible softening in housing demand and apparently had to do some quick restocking during the spring as housing starts held firm. Prices also have been influenced by renewed sparring between Canada and the United States regarding imports of softwood lumber into this country.²¹

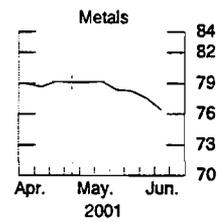
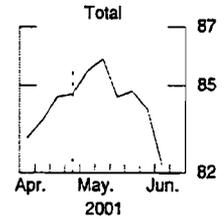
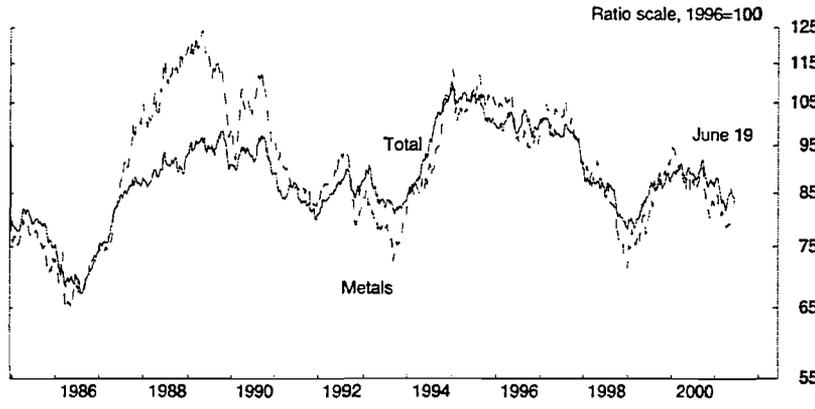
Inflation expectations from the Michigan survey have been little changed on balance. The median expectation for inflation over the coming year moved back down to 3 percent in June after having ticked up earlier in the quarter; the latest reading is near the middle of the range seen over the past couple of years for this expectation. Over a five- to ten-year horizon, median expected inflation also was 3 percent and has remained little changed over the past year and a half.

We have received few new data regarding labor costs. Average hourly earnings of production or nonsupervisory workers on private nonfarm payrolls rose 0.3 percent in May following a similar increase in April. Over the twelve months ended in May, average hourly earnings rose 4.3 percent, 0.5 percentage point faster than over the previous twelve months. Compensation per hour in the nonfarm business sector, a broader measure of compensation than average

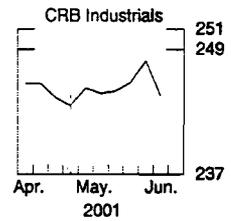
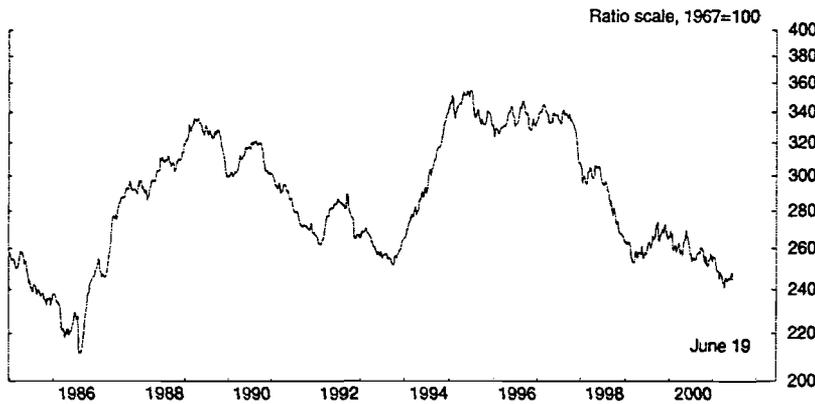
21. A five-year agreement that had limited lumber imports from Canada expired on March 31, but an investigation that is in progress at the International Trade Commission could lead to new restrictions. Meanwhile, Canadian producers are said to be holding down exports voluntarily, partly to avoid provoking an unfavorable ITC ruling later this year.

Commodity Price Measures

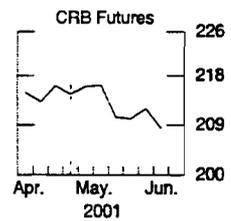
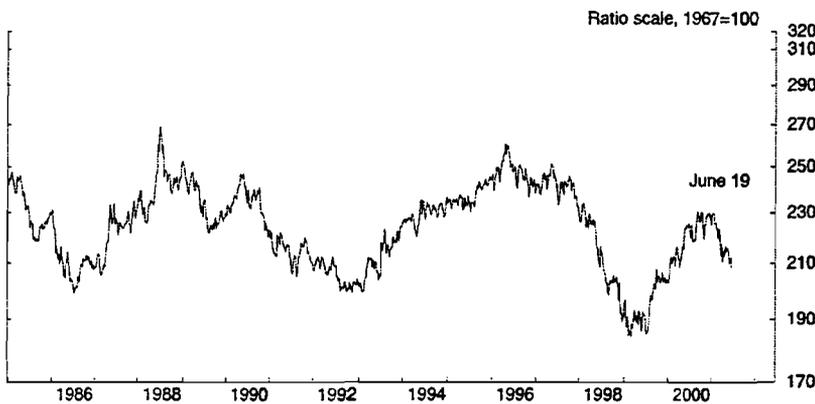
Journal of Commerce Index



CRB Spot Industrials



CRB Futures



Note. Weekly data, Tuesdays. Vertical lines on small panels indicate week of last Greenbook. The Journal of Commerce index is based almost entirely on industrial commodities, with a small weight given to energy commodities, and the CRB spot price 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. Copyright for Journal of Commerce data is held by CIBCR, 1994.

BROAD MEASURES OF INFLATION
(4-quarter percent change)

	1998 Q1	1999 Q1	2000 Q1	2001 Q1
<u>Product prices</u>				
GDP chain price index	1.4	1.5	1.8	2.3
Less food and energy	1.4	1.5	1.8	1.9
Nonfarm business chain price index ¹	1.2	1.2	1.5	1.9
<u>Expenditure prices</u>				
Gross domestic purchases chain price index	0.8	1.2	2.3	2.2
Less food and energy	1.2	1.4	1.7	1.8
PCE chain price index	1.0	1.5	2.5	2.2
Less food and energy	1.5	1.8	1.6	1.7
PCE chain price index, market-based components	0.8	1.2	2.5	2.4
Less food and energy	1.2	1.5	1.5	1.8
CPI	1.5	1.7	3.3	3.4
Less food and energy	2.3	2.2	2.2	2.7
Current-methods CPI	1.3	1.5	3.3	3.4
Less food and energy	2.1	2.0	2.2	2.7
Median CPI	2.9	2.9	2.4	3.3
Trimmed mean CPI	2.0	1.8	2.3	3.0

1. Excluding housing.

SURVEYS OF (CPI) INFLATION EXPECTATIONS
(Percent)

	Actual inflation ¹	University of Michigan				Professional forecasters (10-year) ⁴
		1 year		5 to 10 years		
		Mean ²	Median ²	Mean ³	Median ³	
1999-Q2	2.1	3.1	2.7	3.3	2.8	2.5
Q3	2.3	3.1	2.7	3.4	2.9	2.5
Q4	2.6	3.5	2.9	3.3	2.9	2.5
2000-Q1	3.2	3.6	3.0	3.5	3.0	2.5
Q2	3.3	3.5	3.0	3.3	2.8	2.5
Q3	3.5	3.6	2.9	3.4	2.9	2.5
Q4	3.4	3.8	3.0	3.7	3.0	2.5
2001-Q1	3.4	3.4	2.9	3.6	3.0	2.5
2001-Jan.	3.7	3.8	3.0	3.5	2.9	
Feb.	3.5	3.2	2.8	3.6	3.0	
Mar.	2.9	3.3	2.8	3.6	3.0	2.5
Apr.	3.3	3.7	3.1	3.6	3.1	
May	3.6	3.9	3.2	3.6	3.0	
June		4.1	3.0	3.6	3.0	

1. CPI; 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 the 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 the average, during the next 5 to 10 years?
4. Compiled by the Federal Reserve Bank of Philadelphia.

LABOR COSTS
(Percent change; annual rate; based on seasonally adjusted data)

	1999 ¹	2000 ¹	2000			2001	2000:Q1 to 2001:Q1
			Q2	Q3	Q4	Q1	
<u>Compensation per hour</u>							
Total business	4.5	6.0	7.1	5.7	7.5	5.2	6.3
Nonfarm business	4.4	5.7	6.0	6.2	6.6	5.1	6.0
Nonfinancial corporations ²	4.4	5.6	6.3	6.0	7.4	5.9	6.4
<u>Unit labor costs</u>							
Total business	.6	2.4	.0	3.1	4.5	6.7	3.5
Nonfarm business	.6	2.3	-.2	3.2	4.5	6.3	3.4
Nonfinancial corporations ²	.4	2.2	.7	1.5	7.1	6.0	3.8

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.

2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, finance and insurance companies; the sector accounts for about two-thirds of business employment.

AVERAGE HOURLY EARNINGS
(Percent change; based on seasonally adjusted data)

	12-month percent change			Percent change to May, 2001 from month indicated		2001	
	May 1999	May 2000	May 2001	Nov. 2000	Feb. 2001	Apr.	May
	- - - - -Annual rate-			- - - - -		-Monthly rate-	
Total private nonfarm	3.5	3.7	4.3	4.2	4.3	.4	.3
Manufacturing	2.7	3.1	3.5	2.9	4.2	.5	.3
Construction	3.8	3.7	2.8	1.0	-1.1	-.9	.5
Transportation and public utilities	2.6	3.6	3.3	3.9	2.4	.5	-.2
Finance, insurance, and real estate	4.4	2.8	4.7	5.6	3.9	.2	.4
Retail trade	3.9	4.1	4.1	4.0	4.6	.2	.6
Wholesale trade	3.6	3.8	4.6	4.5	4.7	.5	.1
Services	4.1	3.8	4.9	4.9	4.5	.6	.1

hourly earnings, rose 6.0 percent over the four quarters ended 2001:Q1, an acceleration of 1.5 percentage points from the previous four quarters.

Domestic Financial Developments

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

Instrument	2000		2001			Change to June 19 from selected dates (percentage points)		
	June 26	Mar. 19	May 14	June 19	2000 June 26	2001 Mar. 19	2001 May 14	
	<i>Short-term</i>							
FOMC intended federal funds rate	6.50	5.50	4.50	4.00	-2.50	-1.50	-.50	
<i>Treasury bills</i> ¹								
3-month	5.66	4.42	3.63	3.42	-2.24	-1.00	-.21	
6-month	5.94	4.25	3.64	3.38	-2.56	-.87	-.26	
1-year	5.82	4.07	3.62	3.27	-2.55	-.80	-.35	
<i>Commercial paper</i>								
1-month	6.56	4.85	4.02	3.75	-2.81	-1.10	-.27	
3-month	6.56	4.71	3.94	3.61	-2.95	-1.10	-.33	
<i>Large negotiable CDs</i> ¹								
1-month	6.64	4.93	4.10	3.78	-2.86	-1.15	-.32	
3-month	6.73	4.79	4.05	3.65	-3.08	-1.14	-.40	
6-month	6.89	4.64	4.06	3.65	-3.24	-.99	-.41	
<i>Eurodollar deposits</i> ²								
1-month	6.63	4.90	4.06	3.76	-2.87	-1.14	-.30	
3-month	6.69	4.79	4.06	3.64	-3.05	-1.15	-.42	
Bank prime rate	9.50	8.50	7.50	7.00	-2.50	-1.50	-.50	
<i>Intermediate- and long-term</i>								
<i>U.S. Treasury (constant maturity)</i>								
2-year	6.50	4.32	4.29	3.99	-2.51	-.33	-.30	
10-year	6.11	4.82	5.46	5.26	-.85	.44	-.20	
30-year	5.99	5.30	5.85	5.69	-.30	.39	-.16	
U.S. Treasury 10-year indexed note	4.08	3.29	3.23	3.25	-.83	-.04	.02	
Municipal revenue (Bond Buyer) ³	5.99	5.40	5.56	5.54	-.45	.14	-.02	
<i>Private instruments</i>								
10-year swap	7.38	5.76	6.24	6.14	-1.24	.38	-.10	
10-year FNMA	7.15	5.67	6.14	6.00	-1.15	.33	-.14	
Merrill Lynch BBB	8.49	7.31	7.43	7.14	-1.35	-.17	-.29	
High yield ⁴	11.97	12.03	12.03	12.89	.92	.86	.86	
<i>Home mortgages (FHLMC survey rate)</i> ⁵								
30-year fixed	8.14	6.96	7.10	7.14	-1.00	.18	.04	
1-year adjustable	7.22	6.32	5.90	5.82	-1.40	-.50	-.08	

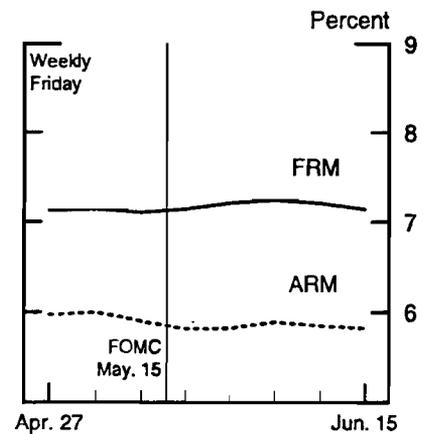
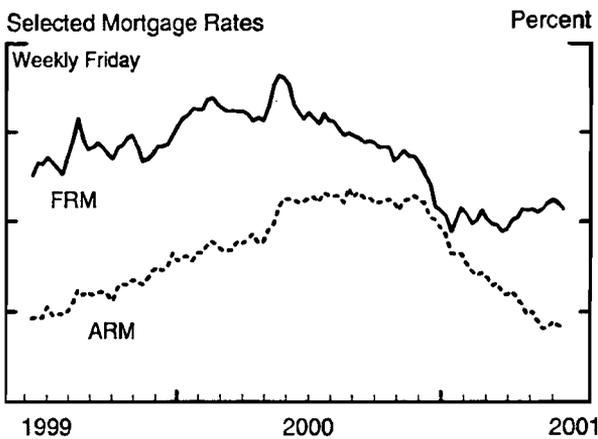
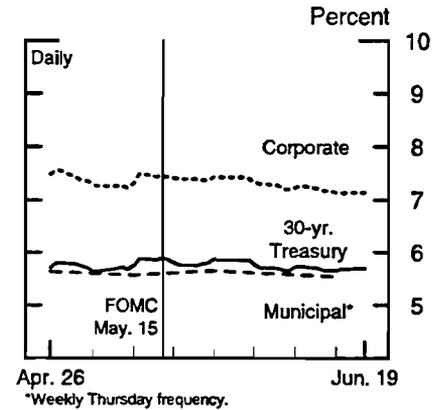
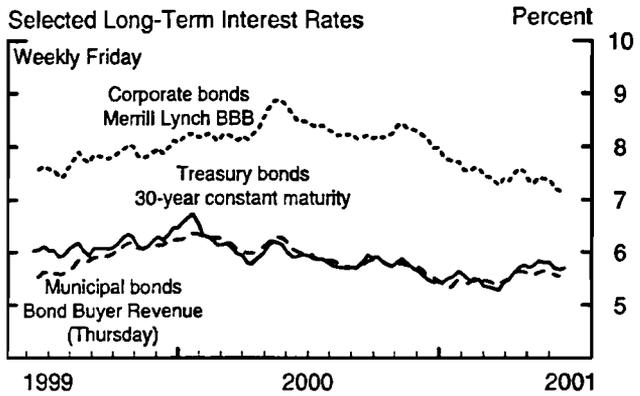
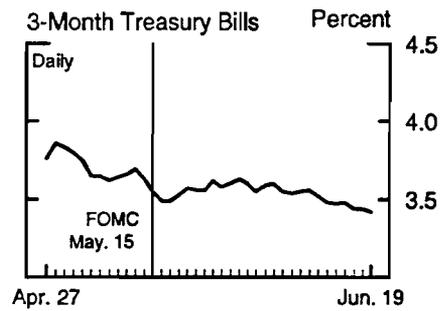
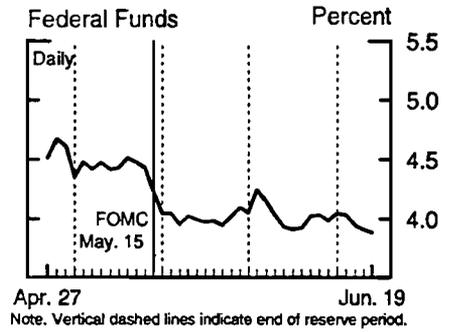
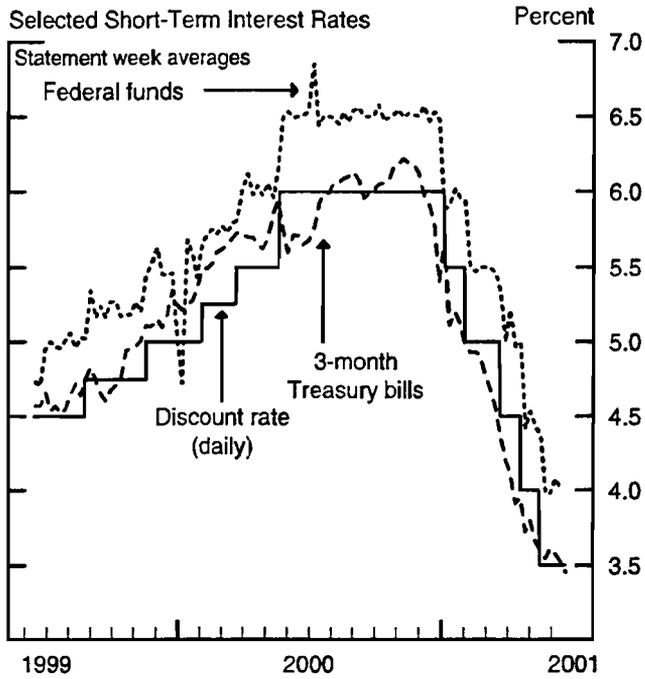
Stock exchange index	Record high		2001			Change to June 19 from selected dates (percent)		
	Level	Date	Mar. 19	May 14	June 19	Record high	2001 Mar. 19	2001 May 14
	Dow-Jones Industrial	11,723	1-14-00	9,959	10,877	10,597	-9.61	6.40	-2.58
S&P 500 Composite	1,527	3-24-00	1,171	1,249	1,213	-20.61	3.57	-2.91
Nasdaq (OTC)	5,049	3-10-00	1,951	2,082	1,993	-60.53	2.13	-4.29
Russell 2000	606	3-9-00	451	487	489	-19.37	8.30	.43
Wilshire 5000	14,752	3-24-00	10,754	11,506	11,195	-24.11	4.10	-2.70

1. Secondary market.
2. Bid rates for Eurodollar deposits collected around 9:30 a.m. Eastern time.
3. Most recent Thursday quote.
4. Merrill Lynch 175 high-yield bond index composite.
5. For week ending Friday previous to date shown.

NOTES:

June 26, 2000, is the day before the FOMC meeting that ended the most recent period of policy tightening.
March 19, 2001, is the day before the March FOMC meeting.
May 14, 2001 is the day before the most recent FOMC meeting.

Selected Interest Rates



Domestic Financial Developments

Overview

Although investors had largely anticipated the 1/2 point easing at the May meeting of the FOMC, some had not ruled out the possibility of a smaller move, and many were wondering whether the Committee would signal that the current easing cycle was drawing to a close. Instead, the Committee's references to restrained inflation pressure and capital spending weakness reinforced investors' perception that they could expect more policy easing in the months ahead. Since that time, weaker-than-expected economic data have strengthened this perception. Current readings from futures markets suggest that investors have fully priced in a 25 basis point easing, and place better-than-even odds on a 50 basis point easing, at next week's meeting. Looking farther out, investors appear to expect the federal funds rate to fall to 3.5 percent or below later this year.

Nominal Treasury coupon yields fell 16 to 30 basis points over the intermeeting period, while real yields (as measured by Treasury indexed debt) were about unchanged, implying that inflation compensation reversed some of its recent rise. Longer-term investment-grade private yields fell about in line with Treasuries. In contrast, worries about near-term earnings, coupled with mounting debt downgrades and defaults, have pushed junk bond yields up more than 80 basis points in recent weeks.

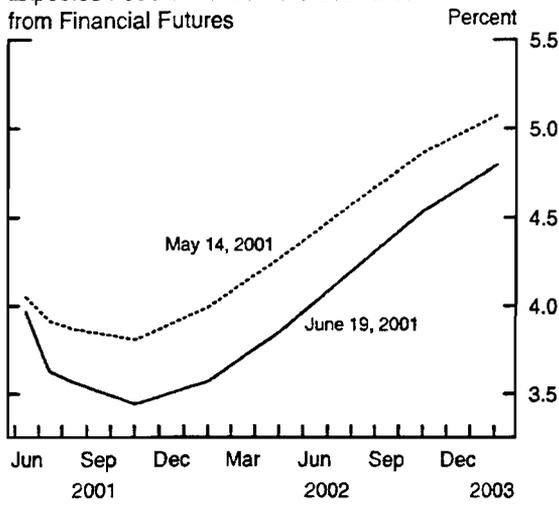
Over the intermeeting period, analysts again revised down their expectations for second-quarter corporate earnings growth. They also trimmed their forecasts for third-quarter earnings growth; nonetheless, their predictions continue to imply a sharp acceleration in corporate profits from the second to third quarters. Although the equity market held up well through most of the intermeeting period, recent earnings warnings have pushed prices down, hitting technology stocks particularly hard. On balance, equity prices have fallen between 2-1/2 percent and 4 percent since the last FOMC meeting.

Corporations took advantage of falling interest rates by issuing a record volume of bonds in May and early June and used some of the proceeds to pay off bank loans and commercial paper obligations. Ratings downgrades and business failures continued to mount in May and June, although private-sector forecasters do not expect bond defaults to rise further from their current elevated levels.

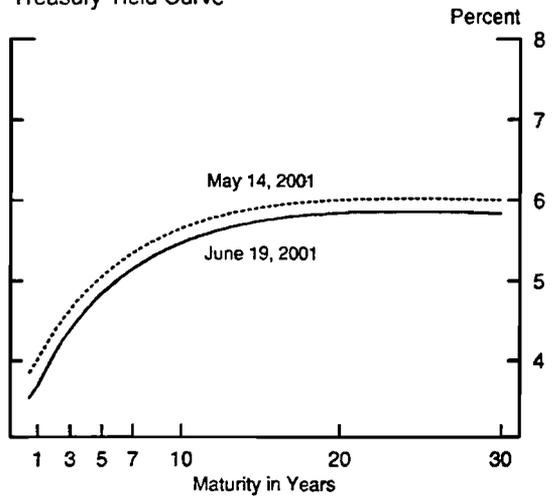
Although consumer interest rates fell and debt growth likely slowed from the first to the second quarter, it appears that the household debt-service burden will rise again, exceeding its previous high reached in the mid-1980s. Households continued to file for bankruptcy in near-record numbers, and credit card delinquency rates continued to rise, although other measures of household credit quality have not shown an appreciable deterioration.

Policy Expectations, Interest Rates, and Stock Prices

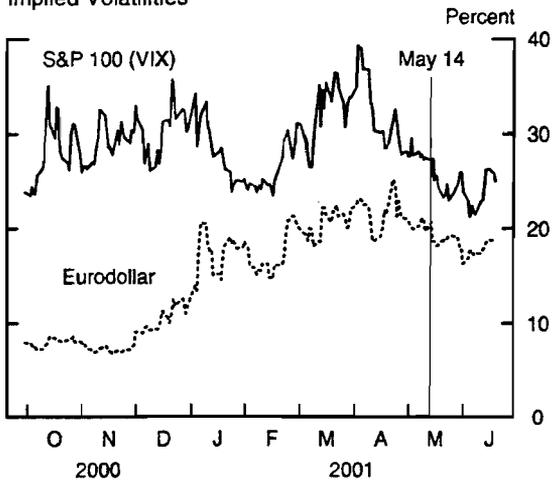
Expected Federal Funds Rate Estimated from Financial Futures



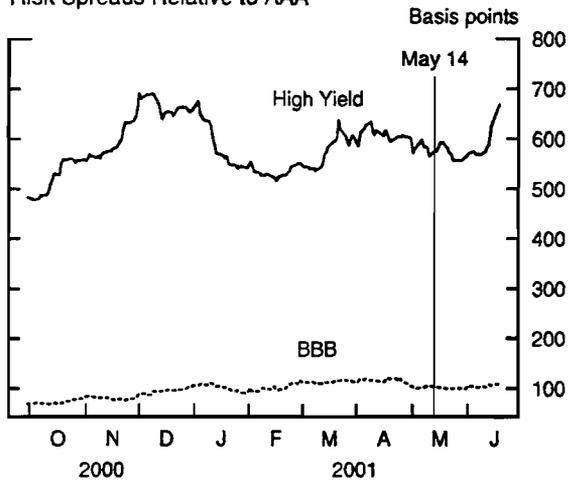
Treasury Yield Curve



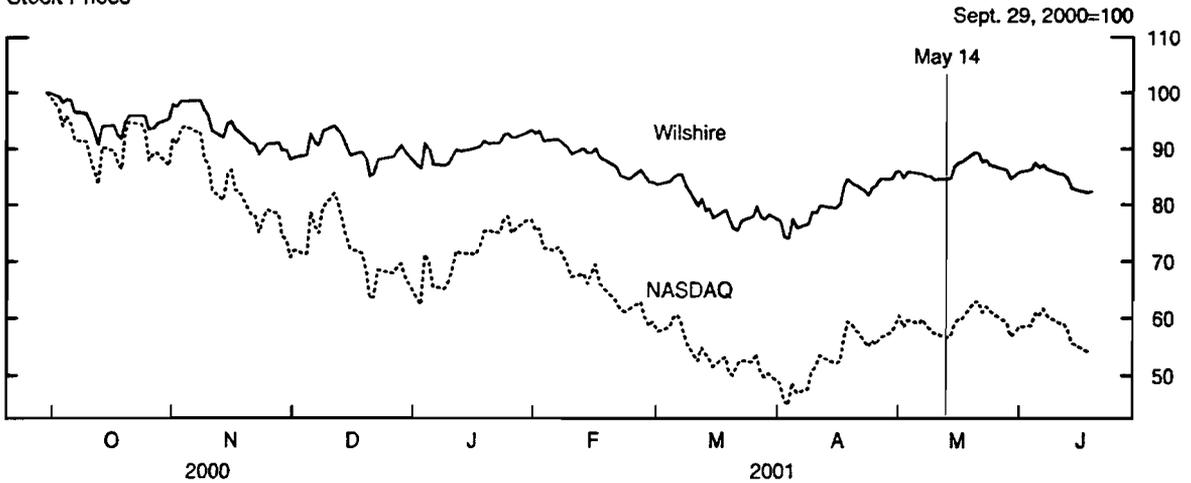
Implied Volatilities



Risk Spreads Relative to AAA



Stock Prices



Business Finance

Stock analysts currently expect S&P 500 operating earnings per share to decline about 17 percent in the second quarter compared with results for a year earlier, the steepest falloff in more than a decade. Looking further out, analysts have also knocked down their forecast for year-ahead earnings, although less dramatically. On balance, with stock prices also down a bit, equity valuations, as measured by the ratio of price to year-ahead expected earnings, are roughly unchanged over the intermeeting period.

Nonfinancial corporations issued over \$67 billion in bonds in May, more than in any other month; firms in the telecom and energy sectors accounted for the bulk of issuance. Nearly a third of May's issuance was speculative grade, indicating that investors, though highly selective, continued to accept junk issues. Preliminary issuance numbers from the first week of June also show continued strength. Corporations have indicated that they plan to use the proceeds from recent issuance for capital expenditures and to replace other funding sources, including bank loans and commercial paper. Indeed, business loans at banks contracted again in May, as did commercial paper. Quality spreads for commercial paper continued their slow return to long-run average levels as lower-quality issuers left the market.

Results from the May Survey of Terms of Business Lending show that banks have firmed the pricing of loans, the overall average spread of domestic C&I loan rates over the federal funds rate target increased 11 basis points, reaching 2.11 percent. Spreads on the riskiest loans not made under commitment climbed, while those on the safest loans declined.

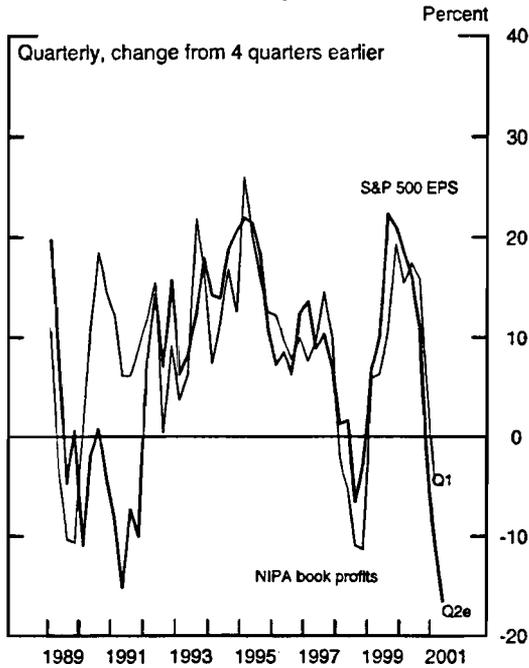
Equity issuance rebounded slightly in May, rising from its low April level on the strength of seasoned issues and issuance by energy firms. The IPO market has revived a bit, bolstered in June by a large issue to fund the spin off of Kraft. Technology firms, however, continue to issue relatively little equity.

Equity retirements have remained low. With profits weak and cash balances sagging, few corporations announced new share repurchase programs. Furthermore, few companies completed acquisitions or merged with other companies in April and May.

Available measures indicate some deterioration in corporate credit quality. Call Reports for the first quarter show a further rise in delinquencies on C&I loans at banks. More recently, Moody's downgraded, on net, about \$30 billion of nonfinancial bonds in May, adding to the large downgrades earlier this year. Another \$50 billion of bonds, on net, are on Moody's watch list and could be downgraded. The default rate on junk bonds edged up in May to nearly 11 percent, mainly because of defaults by a few large tech companies. KMV Corporation's index of year-ahead expected defaults ticked down in May, owing

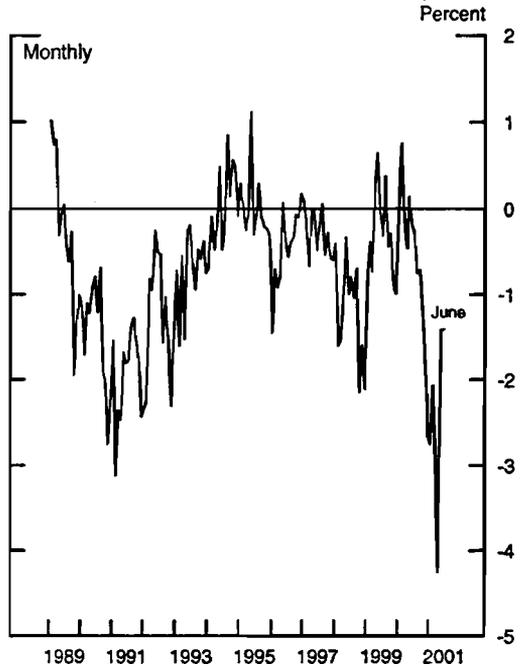
Earnings and Stock Valuations

After-Tax Corporate Earnings

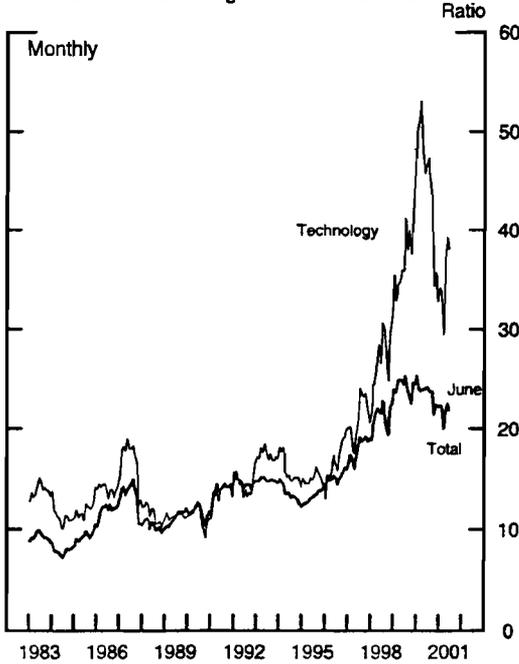


Staff estimate.

Revisions to S&P 500 Year-ahead Earnings

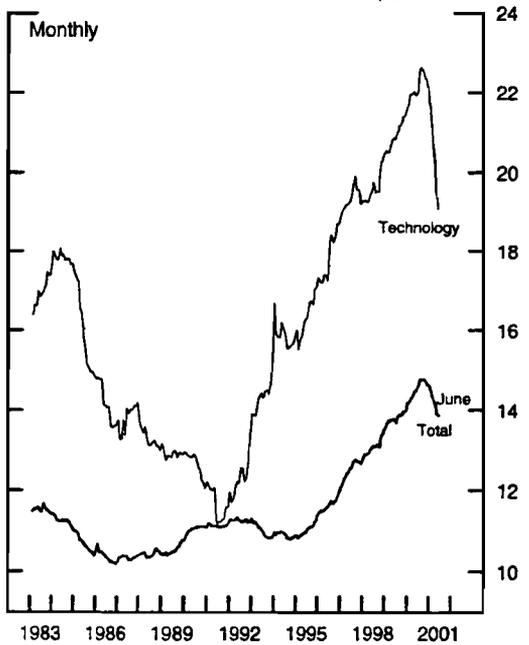


Selected Price-Earnings Ratios for S&P 500



Note. Using expected earnings for 12 months ahead.
Source. I/B/E/S.

Five-Year EPS Growth Expectations for S&P 500



Note. Earnings-weighted average of I/B/E/S consensus firm-level 5-year growth forecasts.

Gross Issuance of Securities by U.S. Corporations

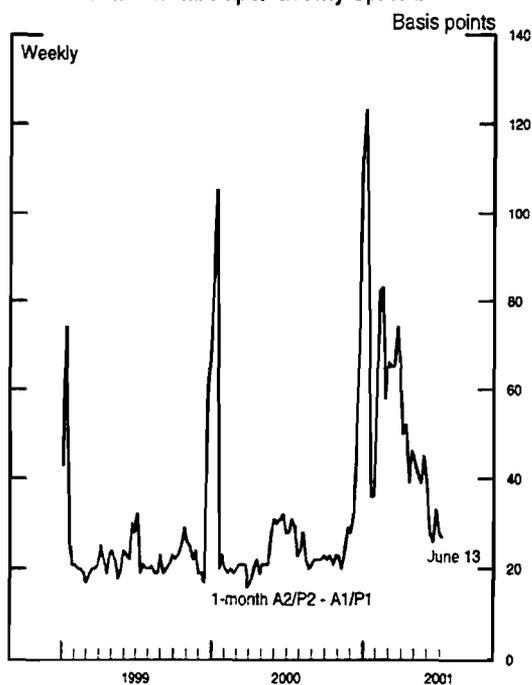
(Billions of dollars: monthly rates, not seasonally adjusted)

Type of security	1998	1999	2000		2001			
			H1	H2	Q1	Mar.	Apr.	May
All U.S. corporations	94.0	89.4	80.0	77.0	120.5	139.3	92.8	163.9
Stocks ¹	10.6	11.0	14.1	8.4	8.7	11.3	6.5	9.3
Bonds	83.5	78.4	65.9	68.6	111.7	128.0	86.3	154.6
<i>Nonfinancial corporations</i>								
Stocks ¹	6.2	9.2	12.4	7.3	5.5	7.7	4.8	6.6
Initial public offerings	2.2	4.2	5.7	3.1	1.7	3.8	2.4	2.0
Seasoned offerings	4.0	5.0	6.7	4.2	3.8	4.0	2.5	4.6
Bonds ²	25.6	24.5	21.3	19.1	41.1	44.4	33.5	67.1
Investment grade ³	14.1	13.9	11.5	12.4	28.5	34.3	25.2	43.6
Speculative grade ³	10.2	7.5	5.4	3.7	10.2	7.0	6.8	20.4
Other (sold abroad/unrated)	1.3	3.1	4.4	3.1	2.4	3.0	1.5	3.2
<i>Financial corporations</i>								
Stocks ¹	4.4	1.8	1.6	1.1	3.2	3.6	1.7	2.6
Bonds	57.8	53.9	44.7	49.5	70.6	83.6	52.7	87.5
<i>Memo</i>								
Net issuance of commercial paper, nonfinancial corporations ⁴	2.3	3.6	6.4	2.7	-17.3	-8.2	-5.2	-7.1
Change in C&I loans at commercial banks ⁴	7.0	4.7	10.5	5.2	4.6	-6.3	-5	-2.1

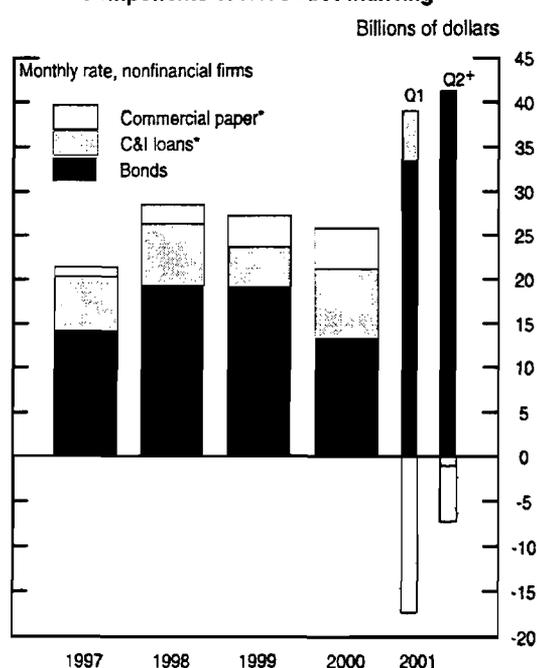
Note. Components may not sum to totals because of rounding. These data include speculative-grade bonds issued privately under Rule 144A. All other private placements are excluded. Total reflects gross proceeds rather than par value of original discount bonds.

1. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings.
 2. Excludes mortgage-backed and asset-backed bonds.
 3. Bonds sold in U.S. categorized according to Moody's bond ratings, or to Standard Poor's if unrated by Moody's.
 4. End-of-period basis, seasonally adjusted.
- c. Staff estimate.

Commercial Paper Quality Spread



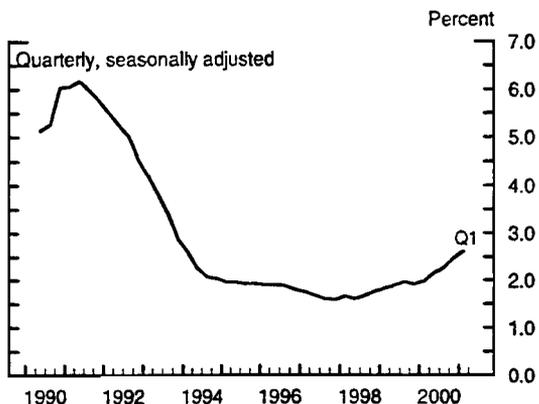
Components of Net Debt Financing



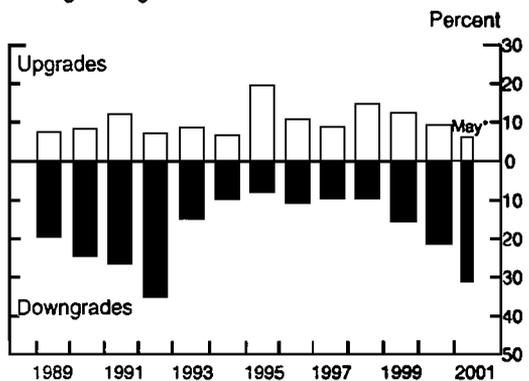
* Seasonally adjusted.
+ Based on data through May.

Corporate Credit Quality

Delinquency Rates on C&I loans at Commercial Banks



Rating Changes

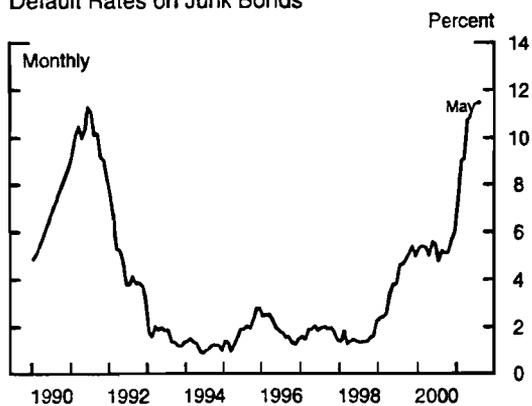


Note. Total debt upgrades (downgrades) as a percentage of par value of bonds outstanding.

*Year-to-date at an annual rate.

Source. Moody's.

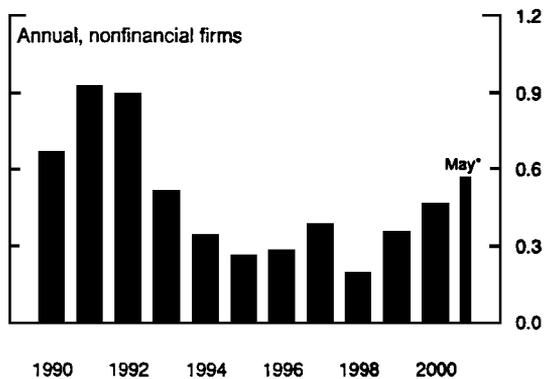
Default Rates on Junk Bonds



*12-month trailing rate.

Source. Moody's.

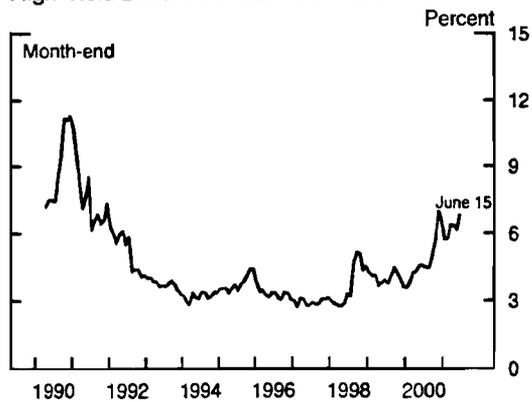
Liabilities of Failed Businesses to Total Liabilities



* 12-month trailing rate

Source. Dun & Bradstreet.

High-Yield Bond Yield less AAA Yield



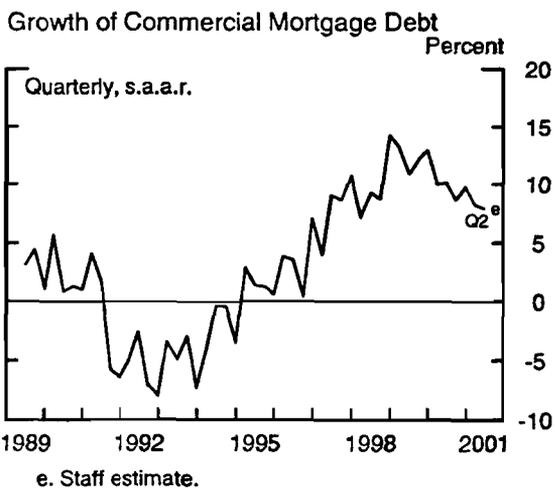
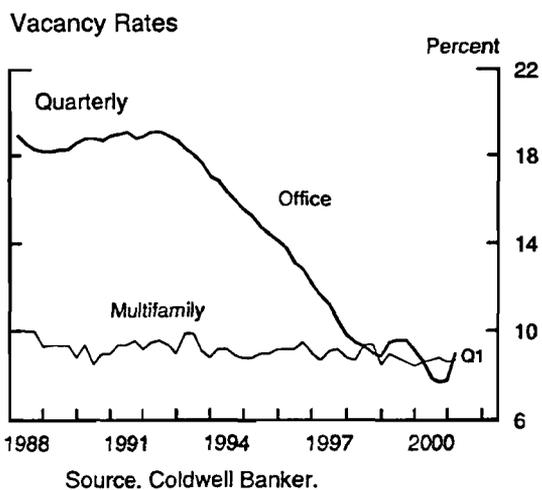
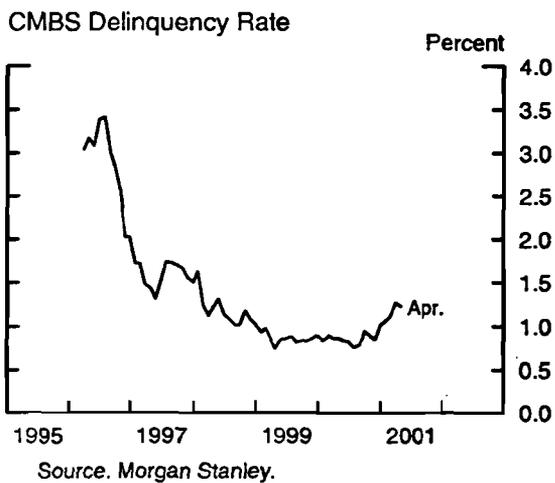
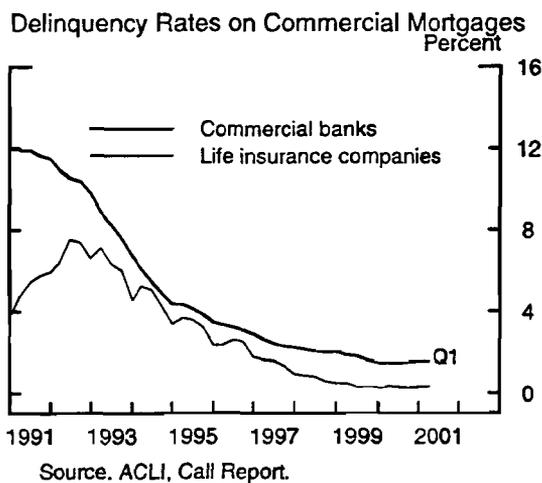
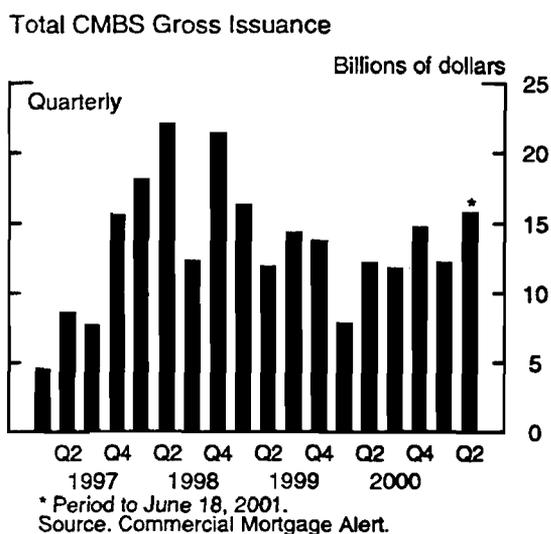
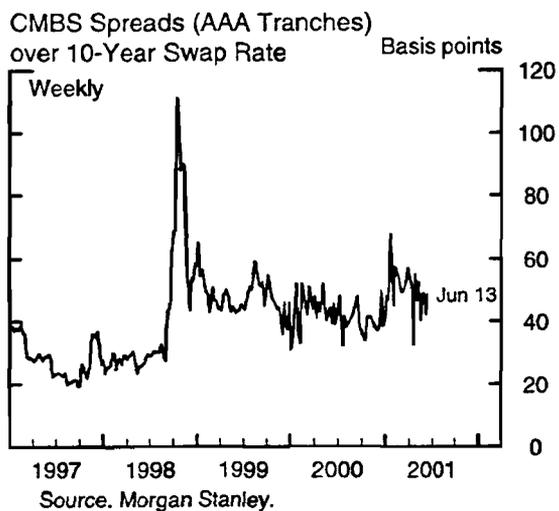
Source. Merrill Lynch.

One-Year-Ahead Expected Default Frequency



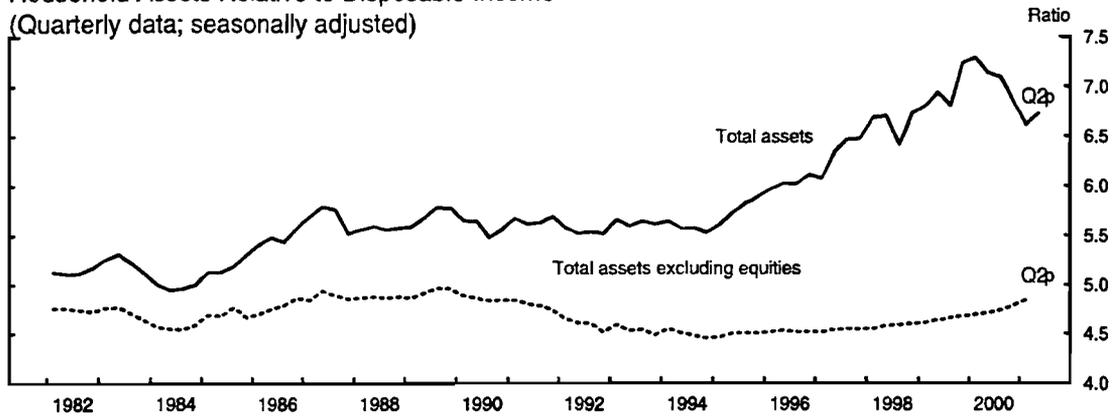
Source. KMV Corporation.

Commercial Real Estate



Household Assets

Household Assets Relative to Disposable Income
(Quarterly data; seasonally adjusted)



p. Staff projection.

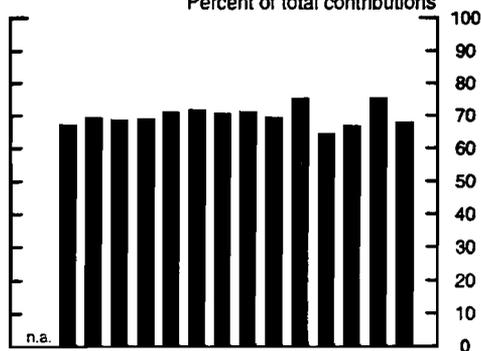
Net Flows into Long-Term Mutual Funds
(Excluding reinvested dividends; billions of dollars, monthly rates.)

	1999	2000	2001 Q1	Mar.	2001 Apr.	May. ^e	Assets Apr.
Total long-term funds	14.2	18.4	9.6	-13.1	21.9	26.7	4,914
Equity funds	15.7	25.1	0.5	-20.6	19.3	18.2	3,719
Domestic	14.8	21.2	2.4	-15.7	17.5	20.2	3,216
Capital appreciation	13.5	25.5	0.4	-14.2	11.2	14.5	1,969
Total return	1.4	-4.3	1.9	-1.5	6.3	5.7	1,247
International	0.9	3.9	-1.8	-4.9	1.8	-2.0	503
Hybrid funds	-1.0	-2.6	0.6	-0.4	1.4	1.1	348
Bond funds	-0.5	-4.0	8.5	7.9	1.3	7.4	847
International	-0.2	-0.2	0.1	-0.2	-0.1	0.0	20
High-yield	-0.2	-1.0	1.6	-0.6	0.3	2.2	97
Other taxable	1.0	-1.6	5.4	7.6	2.4	4.0	449
Municipals	-1.0	-1.2	1.4	1.0	-1.2	1.2	281

e. Staff estimates based on confidential ICI weekly data.

Source. Investment Company Institute (ICI).

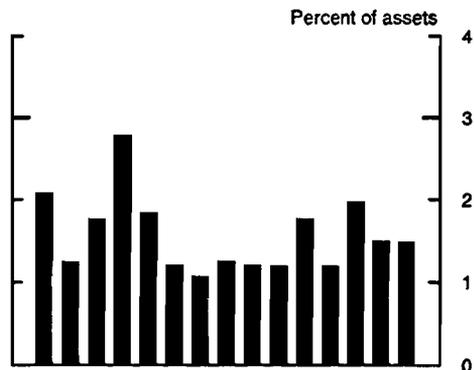
Equity Allocation of New Contributions to 401(k)
Pension Plans* Percent of total contributions



Mar. May July Sept. Nov. Jan. Mar. May
2000 2001

* Includes equity mutual funds and company stock.
Source. Hewitt Associates.

Transfers Among Existing 401(k) Pension Plan Assets* Percent of assets



Mar. May July Sept. Nov. Jan. Mar. May
2000 2001

* Includes money market funds and GICs.
Source. Hewitt Associates.

to that month's increase in stock prices and decrease in volatility, but the index remains high. Equity market developments and widening junk risk spreads in June suggest that the index may reverse some of its recent decline.

The commercial real estate sector continues to show modest deterioration but is far from the doldrums of the early 1990s. Indeed, investors' hearty appetite for commercial-mortgage-backed securities (CMBS) continues, and spreads have changed little despite heavy issuance and rising (although still low) delinquencies. In the first quarter, vacancy rates ticked up from their low levels. Total commercial mortgage debt is estimated to have decelerated in the second quarter to an 8 percent rate.

Household Finance

The ratio of household assets to disposable income in the second quarter is expected to remain about unchanged from the first quarter. Households have, in the past couple of months, appeared to reverse somewhat their earlier, more pessimistic, outlook for equity returns; they stepped up their purchases of equity and high-yield mutual fund shares and continued to allocate relatively high proportions of their contributions to 401(k) plans to equities.

Growth in both consumer and home mortgage debt is estimated to have slowed somewhat in the second quarter, in line with decelerating consumer expenditures and less robust housing activity. Interest rates on home equity lines of credit and new car loans at commercial banks fell 38 and 16 basis points respectively since the last FOMC. Rates on adjustable-rate mortgages fell less sharply, while rates on fixed-rate mortgages remained about unchanged. Despite drops in some interest rates, households' debt-service burden in the second quarter is projected to have risen to its twenty-year high of near 14-1/2 percent of disposable personal income, as income growth slowed more than debt growth.

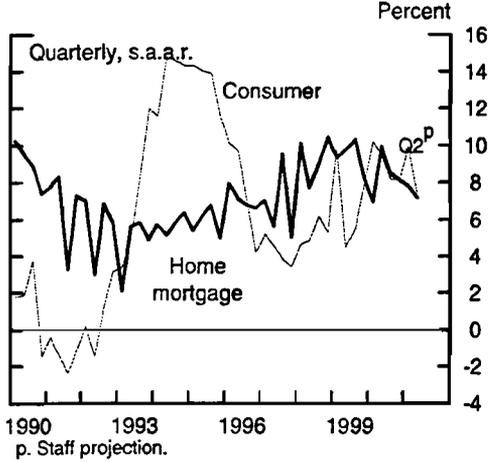
A high debt-service burden has contributed to a decline in household credit quality. Bank Call Report data show that delinquencies on credit cards rose, while delinquencies on other consumer loans (mainly autos) fell in the first quarter. More recent data for April show this pattern continuing, with delinquencies on credit cards in securitized pools rising to a two-year high, and auto-loan delinquencies remaining low. The weekly rate of personal bankruptcy filings has declined from its recent record levels, as the rush to file ahead of pending legislative reform has ebbed somewhat. Despite this recent decline, household bankruptcy filings remain well above their year-earlier levels.

Treasury and Agency Finance

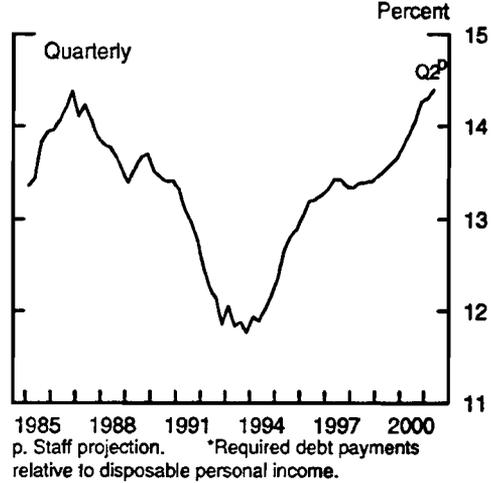
The Treasury continued to pay down sizable amounts of marketable debt over the intermeeting period. To meet short-term funding needs through the June 15

Household Liabilities

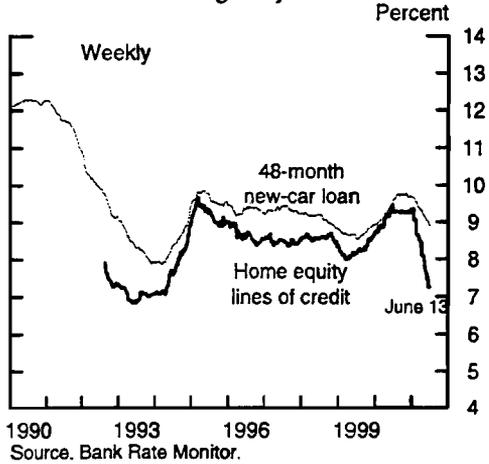
Household Debt Growth



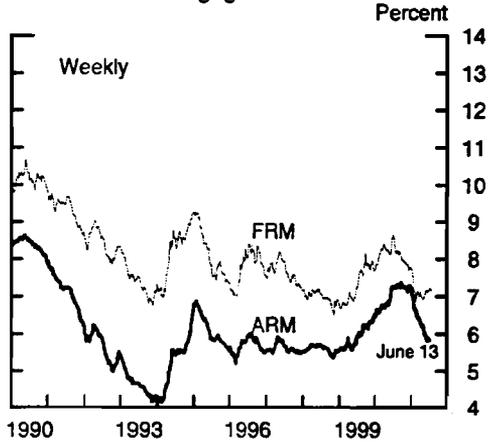
Household Debt Service Burden*



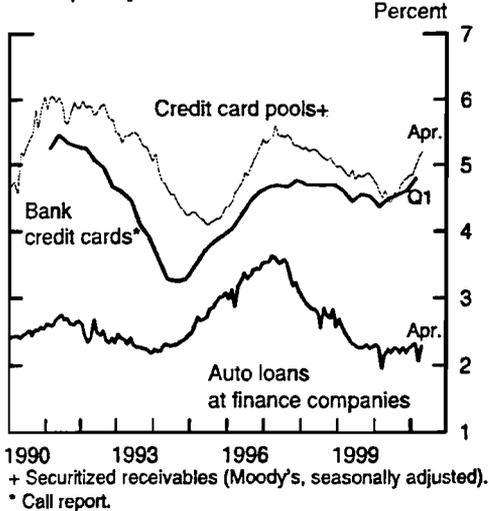
Interest Rates Charged by Banks



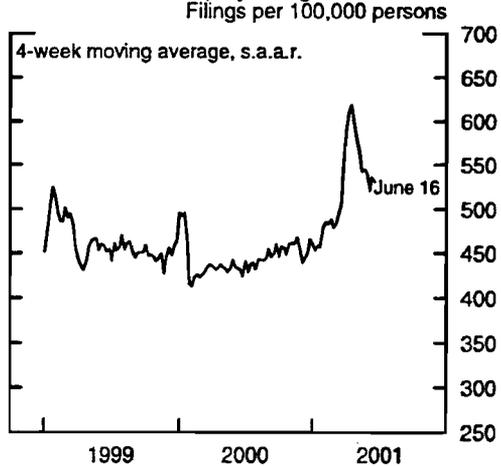
Freddie Mac Mortgage Rates



Delinquency Rates



Household Bankruptcy Filings



Treasury and Agency Finance

Treasury Financing (Billions of dollars)

Item	2000		2001			
	Q3	Q4	Q1	Mar.	Apr.	May.
Total surplus, deficit (-)	60.4	-2.3	-22.5	-50.7	189.8	-27.9
Means of financing deficit						
Net borrowing	-53.6	-25.1	23.7	32.6	-135.6	-20.6
Nonmarketable	-5.5	1.5	6.0	4.8	5.1	2.2
Marketable	-48.1	-26.6	17.6	27.8	-140.6	-22.8
Bills	-14.1	30.4	65.0	31.3	-93.0	-.6
Coupons ¹	-25.7	-48.2	-39.4	0	-42.6	-19.7
Debt buybacks	-8.2	-8.7	-8.0	-3.5	-5.0	-2.5
Decrease in cash balance	4.8	31.6	-7.2	-7.2	-36.8	58.9
Other ²	-11.5	-4.2	6.0	25.3	-17.4	-10.3
MEMO						
Cash balance, end of period	52.7	21.1	28.3	28.3	65.1	6.3

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

1. Does not include Treasury debt buybacks.

2. Direct loan financing, accrued items, checks issued less checks paid, and other transactions.

e. Estimated.

n.a. Not available.

Net Borrowing of Government-Sponsored Enterprises (Billions of dollars)

Agency	2000		2001			
	Q3	Q4	Q1	Mar.	Apr.	May
FHLBs	12.1	13.8	8.4	4.2	n.a.	n.a.
Freddie Mac	22.7	20.0	34.4	5.7	17.1	n.a.
Fannie Mae	28.5	35.7	23.9	-1.6	15.9	11.1
Farm Credit Banks	1.5	3.1	0	0.5	0.3	0.9
Sallie Mae	5.2	3.0	1.9	-6.6	n.a.	n.a.
MEMO						
<i>Outstanding noncallable</i>						
<i>Reference and Benchmark</i>						
<i>Securities</i>						
Notes and Bonds	274.1	313.1	351.2	351.2	361.7	377.1
Bills	222.5	235.0	270.0	270.0	274.0	284.5
Total	496.6	548.1	621.2	621.2	635.7	661.6

NOTE. Excludes mortgage pass-through securities issued by Fannie Mae and Freddie Mac.

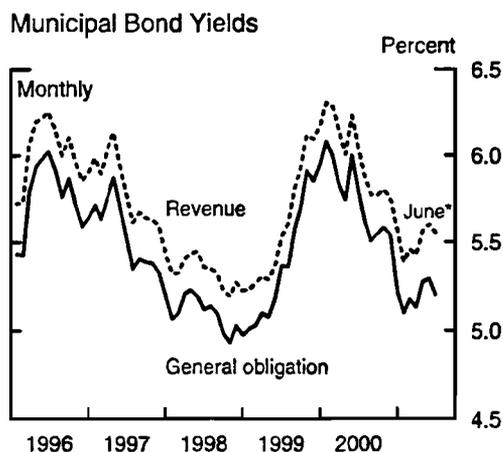
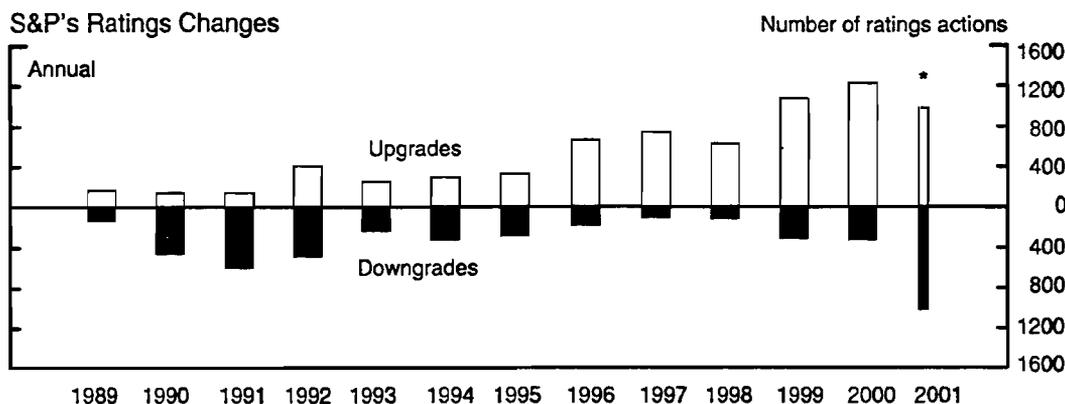
n.a. Not available

State and Local Government Finance

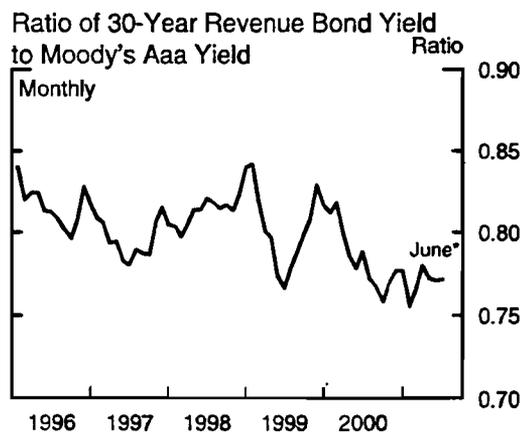
Gross Offerings of Municipal Securities (Billions of dollars; monthly rates, not seasonally adjusted)

	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Long-term ¹	18.0	15.0	17.2	18.5	24.5	17.0	26.2
Refundings ²	4.5	2.2	2.4	6.0	9.1	4.7	6.2
New capital	13.5	12.9	14.7	12.5	15.4	12.3	20.0
Short-term	2.7	2.8	2.5	2.6	2.0	1.6	2.0
Total tax-exempt	20.6	17.9	19.7	21.2	26.5	18.6	28.3
Total taxable	1.1	0.7	0.8	1.0	1.7	0.3	1.6

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



Note. Average of weekly data.
 * Data through June 7.



Note. Average of weekly data.
 * Data through June 7.

corporate tax date, the Treasury issued a large volume of cash management bills. This reliance on cash management bills will presumably drop off later this year after the Treasury introduces its four-week bill. The Treasury is expected to make heavy use of this new funding vehicle when it pays out tax-rebate checks later this summer and into the fall.

Treasury market liquidity conditions were little changed over the intermeeting period. Judging by primary dealer transactions, trading activity remained robust and on-the-run liquidity premiums held fairly constant at about 12 to 15 basis points—considerably below the elevated levels of 1998 and 1999. Bid-ask spreads for most securities edged down over the period, but remained at rather high levels.

Fannie Mae and Freddie Mac have continued to issue benchmark debt at a rapid pace—more than \$20 billion in late May and early June. Issuance of bellwether agency bills has also remained robust. During this period, the GSEs' stock prices appreciated rapidly, as markets interpreted the recent political changes in the Senate as signaling that the GSEs would face less political risk over the coming year.

State and Local Government Finance

Gross issuance of long-term municipal bonds rebounded in May from its low level in April as several governments took advantage of lower rates to issue new debt. With the exception of California, credit quality in the municipal sector remained strong. Standard and Poor's cut California's debt rating two notches, from AA to A+, and kept the state's debt on its watch list; in sum, \$25 billion of outstanding bonds were affected. Early in June, California sold a \$1 billion general obligation bond, using the proceeds to finance a variety of construction projects not related to the energy crisis. The bond was well received, with a lower-than-expected spread. As part of its plan to finance expenditures related to its power crisis, California intends to bring a \$14 billion bond issue to market in August and September.

Money and Bank Credit

After expanding briskly in the first quarter, M2 growth has slowed recently. M2 grew about 7-3/4 percent on average in April and May, though the individual months were affected by tax payments. Households apparently reversed some previous transactions and moved cash out of retail money market mutual funds and into long-term mutual funds, particularly equity funds. M3, in contrast, expanded at a rapid 13-1/4 percent annual rate in May, driven by institution-only money funds.

Bank credit decelerated, increasing less than 2 percent in May. Corporations likely used some of the proceeds from their recent heavy bond issuance to pay down shorter-term debt, including bank loans. Indeed, business loans fell more

Monetary Aggregates
(Based on seasonally adjusted data)

Aggregate or component	2000	2000	2001				Level (bil. \$) May 01 (p)
		Q4	Q1	Mar.	Apr.	May (p)	
<i>Aggregate</i>		Percent change (annual rate) ¹					
1. M2 ²	6.2	6.3	10.7	14.4	10.4	5.1	5166.9
2. M3	9.2	7.0	12.2	9.5	17.6	13.3	7500.1
<i>Selected components</i>							
3. Currency	4.2	3.4	7.1	4.7	6.0	7.7	546.0
4. Liquid deposits ³	3.2	4.8	12.1	21.2	15.0	14.7	2591.1
5. Small time deposits	9.5	6.9	3.8	-5.8	-5.9	-3.8	1037.1
6. Retail money market funds	12.2	11.6	16.9	24.6	18.1	-11.8	984.8
7. M3 minus M2 ⁴	16.6	8.8	15.9	-1.5	34.4	32.0	2333.2
8. Large time deposits, net ⁵	13.6	5.2	0.4	-40.4	33.7	10.1	813.0
9. Institution-only money market mutual funds	23.9	18.6	49.8	40.7	42.4	67.2	970.9
10. RPs	9.3	-3.6	-13.7	-24.3	71.5	3.3	360.2
11. Eurodollars	17.9	10.1	3.1	14.7	-61.8	8.3	189.1
<i>Memo</i>							
12. M1	-1.7	-3.3	5.1	13.8	5.3	-0.6	1117.4
13. Sweep-adjusted M1 ⁶	1.5	0.6	5.6	12.8	7.9	1.0	1541.5
14. Demand deposits	-10.9	-14.3	-0.5	11.9	-13.3	-2.7	312.3
15. Other checkable deposits	-0.8	-1.2	8.4	37.3	28.0	-17.0	251.1
16. Savings deposits	6.7	9.1	14.7	20.6	18.0	21.4	2027.6
17. Monetary base	1.4	2.8	6.4	2.6	7.0	5.8	598.8
		Average monthly change (billions of dollars) ⁷					
<i>Selected managed liabilities at commercial banks</i>							
18. Large time deposits, gross	8.7	4.9	7.3	-20.5	17.8	4.4	960.3
19. Net due to related foreign institutions	1.3	-7.5	-5.4	13.8	-43.5	18.1	207.8
20. U.S. government deposits at commercial banks	-1.4	-1.6	1.1	-10.6	6.5	-2.7	15.3

1. For the years shown, Q4 to Q4 percent change. For the quarters shown, based on quarterly averages.

2. Sum of M1, retail money market funds, saving deposits, and small time deposits.

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

4. Sum of large time deposits, institutional money funds, RP liabilities of depository institutions, and Eurodollars held by U.S. addressees.

5. Net of holdings of depository institutions, money market mutual funds, U.S. government and foreign banks and official institutions.

6. Sweep figures used to adjust these series are the estimated national total of transaction account balances initially swept into MMDAs owing to the introduction of new sweep programs on the basis of monthly averages of daily data.

7. For the years shown, "average monthly change" is the Q4 to Q4 dollar change divided by 12. For the quarters shown, it is the quarter-to-quarter dollar change, divided by 3.

pe—Preliminary Estimate

than 3 percent in May, the third consecutive monthly decline. Both real estate and consumer loans expanded moderately, at about 8 percent.

Commercial Bank Credit

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

Type of credit	2000	Q4 2000	Q1 2001	Mar. 2001	Apr. 2001	May 2001	Level, May 2001 (\$ billions)
Total							
1. Adjusted ¹	9.4	3.4	6.8	1.1	4.9	1.7	5,184
2. Reported	10.0	5.1	7.7	2.6	4.9	2.0	5,318
<i>Securities</i>							
3. Adjusted ¹	1.9	-6.7	5.6	-11.9	14.6	6.6	1,235
4. Reported	4.4	.5	9.0	-4.9	13.8	7.4	1,369
5. Treasury & Agency	-2.3	-10.4	-7.9	-29.3	12.8	4.4	769
6. Other ²	16.3	17.7	34.1	28.3	14.9	11.5	600
<i>Loans³</i>							
7. Total	12.0	6.7	7.2	5.1	1.9	.2	3,949
8. Business	9.1	3.6	8.2	-.5	-3.7	-3.3	1,103
9. Real estate	13.9	5.9	4.8	5.8	4.7	7.6	1,694
10. Home equity	27.7	26.6	22.5	16.9	7.0	11.3	139
11. Other	12.9	4.3	3.3	4.8	4.4	7.1	1,554
12. Consumer	10.8	8.2	6.9	-3.5	9.7	8.1	553
13. Adjusted ⁴	7.9	4.6	9.2	1.5	8.2	5.8	876
14. Other ⁵	13.3	13.2	12.4	22.0	-2.4	-21.1	599

Note. All data are adjusted for breaks caused by reclassifications. Monthly levels are pro rata averages of weekly (Wednesday) levels. Quarterly levels (not shown) are simple averages of monthly levels. Annual levels (not shown) are levels for the fourth quarter. Growth rates are percentage changes in consecutive levels, annualized but not compounded. These data have been benchmarked to the December 1999 Call Report.

1. Adjusted to remove effects of mark-to-market accounting rules (FIN 39 and FIN 115).

2. Includes securities of corporations, state and local governments, and foreign governments and any trading account assets that are not Treasury or Agency securities.

3. Excludes interbank loans.

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

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

International Developments

International Developments

U.S. International Transactions

Trade in Goods and Services

The U.S. trade deficit in goods and services was \$31.2 billion in March, compared with a deficit of \$26.9 billion in February (revised) and \$33.3 billion in January. For the first quarter, the deficit was \$365 billion at an annual rate, \$32 billion smaller than in the fourth quarter of last year.

Net Trade in Goods and Services (Billions of dollars, seasonally adjusted)

	2000	Annual rate			Monthly rate		
		2000		2001	2001		
		Q3	Q4	Q1	Jan.	Feb.	Mar.
<i>Real NIPA¹</i>							
Net exports of G&S	-412.4	-427.7	-441.7	-411.9	...	...	...
<i>Nominal BOP</i>							
Net exports of G&S	-368.9	-382.5	-397.0	-365.1	-33.3	-26.9	-31.2
Goods, net	-449.9	-458.9	-474.6	-441.4	-39.5	-33.2	-37.6
Services, net	81.0	76.4	77.6	76.3	6.2	6.4	6.5

1. Billions of chained (1996) dollars.

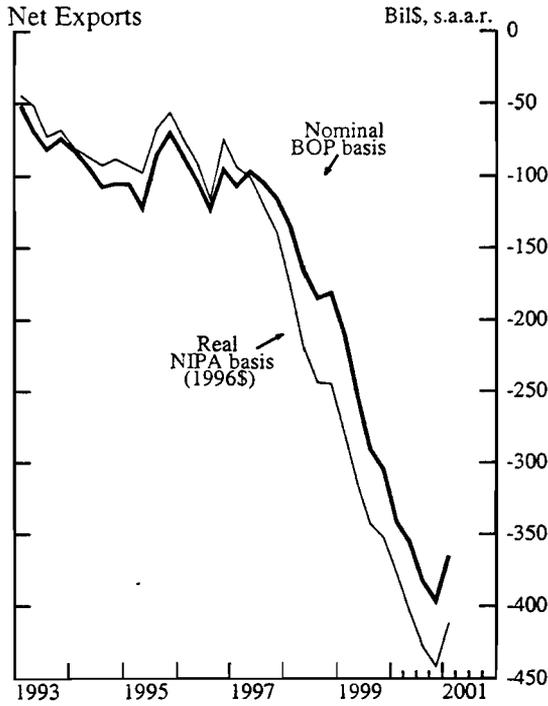
Source: U.S. Department of Commerce, Bureaus of Economic Analysis and Census.

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

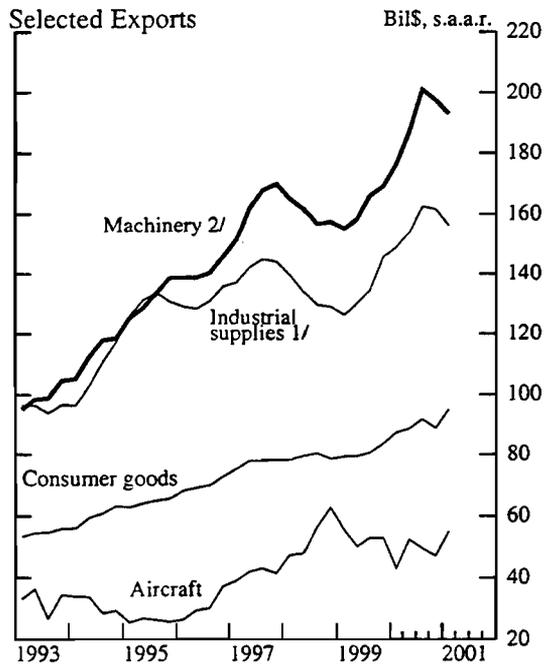
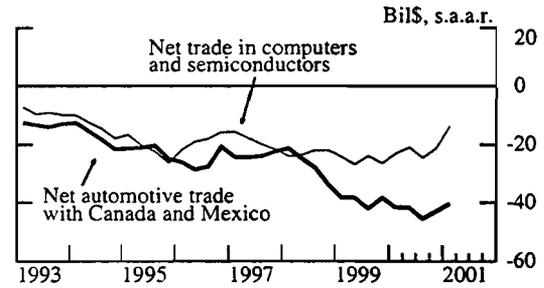
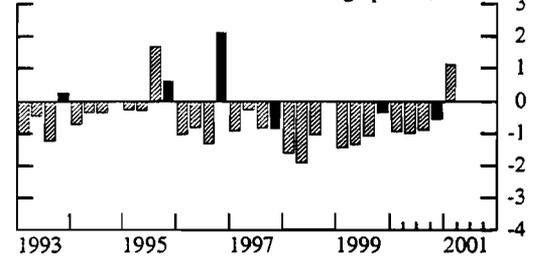
The value of exports of goods and services declined moderately in March to about the same level recorded in January, with much of the decrease in capital goods. In the first quarter, the value of exports declined 3 percent at an annual rate, the second consecutive quarter of negative growth. The largest declines were in automotive products (primarily cross-border trade with Canada), machinery (both high tech and other), and industrial supplies. By region, the recent declines in goods exports were largely to Asia and Latin America. In contrast, goods exports to Western Europe increased.

The value of imports of goods and services rebounded in March from the sharp drop in February, to a level that was nonetheless lower than recorded in any of the eight months preceding February. The jump in March was largely in imported consumer goods. Consumer goods were also the largest single source of import decline in February. In the first quarter, the value of imports fell 10 percent at an annual rate. Imports had leveled off in the fourth quarter of last year following several quarters of strong growth. The largest declines in the first quarter were in high-tech machinery (computers, semiconductors, and telecommunications equipment), automotive products (primarily from Canada), and oil (entirely from a drop in price). In contrast, there were moderately strong increases in imports of consumer goods and non-oil industrial supplies.

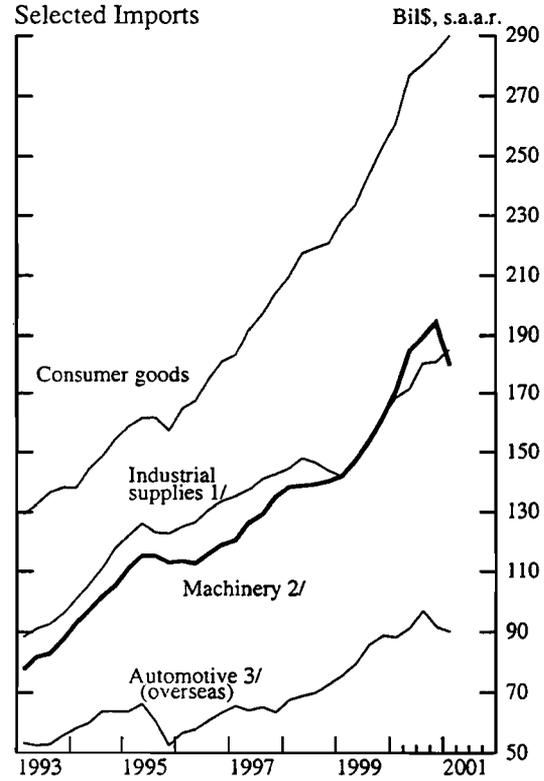
U.S. International Trade in Goods and Services



Contribution of Net Exports to Real GDP Growth
Percentage points, s.a.a.r.



1. Excludes agriculture and gold.
2. Excludes computers and semiconductors.



1. Excludes oil and gold.
2. Excludes computers and semiconductors.
3. Excludes Canada and Mexico.

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

	Levels				Amount Change ¹			
	2000	2001	2001		2000	2001	2001	
	Q4	Q1	Feb.	Mar.	Q4	Q1	Feb.	Mar.
Exports of G&S	1085.8	1077.7	1084.7	1073.6	-15.9	-8.1	9.7	-11.1
Goods exports	785.2	775.5	782.3	769.2	-18.2	-9.7	7.4	-13.2
Gold	6.5	6.7	6.8	7.6	2.3	0.2	1.0	0.8
Other goods	778.6	768.8	775.6	761.6	-20.5	-9.8	6.4	-14.0
Aircraft & parts	47.2	55.0	61.3	57.3	-2.4	7.8	14.8	-4.0
Computers	56.6	56.2	55.8	54.9	-2.1	-0.5	-2.0	-0.9
Semiconductors	62.3	57.1	56.4	52.8	-2.8	-5.2	-5.7	-3.6
Other capital gds	200.2	195.6	197.4	186.3	-3.0	-4.6	-5.8	-11.1
Automotive	78.1	70.6	68.7	73.2	-2.9	-7.5	-1.2	4.5
to Canada	42.0	36.6	35.4	39.6	-2.3	-5.4	0.5	4.2
to Mexico	17.2	16.1	16.4	17.4	1.4	-1.0	1.8	0.9
to ROW	18.9	17.8	16.8	16.2	-1.9	-1.1	-3.6	-0.6
Agricultural	52.7	54.2	55.0	55.8	-2.6	1.5	3.2	0.8
Ind supplies (ex. ag)	161.5	156.3	156.2	157.4	-1.0	-5.2	0.9	1.1
Consumer goods	88.7	95.0	95.5	95.3	-3.0	6.2	1.5	-0.2
All other goods	31.2	28.8	29.3	28.6	-0.7	-2.4	2.7	-0.6
Services exports	300.6	302.3	302.4	304.4	2.3	1.6	2.4	2.0
Imports of G&S	1482.8	1442.9	1407.0	1447.7	-1.4	-39.9	-67.0	40.7
Goods imports	1259.7	1216.9	1181.0	1220.9	-2.6	-42.8	-67.8	39.9
Petroleum	127.5	116.7	114.7	108.6	0.3	-10.8	-12.2	-6.1
Gold	6.7	6.1	6.0	6.2	2.5	-0.6	-0.3	0.2
Other goods	1125.5	1094.1	1060.3	1106.1	-5.3	-31.4	-55.4	45.8
Aircraft & parts	30.6	30.9	28.4	36.3	3.9	0.3	0.5	7.8
Computers	90.2	83.7	82.8	83.6	-4.8	-6.5	-2.1	0.8
Semiconductors	50.1	43.1	42.7	39.2	-3.5	-7.0	-4.5	-3.6
Other capital gds	197.1	182.7	178.5	180.7	4.7	-14.4	-10.5	2.2
Automotive	193.8	183.3	182.0	184.3	-8.7	-10.5	-1.6	2.3
from Canada	61.8	54.5	52.1	56.5	-2.8	-7.3	-2.9	4.4
from Mexico	40.3	38.7	35.8	43.9	-0.6	-1.7	-0.5	8.1
from ROW	91.6	90.1	94.1	83.9	-5.3	-1.5	1.9	-10.2
Ind supplies	180.7	184.9	179.9	185.3	0.5	4.3	-9.8	5.4
Consumer goods	284.6	289.9	271.1	304.2	4.3	5.3	-23.3	33.0
Foods, feeds, bev.	46.4	45.6	45.0	44.3	-0.9	-0.8	-2.4	-0.7
All other goods	52.1	49.9	49.9	48.4	-0.8	-2.2	-1.7	-1.5
Services imports	223.0	226.0	226.0	226.8	1.2	2.9	0.8	0.8
<i>Memo:</i>								
Oil quantity (mb/d)	12.00	12.74	12.27	12.29	-0.13	0.74	-1.34	0.03
Oil import price (\$/bbl)	29.13	25.09	25.60	24.19	0.38	-4.04	0.07	-1.41

¹ Change from previous quarter or month.

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

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

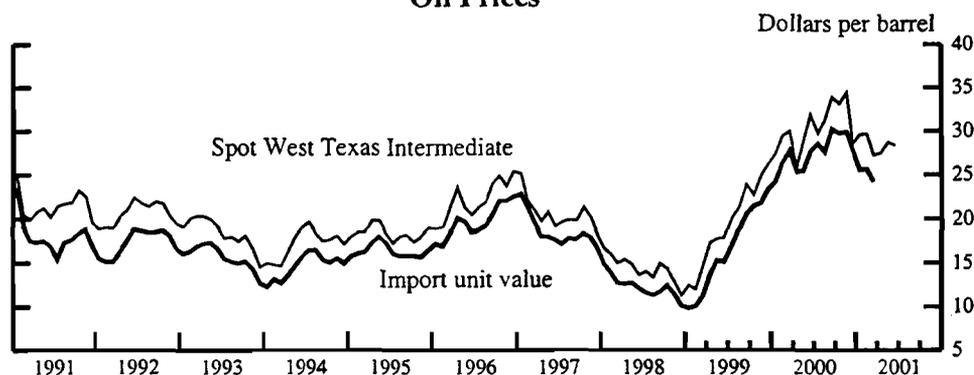
	Annual rates			Monthly rates		
	2000	2001		2001		
	Q4	Q1	Q2 ^e	Mar.	Apr.	May
	----- BLS prices (1995 weights)-----					
Merchandise imports	0.8	-5.3	-6.6	-1.5	-0.6	0.3
Oil	5.0	-44.8	-13.0	-6.5	-1.7	5.5
Non-oil	0.3	2.3	-5.4	-0.9	-0.4	-0.2
Core goods*	0.8	2.8	-5.1	-0.9	-0.3	-0.2
Computers	-10.4	-4.3	-12.1	-0.8	-2.2	-0.2
Semiconductors	-0.2	-3.7	-4.8	-0.3	-0.8	-0.3
Cap. goods ex comp & semi	-1.7	-0.3	-0.6	0.4	-0.4	0.0
Automotive products	0.0	-0.1	-0.9	0.0	-0.1	-0.2
Consumer goods	-1.0	0.4	-0.8	0.0	-0.2	0.0
Foods, feeds, beverages	-2.9	0.1	-6.9	0.9	-1.7	-0.7
Industrial supplies ex oil	6.9	12.4	-16.4	-4.0	-0.4	-0.7
Merchandise exports	0.7	-0.3	-1.7	-0.2	-0.1	-0.3
Core goods*	1.2	-0.1	-1.2	-0.2	0.0	-0.3
Computers	-1.6	-2.4	-3.5	-0.6	0.0	-0.9
Semiconductors	-3.1	-2.9	-5.8	0.6	-1.5	-0.4
Cap. goods ex comp & semi	0.9	2.4	1.4	0.1	0.2	0.0
Automotive products	0.0	0.5	0.5	0.1	0.1	0.0
Consumer goods	-0.8	-0.7	-1.0	-0.1	-0.1	-0.1
Agricultural products	12.4	2.9	-4.2	0.2	-0.7	-0.1
Industrial supplies ex ag	-1.8	-4.1	-5.1	-0.9	-0.2	-0.8
Chain price index	---Prices in the NIPA accounts (1996 weights)---					
Imports of goods & services	0.2	-2.7	n.a.	...	...	...
Non-oil merchandise	0.1	1.2	n.a.	...	...	...
Core goods*	1.0	1.9	n.a.	...	...	...
Exports of goods & services	0.5	-0.4	n.a.	...	...	...
Total merchandise	0.4	-0.5	n.a.	...	...	...
Core goods*	1.1	0.0	n.a.	...	...	...

*/ Excludes computers and semiconductors.

e/ Average of two months.

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

Oil Prices



Trade data for April, and revised figures for all prior months, will be released on Thursday, June 21, as part of the annual revisions of the U.S. international transactions accounts. These data will be reported in the Greenbook supplement.

Prices of Internationally Traded Goods

Oil. The BLS price of imported oil moved up in May following declines in most other months of the year, partly the result of a new round of OPEC supply cuts. Thus, prices of imported oil decreased only moderately in April-May, on average, compared with a much larger drop in the first quarter. The spot price of West Texas intermediate crude remained between \$27 and \$30 per barrel in May and early June. On June 4, Iraq suspended oil exports through the U.N. oil-for-food program to protest the revisions to the sanctions framework that are currently being debated by the U.N. Security Council. OPEC officials have pledged to counteract any significant supply disruption from Iraq, but not before the cartel meets again in early July to re-evaluate the Iraqi situation. Crude oil price movements may also have been damped by increased levels of crude oil inventories, particularly in the United States.

Non-oil imports. Prices of imported non-oil goods (and core goods) declined 0.2 percent in May with all major categories either declining or unchanged. May was the second month of moderate price declines. The largest price decreases in May were in food (mostly vegetable prices) and industrial supplies (primarily falling prices for unfinished metals and chemicals). For April-May combined, prices of imported core goods dropped 5.1 percent at an annual rate from the first quarter, largely, but not entirely, because of declines in the price of natural gas from elevated levels. Excluding natural gas, there were small to moderate price declines in all major trade categories.

Exports. Prices of U.S. goods exports (total and core) decreased 0.3 percent in May, the fourth consecutive month of flat or declining prices. The largest declines in prices of core goods in May were in industrial supplies. For April-May combined, prices of exported core goods declined 1.2 percent at an annual rate. Rising prices of exported capital goods (excluding computers and semiconductors) and automotive products were more than offset by declining prices of consumer goods, agricultural products, and industrial supplies.

U.S. International Financial Transactions

Foreign official reserves held in the United States fell by almost \$10 billion in April (line 1 of the Summary of U.S. International Transactions table). Moderate decreases were reported for France and several Asian countries. Argentina, whose reserves in the United States fell almost \$6 billion in March, showed a \$2 billion increase for April. In April, the composition of official reserves shifted markedly away from U.S. Treasury securities and toward agency

debt and bank liabilities. Official foreigners sold \$20 billion in Treasuries, about half of which was in bills. Because total Treasuries outstanding also fell in April, the percentage of the total in foreign official portfolios remained roughly constant. It should be recalled that the large increase in official reserves held in the United States registered in the first quarter of 2001 was entirely the result of China's decision to shift dollar reserves from Europe to the United States. Preliminary reports for official holdings at FRBNY indicate a further slight fall in May.

Private foreigners also reduced their holdings of Treasuries in April (line 4a), bringing the net decline for the first four months of 2001 to \$14 billion; at the end of April, private foreigners held about 22 percent of outstanding Treasuries, little changed from the end of December. Foreign private net purchases of U.S. agency bonds, corporate and municipal bonds, and equities, while somewhat below the record pace of the first quarter and March, were still quite strong in April (lines 4b, 4c, and 4d). Large purchases of corporate bonds were registered in the United Kingdom and the Caribbean, while agency purchases were concentrated in China, Hong Kong, and the United Kingdom. U.S. equities were purchased primarily in Europe and Japan.

For the fifth straight month, U.S. residents made significant net purchases of foreign equities (line 5b); these were concentrated in Canada and Japan. By contrast, there were widely distributed net sales of foreign bonds (line 5a). Although the acquisition of foreign equities via stock swaps (line 5c) was again zero for April, already completed takeovers indicate that such swaps will be at least \$22 billion in May—largely the result of the takeover of VoiceStream by Deutsche Telekom—and \$9 billion in June.

In the U.S. banking sector, net inflows of \$34 billion were recorded in April (line 3). These inflows were in sharp contrast to the exceptionally large outflows in March of \$100 billion. The partial reversal in April was due in large part to a significant increase in U.S. custodial holdings of domestic money market instruments for foreign customers.

Balance of payments data for 2001:Q1, including direct investment capital flows, will be released on June 21, and will be discussed in the Greenbook supplement.

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

	1999	2000	2000			2001			
			Q2	Q3	Q4	Q1	Mar.			Apr.
Official financial flows	55.0	39.3	9.4	12.2	-4.7	19.7	0.8	-9.8	
1. Change in foreign official assets in the U.S. (increase, +)	46.4	39.6	7.4	12.5	-3.3	19.5	-2.0	-9.8	
a. G-10 countries	49.7	12.3	6.0	-4.2	-8	-5.5	-3.3	-6.0	
b. OPEC countries	2.0	10.7	1.2	3.4	.6	.8	-1.6	-0.2	
c. All other countries	-5.3	16.6	.3	13.3	-3.1	24.2	2.9	-3.6	
2. Change in U.S. official reserve assets (decrease, +)	8.6	-.3	2.0	-.3	-1.4	.2	-.1	.0	
Private financial flows	268.4	359.8	143.2	90.4	91.4	...	...	...
Banks									
3. Change in net foreign positions of banking offices in the U.S. ¹	-12.4	-1.7	44.5	-27.0	10.5	-108.1	-99.6	34.4	
Securities²									
4. Foreign net purchases of U.S. securities (+)	319.0	413.8	67.2	110.4	113.3	140.8	50.2	33.1	
a. Treasury securities	-19.9	-52.3	-20.4	-12.4	-10.3	-8.4	-2.3	-5.7	
b. Agency bonds	71.9	111.9	19.0	28.6	38.3	38.7	18.3	9.8	
c. Corporate and municipal bonds	158.8	180.4	41.6	45.7	49.1	68.8	26.3	21.9	
d. Corporate stocks	108.2	173.8	27.0	48.5	36.2	41.7	8.0	7.1	
5. U.S. net acquisitions (-) of foreign securities	-112.9	-97.2	-32.0	-20.8	-15.5	-27.9	-16.0	-2.1	
a. Bonds	-5.7	-3.9	10.8	-9.0	3.8	-.8	-1.5	5.2	
b. Stock purchases	15.6	-9.3	5.2	-4.1	5.4	-20.0	-14.5	-7.3	
c. Stock swaps ³	-122.9	-84.0	-48.0	-7.7	-24.7	-7.1	-0	-0	
Other flows (quarterly data, s.a.)									
6. U.S. direct investment (-) abroad	-150.9	-161.6	-37.5	-36.2	-45.0	...	...	...
7. Foreign direct investment in U.S.	275.5	316.5	100.4	72.7	94.4	...	...	...
8. Foreign holdings of U.S. currency	22.4	1.1	1.0	.8	6.2	...	...	...
9. Other (inflow, +) ⁴	-72.2	-111.2	-0.5	-9.5	-72.5	...	...	...
U.S. current account balance (s.a.)	-331.5	-435.4	-105.0	-113.8	-115.3	...	...	...
Capital account balance (s.a.)⁵	-3.5	.7	.2	.2	.2	...	...	...
Statistical discrepancy (s.a.)	11.6	35.6	-47.8	11.0	28.4	...	...	...

NOTE. The sum of official and private financial flows, the current account balance, the capital account balance, and the statistical discrepancy is zero. 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 excludes adjustments BEA makes to account for incomplete coverage; therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. U.S. acquisitions of foreign equities associated with foreign takeovers of U.S. firms.

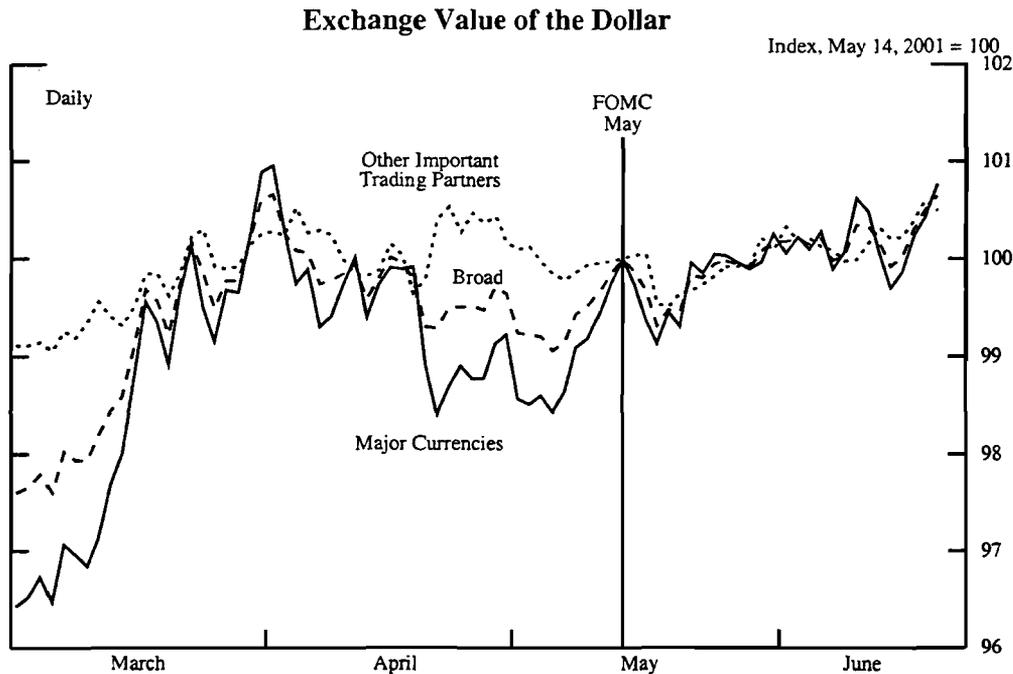
4. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business

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

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

Foreign Exchange Markets

On balance, the major currencies index of the exchange value of the dollar rose $\frac{3}{4}$ percent over the intermeeting period, as the dollar's appreciation against the euro, the Swiss franc and sterling was offset only partially by its depreciation versus the Canadian dollar. Despite indications that the slowdown in U.S. economic growth may last longer than had been anticipated in the spring, market participants generally appeared willing to maintain their holdings of dollar-denominated assets, as data from the euro area and Japan also showed significant slowing. The index of the dollar's value against the currencies of our other important trading rose $\frac{1}{2}$ percent.



The dollar appreciated $2\frac{3}{4}$ percent on balance against the euro during the intermeeting period. The dollar reached its highest level against the common currency since November 2000, before retracing a bit late in the period as several euro-area officials openly discussed the possibility of foreign exchange intervention. Despite data indicating a slowdown in France and Germany, the European Central Bank was thought to be constrained from aggressive monetary easing by rising inflationary pressures. On net, three-month interest rates declined 12 basis points in the euro area during the period, a smaller decline than in the United States.

Financial Indicators in Major Industrial Countries

Country	Three-month rate		Ten-year yield		Equities
	Jun. 20 (Percent)	Percentage Point Change	Jun. 20 (Percent)	Percentage Point Change	Percent Change
Canada	4.41	-.04	5.70	-.17	-3.83
Japan	.01	.00	1.19	-.05	-8.64
Euro area	4.45	-.12	4.98	-.10	-6.58
United Kingdom	5.15	-.04	5.13	.00	-.94
Switzerland	3.09	.04	3.41	-.20	-3.36
Australia	4.97	.07	5.83	-.13	.88
United States	3.65	-.40	5.21	-.25	-2.47
Memo: Weighted-average foreign	3.27	-.04	4.67	-.11	n.a.

NOTE. Change is from May 14 to June 19/20.

n.a. Not available.

The dollar appreciated 1¾ percent on balance against sterling, briefly exceeding a 15-year high set last year before retracing a bit late in the period. Much of the exchange rate move came around the time of the Labour Party's victory in the general elections. Labour's victory was seen as increasing the odds of Britain's entry in the euro area, and many market analysts argued that the British government would want the pound to depreciate substantially versus the euro before entry into the European Monetary Union. With the British economy showing some signs of resilience, and inflation rising to a level close to its target, the Bank of England's Monetary Policy Committee chose not to ease policy.

The Bank of Canada lowered its benchmark rate to 4.75 percent at the end of May. The dollar depreciated 1¼ percent versus the Canadian dollar in an apparent unwinding of moves that occurred earlier this year, as data indicated that the Canadian economy was not slowing as much as had been expected.

The strength of the Japanese yen, which was little changed against the dollar and appreciated 2.5 percent against the euro during the intermeeting period, was puzzling, as data showed that the Japanese economy contracted during the first quarter and remained very weak in the second quarter. Several market participants attributed the yen's strength to unconfirmed reports that some large

Japanese institutional investors were closing out losing foreign investment positions, particularly in the euro area. Despite overt political pressure, the Bank of Japan did not undertake further monetary easing, and called instead for structural reforms by the government. While equity prices in most industrial economies declined during the period, Japanese share prices, led by the banking sector, fell the most, as the market optimism that followed Prime Minister Koizumi's election began to fade.

Financial Indicators in Latin America, Asia, and Russia

Economy	Currency/ US dollar		Short-term Interest rates ¹		Dollar-denominated bond spread ²		Equity prices
	Jun. 20	Percent Change	Jun.19/20 (Percent)	Percentage Point Change	Jun.19/20 (Percent)	Percentage Point Change	Percent Change
Mexico	9.09	-1.12	8.98	-3.80	3.45	-.52	5.25
Brazil	2.48	7.36	19.00	1.40	10.92	.51	1.15
Argentina	1.00	.03	11.00	-9.00	12.20	-.50	.79
Chile	622.50	2.97	5.79	-3.33	2.81	.03	3.91
China	8.28	.00	n.a.	n.a.	1.12	.11	-.70
Korea	1295.00	-.23	5.30	-.05	2.20	-.01	1.99
Taiwan	34.40	4.59	4.03	-.27	...	...	-2.84
Singapore	1.82	.04	2.25	.00	...	...	1.85
Hong Kong	7.80	-.01	3.73	-.10	...	...	-2.57
Malaysia	3.80	-.01	2.91	-.01	1.67	-.28	3.43
Thailand	45.25	-.66	4.50	2.50	2.99	.91	3.56
Indonesia	11280.00	-.84	16.60	.33	7.67	.23	17.39
Philippines	52.10	3.99	9.94	-.63	5.57	.16	-2.38
Russia	29.14	.34	n.a.	n.a.	7.42	-.80	13.16

NOTE. Change is from May 14 to June 19/20.

1. One month interbank interest rate, except Chile: 30-day deposit rate; Korea: 1-week call rate.

No reliable short-term interest rates exist for China or Russia.

2. Spread over similar maturity U.S. Treasury bond yield. Mexico, Brazil, Argentina and Venezuela: Stripped Brady bond yield. Chile, China, and Korea: Global bond yield. Malaysia, Philippines and Russia: Eurobond yield. Thailand and Indonesia: Yankee bond yield. Taiwan, Singapore and Hong Kong do not have outstanding sovereign bonds denominated in dollars.

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

In emerging markets, the focus during the intermeeting period was squarely on Latin America. Argentina's program to exchange current government debt for new bonds with a lower servicing burden in the next few years was completed on June 4. The exchange, which resulted in a larger bond swap than had been anticipated, was generally viewed as a success. Many analysts, however, warned

that Argentina may have traded short-term relief for insurmountable difficulties in the medium and long term. Late in the period, Argentina introduced a de facto dual exchange rate system, with a separate exchange rate based on an equal basket of dollars and euros to be used solely for international trade. The announcement raised fears of an upcoming peso devaluation among international investors. Nevertheless, on net over the period, short-term interest rates fell in Argentina, as did the spread over Treasuries of Argentine sovereign debt. In Brazil, beset by a severe energy crisis and concern over Argentina, the *real* depreciated more than 7 percent against the dollar to an all-time low, despite intervention operations, sales of dollar-indexed debt, and an increase in the main central bank policy rate. The Mexican peso, in contrast, appreciated 1 percent on net versus the dollar, with much of the movement following the announcement of the purchase of a major Mexican bank by a U.S. money center bank. The same news contributed to a large increase in Mexican share prices.

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

Developments in Foreign Industrial Countries

First-quarter real GDP data confirm that activity in the foreign industrial countries has slowed along with the deceleration in U.S. economic activity, although to varying degrees. Recent data indicate that the slowdown has persisted in the current quarter, with industrial output especially weak. In Japan, real GDP declined in the first quarter, with exports down sharply and domestic demand supported only by a sizable increase in public investment. Current-quarter indicators suggest activity may contract further. Real GDP expanded at a moderate pace in the euro area, but exports fell, and domestic demand weakened notably. More recent indicators show further deterioration particularly in manufacturing sentiment. Industrial output contracted in the United Kingdom, while service sector activity has continued at a healthy pace. In Canada, manufacturing output has been especially hard hit by the U.S. slowdown, but domestic demand has been supported by consumption expenditures and residential investment.

Higher food and energy prices have boosted rates of headline consumer price inflation in Europe and Canada; in the euro area, headline inflation is now almost one and a half percentage points above the ECB's 2 percent target ceiling. Measures of core inflation have also moved up somewhat both in the euro area and Canada. In Japan, consumer prices continue to fall by about 1 percent per year.

Faced with slowing growth but some evidence of a pickup in inflation, central banks in Europe and Canada eased monetary policy in May but have left policy rates unchanged so far in June. Since January, policy rates have been lowered 125 basis points in Canada, 75 basis points in the United Kingdom, and 25 basis points in the euro area.

Recent indicators for **Japan** suggest that the economy may be heading into another recession. Real GDP fell at an annual rate of 0.8 percent in the first quarter of 2001 despite a sharp increase in government investment, and indicators for the second quarter suggest the possibility of a further decline. The first-quarter weakness was widespread among components of private demand. Nonresidential investment fell about 4 percent at an annual rate from the high level reached late last year, and residential investment dropped at a rate of nearly 20 percent as the impact of temporary tax incentives has begun to fade. Consumption spending was flat despite a boost from purchases of consumer durables in advance of the introduction of recycling fees for household appliances in April. Both exports and imports fell, but the decline in exports, the first quarterly fall in two years, was particularly pronounced. Last year's

supplemental budget package resulted in a surge in government investment which added nearly 1½ percentage points to real GDP growth.

Japanese Real GDP

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

Component	1999 ¹	2000	2000			2001
			Q2	Q3	Q4	Q1
GDP	.4	2.5	.5	-2.7	2.6	-8
Total domestic demand	.5	2.5	.1	-2.5	4.2	.0
Consumption	-.4	1.5	.5	.1	-2.5	.0
Private investment	3.5	6.9	-11.7	5.3	27.6	-7.0
Public investment	-6.4	-7.5	17.0	-39.7	-2.3	22.3
Government consumption	4.1	3.7	5.0	2.2	3.6	.0
Inventories ²	.0	0.2	.2	-.1	.1	.0
Exports	7.0	9.8	17.1	.9	3.4	-13.7
Imports	10.3	11.1	16.5	5.3	22.1	-8.7
Net exports ²	-.1	.1	.5	-.3	-1.4	-.8

1. Q4/Q4.

2. Percentage point contribution to GDP growth, s.a.a.r.

April data indicate a further contraction. Industrial production fell 2 percent to a level about 3 percent below the first-quarter average, and the unemployment rate edged up as another fall in employment reversed all of the gain that occurred over the second half of last year. On the demand side, shipments of machinery also registered a steep decline, led by weaker demand in the electrical category that includes high-tech equipment. Machinery orders showed a surprisingly large gain in April, but were still about 2½ percent below the recent quarterly peak at the end of last year, consistent with further declines in investment. In addition, both residential and nonresidential building starts were well below their first-quarter levels in April. Household spending also appears to be weakening further, with April household expenditures 3 percent below their first-quarter level, and new passenger car registrations down about 2 percent over the same period.

Japanese Economic Indicators

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

Indicator	2000		2001				
	Q3	Q4	Q1	Feb.	Mar.	Apr.	May
Industrial production	1.3	.4	-3.3	.7	-2.0	-2.0	n.a.
All-industry index	.0	.5	.4	1.5	.4	n.a.	n.a.
Housing starts	-9	1.7	-4.0	-5.7	6.3	-5.8	n.a.
Machinery orders ¹	6.8	1.3	-7.0	3.0	-3.6	6.3	n.a.
Machinery shipments	1.1	1.4	-4.6	.2	-3.9	-3.6	n.a.
New car registrations	-2.9	-.6	2.6	-1.7	-2.3	.1	n.a.
Unemployment rate ²	4.6	4.8	4.8	4.7	4.7	4.8	n.a.
Job offers ratio ³	.62	.65	.63	.64	.61	.62	n.a.
Business sentiment ⁴	-15	-14	-22	...	...	...	...
CPI (Core, Tokyo area) ⁵	-.8	-.9	-1.0	-1.1	-1.1	-.9	-.9
Wholesale prices ⁵	.2	-.1	-.4	-.4	-.5	-.7	-.6

1. Private sector, excluding ships and electric power.

2. Percent.

3. Level of indicator.

4. Tankan survey, diffusion index.

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

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

Prices continue to decline. Core consumer goods prices in the Tokyo area (which exclude fresh food but include energy) were down 0.9 percent in May from a year earlier. Deflation in wholesale prices for domestic goods has intensified as the impact of the earlier run-up in energy prices has faded, with prices in May down 0.6 percent from a year earlier. Land prices also have continued to fall, with prices down 5 percent on average in January 2001 from a year earlier. This marked the tenth consecutive year of decline in prices for both residential and commercial property. The GDP deflator in the first quarter was a little more than 1 percent below its year-earlier level.

The merchandise trade surplus (customs clearance basis) averaged \$58 billion at an annual rate in the first five months of this year, about half the level in the same period in 2000. The declining trend in the surplus reflects the impact of higher oil prices as well as slowing global demand.

The Ministry of Finance's corporate survey showed a further deterioration in business sentiment in the second quarter, with the diffusion index for large corporations down to -12.1 percent from 1.2 percent in the first quarter. Sentiment also declined sharply for both small and medium-sized firms. The declines were generally more severe for manufacturers, but confidence fell for non-manufacturers as well.

Prime Minister Koizumi continues to enjoy high approval ratings, but some of the euphoria that surrounded his election has begun to fade. The government's Council on Economic and Fiscal Policy, which he chairs, recently released a draft of a seven-point program for reform, scheduled to be formally announced on June 27. Some elements, particularly a call for a reduction in public works spending and a review of taxes earmarked for special purposes such as road-building, are likely to face stiff opposition among entrenched interests in the ruling Liberal Democratic Party. The program reportedly will also include a proposal to urge big banks to sell bad loans to the Resolution and Collection Corporation (RCC) if they cannot eliminate them within two to three years, and will recommend that the RCC also be allowed to act as a trustee entity to manage the loans.

Real GDP in the **euro area** increased 2.2 percent (s.a.a.r.) in the first quarter, only slightly below the average pace of growth in the second half of last year, but with notably weak domestic demand. Consumption expenditures increased only 1.3 percent, following two quarters of very modest growth, while fixed investment spending fell 3.7 percent. Net exports contributed 2.4 percentage points to growth, primarily reflecting a sizable decline in imports. Growth remained subdued in Germany at only 1.5 percent; however, this was slightly stronger than in the second half of last year. In France, growth slowed from a 3 percent pace to 2 percent, as a rebound in consumption was offset by a large drawdown in inventories. Real GDP grew 3.4 percent in Italy, but the increase in large part reflected a buildup in inventories.

Euro-area consumer prices rose 0.4 percent in May from the previous month, primarily reflecting further increases in food and energy prices. The twelve-month rate of consumer price inflation in the euro area rose to 3.4 percent, the highest rate in eight years and remaining above the European Central Bank's 2 percent target ceiling for the twelfth consecutive month. The twelve-month rate of core inflation (which excludes food, energy, alcohol and tobacco prices) rose to 2.1 percent in May.

Incoming data indicate weaker activity in the current quarter. Industrial production declined 0.5 percent in April to a level slightly below the first-quarter

Euro-Area Real GDP¹						
(Percent change from previous period, except as noted, s.a.a.r.)						
Component	1999 ²	2000	2000			2001
			Q2	Q3	Q4	Q1
GDP	3.4	2.9	3.0	2.4	2.4	2.2
Total domestic demand	3.2	2.3	3.1	1.4	1.8	-.2
Consumption	2.9	2.0	3.5	.9	1.0	1.3
Investment	5.5	3.5	2.4	3.9	1.3	-3.7
Government consumption	1.7	1.9	1.4	.4	2.4	1.5
Inventories ³	.0	.0	0.3	-.1	0.4	-.4
Exports	10.1	11.6	10.0	12.3	12.5	.4
Imports	9.8	10.5	10.8	9.8	11.3	-5.9
Net exports ³	.3	.6	-.0	1.1	.7	2.4
<i>Memo:</i>						
France	3.8	2.9	2.7	3.2	3.1	2.0
Germany	2.5	2.6	4.8	1.1	.8	1.5
Italy	2.8	2.6	1.1	1.9	3.3	3.4

1. Includes Greece as of 2001 Q1.

2. Q4/Q4.

3. Percentage point contribution to GDP growth, s.a.a.r.

average. The euro-area purchasing managers' surveys for the manufacturing sector moved down further in May, remaining below the level that indicates a contraction in manufacturing activity for the second consecutive month. Service sector purchasing managers' surveys indicate continued expansion of activity in May, but at a much slower pace than a year ago. French consumption of manufactured products fell somewhat in April, reversing some of the strength early in the year.

Forward-looking indicators point to a subdued pace of activity in the months ahead. German manufacturing orders declined for the fourth consecutive month in April; both foreign and domestic orders have deteriorated. Euro-area industrial confidence declined further in May, reflecting more negative opinions on order books and levels of inventories. Euro-area consumer confidence continues to be somewhat more upbeat, but confidence slipped in May, retracing

some of the improvement from late last year, and largely reflecting increasing concerns over unemployment.

Labor market data for the euro area as a whole have yet to show deterioration, as the harmonized unemployment rate for the euro area edged down to 8.3 percent in April. Based on national statistics, the French unemployment rate was unchanged at 8.7 percent in April after moving down in the first quarter. In Germany, the unemployment rate has been unchanged at 9.3 percent from January through May, while the number of unemployed has increased over this period, reversing some of gains made in the second half of last year.

On May 10, the European Central Bank reduced its official interest rates 25 basis points, bringing the minimum bid rate for the main refinancing operation to 4.5 percent. This was the first change to official rates since they were raised 25 basis points last October. The ECB noted that after adjusting for distortions to annual M3 growth, monetary developments no longer pose a threat to price stability. The ECB also noted that although inflation in the near term will continue to be affected by temporary developments in food prices and the indirect effects of past increases in oil prices and depreciation of the euro, a moderation in real GDP growth is expected to dampen inflationary pressures in the medium term. At its June 7 meeting, the ECB left policy rates unchanged.

Euro-Area Economic Indicators¹

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

Indicator	2000		2001				
	Q3	Q4	Q1	Feb.	Mar.	Apr.	May
Industrial production ²	.9	1.5	-1	.6	-3	-.5	n.a.
Retail sales volume	.1	.5	.5	.1	-.4	n.a.	n.a.
Unemployment rate ³	8.8	8.5	8.4	8.4	8.4	8.3	n.a.
Consumer confidence ⁴	-.7	-2.7	-1.7	-2.0	-2.0	-2.0	-4.0
Industrial confidence ⁵	6.7	5.3	1.0	1.0	-1.0	-4.0	-5.0
Mfg. orders, Germany	.9	2.1	-2.8	-.4	-3.0	-1.1	n.a.
CPI ^{6,7}	2.5	2.7	2.5	2.6	2.6	2.9	3.4
Producer prices ^{6,7}	5.8	6.1	4.7	4.7	4.4	4.3	n.a.
M3 ⁸	5.3	5.1	5.1	4.8	5.1	5.2	n.a.

1. Euro-area indicators do not include Greece prior to 2001 but do include Greece as of January.

2. Excludes construction.

3. Euro-area standardized to ILO definition. Includes Eurostat estimates in some cases.

4. Diffusion index based on European Commission surveys in individual countries; Averages of responses to questions on financial situation, general economic situation, and purchasing attitudes.

5. Diffusion index based on European Commission surveys in individual countries; Averages of responses to questions on production expectations, orders, and stocks.

6. Percent change from year earlier.

7. Eurostat harmonized definition.

8. Eurostat harmonized definition, n.s.a., 12-month percent change.

n.a. Not available.

Economic activity in the **United Kingdom** continued to grow at a below-trend pace in the first quarter, with real GDP growth of only 1.7 percent (s.a.a.r.). Total domestic demand grew 3.7 percent, as fixed investment rose 4.7 percent and consumption expenditures increased 2.5 percent. Inventory accumulation added 1.2 percentage points to growth, while net exports subtracted 2 percentage points from growth. As in the previous quarter, the service sector remained robust, but industrial output contracted.

U.K. Real GDP						
(Percent change from previous period, except as noted, s.a.a.r.)						
Component	1999 ¹	2000	2000			2001
			Q2	Q3	Q4	Q1
GDP	3.2	2.6	3.6	3.4	1.6	1.7
Total domestic demand	4.2	2.9	5.4	4.2	1.1	3.7
Consumption	4.9	3.4	3.1	4.7	2.5	2.5
Investment	5.3	3.2	2.8	4.9	10.6	4.7
Government consumption	4.1	2.9	6.9	5.7	1.3	.6
Inventories ²	-.6	-.4	1.8	-.7	-2.7	1.2
Exports	7.2	8.7	12.1	3.9	9.7	4.3
Imports	9.5	8.8	16.8	6.0	6.9	8.9
Net exports ²	-1.1	-.5	-2.2	-1.0	.5	-2.0

1. Q4/Q4.

2. Percentage point contribution to GDP growth, s.a.a.r.

Indicators for the second quarter paint a mixed picture. Consumer confidence has ticked down in recent months but remains at a relatively high level. Retail sales remained strong in April and May; for the two months on average, sales are up 1.4 percent from the first-quarter average. Business confidence, on the other hand, has fallen over the first five months of 2001, with manufacturing confidence the lowest in over two years and industrial production declining 0.1 percent in April, slightly below its trend growth rate of zero. Foot and mouth disease, contained at this point, is expected to have only a modest effect on output in the tourism and transportation sectors this quarter.

Notwithstanding the recent slowing in activity, labor market conditions remain tight. The official claims-based unemployment rate remained at 3.2 percent in May, the lowest rate in 25 years, while the labor force survey measure of the unemployment rate declined to a record low of 5 percent for the three months centered in March. Average earnings growth in April ticked above the 4½ percent rate (from year earlier) that the Bank of England believes to be compatible with its inflation target, as demand for workers pushed up wage costs. In May, the twelve-month rate of retail price inflation (excluding mortgage interest payments) jumped to 2.4 percent, reflecting a rise in food prices.

U.K. Economic Indicators

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

Indicator	2000		2001				
	Q3	Q4	Q1	Feb.	Mar.	Apr.	May
Industrial production	.7	-6	-6	-.4	-.3	-.1	n.a.
Retail sales	1.4	1.3	1.6	.6	.3	.6	.9
Unemployment rate ¹							
Claims-based	3.5	3.4	3.3	3.3	3.3	3.2	3.2
Labor force survey ²	5.4	5.3	5.1	5.1	5.0	n.a.	n.a.
Business confidence ³	3.3	5.3	8.7	9.0	3.0	-2.0	-2.0
Retail prices ⁴	2.1	2.1	1.9	1.9	1.9	2.0	2.4
Producer input prices ⁵	12.1	9.9	4.9	5.5	2.6	6.7	4.7
Average earnings ⁵	4.1	4.4	5.1	6.6	4.3	4.7	n.a.

1. Percent.

2. Three-month average centered on month shown.

3. Percentage of firms expecting output to increase in the next four months less percentage expecting output to decrease.

4. Excluding mortgage interest payments. Percent change from year earlier.

5. Percent change from year earlier.

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

At its June 6, 2001 meeting, the Monetary Policy Committee of the Bank of England voted to keep the official repo rate at 5.25 percent. The repo rate has been cut 75 basis points since the beginning of this year.

Britain's Labour Party led by Prime Minister Tony Blair won a majority in the general elections held on June 7. Prime Minister Blair indicated that if his government were to pursue EMU entry in the near term (Labour ran on a pro-EMU platform), the whole process should be completed before the next election, which would imply that a referendum on EMU entry would have to take place by early 2003.

Real GDP in **Canada** rose a stronger-than-expected 2.5 percent (s.a.a.r.) in the first quarter, up from a growth rate of 1.6 percent in the fourth quarter of 2000. After growing 1.2 percent in the fourth quarter, consumer spending rose 3.6 percent, led by purchases of durables goods. Government spending also picked up from its 2000 pace, rising 4.8 percent in the quarter. However, despite a boom in residential investment, fixed investment continued to decline, reflecting a broad-based decline in machinery and equipment investment. Inventory

investment also slowed further, subtracting 1 percentage point from growth. Exports fell by 5.7 percent, with rising exports of energy products offset by large declines in exports of machinery and equipment and motor vehicles. Mainly as a result of a substantial decline in imports, however, net exports added nearly 2 percentage points to first-quarter growth.

Canadian Real GDP

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

Component	1999 ¹	2000	2000			2001
			Q2	Q3	Q4	Q1
GDP	5.1	3.5	1.9	4.5	1.6	2.5
Total domestic demand	5.7	2.7	3.2	3.7	-1.3	1.0
Consumption	4.2	3.3	3.3	5.2	1.2	3.6
Investment	9.6	3.6	4.0	2.7	-1.2	-3.9
Government consumption	2.7	2.3	2.7	1.2	3.5	4.8
Inventories ²	.6	-.4	-.1	-.1	-2.3	-1.1
Exports	8.7	4.3	3.0	1.2	-.1	-5.7
Imports	10.4	2.1	7.3	-.3	-9.1	-11.0
Net exports ²	-.2	1.1	-1.5	.6	3.8	1.9

1. Q4/Q4.

2. Percentage point contribution to GDP growth, s.a.a.r.

Limited available data for the current quarter suggest the Canadian economy likely slowed from the first quarter pace. Data on housing starts through May suggest residential investment has cooled. The manufacturing sector continues to be weak, with manufacturing shipments declining in April and manufacturing employment falling on average in April and May. Consumer confidence continued to decline in the first quarter, suggesting consumption growth may slow in the second quarter.

The twelve-month rate of consumer price inflation was 3.9 percent in May, above the ceiling of the Bank of Canada's 1 percent to 3 percent target range for the second consecutive month. Higher energy and food prices continued to account for much of the increase in consumer prices, as the twelve-month core rate of inflation (which excludes food and energy prices) was a more moderate 2.1 percent.

Canadian Economic Indicators

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

Indicator	2000		2001				
	Q3	Q4	Q1	Feb.	Mar.	Apr.	May
GDP at factor cost	.9	.5	.3	-.1	.1	n.a.	n.a.
Industrial production	.7	-.1	-.9	-.1	.4	n.a.	n.a.
New mfg. orders	1.9	.2	-5.1	3.7	-3.5	1.7	n.a.
Retail sales	2.5	.1	1.1	-.3	.3	n.a.	n.a.
Employment	.2	.7	.2	-.2	.2	.2	.1
Unemployment rate ¹	6.9	6.9	6.9	6.9	7.0	7.0	7.0
Consumer prices ²	2.7	3.1	2.8	2.9	2.5	3.6	3.9
Consumer attitudes ³	119.8	114.2	109.4	...	...	...	...
Business confidence ⁴	149.4	140.4	117.5	...	...	...	...

1. Percent.

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

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

3. Level of index, 1991 = 100.

4. Level of index, 1977 = 100.

The Bank of Canada has lowered its policy rate, the Bank Rate, a total of 125 basis points this year, most recently by 25 basis points on May 29. The Bank Rate now stands at 4.75 percent. In its May 29 statement, the Bank singled out a pace of economic expansion that was currently below trend as justification for the rate reduction. The Bank reaffirmed its view that the main risk to the Canadian outlook is the possibility of a longer-than-anticipated economic slowdown in the United States, but also mentioned that "given the sustained increases in energy prices, the Bank will need to be vigilant for signs of broader effects on consumer prices generally." The Bank's next policy announcement date is July 17.

External Balances
(Billions of U.S. dollars, s.a.a.r.)

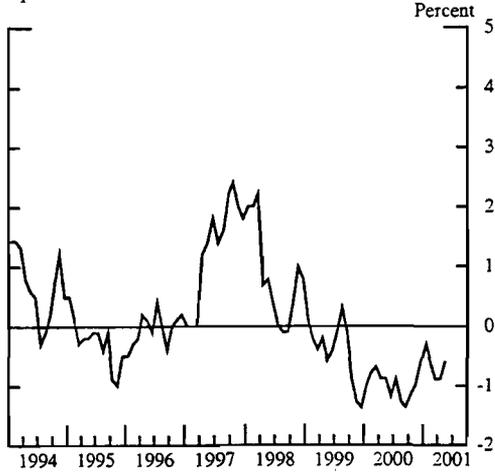
Country and balance	2000		2001			
	Q3	Q4	Q1	Mar.	Apr.	May
<i>Japan</i>						
Trade	102.3	67.9	67.6	79.0	59.3	28.4
Current account	118.5	99.4	101.5	72.3	99.6	n.a.
<i>Euro area</i>						
Trade ¹	17.8	3.4	-16.1	34.9	-32.1	n.a.
Current account ¹	-22.4	-48.8	-34.5	-30.1	n.a.	n.a.
<i>Germany</i>						
Trade	48.9	39.2	75.5	89.2	53.1	n.a.
Current account	-39.4	-33.9	-3.7	33.8	16.1	n.a.
<i>France</i>						
Trade	-4.2	-5.5	6.2	8.6	-5.2	n.a.
Current account	4.2	2.1	4.0	5.0	n.a.	n.a.
<i>Italy</i>						
Trade	-1.9	0.7	8.9	8.2	n.a.	n.a.
Current account ¹	9.4	-9.6	-8.7	-2.0	-6.1	n.a.
<i>United Kingdom</i>						
Trade	-43.7	-44.2	-43.4	-48.1	-49.6	n.a.
Current Account	-23.9	-21.4	n.a.	...	...	...
<i>Canada</i>						
Trade	36.9	41.0	49.6	47.5	n.a.	n.a.
Current Account	18.6	22.4	33.3	...	...	...

1. Not seasonally adjusted.

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

Consumer Price Inflation in Selected Industrial Countries
(12-month change)

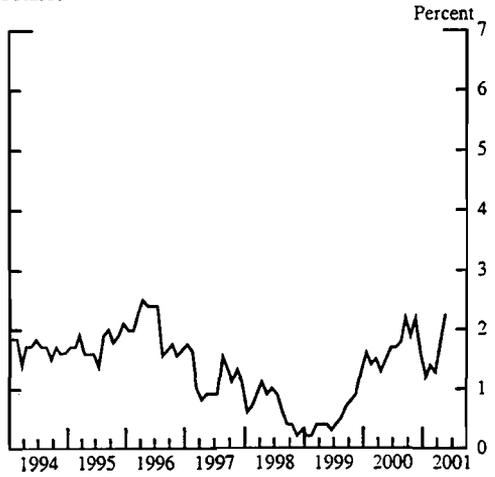
Japan



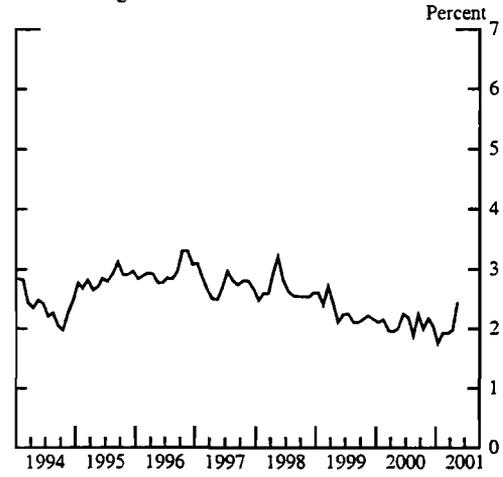
Germany



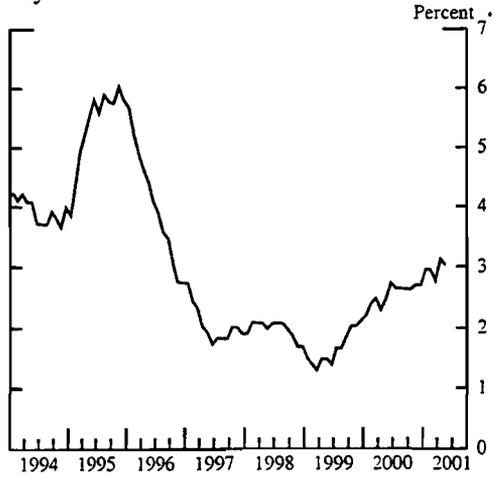
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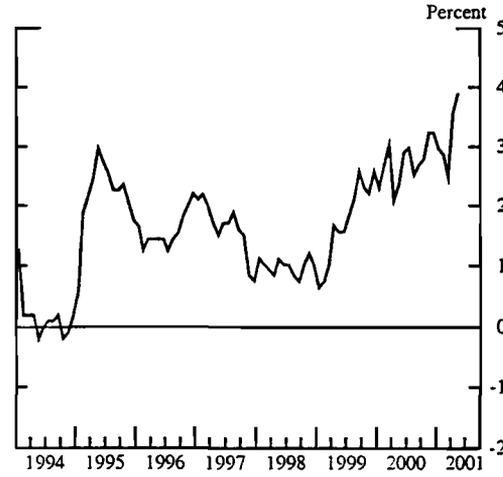
United Kingdom



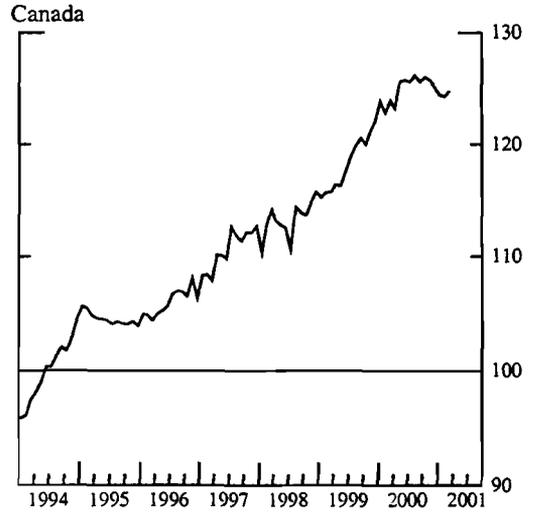
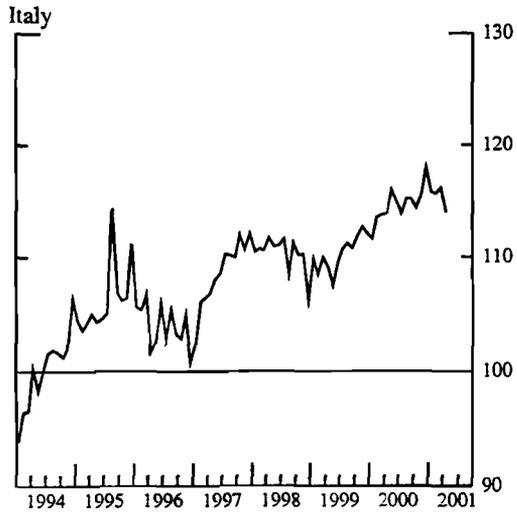
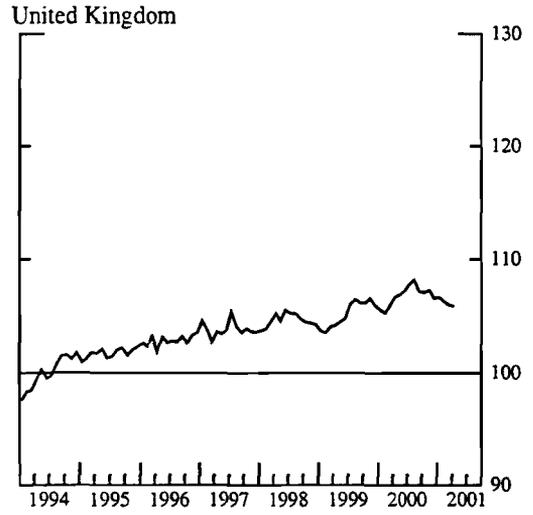
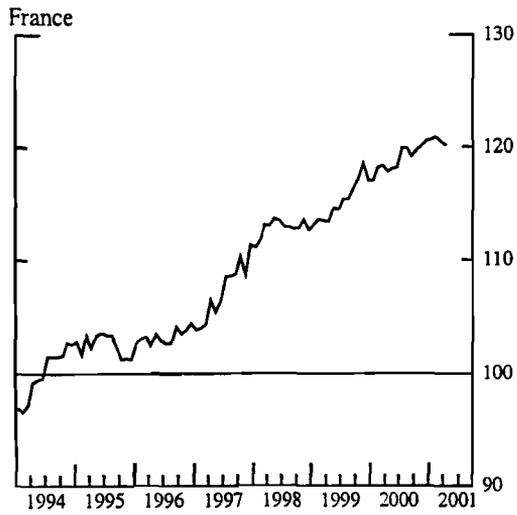
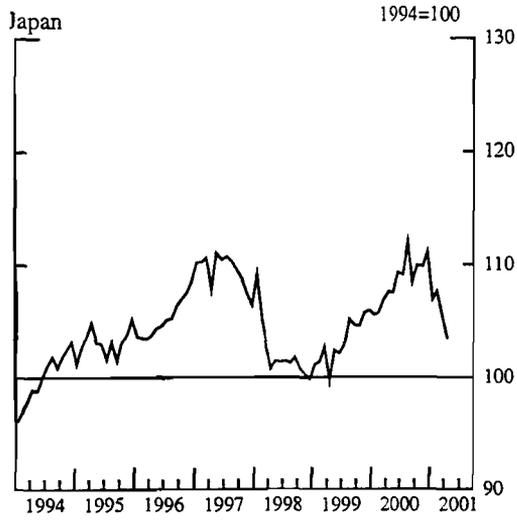
Italy



Canada



Industrial Production in Selected Industrial Countries



Economic Situation in Other Countries

In the major developing countries, the overall pace of economic growth has recently declined, reflecting sluggish external demand and weak domestic conditions. Recent data on real GDP, industrial production, and especially exports have shown slowing or outright declines in most countries. Inflation remains subdued, with some isolated exceptions.

In **Argentina**, data since the last Greenbook provide little indication that a concerted recovery is underway. Industrial production climbed for the second consecutive month in April; however, the April gain was concentrated almost entirely in a few industries—rubber, plastics, and chemicals. Inflation, as measured over the past twelve months, also turned positive for the first time since February 1999, but special factors—including an increase in the tariff rate on consumption goods—were largely responsible for this rise. Tax receipts jumped in May following weak April returns, mostly reflecting gains from the newly implemented tax on financial transactions and taxes on revenues from Argentina's largest oil producer. Revenues from the VAT fell year on year, however, suggesting continued weak economic activity. Consumer confidence fell in May but picked up somewhat in early June in the aftermath of the successful debt swap. The trade balance remained positive again in April, as exports rose and imports were flat.

On June 4, the Argentine government announced the results of a "mega" debt exchange. In the exchange, the Argentine government traded \$29.5 billion in old debt for \$30.4 billion in new bonds, with higher-than-expected foreign participation of about \$8 billion. The average life of the new debt was roughly three years longer than that of the previous bonds, and the exchange generated about \$16 billion in cash flow savings through 2005. While the exchange lightened the financing burden in the near term, it was fairly costly, with yields of up to 16 percent.

Further policy changes were announced by Argentine Finance Minister Cavallo on June 15. Of the changes, market attention focused primarily on a controversial exchange-rate-based system of import taxes and export subsidies. The system establishes an "equivalent transaction rate" on all traded goods except liquid fuels. The transaction rate is calculated on a daily basis as the difference between the exchange rate that would prevail under the "Enhanced Convertibility Law," in which a peso is backed by a simple average of one dollar and one euro, and the exchange rate of one peso per dollar. The transaction rate is currently between 7 and 8 percent. Exporters receive a subsidy equal to the transaction rate, while importers pay a tax equal to that rate. Other less contentious measures included changes to the tax code designed to combat tax

evasion and boost domestic demand. Immediate reaction to the announcement was not positive, with analysts expressing intensified doubts about Argentina's commitment to its currency board arrangement.

Argentine Economic Indicators

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	-6	-2.0	1.4	n.a.	...	...	...
Industrial production	-6.0	1.8	2.1	4.8	2.4	2.1	n.a.
Unemployment rate ²	13.8	15.1	14.7	...	...	...	n.a.
Consumer prices ³	-1.8	-.7	-.6	-1.5	-1.4	-.6	.3
Trade balance ⁴	-.8	2.5	3.5	3.4	1.2	3.5	n.a.
Current account ⁵	-12.4	-9.4	-9.0	n.a.	...	...	...

1. Annual rate. Annual figures are Q4/Q4.

2. Percent, n.s.a. Data are released for May and October only. Figures for Q4 reflect data for October.

3. Percent change from year-earlier period, except annual figures, 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 **Mexico**, economic activity continued to fall, largely reflecting weak external demand. Real GDP fell nearly 1½ percent (s.a.a.r.) in the first quarter, the second consecutive quarterly decline, and industrial production decreased slightly further in April. Exports fell over 4 percent (s.a.) in April, leading to a sharp increase in the trade deficit. However, the current account deficit in the first quarter narrowed slightly to about \$18 billion (a.r.) relative to its value in the same quarter a year ago, as four-quarter import growth slowed sharply. Inflation has remained subdued, with twelve-month consumer price inflation coming in at 7 percent in May, only slightly above the year-end target of 6½ percent.

In an environment with a very strong peso, declining inflation, and weak economic activity, the Bank of Mexico (BOM) loosened monetary policy towards the end of May for the first time in three years. Concurrently, the BOM also announced two changes in its mechanisms for foreign exchange operations. First, it suspended its monthly auctions of U.S. dollar put options, which was its preferred method of building up foreign exchange reserves. Second, the BOM announced that it will be suspending from July the automatic intervention that comes into play if the peso depreciates 2 percent or more in a single day.

Getting rid of the "2-percent rule" will let the peso change more freely in response to downward market pressures.

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

Indicator	1999	2000	2000	2001				
			Q4	Q1	Mar.	Apr.	May	
Real GDP ¹	5.5	5.2	-2.4	-1.4	...	...	...	...
Industrial production	4.5	6.3	-1.4	-1.6	-1.0	-2	n.a.	n.a.
Unemployment rate ²	2.5	2.2	2.2	2.3	2.3	2.2	n.a.	n.a.
Consumer prices ³	12.3	9.0	8.9	7.5	7.2	7.1	7.0	7.0
Trade balance ⁴	-5.6	-8.0	-8.5	-9.1	-9.2	-16.2	n.a.	n.a.
Imports ⁴	142.0	174.5	180.8	177.1	177.6	177.4	n.a.	n.a.
Exports ⁴	136.4	166.4	172.3	168.0	168.4	161.2	n.a.	n.a.
Current account ⁵	-13.7	-17.7	-25.1	-17.6	...	...	...	...

1. Annual rate. Annual figures 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 figures, 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 since the last Greenbook have pointed to a slowdown in economic activity. Real GDP growth slowed in the first quarter to 0.4 percent (s.a.a.r.). Industrial production declined nearly 2 percent over the March-April period, and unemployment edged up in April. The trade deficit widened despite the slowdown. Inflation also rose, driven by rises in food prices, depreciation of the *real*, hikes in transportation costs, and liberalization of some fuel prices.

The *real*, which has depreciated 20 percent since the beginning of the year, continued to move lower over the inter-meeting period as a result of adverse spillovers from Argentina, an energy crisis, and political troubles at home. In mid-May, the government announced an energy rationing scheme to be put in place for much of the country over the second half of this year in response to dangerously low levels of water. (Eighty-five percent of Brazil's electricity comes from hydropower.)

The central bank reacted to the rise in inflationary pressures and the weakness of the *real* by raising the overnight interest rate, the Selic, by 50 basis points to 16.75 percent. This action brought the cumulative rate increase since March to 150 basis points. The primary fiscal surplus over the first four months of this year exceeded the target envisioned in Brazil's IMF program. However, the rise in the Selic and the depreciation of the *real* have greatly raised the government's debt servicing costs, because most of the government's debt is linked to the Selic or to foreign currencies. Brazil's government nevertheless announced that it would not renew its IMF program when it expires at the end of 2001.

Brazilian Economic Indicators

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	3.5	4.7	1.0	.4	...	...	...
Industrial production	-7	6.5	4.0	1.9	-5	-1.6	n.a.
Unemployment rate ²	7.6	7.1	6.7	5.7	5.9	6.1	n.a.
Consumer prices ³	8.9	6.0	6.2	6.2	6.4	6.6	7.0
Trade balance ⁴	-1.2	-.7	-1.5	-.9	-2.9	-2.6	-6.0
Current account ⁵	-25.4	-24.6	-35.6	-26.2	-31.1	-31.5	n.a.

1. Annual rate. Annual figures are Q4/Q4.

2. Percent. "Open" unemployment rate.

3. Percent change from year-earlier period, except annual figures, which are Dec./Dec. Price index is IPC-A.

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**, real GDP rose less than 1 percent in the first quarter, after soaring in the fourth quarter of last year. The high price of oil and government spending are still the main drivers of the economy, although some strength has been seen in the non-oil sectors, particularly in the communication industry. The current account balance showed a smaller surplus in the first quarter, reflecting lower oil exports and a rise in imports. Inflation ticked up in May.

Venezuelan Economic Indicators

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	-4.1	6.1	10.3	.6	...	...	...
Unemployment rate ²	15.2	13.4	11.4	14.2	13.7	n.a.	n.a.
Consumer prices ³	19.5	13.4	14.2	12.4	11.1	10.6	11.2
Non-oil trade balance ⁴	-9.1	-10.8	-11.9	-10.2	...	...	...
Trade balance ⁴	7.6	18.0	17.6	16.8	...	...	...
Current account ⁵	3.7	13.4	15.7	10.5	...	...	...

1. Annual rate. Annual figures are Q4/Q4.

2. Percent, n.s.a.

3. Percent change from year-earlier period, except annual figures, 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 **Korea**, recent indicators suggest that activity has remained weak. Real GDP increased only slightly in the first quarter, not quite reversing the decline of the previous quarter. Consumption was particularly weak in the first quarter, and only a surprising boost from net exports kept overall growth positive. Industrial output fell in April after three consecutive months of increase, depressed by declines in production of semiconductors and office equipment. Inventories rose in April, pushing the inventory to sales ratio up further. Recent readings of forward-looking indicators of activity have been somewhat less bleak, with indexes of both business and consumer sentiment remaining well above their low points of late last year.

Despite the ongoing weakness of economic activity, twelve-month consumer price inflation has risen in recent months, reflecting in large part the delayed impact of earlier depreciation of the won and higher energy prices, as well as unusually sharp seasonal jumps in some agricultural prices. With inflation well above its 2-4 percent target range, the Bank of Korea has not lowered its target interest rate since February, despite the weakness of economic activity.

Korean Economic Indicators

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	13.8	5.2	-1.7	1.2	...	...	...
Industrial production	24.1	17.0	-3.3	.6	.4	-1.3	n.a.
Unemployment rate ²	6.3	4.1	3.9	4.2	4.2	3.8	3.6
Consumer prices ³	1.3	3.1	2.8	4.2	4.4	5.3	5.5
Trade balance ⁴	28.4	16.6	14.7	20.7	24.6	13.6	n.a.
Current account ⁵	24.5	11.0	13.3	12.6	21.7	7.6	n.a.

1. Annual rate. Annual figures are Q4/Q4.

2. Percent.

3. Percent change from year earlier, except annual changes, 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 the ASEAN region, recent data have been mixed. Both Indonesia and Malaysia registered strong GDP growth in the first quarter, while the Philippines posted negative growth and Singapore GDP plummeted more than 10 percent (s.a.a.r.). Industrial production fell throughout the region, and recent monthly production data generally point to further weakness.

Recent trade data have shown declines in both exports and imports. Exports were below their year-ago levels in almost every country, with electronics exports being the hardest hit. The fall in imports primarily reflected a drop in demand for components used in the production of high-tech exports. Inflation has remained quite well contained in the region, with the notable exception of Indonesia.

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

Indicator and country	1999	2000	2000	2001			
			Q4	Q1	Feb.	Mar.	Apr.
<i>Real GDP¹</i>							
Indonesia	5.8	5.3	-3.8	13.9	...	...	...
Malaysia	11.0	6.3	3.8	5.6	...	...	...
Philippines	5.1	3.9	1.8	-2.1	...	...	...
Singapore	8.0	11.0	10.3	-11.4	...	...	...
Thailand	6.7	3.0	3.9	-1.0	...	...	...
<i>Industrial production²</i>							
Indonesia ³	-9	11.6	-4.6	-.4	9.0	1.0	n.a.
Malaysia	9.1	19.2	.8	-3.5	-2.8	-.4	-1.7
Philippines	3.6	13.0	5.6	-17.2	-2.7	.0	n.a.
Singapore	13.9	15.2	4.6	-10.4	13.5	-9.6	-4.1
Thailand	12.5	3.1	2.9	-1.9	-1	-2.3	..3

1. Annual rate. Annual figures are Q4/Q4.

2. Annual figures are annual averages.

3. Staff estimate.

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

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

Country	1999	2000	2000	2001			
			Q4	Q1	Feb.	Mar.	Apr.
Indonesia	24.7	28.6	23.1	24.7	23.9	25.1	23.0
Malaysia	19.1	16.0	17.6	16.6	26.4	9.7	17.0
Philippines	4.3	6.6	8.3	6.3	6.9	3.6	n.a.
Singapore	3.6	3.3	4.6	8.2	3.2	7.1	.6
Thailand	9.3	5.5	2.2	-1.3	-.8	.2	3.9

n.a. Not available.

ASEAN Economic Indicators: CPI Inflation

(Percent change from year earlier, except as noted)

Country	1999 ¹	2000 ¹	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Indonesia	2.0	9.3	8.8	9.3	10.6	10.5	10.8
Malaysia	2.5	1.3	1.7	1.6	1.6	1.6	1.6
Philippines	4.3	6.6	5.9	6.8	6.7	6.7	6.5
Singapore	.9	2.1	2.0	1.7	1.8	2.0	n.a.
Thailand	.7	1.3	1.6	1.4	1.4	2.6	2.8

1. December/December.

n.a. Not available.

In **China**, recent indicators suggest that growth has moderated from its rapid pace in the first quarter. Industrial output rose 10.2 percent in May from the same month last year, somewhat slower than the twelve-month growth rates registered earlier this year. China has begun to feel the impact of the global slowdown, with exports falling in both April and May. Imports have also weakened, largely reflecting the high import content of Chinese exports. Robust domestic demand continued to support growth, however, with indicators of consumer and investment spending remaining strong. Investment was boosted by increased government spending on infrastructure and a pickup in inflows of foreign direct investment. Partly reflecting the strength of domestic demand, the twelve-month inflation rate moved up to 1.7 percent in May, the highest rate in nearly four years.

Chinese Economic Indicators

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	6.2	7.4	7.5	12.3	...	...	...
Industrial production ²	8.0	11.4	10.8	11.2	12.1	11.5	10.2
Consumer prices ²	-1.0	1.5	.9	.7	.8	1.6	1.7
Trade balance ³	29.2	24.1	21.4	18.6	36.5	19.0	20.1

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

2. Percent change from year earlier. Annual figures are year over year.

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

... Not applicable.

In **Hong Kong**, real GDP rose 1.2 percent (s.a.a.r.) in the first quarter, with increased private consumption being roughly offset by a drop in exports. Consumer spending was boosted by unusually large year-end bonuses for 2000, which were paid out in early 2001. Exports continued to slide in April, falling to a level about 7 percent (s.a.) below their first-quarter average. The unemployment rate remained unchanged at 4.6 percent (s.a.) in the March-May period. The twelve-month rate of decline in consumer prices eased further in April, as prices ticked up on a seasonally adjusted basis. In an effort to revive the depressed property market, the government recently announced measures to curb the supply of new housing.

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	9.3	6.6	1.2	1.2	...	...	...
Unemployment rate ²	6.1	5.0	4.4	4.6	4.6	4.6	4.6
Consumer prices ³	-4.0	-2.1	-2.5	-2.0	-2.0	-1.4	n.a.
Trade balance ⁴	-5.6	-11.0	-13.7	-10.9	-7.0	-11.6	n.a.

1. Annual rate. Annual figures are Q4/Q4.

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

3. Percent change from year-earlier period, except annual figures, 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**, weak global demand for high-technology products, compounded by the increasing trend for Taiwanese firms to move their production to China to reduce production costs, continued to weigh on economic activity. Real GDP fell 2.7 percent (s.a.a.r.) in the first quarter, dragged down by plunging real exports and business investment spending. Private consumption was essentially flat, reflecting the dampening effects of deteriorating labor market conditions. More recent data point to further declines in economic activity, with industrial production falling 4.4 percent (s.a.) and the unemployment rate rising to 4.3 percent in April. In addition, exports tumbled 12 percent (s.a.) in May, pulled down by sharply lower exports of electronics and information technology products. Imports fell even more, led by a plunge in capital goods imports. Consumer prices fell slightly in May on a twelve-month basis. In response to the latest signs of economic weakness, Taiwan's central bank has cut interest rates 25 basis points since the last Greenbook, and the legislature has passed a fiscal stimulus package to boost public infrastructure spending.

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

Indicator	1999	2000	2000	2001			
			Q4	Q1	Mar.	Apr.	May
Real GDP ¹	6.5	4.1	.4	-2.7	...	...	...
Unemployment rate	2.9	3.0	3.2	3.8	4.1	4.3	n.a.
Industrial production ²	7.7	7.4	-3.1	-3.8	-9.1	-4.4	n.a.
Consumer prices ³	.1	1.7	1.6	.6	.4	.4	-2
Trade balance ⁴	10.9	8.3	13.2	17.1	21.6	8.8	11.2
Current account ⁵	8.4	9.3	15.9	15.8	...	...	...

1. Annual rate. Annual figures are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual figures, 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.