*Nevada County Economic Resource Council*
*Grass Valley Chamber of Commerce*
*Citizens Bank of Nevada County*

Grass Valley/Nevada County
Chamber of Commerce

# Fed in Brief

## *Grass Valley, CA*

## *June 13, 2007*


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**Federal Reserve Bank of San Francisco**

# *Overview*

I. Monetary policy overview

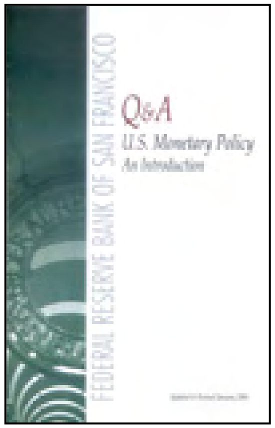
II. National economy

III. FRBSF national forecast

IV. Potential risks to the forecast

# *I. U.S. Monetary Policy*: Two Goals

- **Monetary Policy Goals**
  - "to promote **'maximum' sustainable output** and **employment** and to promote **'stable' prices**."




*U.S. Monetary Policy: An Introduction.* (2004) Federal Reserve Bank of San Francisco, page 5.

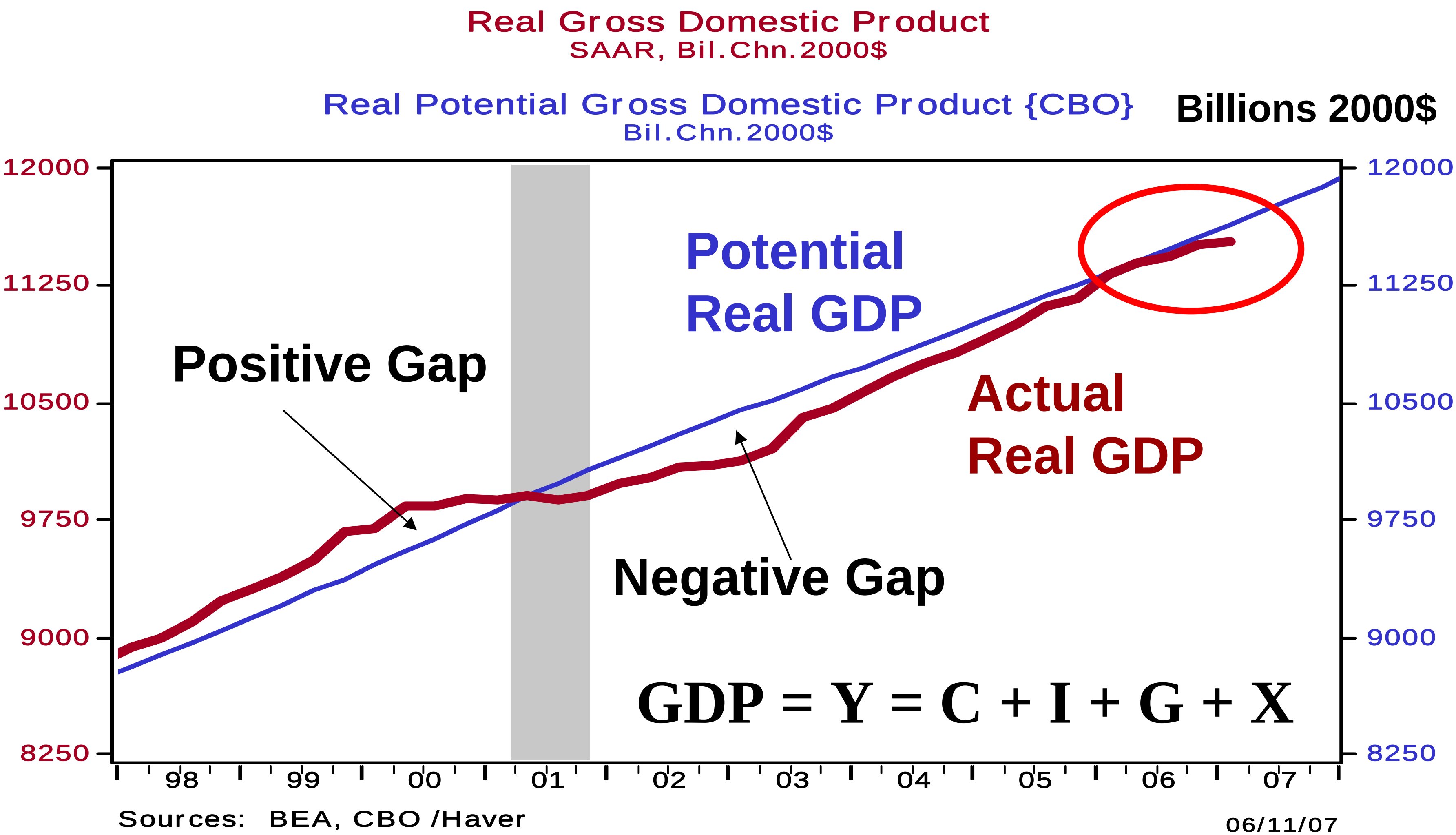
# *The FOMC Statement:* A Second Policy Instrument

- **The FOMC Statement has become a second policy instrument**—wording of the statement:
  - Affects expectations about future fed funds rates
  - Influences long-term interest rates
  - Articulates balance of risks
- Released at 2:15 p.m. (Eastern) after meeting
- *Next meeting: June 27-28, 2007*

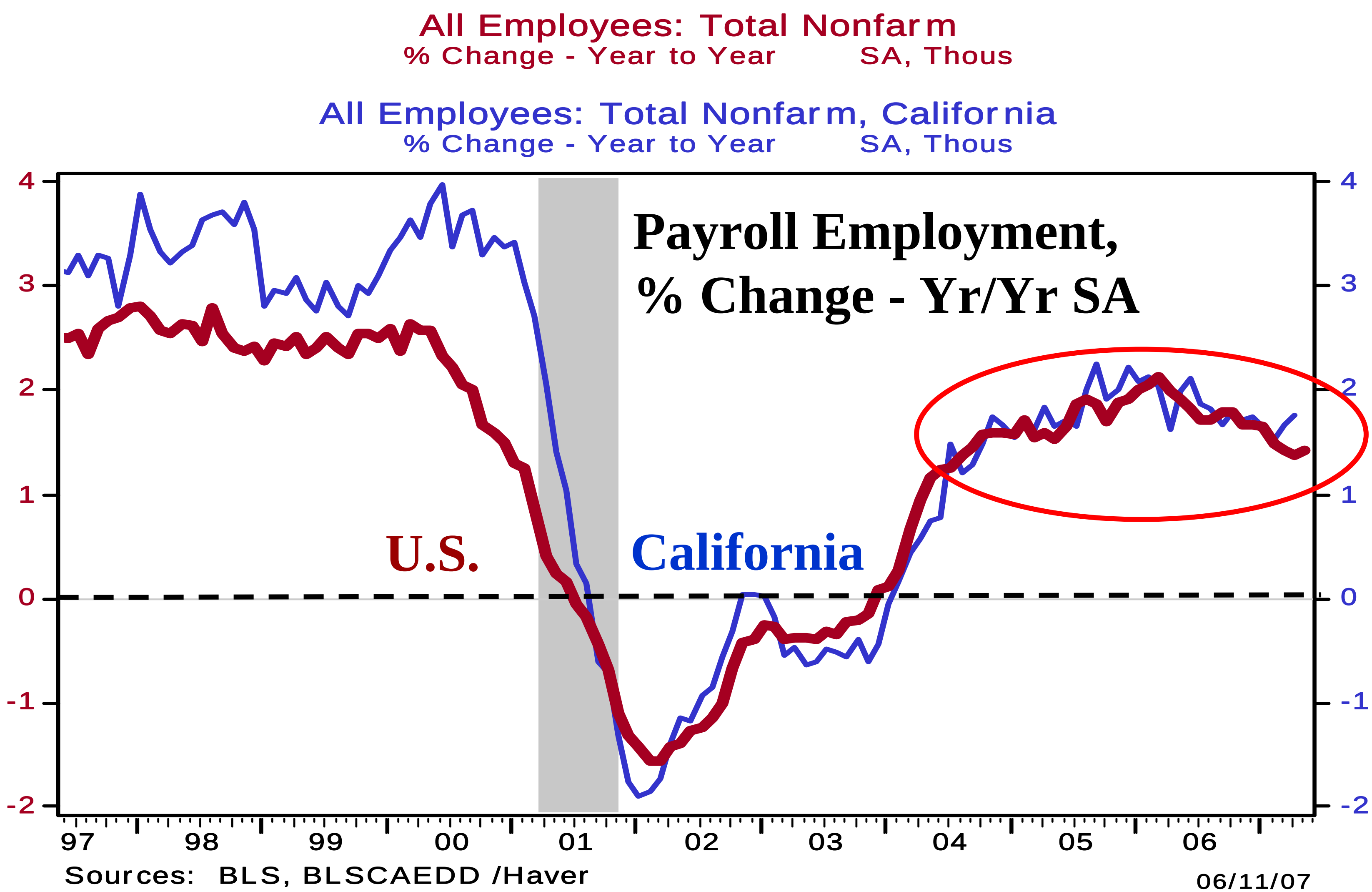
# *II. Big Picture:* Bimodal Economy

- ***Real Gross Domestic Product* (*Output*)**
  – Real GDP growth rate slow to a 0.6% annual rate in 2007:Q1 (preliminary estimate)
  – Reduced growth from housing, inventories, and imports
  – Most of the economy remains on track
- ***Labor market (Jobs)***
  – Still tight, but signs of softening emerge
  – Added 157,000 jobs in May
    - Monthly average of 133,000 in first 5 months of 2007
    - Compared to a monthly average of nearly 190,000 for all of 2006
  – Unemployment rate held at 4.5% in May

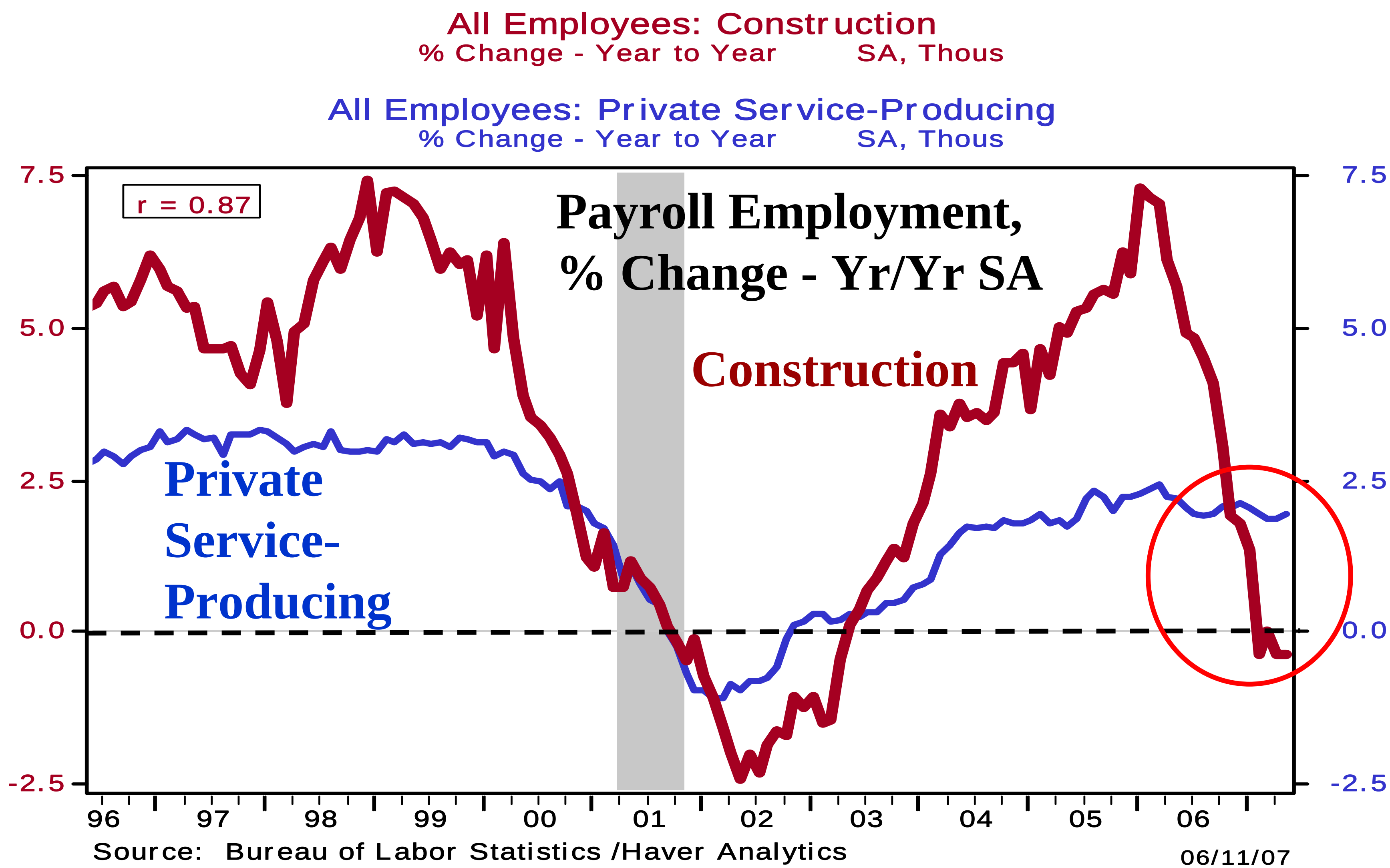
# *U.S. Economic Output*: Real GDP Is Close to Estimated Potential (with core inflation above 'comfort zone')



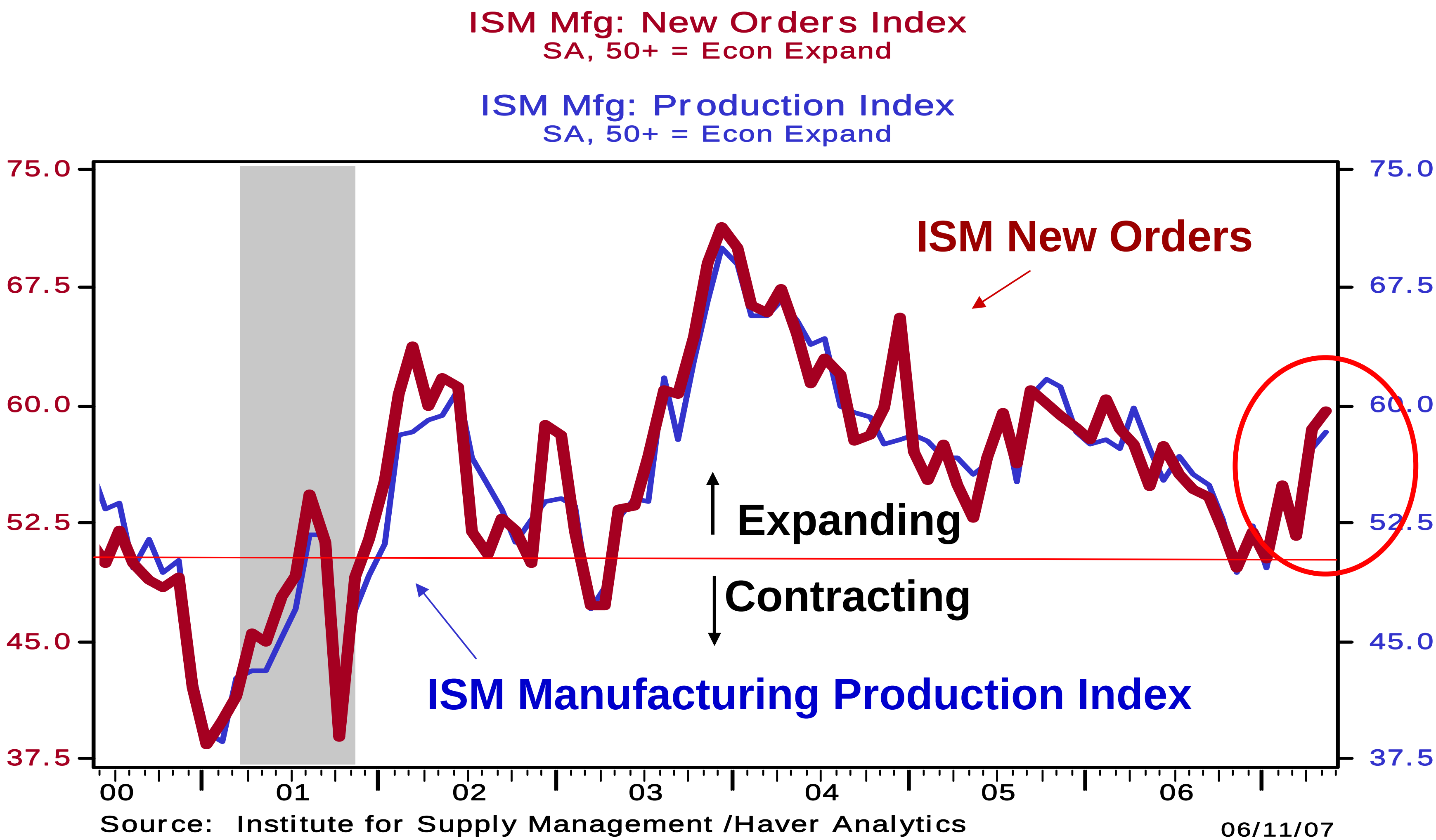
# *Payroll Employment Growth Rate:* California Is Mostly on Pace with the Nation



# *Payroll Employment Growth Rate:* Losses in Construction; Services Strong



# *Manufacturing Production* — Both New Orders and Production Edge Upward

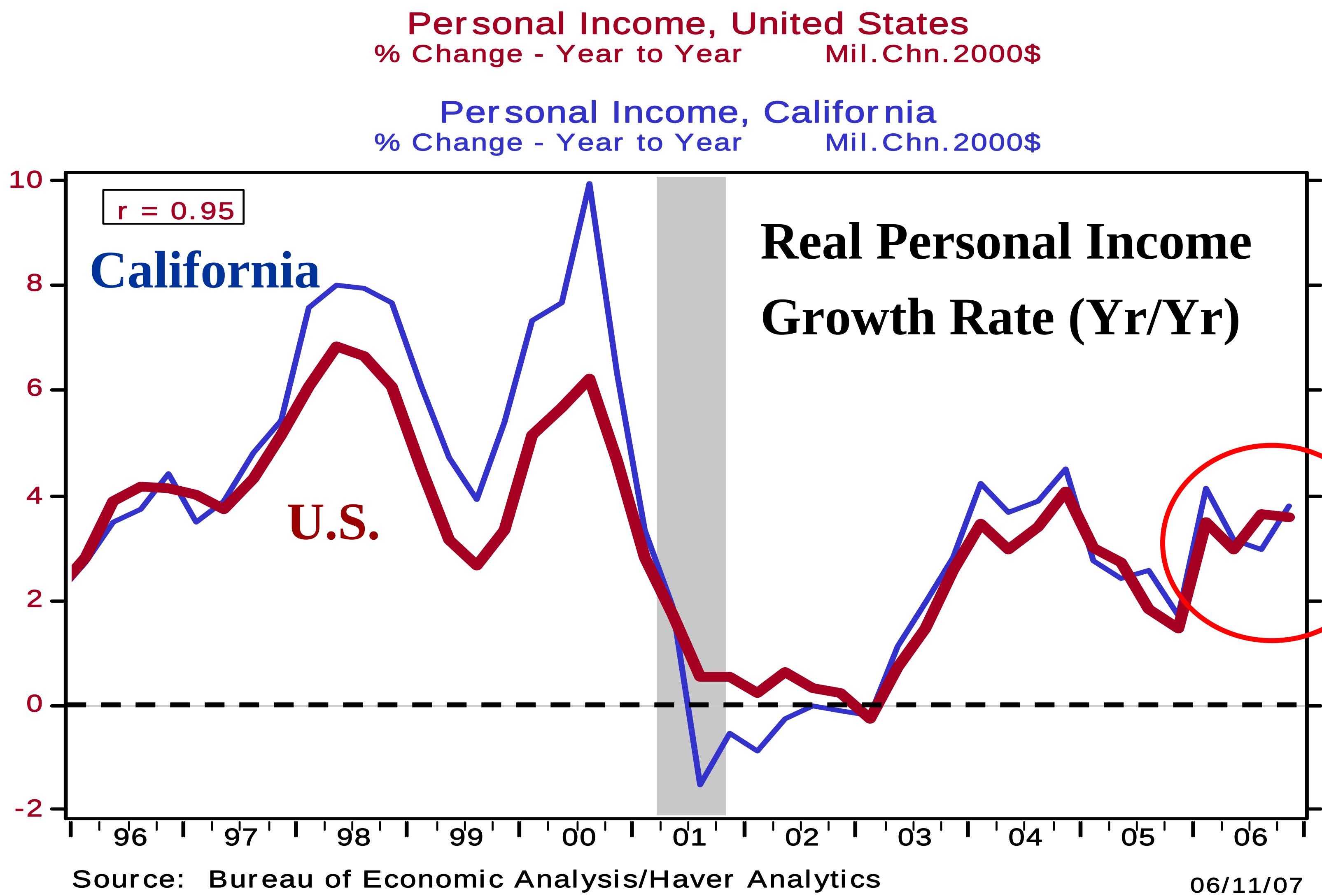


# *Consumer Sector:*
# Spending Remains Strong

- **Consumption growth – main source of GDP growth in 2007:Q1. Fueled by:**
  - Gains in real incomes
  - Low interest rates
  - Past gains in housing wealth

- **Going forward, growth might be limited by:**
  - Higher energy costs
  - Softening in the housing market

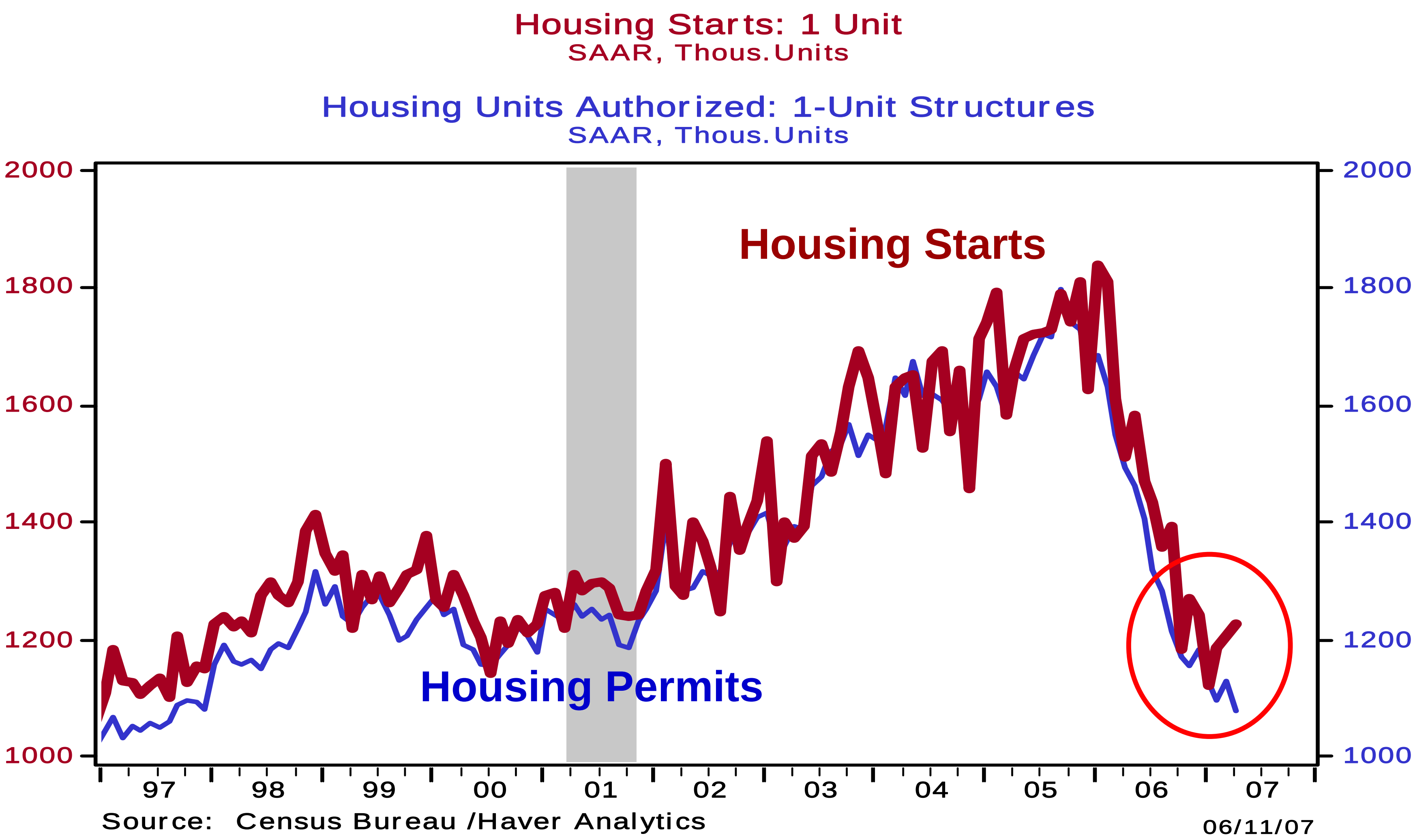
# *Personal Income Growth :*
# California Compares Well with the Nation



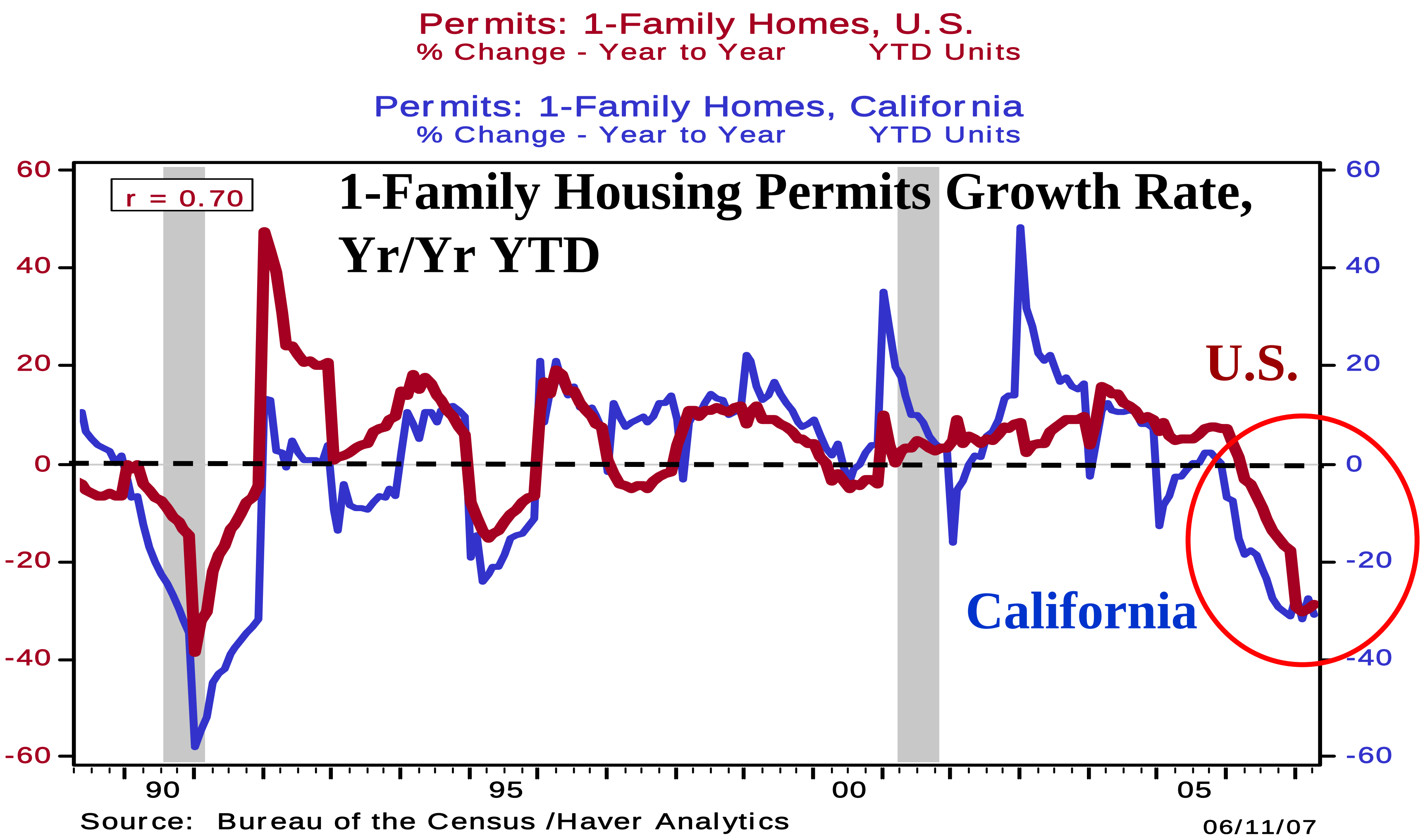
# *Investment Spending:* Housing Continues to Dampen Growth

- **Residential fixed investment remains weak**
  - Contracted by 15.4% at annual rate in 2007:Q1
  - Knocked off 0.9 percentage point from annualized GDP growth for the quarter
- **Business fixed investment growth was revised upwards to 2.9%**

# *Housing Market:*
# New Permits Fall, but Starts Rise



# *New Housing Activity:* U.S. and California Record Similar Declines



# *III. Forecasts for the National Economy*

## *Outlook for 2007 and 2008*

- **FRBSF *FedViews* Forecast:**
  - Available at www.frbsf.org

- ***Blue Chip Consensus Forecast* comparison:**
  - Survey of 50 forecasters

Fed Views

# *U.S. Output Forecast:* Projected Moderate Real GDP Growth

## *FedViews*: Below trend real GDP growth expected

- Expected real GDP growth is about 2.5% annual rate for 2007:H2 and 2008
- Growth outlook has more uncertainty.

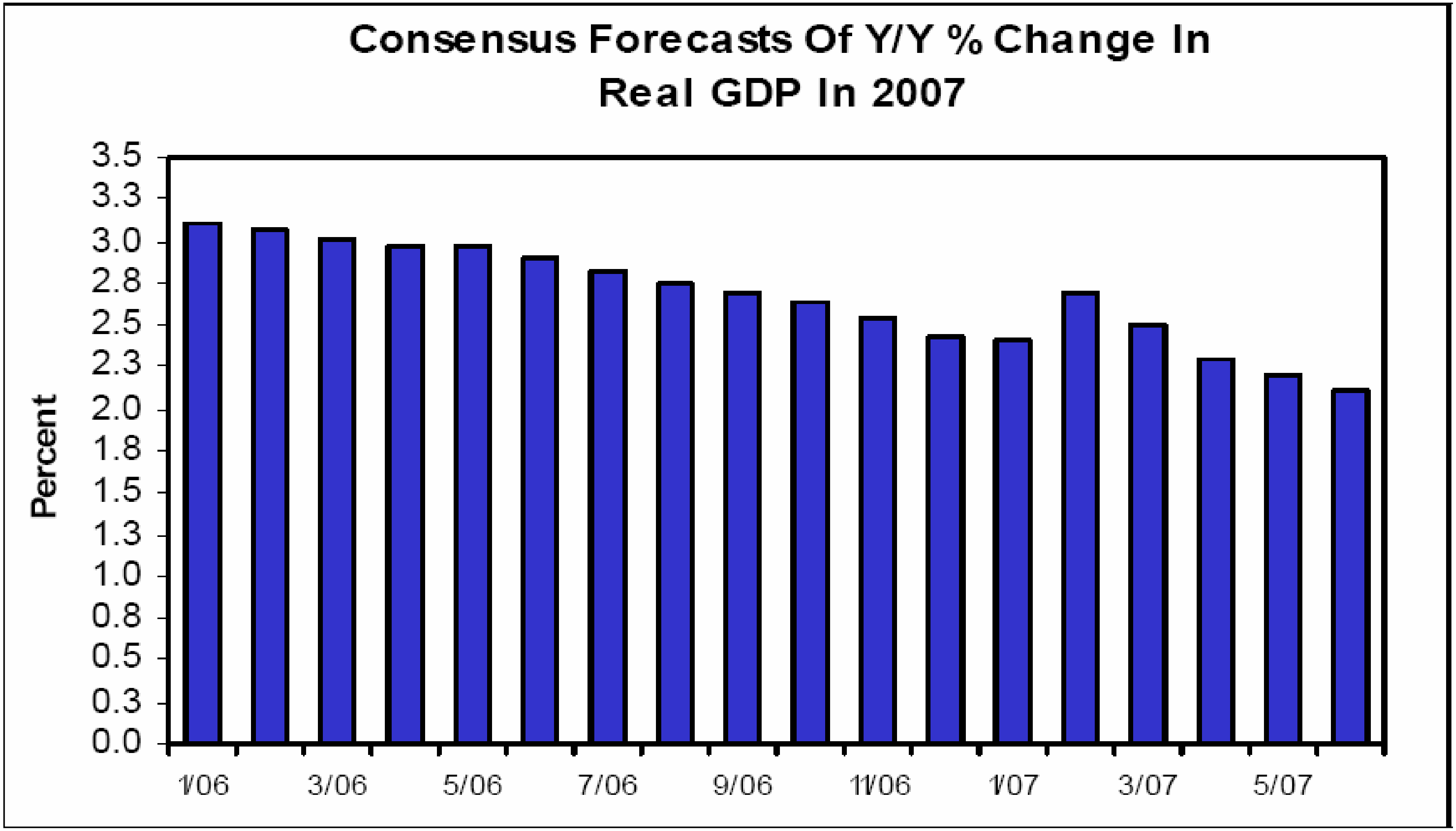
## Blue Chip Forecast

- 2007 forecast slips to 2.1% (from 2.2% in May)
- 2008 forecast at 2.9% (unchanged from May)

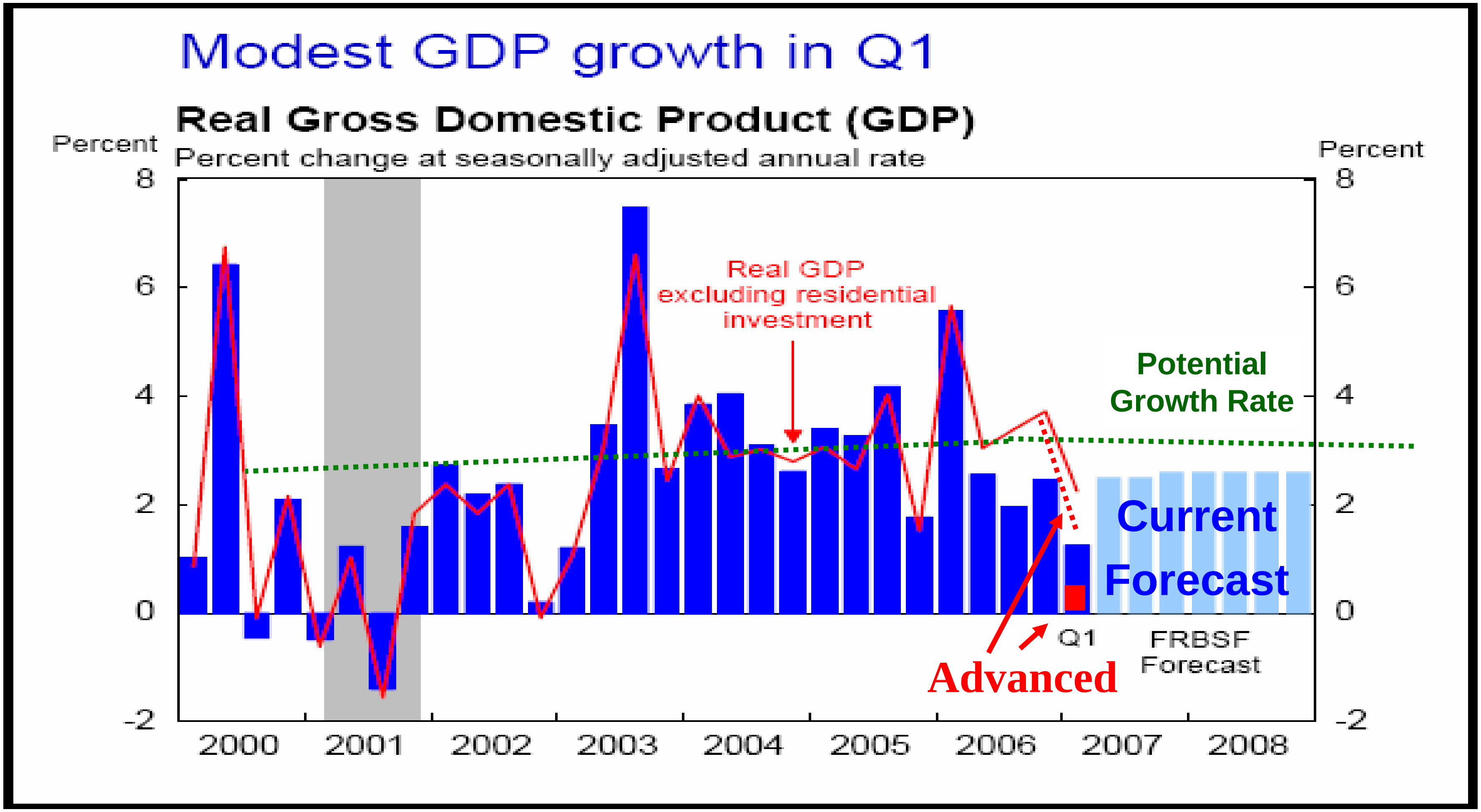
From May 14, 2007, FedViews & June 10, 2007 Blue Chip Financial Forecasts

www.frbsf.org/publications/economics/fedviews/

## *Blue Chip Real GDP Forecasts Over Time:* 2007 Growth Forecast Keeps Falling



# *FRBSF Forecast:* Real GDP is Slightly Below Average Growth for 2007




***FedViews*** of May 14, 2007

# *U.S. Inflation Forecast:* Core Inflation Expected to Ease

***FedViews***:

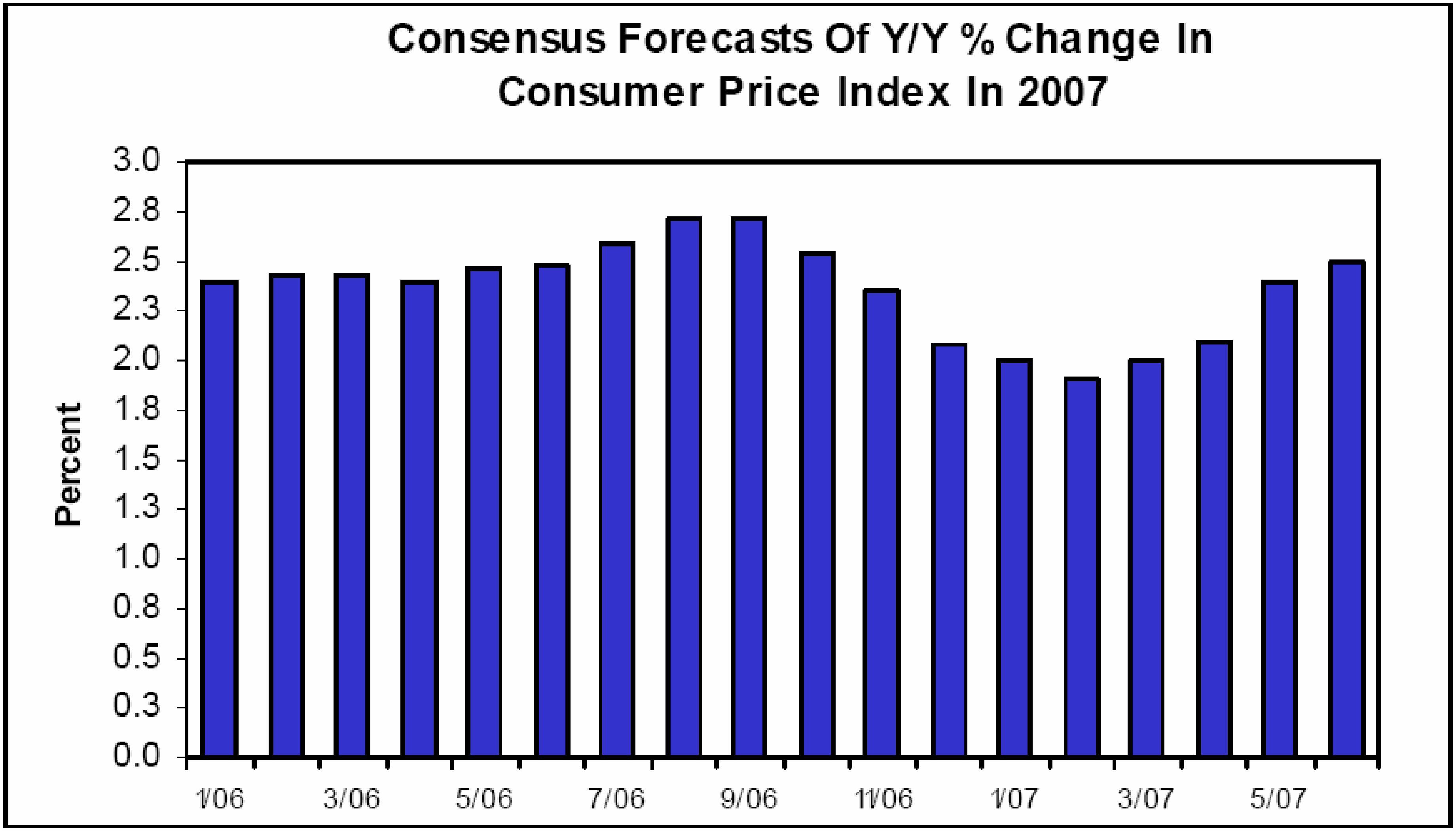
- <u>Core</u> PCE should moderate, falling <u>close to</u> the 2% mark by the end of 2008
- Previously, forecasted <u>core</u> PCE was expected to fall <u>below</u> the 2.0% mark by the end of 2008

***Blue Chip***:

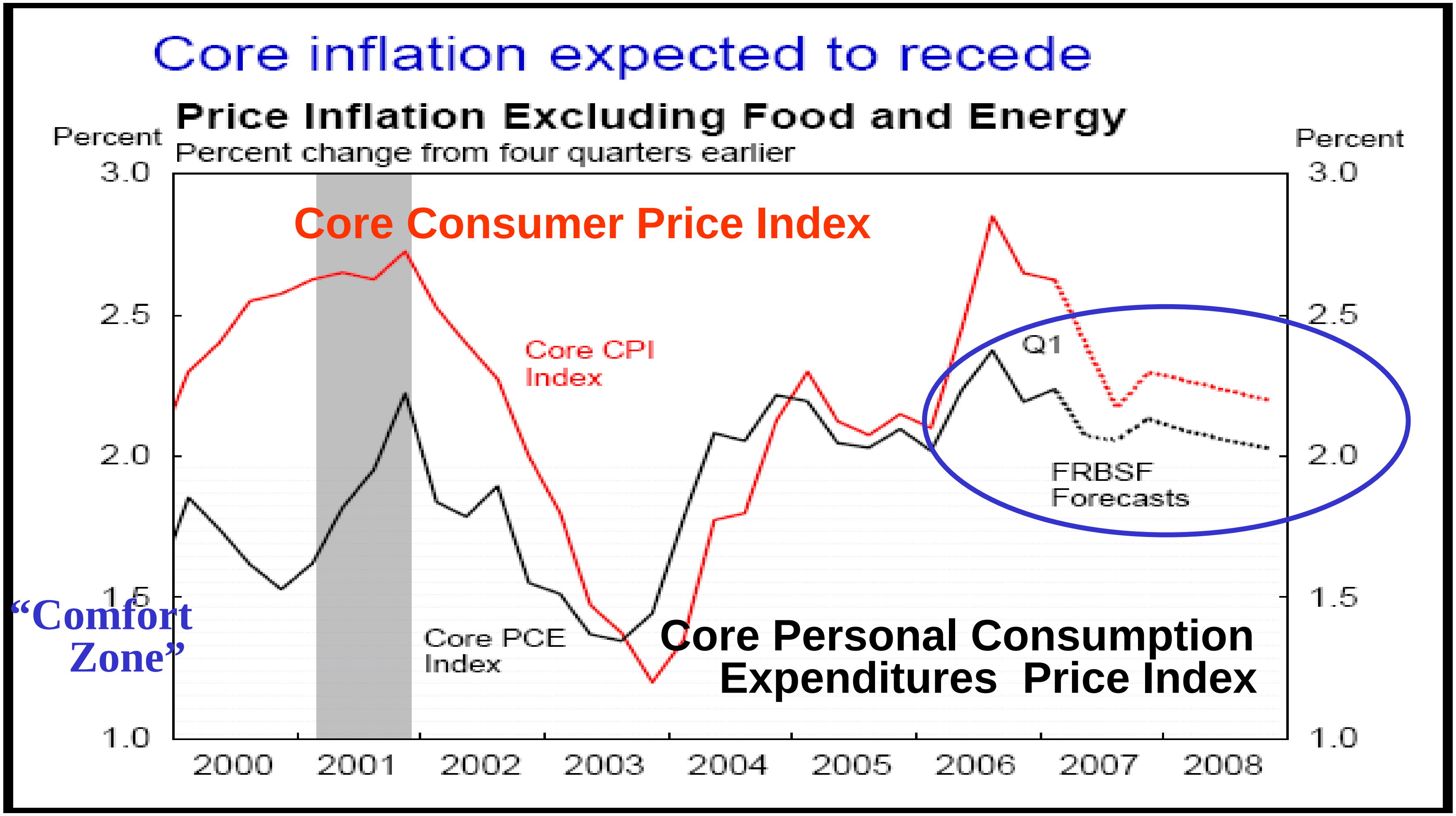
- <u>Overall</u> CPI for 2007 expected to increase by 2.5% (up from 2.4% in May)
- <u>Overall</u> CPI for 2008 expected to increase by 2.5%
- (up from 2.4% in May)

**From May 14, 2007, *FedViews* & June 10, 2007 *Blue Chip Financial Forecasts***
**www.frbsf.org/publications/economics/fedviews/**

# *Blue Chip CPI Forecasts Over Time:*
# Recent Upward Revisions to 2007 Forecast



# *FRBSF Forecast:* Core Inflation to Fall as Growth Moderates

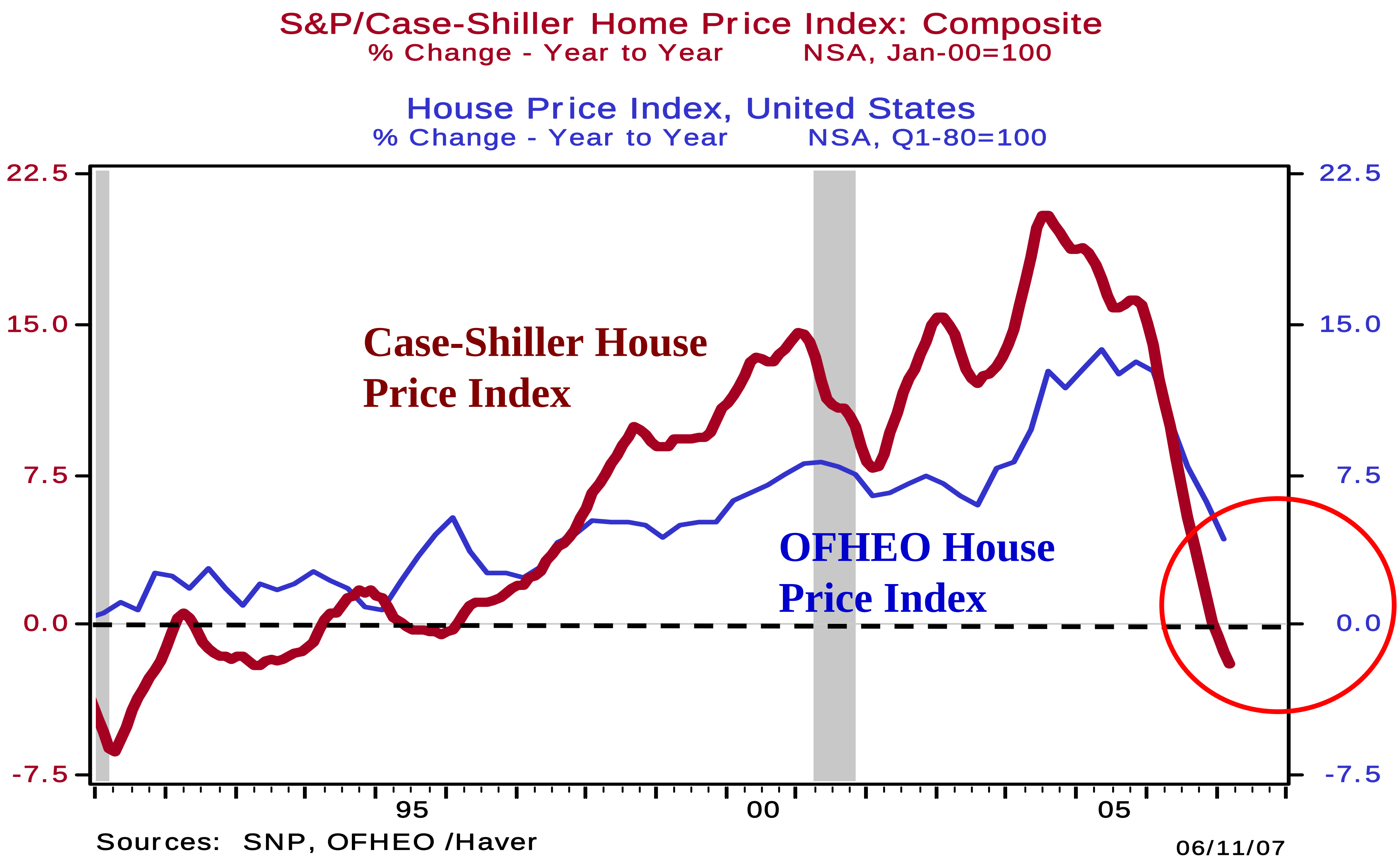



*FedViews* of May 14, 2007

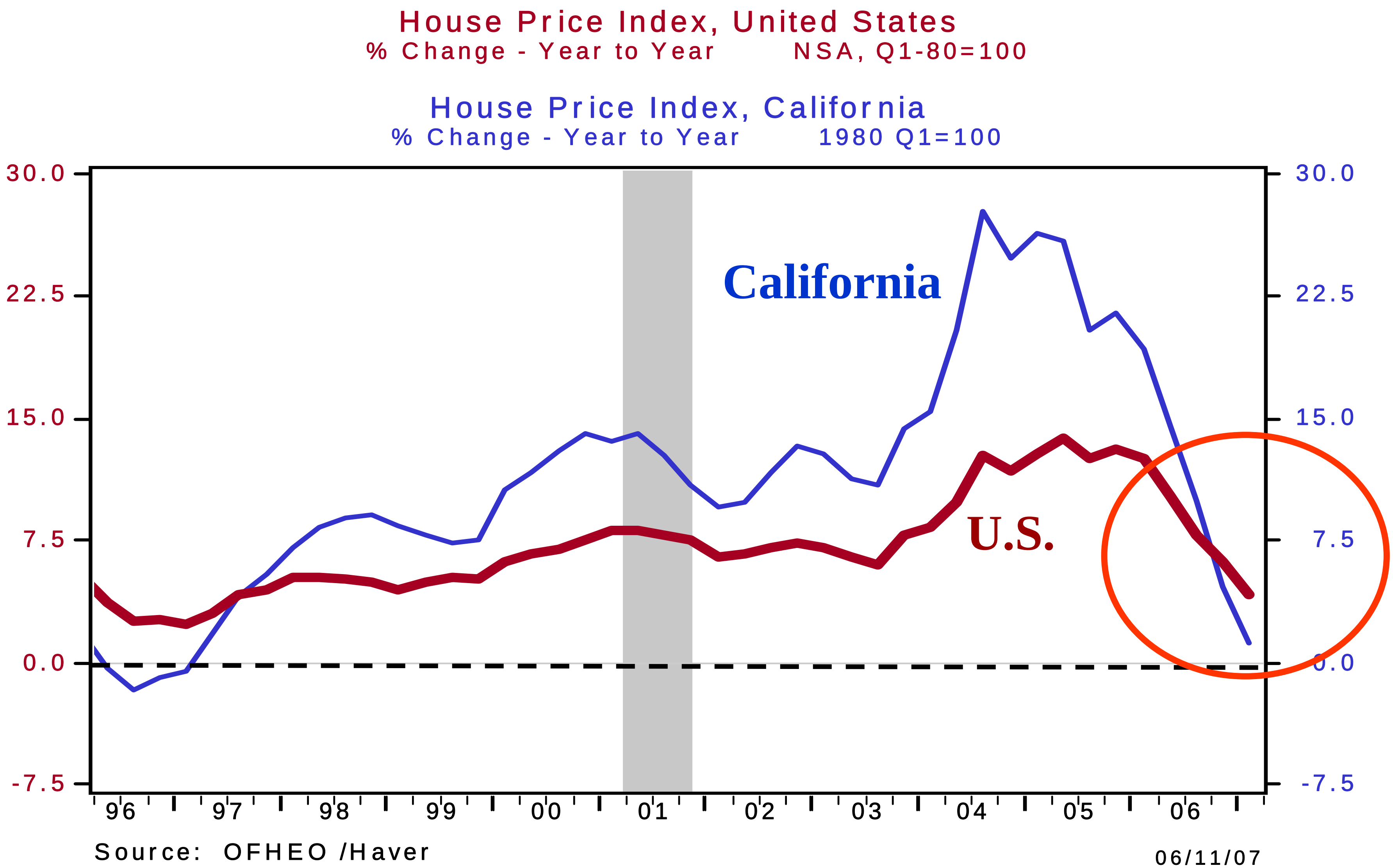
# *IV. Potential Risks to the Forecast*

- ***Housing?***
- ***Investment?***
- ***Productivity?***
- ***Oil and natural gas?***
- *Deficits?*
- *Dollar?*
- *Supply of foreign capital?*
- ***sHoCKs ???***

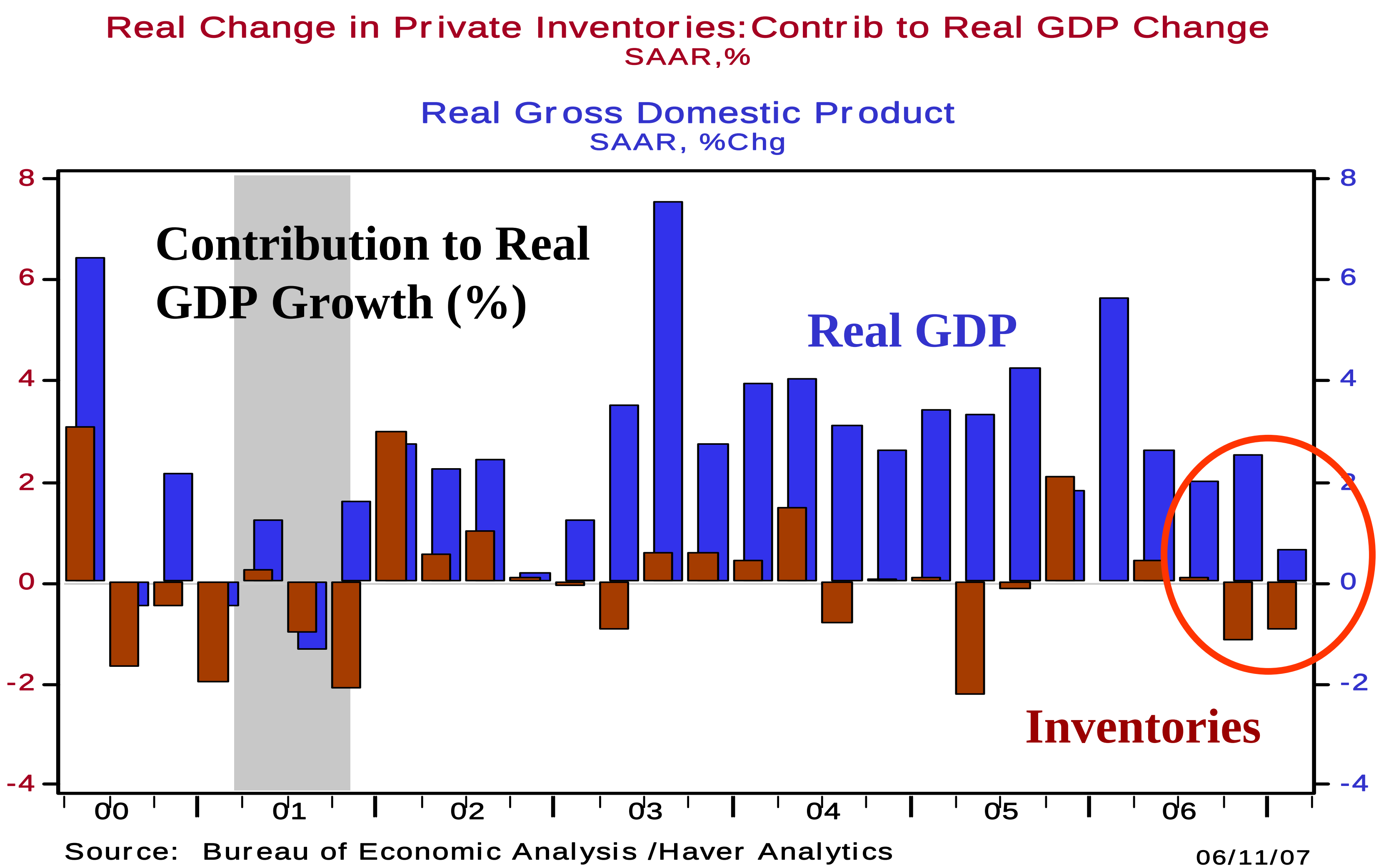
# *National House Price Appreciation:* Some Measures Turn Negative in 2007:Q1



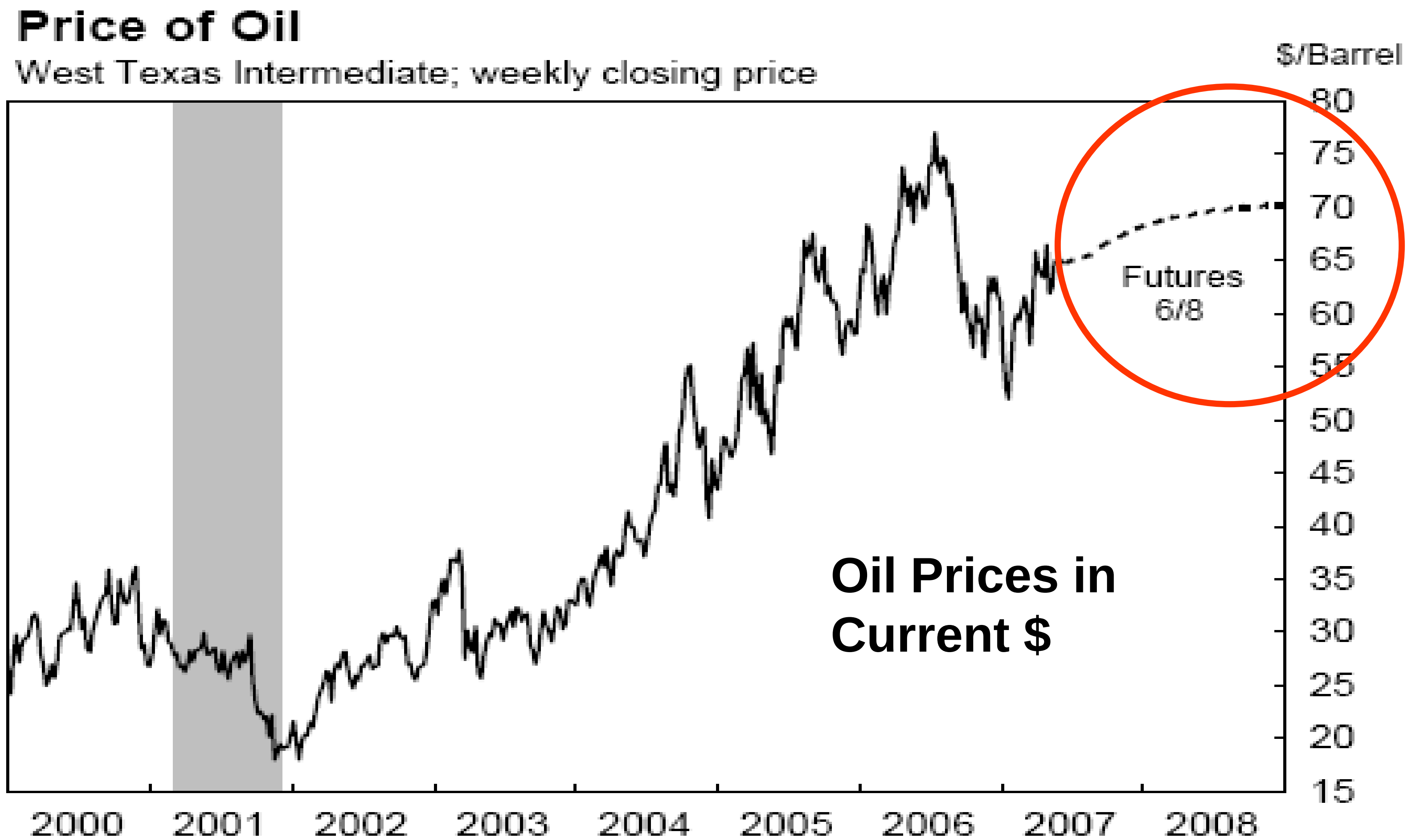
# *House Price Appreciation:* California's Appreciation Rate Falls Below Nation's



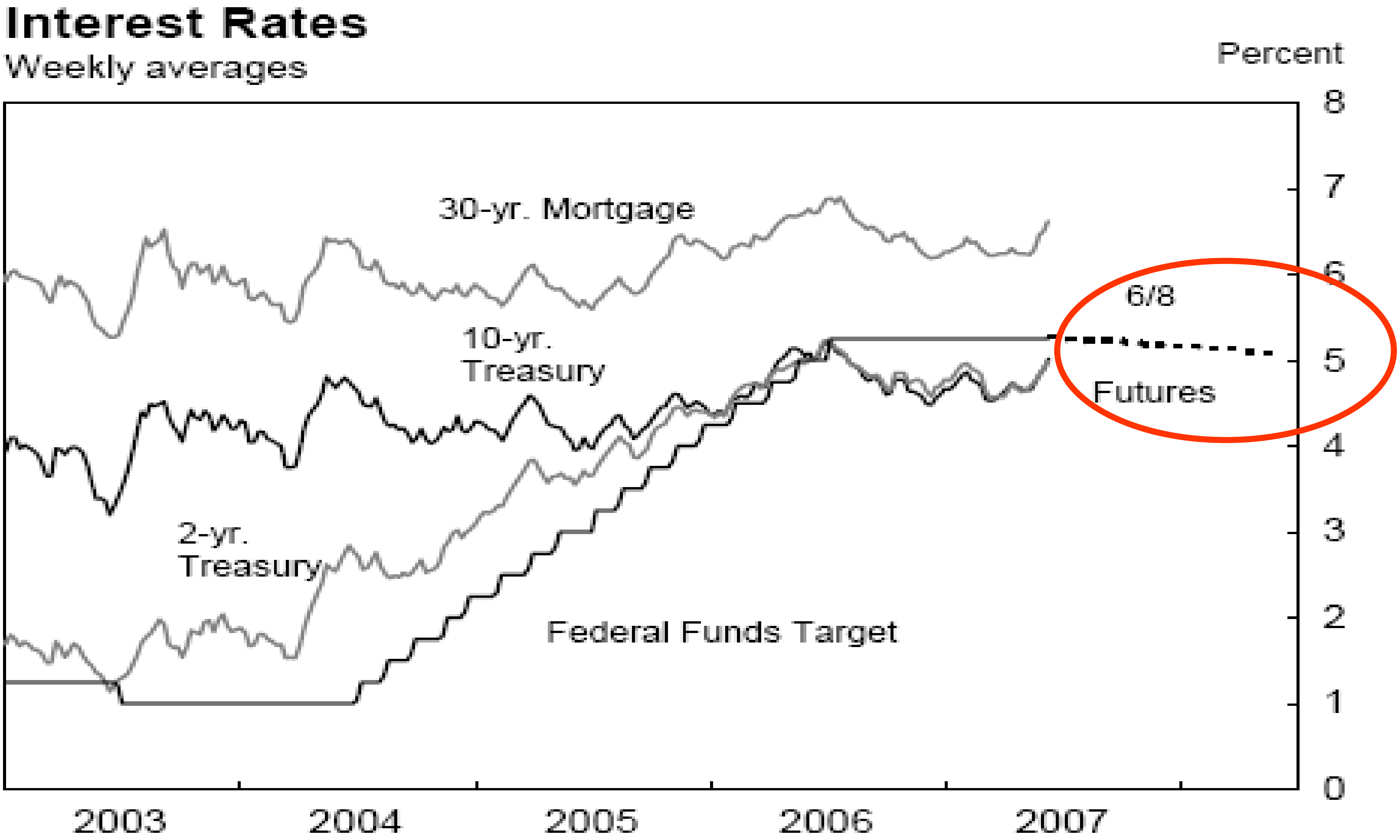
# *Inventory Adjustment:*
# Contributing to Slower Output Growth



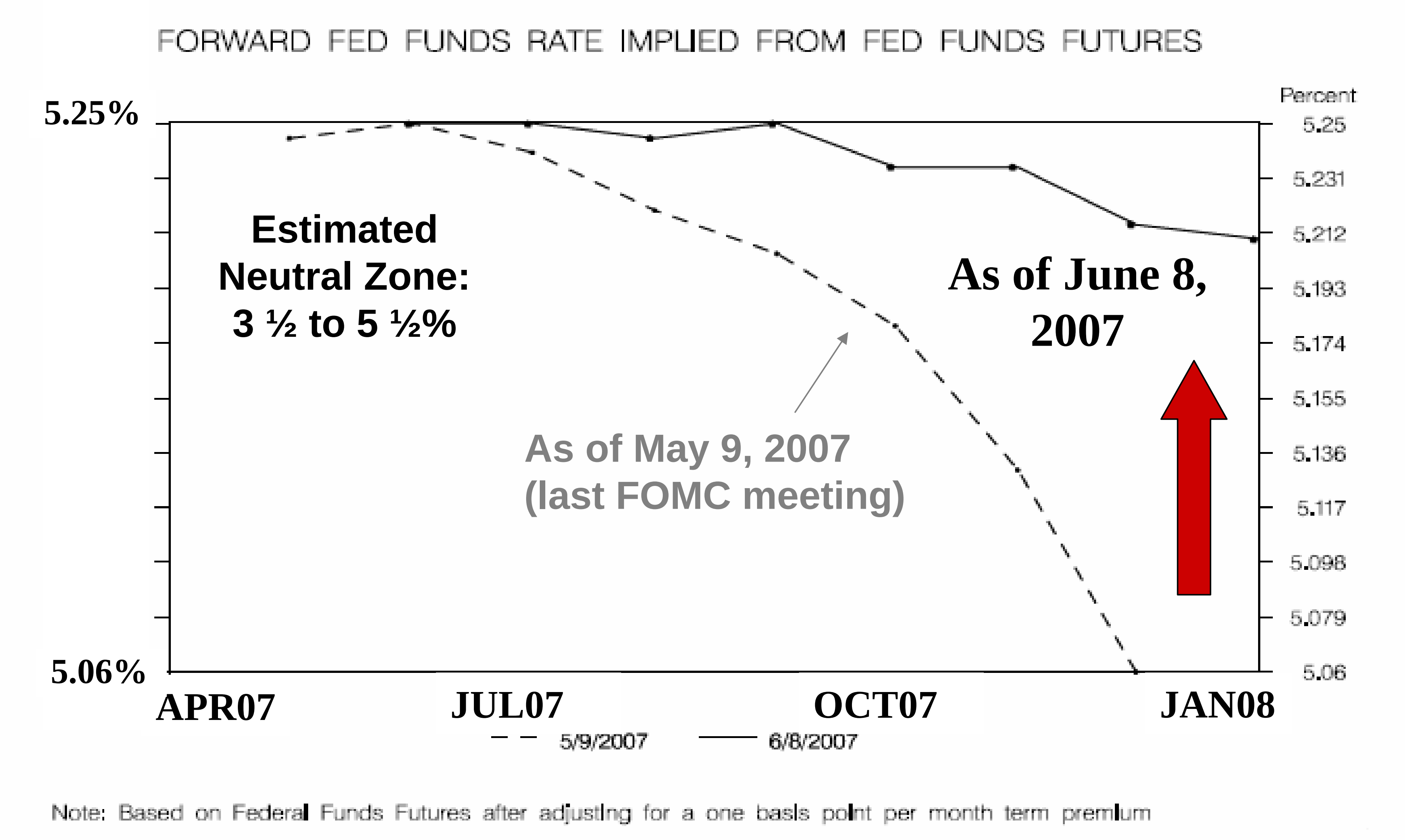
# *Energy Price Concerns:* Futures Predict High Prices to Continue



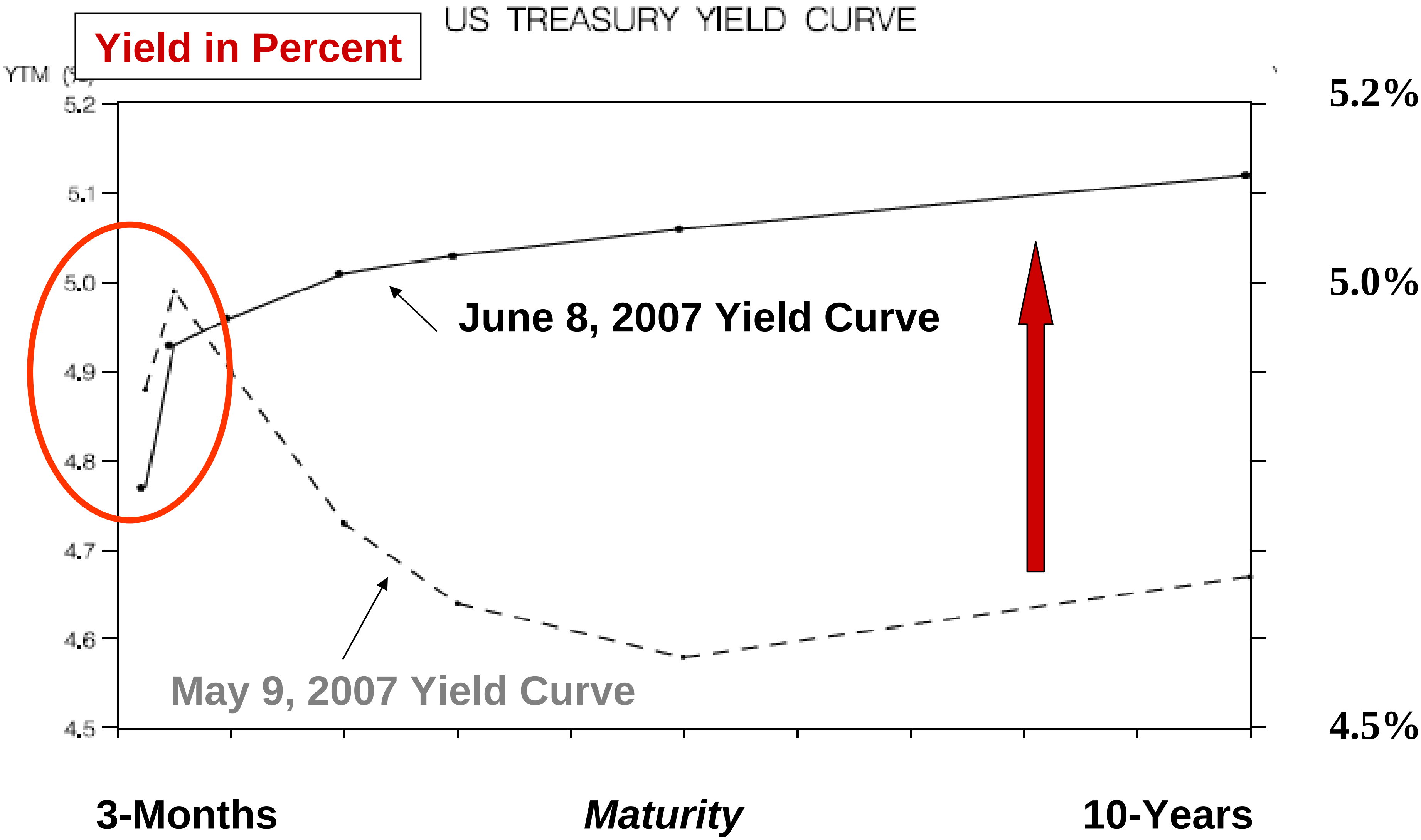
# *Market's Fed Funds Expectations:* Lower Probability of Easing



# *Fed Funds Futures Path:*
# Upward Shift Since Last Meeting



## *U.S. Treasury Yield Curve:* No Longer Inverted – Are Inflation Expectations Changing?



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# *Questions?*


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