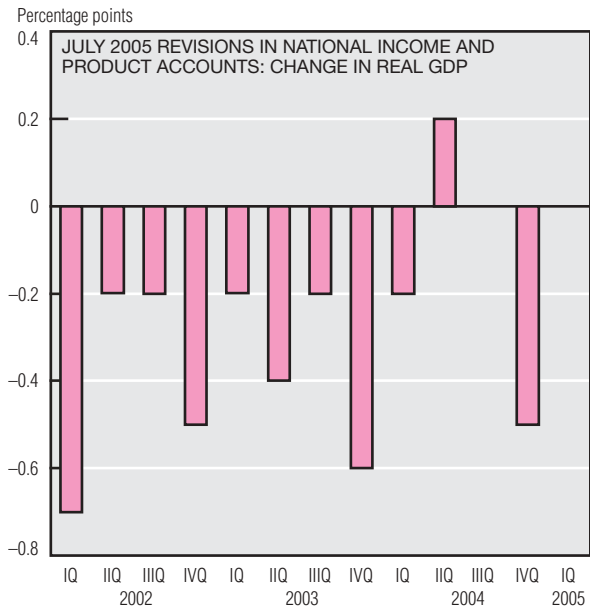
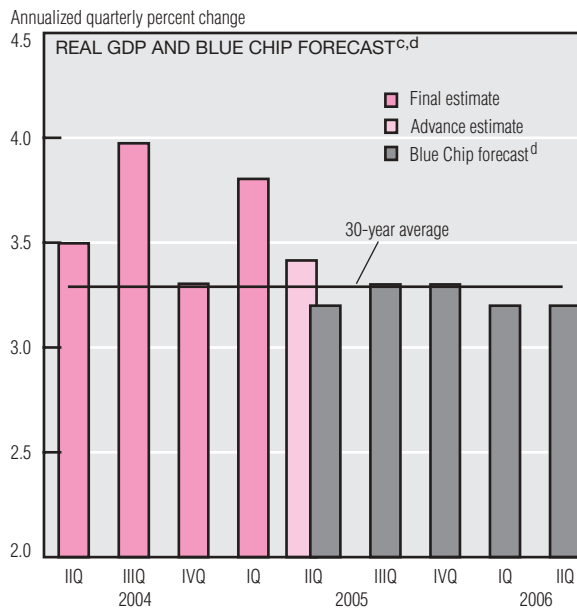
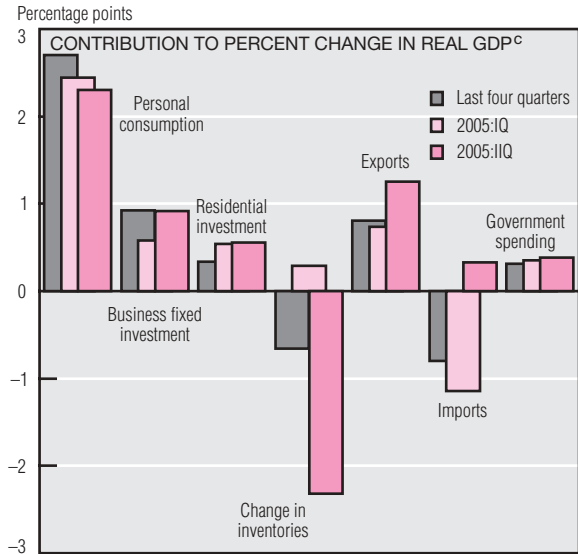


# Economic Activity

|                                | Change, billions of 2000 \$ | Annualized percent change |               |
|--------------------------------|-----------------------------|---------------------------|---------------|
|                                |                             | Current quarter           | Four quarters |
|                                |                             |                           |               |
| Real GDP                       | 92.7                        | 3.4                       | 3.6           |
| Personal consumption           | 63.4                        | 3.3                       | 3.9           |
| Durables                       | 22.6                        | 8.3                       | 6.8           |
| Nondurables                    | 18.3                        | 3.3                       | 4.5           |
| Services                       | 25.4                        | 2.3                       | 3.0           |
| Business fixed investment      | 27.3                        | 9.0                       | 9.2           |
| Equipment                      | 26.9                        | 11.0                      | 11.8          |
| Structures                     | 2.0                         | 3.2                       | 1.8           |
| Residential investment         | 13.8                        | 9.8                       | 5.8           |
| Government spending            | 9.7                         | 2.0                       | 1.6           |
| National defense               | 2.5                         | 2.1                       | 2.6           |
| Net exports                    | 44.1                        | —                         | —             |
| Exports                        | 35.0                        | 12.6                      | 8.1           |
| Imports                        | -9.1                        | -2.0                      | 5.2           |
| Change in business inventories | -64.6                       | —                         | —             |



a. Chain-weighted data in billions of 2000 dollars.

b. Components of real GDP need not add to the total because the total and all components are deflated using independent chain-weighted price indexes.

c. Data are seasonally adjusted and annualized.

d. Blue Chip panel of economists.

SOURCES: U.S. Department of Commerce, Bureau of Economic Analysis; and Blue Chip Economic Indicators, July 10, 2004.

The Commerce Department's advance reading for GDP growth in 2005:IIQ was 3.4%, which was 0.4 percentage point (pp) lower than the final 2005:IQ rate of 3.8%. The deceleration in real GDP growth was attributable primarily to a downturn in inventories, partly offset by deceleration in imports and acceleration in exports.

Foreign trade made the largest positive contribution to the change in real GDP. Net exports contributed 1.6 pp, its largest positive contribution since 1996:IVQ. However, this

was more than offset by a slowdown in inventories, which subtracted 2.3 pp, inventories' largest drag on GDP growth in five years. Most other components' contributions were relatively unchanged.

Real GDP growth in 2005:IIQ beat Blue Chip forecasters' expectations by 0.2 pp. They now predict that the economy will grow at a 3.3% rate for the next two quarters, matching the previous 30-year average, and will remain in this range into the foreseeable future.

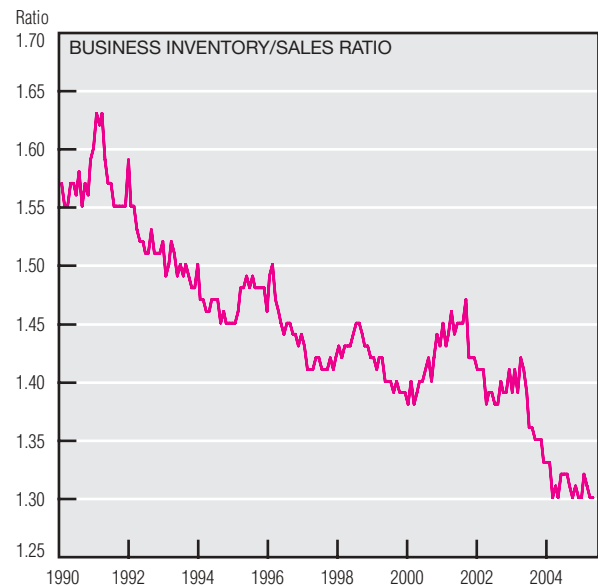
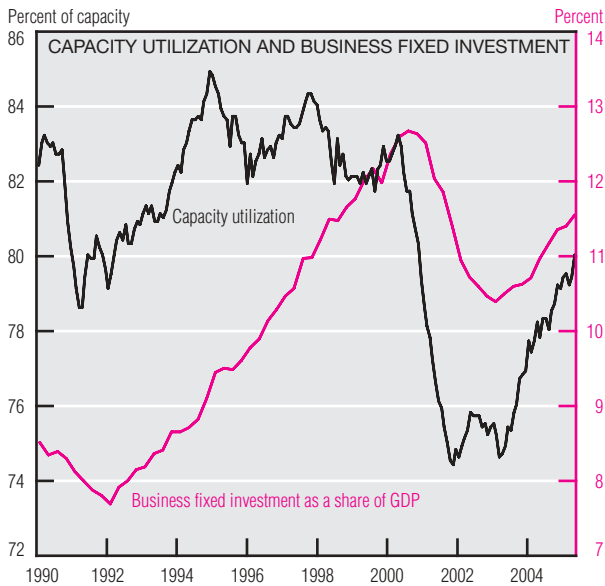
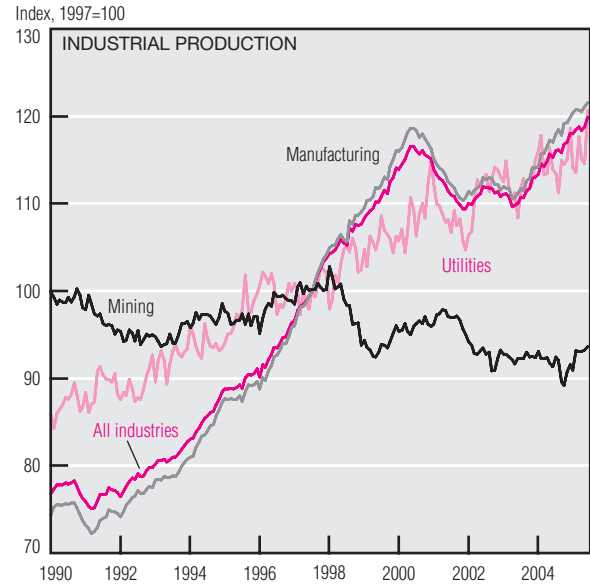
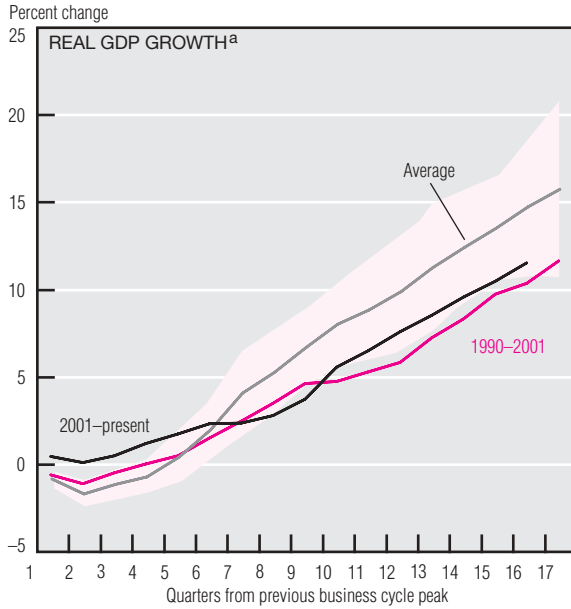
On July 29, the Commerce Department released its annual revision of

the national income and product accounts (NIPAs). This included revisions to real GDP growth from 2002:IQ through 2005:IQ, with an average revision (without regard to sign) of 0.3 pp. The largest revisions were to 2002, with 2002:IQ real GDP growth reduced to 2.7% from its original 3.4%. Only one of the 13 quarters received a positive revision.

Real GDP growth continues to lag the average rate of the last nine expansions, but it does edge out the growth experienced in the 1990–2001

(continued on next page)

## Economic Activity (cont.)



a. The shaded band represents the average for the nine previous business cycles, plus or minus two standard errors.

SOURCES: U.S. Department of Commerce, Bureau of Economic Analysis; U.S. Bureau of the Census; and Board of Governors of the Federal Reserve System.

expansion, even with the recent downward annual revisions. Within the industrial sector, contributions to output growth have been uneven. Utilities have grown fairly steadily over the long run, but mining output has been trending down since the late 1990s. Manufacturing output, the main component of industrial production, has been more attuned to the business cycle than the other two industries. In December 2004, it finally surpassed its previous peak (118.5 in June 2000) and has continued to trend up.

This solid output growth at last boosted capacity utilization to 80% in June 2005, a substantial improvement from its low of 74.4% in December 2004. The higher output rate has not only used up some capital, leading firms to replace it, but has also increased firms' confidence that other investments will generate a profitable return. This has driven up business fixed investment as a share of GDP from its recent low of 10.4% in 2003:1Q to 11.5%, not yet at the 12.7% level reached in 2000:IIIQ but still high by historical standards.

On the sales side, businesses continue to find ways to trim their inventories. May's ratio of business inventories to sales stands at 1.3. This is significantly lower than the ratio at the last business cycle peak in March 2001, and substantially lower than the level businesses operated at in July 1990. More timely and complete information on sales and inventories permits businesses to run much leaner and still ensure that they can adequately meet consumers' demand.