

National and District Overview



By and large, the U.S. economy continues to demonstrate just how much thrust the current expansion still has left. Even after six hikes in the federal funds rate target since mid-1999, output has continued to grow at a rate that many economists consider too fast to sustain. In fact, output hasn't grown at what would normally be considered a sustainable rate—between 3 and 3.5 percent a year—since the second quarter of 1999. Just this year, second-quarter growth was more than half of a percentage point faster than it was in the first. Which begs the question: Has the economy really landed softly? Let's check with the pilot.

Mixed Cockpit Readings— The Output Gauge

Because there are so many gauges to check, the pilot can't give a straight answer. Looking at the gauge marked "GDP" suggests the plane is still airborne. With growth at a 5.6 percent annual rate in the second quarter of 2000—following a 4.8 percent rate in the first—it appears that the flight is not only still airborne, but is, in fact, gaining altitude. Surprisingly, though, the engine that usually propels GDP growth—consumer spending—slowed substantially recently. In the second quarter of this year, consumers scaled back their purchases of big-ticket items, pulling the consumption growth rate down to just about 3 percent from 7.6 percent the quarter before.

Businesses, on the other hand, kicked in the afterburners and drove investment spending growth up to an almost 22 percent rate—significantly faster than the 5 percent rate from a quarter earlier.

Where did most of this spending go? Toward computers and software and toward inventories. In fact, second-quarter 2000 inventory growth is, but for the rate posted in the fourth quarter of 1999, the highest it's been since the beginning of 1998. Some market observers, however, will argue that rising inventories are a sign that a slowdown's possible if inventories are climbing only because production hasn't yet adjusted to fallen demand.

Mixed Cockpit Readings— The Employment Gauge

On the other hand, the gauge marked "Employment" seems to indicate a smooth touchdown, with possibly even some brake pressure already being applied. In August, payroll employment

fell by 91,000 jobs, after a 40,000 job drop in July. That said, both of these declines came during a year in which an average of 268,000 jobs or so were created each month through June. The payroll numbers are only a part of the picture, though.

In July and August, almost 450,000 temporary U.S. Census Bureau workers ended service—a figure that throws the reading off dramatically. During those two months, private firms added 173,000 new jobs. This reading is also distorted, though, because of a strike in the communications industry, which, had it not occurred,

would have put another 87,000 workers on the payrolls, according to Bureau of Labor Statistics reports. These special circumstances, coupled with an unemployment rate that continues to hover around 4 percent, all suggest that there may not have been a touchdown yet.

Mixed Cockpit Readings— The Inflation Gauge

The gauge that the Fed pays the most attention to—the one marked "Inflation"—is probably the one that's most disturbing. During the first eight months of 2000, the CPI increased at a 3.4 percent annual rate. By this reading, the flight is seemingly way off course. For all of 1999, CPI inflation was 2.7 percent, which was up from 1998, when it was only 1.6 percent. Most of the recent increases, however, have come from rising fuel prices, which so far are rising at a 14 percent rate this year, a bit faster than the rate they were up for all of last year.

BY ADAM M. ZARETSKY

Do these numbers mean that the Fed will continue increasing the fed funds rate in an attempt to, at least, level out the economy's flight path? Markets don't seem to think so. Traders in federal funds futures are betting that no further interest rate hikes will happen this year. Time will tell if the course corrections already put in place will work to keep the economy on course and inflation at bay.

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