Prefatory Note

The attached document represents the most complete and accurate version available based on original files from the FOMC Secretariat at the Board of Governors of the Federal Reserve System.

Please note that some material may have been redacted from this document if that material was received on a confidential basis. Redacted material is indicated by occasional gaps in the text or by gray boxes around non-text content. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

Content last modified 02/09/2012.

Class III FOMC - Internal (FR)

Part 2

May 3, 2006

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

Prepared for the Federal Open Market Committee
by the staff of the Board of Governors of the Federal Reserve System

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Domestic Nonfinancial Developments

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Economic activity expanded strongly in the first quarter, and gains were widespread across most categories of final sales. Consumer spending posted a sizable increase, driven by January's bounceback in motor vehicle purchases and an acceleration in spending on other goods at the turn of the year. In addition, favorable weather boosted housing construction early in the quarter. Since then, the pace of consumer spending has moderated, and housing starts have retraced their earlier run-up. Business investment spending strengthened in the first quarter, in part because of a surge in the purchases of transportation and high-tech equipment and a step-up in nonresidential construction. The March employment report showed continuing robust employment gains, and manufacturing production also posted solid gains in the first quarter. Overall consumer price inflation jumped in March because of higher energy prices, while core prices rose a bit more rapidly than in earlier months.

Labor Market Developments

Employment continued to expand briskly in March. Private nonfarm payrolls increased 187,000, close to the gains in the preceding two months. The average workweek of production or nonsupervisory workers held steady at 33.8 hours. Aggregate production-worker hours rose 0.2 percent in March and increased at an annual rate of 3.0 percent for the first quarter as a whole. In the household survey, the unemployment rate edged down in March to 4.7 percent, the same level as in January. The labor force participation rate was unchanged at 66.1 percent.

Other labor market indicators are consistent with continued strong employment gains. The number of persons working part-time for economic reasons as a share of household employment has dropped sharply in recent months, while the number of job losers unemployed less than five weeks as a percent of household employment has remained relatively low. In addition, initial claims for unemployment insurance continued to fluctuate around a low level in April, and the level of insured unemployment continued to trend down.

Long-term unemployment also appears to have declined. The percent of the labor force unemployed more than 26 weeks ticked down in March, while the exhaustion rate—the proportion of workers leaving the unemployment insurance rolls after using their entire period of eligibility—moved down sharply from elevated levels at the start of the year.

Nonetheless, recent changes in business and household perceptions of current and future labor market conditions have been mixed. The percentage of firms reporting to the

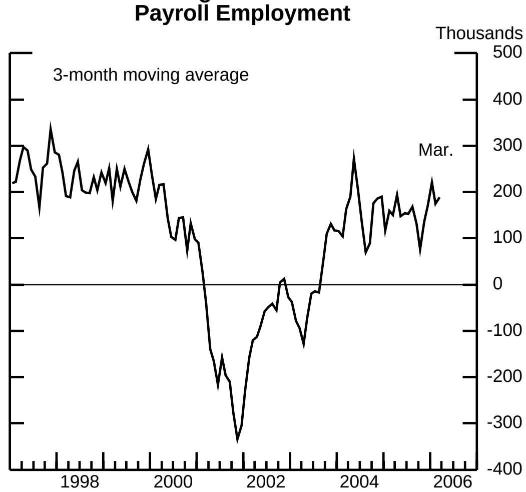
Changes in Employment

(Thousands of employees; seasonally adjusted)

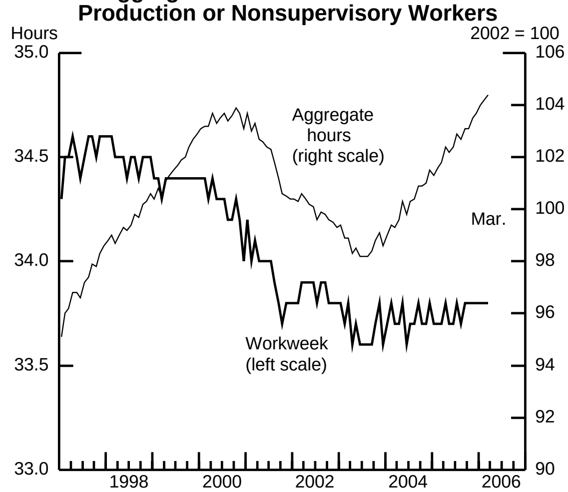
Measure and sector	2005	2005 Q3	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
	Average monthly change				Monthly change		
Nonfarm payroll employment (establishment survey)	165	155	179	197	154	225	211
Private	152	132	171	188	188	190	187
Manufacturing	-6	-15	12	-3	5	-10	-5
Construction	25	16	30	29	44	37	7
Wholesale trade	7	5	7	12	18	8	11
Retail trade	13	4	11	14	0	12	29
Transportation and utilities	6	3	6	2	8	6	-8
Information	-1	3	-2	3	-1	9	2
Financial activities	12	19	17	19	21	21	16
Professional and business services	41	51	41	31	6	35	52
Temporary help services	14	21	18	-3	-23	-1	16
Nonbusiness services[1]	51	43	44	75	82	68	76
Total government	14	23	8	8	-34	35	24
Total employment (household survey)	221	228	115	287	295	183	384
Memo:							
Aggregate hours of private production workers (percent change)[2]	2.3	2.2	2.1	3.0	.3	.2	.2
Average workweek (hours)[3]	33.8	33.8	33.8	33.8	33.8	33.8	33.8
Manufacturing (hours)	40.6	40.6	40.9	41.0	40.9	41.0	41.0

1. Nonbusiness services comprises education and health, leisure and hospitality, and "other."
2. Establishment survey. Annual data are percent changes from Q4 to Q4. Quarterly data are percent changes from preceding quarter at an annual rate. Monthly data are percent changes from preceding month.
3. Establishment survey.

Changes in Private Payroll Employment



Aggregate Hours and Workweek of Production or Nonsupervisory Workers



Selected Unemployment and Labor Force Participation Rates

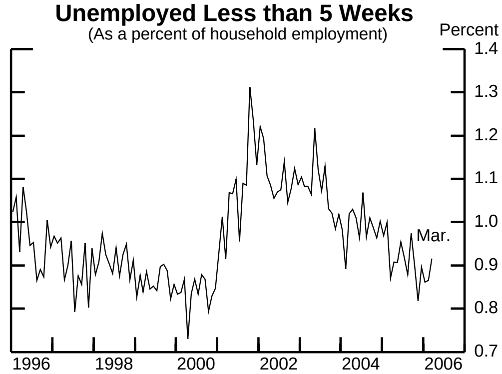
(Percent; seasonally adjusted)

Rate and group	2005	2005 Q3	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
Civilian unemployment rate							
Total	5.1	5.0	5.0	4.7	4.7	4.8	4.7
Teenagers	16.6	16.1	16.1	15.5	15.3	15.4	15.7
20-24 years old	8.8	8.6	8.5	8.1	8.2	8.5	7.6
Men, 25 years and older	3.8	3.8	3.7	3.6	3.5	3.7	3.6
Women, 25 years and older	4.2	4.2	4.2	3.9	4.0	3.9	3.8
Labor force participation rate							
Total	66.0	66.2	66.1	66.0	66.0	66.1	66.1
Teenagers	43.7	43.8	43.4	43.7	43.4	43.8	43.9
20-24 years old	74.6	74.6	74.8	74.0	73.8	74.5	73.9
Men, 25 years and older	75.4	75.6	75.3	75.5	75.4	75.4	75.6
Women, 25 years and older	59.4	59.5	59.6	59.4	59.5	59.4	59.3

Labor Force Participation Rate and Unemployment Rate

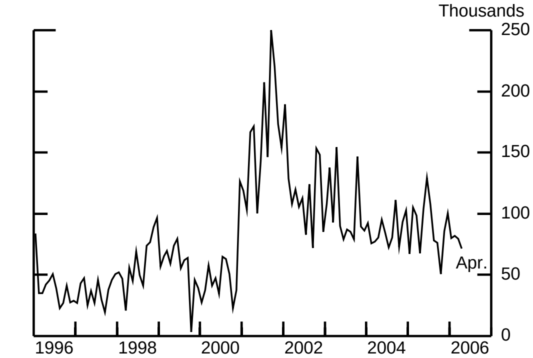
Persons Working Part Time for Economic Reasons
(As a percent of household employment)

Job Losers Unemployed Less than 5 Weeks
(As a percent of household employment)



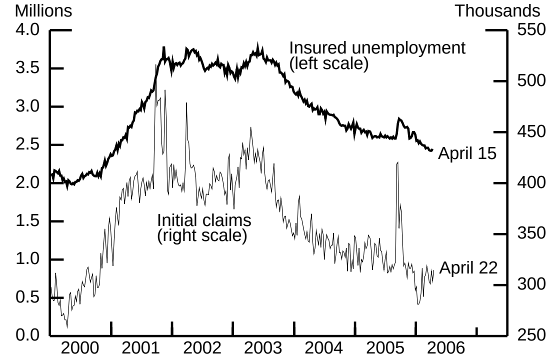
Labor Market Indicators

Layoff Announcements

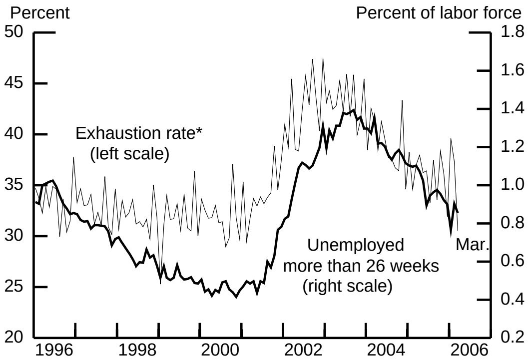


Note. Seasonally adjusted by FRB staff.
Source. Challenger, Gray, and Christmas, Inc.

Unemployment Insurance

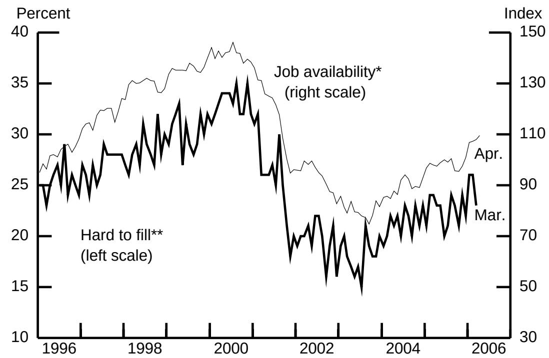


Exhaustion Rate and Long-Term Unemployed



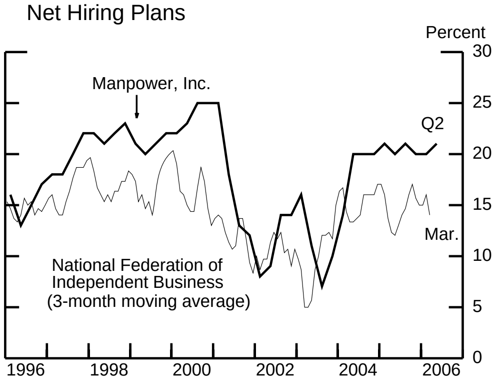
*The exhaustion rate is the number of individuals who were receiving unemployment insurance benefits but reached the end of their potential eligibility expressed as a percent of individuals who began receiving such benefits 6 months earlier.

Labor Market Tightness



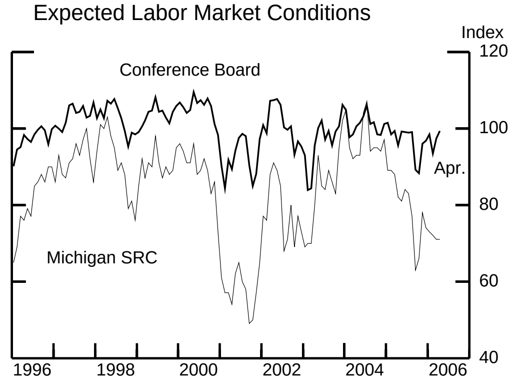
*Proportion of households believing jobs are plentiful, minus the proportion believing jobs are hard to get, plus 100.
**Percent of small businesses surveyed with at least one "hard to fill" job opening.
Source. For job availability, Conference Board; for hard to fill, National Federation of Independent Business.

Net Hiring Plans



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

Expected Labor Market Conditions



Note. The proportion of households expecting labor market conditions to improve, minus the proportion expecting conditions to worsen, plus 100.

National Federation of Independent Businesses (NFIB) that they had a hard-to-fill position fell a bit in March, and hiring plans of NFIB members ticked down again. Manpower's index of net hiring plans edged up in March, although it remains within the narrow band held since the second half of 2004. In contrast, households' assessments of job availability edged up further in April to its highest level in the past five years. The Conference Board measure of expected labor market conditions rose in April but has moved little on balance in recent months, while expectations of labor market conditions in the Michigan survey were unchanged in April.

The staff estimates that productivity in the nonfarm business sector rose at an annual rate of about 3 percent in the first quarter after a decrease of 0.4 percent in the fourth quarter.[1] Over the four quarters ending last quarter, output per hour increased 2¼ percent by our estimate—¾ percentage point below the pace recorded during the preceding four quarters.

Industrial Production

Industrial activity expanded ½ percent per month in February and March, and the available indicators suggest that IP will post another strong gain in April. Utilities output surged in February and edged up in March, but these increases only partly reversed the weather-related plunge in January. Mining output, which includes oil and natural gas extraction, edged up a cumulative 0.3 percent in February and March as the contribution from hurricane-related recoveries diminished. Excluding these sectors, industrial activity slowed recently from its rapid pace in the fourth quarter. Still, monthly increases in manufacturing averaged about 0.4 percent per month during the first quarter—down from the average pace of 1 percent per month in the previous quarter—but somewhat above the pace for 2005 as a whole. These increases in factory output lifted manufacturing capacity utilization in March to 80.4 percent, 0.6 percentage point above its 1972-2005 average.

Despite earlier progress, the production of oil, natural gas, and refined petroleum products has yet to completely recover from the effects of Hurricanes Katrina and Rita. As of May 3, domestic crude production and natural gas extraction were about 94 percent and 97 percent of their pre-Katrina levels, respectively, and in both cases, complete

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[1] The Bureau of Labor Statistics' estimate of productivity for 2006:Q1, which will be released on May 4, will be based on published GDP; our estimate incorporates additional information on first-quarter production released after the BEA's estimate of GDP.

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

Component	Proportion 2005 (percent)	2005[1]	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
			Annual rate		Monthly rate		
Total	**100.0**	**3.0**	**5.3**	**4.5**	**-.4**	**.5**	**.6**
Previous	100.0	3.0	5.3	...	-.3	.7	...
Manufacturing	80.8	4.2	9.1	5.4	.7	-.1	.5
Ex. motor veh. and parts	73.7	4.4	10.3	6.0	.5	-.1	.5
Ex. high-tech industries	68.9	2.9	9.1	5.4	.6	-.1	.3
Mining	9.8	-6.8	-15.0	20.4	1.7	-.7	.9
Utilities	9.5	2.9	-5.7	-16.7	-11.6	8.0	.5
Selected industries							
High technology	4.8	25.7	27.1	15.2	-.3	1.0	2.7
Computers	.8	12.0	14.5	9.8	.4	.3	.4
Communications equipment	1.2	25.4	33.1	27.6	2.6	3.4	2.2
Semiconductors[2]	2.8	29.9	28.1	11.4	-1.7	.1	3.5
Motor vehicles and parts	7.1	2.3	-2.3	-.7	2.6	-1.1	1.5
Market groups excluding energy and selected industries							
Consumer goods	21.0	2.3	4.8	2.1	.1	-.2	.5
Durables	4.1	2.6	8.2	-2.2	-.3	.0	-.5
Nondurables	16.9	2.2	3.9	3.1	.2	-.3	.7
Business equipment	8.0	9.6	27.5	8.2	.3	.1	.7
Defense and space equipment	2.0	9.2	7.4	7.0	.0	1.4	-.3
Construction supplies	4.4	6.5	17.3	-1.1	.1	-.8	.2
Business supplies	7.8	2.7	6.4	3.7	.5	-.4	.2
Materials	24.4	.6	6.9	8.6	1.0	.1	.3
Durables	13.7	3.6	12.9	6.4	.8	.3	.4
Nondurables	10.7	-3.1	-.3	11.6	1.4	.0	.2

1. From fourth quarter of preceding year to fourth quarter of year shown.
2. Includes related electronic components.
... Not applicable.

Capacity Utilization
(Percent of capacity)

Sector	1972-2005 average	1994-2005 high	2001-02 low	2005 Q3	2005 Q4	2006 Q1	2006 Feb.	2006 Mar.
Total industry	**81.0**	**85.0**	**73.9**	**79.8**	**80.5**	**81.0**	**81.0**	**81.3**
Manufacturing	79.8	84.5	72.0	78.5	79.8	80.4	80.2	80.4
High-tech industries	78.1	86.1	57.4	75.3	75.7	74.8	74.3	75.4
Excluding high-tech industries	79.9	84.4	73.1	78.9	80.3	81.0	80.9	81.1
Mining	87.3	89.0	85.6	86.1	82.7	86.8	86.3	87.2
Utilities	86.7	93.7	83.7	88.1	86.9	82.9	84.9	85.3

recoveries are not expected until the second half of 2006.[2] Refining activity is still being held down by the effects of the hurricanes, although all the damaged refineries should be back to full production by the end of June.[3] Overall, the return to production of hurricane-idled facilities in the energy sector and elsewhere had little effect on total industrial production in February and March after having boosted IP an average of ½ percentage point per month from November to January.

Besides the delays in restarting damaged refineries, some refineries are shut down for routine maintenance that was postponed in the immediate aftermath of the hurricanes. These additional shutdowns contributed to a second consecutive monthly decline in refinery output in March, and weekly data suggest output will decline further in April.[4] However, most operations are expected to return to normal by the start of the summer driving season. Weekly physical product data suggest that utilities output and crude oil extraction rose moderately in April.

Motor vehicle production rose about 200,000 units to an annual rate of 11.7 million units in March, and the latest schedules suggest that assemblies likely rose further in April. Given April's sales pace, the scheduled production rate implies that the days' supply of light vehicles moved higher in April from the slightly elevated level of 71 days in March. Total assemblies during the second quarter as a whole are also currently scheduled at a moderate pace of 11.6 million units as manufacturers seek to keep inventories under control.

Elsewhere in transportation, production of commercial aircraft dropped about 2 percent in March after several months of rapid gains.

.[5] The output of military aircraft declined

[2] The Gulf Coast region accounts for nearly 30 percent of U.S. crude oil extraction, about 20 percent of natural gas extraction, and just under half of refining capacity. After Hurricane Rita, all Gulf Coast crude oil extraction and about 80 percent of Gulf Coast natural gas extraction were shut in, as well as similar shares of onshore and near offshore (that is, within three miles of the coast) production in Louisiana.

[3] Three Gulf Coast refineries, representing about 4½ percent of domestic capacity, are still not fully operational.

[4] The effect on seasonally adjusted output is magnified by the timing of this maintenance; normally refineries begin ramping up gasoline production in late March. In addition, the shift by producers of blended gasoline to ethanol-based production has reduced the efficiency of refining operations.

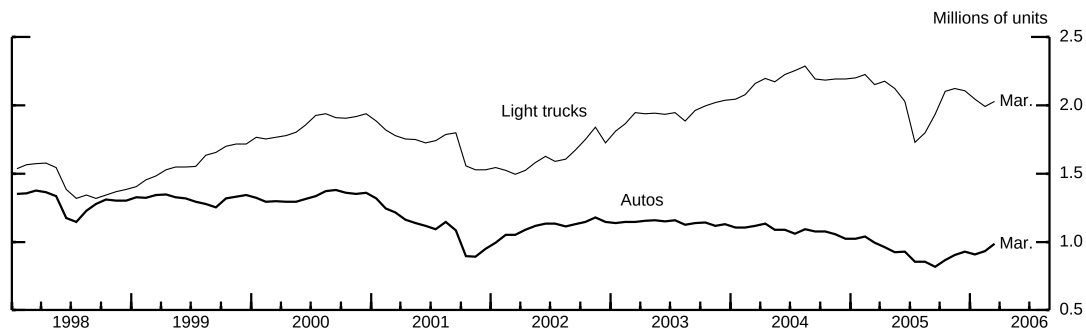
[5] Current monthly production differs from the delivery of finished aircraft, as the production measure includes work in progress on planes for delivery up to ten months ahead.

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

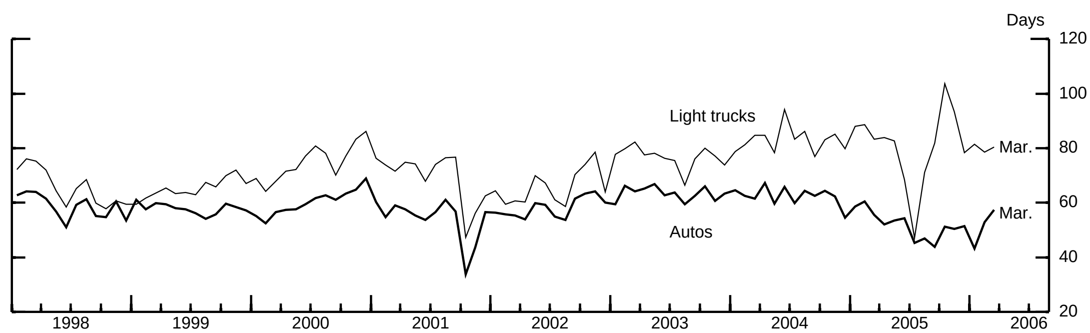
Item	2005	2005 Q4	2006 Q1	2006 Q2	2006 Jan.	2006 Feb.	2006 Mar.	2006 Apr.
U.S. production[1]	11.5	11.4	11.2	11.3	11.3	11.0	11.3	11.4
Autos	4.3	4.4	4.5	4.4	4.6	4.4	4.5	4.6
Light trucks	7.2	7.0	6.7	6.9	6.7	6.6	6.7	6.8
Days' supply[2]	69	74	69	n.a.	64	68	71	n.a.
Autos	52	53	53	n.a.	43	53	57	n.a.
Light trucks	81	90	80	n.a.	82	79	80	n.a.
Inventories[3]	3.04	3.04	3.01	n.a.	2.96	2.93	3.01	n.a.
Autos	.93	.93	.99	n.a.	.91	.93	.99	n.a.
Light trucks	2.11	2.11	2.03	n.a.	2.05	1.99	2.03	n.a.
Memo: U.S. production, total motor vehicles[4]	12.0	11.8	11.7	11.6	11.8	11.5	11.7	11.8

Note. FRB seasonals. Components may not sum to totals because of rounding.
1. Production rates for April and the second quarter reflect the latest schedules from Ward's Communications.
2. Annual and quarterly values are calculated with end-of-period stocks and average reported sales.
3. End-of-period stocks.
4. Includes medium and heavy trucks.
n.a. Not available.

Inventories of Light Vehicles



Days' Supply of Light Vehicles



slightly in the first quarter, and production will likely continue to fall in the coming months because deliveries to the U.S. armed forces are slated to drop in 2006.

The rate of growth in high-tech output slowed sharply in the first quarter. Semiconductor production increased only at an annual rate of 11½ percent, down from a 28 percent pace in the fourth quarter. Intel’s struggle with declining market share has slowed the domestic output of microprocessor units (MPUs), and the company’s revenue guidance for the second quarter suggests a continuation of double-digit declines in seasonally adjusted revenue.[6] In addition, Intel’s inventories have risen to record levels, and efforts to work off unwanted stocks will depress production even further. However, a broader inventory problem for semiconductors does not appear to be developing; major U.S. manufacturers besides Intel have kept supplies in line with easing sales.[7] Production of non-MPU chips also leveled off in the first quarter. Nonetheless, orders for semiconductor manufacturing equipment point to expansion in the semiconductor industry.

Downstream from semiconductors, the recent news on high-tech production has been mixed. The production of computers softened in the first quarter, as sales of PCs and servers to the U.S. market moved sideways; a temporary pause had been anticipated in advance of new product releases expected later this year. In contrast, the output of communications equipment continued to grow smartly. Major telecommunications service providers plan a more moderate expansion in capital expenditures in 2006 after rapid increases in 2005, but first-quarter reports show no signs of such a slowdown as yet.[8] The most recent CIO Magazine diffusion index of future spending, which reflects the plans of a broad array of businesses, points to increases in the production of computers and of communications equipment in coming quarters.

Manufacturing production excluding energy, transportation, and high-tech products picked up in March after a soft January and February. The production of consumer goods, business equipment, and construction supplies rebounded in March after temporary factors, such as the effect of EPA regulations on output of unitary air conditioners, held down production earlier in the year. In contrast, the production of

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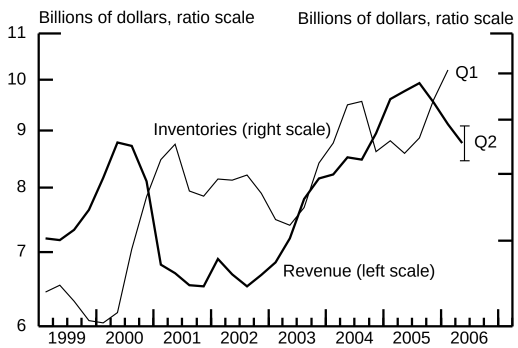
[6] Other things being equal, a loss in Intel market share implies lower U.S. production because AMD, Intel's primary competitor, produces its MPUs in Germany.

[7] However, an industry contact did point out some pockets of excess inventories of motherboards and laptops.

[8] Verizon, AT&T, and Sprint (including recent and pending acquisitions) anticipate a 4 percent increase in capital expenditures in 2006 after a 17 percent increase in 2005.

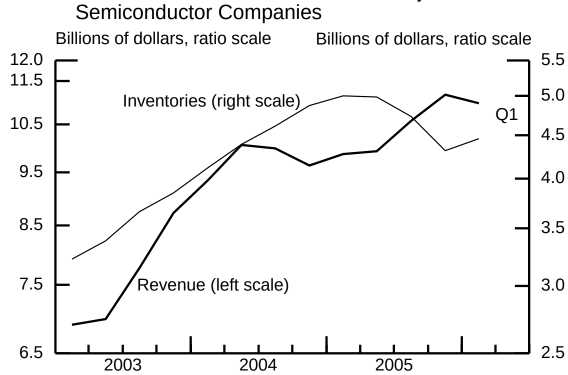
Indicators of High-Tech Manufacturing Activity

Intel Revenue and Inventories



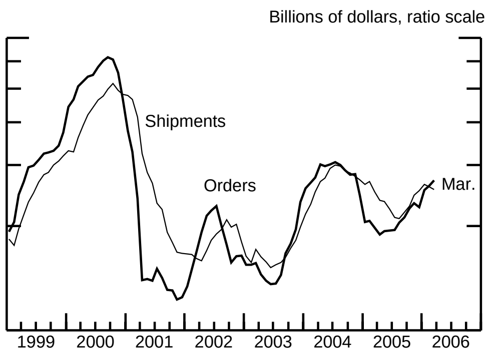
Note. Q2 is the range of Intel's revenue guidance as of April 19, 2006. FRB seasonals.
Source. Intel.

Revenue and Inventories at Other Major U.S. Semiconductor Companies



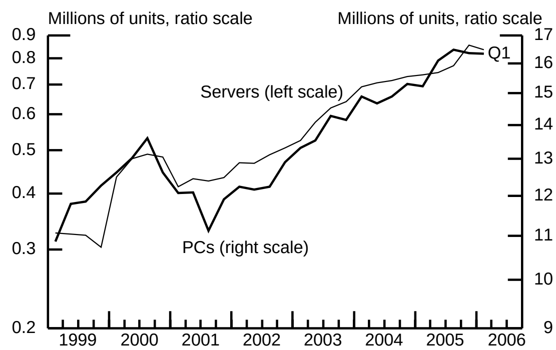
Note. Includes AMD, Texas Instruments, Freescale, Nvidia, ATI, National Semiconductor, Analog Devices, Broadcom, Micron. FRB Seasonals.
Source. Company reports.

Semiconductor Manufacturing Equipment Orders and Shipments



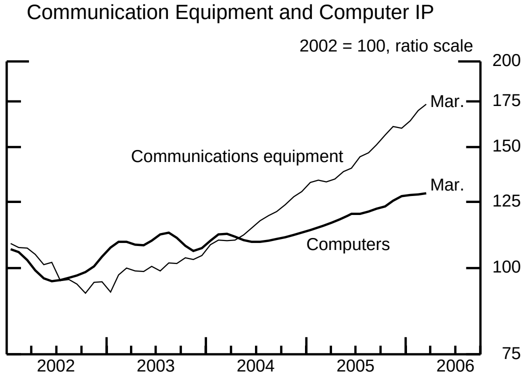
Note. FRB seasonals.
Source. Semiconductor Equipment and Materials International.

U.S. Personal Computer and Server Sales

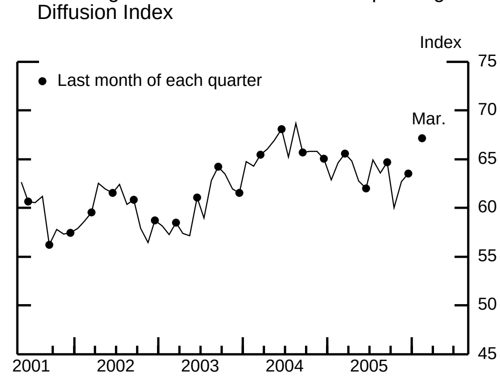


Source. Gartner.

Communication Equipment and Computer IP



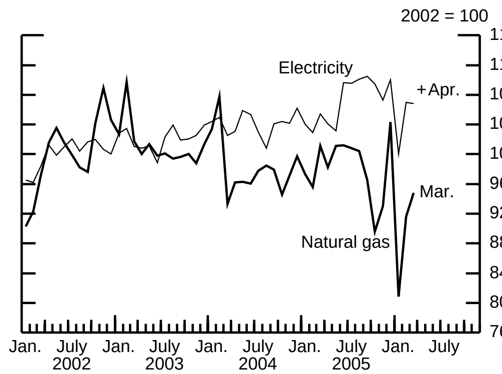
CIO Magazine IT Hardware Future Spending Diffusion Index



Note. The average of diffusion indexes for future spending on computer hardware, data networking equipment, telecom equipment, and storage systems.
Source. CIO Magazine. As of 2006, the survey is collected on the last month of each quarter.

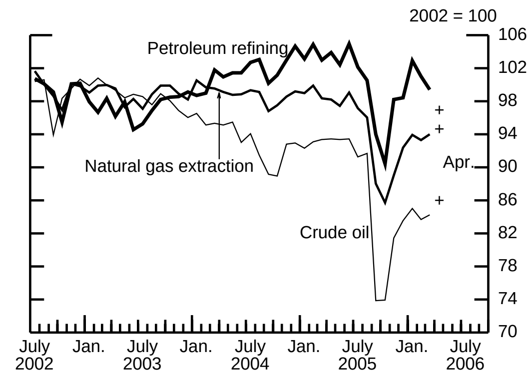
Indicators of Manufacturing Activity

Utilities Output



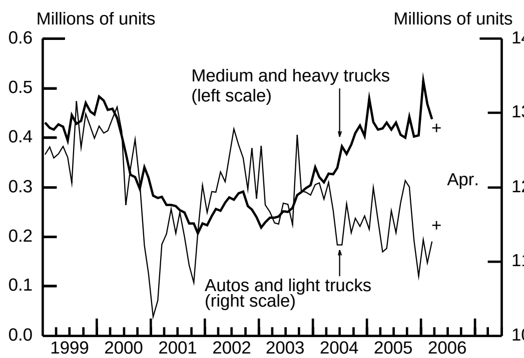
Note. April value for electricity generation is based on weekly data.

Energy IP



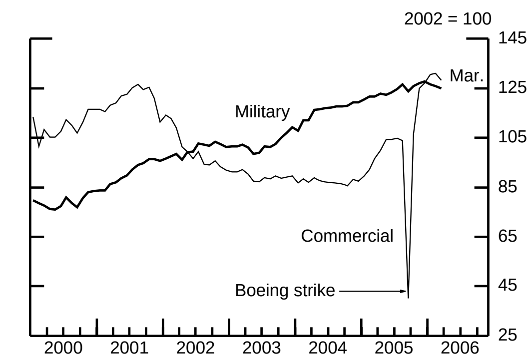
Note. April values are based on available weekly data and estimates of facilities that remain off line.

Motor Vehicle Assemblies

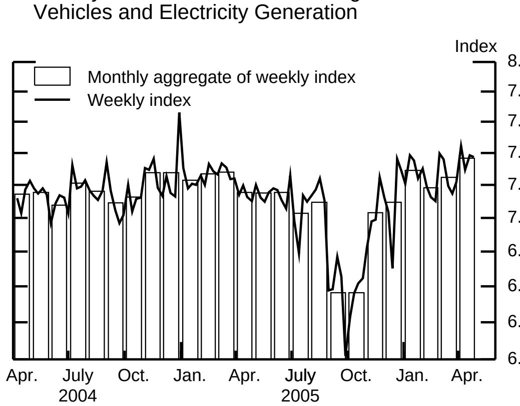


Note. April values are based on latest industry schedules.

IP for Aircraft

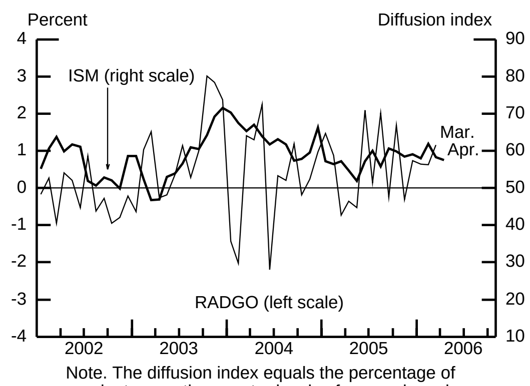


Weekly Production Index Excluding Motor Vehicles and Electricity Generation



Note. One index point equals 1 percent of 1997 total industrial output.

New Orders: ISM Survey and Change in Real Adjusted Durable Goods Orders (RADGO)



Note. The diffusion index equals the percentage of respondents reporting greater levels of new orders plus one-half the percentage of respondents reporting that new orders were unchanged. RADGO is a 3-month moving average.

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

Category	2005	2005 Q3	2005 Q4	2006 Q1	2006 Feb.	2006 Mar.	2006 Apr.
Total	16.9	17.9	15.8	16.9	16.5	16.5	16.7
Autos	7.7	8.0	7.5	7.8	7.4	7.4	8.0
Light trucks	9.2	10.0	8.3	9.1	9.1	9.1	8.7
North American[1]	13.5	14.5	12.6	13.5	13.2	13.0	12.9
Autos	5.5	5.7	5.4	5.7	5.4	5.3	5.6
Light trucks	8.0	8.8	7.2	7.7	7.8	7.7	7.2
Foreign-produced	3.4	3.5	3.3	3.4	3.3	3.5	3.8
Autos	2.2	2.3	2.1	2.1	2.0	2.1	2.4
Light trucks	1.2	1.2	1.2	1.3	1.3	1.4	1.4
Memo: Medium and heavy trucks	.50	.50	.51	.55	.56	.56	n.a.

Note. Components may not sum to totals because of rounding.
1. Excludes some vehicles produced in Canada that are classified as imports by the industry.
n.a. Not available.

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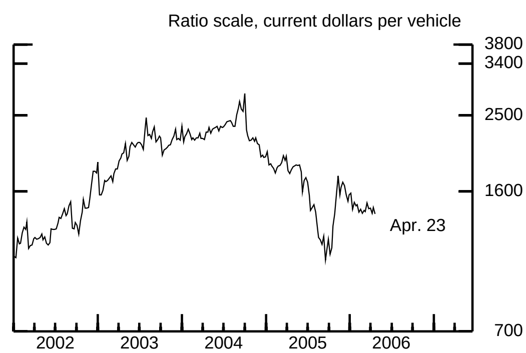
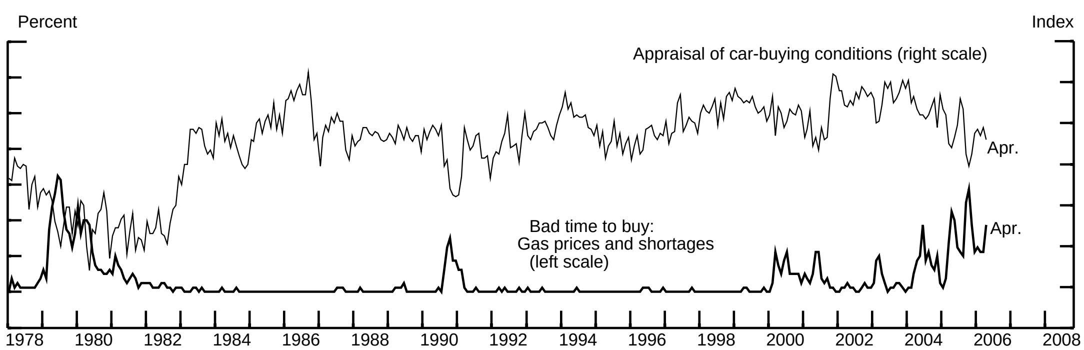
Average Value of Incentives on Light Vehicles



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

Michigan Survey Index of Car-Buying Attitudes



business supplies and materials slowed in February and March after rapid gains in preceding months. Weekly physical product data outside of energy and motor vehicles have edged up so far in April, a rise led by increases in the production of appliances.

Recent indicators of near-term manufacturing activity have been positive. Although the Institute for Supply Management's diffusion index for new orders ticked down in April, it remained at a level that suggests steady gains in output in the coming months. Likewise, the April readings on new orders from the New York and Philadelphia Fed surveys are down a bit from their March readings but are also consistent with continued increases in manufacturing production. The three-month moving average of the staff's measure of real adjusted durable goods orders rose 1.2 percent in March, consistent with moderate production increases in the near term.

Motor Vehicles

Sales of light vehicles were at an annual rate of 16.7 million units in April, a bit above the level in March. All of the increase last month was in sales of automobiles. In particular, manufacturers reported higher sales of smaller autos. In contrast, sales of light trucks fell to the lowest level of the year. The average pace of light vehicle sales thus far this year is well above the rate recorded in the fourth quarter but about even with the average pace in 2005.

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The Michigan Survey Research Center's index of car-buying attitudes edged down in April. Although the percentage of respondents reporting that it was a bad time to buy a car because of gas prices increased last month, it remained well below the high levels reported in the past summer. Average incentives appear to have flattened out in April after having edged down over the past several months. Industry analysts expect automakers to boost incentives in coming months in order to clear out inventories of 2006 models.

Consumer Spending

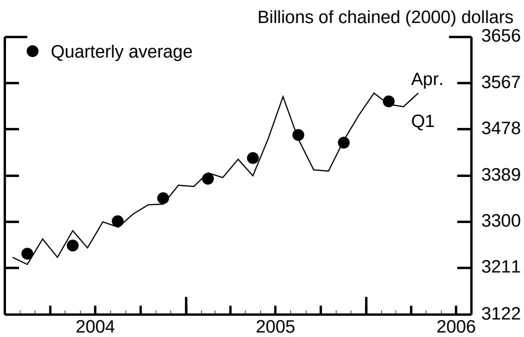
Growth of consumer spending appears to be moderating after posting sizable gains around the turn of the year. Excluding motor vehicles, real outlays rose a moderate 0.2 percent in March. Spending on services continued to rise, while spending on goods excluding motor vehicles posted a second-straight monthly decline after very robust gains over the previous four months. The weekly chain store sales data point to increased spending in this category in April.

Real Personal Consumption Expenditures
(Percent change from the preceding period)

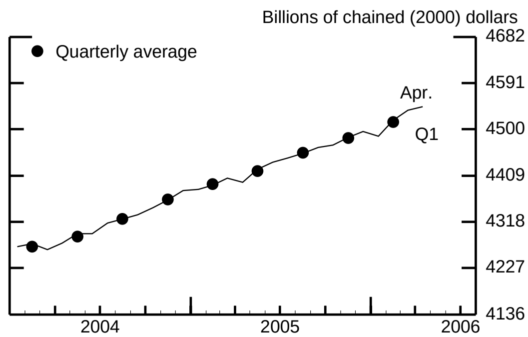
	2005		2006			
	Q3	Q4	Q1	Jan.	Feb.	Mar.
	Annual rate			Monthly rate		
Total real PCE	4.1	.9	5.5	.4	.2	.2
Durable goods	9.3	-16.6	20.6	1.8	-1.7	.6
Motor vehicles	12.7	-42.6	19.8	-2.4	-1.7	-.1
Excluding motor vehicles	6.7	10.2	21.1	4.8	-1.8	1.2
Nondurable goods	3.5	5.0	5.4	1.0	-.2	-.4
Energy[1]	-4.3	1.0	.8	-.6	2.0	-2.5
Other	4.7	5.5	6.1	1.3	-.5	-.2
Services	3.3	2.6	2.8	-.2	.7	.4
Energy[2]	6.2	1.5	-13.6	-12.3	13.0	-.5
Other	3.2	2.7	3.6	.3	.2	.5
Real PCE Control[3]	4.0	5.8	8.4	1.8	-.5	-.2

1. Includes gasoline, motor oil, fuel oil, and coal.
2. Includes natural gas and electricity usage for household operations.
3. Total goods spending excluding autos and trucks.

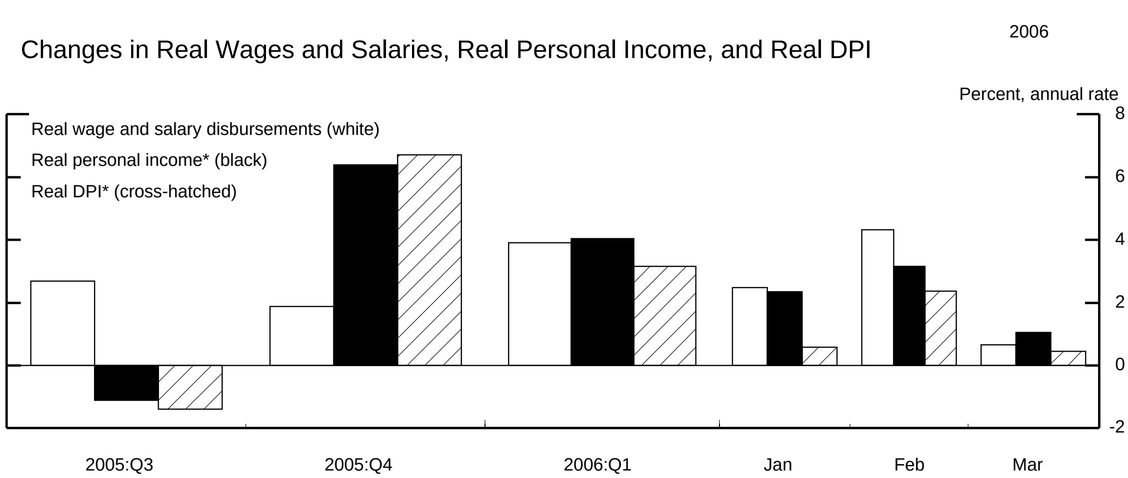
Real PCE Goods



Real PCE Services

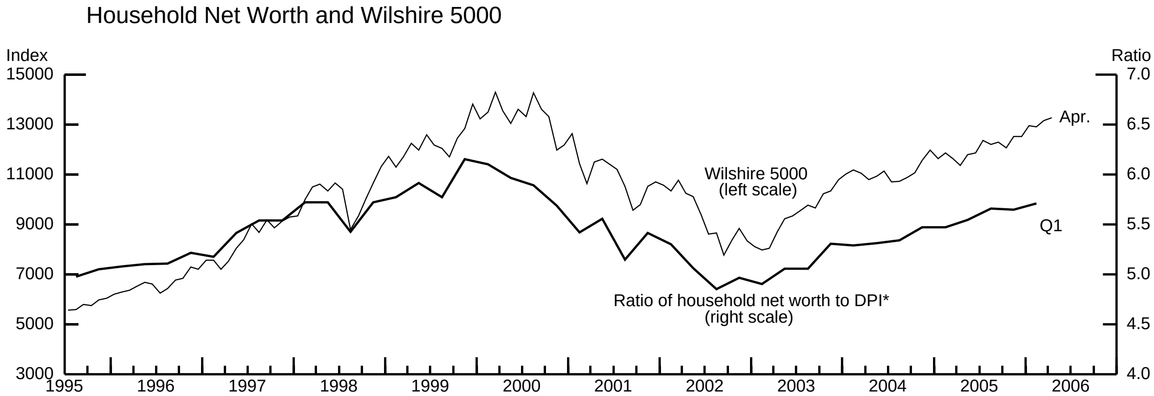


Changes in Real Wages and Salaries, Real Personal Income, and Real DPI

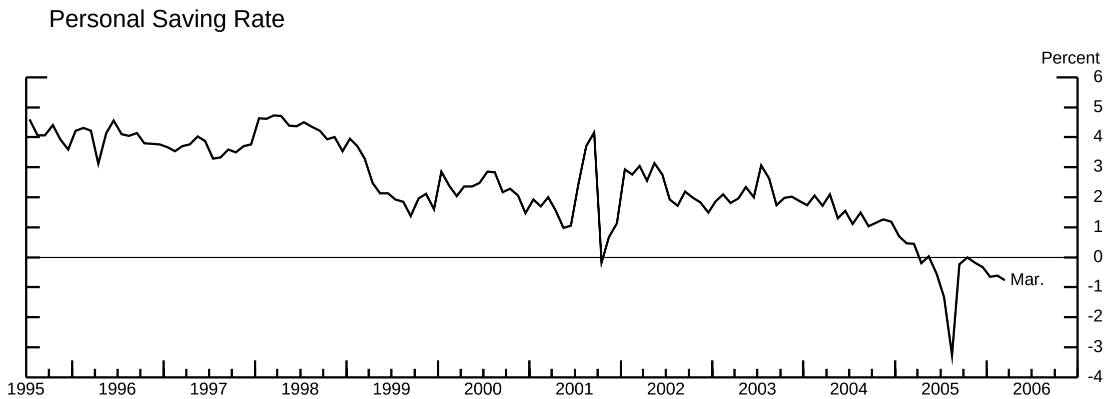


* The March 2006 figures correct the error in transfer payments in the published BEA personal income release.

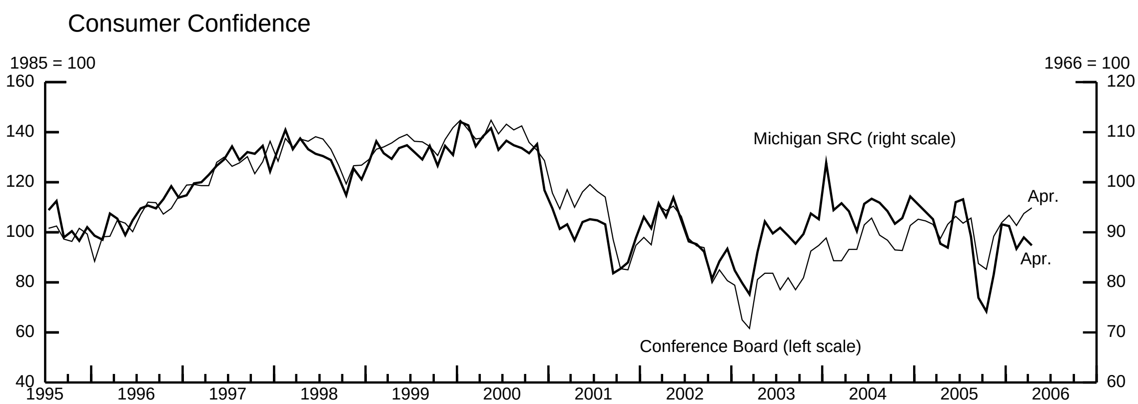
Household Indicators



* Value for 2004:Q4 excludes the effect on income of the one-time Microsoft dividend in December. Value for 2006:Q1 is a staff estimate.



Note. Value for December 2004 excludes the effect on income of the one-time Microsoft dividend in that month. The March 2006 figure corrects the error in transfer payments in the published BEA personal income release.



The fundamental determinants of consumer spending have been generally supportive of solid spending growth last quarter, though they have turned less positive recently. In particular, although continuing improvements in the labor market have been generating considerable gains in nominal wage and salary income, rising gasoline prices held down the rise in real disposable personal income in March and are expected to damp the change in real DPI in April as well. In addition, higher interest rates will likely restrain spending in the near term. In contrast, ongoing increases in home prices and additional gains in the stock market likely further boosted the ratio of household wealth to disposable income last quarter. Moreover, consumer confidence, as measured by both the Michigan survey and the Conference Board survey, remains consistent with moderate increases in consumer spending.

The personal saving rate fell to negative 0.8 percent in March, continuing its steady decline since last October.[9] However, all else being equal, we expect the published saving rate to be boosted ¾ percentage point by this year's annual retail sales revision. This revision does not imply a different contour of the saving rate over the past several months, though it does suggest a somewhat flatter path of the saving rate in recent years.[10]

Housing Markets

The underlying pace of residential construction has moderated in recent months. Single-family housing starts fell in March to an annual rate of 1.59 million units—the lowest level in a year. Part of this decline represents a payback for starts that had been pulled forward into January and February by unusually favorable weather conditions. However, the adjusted level of new permit issuance in this sector—which ticked down again in March— suggests that single-family starts will remain close to the March level in the coming months. In the multifamily sector, starts bounced back to an annual rate of 370,000 units in March, somewhat above their average level since 1995.

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[9] As published, the personal saving rate was negative 0.3 percent in March. However, that figure reflected an overstatement of transfer payments associated with the new Medicare Part D prescription drug plan. Because April 1 was a Saturday, the April payment occurred on March 31. The BEA mistakenly included that additional payment of $41 billion in its March estimate. It is planning to issue a correction this week.

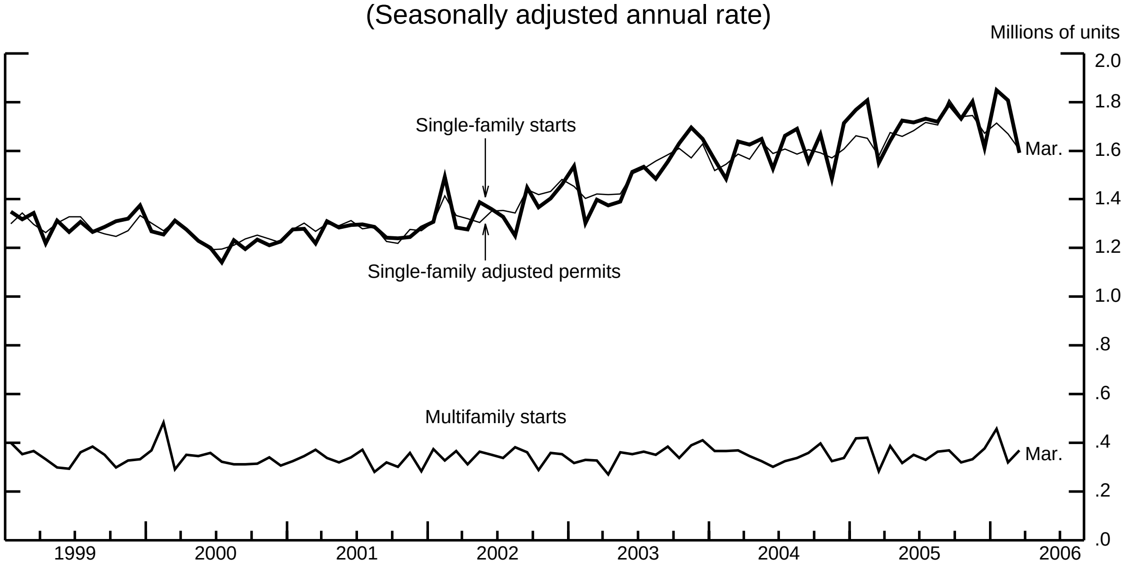
[10] The past two years' annual retail sales revisions together imply that the March saving rate is 1¼ percentage points higher than what is currently reported by the BEA. This summer, the BEA will incorporate the revisions to PCE control from this year's annual retail sales revision, which, as noted, should raise the published saving rate by about ¾ percentage point. BEA will not incorporate the remaining ½ percentage point upward revision to the saving rate, which will affect the saving rate prior to 2003, until the next comprehensive revision in 2008.

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

Sector	2005	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
All units						
Starts	2.07	2.06	2.13	2.31	2.13	1.96
Permits	2.15	2.11	2.16	2.22	2.18	2.09
Single-family units						
Starts	1.72	1.72	1.75	1.85	1.81	1.59
Permits	1.68	1.69	1.64	1.69	1.66	1.56
Adjusted permits[1]	1.69	1.72	1.66	1.71	1.67	1.60
Permit backlog[2]	.17	.17	.16	.17	.16	.16
New homes						
Sales	1.28	1.28	1.16	1.20	1.07	1.21
Months' supply[3]	4.45	4.70	5.70	5.20	6.30	5.50
Existing homes						
Sales	6.18	6.06	5.97	5.79	6.05	6.07
Months' supply[3]	4.40	4.90	5.20	5.10	5.10	5.30
Multifamily units						
Starts	.35	.34	.38	.46	.32	.37
Permits	.47	.42	.53	.53	.52	.53
Permit backlog[2]	.06	.06	.07	.06	.06	.07
Mobile homes						
Shipments	.15	.19	n.a.	.16	.15	n.a.
Condos and co-ops						
Existing home sales	.90	.88	.83	.78	.85	.85

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

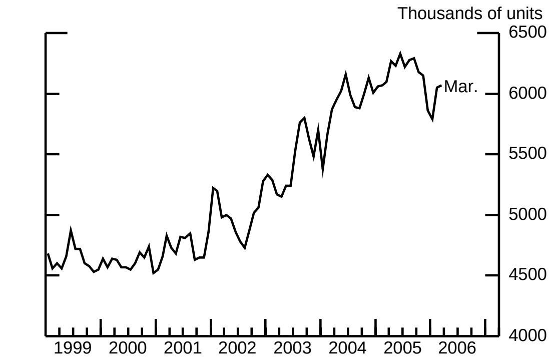
Private Housing Starts and Permits
(Seasonally adjusted annual rate)



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

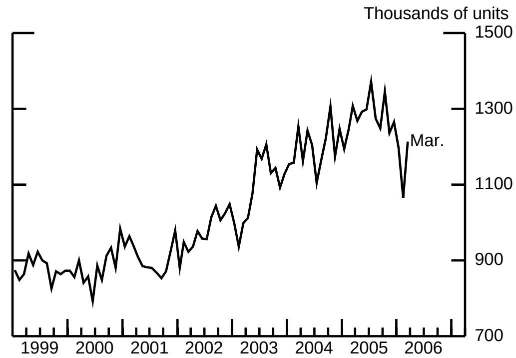
Indicators of Single-Family Housing

Existing Home Sales



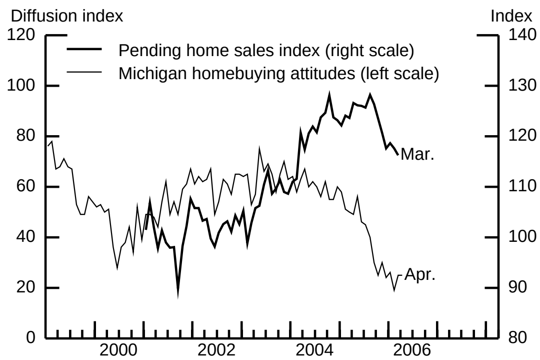
Source. National Association of Realtors.

New Home Sales



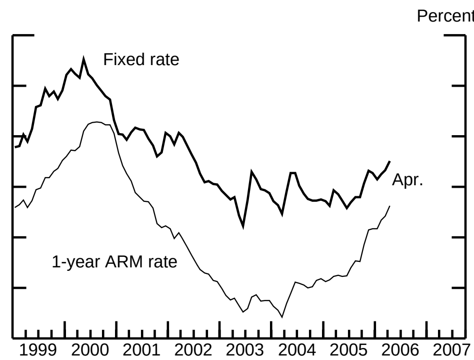
Source. Census Bureau.

Homebuying Indicators



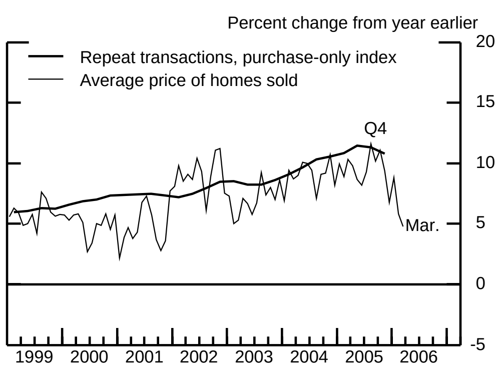
Source. National Association of Realtors and Michigan Survey.

Mortgage Rates



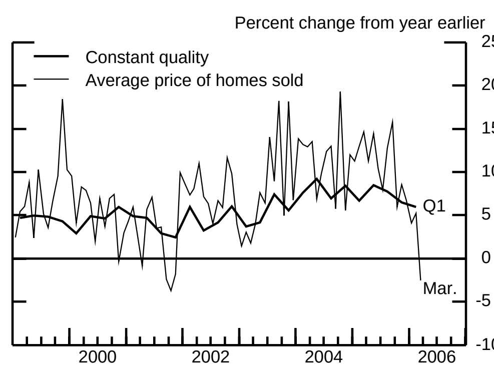
Note. The April readings are based on data through April 26, 2006.
Source. Freddie Mac.

Prices of Existing Homes



Source. For repeat transactions, OFHEO; for average price, National Association of Realtors.

Prices of New Homes



Note. Although average price values have been adjusted by Board staff to take into account new sampling procedures adopted in 2005, they may still not be directly comparable to earlier periods.
Source. Census Bureau.

Home sales have also declined, on net, in recent months. Although sales of existing single-family homes edged up in February and March, the level of sales for the first quarter as a whole was 4¾ percent below the record high in the second quarter of 2005. Sales of new homes also moved up in March, but their average level in the first quarter was down about 11 percent from the peak in the third quarter of last year.

Other indicators also support the view that housing markets have softened in recent months. Measures of months' supply of both new and existing homes have continued to trend higher, and the index of pending home sales—an indicator of existing home sales in the near term—in March stood 9½ percent below its level last August. In April, the Michigan index of homebuying attitudes was also well below its level of last summer. Housing demand should also be held down by higher mortgage rates. Since the peak of home sales in June 2005, the average rate for thirty-year fixed-rate mortgages has risen about 1 percentage point, while the average rate for one-year adjustable-rate mortgages has risen nearly 1½ percentage points.

House price appreciation appears to have slowed from the elevated rates seen over the past summer. The average sales price of existing homes in March was 5 percent above its year-earlier level, a sharp deceleration from the 8 to 10 percent increases seen in recent years.[11] The constant quality price index for new homes—which controls for changes in the geographic composition of sales, home size, and other readily measured attributes—was 6 percent higher in the first quarter than it was in the same period last year, its smallest year-over-year increase in two years. The average price of new homes declined in March relative to last year, but caution should be exercised when interpreting this drop because new sampling procedures implemented in 2005 have reduced the comparability of these prices to earlier periods.

Equipment and Software

Real outlays for equipment and software (E&S) surged at an annual rate of 17 percent in the first quarter after having risen at a relatively subdued annual rate of 5 percent in the final quarter of 2005. This pattern largely reflects sharp swings in spending on transportation equipment. Excluding transportation, E&S spending increased at an

[11] The purchase-only version of the OFHEO price index for existing homes, which controls for differences in quality by tracking repeat sales of the same houses over time, increased 11 percent over the four quarters ending in 2005:Q4. The OFHEO price index for the first quarter will not be published until June.

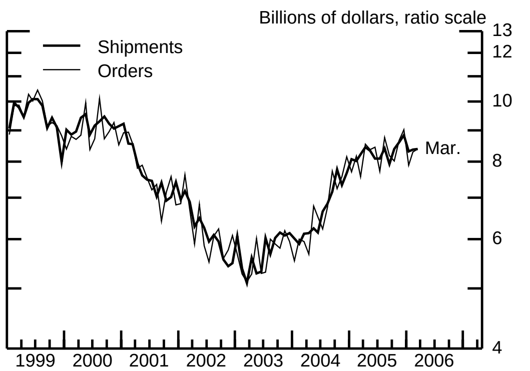
Orders and Shipments of Nondefense Capital Goods

(Percent change; seasonally adjusted current dollars)

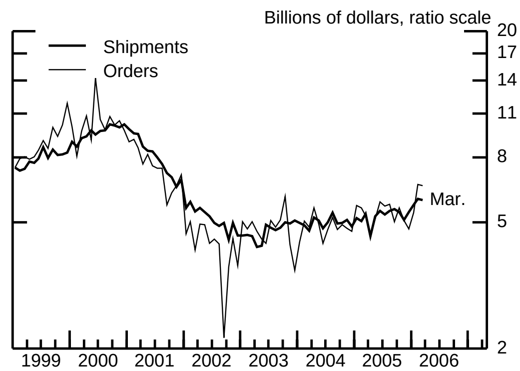
Category	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
	Annual rate		Monthly rate		
Shipments	35.1	5.0	-4.4	1.4	1.0
Excluding aircraft	15.6	12.3	.0	-.5	1.9
Computers and peripherals	24.2	-10.9	-5.7	.5	.2
Communications equipment	-9.2	48.3	5.5	4.4	-.6
All other categories	17.3	13.2	.4	-1.2	2.4
Orders	89.9	-27.2	-20.1	4.2	12.9
Excluding aircraft	11.9	17.7	.0	-.6	3.9
Computers and peripherals	17.7	-15.9	-12.4	5.2	1.1
Communications equipment	-21.3	106.0	12.1	22.9	-.7
All other categories	15.2	16.9	1.0	-3.8	4.9
Memo:					
Shipments of complete aircraft[1]	26.9	n.a.	33.9	29.7	n.a.

1. From Census Bureau, Current Industrial Reports; billions of dollars, annual rate.
n.a. Not available.

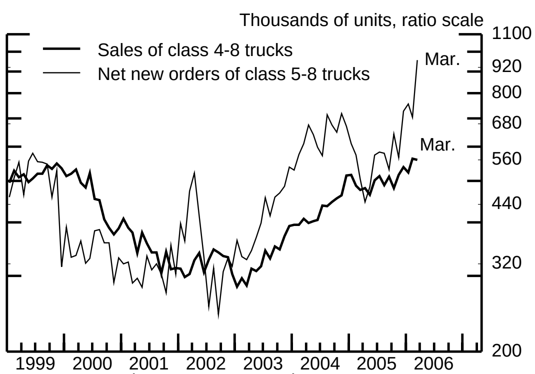
Computers and Peripherals



Communications Equipment

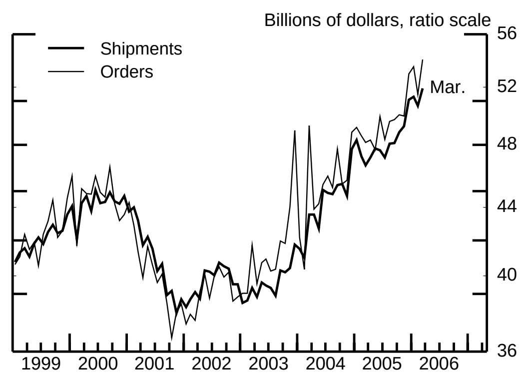


Medium and Heavy Trucks



Note. Annual rate, FRB seasonals.
Source. For class 4-8 trucks, Ward's Communications; for class 5-8 trucks, ACT Research.

Non-high-tech, Non-trans. Equipment



annual rate of 12¾ percent in the first quarter, after an 8½ percent gain in the fourth quarter.

Business outlays for transportation equipment jumped at an annual rate of more than 40 percent in the first quarter of this year. Expenditures on domestic aircraft moved up sharply from the fourth quarter's low value,

. Business purchases of motor vehicles also surged in the first quarter.

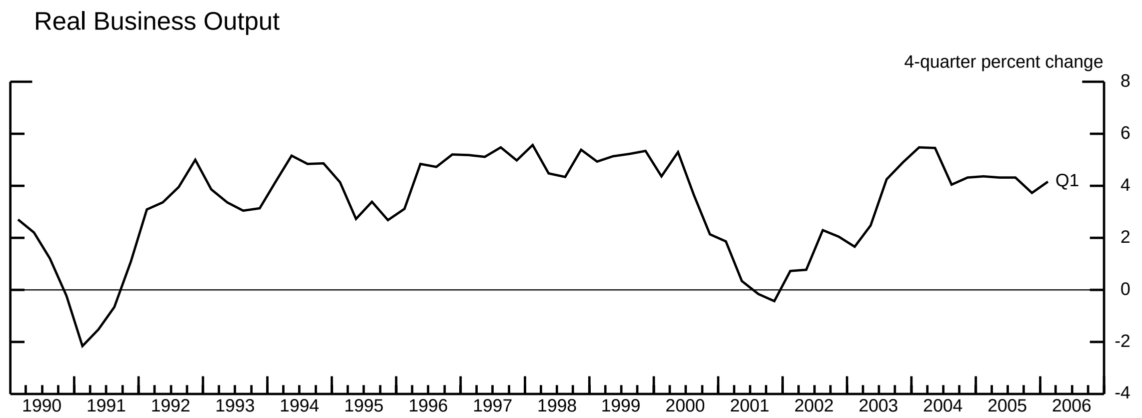
. In addition, the pace of medium and heavy truck sales moved up from the already rapid pace of the previous quarter. According to industry analysts, much of the recent strength in medium and heavy truck purchases reflects a pull-forward in advance of the 2007 EPA regulations on engines. March's record-high orders for medium and heavy trucks suggest that demand will remain strong in the near term.

Real spending on high-tech equipment and software increased at an annual rate of 18 percent in the first quarter, the result of exceptionally strong growth in outlays for communications equipment but fairly soft spending on computers and peripherals and software. Nominal orders and shipments of computers increased in both February and March; these gains reversed part of the January declines, and suggest that computer investment is on a somewhat stronger trajectory going into the second quarter. In the communications sector, orders and shipments declined in March after having risen sharply earlier in the year.

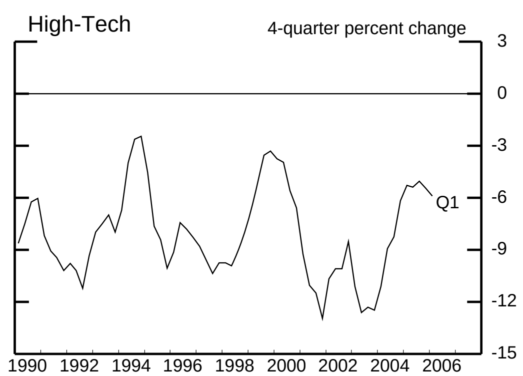
Business spending on equipment other than high tech and transportation increased 8¼ percent in the first quarter, continuing the strong growth in this category that began in the middle of last year. In March, orders and shipments turned up, reversing their February declines. These data suggest that spending in this category of equipment will rise further in the near term.

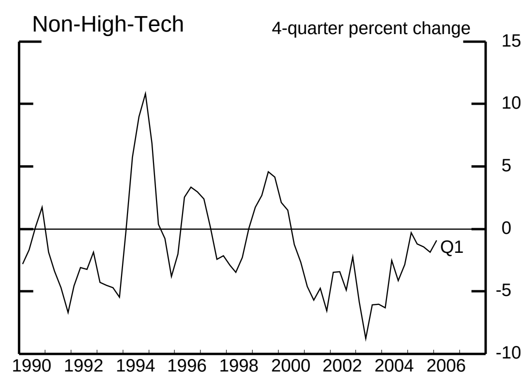
Looking ahead, the underlying fundamentals continue to be supportive of increased business investment. Growth of output and final sales remains brisk, firms' coffers are flush with cash, the user cost of capital continues to decline as the relative prices of both high-tech and non-high-tech equipment maintain their downward trends, and business surveys indicate ongoing expansions of capital spending plans.

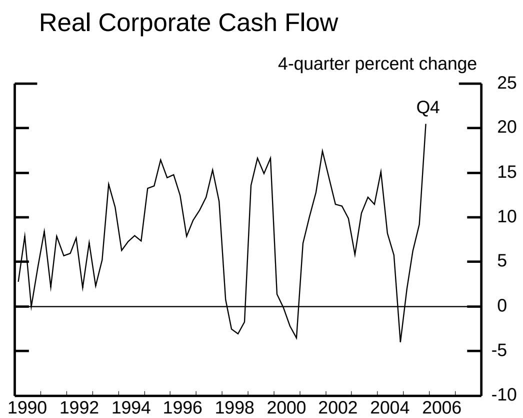
Fundamentals of Equipment and Software Investment

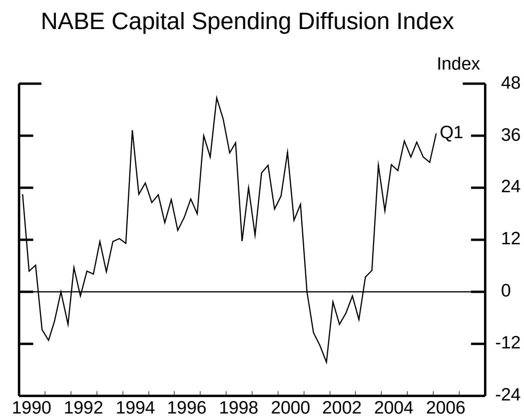


User Cost of Capital









Note. The diffusion index equals the percentage of respondents planning to increase spending minus the percentage of respondents planning to reduce spending.
Source. NABE Industry Survey.

Nonresidential Construction

Conditions in the nonresidential construction sector have improved noticeably of late. Although the level of spending on nonresidential building construction remains well short of the robust levels seen in late 2000, first-quarter spending growth in this sector was at its fastest pace in nearly six years. The rise in construction was broad-based; among the major categories, only the commercial sector did not pick up. This sector has not shown any significant signs of improvement even though vacancy rates remain low by historical standards.

Outlays on drilling and mining structures have continued to climb, growing at an annual rate of 9½ percent in the first quarter. The numbers of rigs drilling for natural gas and petroleum have moved up further in recent months, pointing to a further rise in expenditures in this sector in the current quarter.

Business Inventories

We estimate that real nonfarm inventories increased $29 billion in the first quarter, down from a real increase in stocks of $43 billion in the fourth quarter of last year.[12] The step-down in inventory investment reflects a decline in investment in motor vehicle inventories, which had accumulated rapidly in the fourth quarter. We estimate that real nonfarm inventories excluding motor vehicles increased about $34 billion in the first quarter, well above the pace in the fourth quarter. Over the past twelve months, inventories relative to shipments and sales have moved down moderately on average, continuing their long-run downward trend.

Information from the staff's flow-of-goods inventory system suggests that—excluding motor vehicles and parts—inventory-consumption ratios fell in March after having edged up in January and February. Outside of paper products and semiconductors, where stocks remain excessive, inventories appear to remain well aligned with consumption. Business surveys suggest that firms view their customers' inventory levels to be in a comfortable range.

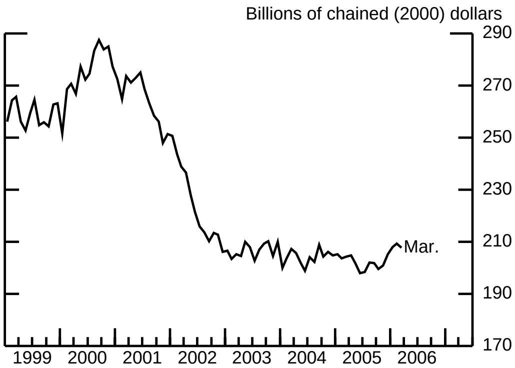
[12] This estimate is $3 billion higher than the BEA advance estimate because it incorporates March manufacturing inventories which were unavailable at the time of the BEA release.

Nonresidential Construction and Indicators

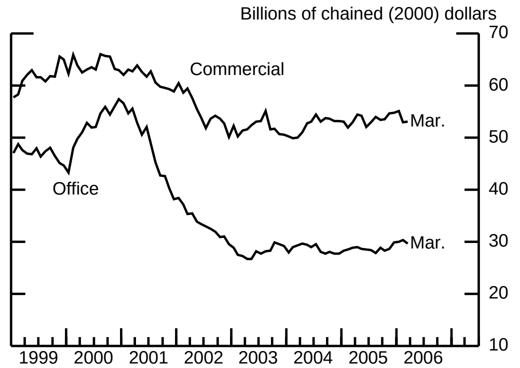
Real Construction

(Seasonally adjusted, annual rate; nominal CPIP deflated by BEA prices through Q4 and by staff projection thereafter)

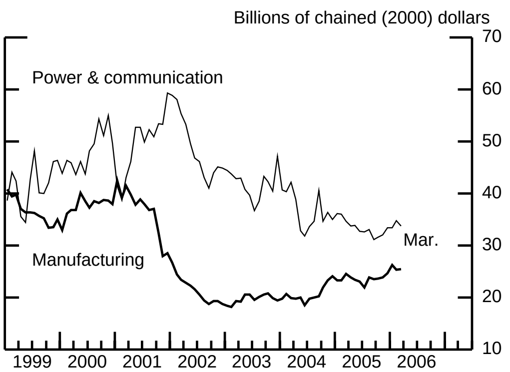
Total Structures



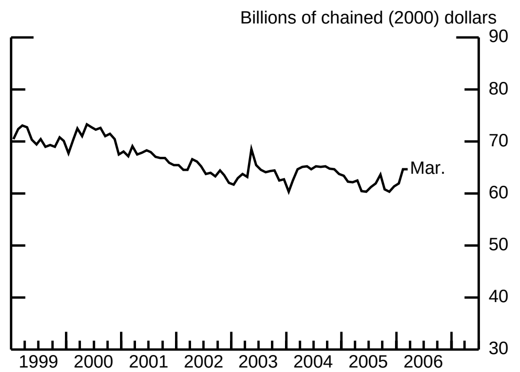
Office and Commercial



Manufacturing and Power & Communication



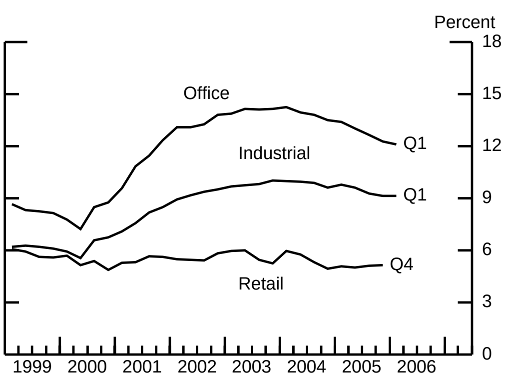
Other



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

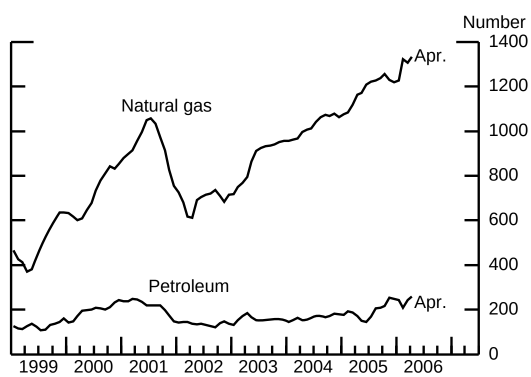
Indicators

Vacancy Rates



Source. For office and industrial, CoStar Property Professional; for retail, National Council of Real Estate Investment Fiduciaries.

Drilling Rigs in Operation



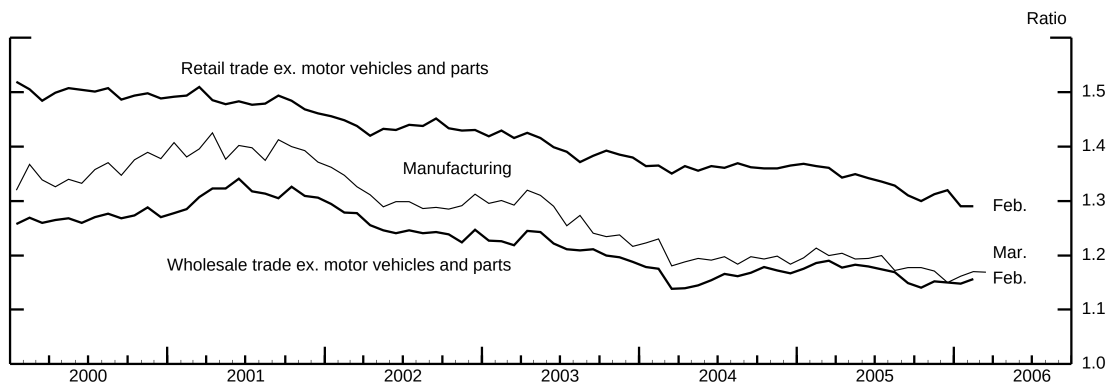
Note. April values are averages through April 28, 2006.
Source. DOE/Baker Hughes.

Changes in Nonfarm Inventories
(Billions of chained (2000) dollars; annual rate)

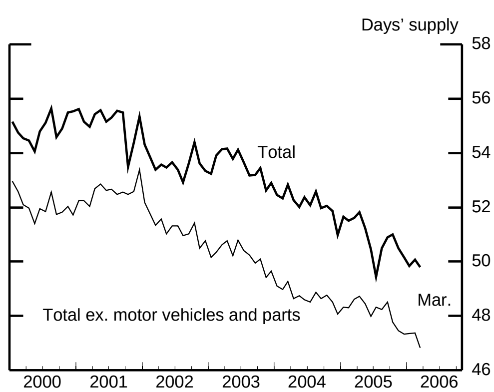
Category	2005 Q1	2005 Q2	2005 Q3	2005 Q4	2006 Q1*
Nonfarm inventory investment	61.8	3.4	-8.1	43.0	28.9
Excluding finished motor vehicles and parts	66.5	22.8	11.5	16.3	33.8
Manufacturing	24.1	-8.2	-2.6	.7	11.7
Merchant wholesalers	18.5	8.0	11.6	7.3	4.4
Retail trade	11.5	10.7	1.8	6.7	-.5
Memo: Manufacturing and trade ex. motor vehicles and parts (book value)	87.8	32.5	38.2	60.4	28.3

* Staff estimate.

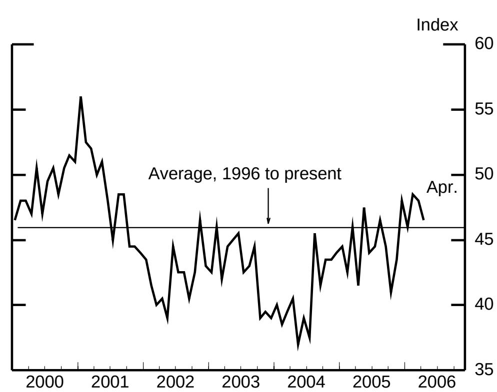
Book-Value Inventories Relative to Shipments and Sales



Inventory-Consumption Ratios, Flow-of-Goods System



ISM Customer Inventories: Manufacturing



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

Federal Government

The federal budget deficit, adjusted for payment timing shifts and financial transactions, showed continued improvement in March.[13] According to the Monthly Treasury Statement, the federal government recorded a deficit of $59 billion, about $11 billion lower than the deficit posted a year earlier. Over the twelve months ending in March, the adjusted deficit was almost $100 billion lower than the deficit recorded over the comparable period a year earlier.

Much of this improvement resulted from strong inflows of tax receipts, which were almost 17 percent higher this March than last. Withheld individual income and social insurance tax receipts were about 9 percent higher, while corporate income tax payments, primarily final payments on last year's corporate tax liability, were 27 percent above the year-earlier level. Daily Treasury Statements show continued robust increases in taxes in April and May: Final payments on individual tax liability for 2005 have come in about 30 percent above those of last year and the first quarterly corporate payments on expected tax liability for 2006 were about 25 percent higher than those of last year.

Federal outlays in March increased more slowly than receipts but still were 6 percent above last year's level. Defense spending in March was almost 11 percent higher than the year-earlier level. March outlays for the new Medicare Part D prescription drug program were about $3 billion, approximately the same amount as in February. Anecdotal reports suggest that Medicare outlays may pick up a bit in coming months as enrollment rises in response to the May 15 deadline. Medicaid spending was about 9 percent lower in March than it was last year; this decline reflects the shift to Medicare of drug spending for elderly Medicaid patients as well as apparent delays in federal Medicaid payments to some big states.

The relatively brisk pace of federal spending was also reflected in NIPA federal purchases in the first quarter. Real NIPA defense purchases increased at an annual rate of 10¼ percent, while spending for hurricane disaster relief helped boost the growth of real NIPA nondefense purchases to an annual rate of 11¾ percent.

Several legislative actions that would affect the budget remain unresolved. A supplemental appropriations bill providing additional funding for the war on terrorism

[13] Apart from our routine timing shift adjustments, we have made an additional adjustment to March refunds and EITC outlays. Refund payments are typically very large on Fridays, and there were five Fridays this March, as opposed to four last year.

Federal Government Outlays and Receipts

(Unified basis; billions of dollars except as noted)

Function or source	March 2005	March 2006	March Percent change	12 months ending in March 2005	12 months ending in March 2006	12 months ending in March Percent change
Outlays	220.0	250.0	13.7	2374.5	2578.8	8.6
Financial transactions[1]	.7	.3	...	-.7	-1.7	...
Payment timing[2]	.0	17.5	...	-.2	17.0	...
Adjusted outlays	219.2	232.2	5.9	2375.4	2563.4	7.9
Receipts	148.8	164.6	10.6	1968.5	2251.9	14.4
Payment timing[2]	.0	9.0	...	.0	9.0	...
Adjusted receipts	148.8	173.6	16.7	1968.5	2260.9	14.9
Surplus or deficit (-)	-71.2	-85.5	...	-406.1	-326.8	...
Selected components of adjusted outlays and receipts						
Adjusted outlays	219.2	232.2	5.9	2375.4	2563.4	7.9
Net interest	15.0	19.4	29.2	167.7	205.5	22.5
Non-interest	204.2	212.9	4.2	2207.6	2357.9	6.8
National defense	43.7	48.4	10.6	473.2	506.9	7.1
Social Security	43.5	46.2	6.3	508.8	538.0	5.7
Medicare	26.6	32.4	21.8	281.7	314.6	11.7
Medicaid	17.2	15.6	-9.4	179.5	181.4	1.1
Income security	36.8	36.5	-.9	339.2	347.7	2.5
Agriculture	.2	1.7	...	23.3	32.2	37.9
Other	36.1	32.0	-11.3	401.8	437.1	8.8
Adjusted receipts	148.8	173.6	16.7	1968.5	2260.9	14.9
Individual income and payroll taxes	106.4	110.0	3.4	1549.5	1730.5	11.7
Withheld + FICA	137.5	150.2	9.2	1442.7	1545.7	7.1
Nonwithheld + SECA	8.0	12.0	49.2	292.7	379.2	29.6
Less: Refunds	39.1	43.2	10.4	188.0	185.4	-1.4
Corporate	27.0	35.9	32.9	221.9	308.7	39.2
Gross	30.8	39.2	27.1	255.5	337.4	32.1
Less: Refunds	3.8	3.2	-14.4	33.6	28.7	-14.8
Other	15.3	27.6	80.5	197.1	221.7	12.5
Adjusted surplus or deficit (-)	-70.5	-58.7	...	-406.9	-302.5	...

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

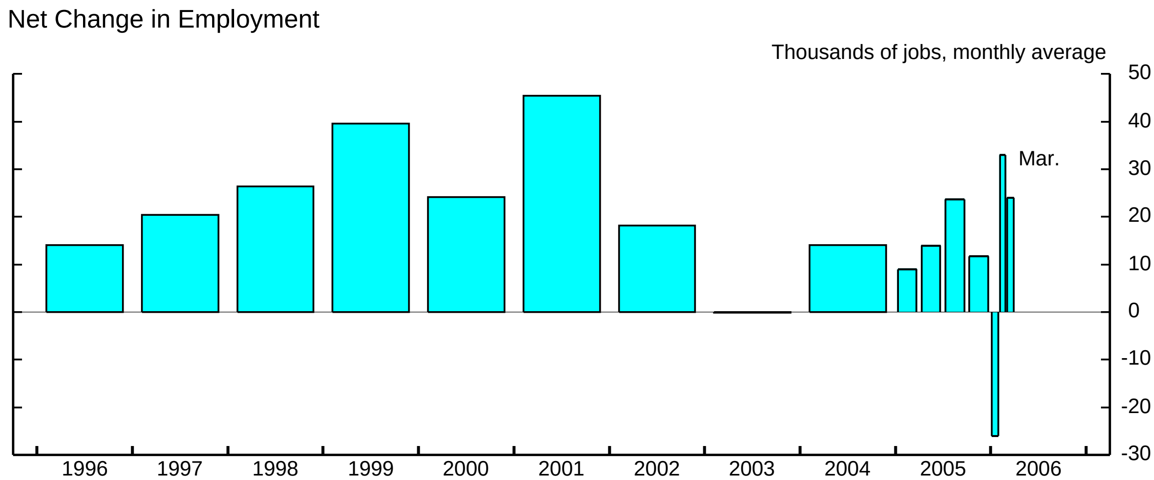
1. Financial transactions consist of deposit insurance, spectrum auctions, and sales of major assets.

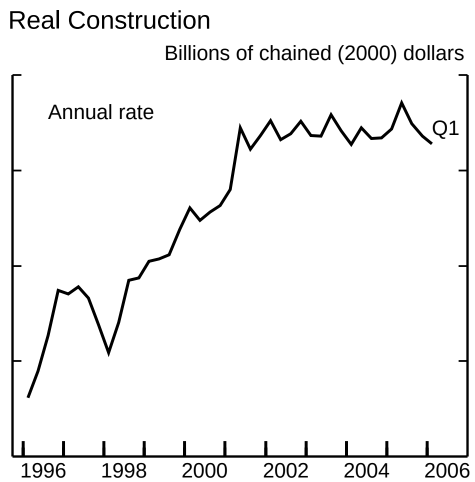
2. A shift in payment timing occurs when the first of the month falls on a weekend or holiday, or when the first 3 days of a month are nonworking days. Outlays for defense, Social Security, Medicare income security, and "other" have been adjusted to account for these shifts. In addition, defense outlays for retiree health have been converted from an annual to a monthly basis. Tax refunds and EITC outlays have been adjusted to reflect a calendar anomaly that boosted payments in March. These payments are large on Fridays, and this March had five Fridays as opposed to four last year.

... Not applicable.

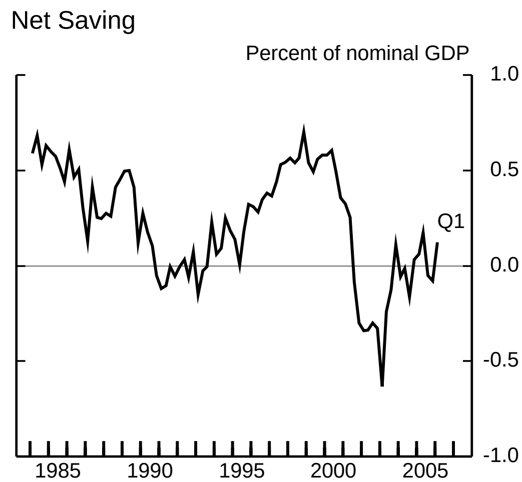
Source. Monthly Treasury Statement.

State and Local Indicators

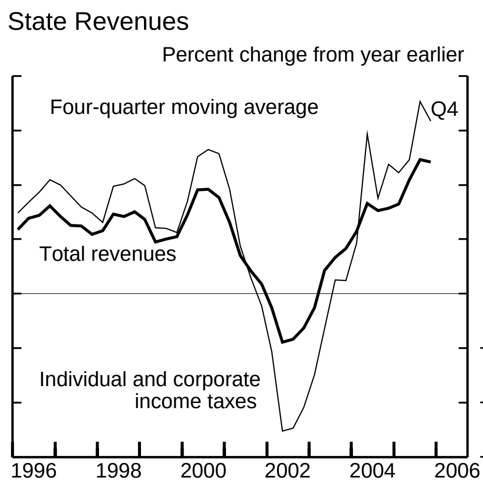




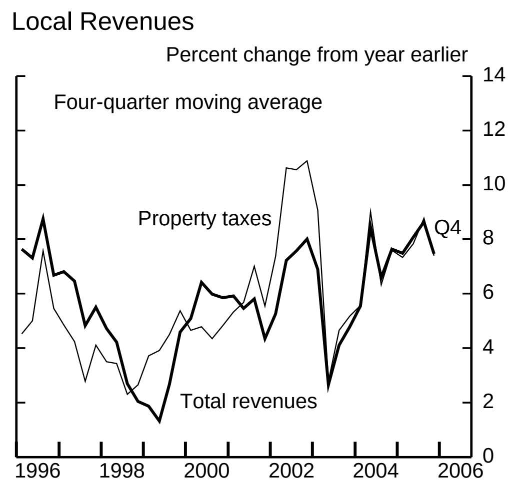
Note. Nominal CPIP deflated by BEA prices.



Note. 2006:Q1 is a staff estimate.



Source. Census Bureau.



Source. Census Bureau.

and for hurricane disaster relief has passed the House, but a larger bill that would add even more funding for disaster relief and other nondefense programs is under consideration in the Senate. In addition, the House and Senate have been unable to agree on a final tax reconciliation bill for fiscal 2006. This legislation is likely to extend both the alternative minimum tax relief that expired at the end of 2005 and the lower rates on dividends and capital gains that are set to expire after 2008. Finally, the Senate passed a budget resolution that would allow $16 billion more in budget authority for fiscal 2007 than was requested in the President's budget, but the House has not yet been able to pass a fiscal 2007 budget resolution.

State and Local Government Sector

Real state and local purchases appear to have posted another small increase in the first quarter of 2006.[14] Employment rose 10,000 per month, on average, during the first quarter, a rate consistent with the gradual pace of hiring that has been evident over the past two years. All of the first-quarter hiring was by local governments. Meanwhile, real construction expenditures fell again in the first quarter and stood around the lower end of the narrow range that has prevailed since 2002.

The recent news on the sector's fiscal situation has generally been favorable. On the basis of partial data, we estimate that the NIPA measure of state and local net saving—which is similar to the surplus in an operating budget—exceeded $15 billion at an annual rate in the first quarter after having totaled just $3 billion in 2005. The National Conference of State Legislatures likewise reported that state budget positions have continued to improve and attributed the improvement to robust growth in revenues. Local governments also appear to have fared relatively well of late, mainly because of substantial increases in property taxes, which rose 7½ percent in calendar year 2005 after a similar increase in 2004.

Prices

Overall PCE prices rose 0.4 percent in March after having edged up 0.1 percent in February. The March upturn reflected a jump in energy prices as well as an above-average increase in core prices. During the twelve months ending in March, overall PCE

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[14] We estimate that real spending on consumption and gross investment by state and local governments rose at an annual rate of about ½ percent in the first quarter, whereas the BEA's advance estimate had shown no change. The anticipated revision is based on the monthly construction data, which became available after the NIPA release and imply that real construction fell at an annual rate of about 3 percent in the first quarter; the advance NIPA estimate had shown a drop in real construction of 7½ percent.

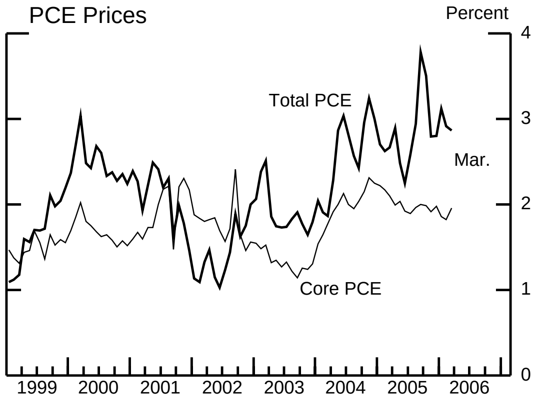
Measures of Inflation
(Percent)

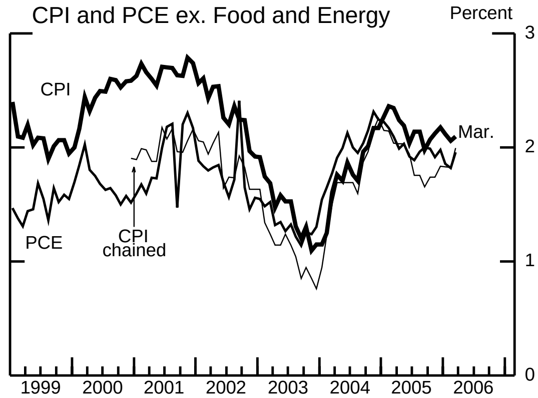
Measures	12-month change		3-month change		1-month change	
			Annual rate		Monthly rate	
	Mar. 2005	Mar. 2006	Dec. 2005	Mar. 2006	Feb. 2006	Mar. 2006
CPI						
Total	**3.1**	**3.4**	**-1.8**	**4.3**	**.1**	**.4**
Food	2.5	2.6	2.5	2.5	.1	.1
Energy	12.4	17.3	-34.7	21.8	-1.2	1.3
Ex. food and energy	**2.3**	**2.1**	**2.6**	**2.8**	**.1**	**.3**
Core goods	.6	.3	-.3	1.4	-.1	.3
Core services	3.0	2.8	3.9	3.4	.3	.3
Chained CPI (n.s.a.)[1]	2.7	3.0	...	...	...	...
Ex. food and energy[1]	2.0	2.0	...	...	...	...
PCE prices						
Total	**2.7**	**2.9**	**-.8**	**3.7**	**.1**	**.4**
Food	2.3	2.5	2.2	2.6	.1	.1
Energy	12.7	17.2	-36.4	22.8	-1.1	1.4
Ex. food and energy	**2.1**	**2.0**	**2.2**	**2.5**	**.1**	**.3**
Core goods	.2	-.2	.2	.8	-.2	.2
Core services	2.9	2.9	3.0	3.3	.3	.4
Core market-based	1.7	1.6	1.9	2.2	.1	.3
Core non-market-based	3.9	3.5	3.6	4.3	.3	.3
PPI						
Total finished goods	**5.0**	**3.5**	**4.1**	**-2.5**	**-1.4**	**.5**
Food	3.7	-1.4	5.0	-7.6	-2.7	.5
Energy	15.7	15.6	15.1	-11.6	-4.7	1.8
Ex. food and energy	**2.6**	**1.7**	**.0**	**3.1**	**.3**	**.1**
Core consumer goods	2.5	1.9	.2	3.2	.2	.2
Capital equipment	2.6	1.5	-.3	2.5	.1	.1
Intermediate materials	8.7	7.0	7.0	3.0	-.3	-.1
Ex. food and energy	7.6	4.4	8.2	6.7	.5	.1
Crude materials	11.4	4.9	5.9	-40.3	-9.2	-2.7
Ex. food and energy	2.4	13.3	9.8	16.9	3.3	.8

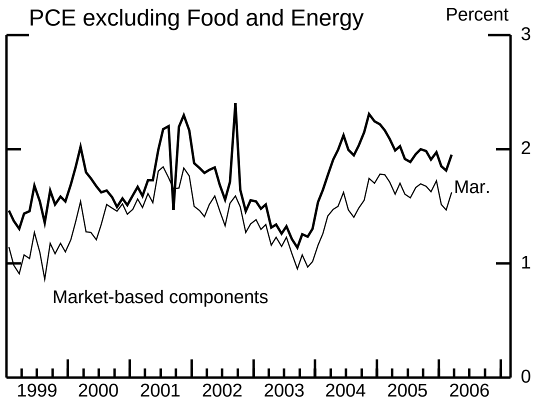
1. Higher-frequency figures are not applicable for data that are not seasonally adjusted.
... Not applicable.

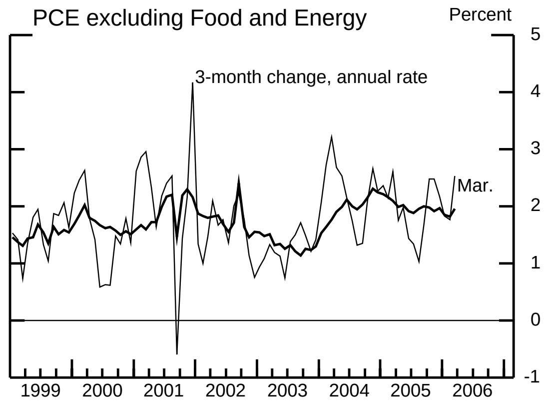
Consumer Price Inflation

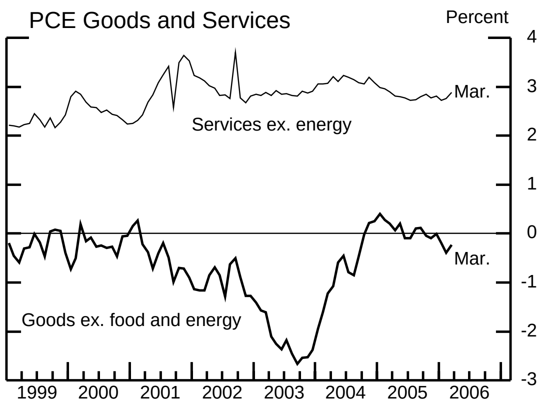
(12-month change except as noted)

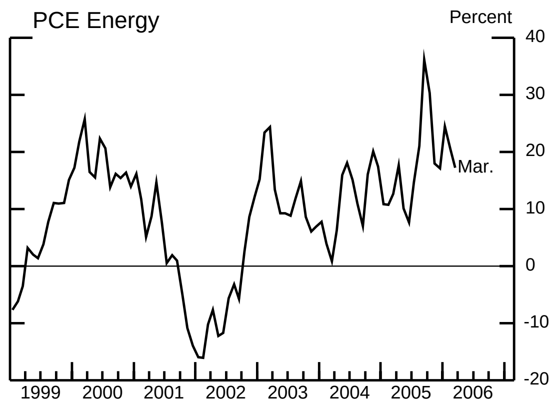












prices rose 2.9 percent, a slightly faster pace than that of the preceding twelve-month period. Excluding food and energy, the twelve-month change in PCE prices was 2.0, a bit less than in the previous year.

PCE energy prices increased 1.4 percent in March, more than reversing February's decline. Although the price of natural gas fell again because of continued plentiful inventories, retail gasoline prices have surged almost 70 cents per gallon (n.s.a.) since their recent trough in mid-February. About half of that increase reflects higher crude oil costs, while the remainder represents higher gasoline margins.

The bulk of the increase in gasoline margins is due to the tight supply situation. Gasoline inventories ran off sharply in March and April, as an unusual amount of refinery maintenance and repairs delayed the normal seasonal pickup in gasoline production. In addition, some of the recent increase in gasoline prices is the result of a switch by refiners to a more expensive method of producing reformulated gasoline that relies on ethanol.[15] Finally, concerns about disruptions in supply this summer have probably raised wholesalers' desired inventories above the level that is normal for the season.

PCE food prices inched up 0.1 percent in both February and March after a large increase in January; the twelve-month change was 2.5 percent. The March figure was held down by a substantial decline in consumer prices of fresh fruits and vegetables that offset some of their increases over the previous three months.

Core PCE price inflation increased 0.3 percent in March, after increase of 0.1 percent in January and February. Much of this pickup in core price inflation reflected a jump in the index for apparel that unwound its February decline. In addition, core inflation was boosted by a one-time step-up in medical prices resulting from the Congress's repeal of a 4½ percent cut in Medicare payments to physicians that had been implemented in January. Over the twelve months ending in March, prices of non-energy services rose 2.9 percent, the same as the year-earlier increase, while core goods prices edged down 0.2 percent, compared with a small increase in the previous year.

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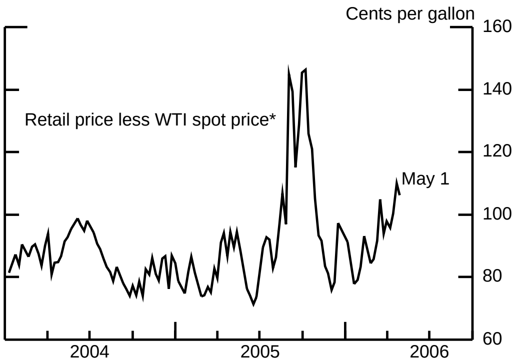
[15] In the past, gasoline with the additive MTBE was mandated by the Clean Air Act for use in areas of the country with particularly high levels of smog. However, these regulations are set to expire on May 5. Out of fear of litigation over MTBE's contribution to water pollution and under federal and state pressure to increase their use of ethanol, gasoline producers are already making reformulated gasoline with ethanol instead of MTBE, even though the ethanol mix is at least 15 cents per gallon more costly to produce and distribute than the MTBE mix. Reformulated gasoline constitutes about 30 percent of total U.S. gasoline consumption.

Energy Prices and Inventories

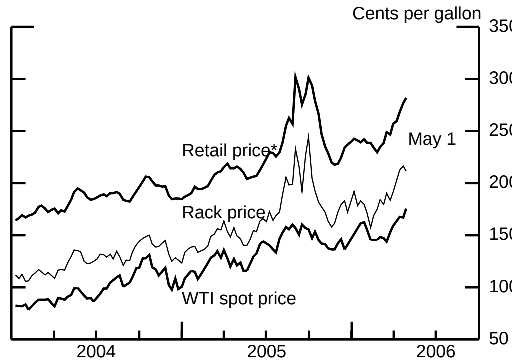
(Data from Energy Information Administration except as noted)

Total Gasoline Margin



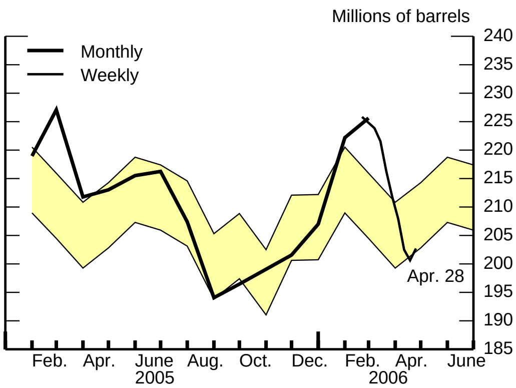
* Regular grade seasonally adjusted by FRB staff, less West Texas intermediate spot price.

Gasoline Price Decomposition



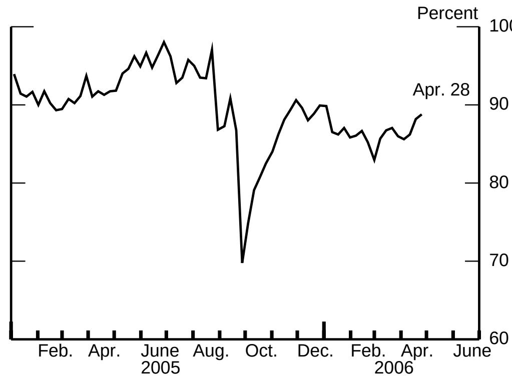
* Regular grade seasonally adjusted by FRB staff.

Gasoline Inventories

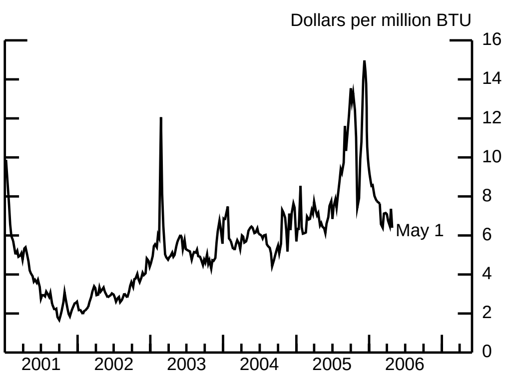


Note. Shaded region is average historical range as calculated by Energy Information Administration.

Petroleum Refinery Capacity Utilization

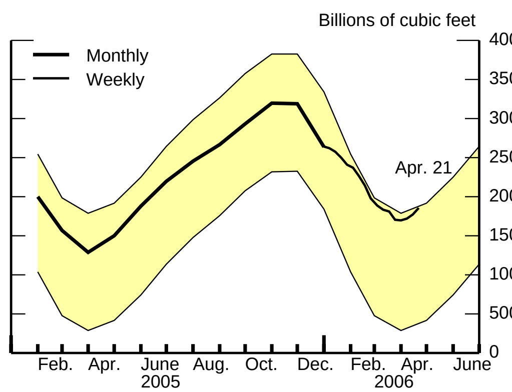


Natural Gas Prices



Note. National average spot price.
Source. Bloomberg.

Natural Gas Inventories



Note. Shaded region is historical range for 2000 to 2004 as calculated by FRB staff.

Inflation expectations have moved up recently, both for the coming year and for the longer term. The Michigan SRC measure of median one-year inflation expectations increased ¼ percentage point in April, to 3.3 percent; median five- to ten-year inflation expectations rose similarly, to 3.1 percent. As of May 2, inflation compensation implied by rate spreads on nominal and CPI-indexed Treasury bonds was about 2.6 percent for five-year maturities and 2.7 percent for ten-year maturities; both figures are about 0.2 percentage point higher than at the time of the March Greenbook.

The price index for gross domestic purchases excluding food and energy rose 2.7 percent over the four quarters ending in the first quarter, about the same rate as in the previous year. An acceleration in nonresidential construction prices was offset by the deceleration in core consumer prices.

The increase in the producer price index (PPI) for core intermediate goods rose just 0.1 percent in March after sizable increases in January and February. Prices of a number of energy-intensive components, such as industrial chemicals, turned down in March (perhaps responding to the first-quarter decline in natural gas prices) after large increases in previous months. In contrast, producer prices of energy-intensive services, such as air and rail transport, rose sharply in March, continuing the string of increases posted over the preceding year.

Surging metals prices pushed up the PPI for core crude materials in February and March to a level more than 13 percent above that of a year earlier. In the past six weeks, the Journal of Commerce (JOC) metals index has risen an additional 11 percent. Copper and zinc prices have risen 46 percent and 33 percent, respectively, and prices of several other metals are also up sharply.[16] The broader JOC industrial price index has moved up 5¾ percent since late March, while the Commodity Research Bureau spot industrial index, which excludes energy items, has risen 6 percent over the same period.

Labor Costs

Over the three months ending in March, the employment cost index (ECI) for hourly compensation of private industry workers rose at an annual rate of 2.4 percent, the slowest pace in several years. On a twelve-month-change basis, the ECI increased 2.6 percent, 0.9 percentage point less than in the previous year.

[16] The recent enormous increases in metals prices reportedly have several causes in addition to strong demand, including labor unrest at copper mines in Mexico and Chile and the possibility of another miners' strike at Canada's zinc mines at the end of May.

Broad Measures of Inflation
(Percent change, Q1 to Q1)

Measure	2003	2004	2005	2006
Product prices				
GDP price index	2.1	2.1	2.8	3.2
Less food and energy	2.0	1.9	2.7	3.0
Nonfarm business chain price index	1.6	1.5	2.6	3.1
Expenditure prices				
Gross domestic purchases price index	2.6	2.1	3.1	3.5
Less food and energy	1.9	1.9	2.6	2.7
PCE price index	2.3	1.9	2.7	3.0
Less food and energy	1.5	1.7	2.2	1.9
PCE price index, market-based components	2.3	1.7	2.4	2.9
Less food and energy	1.3	1.3	1.8	1.5
CPI	2.9	1.8	3.0	3.7
Less food and energy	1.8	1.3	2.3	2.1
Chained CPI	2.5	1.7	2.7	3.2
Less food and energy	1.4	1.2	2.1	1.9
Median CPI	2.7	2.0	2.3	2.6
Trimmed mean CPI	2.1	1.7	2.3	2.6

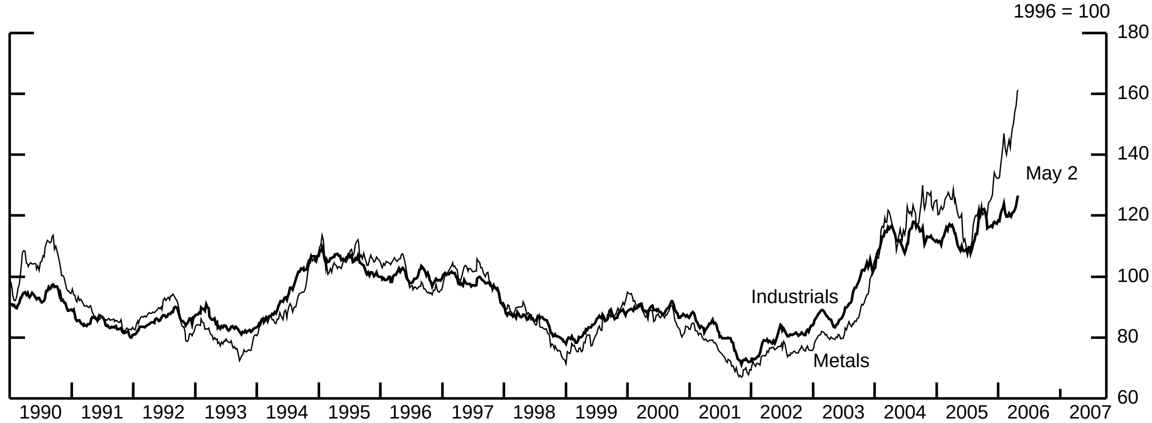
Surveys of Inflation Expectations
(Percent)

Period	Actual CPI inflation [1]	University of Michigan: 1 year [2]		University of Michigan: 5 to 10 years [3]		Professional forecasters (10-year) [4]
		Mean	Median	Mean	Median	
2004:Q2	2.9	4.0	3.3	3.3	2.8	2.5
Q3	2.7	3.3	2.9	3.1	2.8	2.5
Q4	3.3	3.4	3.0	3.1	2.8	2.5
2005:Q1	3.0	3.6	3.0	3.2	2.8	2.5
Q2	2.9	3.9	3.2	3.3	2.9	2.5
Q3	3.8	4.3	3.5	3.5	2.9	2.5
Q4	3.7	4.6	3.7	3.5	3.1	2.5
2006:Q1	3.6	3.7	3.0	3.3	2.9	2.5
Dec.	3.4	4.1	3.1	3.5	3.1	2.5
2006:Jan.	4.0	3.8	3.0	3.4	2.9	...
Feb.	3.6	3.6	3.0	3.3	2.9	...
Mar.	3.4	3.8	3.0	3.3	2.9	2.5
Apr.	n.a.	4.4	3.3	3.6	3.1	...

1. Percent change from the same period in the preceding year.
2. Responses to the question: By about what percent do you expect prices to go up, on average, during the next 12 months?
3. Responses to the question: By about what percent per year do you expect prices to go up, on average, during the next 5 to 10 years?
4. Quarterly CPI projections compiled by the Federal Reserve Bank of Philadelphia.
... Not applicable.
n.a. Not available.

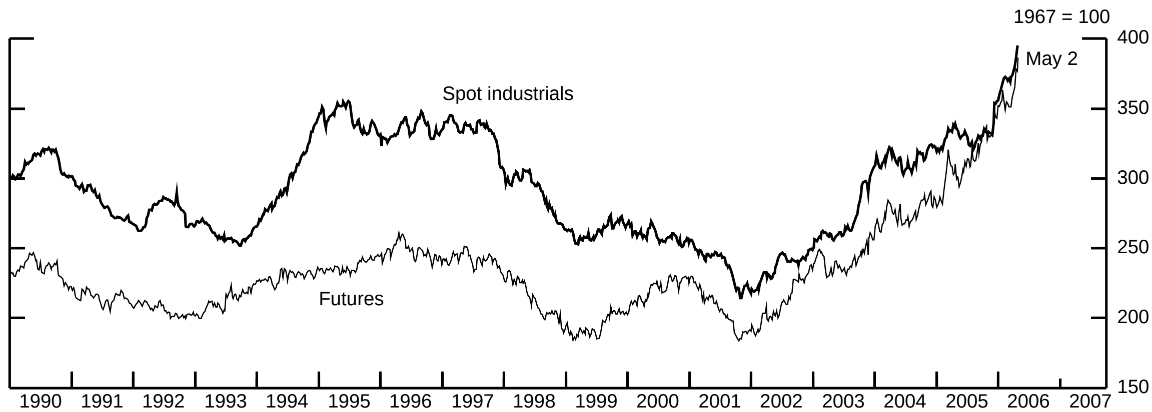
Commodity Price Indexes

Journal of Commerce



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

Commodity Research Bureau



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

Selected Commodity Price Indexes
(Percent change)

Index	2005 [1]	12/27/05 to 3/21/06 [2]	3/21/06 [2] to 5/2/06	52-week change to 5/2/06
JOC industrials	5.3	2.0	5.7	13.0
JOC metals	5.8	9.7	11.1	31.5
CRB spot industrials	10.1	4.9	6.0	17.7
CRB spot foodstuffs	-6.1	-1.1	5.0	-2.3
CRB futures	20.6	2.4	10.0	29.0

1. From the last week of the preceding year to the last week of the year indicated.
2. March 21, 2006, is the Tuesday preceding publication of the March Greenbook.

The wages and salaries component of the ECI rose at a 2.8 percent annual rate over the first three months of this year. Over the past twelve months, this component rose 2.4 percent, ¼ percentage point less than the previous year. The deceleration in this index of wage change, which is calculated using fixed industry-occupation weights and covers both production and non-productions workers, contrasts with the uptrend in the payroll survey measure of average hourly earnings, which is unweighted and only covers production workers. Average hourly earnings were up 3.4 percent in the twelve months ending in March, compared with a rise of 2.6 percent a year earlier.

Benefit costs, as measured in the ECI, rose at an annual rate of 1.6 percent in the three months ending in March, the slowest rate in the past seven years. Benefit costs have risen only 3 percent over the past twelve months, about 2½ percentage points slower than in the previous year. The biggest single contributor to the slower rise in benefit costs was a sharp deceleration in employers' current payments for their workers' defined benefit retirement plans—perhaps reflecting higher stock market returns over the past few years. Also, employers' contributions for health insurance decelerated over the twelve months ending in March, and increases in overtime pay and bonuses slowed markedly.

On the basis of personal income data and employee hours for the first quarter, we estimate that compensation per hour in the nonfarm business sector rose at an annual rate of 5 percent. However, that increase left the four-quarter change at 3.6 percent—below the average pace of the preceding few years. Despite the first-quarter pickup in compensation growth, the markup over unit labor costs in the nonfarm business sector remained high relative to its historical average.

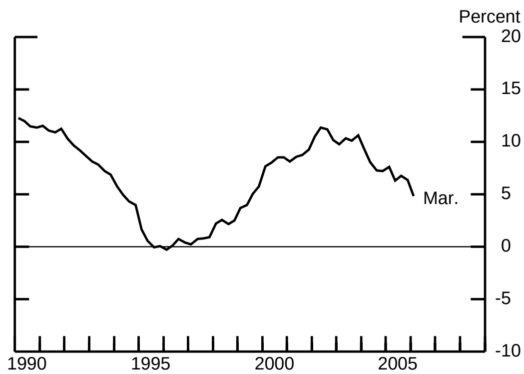
Change in Employment Cost Index of Hourly Compensation for Private-Industry Workers

Measure	2005 Mar.	2005 June	2005 Sept.	2005 Dec.	2006 Mar.
	Quarterly change (compound annual rate)[1]				
Total hourly compensation	**3.8**	**2.5**	**2.9**	**2.8**	**2.4**
Wages and salaries	2.5	2.1	2.5	2.8	2.8
Benefits	6.4	3.3	3.3	3.3	1.6
	12-month change				
Total hourly compensation	**3.5**	**3.1**	**2.9**	**2.9**	**2.6**
Wages and salaries	2.7	2.5	2.3	2.5	2.4
Benefits	5.5	4.7	4.5	4.0	3.0

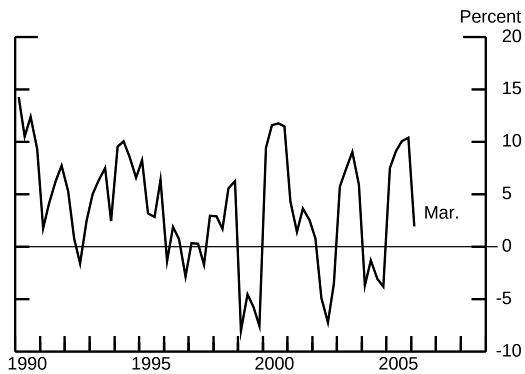
1. Seasonally adjusted by the BLS.

ECI Benefits (confidential)
(Private-industry workers; 12-month change)

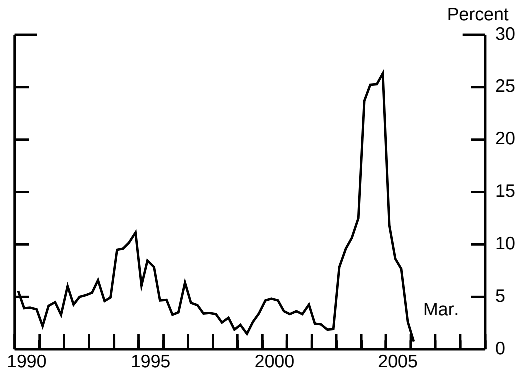
Health Insurance



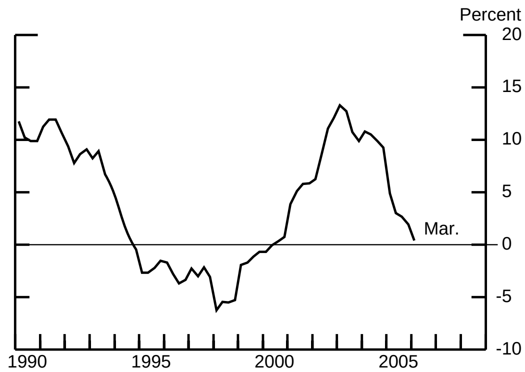
Nonproduction Bonuses



Retirement and Savings



Workers' Compensation Insurance



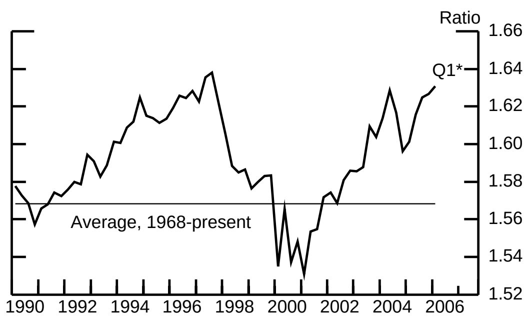
Hourly Compensation and Unit Labor Costs

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

Category	2004:Q1 to 2005:Q1	2005:Q1 to 2006:Q1[e]	2005 Q2	2005 Q3	2005 Q4[e]	2006 Q1[e]
Compensation per hour						
Nonfarm business	6.4	3.6	1.3	5.5	2.6	5.0
Nonfinancial corporations[1]	6.7	n.a.	1.1	6.3	n.a.	n.a.
Unit labor costs						
Nonfarm business	3.4	1.3	-1.0	1.2	3.0	1.9
Nonfinancial corporations[1]	1.2	n.a.	-3.4	2.1	n.a.	n.a.

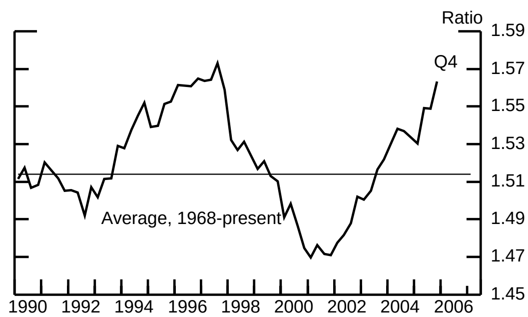
Note. Figures that include the most recent quarter are based on published data rather than the staff forecast.
1. All corporations doing business in the United States except banks, stock and commodity brokers, and finance and insurance companies. The sector accounts for about two-thirds of business employment.
n.a. Not available.
e Staff estimate.

Markup, Nonfarm Business



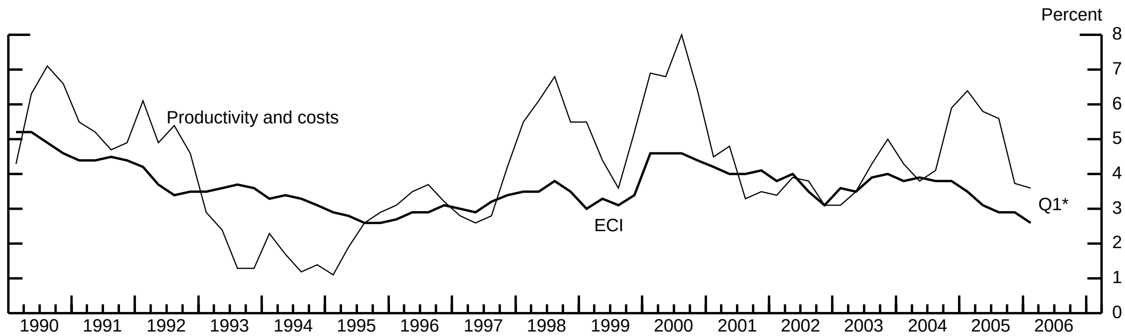
Note. The markup is the ratio of output price to unit labor costs.
* Values for 2005:Q4 and 2006:Q1 are staff estimates.

Markup, Nonfinancial Corporations



Note. The markup is the ratio of output price to unit labor costs.

Compensation per Hour
(Percent change from year-earlier period)



* P&C values for 2005:Q4 and 2006:Q1 are staff estimates.

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Domestic Financial Developments

III-T-1

Selected Financial Market Quotations

(One-day quotes in percent except as noted)

Instrument	2004 June 28	2005 Dec. 30	2006 Mar. 27	2006 May 2	Change to May 2 from selected dates (percentage points) 2004 June 28	2005 Dec. 30	2006 Mar. 27
Short-term							
FOMC intended federal funds rate	1.00	4.25	4.75	4.75	3.75	.50	.00
Treasury bills[1]							
3-month	1.36	3.99	4.51	4.69	3.33	.70	.18
6-month	1.74	4.22	4.62	4.79	3.05	.57	.17
Commercial paper (A1/P1 rates)[2]							
1-month	1.28	4.23	4.76	4.96	3.68	.73	.20
3-month	1.45	4.37	4.84	5.02	3.57	.65	.18
Large negotiable CDs[1]							
3-month	1.53	4.49	4.92	5.11	3.58	.62	.19
6-month	1.82	4.65	5.02	5.22	3.40	.57	.20
Eurodollar deposits[3]							
1-month	1.29	4.36	4.82	5.05	3.76	.69	.23
3-month	1.51	4.52	4.96	5.14	3.63	.62	.18
Bank prime rate	4.00	7.25	7.50	7.75	3.75	.50	.25
Intermediate- and long-term							
U.S. Treasury[4]							
2-year	2.88	4.43	4.76	4.96	2.08	.53	.20
5-year	3.97	4.35	4.68	4.97	1.00	.62	.29
10-year	4.90	4.47	4.80	5.19	.29	.72	.39
U.S. Treasury indexed notes							
5-year	1.56	2.03	2.14	2.23	.67	.20	.09
10-year	2.25	2.10	2.25	2.42	.17	.32	.17
Municipal general obligations (Bond Buyer)[5]	5.01	4.38	4.43	4.59	-.42	.21	.16
Private instruments							
10-year swap	5.21	4.92	5.23	5.63	.42	.71	.40
10-year FNMA[6]	5.30	4.82	5.02	5.34	.04	.52	.32
10-year AA[7]	5.59	5.25	5.57	5.97	.38	.72	.40
10-year BBB[7]	6.18	5.84	6.11	6.46	.28	.62	.35
5-year high yield[7]	8.30	8.28	8.16	8.22	-.08	-.06	.06
Home mortgages (FHLMC survey rate)[8]							
30-year fixed	6.21	6.21	6.35	6.58	.37	.37	.23
1-year adjustable	4.19	5.16	5.51	5.68	1.49	.52	.17

Stock exchange index	Record high Level	Record high Date	2005 Dec. 30	2006 Mar. 27	2006 May 2	Change to May 2 from selected dates (percent) Record high	2005 Dec. 30	2006 Mar. 27
Dow Jones Industrial	11,723	1-14-00	10,718	11,250	11,416	-2.61	6.52	1.48
S&P 500 Composite	1,527	3-24-00	1,248	1,302	1,313	-14.03	5.20	.89
Nasdaq	5,049	3-10-00	2,205	2,316	2,310	-54.25	4.74	-.25
Russell 2000	778	4-19-06	673	754	768	-1.39	14.02	1.80
Wilshire 5000	14,752	3-24-00	12,518	13,158	13,304	-9.81	6.28	1.11

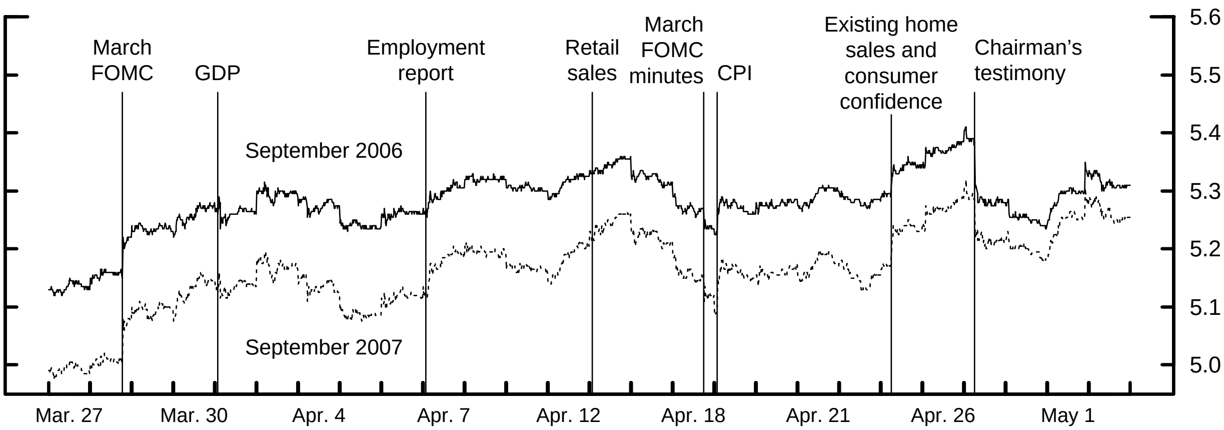
1. Secondary market.
2. Financial commercial paper.
3. Bid rates for Eurodollar deposits collected around 9:30 a.m. eastern time.
4. Derived from a smoothed Treasury yield curve estimated using off-the-run securities.
5. Most recent Thursday quote.
6. Constant-maturity yields estimated from Fannie Mae domestic noncallable coupon securities.
7. Derived from smoothed corporate yield curves estimated using Merrill Lynch bond data.
8. Home-mortgage data for May 2, 2006, is from April 27, 2006.

NOTES:

June 28, 2004, is the day before the most recent policy tightening began.
March 27, 2006, is the day before the most recent FOMC meeting.

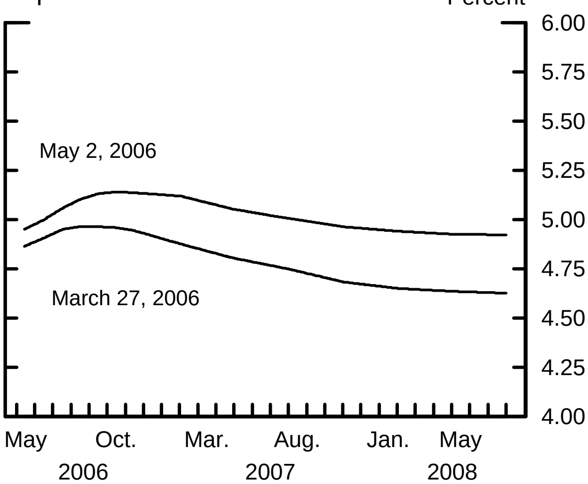
Policy Expectations and Treasury Yields

Eurodollar Futures



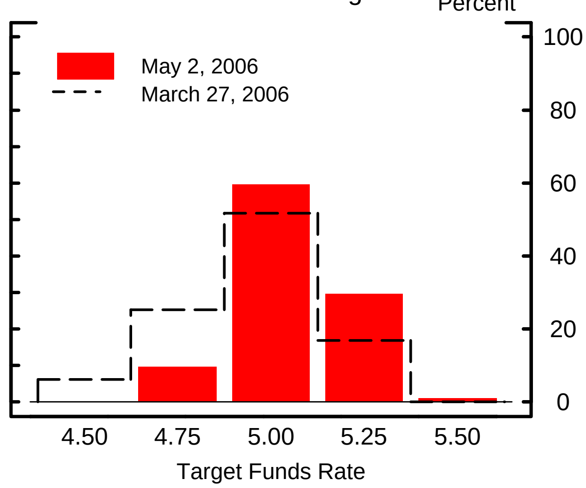
Note. 5-minute intervals.

Expected Federal Funds Rate



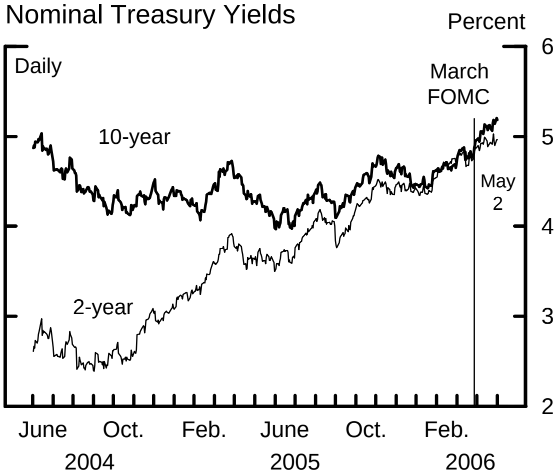
Note. Estimates from federal funds and Eurodollar futures, with an allowance for term premia and other adjustments.

Probability Density for Target Federal Funds Rate after June 2006 Meeting



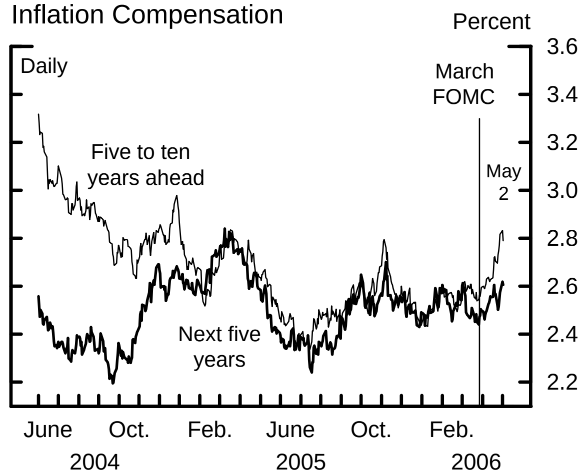
Note. Derived from options on July federal funds futures contracts, with a term premium adjustment.

Nominal Treasury Yields



Note. Estimates from smoothed Treasury yield curve based on off-the-run securities.

Inflation Compensation



Note. Estimates based on smoothed nominal and inflation-indexed Treasury yields and adjusted for the indexation-lag effect.

Domestic Financial Developments

Overview

Monetary policy expectations firmed, on balance, over the intermeeting period, as the effects of stronger-than-expected data releases were only partly offset by Federal Reserve communications that were interpreted as suggesting that the end of the tightening cycle was approaching. Reflecting the upward shift in policy expectations and, perhaps, some rebound in term premiums, long-term yields moved up considerably and the ten-year Treasury yield reached its highest level since June 2002. Stock price indexes ended the period up slightly, as the influence of positive earnings reports apparently outweighed the effects of higher interest rates and energy prices. Business credit quality remained strong, and corporate bond spreads remained low. Household credit quality also continued to be solid overall, although delinquency rates on mortgages have risen a bit since the middle of 2005. Little new data are yet available to assess the effect of higher interest rates on household mortgage borrowing this year.

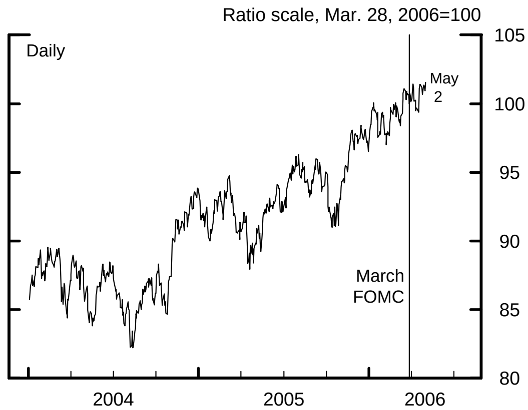
Policy Expectations and Interest Rates

The decision at the March FOMC meeting to raise the target federal funds rate 25 basis points, to 4¾ percent, came as no surprise to market participants; nonetheless, near-term federal funds futures rates edged up on the accompanying statement, reportedly in part because of the retention of the language that "some further policy firming may be needed." More-recent Federal Reserve communications—including the release of the minutes of the March FOMC meeting and the Chairman's testimony to the Joint Economic Committee—had a more substantial effect on policy expectations in the opposite direction. In contrast, data releases over the intermeeting period were generally read by investors as pointing to stronger growth and greater inflation pressures than had been anticipated and pushed up the expected path for policy. Over the intermeeting period, money market futures rates for the end of this year and beyond rose about 20 to 30 basis points on net. Judging from federal funds futures, investors currently are nearly certain of a 25 basis point increase at the May FOMC meeting and assign about a one-third probability to a like-sized rate hike in June. Around the end of this year, the expected policy path begins to tilt down. Uncertainty about the future path of policy further out, implied by options on Eurodollar futures, remained about unchanged at a low level.

Nominal Treasury yields rose over the intermeeting period. Yields at the two- and ten-year maturities increased about 20 and 40 basis points, respectively, leaving the yield curve modestly steeper and the ten-year rate at levels last seen in June 2002. Distant-horizon forward rates rose substantially more than near-term ones, suggesting some

Corporate Yields, Risk Spreads, and Stock Prices

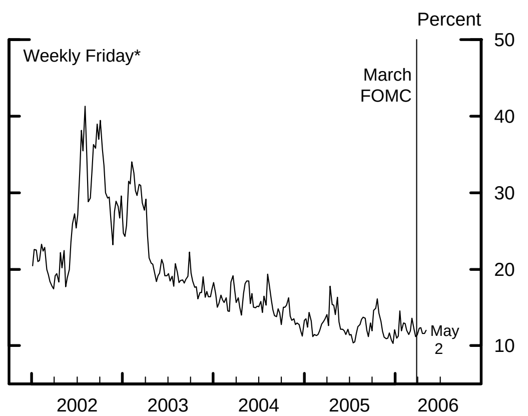
S&P 500



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

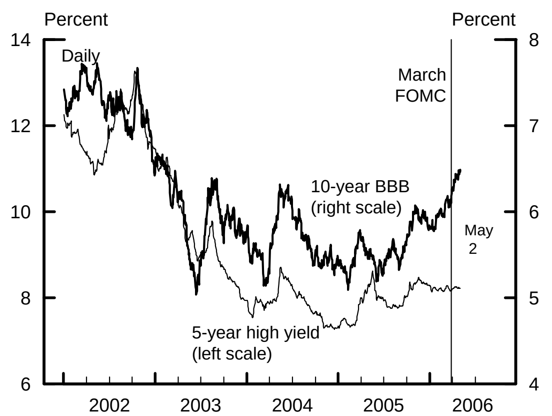
* Yield on synthetic Treasury perpetuity minus Philadelphia Fed 10-year expected inflation.
\+ Denotes the latest observation using daily interest rates and stock prices and latest earnings data from I/B/E/S.

Implied Volatility on S&P 500 (VIX)



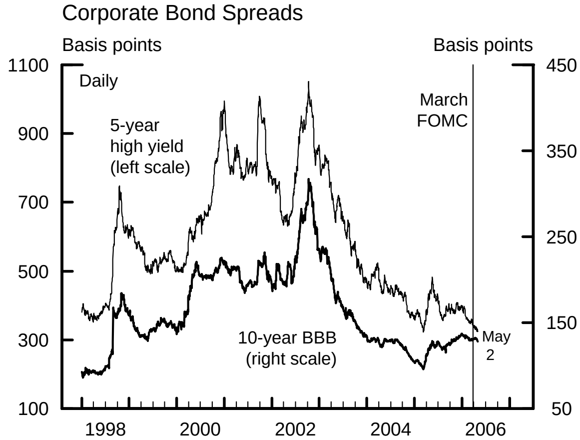
* Latest observation is for most recent business day.

Yields for BBB and High-Yield Corporate Bonds



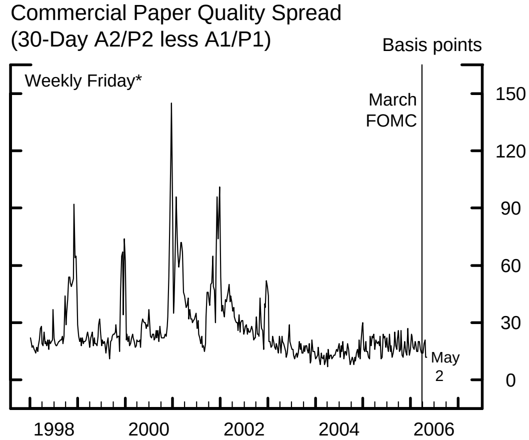
Note. Yields from smoothed yield curves based on Merrill Lynch bond data.

Corporate Bond Spreads



Note. Measured relative to comparable-maturity Treasuries.

Commercial Paper Quality Spread
(30-Day A2/P2 less A1/P1)



* Latest observation is for most recent business day.

rebound in term premiums from their recent exceptionally low levels. The causes of this rise in term premiums are hard to identify but may include heightened inflation uncertainty sparked by recent economic data releases, some waning of foreign demand for Treasury securities, and some reassessment of the pricing of interest rate risk. Inflation compensation over the next five years, measured by Treasury inflation-protected securities, rose about 15 basis points over the period, while inflation compensation five to ten years ahead increased about 25 basis points.

Stock Prices and Corporate Interest Rates

Broad equity market indexes edged up on net over the intermeeting period, as generally positive first-quarter earnings reports more than offset the effects of higher interest rates and increased prices for energy and raw materials. The ratio of trend earnings to price for the S&P 500, a measure of long-run expected equity returns, remained near 5½ percent, where it has hovered for the past several years. At the same time, the recent increase in the long-term real Treasury yield has narrowed the equity premium a bit and brought it closer to its average level over the past two decades. Implied volatility on the S&P 500 remained near its recent low levels.

Over the intermeeting period, yields on investment-grade corporate bonds moved up in line with those on comparable-maturity Treasury securities, so risk spreads on those bonds were about unchanged. In contrast, yields on high-yield corporate bonds were little changed, and their risk spreads narrowed about 25 basis points. The low level of high-yield bond spreads likely reflects investors' sanguine view of corporate credit quality over the next couple of years. In the commercial paper market, the thirty-day quality spread also remained low.

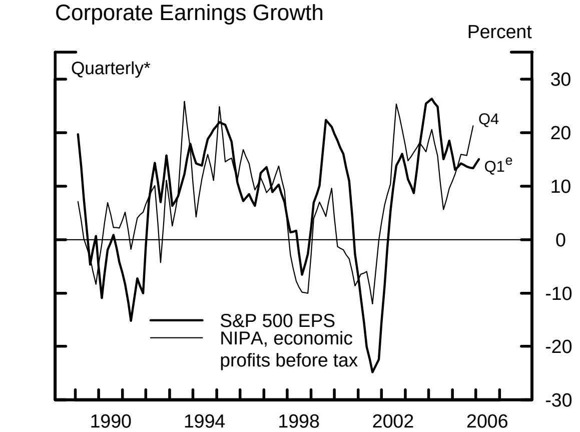
Corporate Earnings and Credit Quality

First-quarter earnings reports have been quite favorable thus far, with only a few firms reporting profits below analysts' expectations and with guidance for the second quarter more positive than typical. Based on reports from about 350 companies in the S&P 500, aggregate earnings per share in the first quarter are estimated to have increased 15 percent from a year earlier, extending the series of double-digit increases seen over the past several years. The reports led analysts to revise up their year-ahead earnings expectations modestly, even outside the energy sector.

Bolstered by robust earnings and strong balance sheets, measures of aggregate business credit quality continued to show few signs of stress. Although bond rating downgrades

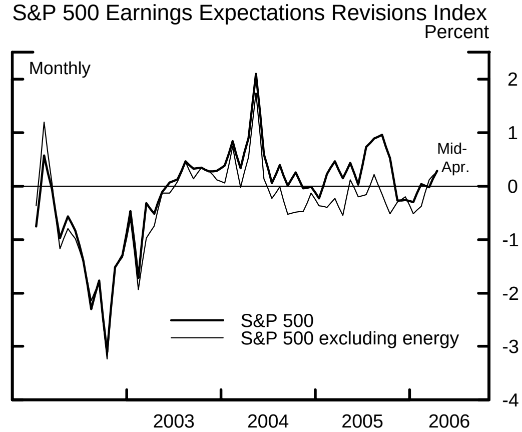
Corporate Earnings and Credit Quality

Corporate Earnings Growth



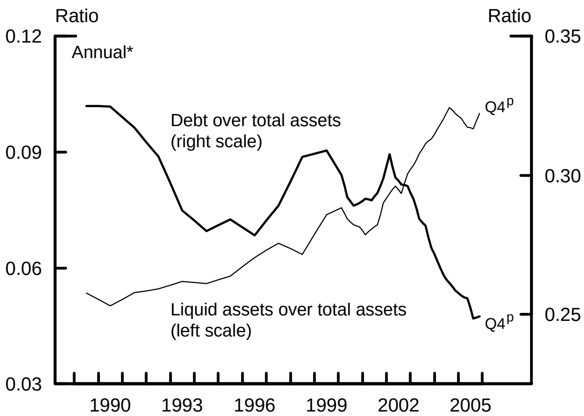
* Change from four quarters earlier.
Source. I/B/E/S for S&P 500 EPS.
e Staff estimate.

S&P 500 Earnings Expectations Revisions Index



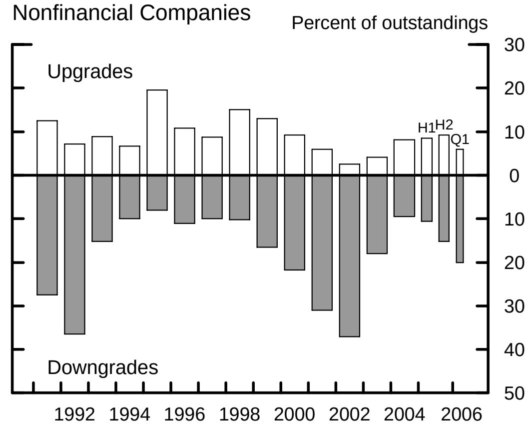
Note. Index is a weighted average of the percent change in the consensus forecasts of current-year and following-year EPS for constant sample.

Financial Ratios for Nonfinancial Corporations



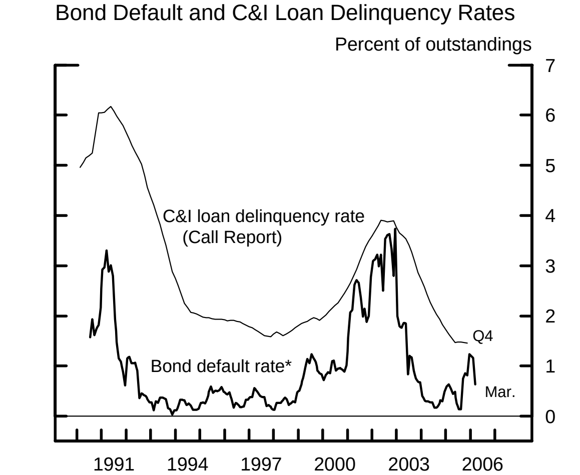
Note. Compustat data.
* Data are quarterly starting in 2000:Q1.
p Preliminary.

Bond Ratings Changes of Nonfinancial Companies



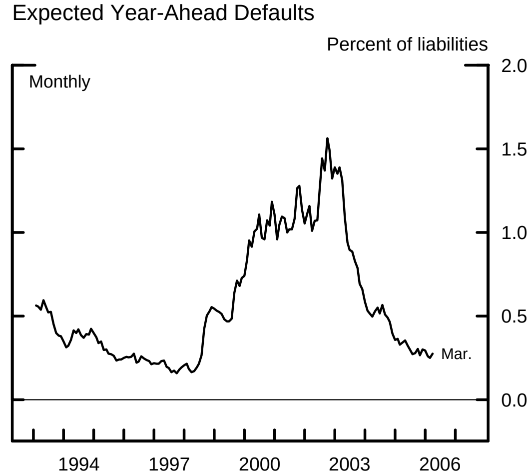
Note. Moody's Investors Service data at an annual rate.

Bond Default and C&I Loan Delinquency Rates



* 6-month moving average, from Moody's Investors Service.

Expected Year-Ahead Defaults



Note. Firm-level estimates of default weighted by firm liabilities as a percent of total liabilities, excluding defaulted firms.
Source. Moody's KMV.

Business Finance

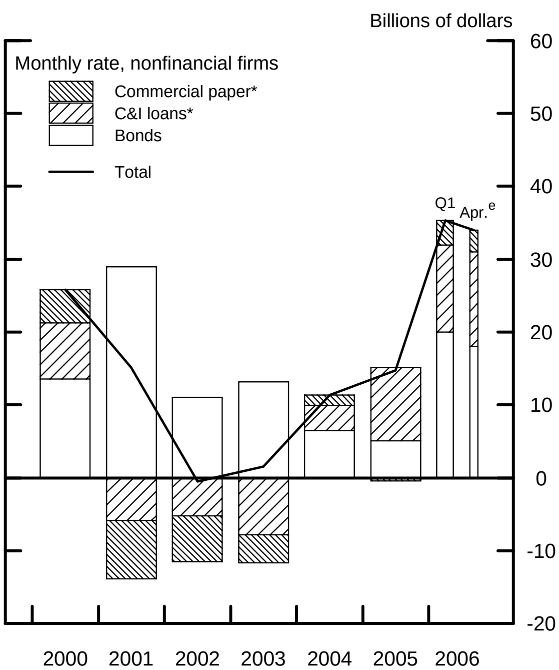
Gross Issuance of Securities by U.S. Corporations

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

Type of security	2002	2003	2004	2005 H1	2005 H2	2006 Q1	2006 Apr.
Nonfinancial corporations							
Stocks[1]	5.2	3.7	5.4	3.8	5.3	5.6	3.3
Initial public offerings	.7	.4	1.6	1.6	1.8	1.7	2.0
Seasoned offerings	4.4	3.3	3.8	2.1	3.5	3.9	1.8
Bonds[2]	24.8	31.6	22.8	18.1	20.3	32.3	27.4
Investment grade	15.7	16.0	8.3	7.9	9.0	15.7	11.0
Speculative grade	4.8	11.3	9.5	6.2	6.5	6.8	5.9
Other (sold abroad/unrated)	4.2	4.3	4.9	4.0	4.8	9.9	10.4
Memo							
Net issuance of commercial paper[3]	-6.3	-3.8	1.4	2.6	-3.4	3.4	3.0
Change in C&I loans at commercial banks[3,4]	-5.2	-7.8	3.5	9.9	10.3	11.9	13.0
Financial corporations							
Stocks[1]	4.0	6.6	6.9	5.3	4.8	3.6	1.8
Bonds[2]	87.0	111.1	139.4	167.3	185.7	178.8	74.7

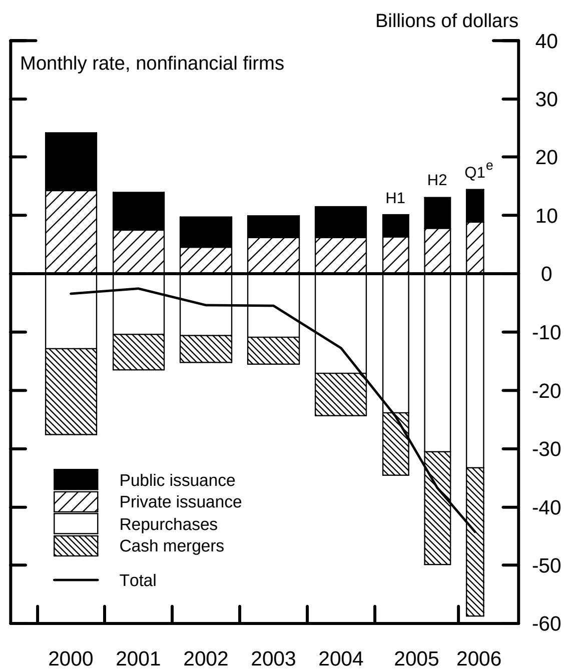
Note. Components may not sum to totals because of rounding.
1. Excludes private placements and equity-for-equity swaps that occur in restructurings.
2. Data include regular and 144a private placements. Bond totals reflect gross proceeds rather than par value of original discount bonds. Bonds are categorized according to Moody's bond ratings, or to Standard & Poor's if unrated by Moody's.
3. End-of-period basis, seasonally adjusted.
4. Adjusted for FIN 46 effects.

Selected Components of Net Debt Financing



* Seasonally adjusted, period-end basis.
e Staff estimate.

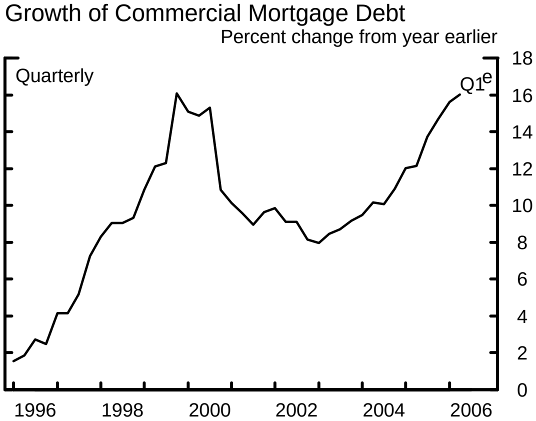
Components of Net Equity Issuance



e Staff estimate.

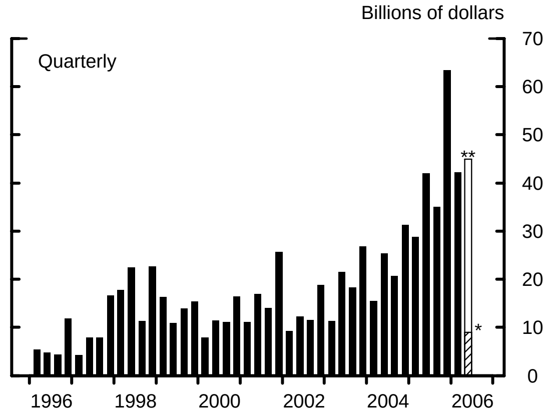
Commercial Real Estate

Growth of Commercial Mortgage Debt



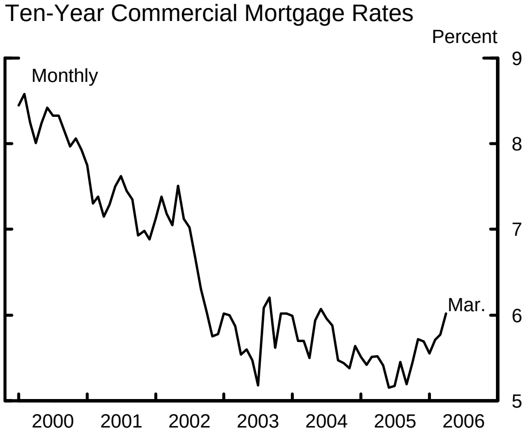
e Staff estimate.

Gross Issuance of CMBS



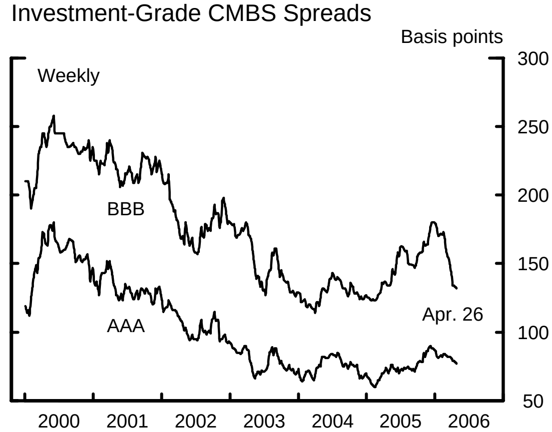
* Through April 27.
** Staff estimate for Q2.
Source. Commercial Mortgage Alert.

Ten-Year Commercial Mortgage Rates



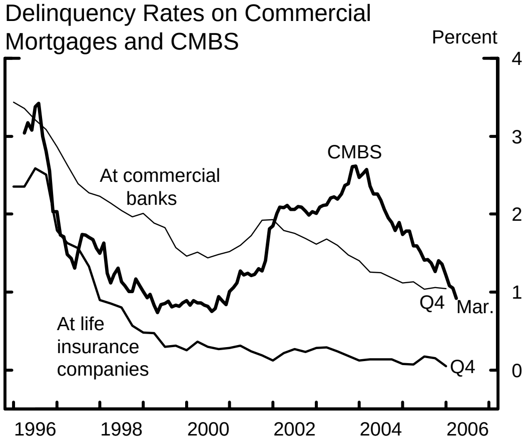
Source. Barron's/Levy.

Investment-Grade CMBS Spreads



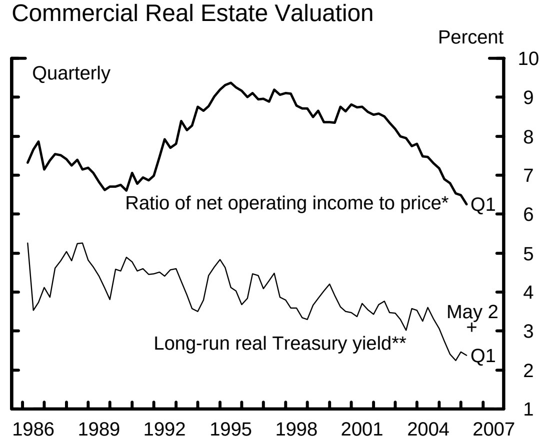
Note. Measured relative to the 10-year Treasury yield.
Source. Morgan Stanley.

Delinquency Rates on Commercial Mortgages and CMBS



Source. Call Report, ACLI, Morgan Stanley.

Commercial Real Estate Valuation



* Staff calculation from NCREIF data, annual rate.
**Yield on synthetic Treasury perpetuity minus Philadelphia Fed 10-year expected inflation.
+ Denotes the latest observation using daily interest rates.

from Moody's increased in the first quarter, downgrades of securities issued by Ford and General Motors represented more than half of the total. Since December, the six-month trailing bond default rate has dropped off, and just a few firms defaulted in the first quarter. A measure of aggregate expected defaults over the next year, based on Moody's KMV data, remained at a low level in March.

Business Finance

Gross bond issuance by nonfinancial firms remained brisk in April and acquisition-related financing again accounted for a notable part of issuance. C&I loans outstanding are estimated to have grown at a double-digit rate in April, while commercial paper continued to move up. In total, net debt financing by nonfinancial corporations in April likely stayed near its robust first-quarter pace.

Gross public equity issuance remained subdued over the intermeeting period, as a slight pickup in initial public offerings was more than offset by a decline in seasoned offerings. Meanwhile, equity retirements have been torrid. Equity retired in the first quarter through cash mergers, which continue to be driven by a surge in leveraged buyout activity, exceeded even the high rate seen in 2005. In addition, corporate announcements suggest that the first-quarter pace of share repurchases, supported by robust earnings and liquid balance sheets, likely surpassed the record clip of the second half of 2005.

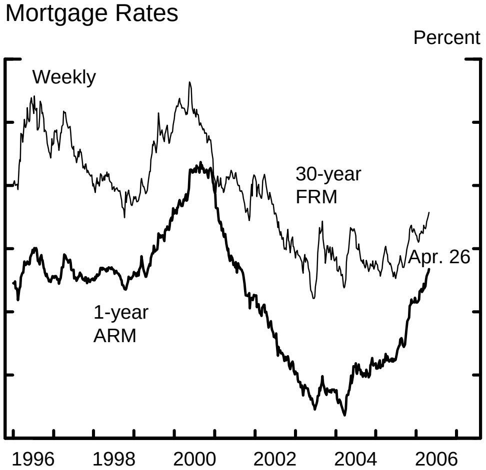
Commercial Real Estate

Commercial mortgage debt appears to have expanded rapidly in the first quarter, and the issuance calendar for commercial-mortgage-backed securities (CMBS) suggests that borrowing will remain strong in the near term despite an increase in commercial-mortgage interest rates to their highest levels since 2004. At the same time, spreads on BBB-rated CMBS over Treasury securities of comparable maturities have declined sharply in recent weeks, reversing last fall's run-up and bringing spreads back in line with those on similarly-rated corporate bonds. Delinquency rates remained low by historical standards, and a decline in vacancy rates and some firming in rents in the first quarter reflected further improvement in market fundamentals.

The ratio of net operating income to property prices—an indicator of the rate of return on commercial real estate—continued its downtrend in the first quarter. The spread of this ratio over the real perpetuity Treasury yield, a rough measure of the risk premium on commercial real estate assets, narrowed in the first quarter. In addition, the recent

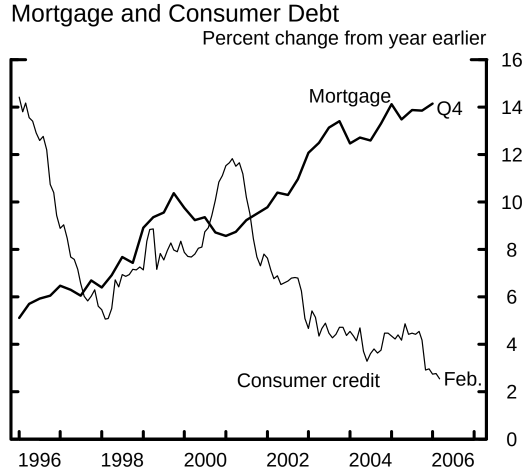
Household Liabilities

Mortgage Rates

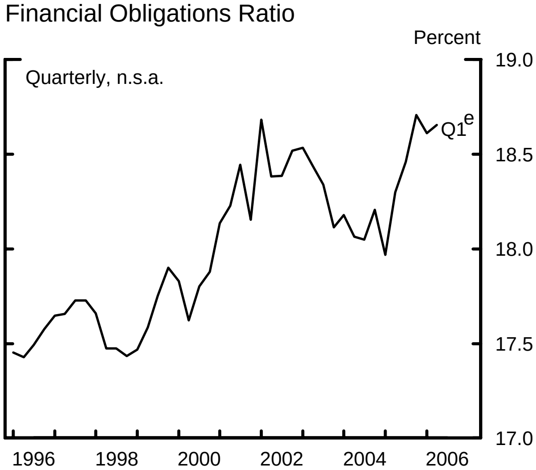


Source. Freddie Mac.

Mortgage and Consumer Debt

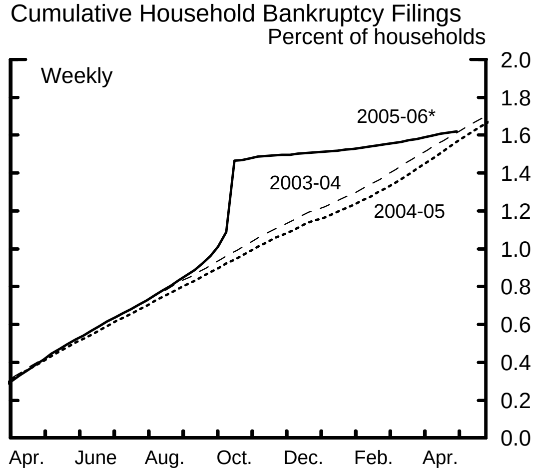


Financial Obligations Ratio



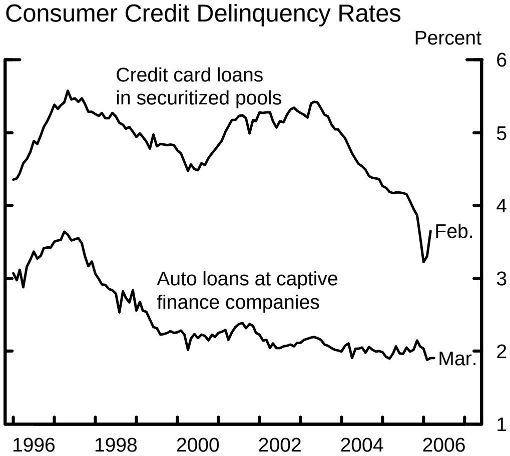
e Staff estimate.

Cumulative Household Bankruptcy Filings



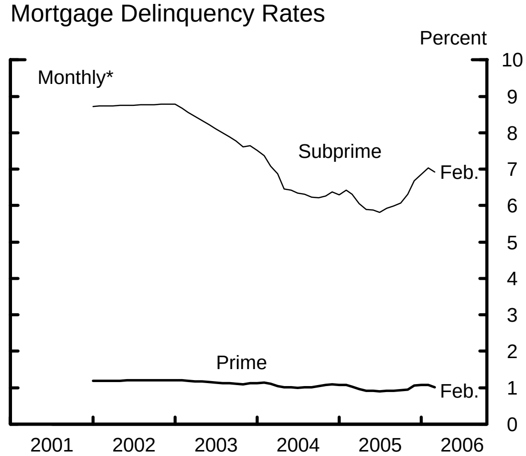
* Through April 29.
Source. Lundquist Consulting, Inc.

Consumer Credit Delinquency Rates



Source. For credit cards, Moody's; for auto loans, Federal Reserve.

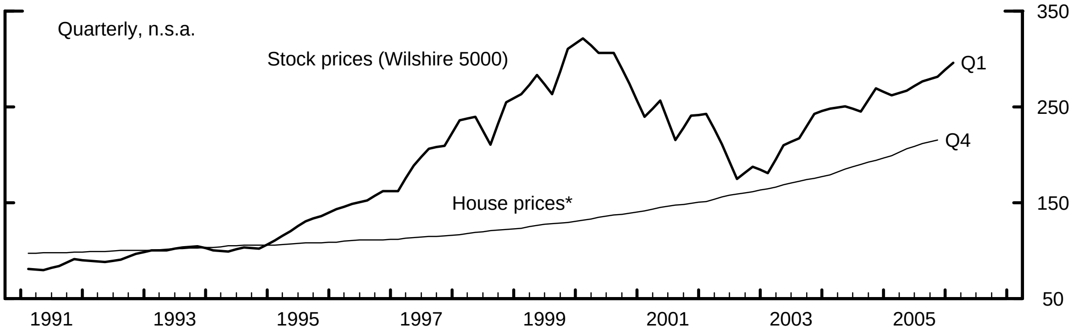
Mortgage Delinquency Rates



Note: 90 days or more delinquent, or in foreclosure.
Source. LoanPerformance.
* Data are year-end prior to September 2003.

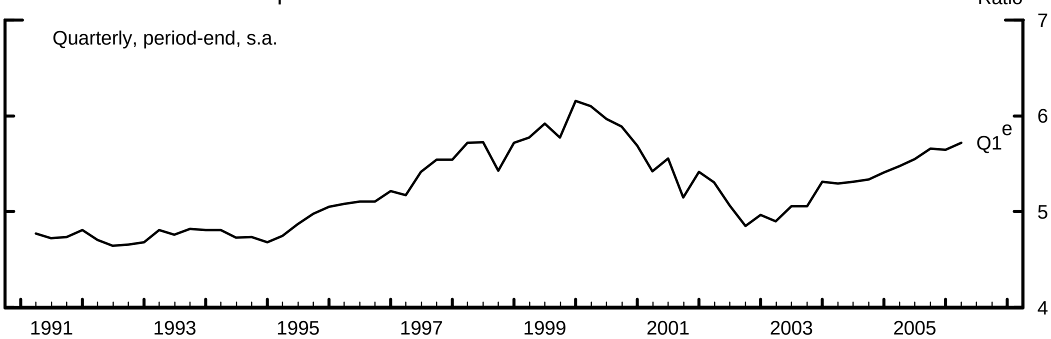
Household Assets

Asset Prices



* Source. Office of Federal Housing Enterprise Oversight (OFHEO) repeat-transactions purchase-only index.

Net Worth Relative to Disposable Income



e Staff estimate.

Net Flows into Long-Term Mutual Funds

(Billions of dollars, monthly rate)

Fund type	2004		2005			2006		Assets
	H1	H2	H1	Q3	Q4	Q1	Apr.[e]	Mar.
Total long-term funds	**20.0**	**15.0**	**18.1**	**15.7**	**11.7**	**38.8**	**28.4**	**7,313**
Equity funds	**19.7**	**10.0**	**12.3**	**8.1**	**12.4**	**31.0**	**24.7**	**5,340**
Domestic	13.7	4.9	4.1	0.7	1.3	10.6	10.4	4,273
International	6.0	5.1	8.1	7.3	11.2	20.4	14.2	1,067
Hybrid funds	**4.1**	**3.0**	**3.4**	**1.5**	**0.2**	**0.4**	**0.1**	**588**
Bond funds	**-3.8**	**2.0**	**2.5**	**6.1**	**-1.0**	**7.4**	**3.6**	**1,385**
High-yield	-2.1	0.5	-1.6	-1.0	-1.0	-0.4	-0.0	146
Other taxable	0.1	1.9	3.7	5.7	0.6	5.8	3.4	893
Municipals	-1.9	-0.4	0.4	1.4	-0.6	2.0	0.2	345

Note. Excludes reinvested dividends.

e Staff estimates based on confidential ICI weekly data.

Source. Investment Company Institute.

Treasury Financing

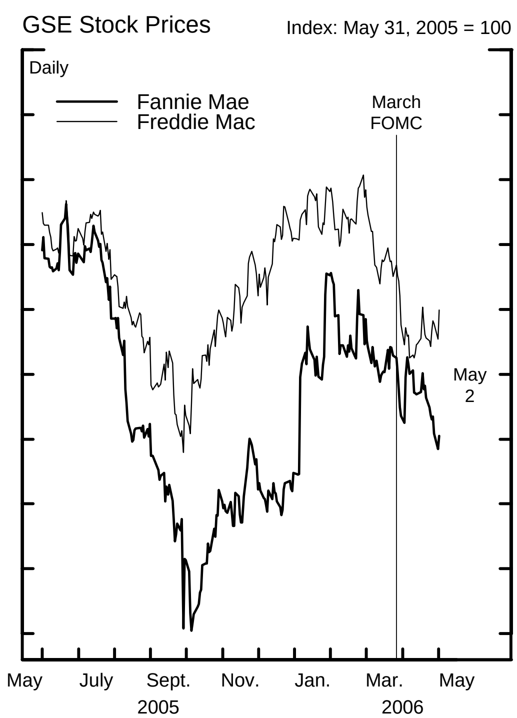
(Billions of dollars)

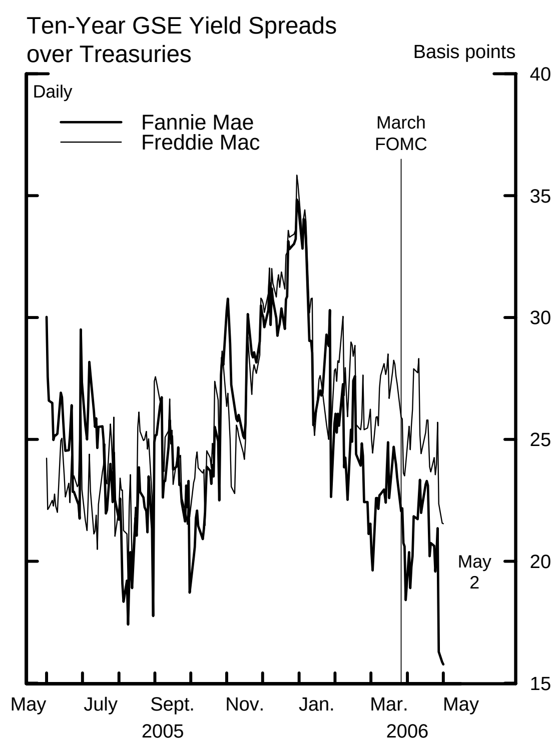
Item	2005				2006		
	Q1	Q2	Q3	Q4	Jan.	Feb.	Mar.
Total surplus, deficit (–)	**-176.6**	**45.2**	**-69.0**	**-119.3**	**21.0**	**-119.2**	**-85.5**
Means of financing deficit							
Net borrowing	164.7	-42.8	72.8	112.2	9.8	45.1	101.2
Nonmarketable	20.8	35.9	20.6	21.2	-3.6	-39.4	40.7
Marketable	143.9	-78.7	52.1	91.0	13.4	84.6	60.5
Bills	55.7	-135.8	-9.3	48.8	-7.6	43.2	42.5
Coupons	88.2	57.1	61.4	42.3	21.1	41.3	18.0
Decrease in cash balance	2.2	-10.7	-2.5	-0.9	-32.2	50.7	9.9
Other[1]	9.7	8.3	-1.2	8.0	1.4	23.3	-25.6
Memo:							
Cash balance, end of period	22.4	33.2	35.7	36.6	68.9	18.1	8.2

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

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

GSE Market Developments





Note. GSE yields based on senior unsecured debt.

increase in the real Treasury yield implies that the spread likely will tighten further in the current quarter.

Household Finance

Average interest rates on both thirty-year fixed-rate and one-year adjustable-rate mortgages continued to climb over the intermeeting period. However, the degree to which higher interest rates may have reduced household mortgage borrowing remains unclear, because only limited data are available for early 2006. Consumer credit—which has accounted for a small share of total household borrowing in recent years—has continued to rise only modestly.

Household credit quality remained solid in the first few months of 2006, even as the financial obligations ratio appears to have stayed near the top of its historical range. Household bankruptcy filings in recent months continued to run at low levels. The cumulative number of filings since the beginning of last year is only a little above the corresponding figure for the year-earlier period, a development consistent with the view that much of the rush to file before bankruptcy reform in October 2005 reflected a shift from subsequent months. Delinquency rates on consumer loans have remained low, albeit in part because of the high rate of charge-offs after last fall's bankruptcy surge. In contrast, while the delinquency rate among prime mortgage borrowers continued to be low and stable, mortgage delinquencies among subprime borrowers have moved up in recent quarters. Even though part of the rise is attributable to the effects of last fall's hurricanes, there also has been a modest deterioration in some households' ability to make their mortgage payments outside of the hurricane-affected areas.

Although the Office of Federal Housing Enterprise Oversight (OFHEO) repeat-transactions house-price index for the first quarter will not be released until June 1, monthly indicators of new and existing home prices so far this year hint that the long-expected cooling in house-price appreciation may have begun. Even with some moderation in house-price gains, the ratio of household net worth to disposable income likely increased in the first quarter, boosted by rising stock prices. Net purchases of equity mutual funds during the first four months of this year were stronger than in any four-month period since early 2000, and a disproportionate share of the inflows continued to go to international funds.

State and Local Government Finance

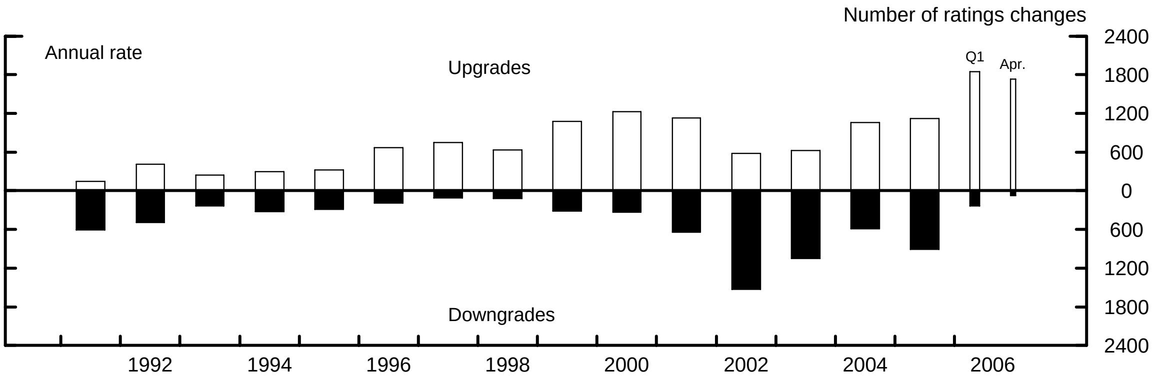
Gross Offerings of Municipal Securities

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

Type of security	2003	2004	2005 H1	2005 H2	2006 Q1	2006 Apr.
Total	37.9	34.7	38.1	38.6	25.9	27.7
Long-term [1]	32.0	29.8	35.0	33.3	24.0	27.0
Refundings [2]	10.0	10.8	17.1	13.8	8.8	7.1
New capital	22.1	19.0	17.9	19.5	15.2	19.8
Short-term	5.8	4.9	3.1	5.3	1.9	.8
Memo: Long-term taxable	3.5	2.0	2.0	2.2	1.2	1.3

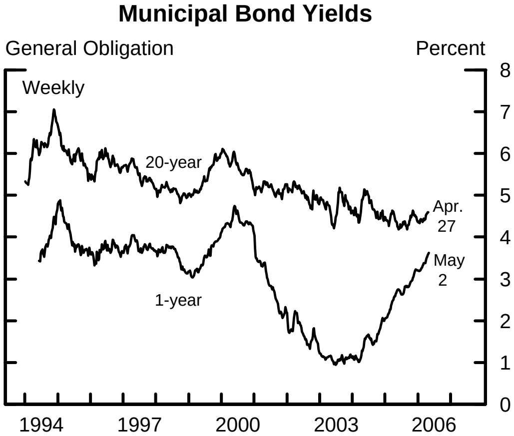
1. Includes issues for public and private purposes.
2. All issues that include any refunding bonds.

Ratings Changes



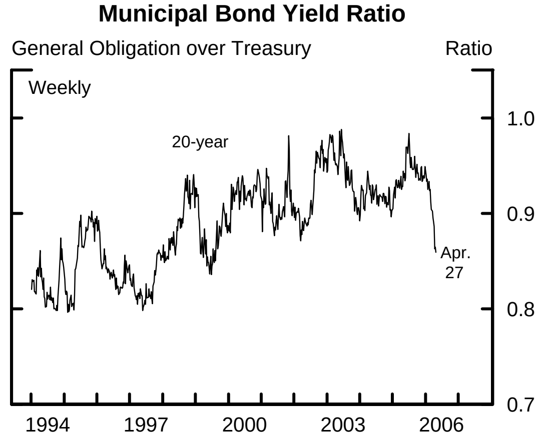
Source. S&P's Credit Week Municipal and Ratings Direct.

Municipal Bond Yields



Source. Bloomberg and Bond Buyer.

Municipal Bond Yield Ratio



Source. Bond Buyer.

Treasury and Agency Finance

Over the intermeeting period, the Treasury conducted auctions of two- and five-year nominal notes and five- and ten-year Treasury inflation-protected securities (TIPS). Demand for securities in these auctions was generally on the weak side. The five-year TIPS auction was particularly poorly received, as indicated by an unusually low bid-to-cover ratio. At just 13 percent in March, the proportion of nominal coupon securities bought by foreign investors continued to fall back from the peak of 24 percent reached in 2004.

Agency stock prices were down roughly 5 percent over the intermeeting period in reaction to rising mortgage interest rates and Freddie Mac's long-delayed, but still disappointing, earnings report. There was only muted stock price reaction to statements by Treasury Secretary Snow and Chairman Bernanke affirming that the Department of the Treasury has the authority to limit agency debt issuance, but the comments may have contributed to a 5 basis point narrowing in agency debt spreads. Announcements that Freddie Mac will pay $410 million in cash to settle shareholder lawsuits and that OFHEO will soon release a report expected to give a negative assessment of Fannie Mae's past accounting practices elicited little response from investors.

State and Local Government Finance

Gross issuance of long-term municipal bonds picked up a bit in April from the tepid pace of the first quarter. New capital issuance rebounded, while refunding issuance fell further because of the increases in interest rates. The volume of short-term issuance in April continued to be light, a sign of improved budget conditions in many states.

Ratings upgrades have been numerous, while downgrades have been scarce so far this year. In line with improving credit quality, yields on long-dated municipal bonds increased less than those on comparable-maturity Treasury securities, sharply reducing the yield ratio. While market commentary offers little explanation for this move, similar large swings in the yield ratio have occurred periodically in past years.

Money and Bank Credit

M2 grew moderately in March and April, largely reflecting continued substantial inflows to small time deposits in response to their favorable offering rates. In April, the growth of M2 likely received an additional lift from tax-related flows.

M2 Monetary Aggregate
(Based on seasonally adjusted data)

Aggregate and components	Percent change (annual rate)[1]						Level (billions of dollars),
			2005	2006			
	2004	2005	Q4	Q1	Mar.	Apr. (e)	Apr. (e)
M2	5.2	3.9	5.1	6.5	2.9	4.4	6,802
Components[2]							
Currency	5.5	3.5	4.2	6.7	3.6	3.8	738
Liquid deposits[3]	10.0	2.0	3.0	3.8	-2.9	1.9	4,290
Small time deposits	-.3	18.7	15.4	16.9	20.0	17.4	1,035
Retail money market funds	-11.7	-.9	4.7	9.0	13.8	1.3	732
Memo:							
Institutional money market funds	-5.7	5.0	12.1	9.0	7.3	14.2	1,169
Monetary base	5.6	3.4	4.2	6.1	2.8	4.1	801

Note. M2 is the sum of currency, liquid deposits, small time deposits, retail money market funds, and nonbank traveler's checks. Acting on its announcement of November 10, 2005, the Board of Governors ceased publishing the M3 monetary aggregate on March 23, 2006.

1. For years, Q4 to Q4; for quarters and months, calculated from corresponding averages.
2. Nonbank traveler's checks are not listed.
3. Sum of demand deposits, other checkable deposits, and savings deposits.

e Estimated.

Commercial Bank Credit

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

Type of credit	2004	2005	2005: Q4	2006: Q1	Mar. 2006	Apr.[e] 2006	Level (billions of dollars), Apr. 2006[e]
Total							
Adjusted[1]	**8.9**	**10.4**	**5.8**	**10.3**	**11.9**	**11.7**	**7,506**
Reported	8.4	9.6	5.2	9.8	10.0	13.5	7,643
Securities							
Adjusted[1]	6.6	7.4	-.6	8.2	13.6	22.7	1,962
Reported	5.2	5.0	-2.4	6.4	6.2	28.7	2,100
Treasury and agency	4.9	-.2	-9.9	8.0	4.1	11.7	1,194
Other[2]	5.6	13.0	8.3	4.3	9.2	51.8	906
Loans[3]							
Total	9.8	11.5	8.1	11.1	11.3	7.9	5,544
Business	1.3	13.4	9.5	16.5	7.2	17.7	1,068
Real estate	14.0	14.0	8.4	9.8	9.9	8.1	2,993
Home equity	43.8	11.1	-1.9	-2.5	3.6	-10.0	430
Other	9.8	14.5	10.2	12.0	11.0	11.2	2,562
Consumer	8.8	3.0	-4.3	3.2	20.3	11.4	711
Adjusted[4]	5.7	.6	-4.4	7.6	15.6	5.7	1,083
Other[5]	7.8	8.2	17.4	16.2	14.4	-9.4	772

Note. Data are adjusted to remove estimated effects of consolidation related to FIN 46 and 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.

1. Adjusted to remove effects of mark-to-market accounting rules (FIN 39 and FAS 115).
2. Includes private mortgage-backed securities, securities of corporations, state and local governments, foreign governments, and any trading account assets that are not Treasury or agency securities, including revaluation gains on derivative contracts.
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.

e Estimated.

Growth in bank credit is estimated to have remained brisk in April. Respondents to the April Senior Loan Officer Opinion Survey reported a further easing of lending standards and terms on business loans but little change in demand, on net. Despite a contraction in home equity lines of credit, which likely resulted from rising interest rates, real estate loans expanded steadily in April. Apart from the effect of a bank's acquisition of a large thrift institution, consumer loans at banks were about flat in March but grew moderately in April.

Appendix

Senior Loan Officer Opinion Survey on Bank Lending Practices

The April 2006 Senior Loan Officer Opinion Survey on Bank Lending Practices addressed changes in the supply of, and demand for, bank loans to businesses and households over the past three months. The survey also contained a set of special questions on the minimum required payment on outstanding credit card balances of individuals and households. This appendix is based on responses from fifty-seven domestic banks and nineteen foreign banking institutions.

In the April survey, domestic commercial banks reported a further net easing of lending standards and terms for commercial and industrial (C&I) loans, while lending standards on commercial real estate loans were reportedly unchanged. At U.S. branches and agencies of foreign banks, lending standards on both C&I and commercial real estate loans were little changed, on net, but like their domestic counterparts, foreign institutions reported a net easing of terms on C&I loans. Demand for both C&I and commercial real estate loans at domestic banks had changed little over the previous three months. By contrast, foreign institutions experienced, on balance, weaker demand for both C&I and commercial real estate loans over the same period. In the household sector, credit standards on residential mortgages and consumer loans were little changed, on net, during the survey period. A moderate net fraction of domestic respondents reported weaker demand for mortgages to purchase homes, while a larger net fraction saw weaker demand for consumer loans over the past three months.

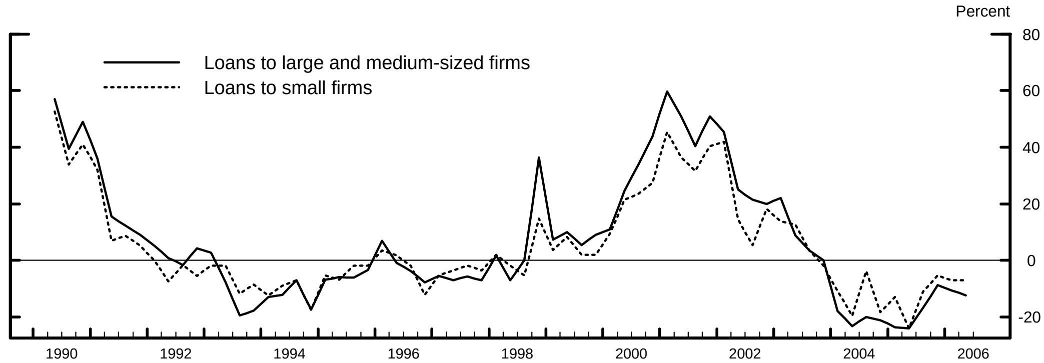
Business Lending

In the April survey, domestic banks indicated that they had further eased credit standards and terms on C&I loans over the past three months. On net, 12 percent of domestic institutions indicated that they had eased standards on such loans to large and middle-market firms, roughly the same net percentage as in the January survey. About 60 percent of domestic respondents—a notably larger net fraction than in the previous survey—reported that they had trimmed spreads of loan rates over their cost of funds for such firms. Almost 40 percent of domestic institutions—again a larger net fraction than in the January survey—indicated that they had reduced the costs of credit lines over the past three months. About one-fifth of domestic banks, on balance, noted that they had increased the maximum maturity of C&I loans or credit lines that they are willing to extend to their business borrowers.

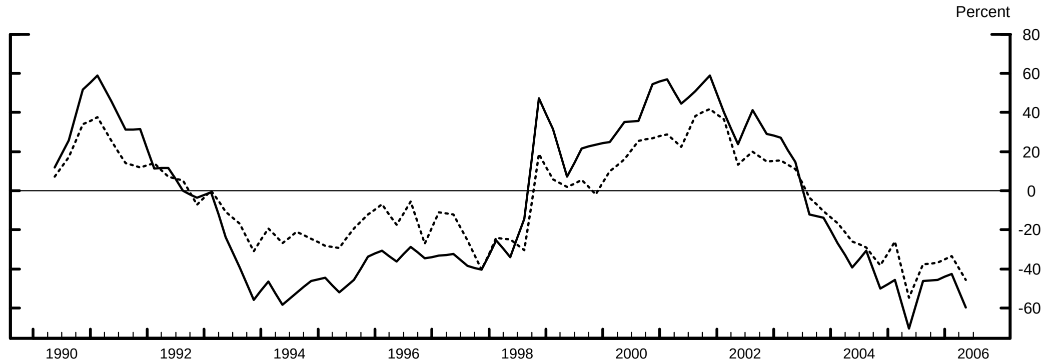
For C&I loans to small firms, 7 percent of domestic respondents, on net, noted that they had eased lending standards in the April survey. On balance, almost 50 percent of respondents indicated that they had narrowed spreads of loan rates over their cost of

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

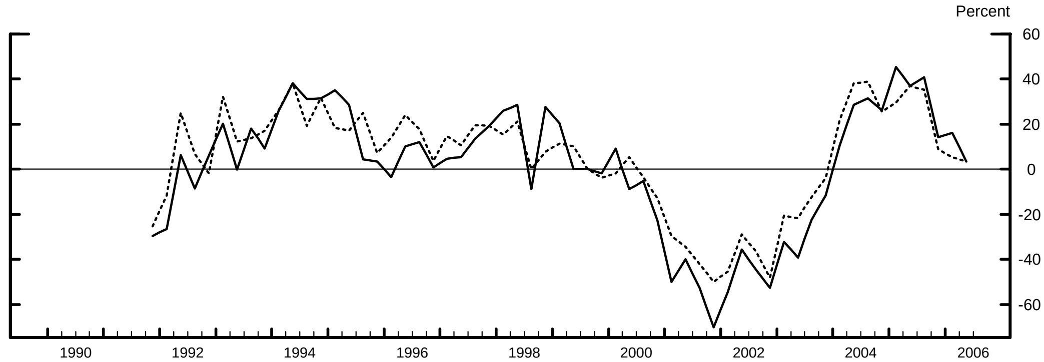
Net Percentage of Domestic Respondents Tightening Standards for C&I Loans



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

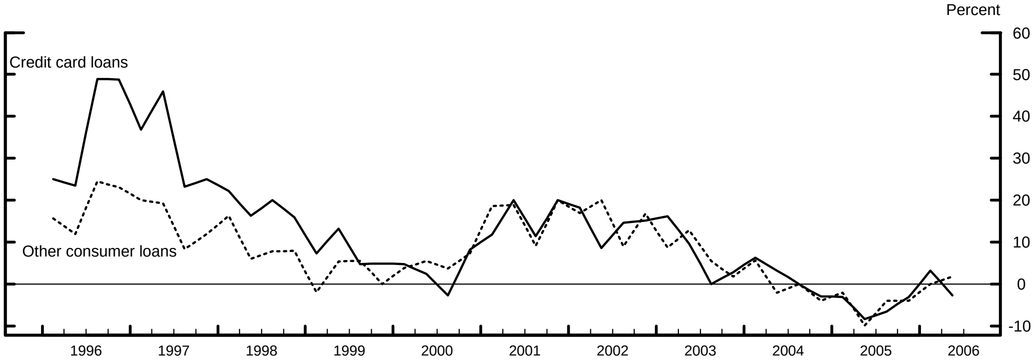


Net Percentage of Domestic Respondents Reporting Stronger Demand for C&I Loans

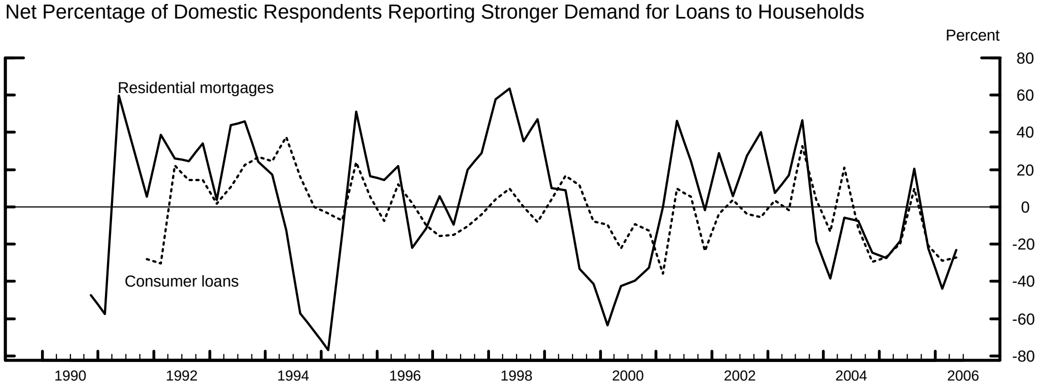


Measures of Supply and Demand for Loans to Households

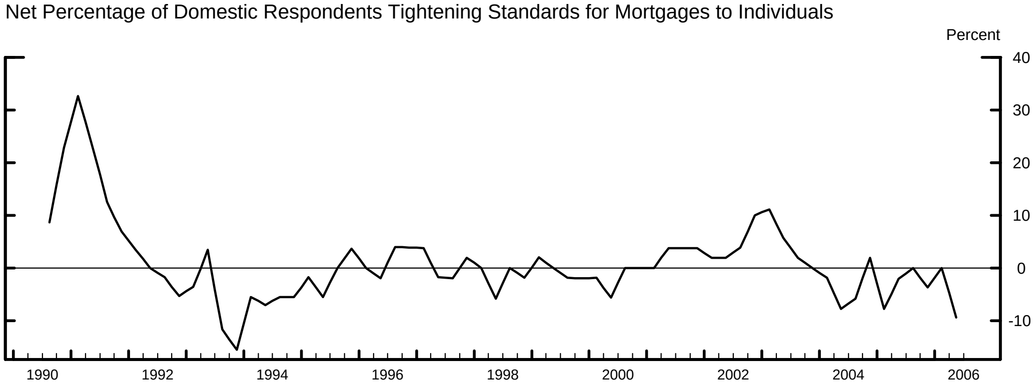
Net Percentage of Domestic Respondents Tightening Standards for Consumer Loans



Net Percentage of Domestic Respondents Reporting Stronger Demand for Loans to Households



Net Percentage of Domestic Respondents Tightening Standards for Mortgages to Individuals



funds, and about 30 percent of them reported having reduced the cost of credit lines over the same period.

As they did in the previous two surveys, U.S. branches and agencies of foreign banks reported essentially no change in their credit standards on C&I loans over the survey period. Nonetheless, significant net fractions of these institutions noted that they had narrowed spreads of loan rates over their cost of funds and reduced the cost of credit lines.

Nearly all domestic respondents that reported an easing of their lending standards or terms on C&I loans in the April survey pointed to more-aggressive competition from other banks or nonbank lenders as an important reason for having done so. Significant net percentages also cited increased liquidity in the secondary market for these loans and increased tolerance for risk as reasons for their move toward a more accommodative lending posture.

On balance, demand for C&I loans from both large and middle-market firms and small firms was reportedly little changed in the April survey at domestic institutions. By contrast, 16 percent of foreign respondents, on balance, noted that they had experienced weaker demand for C&I loans over the previous three months. Among domestic respondents that experienced stronger demand for C&I loans, all cited borrowers' increased needs to finance investment in plant or equipment, while three-quarters pointed to increased needs to finance mergers and acquisitions as reasons for the pickup in demand. Among domestic institutions that experienced weaker demand for C&I loans, 90 percent indicated that customers' internally generated funds had increased, a pattern of responses consistent with continued strong corporate profitability. Nonetheless, about 60 percent of these banks also pointed to borrowers' decreased needs to finance investment in plant or equipment as a reason for weaker loan demand. Regarding future business, about 10 percent of both domestic and foreign institutions, on balance, indicated that the number of inquiries from potential business borrowers had increased over the previous three months.

Domestic institutions reported essentially no change in their lending standards on commercial real estate loans over the past three months, on balance. Similarly, a large majority of foreign respondents indicated that they had not changed standards on such loans. On net, 5 percent of domestic banks saw an increase in demand for commercial real estate loans over the past three months, about the same net fraction as in the January survey. By contrast, about one-fourth of foreign institutions reported that demand for this type of loan was weaker over the same period.

Household Lending

On net, 10 percent of domestic institutions noted that they had eased credit standards on residential mortgage loans over the past three months. Almost one-fourth of domestic banks experienced weaker demand for mortgages to purchase homes, but this net fraction was considerably smaller than in the January survey.

About 15 percent of domestic respondents, on balance, reported an increased willingness to make consumer installment loans over the past three months. Standards and most terms on credit card and non-credit-card consumer loans were reportedly little changed, on net, in the April survey. However, for the second consecutive survey, one-quarter of respondents indicated that they had increased the minimum percent of outstanding credit card balances required to be repaid each month. Demand for consumer loans reportedly weakened further over the past three months: More than one-fourth of domestic banks, on net, saw weaker demand for such loans, about the same net fraction as in the previous survey.

To help the Federal Reserve improve its estimate of the financial obligations ratio in the household sector, the current survey contained a set of special questions regarding minimum required payments on the credit card balances of individuals and households. Twenty-nine domestic institutions responded to these special questions.[1] About three-quarters of these respondents indicated that the minimum required payment is calculated simply as a percentage of total outstanding balances. For banks that calculate the minimum required payment in such a manner, responses regarding the size of this percentage varied notably. About 75 percent indicated that this percentage was more than 1.5 percent but less than or equal to 3.0 percent of total outstanding balances, with about 30 percent reporting a percentage at the high end of this range.

Institutions that do not calculate the minimum required payment on credit card balances simply as a percentage of total outstanding balances were asked to estimate the portion of such minimum required payment attributable to fees, finance charges, and repayment of principal. Three-quarters of these respondents indicated that the approximate ratio of fees required to be paid to total outstanding balances was less than or equal to 0.20 percent—the remainder reported higher ratios. Regarding the ratio of finance charges required to be paid to total outstanding balances, all but one financial institution reported that this ratio was more than 0.50 percent but less than or equal to 1.50 percent. Finally, three-quarters of respondent banks indicated that the ratio of principal balances required to be paid to total outstanding balances at their institution was more

[1] According to the December 31, 2005, Call Report, these banks accounted for almost 40 percent of credit card loans on the books of domestic banks.

than 0.5 percent but less than or equal to 1.5 percent, with the remainder reporting higher ratios.

Banks were also asked to report what fraction of individuals and households paid only the minimum required amount on their outstanding credit card balances in recent months. About 70 percent of respondents noted that 15 percent or less of their customers paid the minimum required amount last month. The banks indicated that a similar percentage of individuals and households paid the minimum required amount in each of the last three months. Finally, one-third of respondents, on net, indicated that they had increased their minimum required payment on credit card balances of individuals and households over the past year.

Last Page of Financial Developments

International Developments

International Developments

U.S. International Transactions

Trade in Goods and Services

The U.S. international trade deficit narrowed to $65.7 billion in February from $68.6 billion in January (revised). The narrowing of the deficit reflected a sharp decrease in imports, which more than offset a modest fall in exports.

Trade in Goods and Services
(Seasonally adjusted)

	2005	Annual rate			Monthly rate		
		2005		2006	2005	2006	
		Q3	Q4	Q1e	Dec.	Jan.	Feb.
	Percent change						
Nominal BOP							
Exports	10.5	5.2	9.2	16.6	2.2	2.5	-1.2
Imports	15.0	10.8	19.7	13.6	1.7	3.6	-2.3
Real NIPA							
Exports	6.7	2.5	5.1	12.1	...	...	...
Imports	9.4	2.4	12.1	13.0	...	...	...
	Billions of dollars						
Nominal BOP							
Net exports	-723.6	-725.6	-789.5	-806.0	-65.1	-68.6	-65.7
Goods, net	-781.6	-789.1	-849.7	-861.7	-70.1	-73.5	-70.1
Services, net	58.0	63.5	60.2	55.7	5.1	5.0	4.3

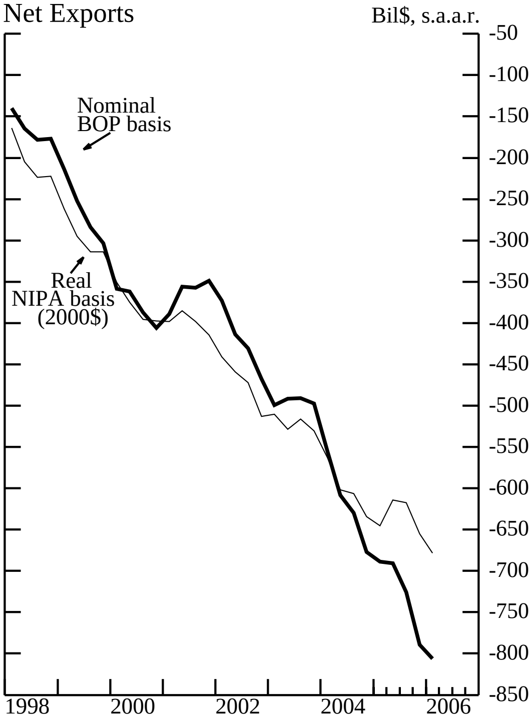
e. BOP data are two months at an annual rate; NIPA data are BEA's advance estimate.
Source. U.S. Department of Commerce, Bureaus of Economic Analysis and Census.
n.a. Not available. ... Not applicable.

In February, the value of exports of goods and services fell 1.2 percent from a high January level. Exports declined across all major product categories, with exports of agricultural products, industrial supplies, and capital goods showing the largest drops. Within capital goods, a large increase in exports of aircraft was more than offset by declines in exports of computers, semiconductors, and other capital goods. Exports of automotive products also moved down somewhat, as did exports of consumer goods. Services exports declined a bit, largely on account of weaker exports of travel services.

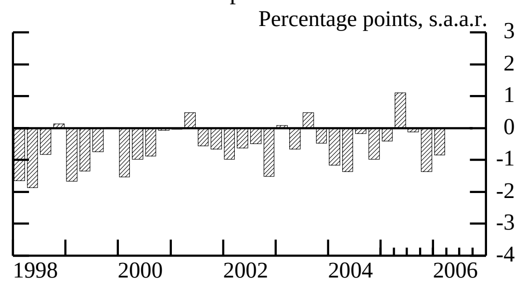
The average value of exports in January and February increased 16½ percent (a.r.) from the fourth quarter. Exports of industrial supplies and capital goods were particularly strong. In real terms, according to the advance NIPA release which includes the BEA's estimate of nominal trade in March, exports of goods and services increased 12 percent (a.r.) in the first quarter, following a rise of just 5 percent in the fourth quarter.

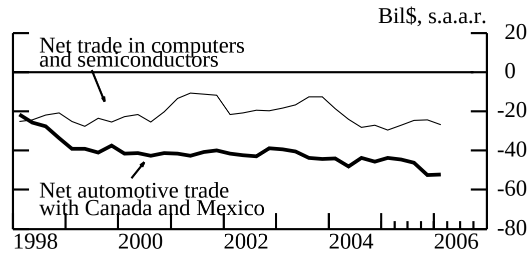
U.S. International Trade in Goods and Services

Net Exports

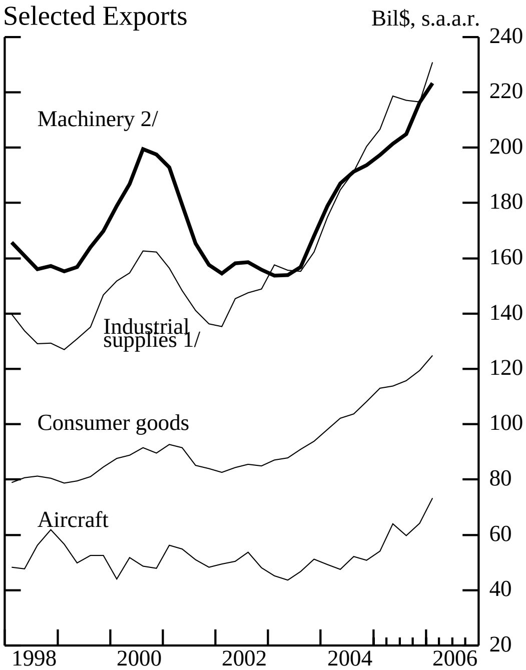


Contribution of Net Exports to Real GDP Growth



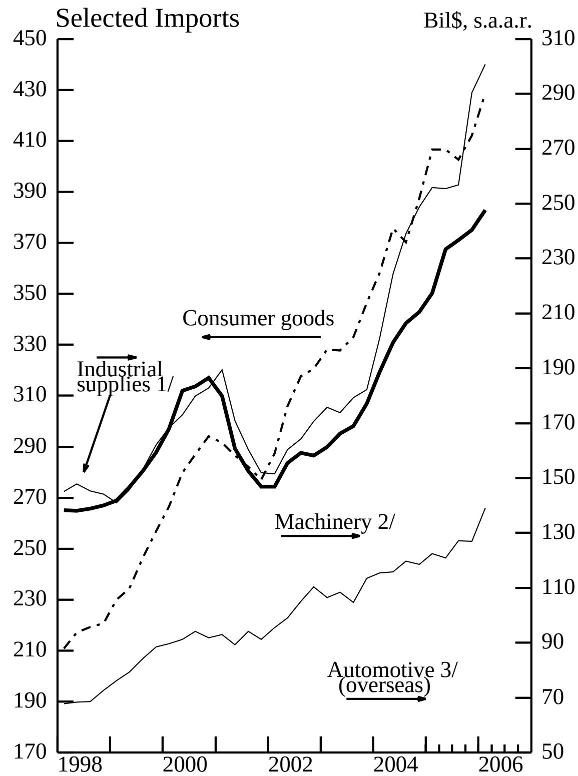


Selected Exports



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

Selected Imports



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				Change[1]			
	2005	2006	2006		2005	2006	2006	
	Q4	Q1[e]	Jan.	Feb.	Q4	Q1[e]	Jan.	Feb.
Exports of G&S	**1312.5**	**1363.9**	**1371.9**	**1355.8**	**28.4**	**51.4**	**33.2**	**-16.1**
Goods exports	925.3	972.3	979.2	965.5	26.1	47.1	29.9	-13.7
Gold	5.8	7.2	7.6	6.8	0.5	1.4	2.1	-0.8
Other goods	919.4	965.2	971.6	958.8	25.6	45.7	27.8	-12.8
Aircraft & parts	64.2	73.3	71.0	75.7	4.5	9.2	11.2	4.7
Computers & accessories	45.4	46.4	47.9	44.9	-1.3	0.9	1.6	-3.0
Semiconductors	50.7	50.3	50.7	49.9	2.0	-0.4	-2.1	-0.7
Other capital goods	220.8	227.1	229.1	225.0	12.6	6.3	0.3	-4.1
Automotive	104.6	108.3	109.3	107.3	6.3	3.7	0.7	-2.0
to Canada	55.2	55.3	58.2	52.5	1.8	0.2	1.4	-5.7
to Mexico	18.6	17.5	17.3	17.7	3.1	-1.1	-0.3	0.4
to ROW	30.8	35.4	33.8	37.1	1.4	4.6	-0.4	3.3
Agricultural	64.2	69.3	70.8	67.8	-2.1	5.1	7.7	-3.0
Ind supplies (ex. ag, gold)	216.6	230.9	232.3	229.5	-0.5	14.4	8.2	-2.8
Consumer goods	119.4	124.8	125.3	124.3	3.6	5.4	-1.6	-0.9
All other goods	33.5	34.8	35.3	34.3	0.6	1.3	11.6	-1.0
Services exports	387.2	391.5	392.8	390.3	2.3	4.3	3.3	-2.4
Imports of G&S	**2102.0**	**2169.9**	**2195.0**	**2144.7**	**92.3**	**67.9**	**75.4**	**-50.3**
Goods imports	1775.0	1834.1	1861.7	1806.4	86.7	59.1	70.7	-55.3
Petroleum	294.8	294.8	294.6	295.1	24.7	0.0	11.1	0.6
Gold	5.4	5.6	6.0	5.3	1.0	0.2	0.2	-0.7
Other goods	1474.7	1533.6	1561.2	1506.0	61.0	58.9	59.4	-55.1
Aircraft & parts	25.5	27.5	28.7	26.4	1.1	2.0	0.1	-2.3
Computers & accessories	93.8	96.5	97.5	95.6	-0.2	2.7	2.0	-2.0
Semiconductors	26.7	27.1	27.2	26.9	0.7	0.3	0.1	-0.2
Other capital goods	242.8	249.9	256.8	243.0	3.6	7.1	13.1	-13.8
Automotive	253.1	264.3	272.1	256.4	11.0	11.1	14.4	-15.7
from Canada	77.6	77.3	82.2	72.5	5.5	-0.3	4.0	-9.8
from Mexico	48.6	47.8	49.3	46.2	5.6	-0.8	4.6	-3.1
from ROW	127.0	139.1	140.6	137.7	-0.1	12.2	5.8	-2.9
Ind supplies (ex. oil, gold)	290.4	300.8	301.9	299.8	33.6	10.5	4.1	-2.1
Consumer goods	412.0	428.7	434.1	423.4	9.5	16.7	12.4	-10.7
Foods, feeds, bev.	70.3	74.5	76.4	72.6	1.5	4.2	4.5	-3.8
All other goods	59.9	64.2	66.5	61.9	0.4	4.3	8.8	-4.6
Services imports	327.0	335.8	333.3	338.3	5.6	8.8	4.6	5.0
Memo:								
Oil quantity (mb/d)	14.56	14.62	14.68	14.56	1.23	0.06	-0.24	-0.11
Oil import price ($/bbl)	55.55	55.22	54.95	55.48	0.02	-0.32	2.92	0.53

1. Change from previous quarter or month. e. Average of two months.
Source. U.S. Department of Commerce, Bureaus of Economic Analysis and Census.

The value of imported goods and services declined 2.3 percent in February after surging in January. The decline in imports was widespread across categories with the exception of imports of oil, which were flat. Imports of capital goods fell back sharply, led by declines in imports of other capital goods (machinery). Imports of automotive products more than reversed January's steep climb, but still remained at a high level. A fall in imports of cell phones contributed to a decline in imports of consumer goods, while weak imports of chemicals held back imports of non-oil industrial supplies. Imports of foods also moved down following a surge in January. In contrast, imports of services jumped, boosted by licensing payments for broadcast rights for the 2006 Winter Olympic Games.

The average value of imports in January and February increased 13½ percent (a.r.) from the fourth quarter. Imports of automotive products, capital goods, consumer goods, and industrial supplies were all strong. In the advance NIPA release which includes the BEA's estimate of nominal trade in March, real imports of good and services rose 13 percent (a.r.) in the first quarter, following a rise of 12 percent in the fourth quarter.

Prices of Internationally Traded Goods

Non-oil imports. In March, BLS import prices of non-oil goods fell 0.3 percent, while prices of imported core goods were unchanged. A 13 percent decline in the price for imported natural gas, a category that we now exclude from core imports, was the main reason for the difference. Within core imports, prices for non-fuel industrial supplies rose 0.8 percent in March, reflecting further increases in the prices for metals, and food prices rose 0.4 percent. These increases were offset by a 0.2 percent decline in prices of consumer goods. Following two months of increases, prices for capital goods (excluding computers and semiconductors) were unchanged in March, as were prices of automotive products. Prices for imported computers fell 0.5 percent, whereas prices for semiconductors edged up 0.1 percent.

In the first quarter, according to the advance NIPA release, core import prices rose 1¾ percent at an annual rate, as prices in all sub-categories posted increases with the exception of automotive products. (According to the BLS monthly data, these price increases occurred mostly in January as core import prices were unchanged in February and March.) The main contributor to the overall price increase was non-fuel industrial supplies. Average prices for food also recorded a large increase. Prices for capital goods (excluding computers and semiconductors) rose at a more modest pace.

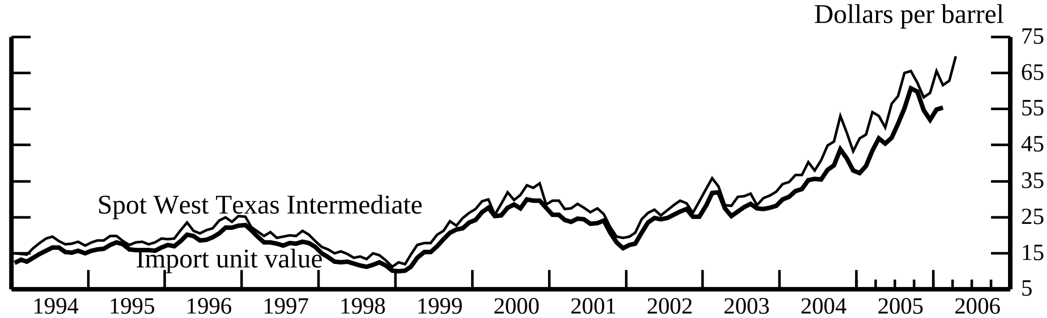
Prices of U.S. Imports and Exports

(Percentage change from previous period)

	Annual rate			Monthly rate		
	2005		2006	2006		
	Q3	Q4	Q1	Jan.	Feb.	Mar.
	BLS prices					
Merchandise imports	14.3	2.5	0.5	1.2	-0.5	-0.4
Oil	110.9	-11.3	7.7	6.0	-0.2	-0.7
Non-oil	-0.1	6.3	-0.9	0.3	-0.6	-0.3
Core goods*	-0.5	2.7	2.4	0.5	0.0	0.0
Cap. goods ex comp & semi	-0.4	0.0	1.6	0.2	0.4	0.0
Automotive products	0.6	0.6	-0.4	-0.1	0.1	0.0
Consumer goods	-0.9	-0.3	0.7	0.2	0.0	-0.2
Foods, feeds, beverages	-3.7	7.5	5.4	1.4	-2.1	0.4
Industrial supplies ex fuels	-1.3	8.0	12.6	1.5	1.4	0.8
Computers	-11.1	-7.7	-9.4	-1.4	-0.6	-0.5
Semiconductors	-4.9	-3.4	1.6	-0.4	0.1	0.1
Natural Gas	67.7	367.1	-61.4	-1.8	-20.3	-13.0
Merchandise exports	0.8	3.4	2.5	0.6	0.1	0.2
Core goods**	2.1	4.7	3.5	0.8	0.2	0.2
Cap. goods ex comp & semi	0.5	2.6	3.6	0.4	0.3	0.2
Automotive products	0.9	1.4	0.5	0.2	0.0	0.0
Consumer goods	-0.1	1.2	0.9	0.4	0.0	-0.3
Agricultural products	1.9	-4.4	-1.6	0.6	-0.7	-0.2
Industrial supples ex ag	6.1	13.0	7.2	1.7	0.5	0.5
Computers	-8.4	-8.3	-4.2	-0.3	-0.1	-0.1
Semiconductors	-12.4	-6.4	-7.9	-0.8	-1.5	0.1
	NIPA prices					
Chain price index						
Imports of goods & services	9.4	4.4	-0.5	...	...	...
Non-oil merchandise	-0.0	5.8	-1.6	...	...	...
Core goods*	-0.2	2.5	1.7	...	...	...
Exports of goods & services	2.9	2.7	2.5	...	...	...
Total merchandise	1.3	2.1	2.3	...	...	...
Core goods**	1.9	4.0	3.3	...	...	...

*/ Excludes computers, semiconductors, and natural gas.
**/ Excludes computers and semiconductors.
n.a. Not available. ... Not applicable.

Oil Prices



Oil. The BLS price index of imported oil fell 0.7 percent in March. Since mid-March, however, oil prices have soared to new highs. The spot price of West Texas Intermediate closed at $74.62 per barrel on May 2, up from an average of $62.90 per barrel in March. The recent increase in oil prices has been driven by heightened concerns about supply, against a backdrop of continued strong global demand. In Nigeria, about 500,000 barrels per day of oil production remain offline because of domestic instability, and the security situation there shows little signs of improvement. In recent weeks, tensions with Iran over its nuclear program have intensified. In April, Iran announced that it processed enriched uranium despite a warning by the United Nations that doing so could lead to economic sanctions. Also adversely impacting oil supplies are continued violence in Iraq, lasting damage from hurricanes in the Gulf of Mexico, and a worsening investment climate in many oil-producing countries. Moreover, low spare production capacity has lent upward pressure to oil prices by intensifying concerns about supply disruptions and increasing the demand for inventories. With world oil demand growth expected to remain relatively robust, market participants appear concerned that capacity additions will have difficulty keeping pace.

Exports. In March, U.S. export prices of total goods and of core goods both increased 0.2 percent. Prices for nonagricultural industrial supplies increased 0.5 percent, with falling prices for chemicals partially offsetting higher prices for metals and petroleum products. In contrast, agricultural prices fell 0.2 percent. Within finished goods, only capital goods (excluding computers and semiconductors) saw an increase, with prices increasing 0.2 percent. Prices of consumer goods fell 0.3 percent, the largest monthly decline since February 2002. In March, prices for exported computers fell 0.1 percent, whereas prices for semiconductors edged up 0.1 percent.

Core export prices rose 3¼ percent (a.r.) in the first quarter, as prices increased in all sub-categories with the exception of agricultural products. A substantial increase in prices for non-agricultural industrial supplies was the main contributor to the overall price increase. Prices of capital goods (excluding computers and semiconductors) and consumer goods also increased, but at a slower rate, in the first quarter.

U.S. International Financial Transactions

Foreign official flows into the United States (line 1 of the Summary of U.S. International Transactions table) eased in February and again in March after a hefty monthly inflow in January. For the quarter as a whole, net inflows are in line with inflows in the fourth quarter and above the average quarterly inflow for all of 2005. On net, inflows from most regions, including those from OPEC nations (line 1b), moved down over the course of the quarter.

. Confidential data on custody accounts at FRBNY point to aggregate inflows in April at a pace similar to that seen in recent months.

As noted in previous Greenbooks, the official monthly transactions data may understate inflows from official sources because they erroneously attribute some foreign official flows to the foreign private sector. For example, there may be misattribution in these data if official entities use a foreign intermediary to acquire U.S. assets. To the extent possible, BEA corrects for this misattribution in quarterly balance of payments statistics using data from FRBNY and elsewhere, and these corrections are carried through to the monthly data shown in the table.

Foreign private purchases of U.S. securities (line 4) picked up for the third consecutive month in March, and for the quarter as a whole, was just below the record level of inflows registered in the fourth quarter. As is typically the case, robust monthly inflows were recorded from the United Kingdom, a major financial center, providing little information about the residence of the ultimate purchaser. While net purchases of Treasury securities (line 4a) were weak in the first quarter, demand for both agency bonds (line 4b) and corporate stocks (line 4d) continued to trend up on balance. Demand for corporate bonds (line 4c) surged in March, and net purchases for the quarter were near a record high.

U.S. residents' acquisitions of foreign securities (line 5) strengthened in the first quarter. U.S. investors' appetite for foreign equities (line 5b) remained strong throughout the quarter, while measured net purchases of foreign bonds (line 5a) moved up over the period. The only stock swap recorded in the quarter is associated with the Israeli acquisition of IVAX Corporation, a generic drug manufacturer. U.S. acquisitions of foreign securities for the year to date are above the average quarterly flows recorded in 2005.

Net flows through the banking sector (line 3) continued to record small net outflows in each month of the first quarter.

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

	2004	2005	2005			2006		
			Q2	Q3	Q4	Q1	Feb	Mar
Official financial flows	**398.1**	**231.0**	**80.4**	**40.1**	**79.3**	**76.5**	**23.6**	**16.8**
1. Change in foreign official assets in the U.S. (increase, +)	395.3	216.9	81.2	35.3	74.5	76.0	23.8	16.6
a. G-10 countries + ECB	161.7	-22.7	-18.2	-5.1	-4.9	-9.1	-2.5	-5.6
b. OPEC	12.1	7.0	4.4	-3.8	10.3	11.6	2.8	0.4
c. All other countries	221.5	232.7	95.0	44.2	69.1	73.6	23.6	21.8
2. Change in U.S. official reserve assets (decrease, +)	2.8	14.1	-0.8	4.8	4.8	0.5	-0.2	0.3
Private financial flows	**186.5**	**569.9**	**70.3**	**213.8**	**155.7**	**n.a.**	**...**	**...**
Banks								
3. Change in net foreign positions of banking offices in the U.S. [1]	-3.8	17.0	-65.3	22.4	56.0	11.2	4.6	5.1
Securities [2]								
4. Foreign net purchases of U.S. securities (+)	506.0	687.6	127.8	196.3	199.4	193.4	66.4	77.0
a. Treasury securities	122.6	214.1	15.1	43.6	68.2	4.5	2.1	7.3
b. Agency bonds	66.0	67.4	19.7	32.7	15.2	42.7	19.4	9.7
c. Corporate and municipal bonds	255.0	316.7	78.6	88.8	91.4	91.3	27.7	42.5
d. Corporate stocks [3]	62.4	89.4	14.4	31.2	24.6	55.0	17.1	17.5
5. U.S. net acquisitions (-) of foreign securities	-146.2	-179.9	-45.7	-36.8	-47.1	-55.0	-13.7	-21.1
a. Bonds	-60.9	-36.6	-20.8	-1.8	-4.0	-11.9	-0.7	-8.2
b. Stock purchases	-97.6	-139.3	-23.0	-35.0	-43.1	-37.4	-13.0	-13.0
c. Stock swaps [3]	12.2	-4.0	-1.9	0.0	0.0	-5.8	0.0	0.0
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-252.0	-21.5	-21.6	25.3	2.1	n.a.	...	...
7. Foreign direct investment in the U.S.	106.8	128.6	14.7	48.4	30.6	n.a.	...	...
8. Foreign acquisitions of U.S. currency	14.8	19.4	4.5	4.7	9.2	n.a.	...	...
9. Other (inflow, +) [4]	-39.2	-81.3	55.8	-46.6	-94.5	n.a.	...	...
U.S. current account balance (s.a.)	**-668.1**	**-804.9**	**-196.9**	**-185.4**	**-224.9**	**n.a.**	**...**	**...**
Capital account balance (s.a.) [5]	**-1.6**	**-5.6**	**-0.3**	**-0.4**	**-0.4**	**n.a.**	**...**	**...**
Statistical discrepancy (s.a.)	**85.1**	**9.6**	**46.6**	**-68.0**	**-9.7**	**n.a.**	**...**	**...**

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

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

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

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

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

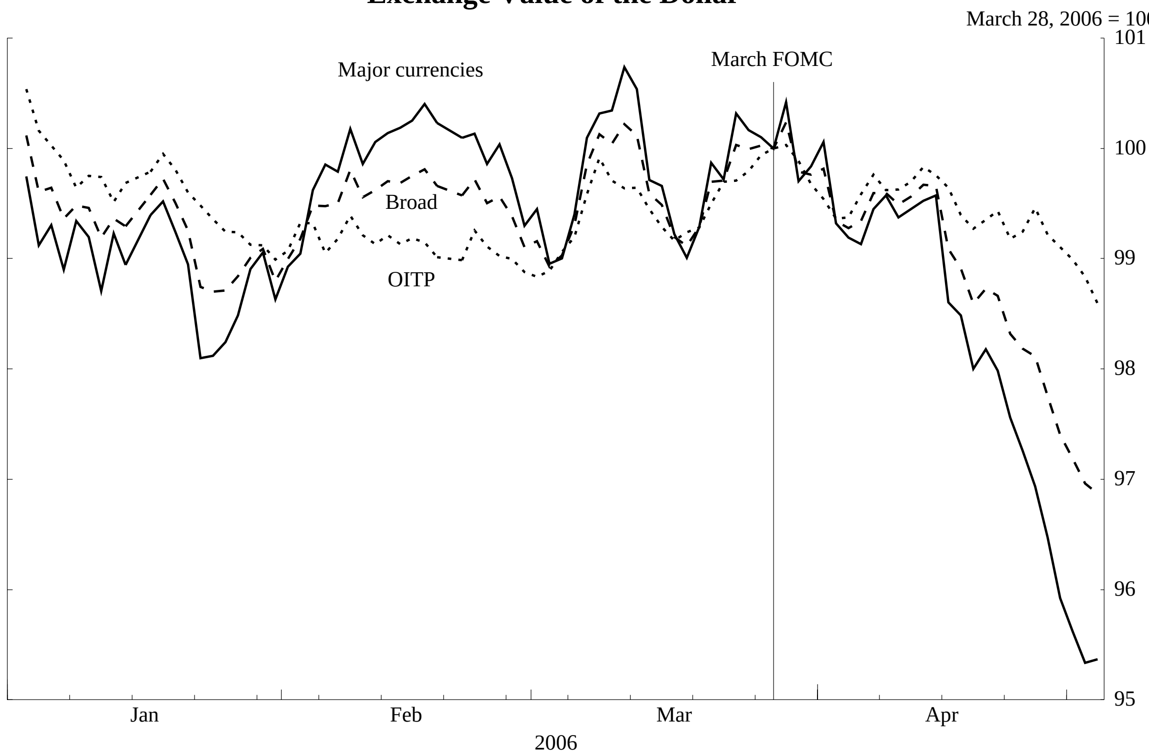
5. Consists of transactions in nonproduced nonfinancial assets and capital transfers.

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

Foreign Financial Markets

The dollar depreciated broadly and sharply over the intermeeting period. This development in the dollar may be, to a considerable degree, the result of a shift in market focus toward structural factors, including the implications of the U.S. external deficit. Global long-term yields rose markedly over the period, buoyed by new data that generally reinforced the strong global economic outlook, and led market participants to expect tighter monetary policy. Major foreign equity indexes generally rose, despite the rise in yields and soaring energy prices, and financial indicators in the emerging market economies improved.

Exchange Value of the Dollar



The dollar depreciated noticeably against all major foreign currencies over the intermeeting period, and the major currencies index dropped more than 4½ percent on net. The Canadian dollar appreciated about 5⅓ percent against the dollar, in part on Canadian economic data releases which were stronger than had been expected, but mainly on soaring commodity prices. The currencies of Australia and New Zealand and other commodity-exporting nations, appreciated about 8 and 6 percent, respectively. The yen appreciated about 3¼ percent against the dollar over the period, with about one half of the movement occurring on April 24 following the release of the G-7 communiqué, which said that "in emerging Asia, particularly China, greater flexibility in exchange rates is critical to allow necessary appreciation."

Financial Indicators in Major Industrial Countries

Country	Three-month rate: May 2/3 (Percent)	Three-month rate: Percentage point change	Ten-year yield: May 2/3 (Percent)	Ten-year yield: Percentage point change	Equities: percent change
Canada	4.22	.25	4.48	.32	1.89
Japan	.18	.00	1.93	.22	2.63
Euro area	2.87	.09	3.99	.26	1.25
United Kingdom	4.66	.09	4.66	.26	1.79
Switzerland	1.38	.16	2.73	.28	1.61
Australia	5.89	.29	5.78	.49	3.57
United States	5.11	.19	5.12	.42	1.57
Memo: Weighted-average foreign	2.69	.12	4.03	.25	n.a.

NOTE. Change is from March 27/28 to May 2/3.
n.a. Not available.

On April 25, the Bank of Canada increased its policy rate 25 basis points, to 4.0 percent. Whereas this decision had been widely expected, the accompanying statement, which was interpreted as signaling future policy rate increases, was not. Canadian three-month rates and ten-year sovereign yields rose 25 and 32 basis points, respectively, over the intermeeting period. In early April, the European Central Bank, the Bank of England, and the Bank of Japan all kept their respective policy rates unchanged. On net, deposits of Japanese financial institutions held at the Bank of Japan decreased about ¥10.5 trillion over the intermeeting period, to less than ¥18 trillion. Three-month spot interest rates were unchanged in Japan and increased 9 basis points in the United Kingdom and in Germany; ten-year sovereign yields in these three countries rose about 22 to 26 basis points. In Japan, Germany, and the United Kingdom, increases in nominal ten-year yields were accompanied by similar-sized increases in real yields, leaving implied inflation compensation rates little changed. Headline equity indexes rose about 1 to 3 percent in Japan, the United Kingdom, and the euro area. The strength of the global economy and some stronger-than-expected earnings reports supported share prices, but these were partly offset by rising yields and soaring energy prices.

Financial Indicators in Latin America, Asia, and Russia

Economy	Currency/ US dollar		Short-term interest rates[1]		Dollar-denominated bond spread[2]		Equity prices
	May 3	Percent change	May 2/3 (Percent)	Percentage point change	May 2/3 (Percent)	Percentage point change	Percent change
Mexico	10.95	.05	7.00	-.37	1.17	-.15	10.52
Brazil	2.06	-7.17	15.65	-.69	2.14	-.23	8.74
Argentina	3.04	-1.37	9.69	.31	3.11	-.43	5.14
Chile	515.35	-3.56	4.78	.13	.78	.06	2.42
China	8.01	-.14	n.a.	n.a.	.68	.01	n.a.
Korea	934.10	-4.34	4.05	.00	...	...	7.80
Taiwan	31.62	-3.02	1.70	.07	...	...	12.22
Singapore	1.57	-2.89	3.31	-.06	...	...	5.01
Hong Kong	7.75	-.08	4.61	.38	...	...	7.38
Malaysia	3.61	-2.34	3.65	.25	.89	.05	1.87
Indonesia	8770.00	-3.07	13.08	.08	2.01	-.19	13.12
Philippines	51.33	.45	7.13	.31	2.04	-.34	7.04
Russia	27.17	-1.99	n.a.	n.a.	1.00	-.08	21.05

NOTE. Change is from March 27/28 to May 2/3.

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. Spreads over similar maturity U.S. Treasuries. Mexico, Brazil, Argentina, Chile, Korea, China, Malaysia, Thailand, Indonesia, the Philippines and Russia: EMBI+/EMBI Global. Taiwan, Singapore, and Hong Kong do not have outstanding sovereign bonds denominated in dollars.

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

Major equity indexes in Latin America and emerging Asia rose about 6 to 13 percent over the intermeeting period. Notwithstanding the global rise in yields, the overall EMBI+ spread declined 24 basis points over the intermeeting period, to 1.75 percentage points, a new all-time low. The dollar depreciated about 7 percent against the Brazilian *real*, but was little changed on net against the Mexican peso. The dollar has depreciated against most floating currencies in emerging Asia: about 4⅓ percent against Korean won, 3 percent against Indonesian rupiah, the Singapore dollar, and the Taiwanese dollar, and about 2⅓ percent against the Malaysian ringgit. Most of these moves came early on April 24, following the release of the G-7 communiqué. The renminbi was little changed on net over the intermeeting period. It fluctuated slightly more than in previous months on a day-to-day basis and reached a high against the dollar on April 11 before retracing later in the intermeeting period. On April 27, the People's Bank of China unexpectedly raised its benchmark one-year lending rate to 5.85 percent, from 5.58 percent; it was the first such increase since October 2004.

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

Developments in Foreign Industrial Countries

Incoming data in the foreign industrial economies are generally favorable and point to continued expansion. Preliminary GDP for the United Kingdom rose 2.6 percent in the first quarter. Canadian monthly GDP through February showed that domestic demand, particularly consumption, remained strong**.** Monthly indicators suggest that the recovery in Japan is ongoing and that euro-area GDP growth has rebounded from its fourth-quarter slowdown.

Increases in oil and other primary commodity prices have raised headline inflation rates abroad, but core inflation has stayed well contained. Core inflation edged up in the euro area in February and remained stable in Canada through March. In Japan, core consumer price inflation has now been slightly positive for the last several months. Inflation in the United Kingdom dropped unexpectedly in March as food prices fell.

Indicators of activity in **Japan** point to continued growth. The Bank of Japan's Tankan diffusion index of business conditions for firms of all sizes and industries remained at its recent high of 5 in March. Industrial production rose 0.6 percent in the first quarter while the manufacturing PMI remained near record highs. Activity in the construction and service sectors also appeared to be solid, as housing starts rose 1.5 percent in the first quarter and the tertiary services index was above its fourth quarter average over the first two months of the year. Although real spending in the first quarter by households fell, retail sales rose 1.8 percent and auto registrations rose 3.3 percent. The real trade balance improved in the first quarter, as exports rose 3.4 percent and imports rose 2.4 percent.

The labor market continued to improve in the first quarter with employment rising 0.3 percent and the unemployment rate falling to 4.1 percent, the lowest rate in eight years. The offers-to-applicants ratio (the number of officially posted job openings relative to the number of officially registered job seekers) fell slightly in March but remained near a thirteen-year high. The March Tankan survey also signaled a tighter labor market, as the number of firms reporting an insufficient number of employees rose. Nominal wages were up 0.2 percent in February compared with the same month a year earlier.

Core consumer prices (which exclude fresh food but include energy) in the Tokyo area were unchanged in April but were 0.3 percent higher than a year ago. Core consumer prices for the country as a whole were 0.5 percent higher in March than a year earlier. Much of the increase was due to energy prices, however, and consumer prices for the country excluding both fresh food and energy were only 0.2 percent higher than a year earlier. Twelve-month wholesale price inflation was 2.7 percent in March. It was also reported that last year commercial land prices rose in Japan's major metropolitan areas for the first time in 15 years; they were up 1 percent from a year earlier.

The outstanding balance of reserves accounts held by the Bank of Japan has steadily decreased since the Bank announced an end to its policy of quantitative easing. Reserves fell to ¥19 trillion in April, well below the ¥30 trillion floor set under quantitative easing, and are expected to continue falling for several more months. Yields on ten-year government bonds have risen 30 basis points since the end of quantitative easing. In the April release of its semiannual Outlook the Bank of Japan’s board members revised their median forecast for real GDP growth in current fiscal year up from 1.8 percent to 2.4 percent while their forecast for core CPI inflation was revised up one tenth to 0.6 percent. For the following fiscal year, board members predicted that real GDP would grow 2.0 percent and core CPI inflation would rise to 0.8 percent.

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

Indicator	2005		2006	2006			
	Q3	Q4	Q1	Jan.	Feb.	Mar.	Apr.
Industrial production[1]	-.5	2.7	.6	-.1	-1.2	.2	n.a.
All-industries index	.2	1.1	n.a.	1.0	-1.0	n.a.	n.a.
Housing starts	6.5	-2.0	1.5	7.7	6.0	-8.8	n.a.
Machinery orders[2]	2.1	4.1	n.a.	-6.2	3.4	n.a.	n.a.
Machinery shipments[3]	1.7	4.0	-.2	-1.0	-1.9	.6	n.a.
New car registrations	-4.8	-4.5	3.0	5.1	-.5	.3	-1.6
Unemployment rate[4]	4.3	4.5	4.2	4.5	4.1	4.1	n.a.
Job offers ratio[5]	.97	1.00	1.03	1.03	1.04	1.01	n.a.
Business sentiment[6]	2.0	5.0	5.0	...	...	...	...
CPI (core, Tokyo area)[7]	-.4	-.3	.2	.1	.2	.2	.3
Wholesale prices[7]	1.7	2.1	2.8	2.7	3.0	2.7	n.a.

1. Mining and manufacturing.
2. Private sector, excluding ships and electric power.
3. Excluding orders for ships and from electric power companies.
4. Percent.
5. Level of indicator.
6. Tankan survey, diffusion index.
7. Percent change from year earlier, n.s.a.
n.a. Not available. . . . Not applicable.

In the **euro area**, survey indicators of activity have risen to high levels and hard data have begun to confirm the increased pace of activity. The PMI for the manufacturing sector advanced further in April to 56.7 (where 50 is the threshold for positive growth), the highest level since 2000. The PMI for services remained elevated in March near 58. Importantly, the employment components of both PMI surveys have made strong gains recently, an indication that firms are likely to step up hiring. In another sign of an improving labor market, the euro-area unemployment rate edged down to 8.1 percent in March, versus 8.8 percent one year ago.

Euro-area industrial production was flat in February, but the January-February average level was 0.8 percent above the fourth-quarter average. Euro-area industrial orders rose sharply in February for the second straight month, suggesting that strength in production is likely to persist. The German manufacturing sector has continued to show particular strength, with the IFO business climate index rising to a 15-year high in April. German industrial production increased 1 percent in February, and the January number was revised up from a small decline to a 0.4 percent increase. The February increase was particularly sharp in the energy and construction sectors, with the latter rebounding from the effects of January's unusually severe weather. Manufacturing output registered fairly strong gains, with capital goods production increasing robustly, although consumer goods production was little changed.

Indicators of euro-area consumption have been mixed. The average volume of euro-area retail sales fell slightly in February from the previous month but average sales for January and February were up 0.3 percent from the fourth quarter. French consumption of manufactured products moved lower in March but posted a strong 1.1 percent gain for the first quarter as a whole. German consumer spending was a relative weak spot, with retail sales falling sharply in March. Euro-area consumer confidence moved back up in April to the 3½-year high reached in February.

The twelve-month rate of euro-area consumer price inflation edged down to 2.2 percent in March. Core inflation, excluding energy and unprocessed food, continued to be well-behaved, edging up from 1.3 percent in February to 1.4 percent in March. The European Central Bank held its main refinancing rate at 2.5 percent at its April meeting. In the post-meeting statement, President Trichet punctured market expectations of a May interest rate hike but left the door wide open for a rise in June.

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

Indicator	2005		2006	2006			
	Q3	Q4	Q1	Jan.	Feb.	Mar.	Apr.
Industrial production[1]	.9	.5	n.a.	.2	.0	n.a.	n.a.
Retail sales volume[2]	.7	.3	n.a.	.5	-.1	n.a.	n.a.
Unemployment rate[3]	8.5	8.3	8.2	8.2	8.2	8.1	n.a.
Consumer confidence[4]	-14.7	-12.3	-10.7	-11.0	-10.0	-11.0	-10.0
Industrial confidence[4]	-7.7	-6.0	-2.3	-4.0	-2.0	-1.0	1.0
Manufacturing orders, Germany	4.2	3.4	n.a.	1.4	[5/8]	n.a.	n.a.
CPI[5]	2.3	2.3	2.3	2.4	2.3	2.2	2.4
Producer prices[5]	4.2	4.4	5.2	5.3	5.4	5.1	n.a.
M3[5]	8.4	7.4	8.6	7.7	7.9	8.6	n.a.

1. Excludes construction.
2. Excludes motor vehicles.
3. Percent. Euro-area standardized to ILO definition. Includes Eurostat estimates in some cases.
4. Diffusion index based on European Commission surveys in individual countries.
5. Eurostat harmonized definition. Percent change from year earlier, s.a.
n.a. Not available.

Real GDP in the **United Kingdom** rose 2.6 percent (a.r.) in the first quarter, according to a preliminary estimate. The production sector rose 0.7 percent compared with a fall of 0.9 in the fourth quarter of 2005. All production sectors showed positive growth. Manufacturing rose 0.5 percent compared with a fall of 1.1 in the fourth quarter. The services sector grew by 0.6 percent, a slowing of growth compared with the previous quarter when it grew by 1.0 percent.

The housing sector is continuing its recovery, with house prices increasing at an annual rate of around 9 percent in the first quarter, and mortgage lending approaching the previous high of £10 billion achieved in late 2003.

The twelve-month change in consumer prices dropped back sharply from 2.1 to 1.8 percent in March, below the Bank of England's target of 2 percent. The fall in inflation owed to a decline in food prices, particularly milk. Consumer prices, excluding energy, fell from 1.4 percent in February to 1.1 percent in March. In its April minutes the Bank of England's Monetary Policy Committee voted to keep its policy rate constant at 4.5 percent.

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

Indicator	2005		2006	2006			
	Q3	Q4	Q1	Jan.	Feb.	Mar.	Apr.
Real GDP*	1.9	2.2	2.6	…	…	…	…
Industrial production	-.6	-.9	n.a.	.3	-.2	n.a.	n.a.
Retail sales volume[1]	.3	1.6	-.7	-1.7	.3	.6	n.a.
Unemployment rate[2]							
Claims-based	2.7	2.8	2.9	2.9	2.9	3.0	n.a.
Labor force survey[3]	4.8	5.0	n.a.	5.1	n.a.	n.a.	n.a.
Business confidence[4]	5.0	-2.0	8.0	1.0	10.0	13.0	12.0
Consumer confidence[5]	-2.0	-4.0	-4.0	-4.0	-2.0	-6.0	-3.0
Consumer prices[6]	2.4	2.1	2.0	1.9	2.1	1.8	n.a.
Producer input prices[7]	12.5	13.5	14.5	15.7	14.9	13.1	n.a.
Average earnings[7]	4.1	3.6	n.a.	3.1	5.3	n.a.	n.a.

* Preliminary estimate (s.a.a.r.)
1. Excludes motor vehicles.
2. Percent.
3. Three-month average centered on month shown.
4. Percentage of firms expecting output to increase in the next four months less percentage expecting output to decrease.
5. Average of the percentage balance from consumers' expectations of their financial situation, general economic situation, unemployment, and savings over the next 12 months.
6. Consumer prices index (CPI), percent change from year earlier.
7. Percent change from year earlier.
n.a. Not available. . . . Not applicable.

In **Canada,** GDP by industry rose 2.7 percent (a.r.) in February, with activity in residential building construction and wholesale trade continuing to grow briskly. Following a sharp decline in January due to mild weather, the energy sector rebounded, in particular the utilities industries. A sizable drop in the manufacturing, mining, and oil and gas extraction sectors restrained growth.

Overall, other indicators for the first quarter have been positive. Housing starts accelerated throughout the quarter, with starts in March hitting their highest monthly level during the current housing boom, which began in 2002. Retail sales continued to climb in February. The composite index of leading indicators advanced sharply in March, with only two of ten components, both related to manufacturing, retreating. The manufacturing sector continues to struggle, with shipments and new orders both down substantially in February.

The labor market continued its recent roll in March, posting a net gain of 51,000 jobs, most of which were full-time positions. The unemployment rate dipped in March to 6.3 percent, a 32-year-low, and the employment rate (the ratio of the working age population that is employed) hit a record high 62.9 percent.

In March, the twelve-month rate of consumer price inflation remained unchanged from its February rate of 2.2 percent. The twelve-month rate of core inflation, which excludes the eight most volatile components, remained unchanged at 1.7 percent.

On April 25, the Bank of Canada increased its target for the overnight rate ¼ percentage point to 4 percent, following ¼ percentage point increases at each of its previous five meetings. The accompanying statement noted that the Bank would monitor developments closely "…in light of the cumulative increase in the policy rate since last September," but also that "…some modest further increase in the policy interest rate may be required to keep aggregate supply and demand in balance and inflation on target over the medium term." On May 2, the Canadian government released a budget plan. The central feature of the plan is a one-percentage point cut in the Goods and Services Tax, effective July 1. Also planned is a corporate income tax cut that would cut the rate to 19 percent by 2010, from its current 21 percent.

Canadian Economic Indicators

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

Indicator	2005		2006	2005	2006		
	Q3	Q4	Q1	Dec.	Jan.	Feb.	Mar.
GDP by industry	1.0	.7	n.a.	.4	.2	.2	n.a.
Industrial production	1.2	.8	n.a.	.8	-.9	.0	n.a.
New manufacturing orders	1.2	.8	n.a.	1.6	.1	-2.1	n.a.
Retail sales	.2	.6	n.a.	.3	.8	.2	n.a.
Employment	.4	.6	.4	-.1	.2	.2	.3
Unemployment rate[1]	6.8	6.5	6.4	6.5	6.6	6.4	6.3
Consumer prices[2]	2.6	2.3	2.4	2.2	2.8	2.2	2.2
Core consumer prices[2,3]	1.6	1.6	1.7	1.5	1.7	1.7	1.7
Consumer attitudes (1991 = 100)	108.3	118.4	121.0	…	…	…	…
Business confidence (1991 = 100)	127.1	147.2	146.0	…	…	…	…

1. Percent.
2. Percent change from year earlier, n.s.a.
3. Excluding the 8 most volatile components (fruits, vegetables, gasoline, fuel oil, natural gas, mortgage interest, intercity transportation, and tobacco).

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

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

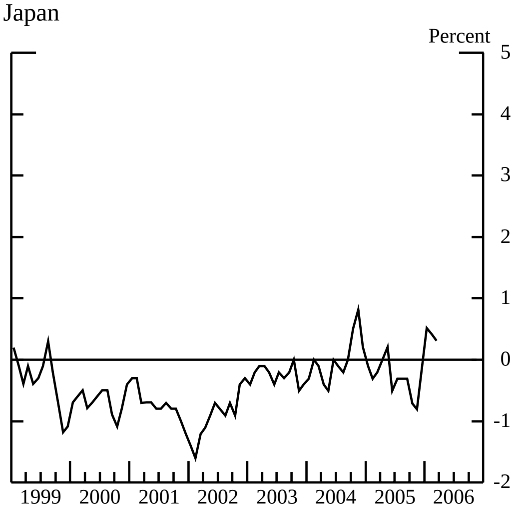
Country and balance	2005 Q3	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
Japan						
Trade	66.1	67.9	67.6	61.6	69.9	71.4
Current account	157.9	180.7	n.a.	155.2	170.5	n.a.
Euro area						
Trade	9.5	-14.3	n.a.	-7.1	-39.0	n.a.
Current account	-45.0	-97.8	n.a.	-10.2	-80.2	n.a.
Germany						
Trade	199.3	181.1	n.a.	174.8	176.9	n.a.
Current account	106.7	100.1	n.a.	96.4	148.9	n.a.
France						
Trade	-28.2	-37.4	n.a.	-35.1	-28.9	n.a.
Current account	-35.4	-53.8	n.a.	-76.9	-4.5	n.a.
Italy						
Trade	-17.5	-18.3	n.a.	-23.9	-30.1	n.a.
Current account	-25.5	-25.1	n.a.	-29.6	-37.1	n.a.
United Kingdom						
Trade	-122.5	-120.6	n.a.	-138.8	-135.9	n.a.
Current account	-78.4	-76.6	n.a.	…	…	…
Canada						
Trade	60.8	74.9	n.a.	63.9	65.9	n.a.
Current account	25.8	45.3	n.a.	…	…	…

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

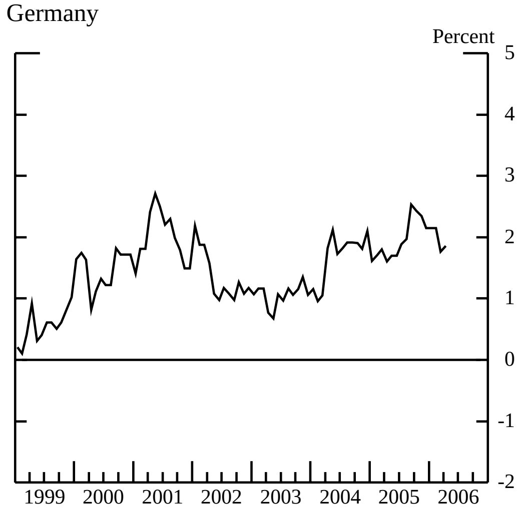
Consumer Price Inflation in Selected Industrial Countries

(12-month change)

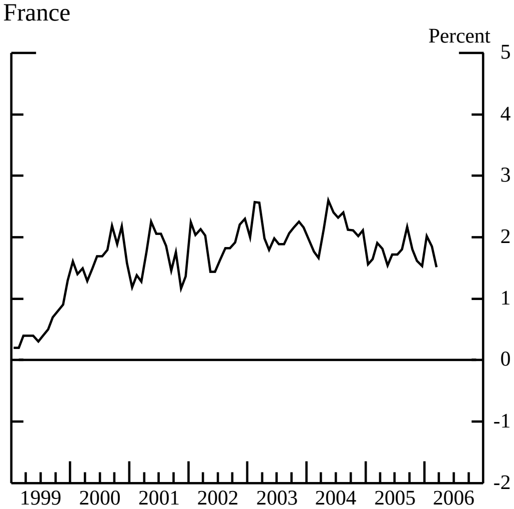
Japan



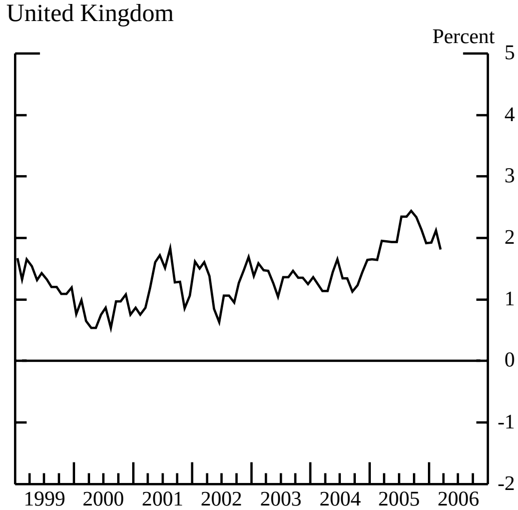
Germany



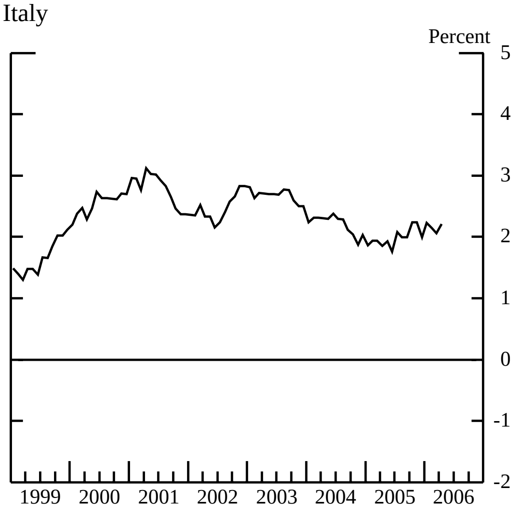
France



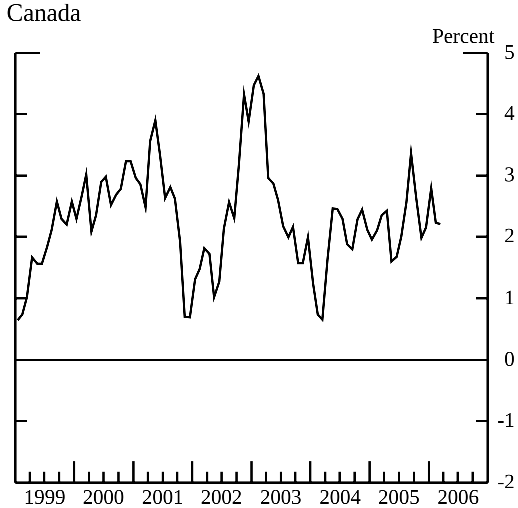
United Kingdom



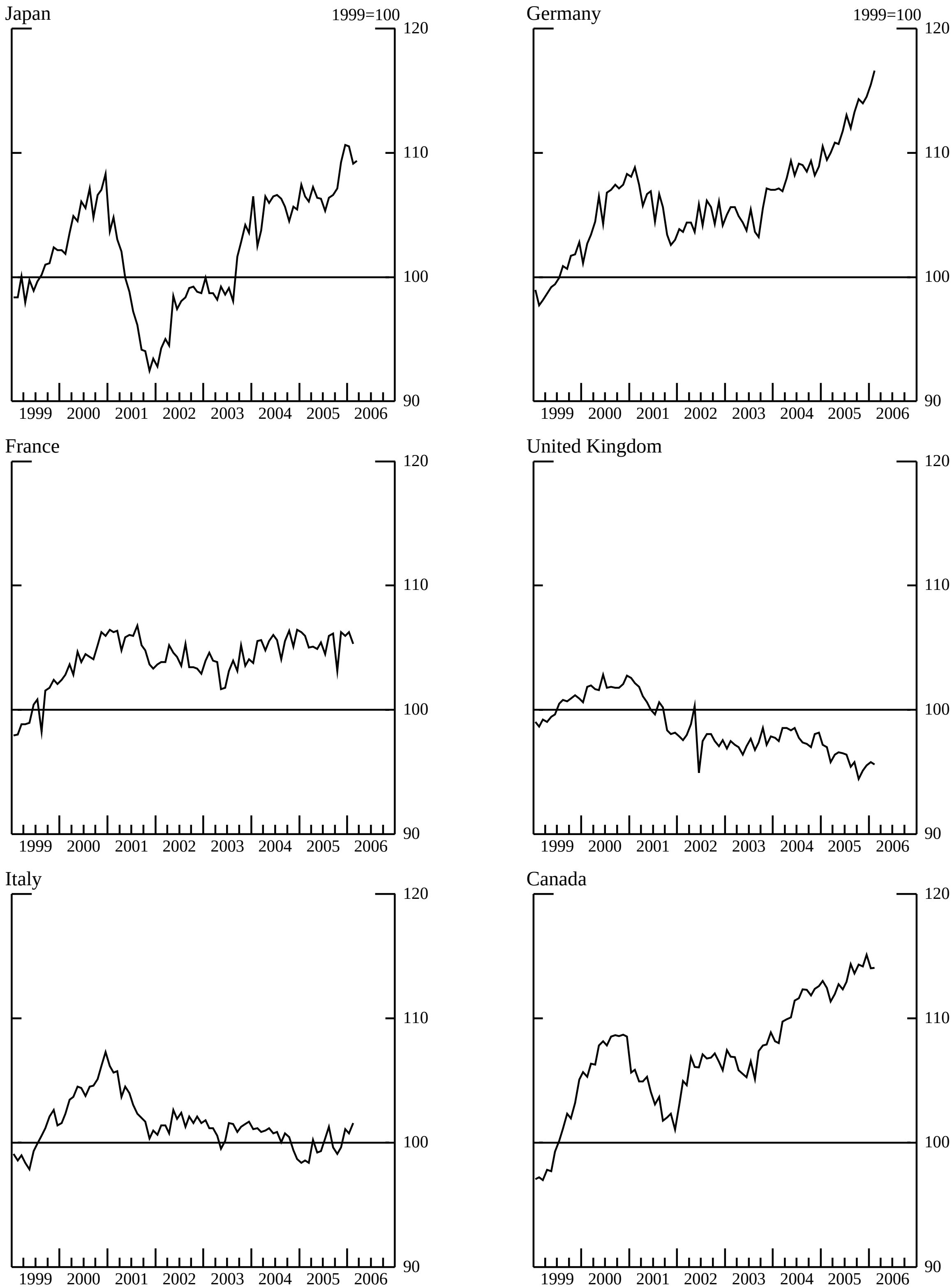
Italy



Canada



Industrial Production in Selected Industrial Countries



Economic Situation in Other Countries

Recent economic indicators from the emerging market economies suggest a slight deceleration in activity from the strong fourth-quarter pace, although with some variation across countries. Chinese growth surged in the first quarter, but advanced estimates of first-quarter GDP for Korea and Singapore pointed to some slowing from the rapid pace observed in the second half of 2005. Indicators for Mexico point to strength in the first quarter, with industrial activity finally bouncing back after being weak last year, but elsewhere in Latin America indicators are not as positive. Despite two years of increases in oil prices, twelve-month consumer price inflation moved down in recent months in most of the major emerging market economies. Monetary policy was tightened in several emerging Asian economies since the last Greenbook, while there was some easing in monetary policy in Latin America.

Chinese real GDP grew almost 13 percent (s.a.a.r.) in the first quarter according to staff estimates. In releasing the figures, Chinese officials cited a surge in investment as well as stronger exports. In late April, the Chinese government announced that controls on credit and land use, as well as stricter approval criteria for investment projects, would be used to slow investment growth in several sectors. These measures to slow investment follow similar measures enacted by the Chinese government only one month ago. In addition, the People's Bank of China raised the benchmark one-year bank lending rate 27 basis points in late April. The trade balance set a new quarterly record in the first quarter, reaching an annual rate of almost $130 billion, with exports accelerating after a relatively weak fourth quarter. Consumer price inflation moved down in the quarter to a four-quarter change of 1.2 percent, as food price inflation dipped noticeably.

The Chinese government announced that restrictions on capital outflows from China would be lessened effective May 1. The new program will allow domestic institutional investors to take money out of China for the purpose of investing in foreign fixed income securities.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Jan	Feb.	Mar.
Real GDP[1]	10.1	9.9	11.5	12.9	…	…	…
Industrial production	14.4	17.1	4.0	5.3	1.9	1.9	1.0
Consumer prices[2]	2.5	1.6	1.4	1.2	1.8	1.0	.8
Trade balance[3]	32.1	102.0	89.1	127.5	139.8	80.6	162.1

1. Annual rate. Quarterly data estimated by staff from reported four-quarter growth rates. Annual data are Q4/Q4.
2. Percent change from year-earlier period, except annual data, which are Dec./Dec.
3. Billions of U.S. dollars, annual rate. Imports are c.i.f.
. . . Not applicable.

In **Hong Kong**, the trade deficit narrowed in the first quarter, as imports slowed noticeably. March unemployment remained at its lowest level in over four years. On average over the past few months, twelve-month consumer price inflation has stayed close to 2 percent.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Jan.	Feb.	Mar.
Real GDP[1]	7.3	7.7	2.4	n.a.	…	…	…
Unemployment rate[2]	6.9	5.7	5.3	5.2	5.2	5.2	5.2
Consumer prices[3]	.2	1.8	1.8	2.0	2.4	1.8	1.8
Trade balance[4]	-12.0	-10.5	-13.4	-6.8	-27.3	11.6	-4.7

1. Annual rate. Annual data are Q4/Q4.
2. Percent. Monthly data are averages of the current and previous two months.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.
n.a. Not available. . . . Not applicable.

In **Taiwan**, industrial production rose slightly on balance in the first quarter, but monthly changes were quite volatile due to the Lunar New Year. Export orders followed a similar pattern. In March, import growth outpaced export growth, contributing to a moderate deterioration in the trade balance from a strong February level. Consumer price inflation moved down sharply in recent months, reaching less than half a percent in March on a twelve-month basis, largely owing to falling food prices. Taiwan's central bank raised interest rates slightly in late March, citing concerns about potential pass through of higher oil prices to other consumer prices. State-controlled fuel prices were raised 8 percent on average in April.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Jan.	Feb.	Mar.
Real GDP[1]	2.6	6.4	7.7	n.a.	…	…	…
Unemployment rate[2]	4.4	4.1	4.0	4.0	4.0	4.0	3.9
Industrial production	9.8	4.1	3.4	.6	-3.3	9.9	-6.8
Consumer prices[3]	1.6	2.2	2.5	1.4	2.7	1.0	.4
Trade balance[4]	6.1	7.8	21.6	13.4	4.9	25.6	9.7
Current account[5]	18.5	16.4	36.9	n.a.	…	…	…

1. Annual rate. Annual data are Q4/Q4.
2. Percent.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.

Korean real GDP grew 5.1 percent (s.a.a.r.) in the first quarter aided by continued growth in private consumption and gains in stocks of inventories. However, fixed investment fell somewhat following strong fourth-quarter growth. Exports and imports both rose in the first quarter, and the trade surplus narrowed. Industrial production growth moderated in the first quarter, and consumer and business confidence softened from their recent peaks, though they remained elevated. Consumer price inflation has been remarkably tame, rising 2 percent over the twelve months ended April, held down by falling food prices.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Feb.	Mar.	Apr.
Real GDP[1]	2.9	5.3	6.7	5.1	…	…	…
Industrial production	10.0	5.9	5.5	3.1	-4.4	.9	n.a.
Unemployment rate[2]	3.5	3.7	3.6	3.5	3.5	3.5	n.a.
Consumer prices[3]	3.0	2.6	2.5	2.4	2.3	2.0	2.0
Trade balance[4]	37.6	33.5	31.9	25.8	18.9	41.9	n.a.
Current account[5]	28.2	16.6	21.7	-4.2	-9.4	-4.4	n.a.

1. Annual rate. Annual data are Q4/Q4.
2. Percent.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.

Incoming data from the **ASEAN** countries suggest that economic activity moderated on average in the first quarter. In Singapore, the advance estimate of first-quarter real GDP growth (unofficial) fell to 1.2 percent from its blistering fourth-quarter rate, due mostly to a contraction in the volatile biomedical sector. In every country in the region, the most recent readings on industrial production were down, and in most of the region, trade balances are up relative to the fourth quarter.

Consumer price inflation remained elevated in the region, reflecting higher food prices in some countries as well as the effect of higher energy prices. The recent increase in energy costs is partly the result of cuts in fuel subsidies, most notably in Indonesia and Malaysia. Citing inflationary pressures, the central banks of Thailand and Malaysia raised interest rates 25 basis points in April.

ASEAN Economic Indicators: Growth

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

Indicator	2004	2005	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
Real GDP[1]							
Indonesia	7.0	5.0	4.0	n.a.	…	…	…
Malaysia	5.8	5.2	4.3	n.a.	…	…	…
Philippines	5.4	6.2	11.1	n.a.	…	…	…
Singapore	6.6	8.5	12.5	n.a.	…	…	…
Thailand	5.5	4.7	3.6	n.a.	…	…	…
Industrial production[2]							
Indonesia[3]	3.3	1.1	-2.7	n.a.	-7.5	-.5	n.a.
Malaysia	11.7	4.1	-.3	n.a.	5.9	-9.1	n.a.
Philippines	1.0	2.2	7.7	n.a.	-11.8	-2.7	n.a.
Singapore	13.9	9.5	5.4	1.5	-8.4	18.4	-4.5
Thailand	11.6	9.1	-1.3	2.1	-1.1	4.9	-.1

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

Indicator	2004	2005	2005 Q4	2006 Q1	2006 Jan.	2006 Feb.	2006 Mar.
Indonesia	25.1	28.0	35.5	39.9	39.1	39.8	40.9
Malaysia	21.2	26.4	25.1	n.a.	32.7	27.8	n.a.
Philippines	-4.4	-6.2	-8.2	n.a.	-4.6	-.2	n.a.
Singapore	17.4	29.6	33.0	40.8	47.7	25.6	49.0
Thailand	1.5	-8.6	-8.6	1.4	3.3	-5.9	6.8

n.a. Not available.

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

Indicator	2004[1]	2005[1]	2005	2006			
			Q4	Q1	Feb.	Mar.	Apr.
Indonesia	6.6	17.0	17.8	17.0	18.0	15.8	15.4
Malaysia	2.1	3.3	3.3	3.8	3.2	4.8	n.a.
Philippines	8.6	6.7	6.9	7.3	7.6	7.6	n.a.
Singapore	1.3	1.3	1.1	1.4	1.2	1.2	n.a.
Thailand	2.9	5.8	6.0	5.7	5.6	5.7	6.0

1. Dec./Dec.
n.a. Not available

Indian economic performance remained robust. Industrial production stabilized in February after surging the previous month. The closely watched wholesale price index has risen a relatively moderate 4.1 percent over the twelve months ended March. India's trade deficit widened to $42.5 billion in the first quarter due to a fall in exports and rise in imports, including a sharp rise in net oil imports. Last month, the government announced its intent to move toward allowing freer capital movements over the next several years.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Jan.	Feb.	Mar.
Real GDP[1]	7.0	7.6	8.4	n.a.	…	…	…
Industrial production	8.5	7.9	2.5	n.a.	2.1	.4	n.a.
Consumer prices[2]	3.8	5.6	5.0	n.a.	4.4	n.a.	n.a.
Wholesale prices[2]	6.7	4.4	4.5	4.1	4.1	4.1	4.1
Trade balance[3]	-21.7	-39.4	-28.1	-42.5	-31.4	-49.1	-47.2
Current account[4]	1.4	-12.9	-15.4	n.a.	…	…	…

1. Annual rate. Annual data are Q4/Q4.
2. Percent change from year-earlier period, except annual data, which are Dec./Dec.
3. Billions of U.S. dollars, annual rate.
4. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.

In **Mexico**, recent indicators point to a solid bounceback in industrial activity, which had been soft during most of 2005. In particular, automobile production and exports soared in the first quarter. The strong performance in the auto sector contributed to a solid January performance in industrial production, which rose 1.2 percent from December, and production moved up further in February. The surge in manufacturing exports led to a sizable improvement in Mexico's trade balance in the first quarter. On the domestic demand side, indicators suggest that in the first quarter fixed investment remained strong, but consumer spending moderated a bit.

Consumer price inflation remained well contained and is within the Bank of Mexico's 2 - 4 percent target range. Twelve-month headline inflation was 3.4 percent in March, while core inflation was 3.1 percent. Benign inflation prospects led the Bank of Mexico (BOM) to ease policy in April, the ninth easing since August. As a result, the rate on 28-day peso-denominated bills, a widely used measure of the monetary policy stance, has fallen from 9.6 percent in August to 7 percent in early May. However, the latest BOM announcement stated that there is no room for additional loosening of monetary policy.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Jan.	Feb.	Mar.
Real GDP[1]	4.8	2.7	2.4	n.a.	…	…	…
Overall economic activity	3.8	3.3	.6	n.a.	2.1	-.6	n.a.
Industrial production	3.9	1.9	2.3	n.a.	1.2	.1	n.a.
Unemployment rate[2]	3.9	3.6	3.3	3.4	3.4	3.5	3.5
Consumer prices[3]	5.2	3.3	3.1	3.7	3.9	3.8	3.4
Trade balance[4]	-8.8	-7.6	-5.9	1.8	10.4	.4	-5.3
Imports[4]	196.8	221.3	237.0	243.0	243.4	242.8	242.7
Exports[4]	188.0	213.7	231.1	244.8	253.8	243.2	237.4
Current account[5]	-7.1	-5.7	-10.7	n.a.	…	…	…

1. Annual rate. Annual data are Q4/Q4.
2. Percent; counts as unemployed those working one hour a week or less.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.

In **Brazil**, recent data releases have been mixed. Industrial output was up on average in January and February from its average level in the fourth quarter. On the other hand, February retail sales decreased by more than had been expected. Headline inflation continued to decline on a twelve-month basis and stood at 5.3 percent in March.

In late March, Antonio Palocci resigned as Brazil's finance minister, and Guido Mantega, head of the national development bank, was appointed to the post. Since taking office, Mantega has stressed that the government will adhere to its primary surplus target of 4¼ percent of GDP, but many observers have expressed concerns over the sharp rise in government spending in recent months.

On April 17, the Brazilian central bank's monetary policy committee reduced its interest rate target ¾ percentage point to 15.75 percent. This is down 400 basis points since the current easing phase began last September. The decision was expected and prompted little reaction in financial markets. In mid-April, the government exercised its call option and bought back the remaining $6.6 billion in Brady bonds.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Feb.	Mar.	Apr.
Real GDP[1]	4.7	1.5	3.4	n.a.	…	…	…
Industrial production	8.3	3.1	.6	n.a.	1.2	n.a.	n.a.
Unemployment rate[2]	11.5	9.8	9.6	10.0	10.2	10.0	n.a.
Consumer prices[3]	7.6	5.7	6.1	5.5	5.5	5.3	n.a.
Trade balance[4]	33.6	44.8	50.3	45.3	40.5	46.0	40.0
Current account[5]	11.7	14.2	12.7	7.2	8.7	16.2	n.a.

1. Annual rate. Annual data are Q4/Q4.
2. Percent.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec. Price index is IPCA.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.

In **Argentina**, monthly economic indicators suggest growth slowed sharply in the first quarter. Industrial production rose just ½ percent in the quarter. Consumer price inflation edged down to 11.1 percent in March on a twelve-month basis, a touch above the central bank's 2006 inflation projection of 8 - 11 percent.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Jan.	Feb.	Mar.
Real GDP[1]	9.1	9.1	8.8	n.a.	…	…	…
Industrial production	10.7	7.7	2.6	.5	-2.2	3.3	.4
Unemployment rate[2]	13.6	11.6	10.1	n.a.	…	…	…
Consumer prices[3]	5.9	12.2	11.6	11.5	12.0	11.4	11.1
Trade balance[4]	12.1	11.3	9.8	9.4	11.3	9.0	10.3
Current account[5]	3.3	5.4	5.9	n.a.	…	…	…

1. Annual rate. Annual data are Q4/Q4.
2. Percent; n.s.a.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.

In **Venezuela**, anecdotal evidence suggests that activity has continued to be strong, supported by expansionary fiscal and monetary policies and the high price of oil. Inflation declined on a twelve-month basis to about 11 percent in April, suppressed by price controls on food. In early April, the Venezuelan government announced that it had completed 75 percent of its planned buyback of $3.9 billion in Brady bond debt and indicated that the remaining buybacks would occur by end-May.

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

Indicator	2004	2005	2005	2006			
			Q4	Q1	Feb.	Mar.	Apr.
Real GDP[1]	12.1	10.2	14.4	n.a.	…	…	…
Unemployment rate[2]	15.1	12.2	11.8	n.a.	n.a.	n.a.	n.a.
Consumer prices[3]	19.2	14.4	15.2	12.5	12.5	12.1	11.3
Non-oil trade balance[4]	-10.5	-16.5	-25.6	n.a.	n.a.	n.a.	n.a.
Trade balance[4]	21.4	31.5	35.7	n.a.	n.a.	n.a.	n.a.
Current account[5]	13.8	25.4	25.6	n.a.	…	…	…

1. Annual rate. Annual data are Q4/Q4.
2. Percent.
3. Percent change from year-earlier period, except annual data, which are Dec./Dec.
4. Billions of U.S. dollars, annual rate.
5. Billions of U.S. dollars, n.s.a., annual rate.
n.a. Not available. . . . Not applicable.