



Economic Outlook

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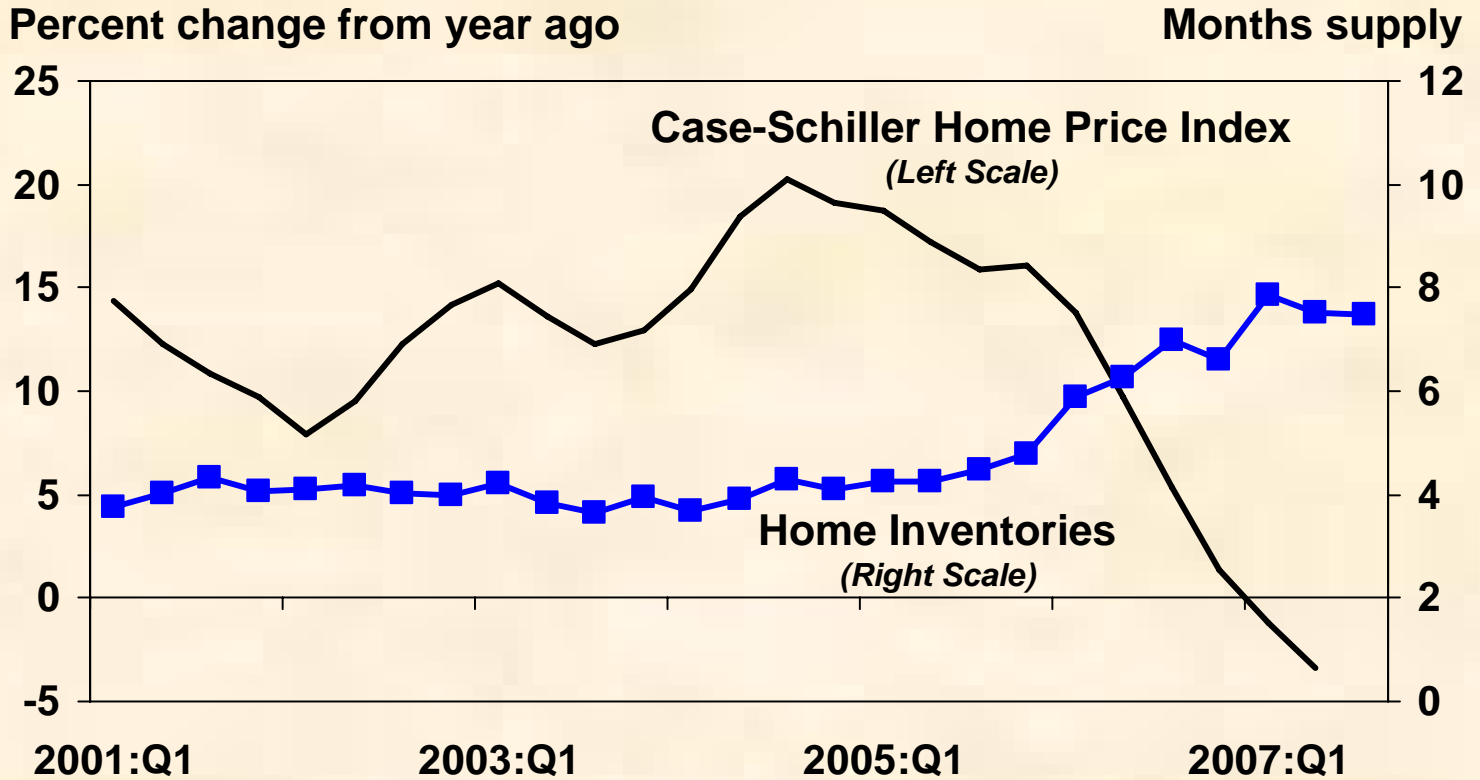
Today's Outline

- **Housing and the financial market crisis**
- **Risks to the Outlook**
 - **Will housing market weakness spread to the overall economy?**
 - **Will inflationary pressures remain contained?**



Home prices have fallen with rising inventories ...

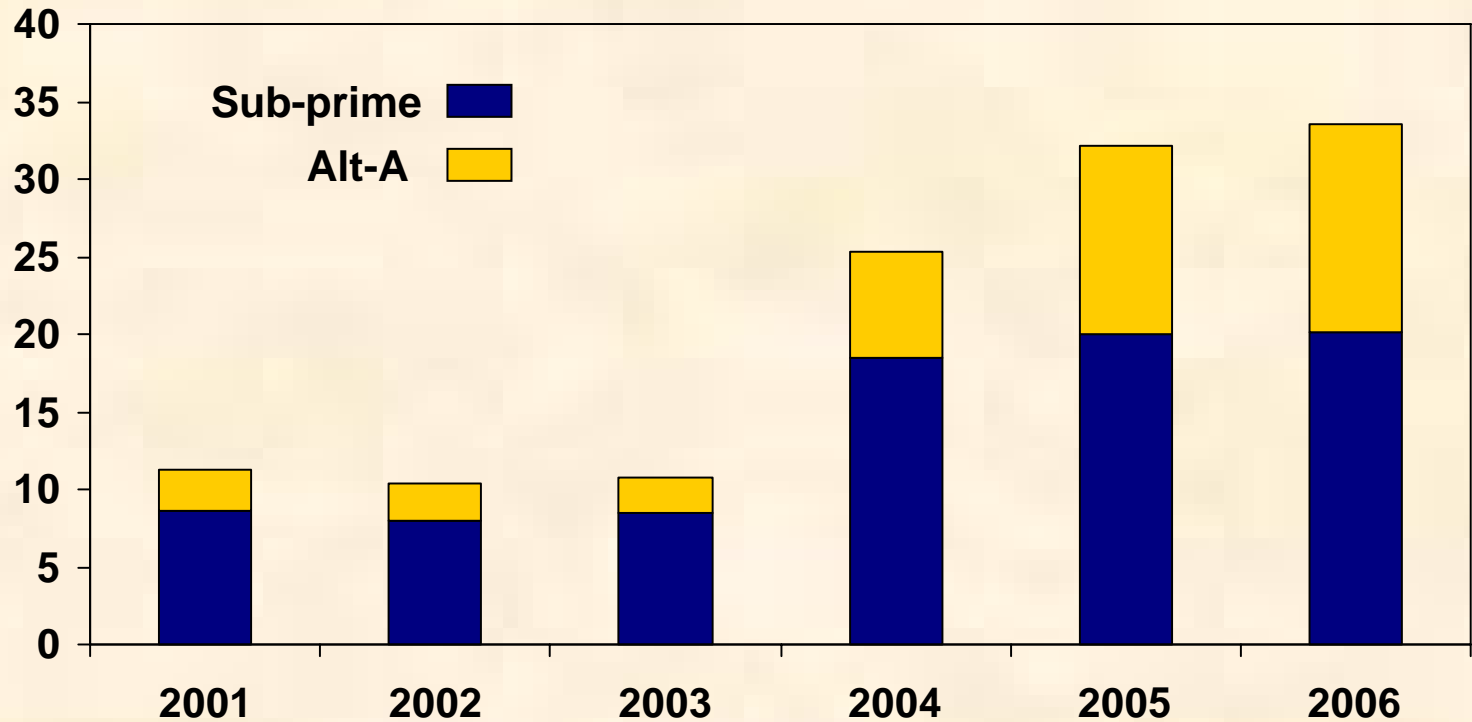
Home Inventories and Prices



... just as adjustable “nonprime” mortgage rates started to be reset.

“Nonprime” Mortgage Originations

Percent

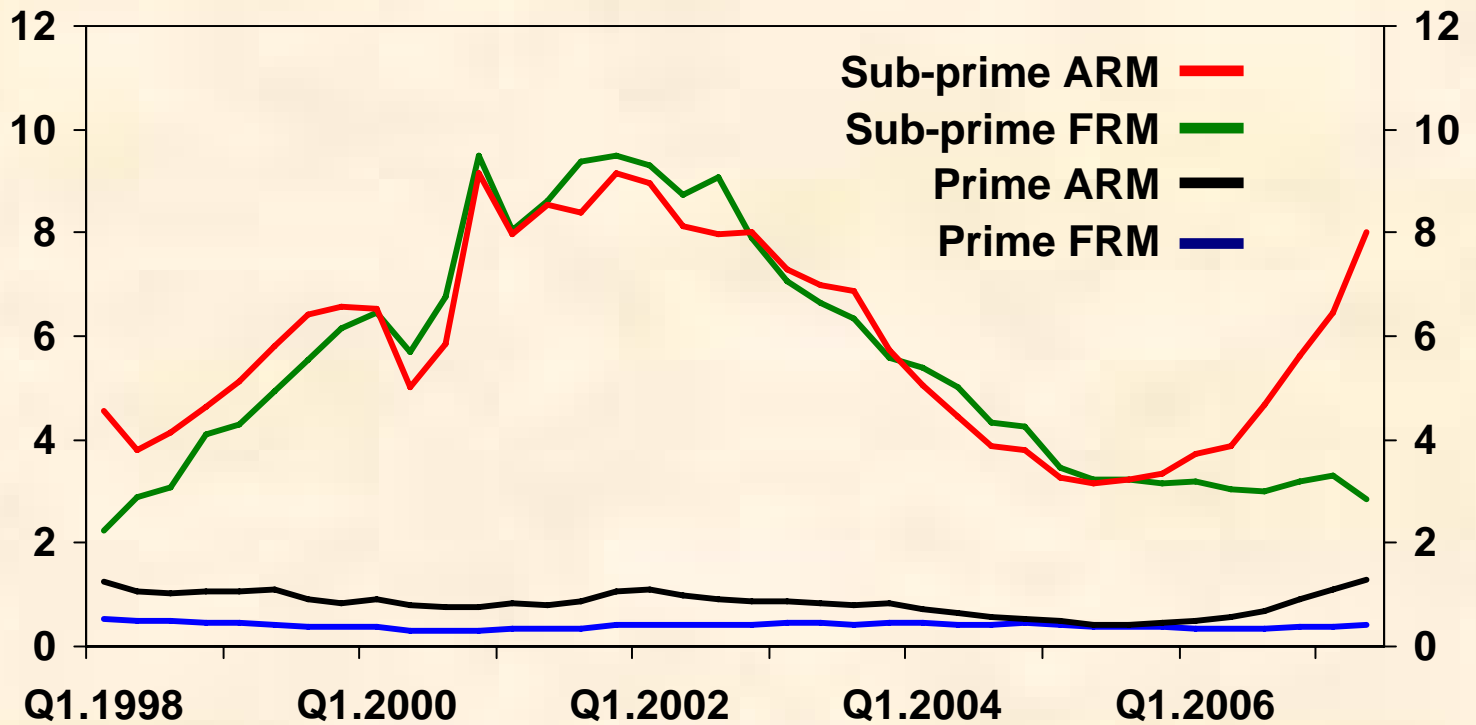


Source: Inside Mortgage Finance

The result is higher foreclosures rates for sub-prime loans.

Foreclosure Rates

Percent of loans serviced

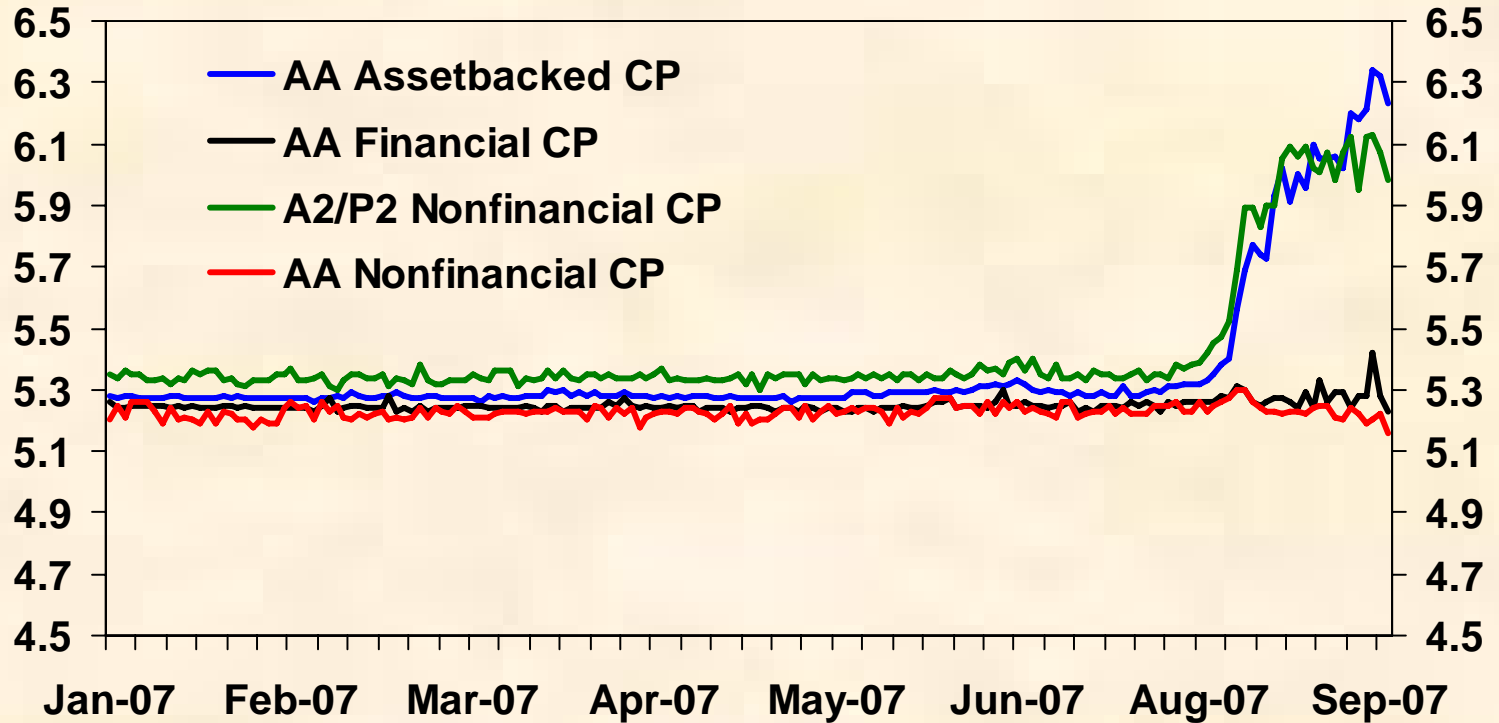


Source: Mortgage Realtors Association

Rates on Asset-backed and Lower-rated Commercial Paper Soared.

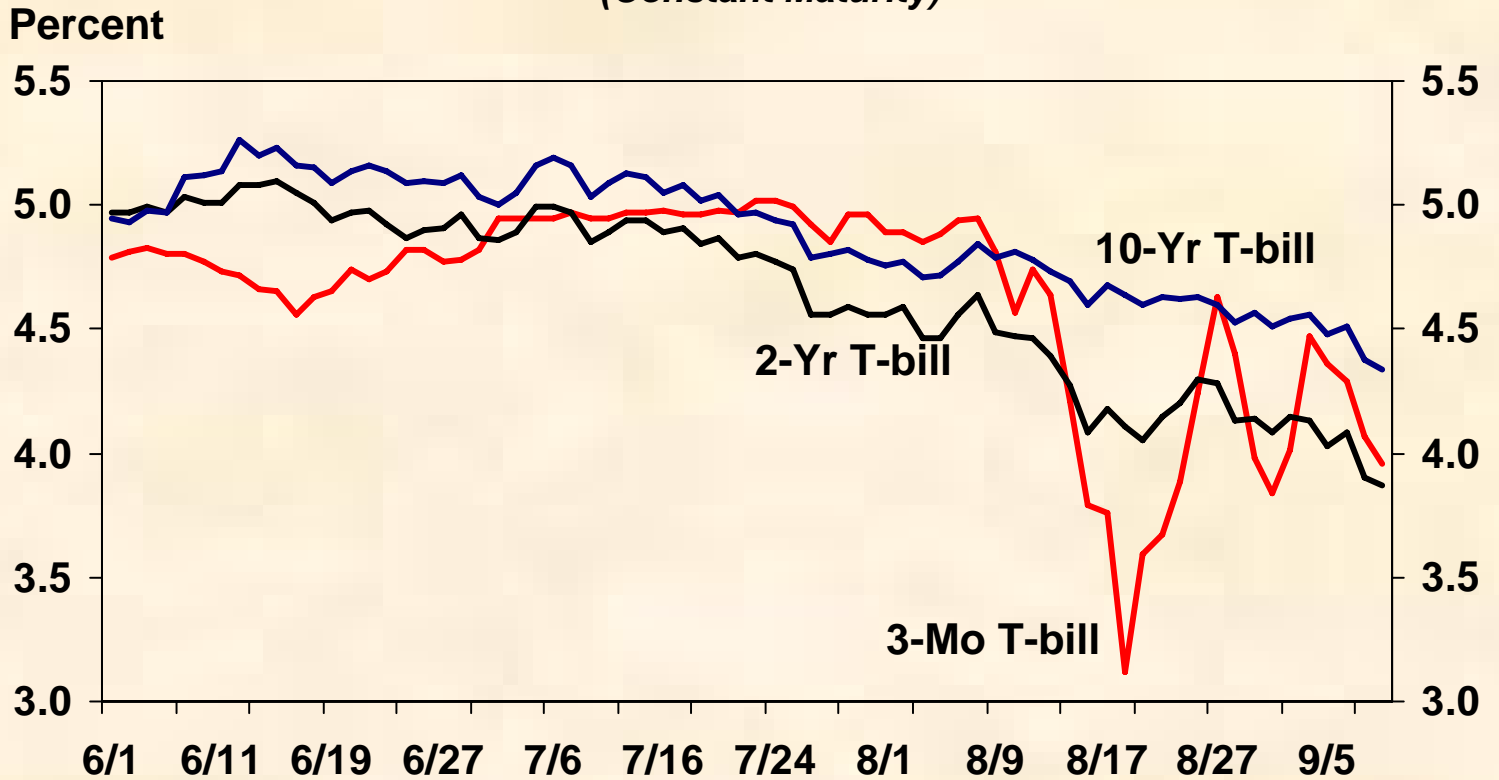
Commercial Paper Rates

Percent



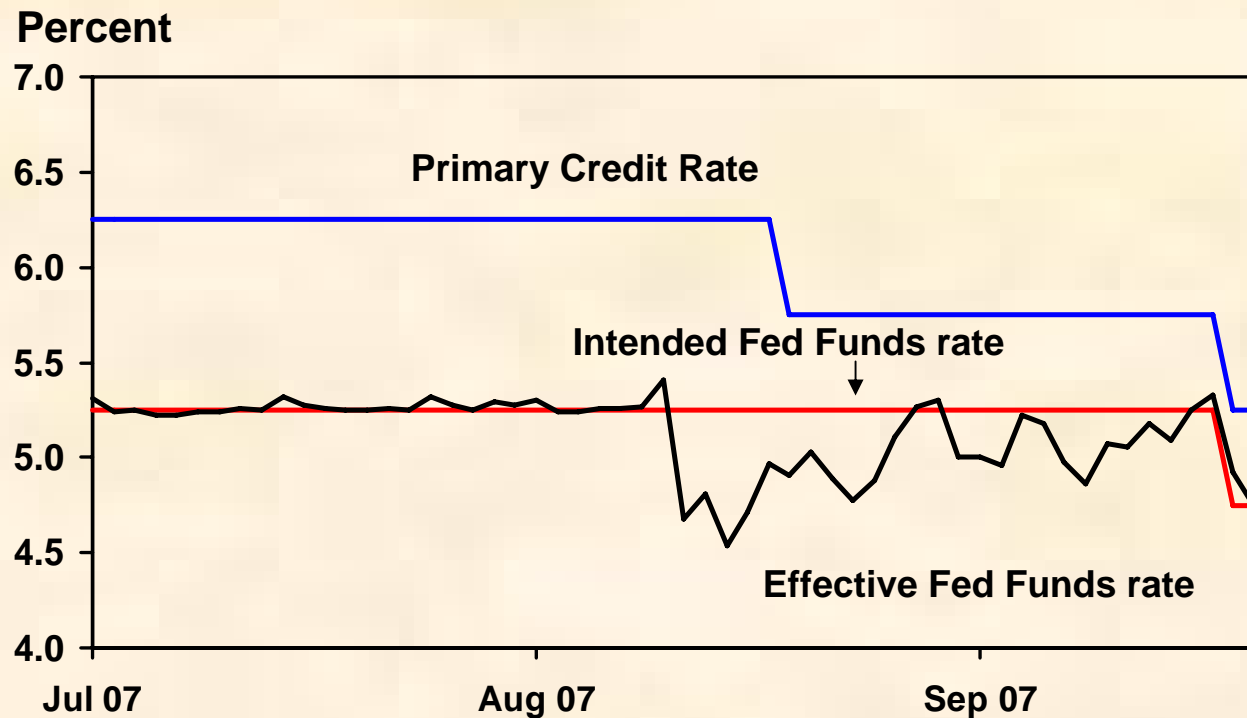
Investors Sought Safety in Treasury Securities.

Treasury Interest Rates (Constant Maturity)



**In response, the Fed and other
Central Banks provided liquidity.**

Interest Rates



Source: Federal Reserve Board of Governors



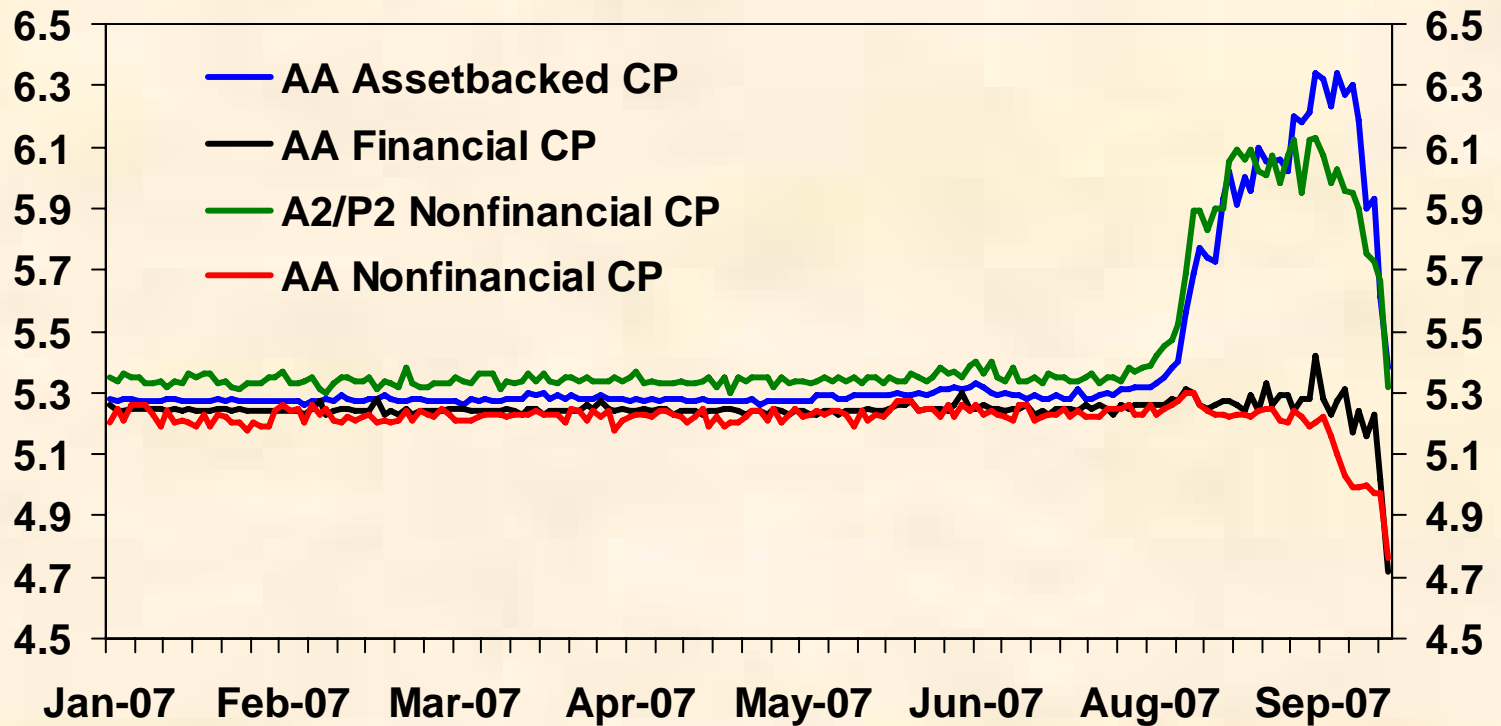
FOMC Statement ***(September 18, 2007)***

- **Economic growth was moderate.**
 - Credit conditions have the potential to intensify the housing correction and to restrain economic growth.
 - Forestall some of the adverse effects on the broader economy.
- **Core inflation ... improved modestly.**
 - Some inflation risks remain.
 - Monitor inflation developments carefully.
- **Developments in financial markets ... have increased the uncertainty surrounding the economic outlook.**

Commercial Paper Rates have dropped after the Fed Funds Rate Cut.

Commercial Paper Rates

Percent of loans serviced





Risks to the Outlook

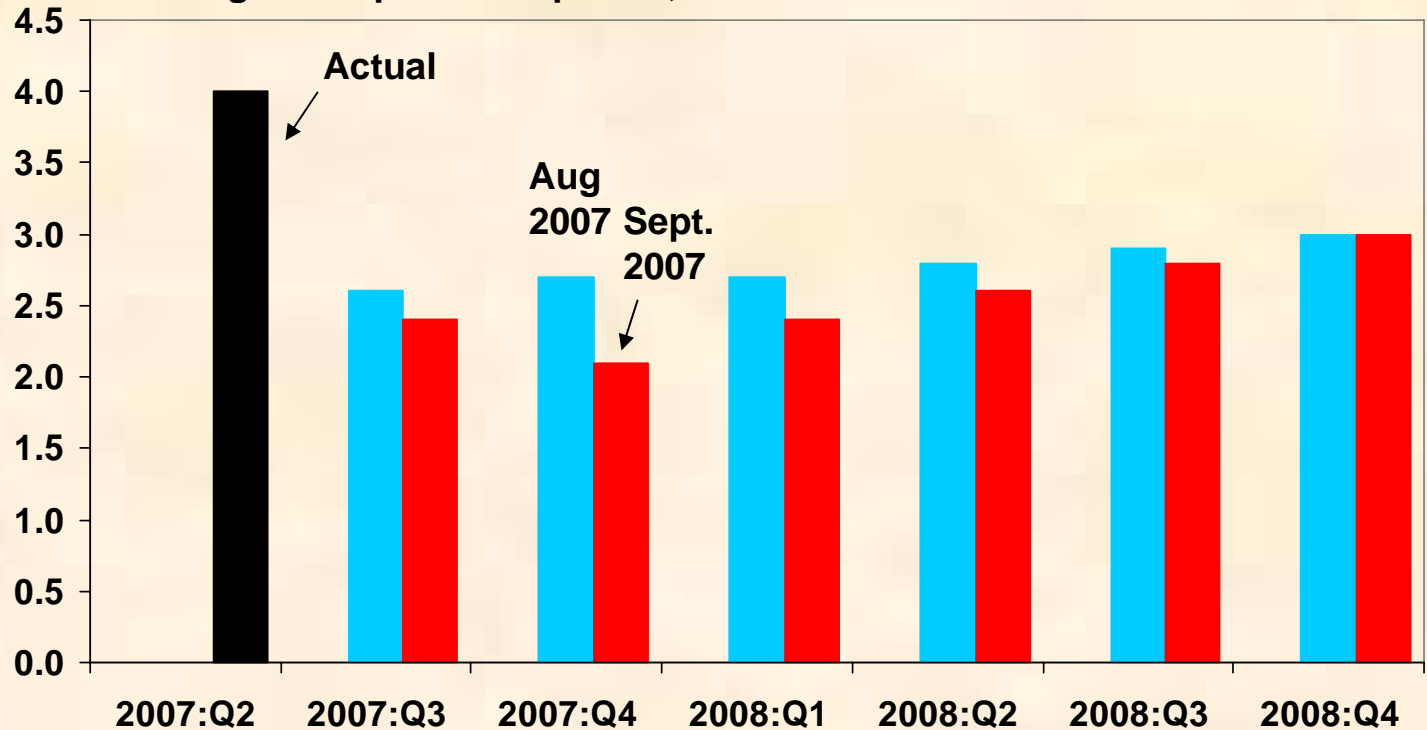
- **Will housing weakness spread?**
 - **Consumer spending**
 - **Business Investment**
 - **Export activity**



Market expectations regarding GDP have eased recently, but still anticipate growth will strengthen in 2008.

U.S. Real GDP Growth- Consensus Forecast

Percent change from previous quarter, annualized



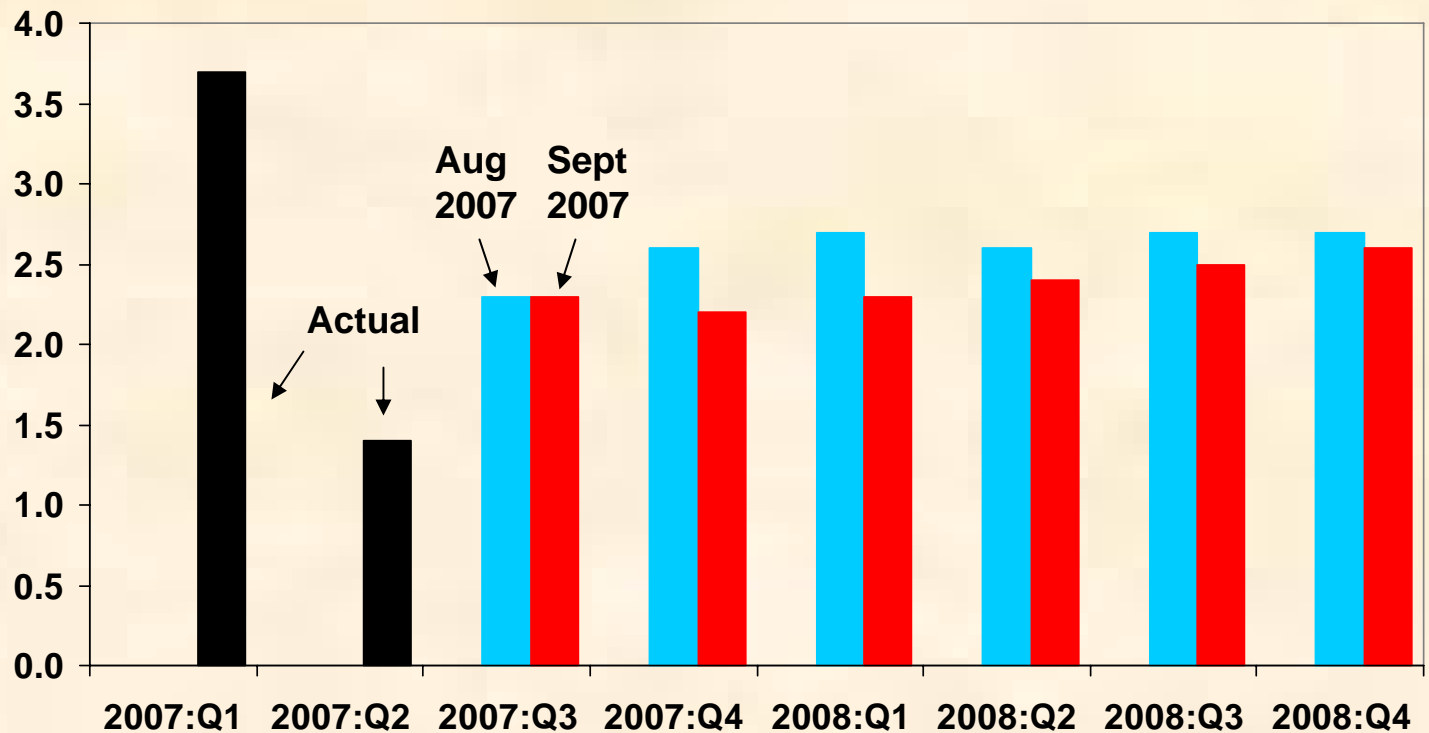
Source: Blue Chip Economic Advisors



Will Consumer Spending Slow?

U.S. Personal Consumption Expenditures

Percent change from previous quarter, annualized

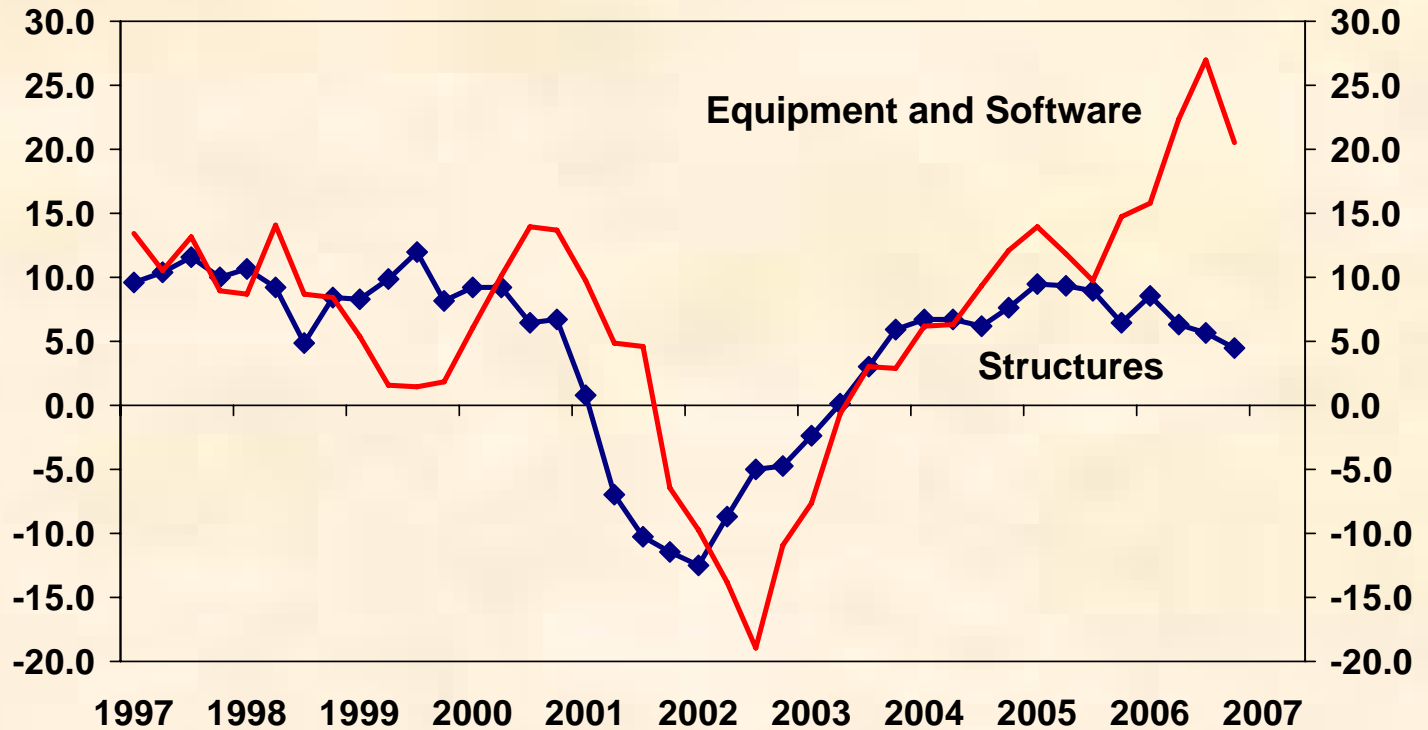


Source: Blue Chip Economic Advisors

Will tighter credit standards lead to softer capital spending?

Nonresidential Fixed Investment

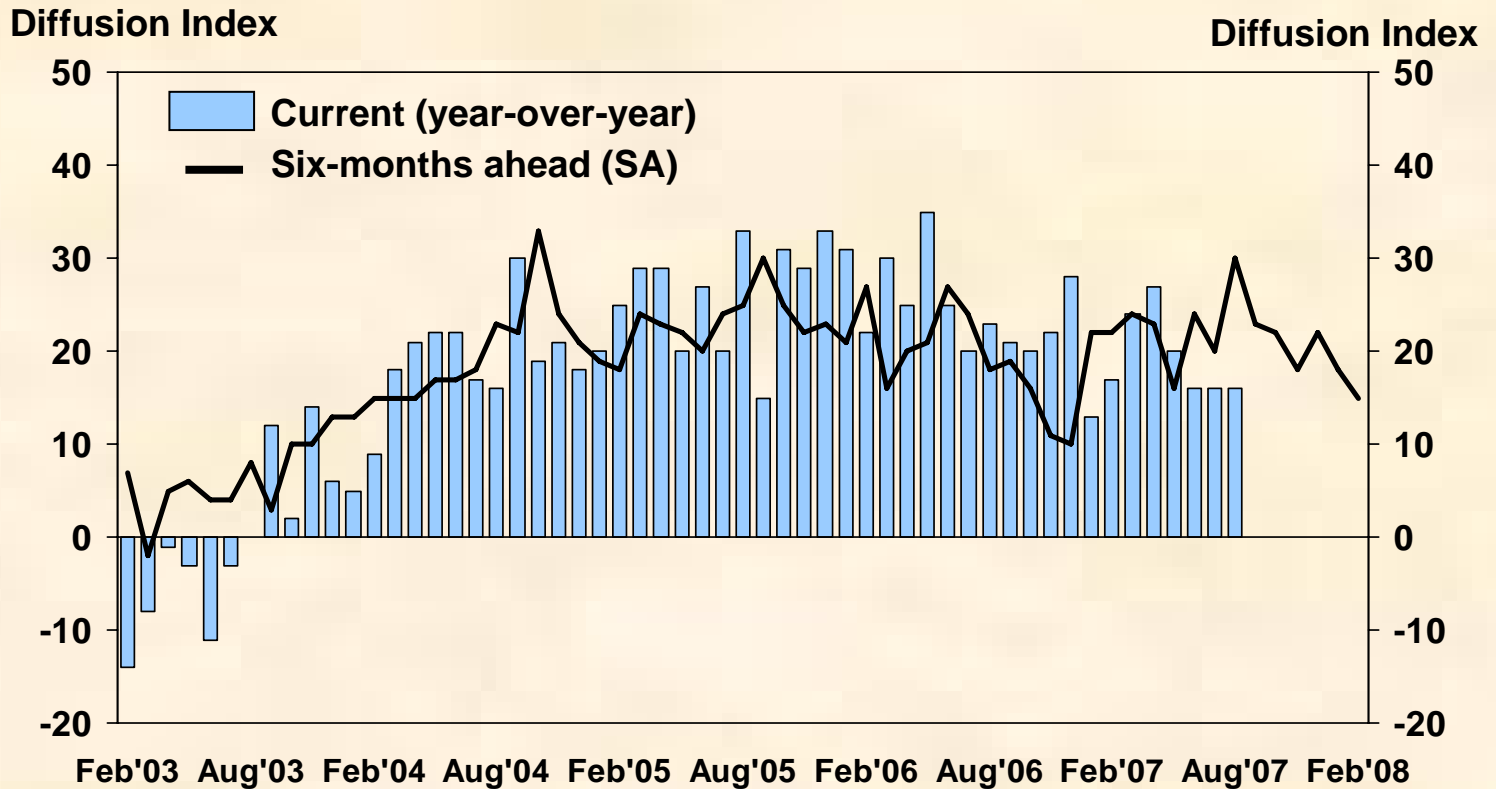
Percent change from year ago



Source: Bureau of Economic Analysis

District manufacturers expect capital spending to slow.

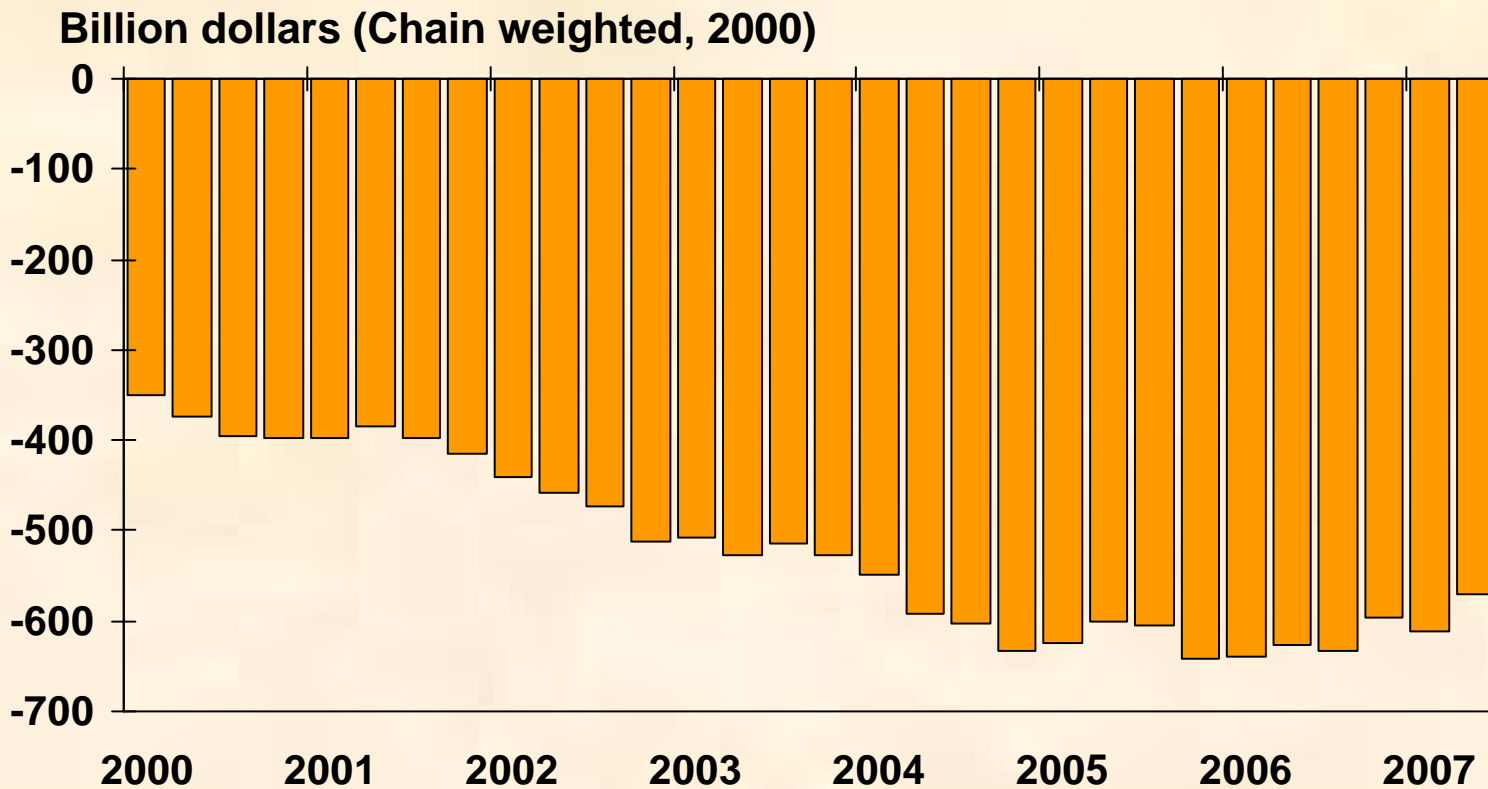
Tenth District Manufacturing Capital Spending Indexes



Source: FRBKC Manufacturing Survey

Will the trade deficit continue to shrink?

U.S. Net Exports



Source: BEA



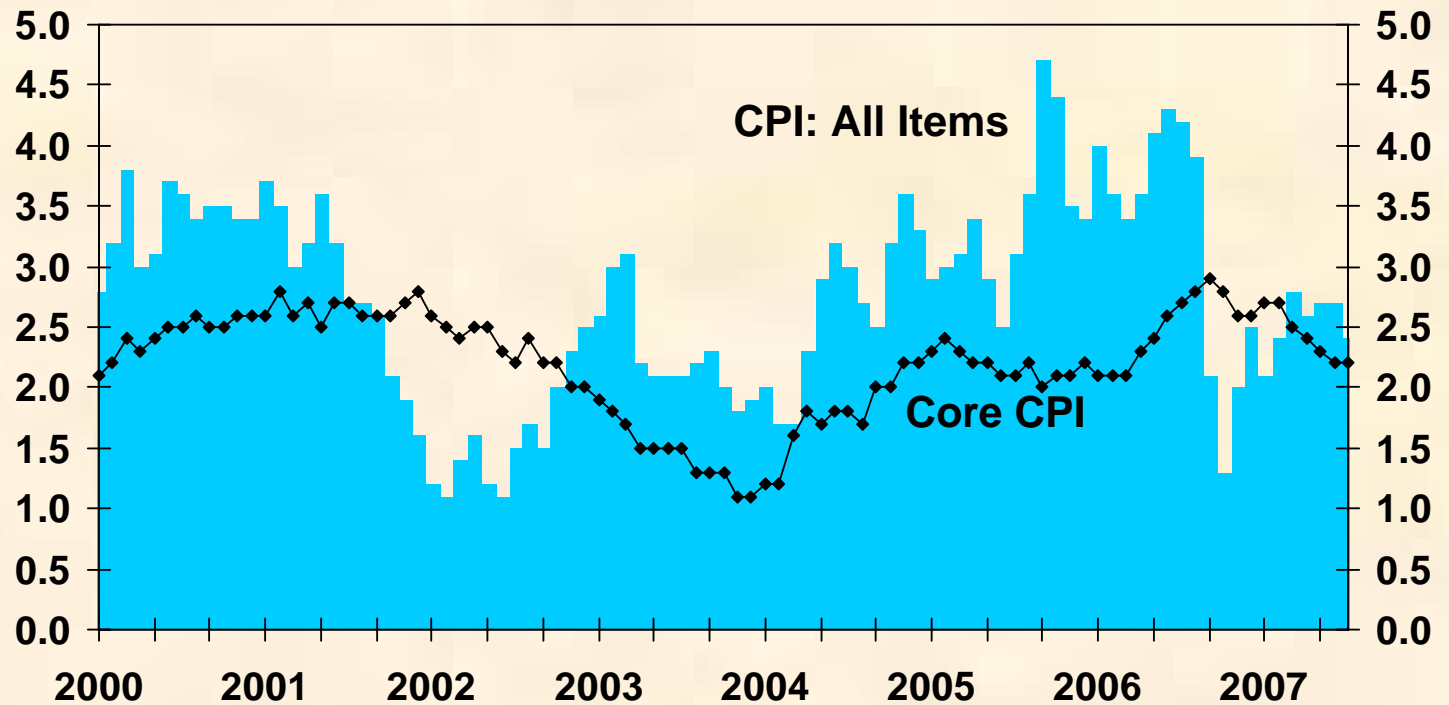
Risks to the Outlook

- 
- **Will housing weakness spread?**
 - **Consumer spending**
 - **Business Investment**
 - **Export activity**
 - **Will inflation continue to ease?**
 - **Commodity Prices**
 - **Capacity Utilization**
 - **Wages**
 - **Import Prices**
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Inflationary pressures have eased, but remain elevated.

Consumer Price Inflation

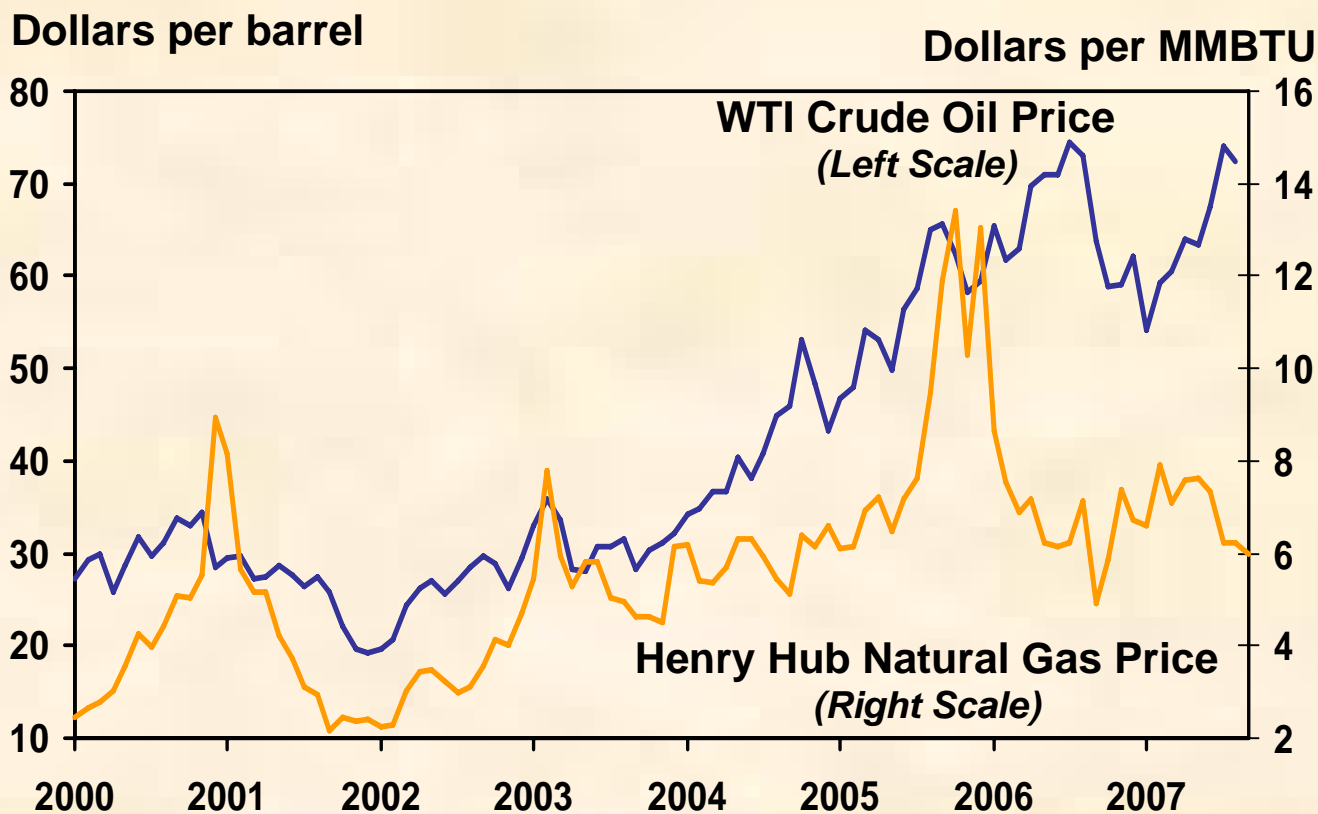
Percent change from a year ago



Source: Bureau of Labor Statistics

What direction will energy prices head?

Crude Oil and Natural Gas Price

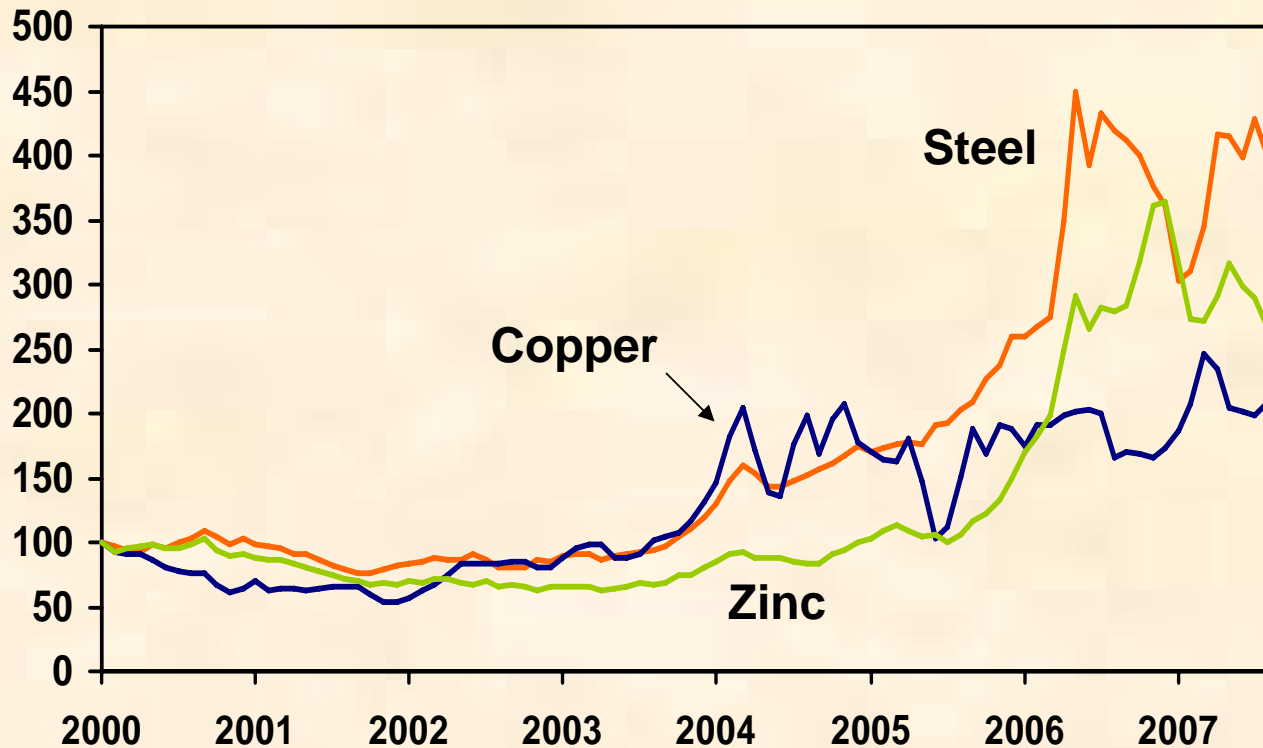


Source: Bloomberg Energy Services

Will commodity prices remain below previous highs?

Materials Prices

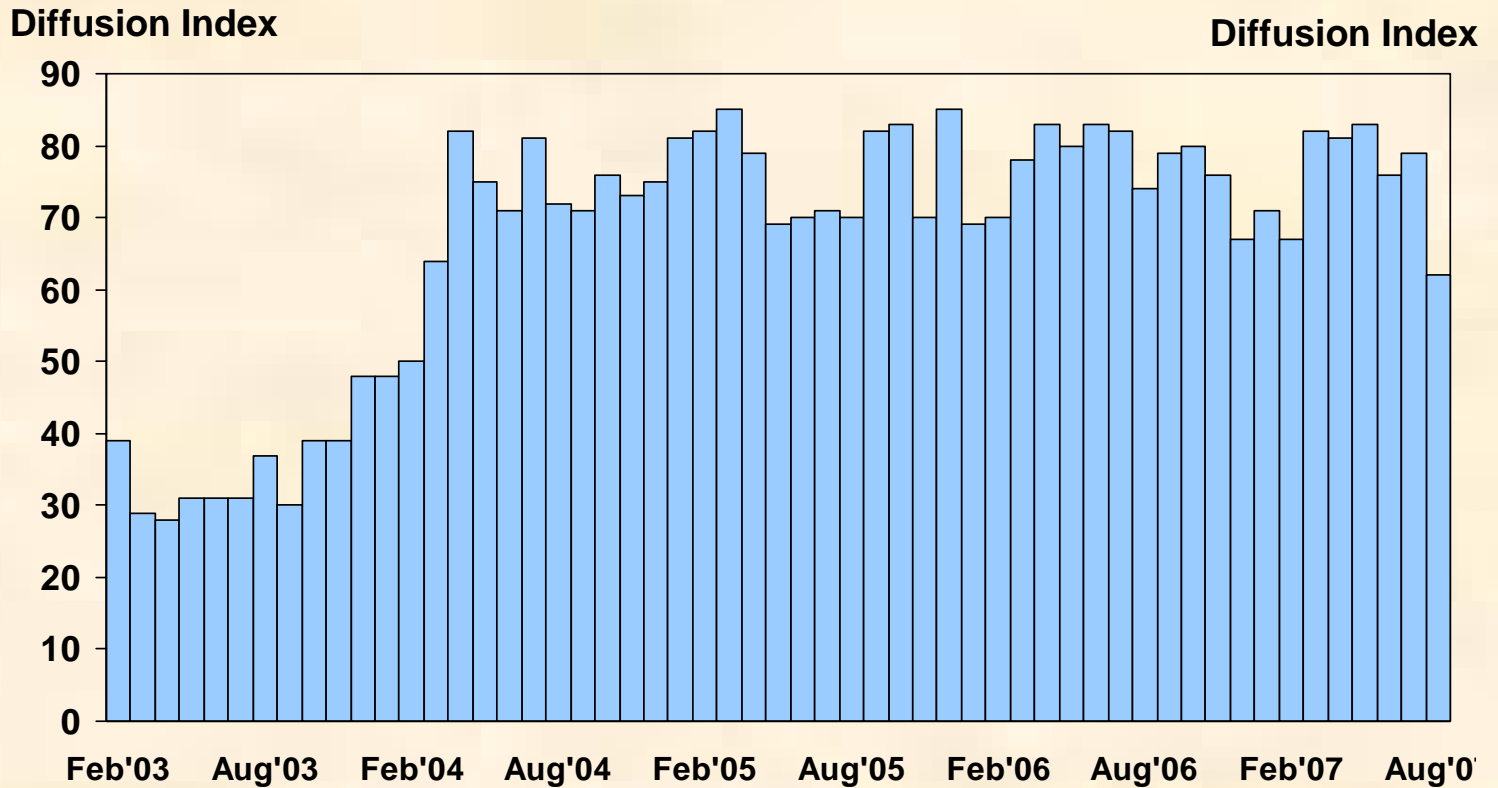
Index Jan 2000=100





In August, input prices declined, but remain elevated.

Tenth District Manufacturing Prices Paid Indexes

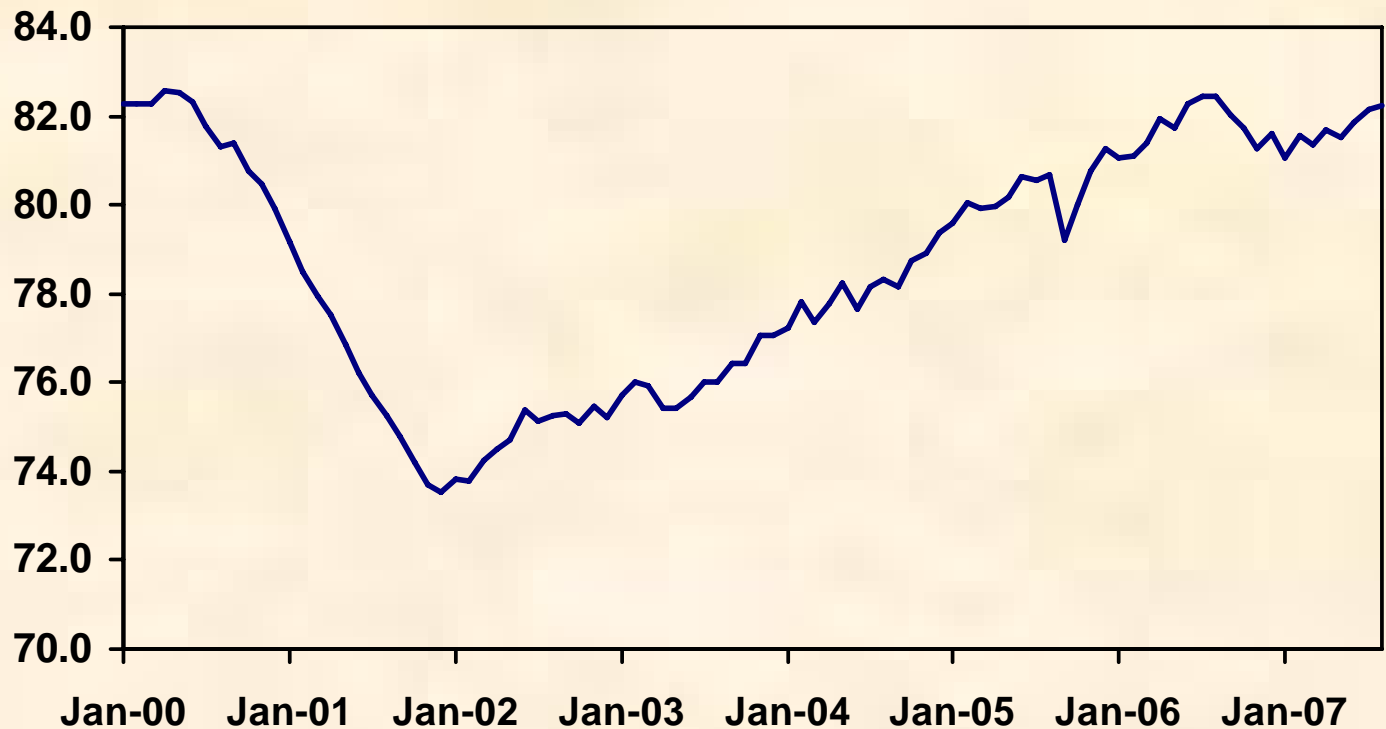


Source: FRBKC Manufacturing Survey

Will capacity constraints limit productivity growth to underpin inflation?

Capacity Utilization

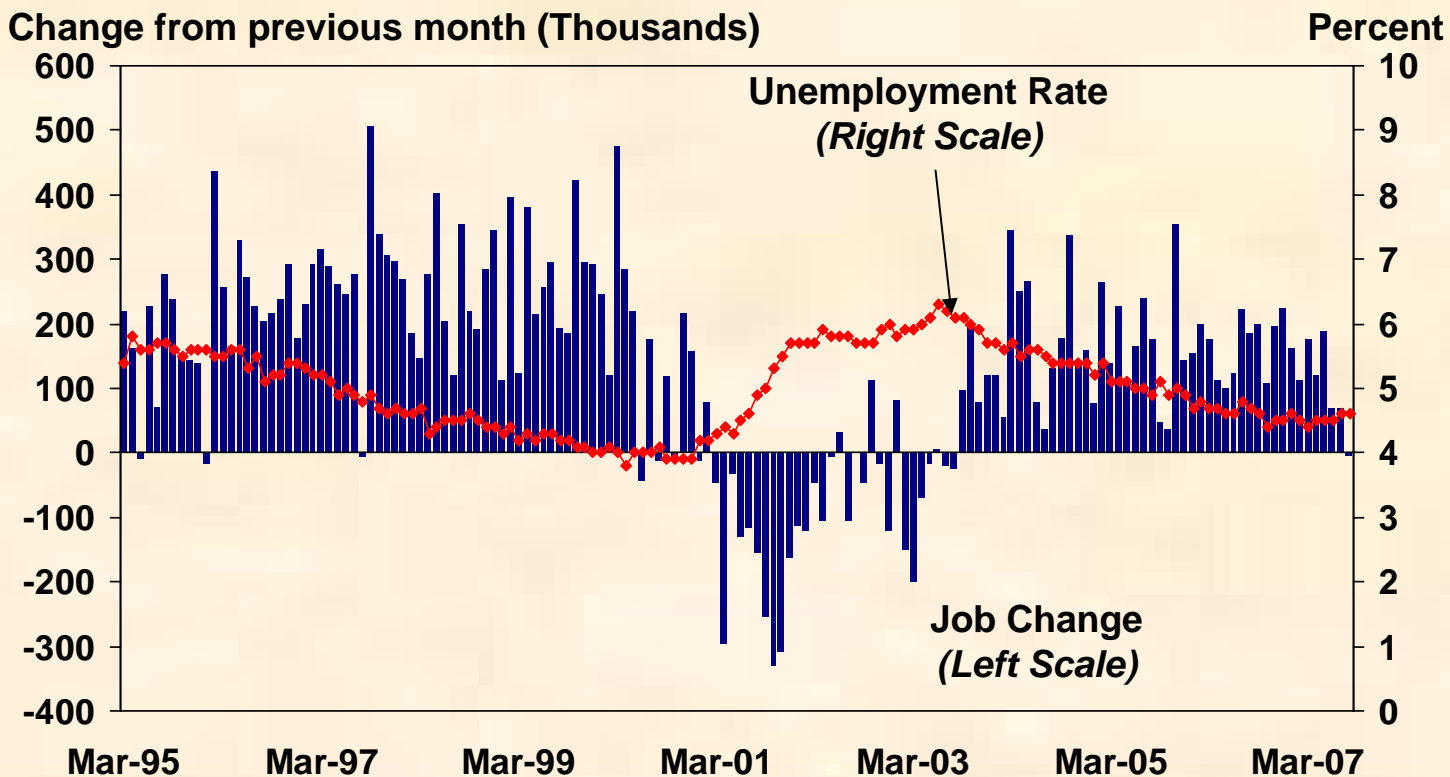
Percent



Source: Federal Reserve Board of Governors

Will slower economic growth ease tight labor markets ...

U.S. Non-farm Job Growth and Unemployment Rate

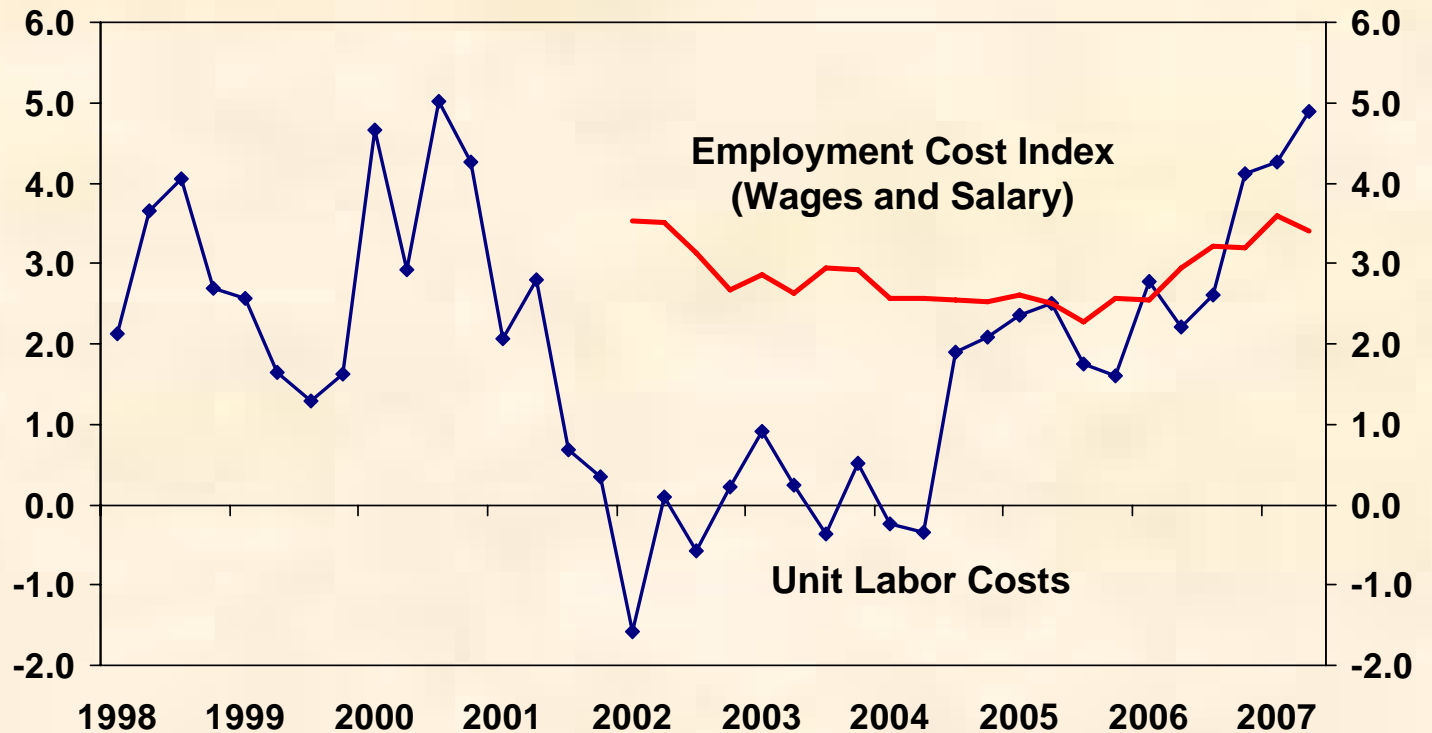


Source: Bureau of Labor Statistics

... and lead to lower wage pressures?

Employment and Unit Labor Costs

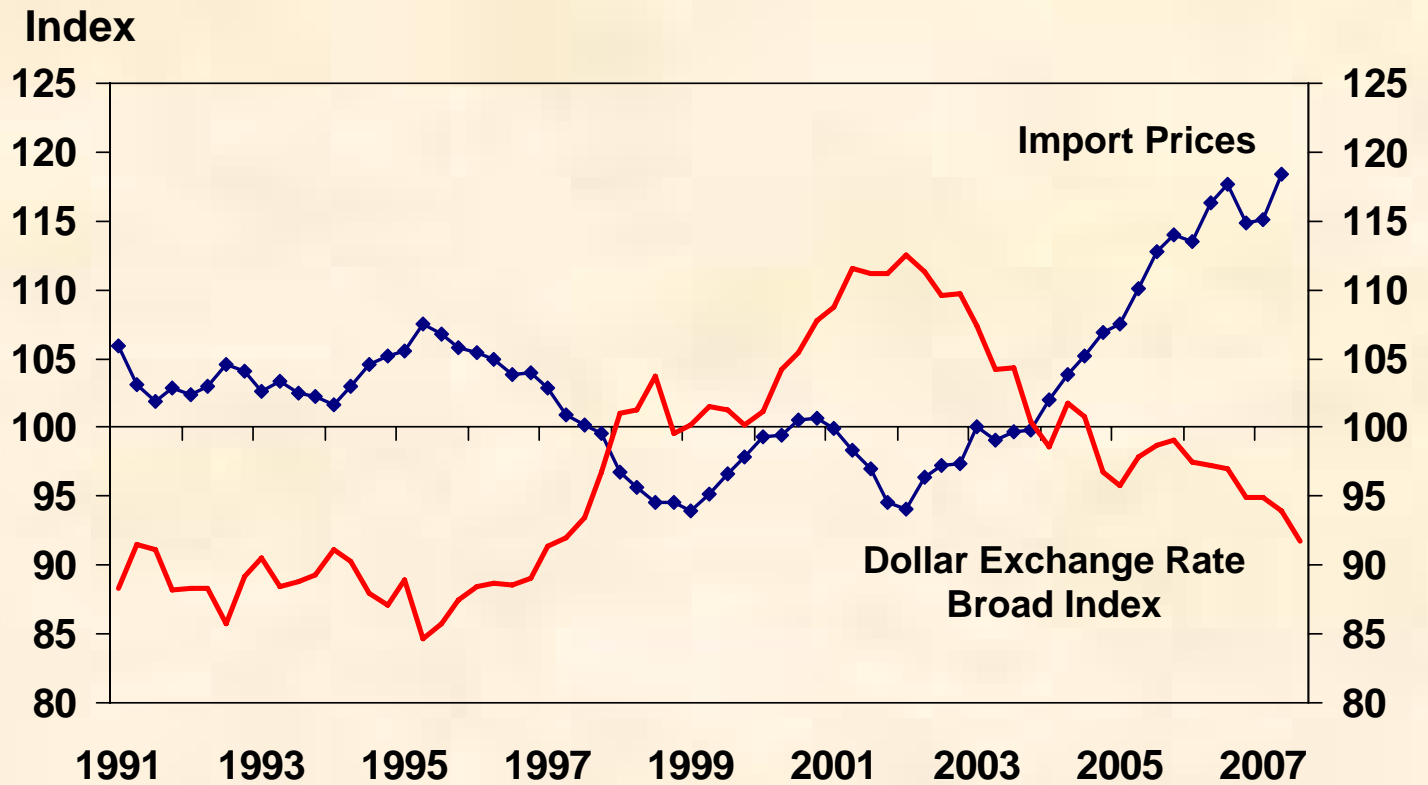
Percent change from year ago



Source: BLS

Will a weaker dollar boost import prices further?

Import Prices and Exchange Rate





Conclusion

- **Economic activity remains solid, outside of housing.**
- **Inflation pressures remain.**
- **Will housing weakness spillover into other segments of the economy?**

The Committee will continue to assess the effects of these and other developments on economic prospects and will act as needed to foster price stability and sustainable economic growth.

FOMC Statement, Sept. 18, 2007