

## **U.S. Economic Report 2H-2009**

(Source: Board of Governors of the Federal Reserve System's Monetary Policy Report to the Congress, February 24, 2010)

### **Summary**

After declining for a year and a half, economic activity in the United States turned up in the second half of 2009, supported by an improvement in financial conditions, stimulus from monetary and fiscal policies, and a recovery in foreign economies. These factors, along with increased business and household confidence, appear likely to boost spending and sustain the economic expansion. However, the pace of the recovery probably will be tempered by households' desire to rebuild wealth, still-tight credit conditions facing some borrowers, and, despite some tentative signs of stabilization, continued weakness in labor markets. With substantial resource slack continuing to suppress cost pressures and with longer-term inflation expectations stable, inflation is likely to be subdued for some time.

### **Gross Domestic Product**

U.S. real gross domestic product (GDP) rose at about a 4 percent pace, on average, over the second half of 2009. Consumer spending--which was boosted by supportive monetary and fiscal policies--posted solid increases, though it remained well below its pre-recession level. Meanwhile, activity in the housing market, which began to pick up last spring, flattened over the second half of 2009. In the business sector, investment in equipment and software posted a sizable gain in the second half of last year, likely reflecting improved conditions in capital markets and brighter sales prospects. In addition, firms reduced the pace of inventory liquidation markedly in the fourth quarter. In contrast, investment in nonresidential structures continued to contract. With the recovery in U.S. and foreign demand, U.S. trade flows rebounded in the second half of 2009 after precipitous declines late in 2008 and early in 2009. Nevertheless, both exports and imports stayed considerably below their earlier peaks.

## **Job Markets**

Despite the pickup in output, employment continued to contract in the second half of 2009, albeit at a markedly slower pace than in the first half. The unemployment rate rose further during the second half, reaching 10 percent by the end of the year--its highest level since the early 1980s--before dropping back in January. Although job losses have slowed, hiring remains weak, and the median duration of unemployment has lengthened significantly.

## **Inflation**

Headline consumer price inflation picked up in 2009 as energy prices rose sharply: Over the 12 months ending in December, prices for personal consumption expenditures (PCE) increased about 2 percent, up from 1/2 percent in 2008. In contrast, price increases for consumer expenditures other than food and energy items--so-called core PCE--slowed noticeably last year. After rising at an annual rate of about 1-3/4 percent in 2008 and the first half of 2009, core PCE prices increased at an annual rate of just over 1 percent in the second half of the year.

## **Financial Markets**

The recovery in financial markets that began last spring continued through the second half of the year and into 2010. Broad equity price indexes increased further, on balance, and risk spreads on corporate bonds narrowed considerably. Conditions in short-term funding markets returned to near pre-crisis levels; liquidity and pricing in bank funding markets continued to normalize, while risk spreads in the commercial paper market were stable at the low end of the range observed since the fall of 2007. The functioning of financial markets more generally improved further.