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**Daily Economic Comment**

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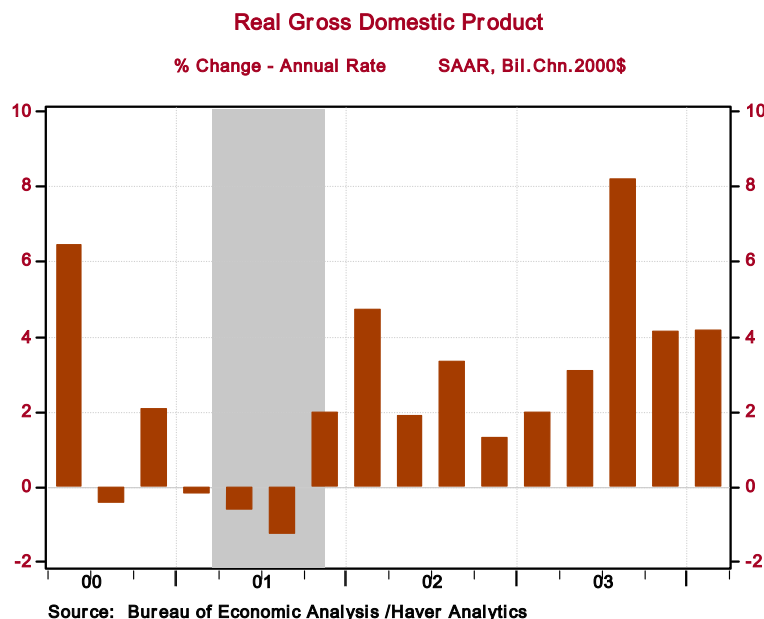
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### Q1 Real GDP Growth Is Strong, But Decelerating Trends Should Be Noted

Real GDP grew at an annual rate of 4.2% in the first quarter, about one percentage point less than expected. On a year-to-year basis, real GDP grew 4.9% in the first quarter, the largest increase since the fourth quarter of 1984.



In the first quarter, consumer spending rose 3.8% vs. a 3.2% increase in the previous quarter. Non-durable consumer goods (+6.4%) and services (+4.7%) accounted for overall increase in consumer goods outlays. The gains of these two components more than offset the 4.7% drop in purchases of durable goods, reflecting largely a drop in sales of cars and light trucks.

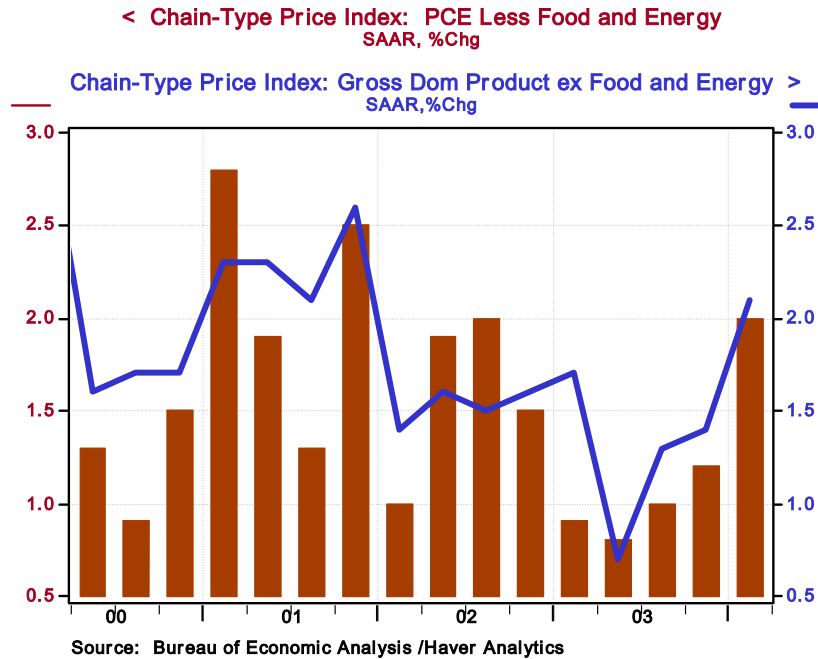
Of the major components of business sector spending, non-residential structures dropped at an annual rate of 6.5% in the first quarter compared, with a 1.4% decline in the previous quarter. This component of GDP has declined in all but two quarters since the first quarter of 2000. Equipment and software spending increased 11.5% in the fourth quarter, representing a deceleration after 17.6% and 14.9% gains in the third and fourth quarters of 2003, respectively. The upward trend of corporate profits supports forecasts of continued growth in capital spending for the rest of 2004. The 2.1% increase in residential investment expenditures in the first quarter is small advance after a

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robust 21.9% jump in the third quarter and a 7.9% increase in the fourth quarter. Growth in residential construction will likely pick up in the second quarter as builders and buyers try to “get in” before interest rates rise more. The contribution to GDP growth from inventory accumulation in the first quarter was noticeably smaller than the fourth quarter.

The trade deficit narrowed to \$514.6 billion vs. \$515.2 billion in the first quarter. A revival in worldwide economic growth should spur growth in exports during the rest of 2004.

The price indexes show a significant increase in inflation. The GDP price index rose 2.5% in the first quarter and the core GDP price deflator advanced 2.1%. The core personal consumption deflator increased 2.0% in the first quarter vs. a 1.2% gain in the fourth quarter.



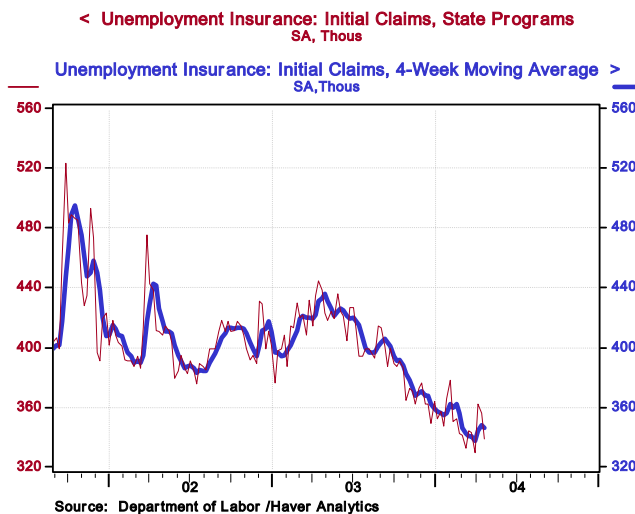
A growing economy with rising prices is an expected sequence of events. However, a growing economy, rising prices, and an unclear trend of employment growth is an atypical combination that has kept the FOMC on hold. With growing evidence of strong growth, the Fed is expected to tap on the monetary policy brakes once convincing evidence of an improving labor market is available. This could be evident as early as the June 29-30 FOMC meeting. The May 4 FOMC meeting should close with the Fed changing its rhetoric to reflect no lingering concerns about disinflation. In other words, the FOMC will communicate to the financial markets that it sees the risks evenly balanced on inflation and economic growth.

## REAL GROSS DOMESTIC PRODUCT 2004:Q1 ADVANCE ESTIMATE

	Levels (Billions of chained 2000 dollars)			Percent Change (SAAR)		
	03:3 Final	03:4 Final	04:1 Advance	From 03:2 to 03:3	From 03:3 to 03:4	From 03:4 to 04:1
GDP	10493.1	10600.1	10708.6	8.2	4.1	4.2
CONSUMPTION	7426.6	7486.2	7555.6	6.9	3.2	3.8
DURABLE GOODS	1069.1	1070.8	1058.1	28.0	0.7	-4.7
NONDURABLE GOODS	2134.3	2162.4	2196.5	7.3	5.4	6.4
SERVICES	4237.2	4266.4	4311.1	2.8	2.8	4.3
INVESTMENT	1656.1	1714.6	1744.7	14.8	14.9	7.2
FIXED INVESTMENT	1661.0	1700.6	1723.2	15.8	9.9	5.4
NONRESIDENTIAL	1139.5	1169.4	1189.8	12.8	10.9	7.2
STRUCTURES	237.7	236.9	232.9	-1.8	-1.4	-6.5
EQUIPMENT & SOFTWARE	907.7	939.7	965.5	17.6	14.9	11.5
RESIDENTIAL	516.7	526.6	529.3	21.9	7.9	2.1
CHG. BUS. INVENT.	-9.1	9.0	15.3			
NET EXPORTS	-505.2	-515.2	-514.6			
EXPORTS	1033.7	1083.1	1091.6	9.9	20.5	3.2
IMPORTS	1538.9	1598.3	1606.2	0.8	16.4	2.0
GOVERNMENT (Cons. & Invest.)	1911.1	1910.7	1920.3	1.8	-0.1	2.0
FEDERAL	714.3	715.5	732.9	1.2	0.7	10.1
DEFENSE	471.2	474.7	491.7	-1.3	3.0	15.1
OTHER	243.1	240.8	241.3	6.5	-3.7	0.7
STATE AND LOCAL	1197.4	1195.9	1188.1	2.1	-0.5	-2.6
DISP. PERS. INC.	7872.3	7893.0	7977.1	6.3	0.5	4.3
FINAL SALES	10497.7	10586.4	10687.8	8.3	3.4	3.9
FINAL SALES TO DOM. PURCHASERS	11000.1	11097.8	11198.9	7.2	3.6	3.7
PRICE DEFLATORS:						
GDP CHAIN TYPE	105.9	106.3	106.9	1.6	1.5	2.5
GDP EX. FOOD & ENERGY				1.3	1.4	2.1
PCE CHAIN TYPE	105.5	105.8	106.6	1.8	1.0	3.2
PCE EX. FOOD & ENERGY	112.4	105.3		1.7	1.2	2.0

### Jobless Claims Continue To Signal Improving Conditions

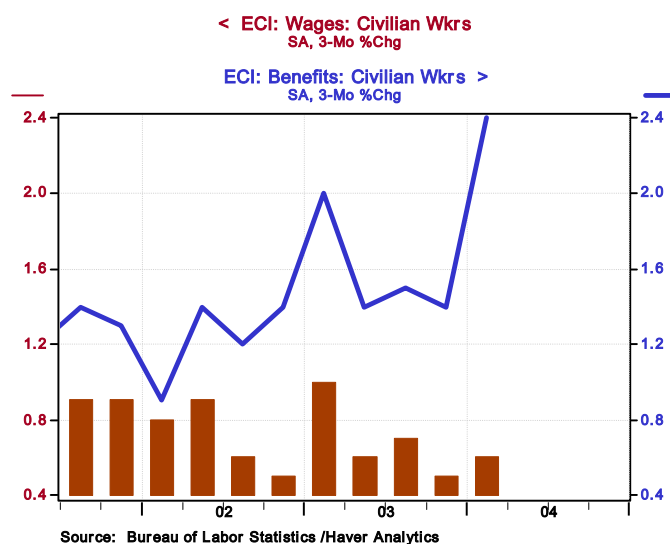
Initial jobless claims dropped 18,000 to 338,000 during the week ended April 24. Continuing claims increased 3,000 to 3.013 million during the week ended April 17 and the insured unemployment rate held at 2.4% for the eighth straight week. On a year-to-year basis, initial jobless claims dropped 22.0%, reinforcing the perception of improving labor market conditions.



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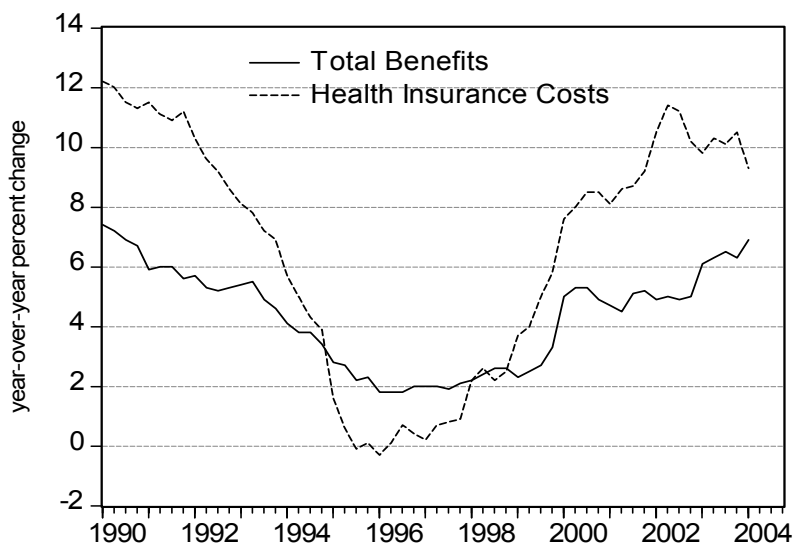
## Employment Cost Index Reflects Sharp Gains in Benefit Costs

The Employment Cost Index increased 1.1% in the first quarter vs. a 0.8% advance in the fourth quarter. Both the major components of this index – wages and salaries and benefits rose in the first quarter to lift the overall index. However, the benefit costs component showed a sharp increase of 2.4% in the first quarter compared with a 1.4% gain in the fourth quarter.



Rising health insurance costs is the major reason for the acceleration of the benefit costs index. The good news is that although the year-to-year increase in health insurance costs was 9.3% in the first quarter, it is a slower pace of growth compared with a 10.3% average gain in the last three quarters of 2003 (see chart below).

Employment Cost Index - Benefits  
Total Benefits vs. Health Insurance



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