FEDERAL RESERVE BANK OF BOSTON™

The President's Report *to the* Board *of* Directors

December 7, 2012

CURRENT ECONOMIC DEVELOPMENTS - December 7, 2012

Data released since your last Directors' meeting has shown that growth in the third quarter was stronger than previously estimated, but that growth is likely to be slower in the near term. The auto and housing markets continue to gain strength. However, weakness in the manufacturing sector remains, due in part to the effects of Hurricane Sandy, and consumer sentiment has declined. Threats posed by the fiscal cliff here and the ongoing financial crisis in Europe provide considerable downside risks. Uncertainty is likely to surround the economic outlook until these issues are addressed.

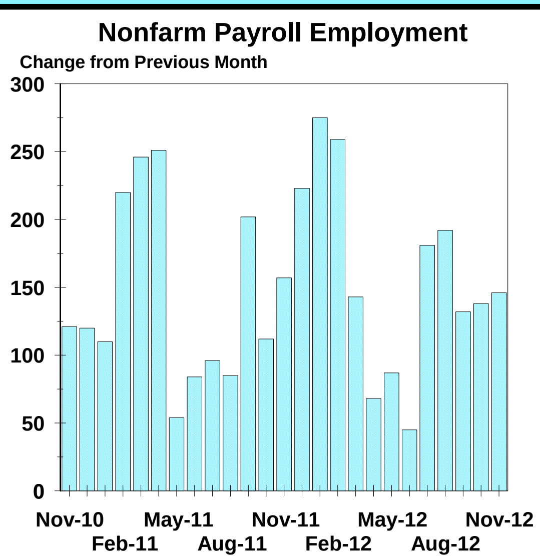
In November, nonfarm payrolls posted a higher-than-expected increase, and the unemployment rate fell two-tenths of a percentage point to a nearly four-year low. However, job gains from the previous two months were revised lower. Initial claims for unemployment insurance rose in November to their highest level in over a year. Consumer attitudes improved in November to their highest levels since the recession began, but an initial reading of consumer sentiment shows expectations plunging in early December. Real personal incomes and consumption declined in October.

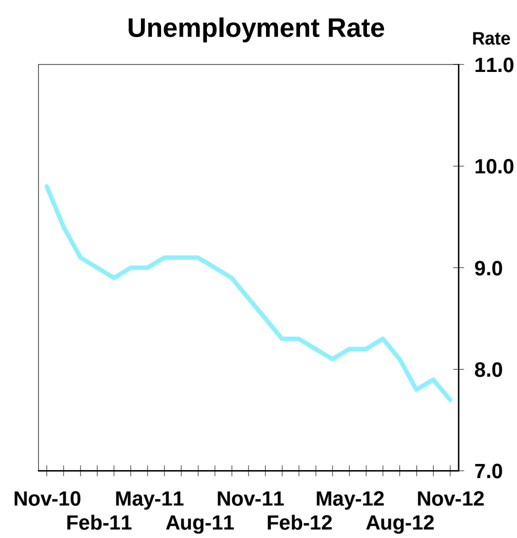
The real estate market continued to show signs of recovery, despite mixed data in October. New home sales eased slightly in October, but remain above their 12-month average, while existing home sales increased. New construction data also showed some improvement, as housing starts increased in October, while permits decreased but remain well above the levels seen since the end of the recession.

In the manufacturing sector, the ISM index fell below 50 in November for the fourth time in the past six months. Industrial production dropped in October and capacity utilization decreased to its lowest level so far this year. Orders for both durable goods and nondefense capital goods, excluding aircraft, increased in October, but the latter was well below its year-ago level.

Total price indices for both consumers and wholesalers rose slightly in October, but remain in line with recent trends, as the core indices held steady for consumers and fell slightly for wholesalers. Oil prices fell in November, while unit labor costs fell in the third quarter, following a downwardly revised second quarter estimate.

In November, nonfarm payrolls added 146,000 jobs, but payroll gains for the previous two months were revised lower by a total of 49,000 jobs. Earlier estimates saw these payrolls up by 171,000 and 148,000 jobs in October and September, respectively, while updated data show increases of 138,000 and 132,000. The unemployment rate fell two-tenths of a percentage point to 7.7% in November, its lowest level since December 2008, but the drop was mainly due to a decrease in the size of the labor force.

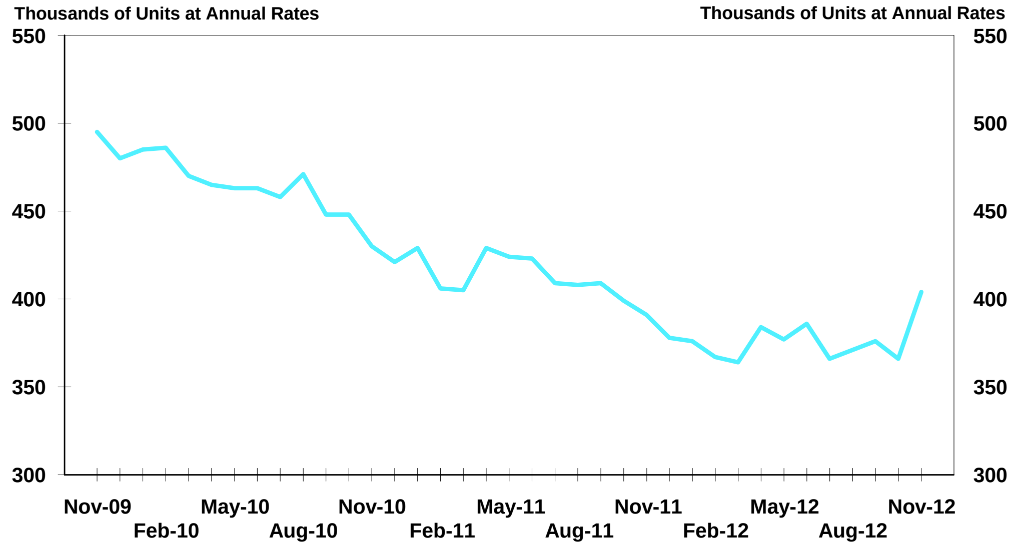




Source: Bureau of Labor Statistics / Haver Analytics.

Initial claims for unemployment insurance jumped up in November, rising above 400,000 for the first time in over one year, due to the effects of Hurricane Sandy. However, claims have fallen in the last three weeks of the month, posting 370,000 in the week ended December 1.

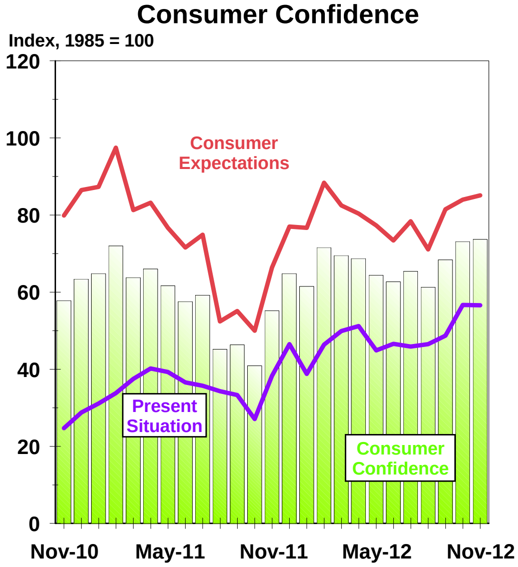
Initial Claims



Source: Department of Labor, Employment and Training Administration / Haver Analytics.

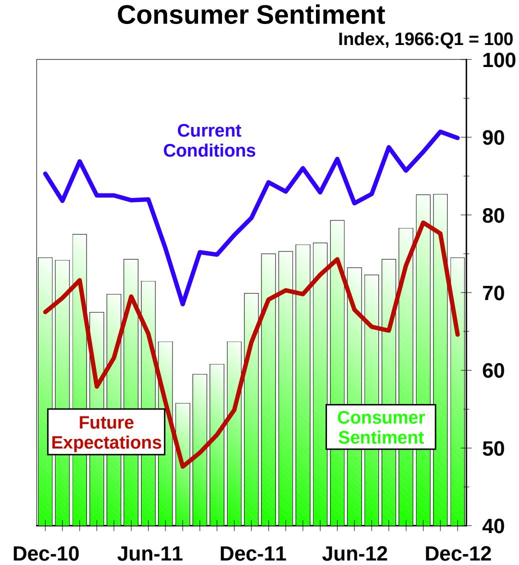
Consumer attitudes improved in November, as both the confidence and sentiment indexes increased to their highest levels since the beginning of the recession. However, in early December, the sentiment index dropped well below expectations, primarily due to uncertainty over fiscal policy, as the expectations index plunged to its lowest level in a year. The uptick in confidence in November was due in part to improvement in expectations for the state of the job market.

Consumer Confidence



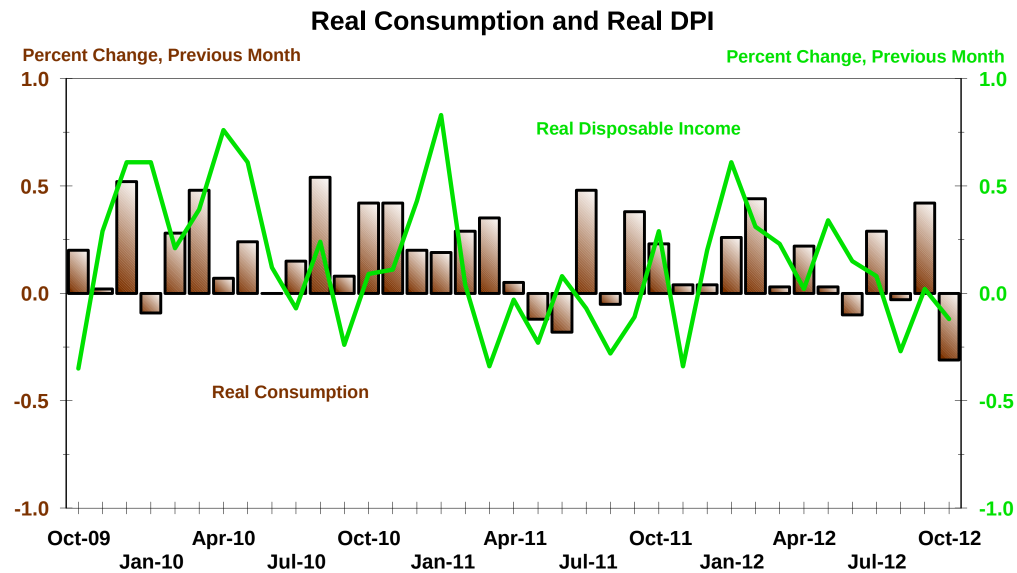
Source: The Conference Board / Haver Analytics.

Consumer Sentiment



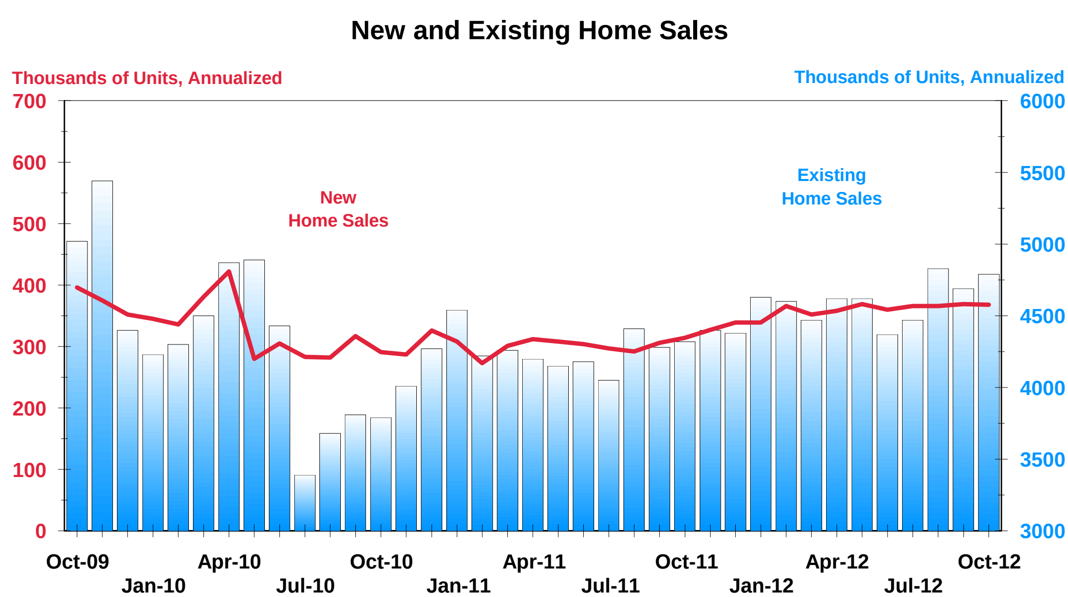
Source: The University of Michigan / Haver Analytics.

Consumption fell in October, aided by a decrease in disposable income, and offset most of the gain from the prior month. The weakness in consumption and disposable income growth is likely due in part to the effects of Hurricane Sandy at the end of October.



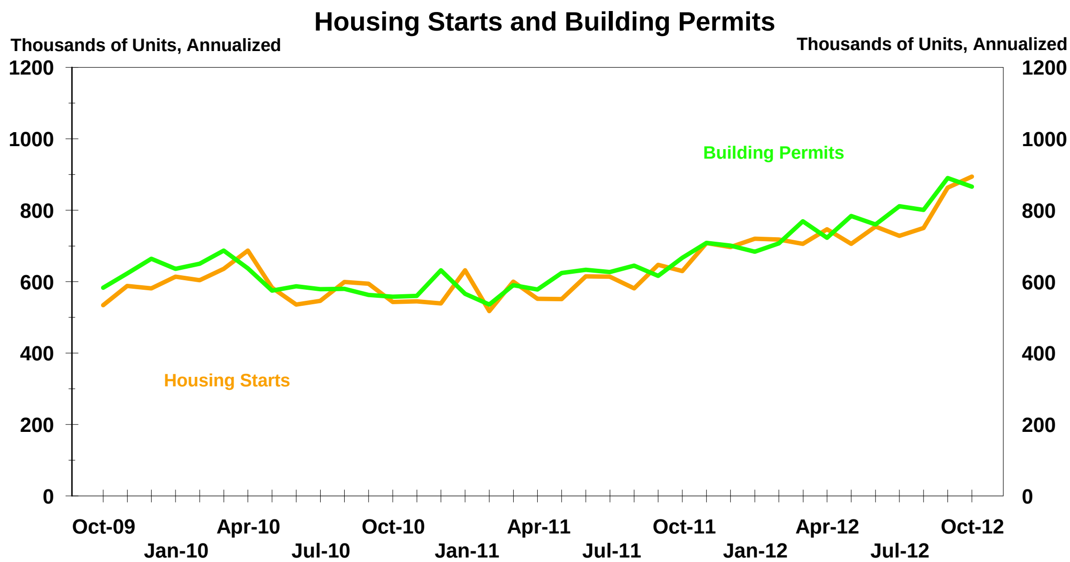
Source: Bureau of Economic Analysis / Haver Analytics.

Housing market data was mixed in October, as new home sales fell slightly, while existing home sales increased. Over the past year, however, both series have generally trended upward as the housing market has undergone a modest recovery.



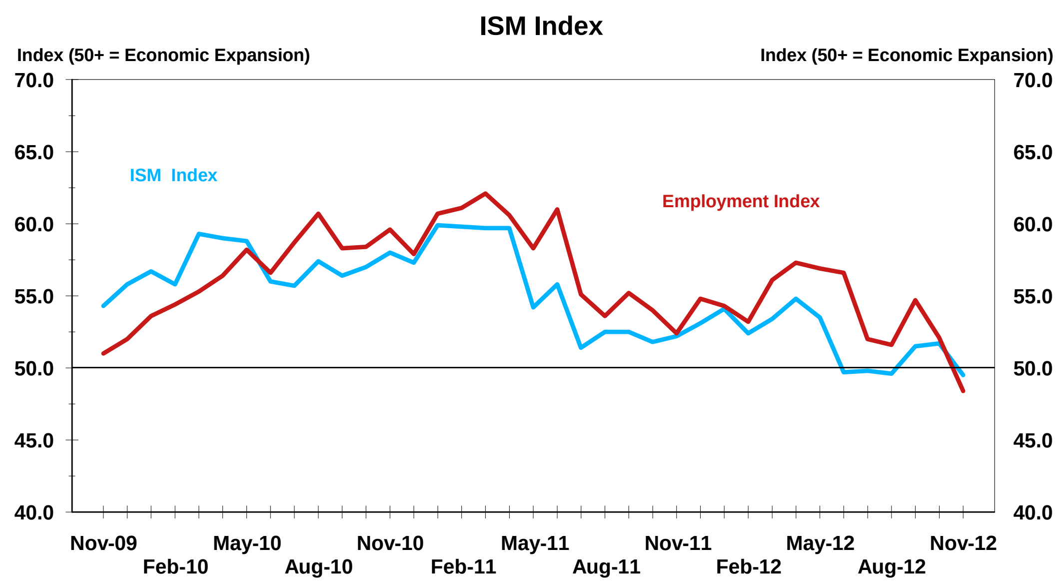
Source: U.S. Census Bureau / Haver Analytics.

New residential construction data continued to show promissing signs in October, as both measures came in above expectations. Housing starts rose to their highest level since July 2008, led by multifamily units. Building permits declined a bit in October, but still registered one of their best months of the year.



Source: U.S. Census Bureau / Haver Analytics.

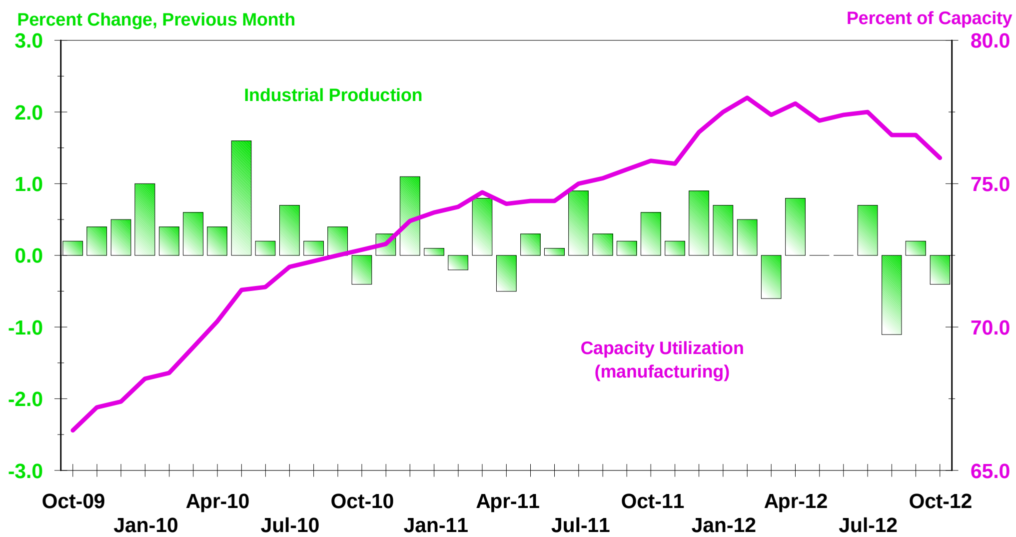
The ISM manufacturing index dropped below 50 in November for the fourth time this year, reaching its lowest level since July 2009. Readings below 50 signal contraction in the manufacturing industry. The employment component of the index also declined in November, falling below 50 for the first time in over three years.



Source: Institute for Supply Management / Haver Analytics.

Industrial production fell more than expected in October, due mostly to the effects of Hurricane Sandy in the Northeast. Capacity utilization also declined in October, reaching its lowest level so far this year.

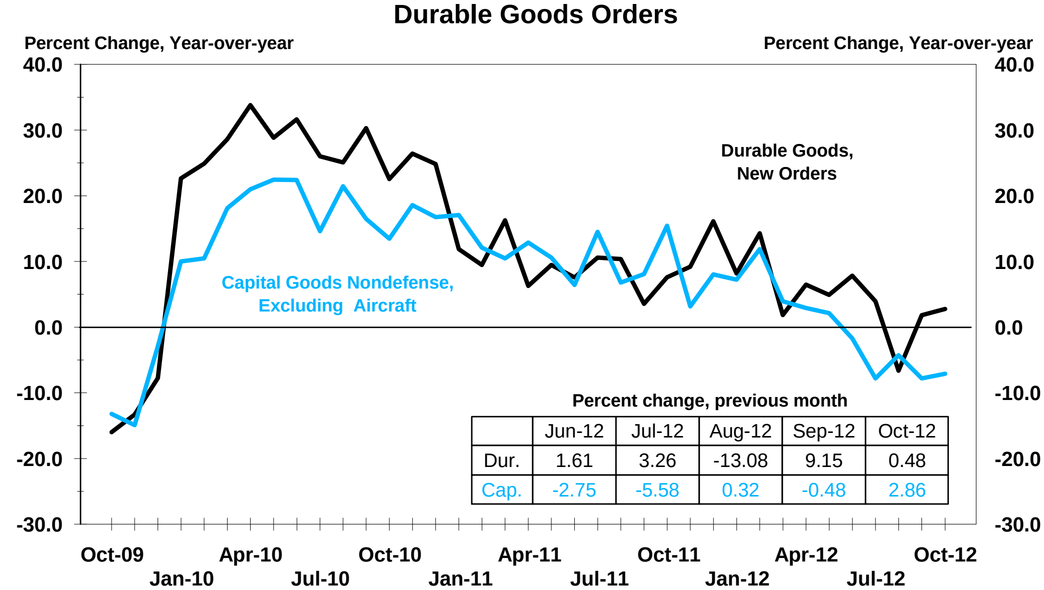
Industrial Production and Capacity Utilization



Source: Federal Reserve Board of Governors / Haver Analytics.

Orders for both durable goods and nondefense capital goods excluding aircraft rose in October, with the latter posting its largest increase since February. Despite the monthly gain, nondefense capital goods excluding aircraft continued to decrease on a year-over-year basis.

Durable Goods Orders



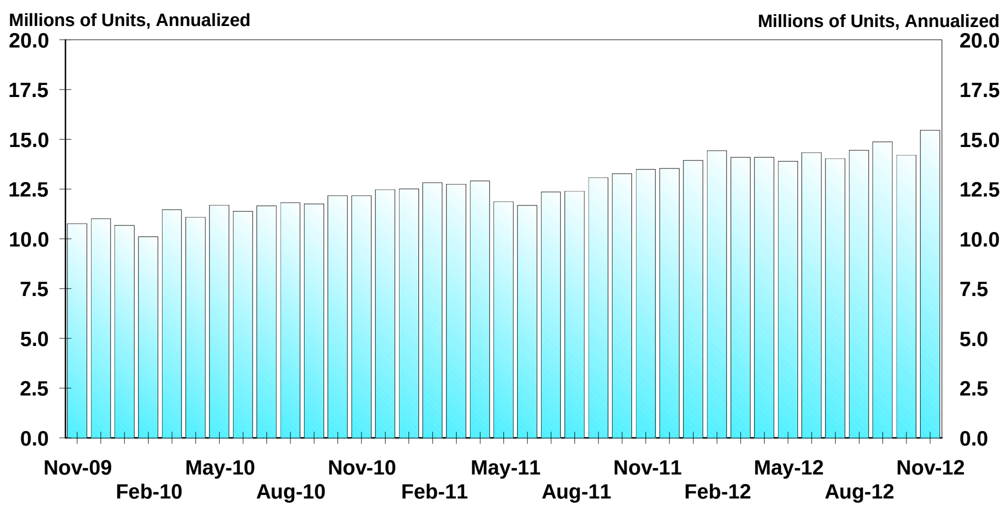
Percent change, previous month

	Jun-12	Jul-12	Aug-12	Sep-12	Oct-12
Dur.	1.61	3.26	-13.08	9.15	0.48
Cap.	-2.75	-5.58	0.32	-0.48	2.86

Source: U.S. Census Bureau / Haver Analytics.

Total auto and light truck sales rose above expectations in November, more than offsetting their drop in October and reaching their highest sales pace since December 2007. The annual sales rate has averaged 14.4 million vehicles so far in 2012, up about 13 percent from the 2011 total of 12.7 million. In the ten years preceding the recession, however, annual sales averaged almost 17 million.

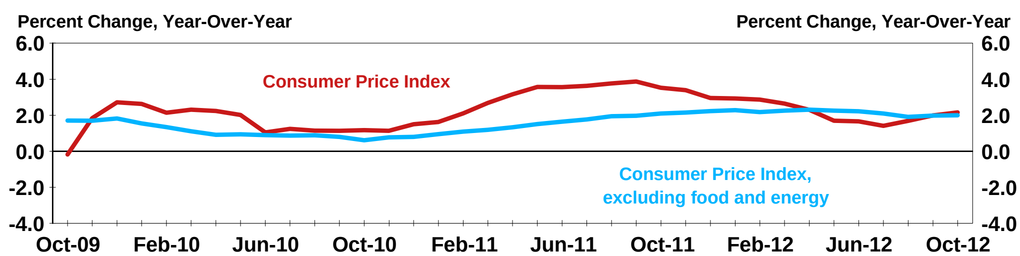
Total Auto and Light Truck Sales



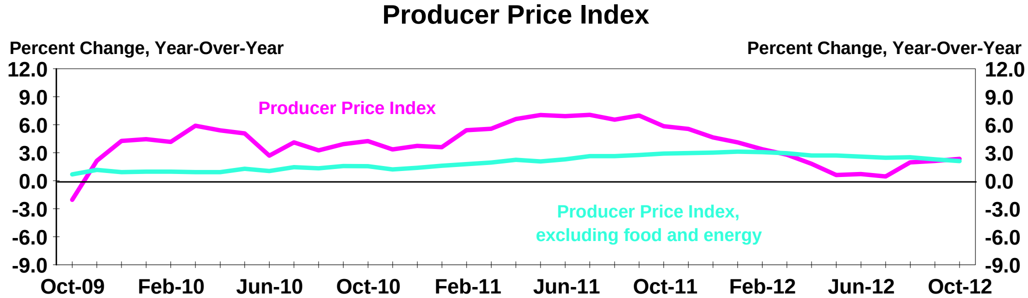
Source: Bureau of Economic Analysis / Haver Analytics.

Headline consumer prices accelerated in October for the third consecutive month, and the core index, which excludes food and energy, held mostly steady. Headline producer prices were similar, as the total index accelerated in October, but the core index slowed for the second month in a row.

Consumer Price Index

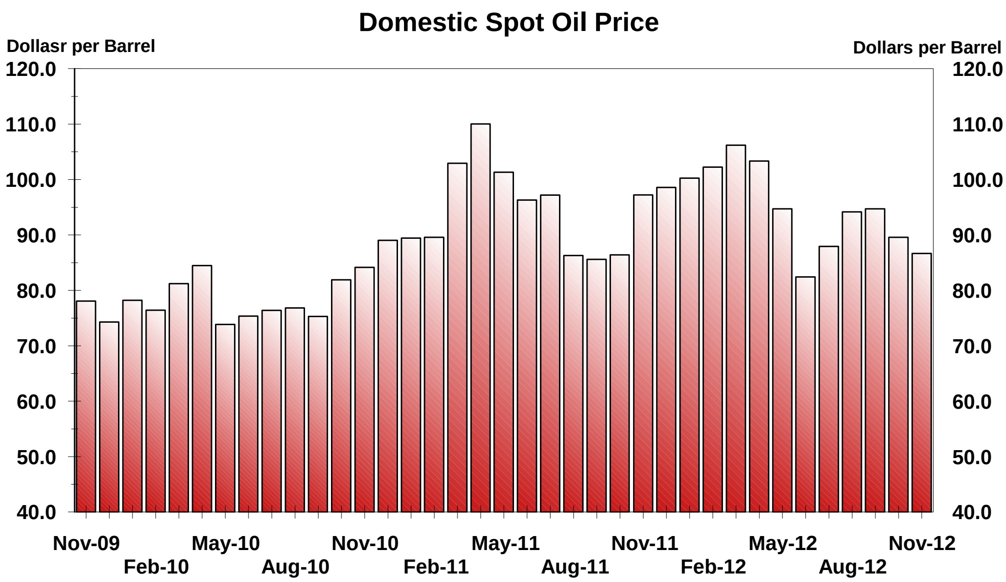


Producer Price Index



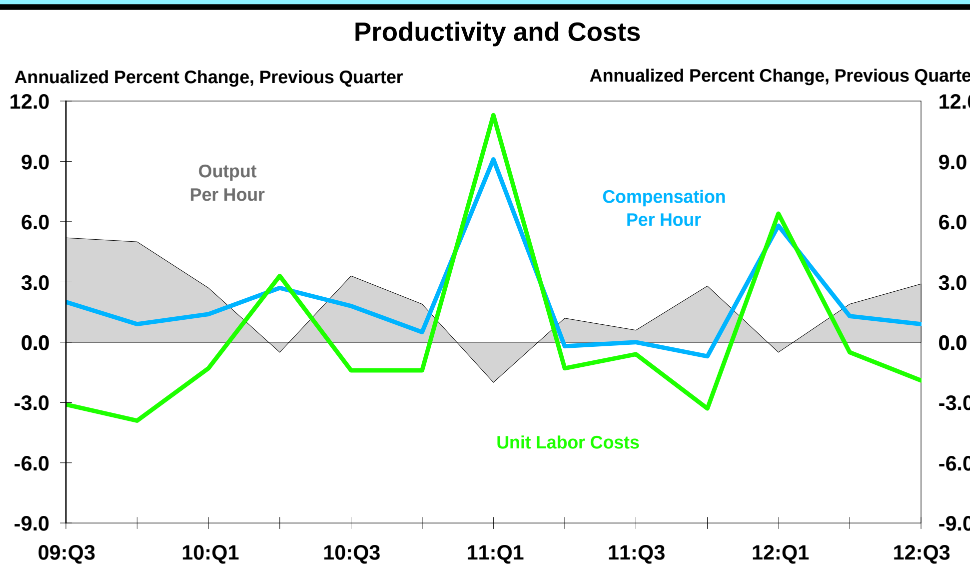
Source: Bureau of Labor Statistics / Haver Analytics.

Oil prices fell in November for the second consecutive month, recording their lowest monthly average since June. Prices were at $86.3 per barrel on December 6th, approximately in line with their November average.



Source: Wall Street Journal / Haver Analytics.

Productivity was revised higher in the third quarter, reflecting an upward adjustment to output and a steady reading on hours worked. Significant downward revisions were made to costs in the third quarter. Compensation per hour rose only 0.9%, as compared to the 1.8% increase initially reported, and unit labor costs eased 1.9%, down from the previously reported decrease of 0.1%.

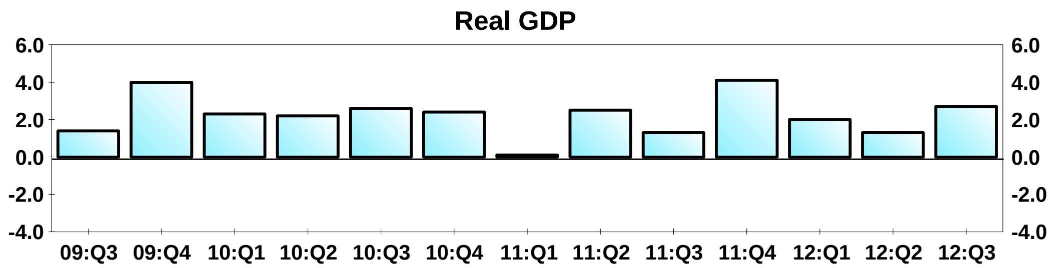


Source: Bureau of Labor Statistics / Haver Analytics.

Real GDP growth in the third quarter was stronger than originally thought. The higher growth rate was due primarily to upward revisions to private inventory investment and to exports, which were partly offset by downward revisions to personal consumption expenditures and to nonresidential fixed investment.

Revisions to Third Quarter Real GDP

Description	Advance	2nd Estimate
Real GDP	2.0	2.7
Personal Consumption	2.0	1.4
Business Investment	-1.3	-2.2
Equipment and Software	0.0	-2.7
Residential Investment	14.4	14.2
Government	3.7	3.5
Exports	-1.6	1.1
Imports	-0.2	0.1
Final Sales	2.1	1.9



Source: Bureau of Economic Analysis / Haver Analytics.

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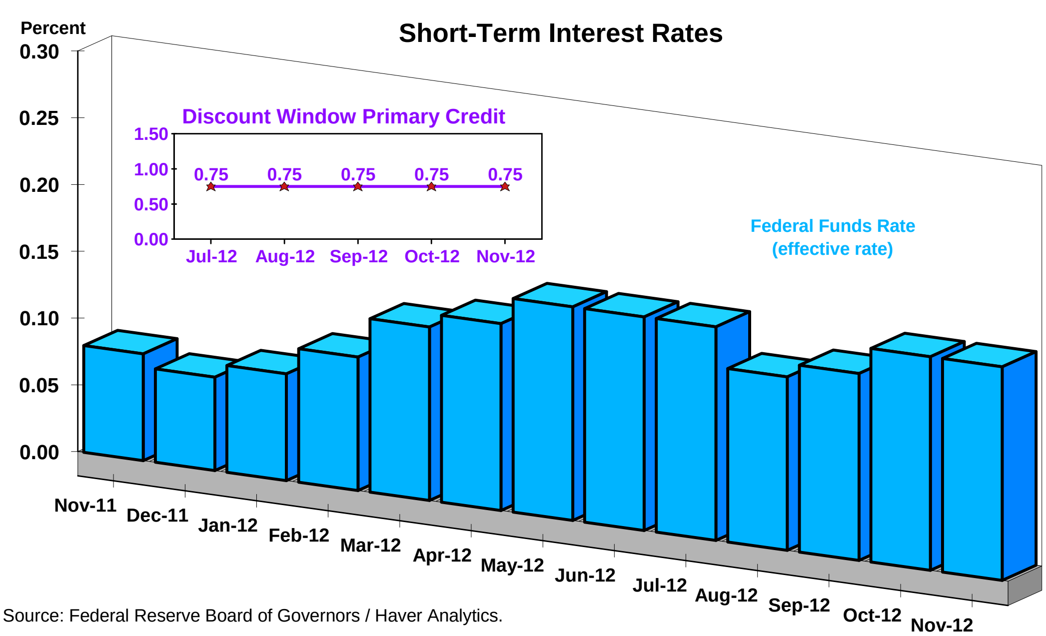

Source: Federal Reserve Board of Governors / Haver Analytics.