PRESIDENT'S REPORT TO THE BOARD OF DIRECTORS,
FEDERAL RESERVE BANK OF BOSTON
Current Economic Developments - February 10, 2005

Data since your previous Directors' meeting show the economy grew at a slower pace in the fourth quarter than seen in the third quarter. Core inflation has become a greater concern and continued employment increases remain key in sustaining a vibrant economy.

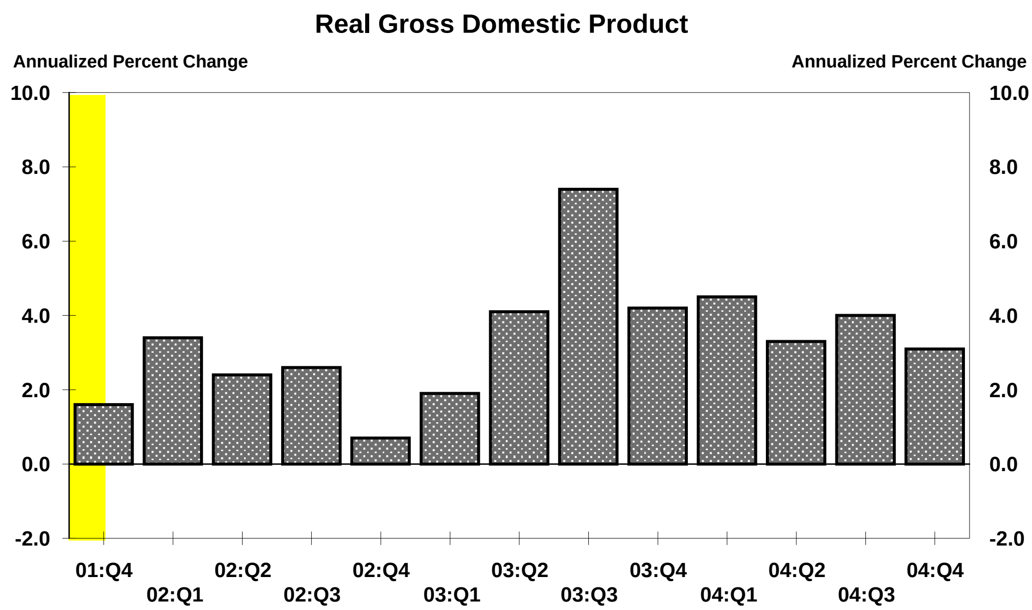
During the fourth quarter, real GDP posted a moderate gain, led by growth in consumption, equipment and software and inventory investment. The gains in these areas were partly offset by a negative contribution from exports and an increase in imports.

Despite the sustained increases in core inflation for consumers and wholesalers, consumption remains strong. Total compensation costs, as measured by the ECI, declined slightly even as benefit costs edged up. Wage and salary inflation held steady. Productivity growth slowed in the fourth quarter, while unit labor costs edged up and compensation costs fell slightly.

The limited data available for 2005 suggest continued economic strength. In January, payroll employment increased and the unemployment rate fell. Initial claims continued to edge down further.

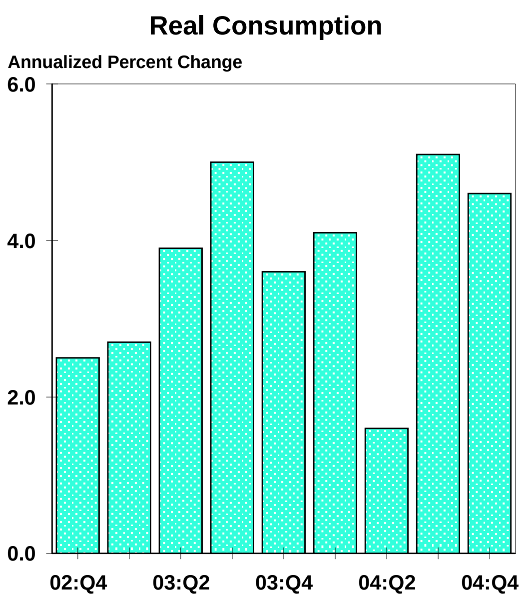
Also in January, the ISM index declined despite an increase in the employment component.
Consumer confidence and sentiment rose while expectations remained relatively flat.
Auto and light truck sales fell in January after two successive quarters of growth.

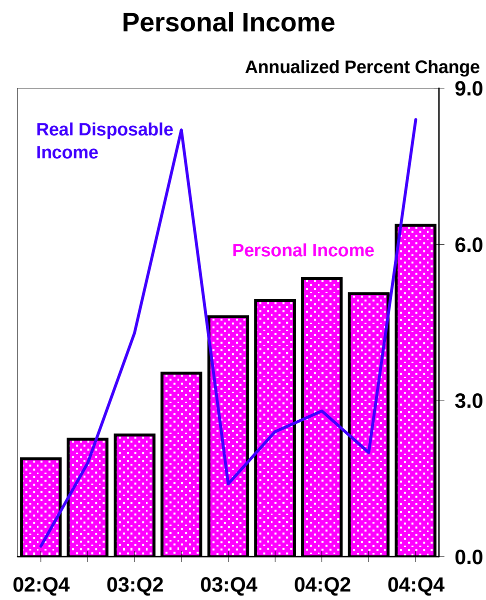
During the fourth quarter, real GDP decelerated due primarily to a downturn in exports and an acceleration in imports. Still, the GDP figures portray an expanding economy, as consumers continue to spend and businesses continue to invest.



Source: Bureau of Economic Analysis.

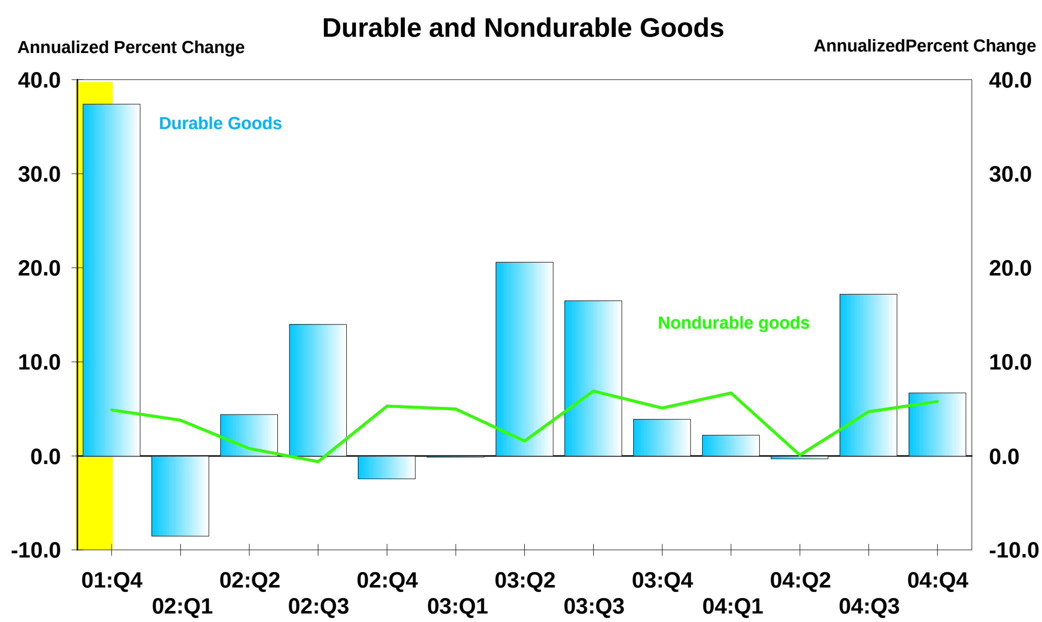
Real consumption remained robust in the fourth quarter, aided by increases in both personal and real disposable income.





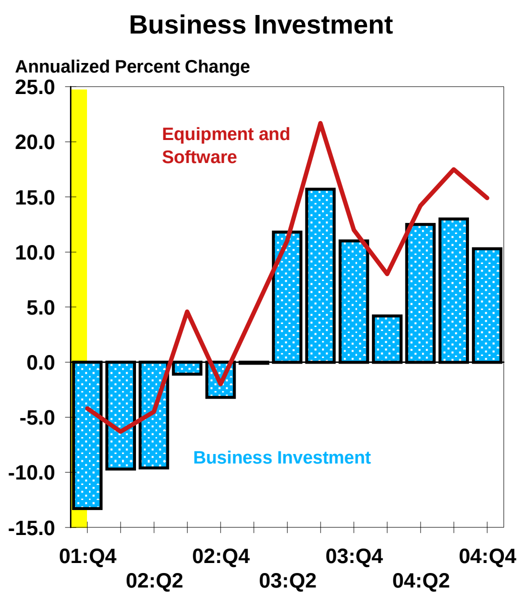
Source: Bureau of Economic Analysis.

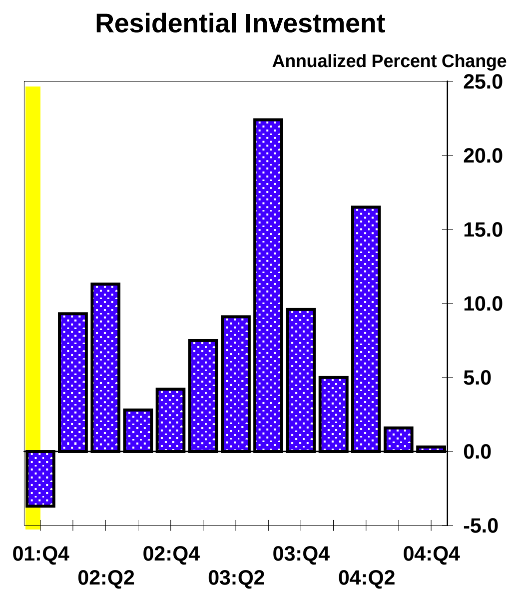
Still, consumer spending was somewhat lower in the fourth quarter as consumption of durable goods decreased. Spending on nondurable goods rose for the second consecutive quarter.



Source: Bureau of Economic Analysis.

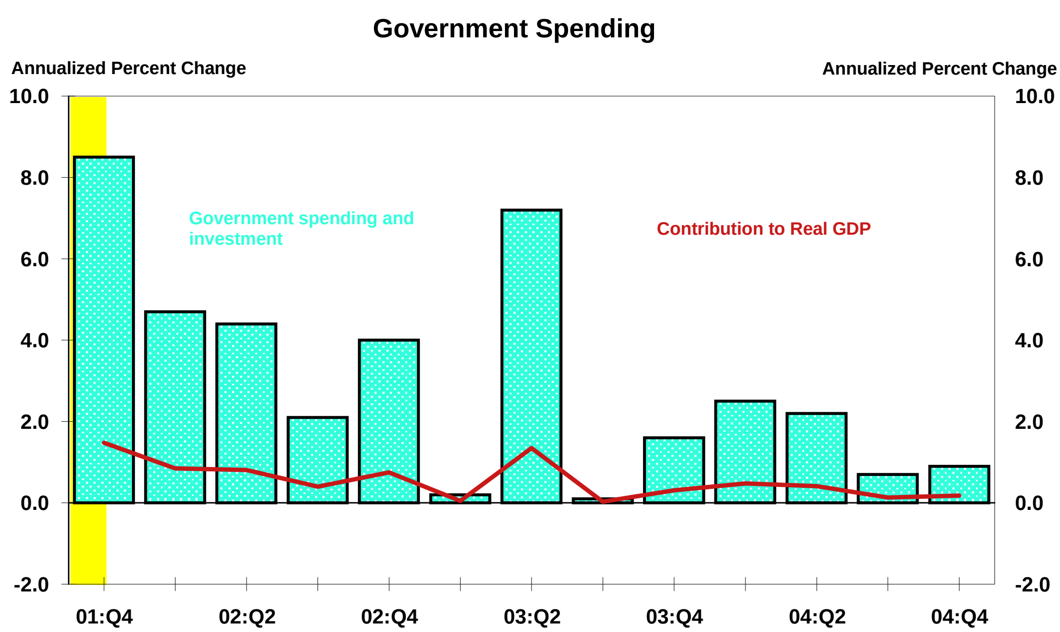
During the fourth quarter, businesses continued to invest in equipment and software, although at a slower pace than seen in the third quarter. Residential investment posted its smallest gain in three years.





Source: Bureau of Economic Analysis.

Government spending increased slightly in the fourth quarter, yet continues to contribute less than two-tenths of a percentage point to real GDP.

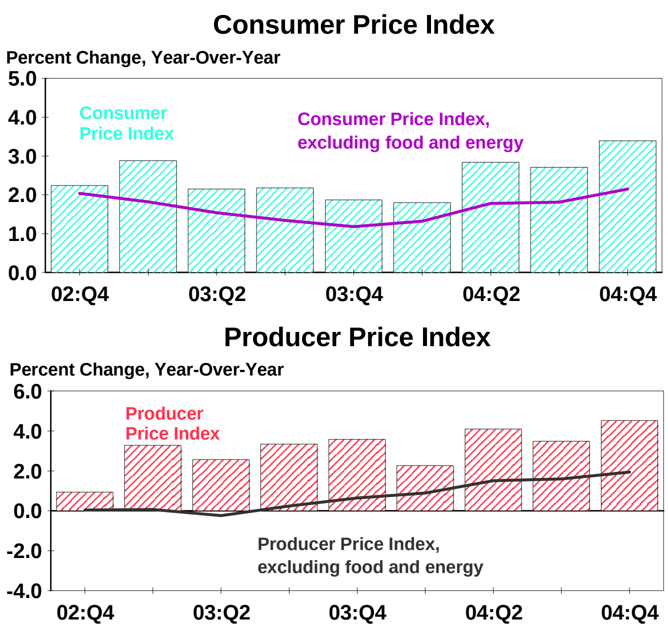


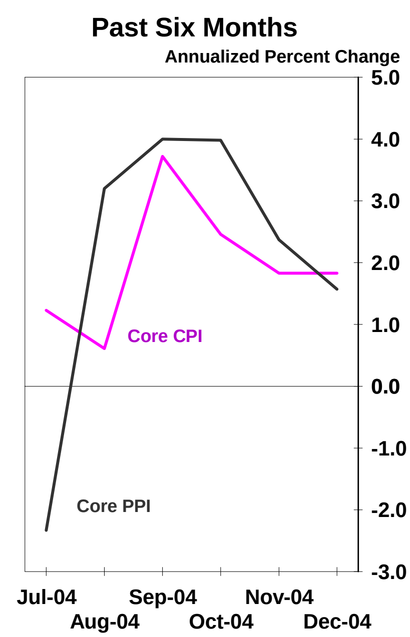
Source: Bureau of Economic Analysis.

Following a year of diminishing growth, exports fell in the fourth quarter. Imports also increased to further subtract from real growth.

Source: Bureau of Economic Analysis.

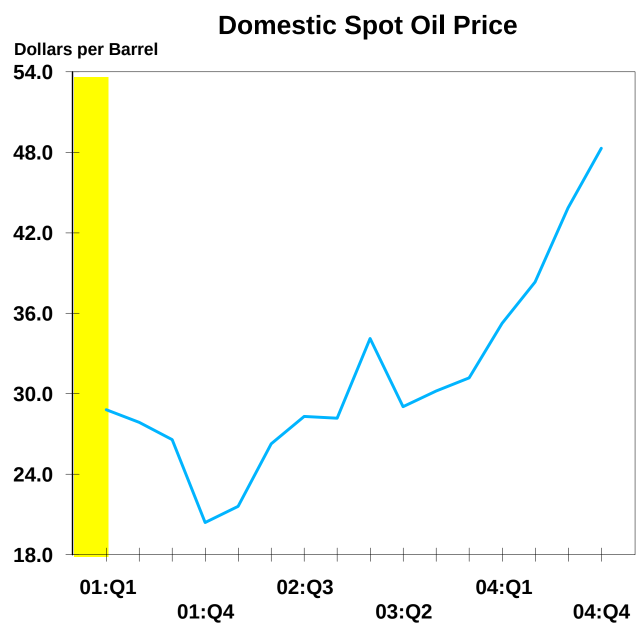
Both consumer and producer prices rose in the fourth quarter, due in large part to record high energy prices. Inflation in the core indices, which exclude food and energy, has eased after the rapid increases seen earlier in the year.

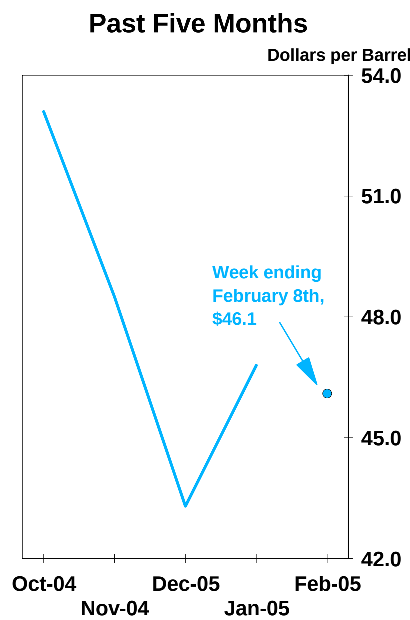




Source: Bureau of Labor Statistics.

Oil prices peaked in the fourth quarter, reaching an all-time high in October before receding in November and December. Recent data shows prices remain at historically high levels.





Source: Wall Street Journal (oil prices).

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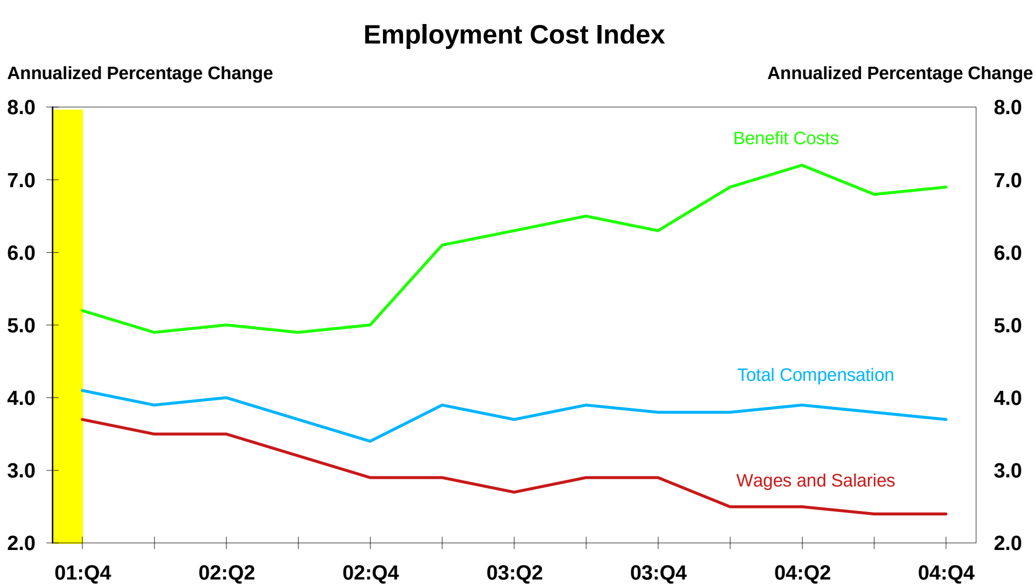
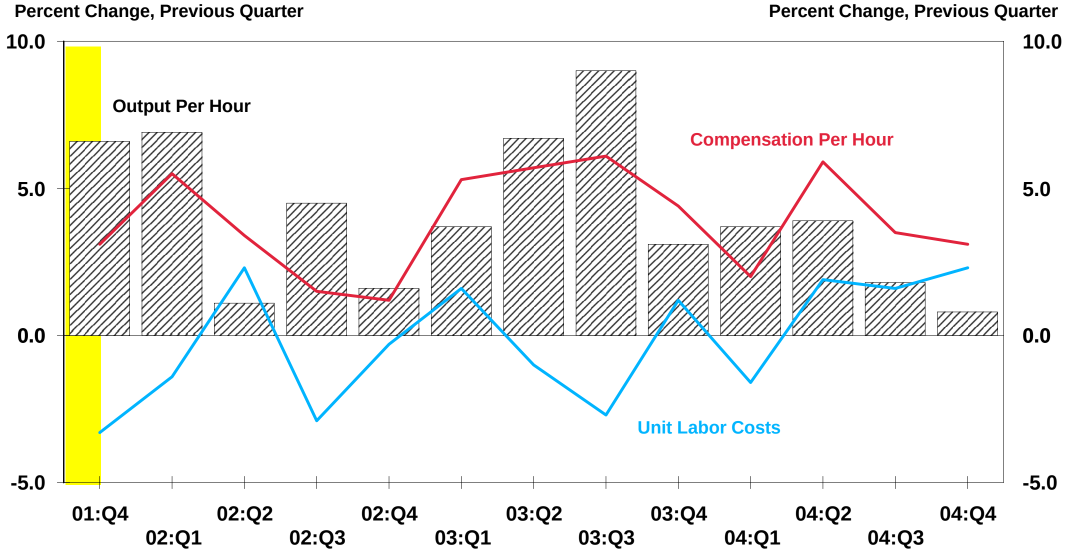
Employee costs decelerated during the fourth quarter, as wages and salaries were flat and benefit costs increased.



Source: Bureau of Labor Statistics.

Productivity growth slowed in the fourth quarter, compared to the third, seeing its smallest increase in nearly four years. Unit labor costs rose slightly while compensation costs fell somewhat.

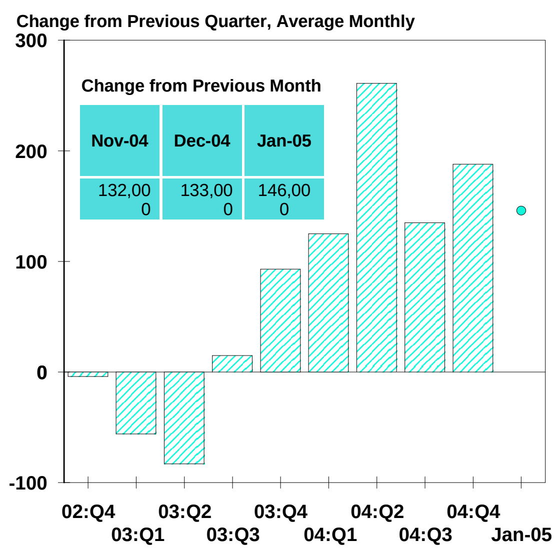
Productivity and Costs



Source: Bureau of Labor Statistics.

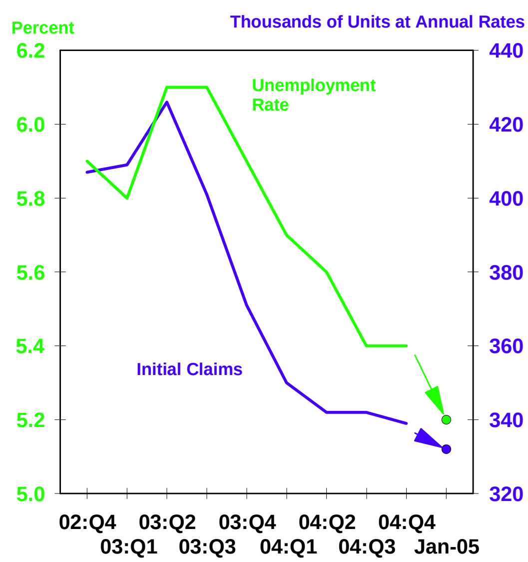
The labor market continues to show signs of strength. Payroll employment increased again in January and initial claims edged down further. The unemployment rate fell to its lowest point in over three years.

Nonfarm Payroll Employment



Nov-04	Dec-04	Jan-05
132,000	133,000	146,000

Unemployment Rate and Initial Claims



Source: Bureau of Labor Statistics (employment) Department of Labor, Employment and Training Administration (claims).

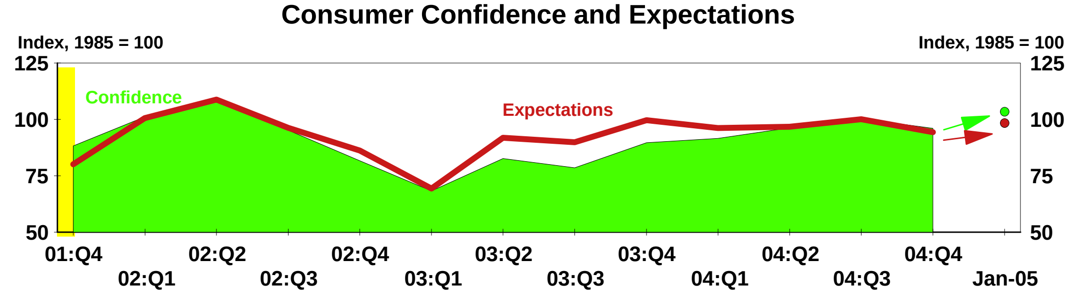
The ISM index continued to fall in January, despite a rise in the employment index.

ISM Index

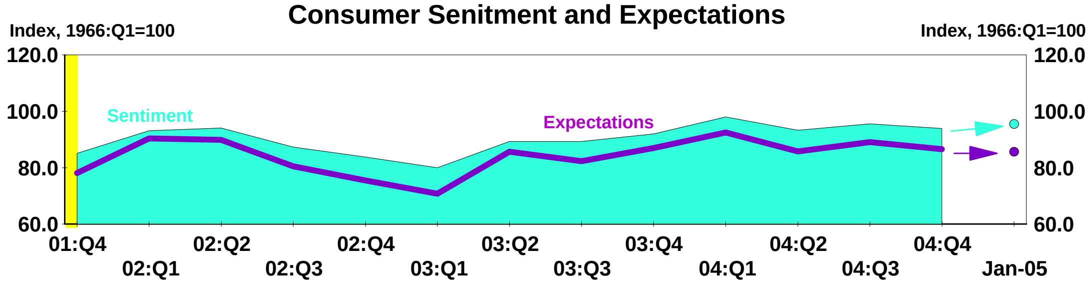
Source: National Association of Purchasing Management.

Consumer confidence increased and sentiment rose slightly in January while expectations were bascially flat.

Consumer Confidence and Expectations

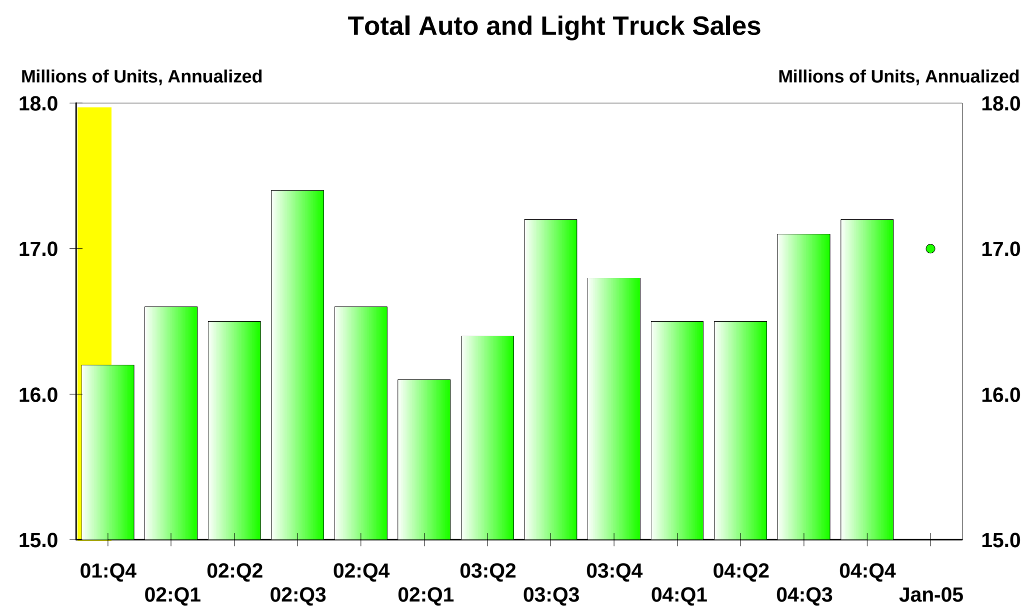


Consumer Senitment and Expectations



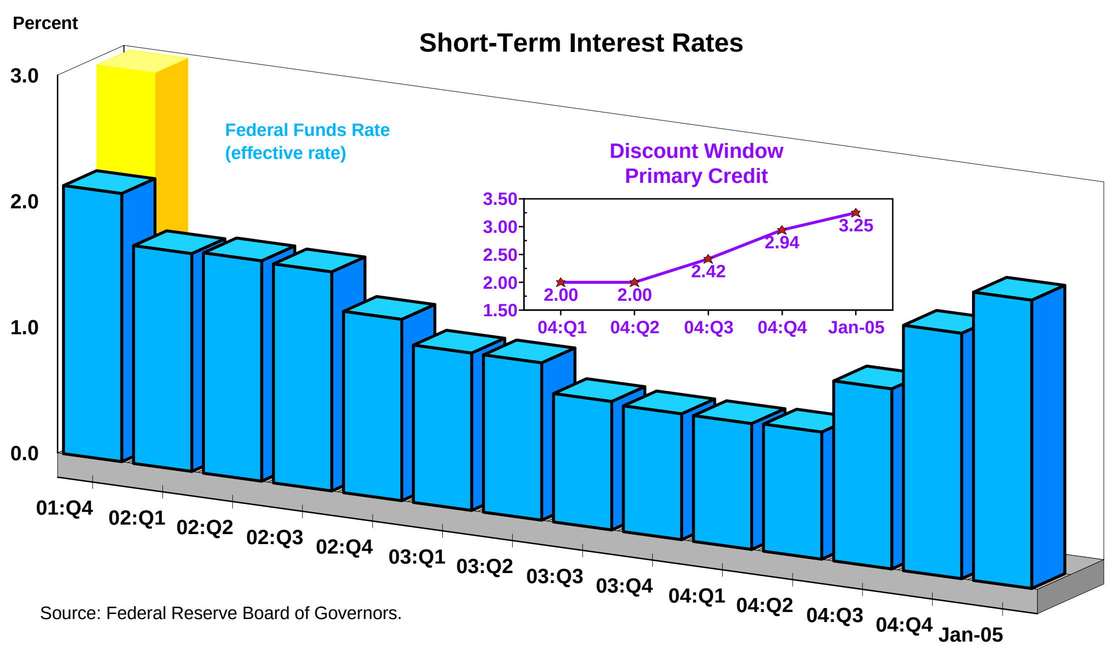
Source: The Conference Board (confidence) and University of Michigan (sentiment).

Despite the increases in consumer attitudes, auto and light truck sales fell in January but remain at a high level.



Source: Federal Reserve, Board of Governors.

Overall the economy grew at a slower pace in the fourth quarter than seen in the third quarter. Core inflation has become a greater concern and continued employment increases remain key to sustaining a vibrant economy.



Source: Federal Reserve Board of Governors.