National Outlook

Overview
The economic status of the United States is currently characterized by a slowdown in consumer spending. Consumers are slowly being affected by higher interest rates and energy prices. Construction spending, however, remains strong and is anticipated to continue. To keep the economy moving, businesses may need to compensate for the slowdown in consumer spending. The continued high price of oil will affect GDP growth and spending patterns for the foreseeable future.

Summary of Economic Conditions
The Federal Reserve Board continues to tighten monetary policy. Tightening moves are also expected throughout 2005 into 2006. In 2004 the price of oil was volatile, causing much consternation among consumers and financial markets. The prospects for growth in business lending over the next fiscal year remain encouraging, largely due to a resurgence in business confidence and, along with it, a revival in inventory investment and capital spending activity. Housing, autos, and retail sales are doing very well. Employment has been expanding consistently throughout 2004.

Real GDP is estimated to have grown by 4.4% in 2004, followed by 3.2% growth in 2005. Consumer prices are expected to advance by 2.2% in 2005, a slight decrease from the 2004 growth rate of 2.7%.

Outlook for 2005
Real GDP, incomes, profits, and even employment are now near or above their pre-recession peaks. The economy's prospects through 2005 are upbeat. Also, if energy prices moderate a bit further, real GDP growth next year should reach 3.2%.

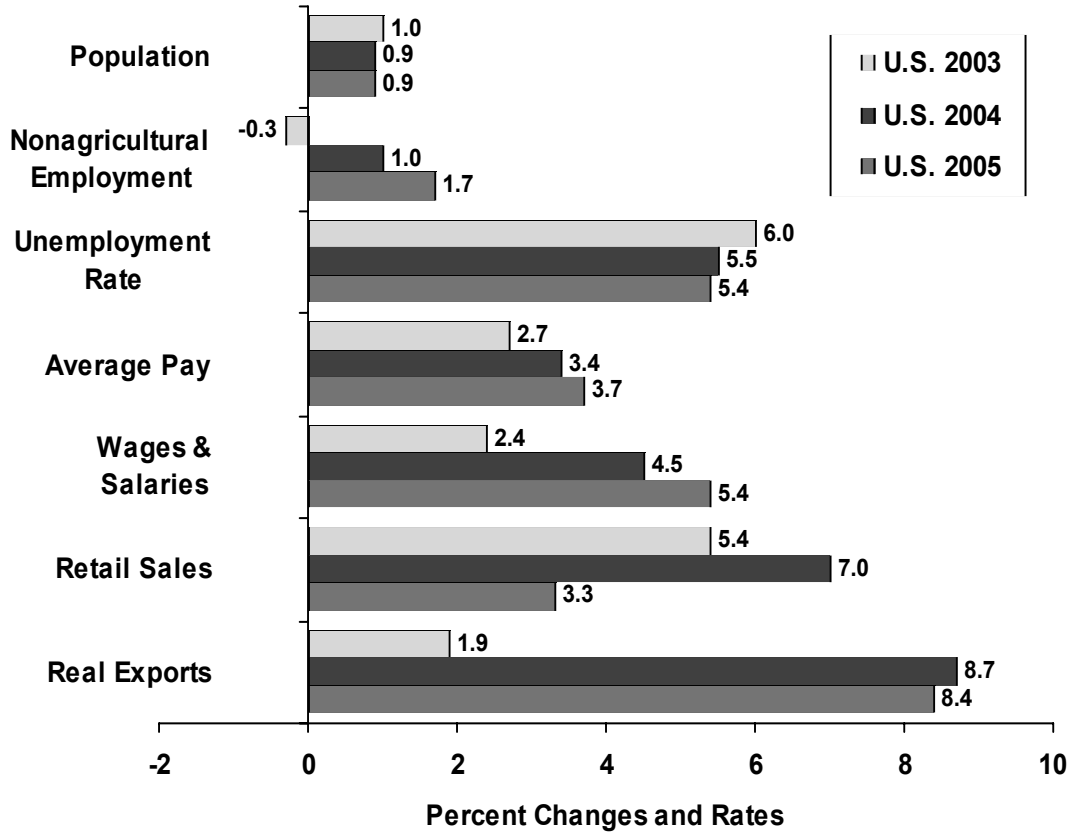
Rising interest rates will work against the national economy in 2005. Housing starts and home sales continue to be positively influenced by low mortgage rates and high affordability ratios.

Significant Issues
Business Investment. Healthy corporate balance sheets indicate a positive outlook for business and financial services. However, these industries face a number of significant risks. Revenue growth for financial and business providers is expected to be in line with that of other industry groups throughout 2005. However, in aggregate, profit margins are expected to be considerably stronger, thanks to cost-cutting measures, pricing power, and still favorable interest rates. Risks include: a negative shock to business confidence or to profits and cash flow by way of elevated oil and other commodity prices; the impacts of higher interest rates and a flat equities market; and greater erosion in household credit quality.

Energy Prices. Rising energy prices pose a significant risk to the economy. The higher prices are weighing on economic growth, and an increase to these high prices would threaten the economic expansion. The future path of energy prices will also be a significant factor in the performance of the economy in 2005. Forecasts for natural gas suggest a continuation of prices in the $4.50-5.50 per thousand cubic feet range through 2005. Forecasts for crude oil call for some moderation in 2005, but prices are projected to remain above the $35 per barrel range throughout 2005.

Consumer Spending. The slow growth of consumer spending is projected to affect GDP growth. This is due to the fact that consumer spending accounts for more than two thirds of the GDP. The decrease in consumer spending has resulted from soaring gasoline prices. High gas prices are leaving consumers with less to spend on other items.

Figure 1
U.S. Economic Indicators: 2003-2005



Source: Council of Economic Advisors' Revenue Assumptions Committee