

ALTERNATIVE FORECASTS

Global Insight has assigned a 60% probability of occurrence to its September 2005 baseline forecast of the U.S. economy. The major features of this forecast include:

- Real GDP increases 3.5% in 2005, 3.4% in 2006, 3.2% in 2007, and 3.4% in 2008;
- U.S. nonfarm employment grows 1.6% in 2005, 1.5% in 2006, 1.4% in 2007, and 1.3% in 2008;
- the annual U.S. civilian unemployment rate hovers near 5.0% in each year of the forecast;
- consumer inflation is 3.5% in 2005, 2.3% in 2006, 1.5% in 2007, and 1.9% in 2008; and
- the federal unified budget deficit is \$343 billion in 2005, then it recedes to \$251 billion in 2008.

OPTIMISTIC SCENARIO

The *Optimistic Scenario* represents the upside to the baseline forecast. It has been assigned a 20% probability of occurrence. This scenario has been nicknamed “Everything goes Right” because six key assumptions outperform their baseline counterparts, causing the economy to grow stronger than in the baseline. First, total factor productivity is stronger. It is an economic panacea. It makes economic headaches such as inflation, budget deficits, and sluggish growth disappear. Second, foreign economic growth is stronger, which raises U.S. exports and strengthens domestic manufacturing. Third, business investment, especially for equipment and software, is higher. Fourth, the federal government budget deficit is lower because the stronger economy simultaneously boosts tax revenues and lowers federal transfer payments. Lower interest rates also push down government interest payments. Fifth, housing starts are stronger in this alternative forecast. The stronger starts result from better job growth, lower interest rates, higher consumer confidence, and lower long-term mortgage rates. Sixth, oil prices are assumed to be about \$5/barrel lower than in the *Baseline Scenario*.

These assumptions produce a rosier outlook, with real output growing 0.9 percentage point faster than in the baseline during 2006 and 0.8 percentage point faster in 2007. Although economic growth and labor markets are stronger, inflation is lower because of the stronger dollar and the higher productivity gains. The lower inflation rate allows the Federal Reserve to keep the federal funds rate below the baseline value. Job growth is also stronger in this scenario. Nonfarm employment is 1 million higher than in the baseline at the end of 2006 and 1.7 million higher at the end of 2007. This strong job growth keeps the U.S. unemployment rate below its baseline counterpart over the forecast period.

The Idaho optimistic and baseline forecasts diverge noticeably in 2007 and 2008. Ironically, the assumed strong productivity gains that allow U.S. output to grow faster than in the baseline without causing inflation dampen Idaho’s employment prospects. Specifically, Idaho nonfarm employment averages about 1.9% growth during 2007 and 2008, which is a hair under the projected 2.0% rate in the baseline. As a result, there are 2,700 fewer jobs in 2008 in the *Optimistic Scenario* compared to the *Baseline Scenario*. Idaho’s goods-producing sector is hit the hardest. This sector’s employment declines steeply, shedding 3,700 jobs from 2005 to 2008. In comparison, about 1,400 Idaho goods-producing jobs are lost in the baseline case over the same period. Idaho nominal personal income also grows more slowly than its baseline counterpart, averaging 5.5% annual growth from 2006 to 2008. Idaho nominal personal income averages 6.2% growth in the *Baseline Scenario*. The gap between the optimistic and baseline Idaho real personal income is narrower because inflation is lower in the *Optimistic Scenario*.

IDAHO ECONOMIC FORECAST
BASELINE AND ALTERNATIVE FORECASTS
OCTOBER 2005

	BASELINE				OPTIMISTIC				PESSIMISTIC			
	2005	2006	2007	2008	2005	2006	2007	2008	2005	2006	2007	2008
GDP (BILLIONS)												
Current \$	12,473	13,185	13,887	14,664	12,479	13,282	14,053	14,857	12,463	13,107	13,726	14,578
% Ch	6.3%	5.7%	5.3%	5.6%	6.3%	6.4%	5.8%	5.7%	6.2%	5.2%	4.7%	6.2%
2000 Chain-Weighted	11,135	11,513	11,885	12,293	11,140	11,617	12,090	12,565	11,124	11,374	11,529	11,837
% Ch	3.5%	3.4%	3.2%	3.4%	3.6%	4.3%	4.1%	3.9%	3.4%	2.2%	1.4%	2.7%
PERSONAL INCOME - CURR \$												
Idaho (Millions)	40,172	42,801	45,349	48,056	40,157	42,496	44,758	47,166	40,195	43,244	46,546	49,974
% Ch	7.4%	6.5%	6.0%	6.0%	7.4%	5.8%	5.3%	5.4%	7.5%	7.6%	7.6%	7.4%
U.S. (Billions)	10,295	10,965	11,586	12,266	10,296	11,008	11,675	12,372	10,291	10,949	11,561	12,281
% Ch	6.0%	6.5%	5.7%	5.9%	6.0%	6.9%	6.1%	6.0%	6.0%	6.4%	5.6%	6.2%
PERSONAL INCOME - 2000 \$												
Idaho (Millions)	36,068	37,589	39,144	40,660	36,067	37,505	38,978	40,410	36,028	37,240	38,806	40,270
% Ch	4.4%	4.2%	4.1%	3.9%	4.4%	4.0%	3.9%	3.7%	4.3%	3.4%	4.2%	3.8%
U.S. (Billions)	9,243	9,630	10,001	10,378	9,247	9,715	10,167	10,600	9,225	9,430	9,639	9,896
% Ch	3.0%	4.2%	3.9%	3.8%	3.1%	5.1%	4.7%	4.3%	2.8%	2.2%	2.2%	2.7%
TOTAL NONFARM EMPLOYMENT												
Idaho	609,424	620,621	633,087	646,691	609,440	620,308	631,578	643,980	609,508	618,941	628,272	640,924
% Ch	3.6%	1.8%	2.0%	2.1%	3.6%	1.8%	1.8%	2.0%	3.7%	1.5%	1.5%	2.0%
U.S. (Thousands)	133,627	135,675	137,508	139,261	133,637	136,368	138,958	141,121	133,588	134,916	135,174	135,959
% Ch	1.6%	1.5%	1.4%	1.3%	1.6%	2.0%	1.9%	1.6%	1.6%	1.0%	0.2%	0.6%
GOODS-PRODUCING SECTOR												
Idaho	112,091	110,879	109,359	109,434	112,122	110,839	108,342	107,141	112,288	111,094	107,980	108,618
% Ch	6.3%	-1.1%	-1.4%	0.1%	6.3%	-1.1%	-2.3%	-1.1%	6.5%	-1.1%	-2.8%	0.6%
U.S. (Thousands)	22,142	22,203	22,169	22,186	22,147	22,373	22,603	22,768	22,159	22,244	21,606	21,063
% Ch	1.2%	0.3%	-0.2%	0.1%	1.2%	1.0%	1.0%	0.7%	1.3%	0.4%	-2.9%	-2.5%
NONGOODS-PRODUCING SECTOR												
Idaho	497,332	509,742	523,728	537,258	497,319	509,470	523,236	536,839	497,221	507,847	520,292	532,306
% Ch	3.1%	2.5%	2.7%	2.6%	3.1%	2.4%	2.7%	2.6%	3.0%	2.1%	2.5%	2.3%
U.S. (Thousands)	111,485	113,471	115,339	117,075	111,491	113,995	116,355	118,353	111,429	112,672	113,568	114,895
% Ch	1.7%	1.8%	1.6%	1.5%	1.7%	2.2%	2.1%	1.7%	1.7%	1.1%	0.8%	1.2%
SELECTED INTEREST RATES												
Federal Funds	3.1%	4.3%	4.6%	4.8%	3.1%	4.0%	4.1%	4.3%	3.2%	5.5%	6.9%	7.4%
Bank Prime	6.1%	7.3%	7.6%	7.8%	6.1%	7.0%	7.1%	7.3%	6.2%	8.5%	9.9%	10.4%
Existing Home Mortgage	5.8%	6.4%	6.7%	7.0%	5.8%	6.1%	6.2%	6.4%	5.9%	8.8%	9.4%	7.7%
INFLATION												
GDP Price Deflator	2.7%	2.2%	2.0%	2.1%	2.7%	2.1%	1.7%	1.7%	2.7%	2.8%	3.3%	3.4%
Personal Cons Deflator	2.9%	2.2%	1.7%	2.0%	2.7%	2.1%	1.7%	1.7%	3.1%	4.1%	3.3%	3.5%
Consumer Price Index	3.5%	2.3%	1.5%	1.9%	3.4%	1.8%	1.1%	1.5%	3.7%	4.0%	2.6%	3.0%

Forecast Begins the **THIRD** Quarter of 2005

PESSIMISTIC SCENARIO

The downside risks to the baseline scenario are explored in the *Pessimistic Scenario*. Also known as the *Stagflation Scenario*, this alternative forecast has been assigned 20% probability of occurrence. A significant feature of the *Pessimistic Scenario* is that after a relatively long dormant period, inflation once again rears its ugly head. The pickup of inflation reflects higher oil prices, a weaker dollar, two-and-one half years of accommodative monetary policy, and loose fiscal policy. A key assumption in this *Scenario* is there is less spare capacity in both the global and U.S. economies than had been previously believed. Ironically, some of this limited capacity is the result of recent economic achievements. Namely, rapid technological advances and higher oil prices may have rendered current idle capacity obsolete. It is also assumed the swelling U.S. trade deficit will scare off the foreign investors that have shored up the economy, causing the U.S. dollar to rapidly weaken. The lower dollar raises the relative prices for imported goods and services, which raises their prices. But price increases may not be limited to imports. American businesses, which have been forced to keep prices in check to compete with imports, may take this opportunity to also increase prices. In addition, the anticipated flight from greenback-valued investments will put upward pressure on domestic interest rates, which could lower the United State's long-term economic growth trajectory.

Between the higher interest rates and stubbornly high energy prices, consumer confidence wavers. As a result, consumers rein in discretionary spending and the U.S. economy slows. The economy does not suffer a recession in this alternative, but it fails to live up to the expectations set in the baseline. Specifically, real GDP growth is 1.2 percentage points lower than in the baseline in 2006 and it is 1.9 percentage points lower in 2007. Production shifts from satisfying domestic demand to serving foreign demand, thanks to the weaker dollar. As a result of higher interest rates and higher prices for foreign goods, the U.S. household saving rate rises to 2.3% in 2008. This is more than twice the 1.1% saving rate forecast in the *Baseline Scenario*.

After receiving a mild boost in 2005, Idaho nonfarm employment and real personal income grow slower in the remaining years of the forecast compared to their baseline counterparts. As the accompanying table shows, Idaho nonfarm employment increases by 3.7% in 2005 in the *Pessimistic Scenario*. After 2005, however, Idaho's job growth slows to 1.5% in both 2006 and 2007 and to 2.0% in 2008. As a result, there are 640,900 jobs in the Gem State in 2008, or about 5,800 lower than in the *Baseline Forecast*. Unlike the *Optimistic Case*, both the goods-producing and nongoods-producing sectors experience sub-par growth. The higher inflation causes Idaho nominal personal income to grow faster than in the baseline case. Indeed, Idaho real personal income actually grows slower in this scenario than in the baseline.