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CONFIDENTIAL (FR)

February 9, 1977

SUMMARY AND OUTLOOK

By the Staff
Board of Governors
of the Federal Reserve System

SUMMARY AND OUTLOOK

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary. Economic activity apparently gained additional momentum through mid-January, extending the strong advance evident toward the end of 1976. Later in the month, however, unusually severe winter weather and natural gas shortages caused disruptions of production, transportation, and retail sales activity, the magnitude and duration of which are still uncertain.

Labor market data relating to the week ending January 15th gave evidence of increasing labor demand. Nonfarm payroll employment rose by 230,000 from mid-December, with almost 95,000 jobs added in manufacturing. Two-thirds of the industries covered in the survey reported employment increases, but severe weather had already caused a further drop in construction employment and widespread large reductions in the length of the average workweek. The unemployment rate was reported to have dropped by half a point to 7.3 per cent, but the sharpness of this decline may also have reflected the weather since it was due largely to individuals leaving the labor force. By late January, there were widespread reports of industrial layoffs because of natural gas shortages, but only a modest increase was evident in initial claims for unemployment insurance by the final week of January.

Fragmentary data suggest that industrial production may have declined by about 1 per cent in January, with widespread cuts except in the utilities industries. A sharp decline in auto assemblies

(about 15 per cent), however, was partly attributable to reductions of small car production as a result of weak sales and heavy stocks.

Bad weather may have discouraged some shoppers, but sales at retail outlets other than auto and building materials probably were near the high level attained in December. However, unit sales of domestic autos, which continued at the advanced December pace early in the month, did slip in the final ten days of January. For the month as a whole, the annual rate fell to 8.8 million units--off one-half million from December. Sales of imported models, which were boosted by price incentives, rose to an annual rate of 1.7 million units in January.

Residential construction activity showed surprising strength in December as private housing starts rose to a 1.94 million unit annual rate--the highest level in over three years. Starts of multifamily units, some of which have been influenced by HUD subsidy programs in recent months, rose sharply further in December.

Shipments of nondefense capital goods strengthened in December, and newly available data suggest that the weakness in expenditures on producer's durable equipment during the fourth quarter as a whole was concentrated in autos, trucks and agricultural equipment. Production of this equipment was reduced by strikes. Business spending on other types of equipment was at an advanced rate. New orders for nondefense capital equipment rose 6-1/4 per

cent in December, recovering about 60 per cent of the sharp November decline. However, advance indicators of nonresidential building activity continued weak.

The book value of manufacturers' inventories was virtually unchanged in December as a further decline in nondurable inventories was about offset by a modest rise in durable stocks. Because of a large increase in shipments the inventory-sales ratio for durables fell sharply. With the strong gain in retail sales late last year, it is likely that there was a net runoff of physical stocks at retail outlets.

Consumer prices rose 0.4 per cent in December, equal to the average rise for the year. Energy prices rose sharply--by 1.1 per cent--mainly as a result of higher natural gas and fuel oil prices. Price increases for services and nonfood commodities continued moderate in December. While food prices were up only fractionally in December, larger increases appear likely this quarter because of freeze damage to the Florida vegetable and citrus crops.

Outlook. The rate of economic expansion is being held down this quarter by weather-induced production interruptions and associated income losses. These effects are roughly estimated to amount to about 2 percentage points in terms of the annual rate of growth of real GNP, primarily reflecting a substantial increase in fuel imports, a smaller overall rate of net inventory investment, and some downward effects on construction. After making an allowance

for underlying additional strength we now project a first quarter growth rate of 3.8 per cent (annual rate)--as compared to the 5 per cent rate that was projected last month.

The first quarter projection assumes that the amount of worktime lost as a result of severe weather and fuel shortages is equivalent to around a quarter of a million people off the job for the entire quarter. This unusual increase in lost time is assumed to have reached a peak in late January and early February, and to be largely over by mid-March. Apart from losses in industrial production, we expect a noticeable dip in housing starts as well as slower progress on construction under way. Rather than rising as previously projected, aggregate corporate profits are now expected to be virtually unchanged in the first quarter with some shift in composition toward utilities and fuel producers.

Although it appears that growth in some consumer outlays is being damped by income losses due to lost work time and by difficulties of shopping, total consumer outlays are projected to rise as a result of sharply higher expenditures for home heating. Since it normally takes time for consumers to adjust their buying patterns, the higher fuel costs are likely to be financed partly by a decline in the saving rate.

The fiscal and monetary assumptions for the current year still anticipate early passage of the Carter fiscal package, and thus are quite similar to those shown in the last Greenbook. However, additional assumptions with respect to fiscal policy are

introduced since the projection is now extended into the first half of 1978. For FY 1978, which begins on October 1 of this year, we assume spending of \$459 billion, considerably higher than the \$440 billion budget recently submitted by the outgoing Administration. On the tax side, hikes in payroll taxes for social security and unemployment, presently scheduled for early 1978 are expected to be implemented; these should increase tax revenues by almost \$9 billion during the year.

Our monetary policy assumptions continue to specify a growth path of 5-1/2 per cent for M_1 during the projection period. We expect a rise in interest rates, with upward pressure on short-term rates beginning this spring.

The staff believes that the weather-related output losses during the current quarter will be made up by faster growth in subsequent quarters of 1977. Over the year we now project a 5.9 per cent growth rate in real GNP, virtually unchanged from the projection made last month. Growth in real GNP is expected to be particularly rapid in the second quarter when the rebound from the cold weather shutdowns will coincide with the \$11.4 billion (not at an annual rate) in tax rebates and similar payments to nontaxpayers. Growth of GNP in that quarter is projected to be about 7-3/4 per cent at an annual rate.

During the second half of 1977 real GNP is projected to increase at around a 6 per cent annual rate. The annual rate of

growth of real business fixed investment is expected to average about 10 per cent compared to 6-1/2 per cent during the first half; housing starts are projected to edge up slightly further; and the rate of inventory investment should expand moderately.

During the first half of 1978, real growth is expected to be at about a 5-1/2 per cent annual rate. We expect continued expansion of business fixed and inventory investment and good gains in personal consumption outlays accompanying the associated growth of employment and income. On the basis of these GNP developments, we project the unemployment rate to edge down to the vicinity of 7 per cent by year end and to reach 6.8 per cent by the spring of 1978.

The rate of increase of prices projected for the first quarter of 1977 has been raised slightly, reflecting higher expected prices for fruits and vegetables and some increases in average fuel prices. For the balance of the year, however, our projections of price increases remain essentially unchanged. The fixed-weighted price index for gross business product is expected to increase at an annual rate of 5.7 per cent in the first quarter and to moderate after mid-year to a 5 to 5-1/4 per cent rate of increase.

Details of the staff projection are shown in the tables that follow.

STAFF GNP PROJECTIONS

	Per cent change, annual rate							
	Nominal GNP		Real GNP		Gross business product fixed-weighted price index		Unemployment rate (per cent)	
	1/12/77	2/9/77	1/12/77	2/9/77	1/12/77	2/9/77	1/12/77	2/9/77
1973 ^{1/}	11.6	11.6	5.5	5.5	5.7	5.7	4.9	4.9
1974 ^{1/}	8.2	8.2	-1.7	-1.7	10.2	10.2	5.6	5.6
1975 ^{1/}	7.3	7.3	-1.8	-1.8	9.3	9.3	8.5	8.5
1976 ^{1/}	11.6	11.6	6.1	6.2	4.6	5.2	7.7	7.7
1977	10.6	10.7	4.9	4.9	5.2	5.3	7.5	7.3
1976-III ^{1/}	8.5	8.5	3.9	3.9	4.3	4.3	7.8	7.8
1976-IV ^{1/}	8.8	9.4	2.8	3.0	5.2	5.0	8.0	7.9
1977-I	11.1	9.2	5.0	3.8	5.5	5.7	7.9	7.7
1977-II	11.9	14.1	6.5	7.8	5.4	5.5	7.6	7.4
1977-III	11.9	11.9	6.1	6.0	5.0	5.0	7.3	7.2
1977-IV	12.1	12.4	5.7	5.8	5.0	5.0	7.1	7.1
1978-I		11.3		5.5		5.2		6.9
1978-II		11.2		5.5		5.3		6.7
Change:								
75-IV to								
76-IV ^{1/}	9.9	10.1	5.1	5.1	4.6	4.6	- .5	- .5
76-II to								
77-II	10.1	10.3	4.6	4.6	5.1	5.3	.2	.0
76-IV to								
77-IV	11.8	11.9	5.8	5.9	5.2	5.3	- .9	- .8
77-II to								
78-II		11.7		5.7		5.0		- .7

^{1/} Actual

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GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income
figures are billions of dollars, with quarter figures at annual rates.)

	1976		1977				1978	
	III	IV	Projected				I	II
			I	II	III	IV		
Gross National Product	1709.8	1748.5	1787.5	1847.5	1900.2	1956.5	2009.5	2063.4
Final purchases	1694.7	1740.6	1782.1	1839.1	1887.3	1939.1	1987.1	2036.0
Private	1325.1	1363.8	1397.6	1444.3	1480.4	1519.4	1559.6	1600.1
Excluding net exports	1320.4	1358.6	1398.9	1441.8	1477.6	1515.1	1554.6	1595.6
Personal consumption expenditures	1088.5	1117.5	1147.6	1180.8	1206.3	1233.0	1262.5	1293.0
Goods	599.4	616.7	630.7	650.6	663.6	677.8	693.8	710.8
Services	489.1	500.8	516.9	530.2	542.7	555.2	568.7	582.2
Gross private domestic investment	247.0	249.0	256.7	269.4	284.2	299.5	314.5	330.0
Residential construction	68.9	75.6	81.1	86.1	90.4	94.7	97.7	100.7
Business fixed investment	163.0	165.5	170.2	174.9	180.9	187.4	194.4	201.9
Change in business inventories	15.1	7.9	5.4	8.4	12.9	17.4	22.4	27.4
Nonfarm	15.6	8.9	5.9	8.4	12.9	17.4	22.4	27.4
Net exports of goods and services ^{1/}	4.7	5.2	-1.3	2.5	2.8	4.3	5.0	4.5
Exports	167.7	165.6	168.5	174.7	180.4	186.1	190.9	196.4
Imports	163.0	160.4	169.8	172.2	177.6	181.8	185.9	191.9
Gov't. purchases of goods and services	369.6	376.8	384.5	394.8	406.9	419.7	427.5	435.9
Federal ^{2/}	134.5	138.9	141.3	144.2	149.0	155.1	156.8	159.1
State and local	235.0	238.0	243.2	250.6	257.9	264.6	270.7	276.8
Gross national product in constant (1972) dollars	1272.2	1281.5	1293.5	1318.2	1337.7	1356.8	1375.2	1393.7
Personal income	1386.0	1422.1	1457.0	1508.2	1533.4	1574.2	1612.2	1650.3
Wage and salary disbursements	897.8	921.0	939.2	965.3	989.3	1018.3	1044.1	1069.9
Disposable income	1190.2	1216.9	1245.6	1324.2	1314.2	1347.8	1382.2	1413.8
Saving rate (per cent)	6.4	6.0	5.7	8.7	6.1	6.4	6.5	6.4
Corporate profits with I.V.A. and C.C. Adj.	122.0	121.4	121.4	134.8	145.6	155.4	158.7	167.7
Corporate profits before tax	150.2	157.8	155.4	166.8	175.1	182.4	183.7	191.7
Federal government surplus or deficit (-) (N.I.A. basis)	-57.4	-58.3	-58.2	-103.6	-64.8	-65.8	-62.8	-58.6
High employment surplus or deficit (-)	-9.9	-8.6	-4.6	-53.4	-16.1	-18.3	-15.9	-12.6
State and local government surplus or deficit (-) (N.I.A. basis)	12.7	21.4	20.7	23.2	23.8	24.5	25.8	26.2
Excluding social insurance funds	-.6	7.9	6.9	9.1	9.4	9.8	10.8	10.9
Civilian labor force (millions)	95.3	95.7	95.7	96.3	96.9	97.4	97.9	98.5
Unemployment rate (per cent)	7.8	7.9	7.7	7.4	7.2	7.1	6.9	6.7
Nonfarm payroll employment (millions)	79.7	80.1	80.4	81.0	81.8	82.3	83.0	83.8
Manufacturing	19.0	19.0	19.1	19.4	19.6	19.9	20.2	20.5
Industrial production (1967=100)	130.9	131.7	131.9	135.2	138.0	140.8	143.7	146.8
Capacity utilization: all manufacturing (per cent)	80.8	80.5	80.0	81.4	82.5	83.6	84.7	85.9
Materials (per cent)	81.3	80.4	79.1	80.4	81.5	82.6	83.7	84.9
Housing starts, private (millions, A.R.)	1.59	1.82	1.65	1.85	1.95	2.00	2.00	2.00
Sales new autos, (millions, A.R.)	10.23	9.93	10.25	10.85	11.20	11.35	11.45	11.60
Domestic models	8.61	8.32	8.60	9.15	9.50	9.60	9.70	9.80
Foreign models	1.62	1.62	1.65	1.70	1.70	1.75	1.75	1.80

^{1/} Balance of payments data and projection underlying these estimates are shown in the International Developments section of this part of the Greenbook.

^{2/} Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

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CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1976		1977				1978	
	III	IV	I	II	Projected		I	II
					III	IV		
-----Billions of Dollars -----								
Gross National Product	34.6	38.7	39.0	60.0	52.7	56.3	53.0	53.9
Inventory change	-.9	-7.2	-2.5	3.0	4.5	4.5	5.0	5.0
Final purchases	35.5	45.9	41.5	57.0	48.2	51.8	48.0	48.9
Private	27.9	38.7	33.8	46.7	36.1	39.0	40.2	40.5
Net exports	-4.6	.5	-6.5	3.8	.3	1.5	.7	-.5
Excluding net exports	32.5	38.2	40.3	42.9	35.8	37.5	39.5	41.0
Personal consumption expenditures	23.8	29.0	30.1	33.2	25.5	26.7	29.5	30.5
Goods	9.6	17.3	14.0	19.9	13.0	14.2	16.0	17.0
Services	14.2	11.7	16.1	13.3	12.5	12.5	13.5	13.5
Residential fixed investment	3.6	6.7	5.5	5.0	4.3	4.3	3.0	3.0
Business fixed investment	5.1	2.5	4.7	4.7	6.0	6.5	7.0	7.5
Government	7.6	7.2	7.7	10.3	12.1	12.8	7.8	8.4
Federal	3.3	4.4	2.4	2.9	4.8	6.1	1.7	2.3
State and local	4.1	3.0	5.2	7.4	7.3	6.7	6.1	6.1
GNP in constant (1972) dollars	12.2	9.3	12.0	24.7	19.5	19.1	18.4	18.5
Final purchases	13.2	14.8	13.5	23.0	17.0	16.6	15.5	15.9
Private	11.3	14.5	12.3	19.4	12.7	13.9	14.2	14.2
----- In Per Cent Per Year ^{1/} -----								
Gross National Product	8.5	9.4	9.2	14.1	11.9	12.4	11.3	11.2
Final purchases	8.8	11.3	9.9	13.4	10.9	11.4	10.3	10.2
Private	8.9	12.2	10.3	14.1	10.4	11.0	11.0	10.8
Personal consumption expenditures	9.2	11.1	11.2	12.1	8.9	9.2	9.9	10.0
Goods	6.7	12.1	9.4	13.2	8.2	8.8	9.8	10.2
Services	12.5	9.9	13.5	10.7	9.8	9.5	10.1	9.8
Gross private domestic investment	13.8	3.2	13.0	21.3	23.9	23.3	21.6	21.2
Residential structures	24.3	44.9	32.4	27.0	21.5	20.4	13.3	12.9
Business fixed investment	13.5	6.2	11.9	11.5	14.4	15.2	15.8	16.3
Gov't. purchases of goods & services	8.6	8.1	8.4	11.2	12.8	13.2	7.6	8.1
Federal	10.7	13.6	7.2	8.5	14.0	17.4	4.5	6.0
State and local	7.4	5.1	9.1	12.7	12.2	10.8	9.5	9.3
GNP in constant (1972) dollars	3.9	3.0	3.8	7.8	6.0	5.8	5.5	5.5
Final purchases	4.3	4.8	4.3	7.3	5.3	5.1	4.7	4.7
Private	4.7	5.9	4.9	7.8	5.0	5.4	5.4	5.3
GNP implicit deflator ^{2/}	4.4	6.2	5.2	5.8	5.5	6.2	5.5	5.4
Gross business product fixed-weight price index ^{3/}	4.3	5.0	5.7	5.5	5.0	5.0	5.2	5.3
Personal income	7.2	10.8	10.2	14.8	6.9	11.1	10.0	9.8
Wage and salary disbursements	7.8	10.7	8.1	11.6	10.3	12.3	10.5	10.3
Disposable income	6.2	9.3	9.8	27.7	-3.0	10.6	10.6	9.5
Corporate profits before tax	11.4	21.8	-6.2	32.7	21.5	17.8	2.8	18.5
Nonfarm payroll employment	2.0	2.0	1.5	3.0	4.0	2.5	3.4	3.9
Manufacturing	.0	.0	2.1	6.4	4.2	6.3	6.2	6.1
Industrial production	4.7	2.5	.6	10.4	8.6	8.4	8.4	8.9
Housing starts, private	52.8	71.7	-32.4	58.0	23.4	10.7	.0	.0
Sales new autos	-4.2	-11.2	13.5	25.6	13.5	5.5	3.6	5.3
Domestic models	-12.4	-12.8	14.2	28.1	16.2	4.3	4.2	4.2
Foreign models	55.8	.0	7.6	12.7	.0	12.3	.0	11.9

^{1/} Percentage rates are annual rates compounded quarterly.

^{2/} Excluding Federal pay increases rates of change are: 1976-IV, 5.7 per cent; 1977-I, 5.1 per cent; 1977-IV, 5.6 per cent; 1978-I, 5.4 per cent.

^{3/} Using expenditures in 1972 as weights.

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GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Expenditures and income figures are billions of dollars)

	1970	1971	1972	1973	1974	1975	1976	1977	Projected
Gross National Product	982.4	1063.4	1171.1	1306.6	1413.2	1516.3	1692.4	1872.9	
Final purchases	978.6	1057.1	1161.7	1288.6	1402.5	1531.0	1679.0	1861.9	
Private	759.7	823.4	908.6	1019.1	1099.2	1192.0	1313.2	1460.4	
Excluding net exports	755.8	821.8	911.9	1012.0	1091.7	1171.5	1306.3	1458.3	
Personal consumption expenditures	618.8	668.2	733.0	809.9	887.5	973.2	1078.6	1191.9	
Goods	349.6	374.8	410.5	457.5	497.8	540.8	596.6	655.7	
Services	269.1	293.4	322.4	352.3	389.6	432.4	482.0	536.2	
Gross private domestic investment	140.8	160.0	188.3	220.0	215.0	183.7	241.2	277.4	
Residential construction	36.6	49.6	62.0	66.1	55.1	51.2	67.8	88.1	
Business fixed investment	100.5	104.1	116.8	136.0	149.2	147.1	160.0	178.3	
Change in business inventories	3.8	6.4	9.4	17.9	10.7	-14.6	13.5	11.0	
Nonfarm	3.7	5.1	8.8	14.7	12.2	-17.6	13.6	11.1	
Net exports of goods and services	3.9	1.6	-3.3	7.1	7.5	20.5	6.9	2.1	
Exports	62.5	65.6	72.7	101.6	144.4	148.1	161.9	177.4	
Imports	58.5	64.0	75.9	94.4	136.9	127.6	155.1	175.3	
Gov't. purchases of goods and services	218.9	233.7	253.1	269.5	303.3	339.0	365.8	401.5	
Federal	95.6	96.2	102.1	102.2	111.6	124.4	133.4	147.4	
State and local	123.2	137.5	151.0	167.3	191.6	214.5	232.3	254.1	
Gross national product in constant (1972) dollars	1075.3	1107.5	1171.1	1235.0	1214.0	1191.7	1265.0	1326.5	
Personal income	801.3	859.1	942.5	1052.4	1153.3	1249.7	1375.4	1518.2	
Wage and salary disbursements	546.5	579.4	633.8	701.3	765.0	806.7	890.4	978.0	
Disposable income	685.9	742.8	801.3	901.7	982.9	1080.9	1181.8	1307.9	
Saving rate (per cent)	7.4	7.7	6.2	7.8	7.3	7.8	6.6	6.7	
Corporate profits with I.V.A. and C.C. Adj.	67.9	77.2	92.1	99.1	84.8	91.6	118.7	139.3	
Corporate profits before tax	71.5	82.0	96.2	115.8	127.6	114.5	148.8	169.9	
Federal government surplus or deficit (-) (N.I.A. basis)	-12.1	-22.0	-17.3	-6.7	-11.5	-71.2	-58.3	-73.1	
High employment surplus or deficit (-)	3.0	-5.3	-5.9	-.7	16.8	-17.2	-11.3	-23.1	
State and local government surplus or deficit (-) (N.I.A. basis)	2.8	3.7	13.7	13.0	7.3	6.9	13.9	23.0	
Excluding social insurance funds	-4.0	-3.8	5.6	4.1	-2.8	-5.1	.8	8.8	
Civilian labor force (millions)	82.8	84.1	86.5	88.7	91.0	92.6	94.8	96.6	
Unemployment rate (per cent)	5.0	6.0	5.6	4.9	5.6	8.5	7.7	7.3	
Nonfarm payroll employment (millions)	70.9	71.2	73.7	76.9	78.4	77.0	79.4	81.4	
Manufacturing	19.3	18.6	19.1	20.1	20.0	18.3	19.0	19.5	
Industrial production (1967=100)	107.8	109.6	119.7	129.8	129.3	117.8	129.8	136.5	
Capacity utilization: all manufacturing (per cent)	79.2	78.0	83.1	87.5	84.2	73.6	80.1	81.9	
Materials (per cent)	84.3	83.1	88.0	92.4	87.7	73.6	80.3	80.9	
Housing starts, private (millions, A.R.)	1.43	2.05	2.36	2.05	1.34	1.16	1.56	1.86	
Sales new autos (millions, A.R.)	8.40	10.24	10.93	11.42	8.91	8.66	10.12	10.91	
Domestic models	7.12	8.68	9.32	9.65	7.49	7.08	8.63	9.21	
Foreign models	1.28	1.56	1.61	1.77	1.42	1.58	1.50	1.70	

February 9, 1977

CONFIDENTIAL - FR
CLASS II FOMCCHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1970	1971	1972	1973	1974	1975	1976	Projected 1977
-----Billions of Dollars-----								
Gross National Product	46.9	81.0	107.7	135.5	106.6	103.1	176.1	180.5
Inventory change	-5.6	2.6	3.0	8.5	-7.2	-25.3	28.1	-2.5
Final purchases	52.4	78.5	104.6	126.9	113.9	128.5	148.0	182.9
Private	41.4	63.7	85.2	110.5	80.1	92.8	121.2	147.2
Net exports	2.1	-2.3	-4.9	10.4	.4	13.0	-13.6	-4.8
Excluding net exports	39.3	66.0	90.1	100.1	79.7	79.8	134.8	152.0
Personal consumption expenditures	39.1	49.4	64.8	76.9	77.6	85.7	105.4	113.3
Goods	17.1	25.2	35.7	47.0	40.3	43.0	55.8	59.1
Services	21.9	24.3	29.0	29.9	37.3	42.8	49.6	54.2
Residential fixed investment	-1.3	13.0	12.4	4.1	-11.0	-3.9	16.6	20.3
Business fixed investment	1.6	3.6	12.7	19.2	13.2	-2.1	12.9	18.3
Government	11.0	14.8	19.4	16.4	33.8	35.7	26.8	35.7
Federal	-1.9	.6	5.9	.1	9.4	12.8	9.0	14.0
State and local	12.8	14.3	13.5	16.3	24.3	22.9	17.8	21.8
GNP in constant (1972) dollars	-3.5	32.2	63.6	63.9	-21.0	-22.3	73.3	61.5
Final purchases	2.8	29.9	60.8	56.8	-13.0	-1.8	52.2	64.3
Private	9.3	30.7	57.1	57.4	-16.9	-6.4	49.0	56.0
-----In Per Cent Per Year-----								
Gross National Product	5.0	8.2	10.1	11.6	8.2	7.3	11.6	10.7
Final purchases	5.7	8.0	9.9	10.9	8.8	9.2	9.7	10.9
Private	5.8	8.4	10.3	12.2	7.9	8.4	10.2	11.2
Personal consumption expenditures	6.7	8.0	9.7	10.5	9.6	9.7	10.8	10.5
Goods	5.1	7.2	9.5	11.4	8.8	8.6	10.3	9.9
Services	8.9	9.0	9.9	9.3	10.6	11.0	11.5	11.2
Gross private domestic investment	-3.7	13.6	17.7	16.8	-2.3	-14.6	31.3	15.0
Residential structures	-3.4	35.5	25.1	6.6	-16.7	-7.1	32.5	29.9
Business fixed investment	1.6	3.6	12.3	16.4	9.7	-1.4	8.7	11.4
Gov't. purchases of goods & services	5.3	6.8	8.3	6.5	12.5	11.8	7.9	9.8
Federal	-1.9	.6	6.1	.1	9.2	11.5	7.2	10.5
State and local	11.6	11.6	9.8	10.8	14.5	11.9	8.3	9.4
GNP in constant (1972) dollars	-.3	3.0	5.7	5.5	-1.7	-1.8	6.2	4.9
Final purchases	.3	2.8	5.5	4.9	-1.1	-.1	4.3	5.1
Private	1.1	3.7	6.7	6.3	-1.7	-.7	5.2	5.7
GNP implicit deflator	5.4	5.1	4.1	5.8	10.0	9.3	5.1	5.5
Gross business product fixed weighted price index ^{1/}	4.4	4.4	3.3	5.7	10.2	9.3	5.2	5.3
Personal income	7.4	7.2	9.7	11.7	9.6	8.4	10.1	10.4
Wage and salary disbursements	6.2	6.0	9.4	10.7	9.1	5.5	10.4	9.8
Disposable income	8.8	8.3	7.9	12.5	9.0	10.0	9.3	10.7
Corporate profits before tax	-14.3	14.7	17.3	20.4	10.2	-10.3	30.0	14.2
Nonfarm payroll employment	.7	.4	3.5	4.3	2.0	-1.8	3.1	2.5
Manufacturing	-4.5	-3.6	2.7	5.2	-.5	-8.5	3.8	2.6
Industrial production	-3.0	1.7	9.2	8.4	-.4	-8.9	10.2	5.2
Housing starts, private	-2.7	43.4	15.1	-13.1	-34.6	-13.4	34.5	19.2
Sales new autos	-12.2	21.9	6.7	4.5	-22.0	-2.8	16.9	7.8
Domestic models	-15.8	21.9	7.4	3.5	-22.4	-5.5	21.9	6.7
Foreign models	15.3	21.9	3.2	9.9	-19.8	11.3	-5.1	13.3

^{1/} Using expenditures in 1972 as weights.

FEDERAL SECTOR ACCOUNTS
(Billions of dollars)

	F.R.B. staff estimates													
	Fiscal Year 1976*/1/	FY 1977 e/ 2/		FY 1978 e/		CY 1976* 4/	CY 1977 F.R. Board	Calendar quarters; unadjusted data						
		Admin.	F.R. Board	Admin.	F.R. Board			1977				1978		
								IV*4/	I	II	III	IV	I	II
Unified budget receipts	300.0	354.0	345.0	393.0	395.0	318.5	353.7	76.2	77.7	99.0	92.1	84.8	87.2	118.7
Unified budget outlays	366.5	411.2	415.0	440.0	459.0	374.9	427.2	99.0	97.7	107.0	111.3	111.2	111.8	116.4
Surplus(+)/Deficit(-), unified budget	-66.5	-57.2	-70.0	-47.0	-64.0	-56.4	-73.5	-22.8	-20.0	-8.0	-19.2	-26.4	-24.6	2.3
Surplus(+)/Deficit(-), off-budget agencies 5/	-7.2	-10.8	-10.7	-9.2	-8.6	-5.7	-10.5	.4	-3.9	-1.7	-5.5	.6	-3.7	-1.6
Means of financing combined deficits:														
Net borrowing from public	83.4	62.0	75.1	55.5	71.6	68.9	84.0	17.4	24.1	11.3	22.3	26.3	25.8	2.3
Decrease in cash operating balance	-7.2	n.a.	7.4	n.a.	-5	-3.2	1.7	5.7	-.2	-.1	2.0	--	1.0	-1.5
Other 6/	-2.5	n.a.	-1.8	n.a.	-5	-3.5	-1.6	-.8	--	-1.6	.5	-.5	1.5	-1.5
Cash operating balance, end of period	14.8	n.a.	10.0	n.a.	10.5	11.7	10.0	11.7	11.9	12.0	10.0	10.0	9.0	10.5
Memo: Sponsored agency borrowing 7/	3.4	n.a.	3.3	n.a.	n.a.	2.9	n.a.	.3	.8	1.2	.9	n.a.	n.a.	n.a.
NIA Budget								Seasonally adjusted, annual rates						
Receipts	313.6	360.7	351.3 ^{8/}	405.7	n.a.	330.6	361.7	347.3	354.8	332.9	373.5	385.7	401.0	413.0
Outlays	373.0	419.9	423.4	447.1	n.a.	388.9	434.8	405.6	413.0	436.5	438.3	451.5	463.8	471.6
Purchases	127.2	144.8	143.4	160.0	n.a.	133.5	147.4	138.9	141.3	144.2	149.0	155.1	156.8	159.1
Defense	85.8	94.8	94.3	105.4	n.a.	88.2	97.1	91.3	92.8	94.7	98.3	102.6	103.7	105.1
Non-defense	41.4	50.0	49.1	54.6	n.a.	45.2	50.3	47.6	48.5	49.5	50.7	52.5	53.1	54.0
All other expenditures	245.8	275.1	280.0 ^{8/}	287.1	n.a.	255.4	287.4	266.7	271.7	292.3	289.3	296.4	307.0	312.5
Surplus(+)/Deficit(-)	-59.4	-59.2	-72.0 ^{8/}	-41.4	n.a.	-58.3	-73.1	-58.3	-58.2	-103.6	-64.8	-65.8	-62.8	-58.6
High Employment Surplus(+)/Deficit(-) (NIA basis) 9/	-14.7	n.a.	-20.7	n.a.	n.a.	-11.3	-23.1	-8.6	-4.6	-53.4	-16.1	-18.3	-15.9	-12.6

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- *actual e--estimated r--revised n.e.--not estimated n.a.--not available p--preliminary
- 1/ Revised to include the Export-Import Bank in the unified budget instead of with the off-budget entities. Revised NIA data from The Budget of the U. S. Government, Fiscal Year 1978.
- 2/ Congress' Second Concurrent Resolution on the Budget (September 10, 1976) set receipts at 362.5, outlays at 413.1 and unified deficit at -50.6.
- 3/ The Budget of the U. S. Government, Fiscal Year 1978. 4/ NIA data are preliminary.
- 5/ Includes Federal Financing Bank, Postal Service, U. S. Railway Association, Rural Electrification and Telephone Revolving fund, Housing for the Elderly or Handicapped Funds, and Pension Benefit Guaranty Corporation.
- 6/ Checks issued less checks paid, accrued items and other transactions.
- 7/ Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.
- 8/ Quarterly average exceeds fiscal year total by \$.8 billion for FY 1977 due to spreading of wage base effect over calendar year.
- 9/ Estimated by F.R.B. staff. The high employment budget forecast incorporates the Council of Economic Advisors revised estimates of potential GNP and also fully incorporates taxes on inventory profits beginning 1973.

Comments on the Federal Sector Outlook

Since the last Greenbook, more details of the Carter Administration's fiscal proposals have become available and they have now been incorporated into the staff forecast. These proposals include:

- (1) tax rebates of \$8.2 billion, and special payments to both social security recipients and non-taxpayers totalling \$3.2 billion;
- (2) personal tax reform that substitutes a flat deduction of \$2,400 for single people and \$2,800 for married couples in place of the present set of minimum and maximum standard deductions;
- (3) corporate tax cuts that permit businessmen to choose between an additional 2 per cent investment tax credit (from 10 per cent to 12 per cent) and a refundable tax credit equal to 4 per cent of an employer's share of social security taxes; and
- (4) an increase in grants-in-aid to states and localities--especially for public service jobs, public works, counter-cyclical revenue sharing and manpower training.

Overall the President's program is estimated to cost around \$15-1/2 billion in both fiscal year 1977 and 1978. The new Administration is also expected to make other recommendations for the U.S. Budget later this month.

The staff now forecasts that the fiscal 1977 deficit will total around \$70 billion. Projected receipts have been revised upward from \$343 to \$345 billion, due to a re-estimate of corporate tax payments. Outlays, on the other hand, have been increased by \$1 billion--from \$414 to \$415 billion--due to more information on the Administration's recent proposals.

The above estimates suggest that the combined deficit (unified and off-budget) for this fiscal year will be around \$80 billion. With the completion of the mid-February refunding operation, the Treasury

has already raised a total of \$10.0 billion during the current calendar quarter, including \$9.2 billion from the market. The staff estimates that an additional \$12.6 billion of new cash will be needed to carry the Treasury through the end of the quarter. By the end of March, the Treasury would then have borrowed a net \$35.4 billion for the fiscal year so far, about one-half of its total requirements for the fiscal year ending in September. During the April to June quarter of 1977, tax receipts are expected to be seasonally high and thus we expect that the Treasury's new cash needs will moderate during that period, with total borrowing of only \$11.3 billion. These borrowing estimates imply that the cash balance at the end of June will be \$12.0 billion.

While the size of the President's package in fiscal year 1978 remains about the same as in fiscal year 1977, the components of the program shift substantially (see table on next page). The tax rebates are not continued in fiscal year 1978; consequently, the size of the tax reduction falls from the \$13.7 billion level expected this year to only \$8 billion in fiscal 1978. This decline, however, is offset by a rise--to a \$7.6 billion level--in the President's spending programs.

The staff assumes that fiscal 1978 outlays will total \$459 billion, reflecting not only the President's proposed package but also staff estimates of other outlays, including interest payments--which assumed a constant 4.4 per cent bill rate in the January Budget. Fiscal year 1978 receipts are projected to amount to \$395 billion. This results in a deficit of \$64 billion for FY 1978.

For calendar year 1977, the staff continues to project a \$12 billion increase in the full employment deficit (to a level of \$23 billion), reflecting in part the policy proposals that have been incorporated into the forecast.

Reconciliation of the January Budget's Current Services
Estimates with the Staff's Forecast
(billions of dollars; fiscal years)

	1977	1978
<u>January Budget Receipts</u>		
Under current law, extended	\$360.9	\$407.6
Proposed Reductions (-)--Carter Adm. Total	-10.6	-8.2
Tax Rebate	(-8.2)	(--)
Personal Tax Reform	(-1.5)	(-5.5)
Corporate Tax Cuts	(-0.9)	(-2.7)
Differences due to economic assumptions and tax rates	<u>-5.3</u>	<u>-4.4</u>
<u>Staff Estimate</u>	\$345.0	\$395.0

<u>January Budget Outlays</u>		
Current programs, unchanged	\$411.2	\$445.2
Proposed increases--Carter Adm. Total	4.9	7.6
Payments to OASDI and non-taxpayers	(3.2)	(--)
Expenditure increases for:		
Counter Cyclical Revenue Sharing	(.5)	(.6)
Public Service Jobs	(.7)	(3.4)
Public Works	(.2)	(2.0)
Job Training	(.3)	(1.6)
Higher Interest Payments	0.4	4.6
Other Changes in Expenditure, net	<u>-1.5</u>	<u>1.6</u>
<u>Staff Estimate</u>	\$415.0	\$459.0

DOMESTIC FINANCIAL DEVELOPMENTS

Summary. Following the January FOMC meeting, market interest rates remained under upward pressure for a time, as estimates of future credit demands apparently were raised further in response to continued indications of a strengthening in economic activity. Also, the Treasury announced that it planned to raise significantly more new money in the February refunding and over the first quarter than many in the market had been expecting. More recently, concerns about a near term tightening of monetary policy have been allayed by the apparent slowing in monetary aggregate growth and by the adverse impact on the economy of the persistently severe winter weather. As a result, interest rates have edged lower. Compared with their December lows, short-term rates now are up 12 to 35 basis points, long-term bond yields 10 to 30 basis points, and intermediate-term Treasury yields as much as 75 basis points. Both short- and long-term interest rates, however, still remain generally below levels prevailing in the summer and early fall of last year.

Aggregate demands on credit markets recently have continued to be strong. In addition to the Treasury's expanded financing activity, State and local government issuance of long-term bonds has been exceptionally large. Growth in residential mortgage and consumer instalment credit in December (the latest month for which data are available) was also relatively rapid.

Business demands for funds also have been strong. Publicly offered bonds marketed in January exceeded December's relatively large volume, despite substantial postponements or cancellations near the end of the month resulting from the backup in corporate yields since year-end. Short-term borrowing at banks and in the commercial paper market (net of bankers acceptances) expanded at an average annual rate of about 8.0 per cent over the months of December and January. This is down somewhat from the pace established over October and November when growth was bolstered by substantial inventory accumulation, but it is decidedly stronger than last summer's performance.

Growth of savings deposits and small denomination time deposits at commercial banks slowed significantly in January. The slowing apparently resulted from the higher returns available on market instruments following the late December backup of rates as well as from reductions in deposit offering rates. Deposit inflows at non-bank thrift institutions also moderated in January. Nevertheless, it appears that funds remain readily available in the mortgage market. Outstanding commitments reached a new record level in December, and, though secondary market rates have risen since late December along with bond yields, primary mortgage rates have declined slightly.

Outlook. Given the staff's GNP forecast, overall demands for funds are expected to be sizable in coming months. The staff is estimating that the Treasury still has more than \$19 billion of

new money to raise by mid-April, and additional financing needs are expected to be generated in May by tax rebates and other associated one-time payments now expected to begin in that month. State and local borrowing is also likely to be quite large; the February and March calendars essentially match January's large volume.

Business demands for long-term funds may moderate in coming months, as higher yield levels recently established on such issues may tend to discourage--at least for a time--further aggressive efforts to achieve a lengthening in debt structure. But with growth in corporate profits constrained by recent weather conditions and with upcoming final payments on 1976 tax liabilities large, demands for short-term credit accommodation at banks and in the commercial paper market might well be sustained at around current levels. Household demands for mortgages and consumer instalment credit may moderate over the near term before picking up in the spring.

Given this outlook, it appears that supplies of funds might be adequate to meet credit demands over the near term without the development of significant upward pressures on interest rates. Primary mortgage rates also may remain around present levels, as flows to thrift institutions are likely to remain strong, though perhaps somewhat less so than in the latter part of last year. On into the spring, however, as economic activity accelerates, strengthening demands for money and credit are likely to generate upward pressures on short-term interest rates. Under such conditions, longer-term rates also may begin to move somewhat higher.

INTERNATIONAL DEVELOPMENTS

Summary. Over the past four weeks the dollar has appreciated about 1/3 per cent on a trade-weighted average basis. The dollar rose about 1-1/4 per cent against most Continental European currencies and the Canadian dollar, but declined by almost 2-1/2 per cent against the yen and held steady against sterling,

The most notable development in exchange markets over the past four weeks has been the strong upward pressure on sterling,

. In addition to the on-going arrangements for financing the reduction of official holdings of sterling balances, the U.K. authorities announced they had obtained a \$1.5 billion loan from a group of banks in the Euro-dollar market, of which \$1 billion would be available promptly. The recent strength of sterling probably reflects, in part, the influence of these financial arrangements, and the IMF standby credit, on the markets' view of the ability of the authorities to stabilize the rate. There were also short-term factors in the recent run-up, such as foreign purchases of sterling bond issues with the expectation of quick profits as U.K. interest rates dropped, the withdrawal of U.K. banks from the financing of third-country trade, and the reversal of leads and lags.

. The Mexican peso came under renewed downward pressure in late January and depreciated to 4.5 cents from its previous 5 cent level. Some downward pressure also developed on the Canadian dollar as Canadian interest rates fell and the political situation in Quebec caused some anxiety.

Developments in U.S. international transactions in December included a rise in the trade deficit, sizable net outflows of bank-reported private capital (though less than in November), and large net purchases of foreign securities. For the fourth quarter as a whole the trade deficit rose somewhat to an annual rate of \$13 billion, bringing the deficit for the year to about \$10 billion. Exports in the fourth quarter were up slightly over the third quarter, with a surge in December partly associated with the end of the strike at Ford. Agricultural exports were a little lower than in the third quarter. On the import side, nonfuel imports were up in December, and the fourth quarter total was a little above the third quarter level. Fuel imports remained high, at about the same \$40 billion rate as the third quarter. Inventory building prior to the OPEC price increase, and the effects of colder than normal weather beginning in October, held imports well above the levels that would be associated with normal demand conditions.

Net bank-reported private capital outflows in the fourth quarter were \$4.1 billion, and for the year totaled about \$10 billion --

down from the \$12.8 billion net outflow for 1975. Much of the fourth-quarter outflow was from U.S. offices of foreign banks to their head offices abroad -- perhaps including a sizable amount of temporary borrowing for window-dressing at year end. The U.S. banks did more of their foreign lending out of head offices in the fourth quarter, including over \$1 billion in acceptance financing (mainly to Japan) that may have reflected the withdrawal of U.K. banks from the financing of third-country trade. The large outflow of banking funds from the U.S. in the fourth quarter reflected, apart from these special factors, the relative easing of U.S. money markets. Foreign borrowers, especially Canada and the World Bank, also found market conditions favorable for placing about \$1.7 billion of bonds in the U.S. in December, raising the fourth quarter total to about \$2.6 billion. When the U.S. stock market strengthened in December foreign investors shifted from net selling to moderate net purchases of U.S. equities; for the year as a whole, however, net foreign purchases of U.S. equities (apart from OPEC) were down to \$750 million from over \$3 billion in 1975.

OPEC investments in the U.S. in the fourth quarter may have been \$1.5 billion, a very small part of their investible surplus for the quarter, which may have totaled over \$12 billion. These figures are more than usually conjectural, because very little of that estimated surplus can be identified as yet in available statistics. OPEC assets in sterling did not change significantly in the fourth quarter and placements with international institutions were minor.

Outlook. The U.S. trade and current account deficits are expected to rise sharply in the first quarter, with the trade deficit rising towards \$20 billion at an annual rate, compared with \$13 billion in the fourth quarter of last year. Most of the increase reflects weather-induced fuel imports. The trade deficit should diminish in the course of the year, but is not likely to fall much below \$15 billion through the first half of 1978. The corresponding current account deficit at that time could be about \$4 billion. Some offset to the large trade deficit in the near term may come from reduced outflows of banking funds as interest rates abroad decline relative to U.S. rates. For the year ahead it is still expected that the average value of the dollar will appreciate on the order of 5 per cent. This view is generally consistent with one-year forward exchange rates and projections of relative rates of price inflation.

On balance, foreign economic activity continues to show a lack of vitality. The great divergencies in domestic and international economic performance that created strains last year may be narrowed somewhat if present policies succeed, but imbalances among countries and regions are likely to remain very large.

	1975	1976	1977 ^P	1976				1977 ^P				1978 ^P	
				I	II	III	IV	I	II	III	IV	I	II
Billions of dollars													
Net Exports of Goods and Services (GNP basis of net exports) ^{1/}	16.3 (20.5)	4.3 ^e (6.9)	-.1 (2.1)	3.8 (8.4)	6.6 (9.3)	3.1 (4.7)	3.7 ^e (5.2)	-2.9 (-1.3)	.5 (2.5)	.3 (2.8)	1.5 (4.3)	2.1 (5.0)	1.5 (4.5)
Merchandise Trade Balance (excl. military)	9.0	-9.6	-16.8	-7.0	-5.7	-12.4	-13.0	-19.7	-16.3	-16.3	-15.0	-14.5	-15.1
Exports (excl. military)	107.1	114.5	127.5	107.1	113.5	118.1	119.3	120.9	125.4	129.6	133.9	137.7	142.3
Agricultural	22.2	23.4	22.9	21.2	23.3	25.3	23.7	21.8	22.7	23.3	23.8	23.8	24.3
Nonagricultural	84.8	91.2	104.6	85.9	90.2	92.9	95.6	99.1	102.7	106.3	110.1	113.9	118.0
Imports	98.1	124.1	144.3	114.2	119.2	130.6	132.3	140.6	141.7	145.9	148.9	152.2	157.4
Fuels	28.5	37.0	43.4	31.6	36.4	39.8	40.3	45.6	42.5	43.1	42.2	41.8	43.2
Nonfuels	69.5	87.0	100.9	82.6	82.8	90.8	92.0	95.0	99.2	102.8	106.7	110.4	114.2
Military and Service Transactions, net	7.3	13.9 ^e	16.7	10.9	12.3	15.6	16.7 ^e	16.8	16.8	16.6	16.5	16.6	16.6
Military transactions, net	-9	.6 ^e	1.5	--	-.6	1.5	1.4 ^e	1.4	1.5	1.5	1.6	1.6	1.7
Investment income, net	6.0	10.4 ^e	11.7	9.1	9.8	10.8	11.9 ^e	11.9	11.9	11.6	11.5	11.6	11.6
Other services, net	2.1	2.9 ^e	3.5	1.8	3.1	3.3	3.4	3.5	3.4	3.5	3.4	3.4	3.3
U.S. Current Account Balance ^{2/}	11.7	-.8 ^e	-5.1	-.5	3.0	-4.5	-.8 ^e	-7.8	-4.3	-4.8	-3.5	-3.0	-3.6
Constant (1972) dollars													
Merchandise exports (excl. military) (% change, annual rates)	64.6 (-2.4)	66.4 (2.8)	70.1 (5.6)	63.2 (19.7)	66.4 (22.5)	68.3 (11.7)	67.6 (-4.5)	68.2 (3.2)	69.5 (7.8)	70.6 (6.6)	71.9 (7.8)	72.9 (5.3)	74.2 (7.3)
Merchandise imports (% change, annual rates)	51.3 (-12.5)	62.7 (22.2)	68.4 (9.1)	59.1 (45.9)	60.6 (10.4)	65.4 (35.5)	65.6 (1.4)	68.4 (18.0)	67.5 (-5.3)	68.4 (5.7)	68.8 (2.4)	69.4 (3.6)	70.9 (8.6)
Foreign Outlook - Major Industrial Countries ^{3/}													
Real GNP, % change, annual rate	-1.1	4.7 ^e	3.2	8.1	3.2	1.6	2.9 ^e	2.7	3.6	4.8	5.2	5.3	5.1
Wholesale Prices, % change, A.R. ^{4/}	5.9	9.5 ^e	9.2	11.3	17.0	11.9	6.4 ^e	8.4	8.7	7.8	6.7	6.7	6.3

^{1/} The GNP account excludes from service imports, U.S. Government interest payments to foreigners (\$4.5 billion in 1975), and excludes from exports, military shipments to Israel under cash grant programs (\$340 million in 1975).

^{2/} Includes goods and services plus private and official remittances and pensions and U.S. Government grants.

^{3/} Weighted by the shares of Canada, France, Germany, Italy, Japan and the United Kingdom in the sum of the real GNP of the six countries in dollar terms.

^{4/} Data are largely manufactured goods prices.

^P Projected

^e Estimated