Prefatory Note

The attached document represents the most complete and accurate version available based on original copies culled from the files of the FOMC Secretariat at the Board of Governors of the Federal Reserve System. This electronic document was created through a comprehensive digitization process which included identifying the best-preserved paper copies, scanning those copies,[1] and then making the scanned versions text-searchable.[2] Though a stringent quality assurance process was employed, some imperfections may remain.

Please note that some material may have been redacted from this document if that material was received on a confidential basis. Redacted material is indicated by occasional gaps in the text or by gray boxes around non-text content. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

[2] A two-step process was used. An advanced optical character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

Content last modified 6/05/2009.

Part I

CONFIDENTIAL (FR)

CURRENT ECONOMIC and FINANCIAL CONDITIONS

Summary and Outlook

Prepared for the
Federal Open Market Committee

By the Staff
BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM

December 11, 1974

CONFIDENTIAL (FR)

SUMMARY AND OUTLOOK

By the Staff
Board of Governors
of the Federal Reserve System

December 11, 1974

Summary and Outlook

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary and outlook. Recent statistics indicate that the recession is gathering momentum. Declines in output and employment have been both widespread and deep, and unemployment is rising rapidly. The staff is now estimating a decline in real GNP this quarter at an annual rate of 6.5 per cent, with only about one percentage point attributable to the coal strike. Demands have been particularly weak for consumer goods, especially autos and other durables. In real terms, business fixed investment apparently is declining considerably further, and so is residential construction. Prices and wage rates have continued to increase at a rapid rate. However, there is some evidence of price moderation in commodity markets, and wage rates of late also have risen less rapidly than earlier this year.

In November, industrial production is estimated to have declined at least 2 per cent further. Reductions in output were widespread. In addition to well-publicized cuts in autos, coal, and steel, output was down for business equipment and for a wide range of other goods and materials.

The labor market also showed pronounced deterioration in November. Despite a decline in the labor force, the unemployment rate jumped to 6.5 per cent--the highest rate since October 1961. Nonfarm payroll employment declined by 440,000. Manufacturing was especially weak, with employment and average weekly hours both down sharply.

Since the November survey week, numerous layoffs have been reported in autos and in a wide range of other industries, and initial claims for unemployment compensation remain at very high levels--suggesting a further increase in the unemployment rate this month.

Consumer demands have weakened materially, reflecting in part a further decline in real disposable incomes. Automobile demand has been hit especially hard, with November sales of domestic-type autos--at an annual rate of only 5.7 million units--were down one-third from a year earlier. Sales of foreign cars were also down sharply in November. Demands have also been soft for other consumer durables goods and for nondurable goods. The dollar value of retail sales other than autos was off somewhat in November, implying a further decline in real volume.

Business demands for fixed capital are being cut back. New orders for nondefense equipment have dropped appreciably in recent months, and the latest Commerce survey suggests that real investment outlays will decline in the first half of 1975. With final demands falling rapidly, businesses are making strenuous efforts to cut stocks. Notwithstanding sharp cutbacks in production, auto stocks at the end of November were at record postwar levels, both absolutely and relative to sales. Data are scanty in other sectors, but the staff expects an increase in inventory investment--largely involuntary--this quarter.

The increase in the adjusted hourly earnings index for the private nonfarm economy slowed in October and November, and was 9 per cent above a year earlier. However, the recent coal settlement is reported to be very costly, especially when the full potential cost-of-living adjustment is included.

There is some evidence, also, of slowing in the rate of price increase. Since last April, prices of a number of sensitive industrial materials have declined. More recently, wholesale price increases for intermediate materials have also slowed, but prices have continued up at exceptionally rapid rates for finished products, including machinery. In October, the consumer price index rose 0.9 per cent, to a level 12 per cent above a year earlier. Prices of foods and services were up sharply, but the rise for nonfood commodities has been slower in the past two months than earlier this year.

Outlook. The following monetary and fiscal assumptions underlying the current staff projection differ in some respects from those of four weeks ago. (1) Growth in M_1 is assumed to increase in the first half of 1975 by enough to make up for the shortfall since late summer, and to remain on a 5-3/4 per cent growth path thereafter. In view of the greater weakness now projected for both nominal and real GNP, both short-term and long-term interest rates are assumed to decline further in the first half of 1975 before moving up again. (2) Our estimate of Federal expenditures in fiscal 1975 has been increased to around $307 billion. This is above the Administration's present target of $302 billion because the staff has assumed a larger public employment program and more unemployment compensation payments. Also, expenditures thus far in the fiscal year have been running at a rate consistent with the current staff projection, and the Congress appears unlikely to act on the Administration's proposed expenditure cutbacks. (3) The projection still includes an increase in social security benefits of almost $5 billion, effective July 1, 1975, resulting from the automatic cost-of-living adjustments provided by existing legislation.

The current staff GNP projection is significantly weaker through the first half of 1975 than that of four weeks ago. Real GNP is now shown to decline at an average annual rate of 4-1/2 per cent in the current and following two quarters. An upturn is still projected to begin in the summer of 1975 and to continue through the forecast period to mid-1976, but the recovery is expected to be relatively sluggish.

The weaker outlook in the first half of 1975 is predicated in large part on the assumption that there will be a shift from substantial inventory accumulation this quarter to outright liquidation in the spring of next year. Business fixed investment in real terms is projected to decline throughout the year. Real consumer purchases change little in the first half of the year, and residential construction activity is projected to be bottoming out.

Recovery in the second half of next year is mainly based on the assumption that housing will pick up in response to an earlier build-up in savings inflows to thrift institutions, that real consumer purchases will be moving up along with real disposable incomes, and that the downward adjustment in inventories will be completed.

The unemployment rate is projected to rise to the highest levels of the post-World War II period, even though growth in the civilian labor force is assumed to be quite slow. The projected rise in the unemployment rate is particularly sharp in the first half of next year, when output declines. But unemployment would continue to edge up somewhat further thereafter if recovery in output remains below our long-term potential, as projected.

With output remaining weak throughout the projection period, a somewhat more moderate--but still appreciable--rate of price increase is now anticipated. The rise in the fixed-weighted GNP price index is now shown to slow to an annual rate of around 6-1/2 per cent in the fourth quarter of 1975 and about 5-1/2 per cent in the spring of 1976.

STAFF GNP PROJECTIONS

	Changes in nominal GNP ($ billions)		Per cent change, annual rate: Real GNP		Per cent change, annual rate: Gross private product fixed weighted price index		Unemployment rate (per cent)	
	11/13/74	12/11/74	11/13/74	12/11/74	11/13/74	12/11/74	11/13/74	12/11/74
1971 1/	77.8	77.8	3.3	3.3	4.3	4.3	5.9	5.9
1972 1/	103.1	103.1	6.2	6.2	3.3	3.3	5.6	5.6
1973 1/	136.9	136.9	5.9	5.9	6.3	6.3	4.9	4.9
1974	101.8	102.3	-2.0	-2.0	11.7	11.5	5.6	5.6
1975	97.7	85.1	-2.2	-2.9	10.2	9.6	7.4	7.8
1973-III 1/	31.0	31.0	1.6	1.6	8.4	8.4	4.7	4.7
IV 1/	35.1	35.1	2.3	2.3	9.1	9.1	4.7	4.7
1974-I 1/	14.8	14.8	-7.0	-7.0	14.1	14.1	5.2	5.2
II 1/	25.0	25.0	-1.6	-1.6	12.3	12.3	5.1	5.1
III 1/	27.8	31.6	-2.9	-2.1	14.0	13.8	5.5	5.5
IV	20.9	15.6	-5.5	-6.5	12.7	11.9	6.4	6.5
1975-I	21.0	14.5	-2.5	-4.0	9.7	8.8	6.8	7.3
II	21.0	16.0	-1.9	-3.0	8.3	7.9	7.2	7.7
III	32.0	31.5	1.5	1.0	7.6	7.6	7.6	8.0
IV	36.5	36.5	2.4	2.8	7.0	6.5	7.8	8.1
1976-I	--	33.5	--	3.0	--	5.9	--	8.2
II	--	32.5	--	3.0	--	5.4	--	8.3
Change:								
73-IV to 74-IV	88.5	87.0	-4.3	-4.3	13.3	12.9	1.7	1.8
74-II to 75-II	90.7	77.7	-3.2	-3.9	11.1	10.4	2.1	2.6
74-IV to 75-IV	110.5	98.5	-.1	-.8	8.1	7.7	1.4	1.6
75-II to 76-II	--	134.0	--	2.5	--	6.3	--	.6

1/ Actual.

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.)

	1974		1975				1976	
		Projection						
	III	IV	I	II	III	IV	I	II
Gross National Product	1415.4	1431.0	1445.5	1461.5	1493.0	1529.5	1563.0	1595.5
Final purchases	1406.7	1417.5	1442.5	1466.5	1497.0	1529.5	1560.5	1591.5
Private	1094.4	1097.7	1117.4	1136.1	1158.7	1182.0	1204.5	1227.5
Excluding net exports	1098.4	1099.6	1118.9	1139.4	1164.3	1189.4	1212.9	1235.8
Personal consumption expenditures	901.3	906.2	923.3	940.0	959.7	979.0	997.6	1016.3
Durable goods	136.1	124.0	126.0	127.3	129.8	132.6	135.5	138.3
Nondurable goods	389.0	396.2	402.5	409.3	417.9	426.2	433.9	441.8
Services	376.2	386.0	394.8	403.4	412.0	420.2	428.2	436.2
Gross private domestic investment	205.8	206.9	198.6	194.4	200.6	210.4	217.8	223.5
Residential construction	46.2	41.4	40.1	41.4	44.3	48.1	51.0	53.2
Business fixed investment	150.9	152.0	155.5	158.0	160.3	162.3	164.3	166.3
Change in business inventories	8.7	13.5	3.0	-5.0	-4.0	.0	2.5	4.0
Nonfarm	6.6	12.0	3.0	-5.0	-4.0	.0	2.5	4.0
Net exports of goods and services 1/	-4.0	-1.9	-1.5	-3.3	-5.6	-7.4	-8.4	-8.3
Exports	142.6	146.3	146.5	144.8	144.5	145.1	147.5	151.9
Imports	146.6	148.2	148.0	148.1	150.1	152.5	155.9	160.2
Gov't. purchases of goods and services	312.3	319.8	325.1	330.4	338.3	347.5	356.0	364.0
Federal	117.2	120.0	120.5	120.8	122.3	126.5	130.0	133.5
Defense	78.4	80.3	80.5	80.7	82.1	85.1	86.9	89.4
Other	38.8	39.7	40.0	40.1	40.2	41.4	43.1	44.1
State & local	195.1	199.8	204.6	209.6	216.0	221.0	226.0	230.5
Gross national product in constant (1958) dollars	822.7	809.0	800.8	794.7	796.7	802.2	808.2	814.2
GNP implicit deflator (1958 = 100)	172.0	176.9	180.5	183.9	187.4	190.6	193.4	196.0
Personal income	1168.2	1188.4	1208.7	1228.5	1258.3	1284.3	1307.0	1330.9
Wage and salary disbursements	763.0	773.5	784.9	797.6	814.4	833.2	850.1	865.4
Disposable income	993.1	1009.2	1026.3	1042.0	1068.4	1090.2	1108.8	1128.9
Personal saving	65.5	76.4	76.2	75.0	81.4	83.6	83.2	84.3
Saving rate (per cent)	6.6	7.6	7.4	7.2	7.6	7.7	7.5	7.5
Corporate profits & inventory val. adj.	106.7	99.5	92.4	85.6	89.0	95.2	98.9	103.0
Corporate profits before tax	158.4	148.5	132.5	119.0	118.5	117.5	118.0	119.0
Federal government receipts and expenditures, (N.I.A. basis)								
Receipts	303.5	304.4	304.6	304.4	309.8	314.9	323.6	328.8
Expenditures	304.7	312.8	321.0	325.6	337.3	345.6	353.1	359.8
Surplus or deficit (-)	-1.1	-8.4	-16.4	-21.2	-27.5	-30.7	-29.5	-31.0
High employment surplus or deficit (-) 2/	8.8	14.8	19.7	26.5	26.6	30.0	35.7	39.3
State and local government surplus or deficit (-), (N.I.A. basis)	2.1	2.3	.8	- .1	-2.1	-2.5	-2.9	-3.2
Total labor force (millions)	93.6	94.0	94.2	94.3	94.5	94.7	94.9	95.2
Armed forces "	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
Civilian labor force "	91.4	91.8	92.0	92.1	92.3	92.5	92.7	93.0
Unemployment rate (per cent)	5.5	6.5	7.3	7.7	8.0	8.1	8.2	8.3
Nonfarm payroll employment (millions)	78.7	78.3	77.8	77.5	77.4	77.5	77.6	77.7
Manufacturing	20.1	19.6	18.9	18.5	18.4	18.4	18.4	18.5
Industrial production (1967 = 100)	125.5	122.5	120.9	119.2	119.5	120.6	121.9	123.2
Capacity utilization, mfg. (per cent)	79.2	76.5	74.8	73.1	72.6	72.6	72.7	72.8
Major materials (per cent)	88.3	86.2	82.9	80.2	79.4	79.3	79.5	79.6
Housing starts, private (millions, A.R.)	1.20	1.15	1.15	1.25	1.45	1.55	1.60	1.60
Sales new autos (millions, A.R.)	10.03	7.50	7.75	7.75	8.00	8.50	9.20	9.80
Domestic models	8.48	6.00	6.25	6.25	6.50	7.00	7.50	8.00
Foreign models	1.55	1.50	1.50	1.50	1.50	1.50	1.70	1.80
1/ Net exports of g. & s. (Bal. of Paymts.)	-3.2 3/	-1.1 3/	- .7 3/	-2.5 3/	-4.8	-6.6	-7.6	-7.5
Exports	144.2 3/	147.9 3/	148.1 3/	146.4 3/	146.1	146.7	149.1	153.5
Imports	147.4	149.0	148.8	148.9	150.9	153.3	156.7	161.0

2/ The method of computing this series has been changed; the new method is described in an appendix of Part II.

3/ Includes shipments of military equipment and supplies to Israel which are not included in GNP exports; amounts are: 1974-III, $.3 billion; 1974-IV, $.4 billion; 1975-I and II $.3 billion.

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1974 Proj. III	1974 Proj. IV	1975 Projection I	1975 Projection II	1975 Projection III	1975 Projection IV	1976 Projection I	1976 Projection II
	Billions of Dollars							
Gross National Product	31.6	15.6	14.5	16.0	31.5	36.5	33.5	32.5
Inventory change	-4.8	4.8	-10.5	-8.0	1.0	4.0	2.5	1.5
Final purchases	36.4	10.8	25.0	24.0	30.5	32.5	31.0	31.0
Private	28.5	3.3	19.7	18.7	22.6	23.3	22.5	23.0
Net exports	-2.5	2.1	.4	-1.8	-2.3	-1.8	-1.0	.1
Excluding net exports	31.0	1.2	19.3	20.5	24.9	25.1	23.5	22.9
Personal consumption expenditures	32.2	4.9	17.1	16.7	19.7	19.3	18.6	18.7
Durable goods	6.6	-12.1	2.0	1.3	2.5	2.8	2.9	2.8
Nondurable goods	13.2	7.2	6.3	6.8	8.6	8.3	7.7	7.9
Services	12.4	9.8	8.8	8.6	8.6	8.2	8.0	8.0
Residential fixed investment	-2.6	-4.8	-1.3	1.3	2.9	3.8	2.9	2.2
Business fixed investment	1.5	1.1	3.5	2.5	2.3	2.0	2.0	2.0
Government	7.9	7.5	5.3	5.3	7.9	9.2	8.5	8.0
Federal	2.9	2.8	.5	.3	1.5	4.2	3.5	3.5
State and local	5.0	4.7	4.8	5.0	6.4	5.0	5.0	4.5
GNP in constant (1958) dollars	-4.4	-13.7	-8.2	-6.1	2.0	5.5	6.0	6.0
Final purchases	-1.2	-17.0	-1.8	- .9	2.4	3.9	3.7	4.5
Private	-1.3	-18.6	-1.7	- .6	1.4	2.3	1.9	2.4
	Per Cent Per Year 1/							
Gross National Product	9.5	4.5	4.1	4.5	8.9	10.1	9.1	8.6
Final purchases	11.1	3.1	7.2	6.8	8.6	9.0	8.4	8.2
Private	11.1	1.2	7.4	6.9	8.2	8.3	7.8	7.9
Personal consumption expenditures	15.7	2.2	7.8	7.4	8.7	8.3	7.8	7.7
Durable goods	22.0	-31.1	6.6	4.2	8.1	8.9	9.0	8.5
Nondurable goods	14.8	7.6	6.5	6.9	8.7	8.2	7.4	7.5
Services	14.3	10.8	9.4	9.0	8.8	8.2	7.8	7.7
Gross private domestic investment	-10.9	2.2	-15.1	-8.2	13.4	21.0	14.8	10.9
Residential structures	-19.7	-35.5	-12.0	13.6	31.1	39.0	26.4	18.4
Business fixed investment	4.1	2.9	9.5	6.6	6.0	5.1	5.0	5.0
Gov't. purchases of goods & services	10.8	10.0	6.8	6.7	9.9	11.3	10.1	9.3
Federal	10.5	9.9	1.7	1.0	5.1	14.5	11.5	11.2
Defense	9.7	10.1	1.0	1.0	7.1	15.4	8.7	12.0
Other	12.2	9.6	3.1	1.0	1.0	12.5	17.5	9.6
State and local	10.9	10.0	10.0	10.1	12.8	9.6	9.4	8.2
GNP in constant (1958) dollars	-2.1	-6.5	-4.0	-3.0	1.0	2.8	3.0	3.0
Final purchases	- .6	-8.1	- .9	- .4	1.2	2.0	1.9	2.2
Private	- .8	-10.6	-1.1	- .4	.8	2.3	1.9	2.4
GNP implicit deflator	11.8	11.9 2/	8.4 2/	7.8	7.8	7.0 2/	6.0 2/	5.5
Private GNP fixed weighted index 3/	13.8	11.9	8.8	7.9	7.6	6.5	5.9	5.4
Personal income	12.4	7.1	7.0	6.7	10.1	8.5	7.3	7.5
Wage and salary disbursements	9.9	5.6	6.0	6.6	8.7	9.6	8.4	7.4
Disposable income	11.5	6.6	7.0	6.3	10.5	8.4	7.0	7.5
Corporate profits before tax	68.6	-22.8	-36.6	-34.9	-1.7	-3.3	1.7	3.4
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	22.3	1.2	.3	- .3	7.3	6.7	11.5	6.6
Expenditures	19.2	11.1	10.9	5.9	15.2	10.2	9.0	7.8
Nonfarm payroll employment	1.7	-2.0	-2.5	-1.5	- .5	.5	.5	.5
Manufacturing	- .6	-9.6	-13.5	-8.2	-2.1	0	.0	2.2
Industrial production	.0	-11.4	-5.1	-5.3	1.0	3.8	4.4	4.2
Housing starts, private	-65.4	-15.7	.0	39.6	16.0	30.6	13.5	.0
Sales new autos	41.4	-68.7	14.0	.0	13.5	27.4	37.2	28.8
Domestic models	29.4	-74.9	17.7	.0	17.0	34.5	31.8	29.5
Foreign models	138.3	-12.3	.0	.0	.0	.0	65.0	25.7

1/ Percentage rates are annual rates compounded quarterly.
2/ Excluding Federal pay increases rates of change are: 1974-IV, 11.1 per cent; 1975-I, 8.3 per cent; 1975-IV, 6.5 per cent; and 1976-I, 5.9 per cent.
3/ Using expenditures in 1967 as weights.

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.)

	1969	1970	1971	1972	1973	1974 ---Projected---	1975
Gross National Product	930.3	977.1	1054.9	1158.0	1294.9	1397.3	1482.4
Final purchases	922.5	972.6	1048.6	1149.5	1279.6	1384.1	1483.9
Private	712.5	753.1	814.4	893.8	1003.2	1075.9	1148.6
Excluding net exports	710.6	749.5	814.6	899.8	999.3	1074.9	1153.0
Personal consumption expenditures	579.5	617.6	667.1	729.0	805.2	879.3	950.5
Durable goods	90.8	91.3	103.9	118.4	130.3	128.4	128.9
Nondurable goods	245.9	263.8	278.4	299.7	338.0	381.4	414.0
Services	242.7	262.6	284.8	310.9	336.9	369.6	407.6
Gross private domestic investment	139.0	136.3	153.7	179.3	209.4	208.8	201.0
Residential construction	32.6	31.2	42.8	54.0	57.2	46.2	43.5
Business fixed investment	98.5	100.6	104.6	116.8	136.8	149.4	159.0
Change in business inventories	7.8	4.5	6.3	8.5	15.4	13.2	-1.5
Nonfarm	7.7	4.3	4.9	7.8	11.4	10.6	-1.5
Net exports of goods and services 1/	1.9	3.6	- .2	-6.0	3.9	1.0	-4.5
Exports	55.5	62.9	65.4	72.4	100.4	139.7	145.2
Imports	53.6	59.3	65.6	78.4	96.4	138.7	149.7
Gov't. purchases of goods and services	210.0	219.5	234.2	255.7	276.4	308.2	335.3
Federal	98.8	96.2	97.6	104.9	106.6	115.8	122.5
Defense	78.4	74.6	71.2	74.8	74.4	77.8	82.1
Other	20.4	21.6	26.5	30.1	32.2	38.0	40.4
State & local	111.2	123.3	136.6	150.8	169.8	192.5	212.8
Gross national product in constant (1958) dollars	725.6	722.5	746.3	792.5	839.2	822.3	798.6
GNP implicit deflator (1958 = 100)	128.2	135.2	141.4	146.1	154.3	170.0	185.6
Personal income	750.9	808.3	864.0	944.9	1055.0	1150.9	1245.0
Wage and salary disbursements	509.7	542.0	573.0	626.8	691.7	752.3	807.5
Disposable income	634.4	691.7	746.4	802.5	903.7	979.9	1056.7
Personal saving	38.2	56.2	60.5	52.6	74.4	74.5	79.1
Saving rate (per cent)	6.0	8.1	8.1	6.6	8.2	7.6	7.5
Corporate profits & inventory val. adj	79.8	69.2	78.7	92.2	105.1	104.9	90.6
Corporate profits before tax	84.9	74.0	83.6	99.2	122.7	145.3	121.9
Federal government receipts and expenditures, (N.I.A. basis)							
Receipts	197.3	192.0	198.5	227.2	258.5	293.7	308.4
Expenditures	189.2	203.9	220.3	244.7	264.2	297.5	332.4
Surplus or deficit (-)	8.1	-11.9	-21.9	-17.5	-5.6	-3.8	-24.0
High employment surplus or deficit (-) 2/	8.8	6.2	2.6	-3.4	1.9	10.5	25.7
State and local government surplus or deficit (-), (N.I.A. basis)	.7	1.8	3.4	12.3	9.2	2.4	-1.0
Total labor force (millions)	84.2	85.9	86.9	89.0	91.0	93.3	94.4
Armed forces "	3.5	3.2	2.8	2.4	2.3	2.2	2.2
Civilian labor force "	80.7	82.7	84.1	86.5	88.7	91.1	92.2
Unemployment rate (per cent)	3.5	4.9	5.9	5.6	4.9	5.6	7.8
Nonfarm payroll employment (millions)	70.4	70.9	71.2	73.7	76.8	78.3	77.6
Manufacturing	20.2	19.3	18.6	19.1	20.1	20.0	18.6
Industrial production (1967 = 100)	110.7	106.7	106.8	115.2	125.6	124.6	120.1
Capacity utilization, mfg. (per cent)	86.5	78.3	75.0	78.6	83.0	79.1	73.3
Major materials (per cent)	90.0	86.2	85.3	89.6	93.0	88.7	80.4
Housing starts, private (millions, A.R.)	1.47	1.43	2.05	2.36	2.05	1.39	1.35
Sales new autos (millions, A.R.)	9.57	8.40	10.24	10.93	11.44	8.94	8.00
Domestic models	8.46	7.12	8.68	9.32	9.67	7.48	6.50
Foreign models	1.11	1.28	1.56	1.61	1.77	1.46	1.50
1/ Net exports of g. & s. (Bal. of Paymts.)	1.3	2.9	- .2	-6.0	4.4 3/	1.8 3/	-3.9 3/
Exports	55.0	62.3	65.4	72.4	101.0 3/	141.3 3/	146.6 3/
Imports	53.6	59.4	65.6	78.4	96.6	139.5	150.5

2/ The method of computing this series has been changed; the new method is described in an appendix of Part II.

3/ Includes shipments of military equipment and supplies to Israel which are not included in GNP exports; amounts are 1973, $.6 billion; 1974, $.325 billion; and 1975, $.150 billion.

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1969	1970	1971	1972	1973	Projected 1974	Projected 1975
	---Billions of Dollars---						
Gross National Product	66.1	46.8	77.8	103.1	136.9	102.3	85.1
Inventory change	.7	-3.3	1.8	2.2	6.9	-2.2	-14.7
Final purchases	65.4	50.1	76.0	100.9	130.1	104.5	99.8
Private	55.0	40.6	61.3	79.4	109.4	72.7	72.7
Net exports	- .6	1.7	-3.8	-5.8	9.9	-2.9	-5.5
Excluding net exports	55.6	38.9	65.1	85.2	99.5	75.6	78.1
Personal consumption expenditures	43.3	38.1	49.6	61.8	76.2	74.1	71.2
Durable goods	6.8	.5	12.6	14.5	11.9	-1.9	.5
Nondurable goods	15.1	17.9	14.6	21.6	38.3	43.4	32.6
Services	21.4	19.9	22.2	26.1	26.0	32.7	38.0
Residential fixed investment	2.5	-1.4	11.6	11.2	3.2	-11.0	-2.7
Business fixed investment	9.7	2.1	4.0	12.2	20.0	12.6	9.6
Government	10.4	9.5	14.7	21.5	20.7	31.8	27.1
Federal	.0	-2.6	1.4	7.3	1.7	9.2	6.7
State and local	10.4	12.1	13.3	14.2	19.0	22.7	20.3
GNP in constant (1958) dollars	19.0	-3.1	23.8	46.2	46.7	-16.9	-23.7
Final purchases	18.7	- .4	-22.5	-44.4	43.0	-14 1	-13 9
Private	20.6	6.2	18.5	46.1	45.2	-16.0	-15.4
	---Per Cent Per Year 1/---						
Gross National Product	7.6	5.0	8.0	9.8	11.8	7.9	6.1
Final purchases	7.6	5.4	7.8	9.6	11.3	8.2	7.2
Private	8.4	5.7	8.1	9.7	12.2	7.2	6.8
Personal consumption expenditures	8.1	6.6	8.0	9.3	10.5	9.2	8.1
Durable goods	8.1	.6	13.8	14.0	10.1	-1.5	.4
Nondurable goods	6.5	7.3	5.5	7.7	12.8	12.8	8.5
Services	9.7	8.2	8.5	9.2	8.4	9.7	10.3
Gross private domestic investment	10.3	-1.9	12.8	16.7	16.8	- .3	-3.7
Residential structures	8.3	-4.3	37.2	26.2	5.9	-19.2	-5.8
Business fixed investment	10.9	2.1	4.0	11.7	17.1	9.2	6.4
Gov't. purchases of goods & services	5.2	4.5	6.7	9.2	8.1	11.5	8.8
Federal	.0	-2.6	1.5	7.5	1.6	8.6	5.8
Defense	.1	-4.8	-4.6	5.1	- .5	4.6	5.5
Other	- .5	5.9	22.7	13.6	7.0	18.0	6.3
State and local	10.3	10.9	10.8	10.4	12.6	13.4	10.5
GNP in constant (1958) dollars	2.7	- .4	3.3	6.2	5.9	-2.0	-2.9
Final purchases	2.7	- .1	3.1	6.0	5.5	-1 7	-1.7
Private	3.7	1.1	3.9	6.7	6.5	-2 3	-2.3
GNP implicit deflator	4.8	5.5	4.6	3.4	5.6	10.2	9.2
Private GNP fixed weighted index 2/	4.7	4.8	4.3	3.3	6.3	11.5	9.6
Personal income	9.0	7.6	6.9	9.4	11.7	9.1	8.2
Wage and salary disbursements	9.6	6.3	5.8	9.3	10.4	8.8	7.3
Disposable income	7.3	9.0	7.9	7.5	12.6	8.4	7.8
Corporate profits before tax	-3.1	-12.8	13.0	18.7	23.7	18.4	-16.1
Federal government receipts and expenditures (N.I.A. basis)							
Receipts	12.7	-2.7	3.4	14.5	13.8	13.6	5.0
Expenditures	4.2	7.8	8.0	11.1	8.0	12.6	11.7
Nonfarm payroll employment	3.7	.7	.4	3.5	4.2	2.0	- .9
Manufacturing	2.0	-4.1	-4.0	2.8	5.0	- 5	-7.0
Industrial production	4.7	-3.6	.1	7.9	9.0	- 8	-3 6
Housing starts, private	-2.7	-2.3	43.2	14.9	-13.2	-32.2	-2.9
Sales new autos	- .6	-12.3	21.9	6.7	4.7	21.9	-10.5
Domestic models	-1.8	-15.9	21.9	7.4	3.7	-22.6	-13.1
Foreign models	9.0	15.5	21.8	3.3	9.8	-17.5	2.7

1/ Percentage rates are annual rates compounded quarterly.
2/ Using expenditures in 1967 as weights.

DOMESTIC FINANCIAL SITUATION

Summary. Short-term market interest rates rose 1/4 to close to a full percentage point in the last half of November as the Federal funds rate, after several weeks of decline, stabilized in a 9-3/8 to 9-1/2 per cent range, thus eroding the widespread expectation of further monetary policy ease. In the last few days, however, short-term market interest rates declined substantially as the Federal funds rate dropped to below 9 per cent and the discount rate was lowered to 7-3/4 per cent. At this writing, short-term yields are about equal to (and, in the case of the bill rate, below) their levels at the time of the last Committee meeting. Corporate bond rates--which had increased 60 basis points--have also declined most recently, but remain above their mid-November levels, while municipal bond rates have continued to increase.

The prime rate at commercial banks, which has been adjusting to market rates with a lag, declined only a further one-fourth point since the last Committee meeting, and at a level of 10-1/2 per cent at most banks, still remained high relative to the commercial paper rate. As a result, prime borrowers continued to rely heavily on the commercial paper market. Total short-term borrowing at banks and in the commercial paper market expanded at about an 11 per cent rate--somewhat below the already reduced average of the previous three months.

Banks apparently are continuing to be cautious lenders. The November Lending Practices Survey confirms that bank lending policies--both rate and non-rate--are remaining restrictive. With increases in loans and securities continuing modest, expanded inflows of demand and small-denomination time and savings deposits were again used by banks in November to reduce CD's. In late November and early December, however, the New York City banks did step-up CD and Euro-dollar borrowings, apparently to finance loan growth late in November and to position themselves for CD maturities and tax-loan demands in mid-December.

The thrift institutions, like commercial banks, apparently used their increased deposit inflows in November in large part to rebuild liquidity and repay debt. There are no indications yet of a significant turnaround in new mortgage commitment activity by these institutions. But, in lagged response to declines in market yields, and a more optimistic view as to future savings inflows on the part of lenders, average rates on home mortgages declined in the primary market another 10 basis points, and in the secondary market by 20 basis points. Since the peaks of early fall, primary market rates have dropped a total of about 30 basis points, and secondary market yields almost one full percentage point.

Manufacturing corporations and public utilities continued to borrow heavily in the bond markets during November, with only a modest amount of postponements resulting from rate increases after mid-month. In the tax-exempt bond markets, however, the continued large November offerings, the light demands of banks and casualty companies, and a large New York city issue, contributed to more difficult market conditions and a build-up in dealer inventories.

In the Treasury market, $5 billion of new bills offered for cash in November were readily absorbed. The Fed and foreign accounts purchased about $1-1/2 billion of bills. Agency borrowing, on balance, remained about unchanged in November.

Outlook. Credit demands are expected to moderate in the months ahead as economic activity weakens further. However, borrowing is likely to remain relatively large in the corporate bond market, as corporations are expected to continue borrowing to restructure balance sheets and to cover a still large external financing gap. Nevertheless, such financings are likely to be below the $4 billion monthly average pace of the fourth quarter. With Government expenditures now projected higher than in the last Greenbook, Treasury borrowing will also be larger than seasonal in the first quarter, though only about half as large as the fourth quarter. As the position of thrift institutions continues to improve, outstanding agency debt can be expected to decline.

In the first quarter of 1975, reduced inventory accumulation and general working capital requirements, as well as the large volume of capital market financing, are expected to lead to further moderation of business short-term credit demands. Banks, with their inflows of consumer-type time and savings deposits and demand deposits remaining relatively high, are unlikely to be aggressive issuers of CD's or borrowers of Euro-dollars. Bank lending terms should tend to ease, but--as a result of concerns about credit quality--lending standards may remain relatively stringent. This suggests that banks are likely to step-up their portfolio investment purchases soon, but reduced needs for tax-exempt income may limit acquisitions of State and local bonds. Difficulties of casualty insurance companies--resulting primarily from large underwriting losses and declining equity prices--may also reduce their demands for tax-exempt bonds in the months ahead, suggesting that

State and local bond markets may not share fully the expected decline in bond yields.

Thrift institutions, with deposit inflows rising, can be expected to increase their new commitment activity in the residential mortgage market. However, these institutions--absent a change in FHLBB policy--will continue to divert a portion of inflows to debt repayment and portfolio liquidity. Such actions will tend to moderate the pace of decline of average mortgage rates in the primary market. Consumer credit expansion is also expected to remain weak, in line with expectations of modest consumer expenditures, particularly on durables. And, in this market, too, lender caution is tending to moderate credit flows.

Thus, the weakening in credit demands that appears to be in prospect suggests that interest rates will continue to trend downward. Expected sizable corporate bond volume, and investor concerns about inflation, suggest that rate declines are likely to be smaller in long-term markets than in short-term markets.

INTERNATIONAL DEVELOPMENTS

Summary and outlook. The period of general weakness of the dollar in foreign exchange markets, that began in mid-September, continued into early December. During the past twelve weeks the dollar has lost about 3-1/4 per cent of its foreign exchange value on a weighted average basis. Recent upward pressure on the German mark and the Swiss franc partly explains the weakening of the dollar at this particular time. Heavy sales of dollars by the central banks of the United Kingdom and Italy, as they intervened to moderate downward pressures on their currencies, also were a contributing factor. As a result, the exchange value of the dollar declined during the past month against all major European currencies except the pound sterling and the Italian lira.

The combination of recent declines in interest rates, unsettled exchange markets and anticipation of large gold purchases by U.S. residents, once such purchases become legal at the turn of the year, contributed to a rise in the price of gold from $155 per ounce between early August and mid-October to a peak of $190 in mid-November. With the announcement early this month that the Treasury would auction 2 million ounces of gold in early January, gold prices came down sharply, but briefly, and then recovered to hold around $180.

In October no marked changes occurred in the various components of the U.S. balance of payments. Liabilities to foreign official institutions rose in October, as in September, by about $1 billion, mainly to OPEC countries. Preliminary data for November show a similar increase.

The net inflow of bank-reported private capital amounting to about $1/2 billion in October, was somewhat below the monthly average inflow in the third quarter. Liquid liabilities to commercial banks abroad rose slightly in October and lending to foreigners reported through banks changed only little. Some short-term loans were repaid by countries, such as Japan, which received funds directly from OPEC countries, but these repayments were offset by an increase in long-term lending to Europe.

Private security transactions in October were dominated by sizable U.S. purchases of newly issued Canadian bonds. The volume of such purchases probably declined in November, but indications are that they are likely to be very sizable again in December. Transactions with foreigners in outstanding U.S. securities were more or less in balance as foreign holders moved out of U.S. stocks and into bonds.

The U.S. trade deficit declined during September and October, dropping from the third quarter annual rate (seasonally adjusted) of

$10.3 billion to $4.3 billion in September-October. This improvement may well reflect some correction to the especially high August deficit, so that the trade deficit over the next several months is likely to stabilize at a rather higher level than that recorded in September-October.

Imports of finished goods are declining in line with declining domestic demand. The weakening cyclical situation in other countries is reflected in some moderation in the rate of price increase for imports of industrial materials, but the volume of such imports has remained high. On the export side, shipments of capital goods abroad also have remained high, reflecting relatively high, though not growing, order books. The physical volume of exports of industrial materials has fallen since early summer, but the nominal value has declined only little because of continued rises in prices. With the continuing weak business situation here and abroad, the growth of both imports and exports is likely to decline, leaving the trade balance at a deficit of about $7-8 billion over the next few quarters.

Economic conditions in foreign countries have weakened further in recent weeks. Unemployment is rising sharply in a number of countries, investment intentions are falling off, inventories of finished goods are building up, while those at earlier stages in the production process are being worked down. In view of these developments, policies abroad are shifting toward checking the increase in idle resources. The German, Dutch, Canadian, British and Australian governments have each adopted stimulative measures. These include fiscal measures to encourage business investment and aid the construction industry in Canada, the United Kingdom and Australia, and fiscal measures increasing personal incomes in Germany and the Netherlands. Further measures aiming at strengthening private and public investment in Germany are expected to be announced this week. In addition, monetary policy in most of these countries has become more accommodating albeit not clearly expansionary.

Other governments, fearing that inflationary expectations are still strong and in some cases under added constraint from their external positions, are maintaining their restrictive postures. Nevertheless, it appears that virtually all major countries will have adopted some reflationary measures by early spring. But the timing and strength of any general upturn in economic activity abroad next year remains very uncertain.