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CONFIDENTIAL (FR)

October 13, 1976

SUMMARY AND OUTLOOK

By the Staff  
Board of Governors  
of the Federal Reserve System

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## **SUMMARY AND OUTLOOK**

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DOMESTIC NONFINANCIAL DEVELOPMENTS

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Summary. The lull in the pace of business expansion continued into September. Gains in employment remained moderate, and industrial production apparently changed little. Prospects remain favorable, however, for stronger growth later this year and in 1977. Consumer demand appears to be firming, and the outlook for business capital spending is still good. And underlying inflationary pressures do not appear to have worsened, despite a surge in wholesale prices in September.

Industrial production apparently remained about unchanged in September. The beginning of the Ford strike at mid-month affected mainly the output of consumer durables--which declined sharply. Production of business equipment apparently rose only slightly last month, following moderate gains recently, and materials output showed a small increase, reflecting in part the post-strike rebound of rubber production and coal.

Demand for labor continued moderate last month, with a gain in payroll employment of under 150,000 after adjustment for the number of workers on strike. In addition, the August increase was revised down by half, to 100,000. The length of the factory workweek declined again in September--largely because of the effects of the Ford strike which began in the middle of the survey week. The unemployment rate edged off by one-tenth to 7.8 per cent, returning to its July level.

Consumer demand appears to have developed a better tone. Excluding autos and building equipment, retail sales rose by 0.8 per cent in September, about equal to the downward revised August increase. For the third quarter as a whole, these sales were up 1.7 per cent, somewhat better than the second quarter performance. Sales at the GAF group of stores were particularly strong, rising by 3.3 per cent last quarter after declining slightly in the second quarter. The Michigan survey reported an improvement in consumer attitudes in late August and early September.

Unit auto sales dropped last month, however, to an 8.2 million annual rate for domestic units--down from 8.9 million in August. Most of the decline occurred in the last 10 days of September and could reflect the timing of new model introductions and its effect on the seasonals. Foreign car sales picked up in September to a 1.8 million annual rate--the highest since February 1975.

Businessmen are still struggling to keep inventories under tight control. The book value of manufacturers' stocks rose at an \$11 billion annual rate in August--about the same as in July, and for the second quarter as a whole. Most of the accumulation was in nondurable goods, and the inventory-sales ratio rose slightly for nondurable manufacturers. Inventories held by merchant wholesalers rose at a \$5.3 billion annual rate in August in book value terms, somewhat more than in July.

The outlook for business fixed capital spending remains generally good, although somewhat less expansive than it appeared a month or two ago. Contracts for commercial and industrial building declined in both July and August, and the August decline in new orders for nondefense capital goods erased the strong July gain. Most of the July increase and August decline in these orders occurred in one sector of transportation equipment; excluding this component, capital goods orders remain above the June level. A preliminary tabulation of the confidential Edie capital spending survey for 1977, taken in September, indicates a rise of about 14 per cent--somewhat less spending than we had been expecting.

A somewhat better tone has developed in the housing industry recently. Starts rebounded in August, with a marked recovery in the multifamily sector. Moreover, residential building permits rose 7 per cent further to their highest rate in 2-1/2 years. The outlook for residential construction activity has also been enhanced by a further increase in mortgage commitments.

Federal government spending in the third quarter fell short of expectations contributing to some extent to the sluggishness of the overall recovery, and growth in State and local expenditures also slowed. The reasons for the shortfall in Federal outlays are not clear at this juncture.

Consumer prices have continued to rise at about a 6 per cent annual rate recently--with increases in food prices relatively small and those in the energy sector relatively large. The rise of wholesale prices accelerated in September to an 11 per cent annual rate, with both food and industrial prices up strongly. Energy prices rose sharply, as did prices of machinery and metal products--the latter reflecting in part steel price increases announced earlier this year. Underlying pressures on prices do not appear to have intensified, however. In particular, wage increases continue moderate relative to the very high rates of recent years. From the second to the third quarter, the average hourly earnings index rose at an annual rate of 5-3/4 per cent.

Outlook. The staff projection of real GNP growth has been shaded downward because the prolonged period of sluggish expansion appears likely to induce greater caution in business spending. The recovery process, however, remains basically sound, and a pick-up in the pace of activity is anticipated relatively soon.

The policy assumptions underlying the current projection have been changed only in minor respects. The shortfall of Federal budget outlays relative to earlier expectations has led to some downward adjustment in projected fiscal year totals--for FY 1977, we now project a \$408 billion level of Federal spending, down from \$410 billion last month.

In the monetary area, we continue to assume a 5-3/4 per cent growth rate of  $M_1$  during the projection period; the base period for the monetary ranges has been moved forward to the third quarter of 1976. Interest rate projections have again been revised downward, but a rise in short-term rates beginning early next year is still envisaged.

With respect to energy prices, we had previously assumed a \$1.00 per barrel increase in crude oil to be announced by OPEC in December. Based largely on statements by OPEC members, we now assume an increase of \$1.75--or nearly 15 per cent. Allowing for adjustments in the prices of competing domestic fuels, the over-all impact on the domestic price level of the \$1.75 increase is estimated to be about 0.6 per cent by late 1977. Some additional upward pressure on prices would continue into 1978 as adjustments are made in long-term contracts for natural gas and coal and as wage levels are affected.

We now estimate real GNP growth during the quarter just ended at 3.3 per cent, annual rate, down from the 4.0 per cent projected in the last Greenbook. We still anticipate a return to larger real GNP gains in the fourth quarter and through 1977. We assume that consumer outlays will continue to move upward at a reasonable pace; moderate gains in residential construction are likely over the next several quarters, and business fixed investment seems clearly on the increase. We also anticipate Federal outlays

to return close to earlier projected rates of growth, following the third quarter slowdown.

The anticipated vigor of economic expansion in 1977 has been damped somewhat, however, by the extended adjustment of production to rising inventories. Purchasing power has been lost, and some uncertainty has been created in the business community. We have therefore reduced our projected rate of expansion in real GNP during the next 5 quarters to slightly under 5 per cent annual rate--about half a per cent under that of last month's Greenbook. Such a rate of expansion would still imply a decline in the unemployment rate--to 6.8 per cent by the fourth quarter of 1977.

Our price projection this month reflects the impact of the larger price hike assumed for imported oil. The fixed-weighted price index for gross business product is now expected to rise at a 5-1/2 per cent annual rate in the second half of 1977--rather than the approximately 5 per cent rate projected last month.

Details on the staff projections are shown in the tables that follow.

## STAFF GNP PROJECTIONS

	Changes in nominal GNP (\$ billions)		Per cent change, annual rate				Unemployment rate (per cent)	
			Real GNP		Gross business product fixed-weighted price index			
	9/15/76	10/13/76	9/15/76	10/13/76	9/15/76	10/13/76	9/15/76	10/13/76
1973 <u>1/</u>	135.5	135.5	5.5	5.5	5.7	5.7	4.9	4.9
1974 <u>1/</u>	106.6	106.6	-1.7	-1.7	10.2	10.2	5.6	5.6
1975 <u>1/</u>	103.1	103.1	-1.8	-1.8	9.3	9.3	8.5	8.5
1976	179.8	178.2	6.3	6.2	4.9	4.8	7.5	7.6
1977	186.4	178.6	5.2	4.7	5.2	5.3	6.8	7.0
1976-I	48.0	48.0	9.2	9.2	3.7	3.7	7.6	7.6
1976-II	37.9	39.0	4.3	4.5	5.2	5.2	7.4	7.4
1976-III	37.7	34.4	4.0	3.3	5.4	5.0	7.8	7.8
1976-IV	50.3	47.4	5.7	5.1	5.4	5.4	7.4	7.5
1977-I	48.0	46.6	5.4	5.0	5.4	5.1	7.1	7.2
1977-II	45.7	42.3	5.2	4.8	5.1	5.1	6.9	7.0
1977-III	50.1	49.7	5.2	4.9	5.1	5.5	6.7	6.9
1977-IV	52.3	51.9	5.2	4.9	5.1	5.5	6.6	6.8
Change:								
75-II <u>1/</u> to								
76-II	191.8	192.9	7.0	7.0	5.6	5.6	-1.3	-1.3
75-IV <u>1/</u> to								
76-IV	173.9	168.8	5.8	5.5	4.9	4.8	-1.1	-1.0
76-II to								
77-II	181.7	170.7	5.1	4.5	5.3	5.2	-.5	-.4
76-IV to								
77-IV	196.1	190.5	5.3	4.9	5.2	5.3	-.8	-.7

1/ Actual

October 13, 1976

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CLASS II FOMCGROSS 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			
	I	II	III	IV	Projected			
	I	II	III	IV	I	II	III	IV
Gross National Product	1636.2	1675.2	1709.6	1757.0	1803.6	1845.9	1895.6	1947.5
Final purchases	1621.4	1659.2	1695.6	1742.0	1787.6	1828.4	1877.9	1929.0
Private	1266.7	1297.2	1326.5	1362.6	1399.0	1432.5	1473.8	1514.1
Excluding net exports	1258.3	1287.9	1318.4	1353.7	1389.6	1426.4	1463.1	1500.8
Personal consumption expenditures	1043.6	1064.7	1086.9	1113.4	1139.9	1167.4	1194.9	1222.6
Goods	580.5	589.8	601.3	615.8	630.3	645.3	660.3	675.5
Services	463.2	474.9	485.6	497.6	509.6	522.1	534.6	547.1
Gross private domestic investment	229.6	239.2	245.5	255.3	265.7	276.5	285.9	296.7
Residential construction	61.3	65.3	68.3	71.6	75.0	77.4	79.1	80.6
Business fixed investment	153.4	157.9	163.2	168.7	174.7	181.6	189.1	197.6
Change in business inventories	14.8	16.0	14.0	15.0	16.0	17.5	17.7	18.5
Nonfarm	12.7	17.3	14.5	15.0	16.0	17.5	18.2	19.0
Net exports of goods and services <sup>1/</sup>	8.4	9.3	8.1	8.9	9.4	6.1	10.7	13.3
Exports	154.1	160.3	168.3	170.7	175.8	182.1	187.8	193.4
Imports	145.7	151.0	160.2	161.8	166.4	176.0	177.1	180.1
Gov't. purchases of goods and services	354.7	362.0	369.1	379.4	388.6	395.9	404.1	414.9
Federal <sup>2/</sup>	129.2	131.2	133.7	137.8	140.4	142.0	144.4	149.1
State and local	225.5	230.9	235.4	241.6	248.2	253.9	259.7	265.8
Gross national product in constant (1972) dollars	1246.3	1260.0	1270.1	1285.9	1301.8	1317.0	1332.9	1348.9
Personal income	1331.3	1362.0	1392.5	1427.8	1461.2	1491.4	1524.8	1560.6
Wage and salary disbursements	861.5	881.1	897.1	922.3	945.3	967.1	988.2	1015.4
Disposable income	1147.6	1172.5	1198.0	1227.8	1255.9	1281.1	1308.9	1338.7
Saving rate (per cent)	6.9	7.1	7.1	7.2	7.2	6.8	6.7	6.7
Corporate profits with I.V.A. and C.C. Adj.	115.1	116.4	118.9	124.6	130.5	135.1	147.0	155.1
Corporate profits before tax	141.1	146.2	146.0	150.9	156.8	161.6	173.0	180.5
Federal government surplus or deficit (-) (N.I.A. basis)	-63.8	-54.1	-57.5	-61.2	-58.9	-56.1	-56.2	-53.9
High employment surplus or deficit (-)	-9.2	2.8	1.7	-2.3	-1.7	3.3	1.9	4.1
State and local government surplus or deficit (-) (N.I.A. basis)	12.2	9.2	10.1	13.8	12.8	12.5	13.7	13.1
Excluding social insurance funds	-6	-3.8	-3.1	3	-1.0	-1.6	-7	-1.6
Civilian labor force (millions)	93.6	94.5	95.3	95.6	95.9	96.4	96.8	97.3
Unemployment rate (per cent)	7.6	7.4	7.8	7.5	7.2	7.0	6.9	6.8
Nonfarm payroll employment (millions)	78.4	78.9	79.4	79.8	80.5	81.1	81.5	82.1
Manufacturing	18.8	19.0	19.0	19.2	19.4	19.5	19.6	19.8
Industrial production (1967=100)	127.0	129.3	131.1	133.3	135.6	138.1	140.4	142.9
Capacity utilization: all manufacturing (per cent)	72.1	73.0	73.6	74.4	75.3	76.3	77.1	78.0
Materials (per cent)	78.9	80.4	81.4	82.1	82.9	83.9	84.6	85.5
Housing starts, private (millions, A.R.)	1.40	1.43	1.49	1.54	1.60	1.65	1.65	1.65
Sales new autos, (millions, A.R.)	9.99	10.34	10.23	10.60	10.85	11.00	11.05	11.15
Domestic models	8.68	8.90	8.61	9.00	9.25	9.40	9.45	9.50
Foreign models	1.31	1.45	1.62	1.60	1.60	1.60	1.60	1.65

<sup>1/</sup> Balance of payments data and projection underlying these estimates are shown in the International Developments section of this part of the Greenbook.

<sup>2/</sup> Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

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CLASS II FORM

CHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1976				1977			
	I	II	III	IV	Projected I	II	III	IV
-----Billions of Dollars-----								
Gross National Product	48.0	39.0	34.4	47.4	46.6	42.3	49.7	51.9
Inventory change	19.1	1.2	-2.0	1.0	1.0	1.5	.2	.8
Final purchases	28.9	37.8	36.4	46.4	45.6	40.8	49.5	51.1
Private	28.0	30.5	29.3	36.1	36.4	33.5	41.3	40.3
Net exports	-12.6	.9	-1.2	.8	.5	-3.3	4.6	2.6
Excluding net exports	40.6	29.6	30.5	35.3	35.9	36.8	36.7	37.7
Personal consumption expenditures	31.6	21.1	22.2	26.5	26.5	27.5	27.5	27.7
Goods	17.1	9.3	11.5	14.5	14.5	15.0	15.0	15.2
Services	14.6	11.7	10.7	12.0	12.0	12.5	12.5	12.5
Residential fixed investment	4.3	4.0	3.0	3.3	3.4	2.4	1.7	1.5
Business fixed investment	4.7	4.5	5.3	5.5	6.0	6.9	7.5	8.5
Government	.9	7.3	7.1	10.3	9.2	7.3	8.2	10.8
Federal	-1.2	2.0	2.5	4.1	2.6	1.6	2.4	4.7
State and local	2.1	5.4	4.5	6.2	6.6	5.7	5.8	6.1
GNP in constant (1972) dollars	27.1	13.7	10.1	15.8	15.9	15.2	15.9	16.0
Final purchases	11.2	12.9	11.5	14.8	15.4	13.7	16.3	15.4
Private	14.5	11.2	9.9	12.8	13.1	12.1	14.6	14.0
-----In Per Cent Per Year <sup>1/</sup> -----								
Gross National Product	12.6	9.9	8.5	11.6	11.0	9.7	11.2	11.4
Final purchases	7.5	9.7	9.1	11.4	10.9	9.4	11.3	11.3
Private	9.4	10.0	9.3	11.3	11.1	9.9	12.0	11.4
Personal consumption expenditures	13.1	8.3	8.6	10.1	9.9	10.0	9.8	9.6
Goods	12.7	6.6	8.0	10.0	9.8	9.9	9.6	9.5
Services	13.7	10.5	9.3	10.3	10.0	10.2	9.9	9.7
Gross private domestic investment	68.9	17.9	11.0	16.9	17.3	17.3	14.3	16.0
Residential structures	34.0	28.3	20.0	20.8	20.4	13.4	9.1	7.8
Business fixed investment	13.3	12.3	14.1	14.2	15.0	16.8	17.6	19.2
Gov't. purchases of goods & services	1.0	8.6	8.0	11.6	10.1	7.7	8.5	11.1
Federal	-3.7	6.3	7.9	12.8	7.8	4.6	6.9	13.7
State and local	3.8	9.9	8.1	11.0	11.4	9.5	9.5	9.7
GNP in constant (1972) dollars	9.2	4.5	3.3	5.1	5.0	4.8	4.9	4.9
Final purchases	3.7	4.2	3.7	4.8	4.9	4.3	5.1	4.8
Private	6.2	4.7	4.1	5.2	5.3	4.8	5.8	5.5
GNP implicit deflator <sup>2/</sup>	3.2	5.2	5.1	6.2	5.7	4.7	6.0	6.2
Gross business product fixed-weighted price index <sup>3/</sup>	3.7	5.2	5.0	5.4	5.1	5.1	5.5	5.5
Personal income	10.1	9.5	9.3	10.5	9.7	8.5	9.3	9.7
Wage and salary disbursements	12.6	9.4	7.7	11.4	10.4	9.5	9.0	11.5
Disposable income	10.3	9.0	9.3	10.5	9.7	8.5	9.3	9.7
Corporate profits before tax	33.4	15.3	-5	14.3	16.5	12.8	31.4	18.5
Nonfarm payroll employment	4.2	2.6	2.6	2.0	3.6	3.0	2.0	3.0
Manufacturing	6.6	4.3	.0	4.3	4.2	2.1	2.1	4.1
Industrial production	12.6	7.4	5.7	7.0	6.9	7.5	6.9	7.4
Housing starts, private	9.1	8.9	17.9	14.1	16.5	13.1	.0	.0
Sales new autos	38.4	14.8	-4.2	15.3	9.8	5.6	1.8	3.7
Domestic models	48.0	10.5	-12.4	19.4	11.6	6.6	2.1	2.1
Foreign models	-5.9	50.1	55.8	-4.8	.0	.0	.0	13.1

<sup>1/</sup> Percentage rates are annual rates compounded quarterly.

<sup>2/</sup> Excluding Federal pay increases rates of change are: 1976-I, 3.0 per cent; 1976-IV, 5.8 per cent; 1977-I, 5.6 per cent; 1977-IV, 5.6 per cent.

<sup>3/</sup> Using expenditures in 1972 as weights.

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CLASS II FOMC

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

	1970	1971	1972	1973	1974	1975	Projected	
							1976	1977
Gross National Product	982.4	1063.4	1171.1	1306.6	1413.2	1516.3	1694.5	1873.1
Final purchases	978.6	1057.1	1161.7	1288.6	1402.5	1531.0	1679.5	1855.7
Private	759.7	823.4	908.6	1019.1	1099.2	1192.0	1313.3	1454.8
Excluding net exports	755.8	821.8	911.9	1012.0	1091.7	1171.5	1304.6	1445.0
Personal consumption expenditures	618.8	668.2	733.0	809.9	887.5	973.2	1077.1	1181.2
Goods	349.6	374.8	410.5	457.5	497.8	540.8	596.9	652.9
Services	269.1	293.4	322.4	352.3	389.6	432.4	480.3	528.3
Gross private domestic investment	140.8	160.0	188.3	220.0	215.0	183.7	242.4	281.2
Residential construction	36.6	49.6	62.0	66.1	55.1	51.2	66.6	78.0
Business fixed investment	100.5	104.1	116.8	136.0	149.2	147.1	160.8	185.7
Change in business inventories	3.8	6.4	9.4	17.9	10.7	-14.6	15.0	17.4
Nonfarm	3.7	5.1	8.8	14.7	12.2	-17.6	14.9	17.7
Net exports of goods and services	3.9	1.6	-3.3	7.1	7.5	20.5	8.7	9.9
Exports	62.5	65.6	72.7	101.6	144.4	148.1	163.3	184.8
Imports	58.5	64.0	75.9	94.4	136.9	127.6	154.7	174.9
Gov't. purchases of goods and services	218.9	233.7	253.1	269.5	303.3	339.0	366.3	400.9
Federal	95.6	96.2	102.1	102.2	111.6	124.4	133.0	144.0
State and local	123.2	137.5	151.0	167.3	191.6	214.5	233.3	256.9
Gross national product in constant (1972) dollars	1075.3	1107.5	1171.1	1235.0	1214.0	1191.7	1265.6	1325.2
Personal income	801.3	859.1	942.5	1052.4	1153.3	1249.7	1378.5	1509.5
Wage and salary disbursements	546.5	579.4	633.8	701.3	765.0	806.7	890.6	979.0
Disposable income	685.9	742.8	801.3	901.7	982.9	1080.9	1186.6	1296.1
Saving rate (per cent)	7.4	7.7	6.2	7.8	7.3	7.8	7.1	6.8
Corporate profits with I.V.A. and C.C. Adj.	67.9	77.2	92.1	99.1	84.8	91.6	118.8	141.9
Corporate profits before tax	71.5	82.0	96.2	115.8	127.6	114.5	146.1	168.0
Federal government surplus or deficit (-) (N.I.A. basis)	-12.1	-22.0	-17.3	-6.7	-11.5	-71.2	-59.2	-56.2
High employment surplus or deficit (-)	6.5	-1.7	-1.0	6.6	26.3	-9.8	-1.8	1.9
State and local government surplus or deficit (-) (N.I.A. basis)	2.8	3.7	13.7	13.0	7.3	6.9	11.3	13.0
Excluding social insurance funds	-4.0	-3.8	5.6	4.1	-2.8	-5.1	-1.8	-1.2
Civilian labor force (millions)	82.7	84.1	86.5	88.7	91.0	92.6	94.8	96.6
Unemployment rate (per cent)	4.9	5.9	5.6	4.9	5.6	8.5	7.6	7.0
Nonfarm payroll employment (millions)	70.9	71.2	73.7	76.9	78.4	77.0	79.1	81.3
Manufacturing	19.3	18.6	19.1	20.1	20.0	18.3	19.0	19.6
Industrial production (1967=100)	107.8	109.6	119.7	129.8	129.3	117.8	130.2	139.2
Capacity utilization: all manufacturing (per cent)	78.3	75.0	78.6	83.0	78.9	68.7	73.3	76.7
Materials (per cent)	84.3	83.1	88.0	92.5	87.7	73.5	80.7	84.2
Housing starts, private (millions, A.R.)	1.43	2.05	2.36	2.05	1.34	1.16	1.47	1.64
Sales new autos (millions, A.R.)	8.40	10.24	10.93	11.44	8.87	8.66	10.29	11.01
Domestic models	7.12	8.68	9.32	9.67	7.45	7.08	8.80	9.40
Foreign models	1.28	1.56	1.61	1.77	1.42	1.58	1.50	1.61

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

	1970	1971	1972	1973	1974	1975	Projected	
							1976	1977
-----Billions of Dollars-----								
Gross National Product	46.9	81.0	107.7	135.5	106.6	103.1	178.2	178.6
Inventory change	-5.6	2.6	3.0	8.5	-7.2	-25.3	29.6	2.5
Final purchases	52.4	78.5	104.6	126.9	113.9	128.5	148.5	176.2
Private	41.4	63.7	85.2	110.5	80.1	92.8	121.3	141.5
Net exports	2.1	-2.3	-4.9	10.4	.4	13.0	-11.8	1.2
Excluding net exports	39.3	66.0	90.1	100.1	79.7	79.8	133.1	140.4
Personal consumption expenditures	39.1	49.4	64.8	76.9	77.6	85.7	103.9	104.1
Goods	17.1	25.2	35.7	47.0	40.3	43.0	56.1	55.9
Services	21.9	24.3	29.0	29.9	37.3	42.8	47.9	48.0
Residential fixed investment	-1.3	13.0	12.4	4.1	-11.0	-3.9	15.4	11.4
Business fixed investment	1.6	3.6	12.7	19.2	13.2	-2.1	13.7	24.9
Government	11.0	14.8	19.4	16.4	33.8	35.7	27.3	34.6
Federal	-1.9	.6	5.9	.1	9.4	12.8	8.6	11.0
State and local	12.8	14.3	13.5	16.3	24.3	22.9	18.8	23.6
GNP in constant (1972) dollars	-3.5	32.2	63.6	63.9	-21.0	-22.3	73.9	59.4
Final purchases	2.8	29.9	60.8	56.8	-13.0	-1.8	51.3	57.8
Private	9.3	30.7	57.1	57.4	-16.9	-6.4	47.9	50.2
-----In Per Cent Per Year-----								
Gross National Product	5.0	8.2	10.1	11.6	8.2	7.3	11.8	10.5
Final purchases	5.7	8.0	9.9	10.9	8.8	9.2	9.7	10.5
Private	5.8	8.4	10.3	12.2	7.9	8.4	10.2	10.8
Personal consumption expenditures	6.7	8.0	9.7	10.5	9.6	9.7	10.7	9.7
Goods	5.1	7.2	9.5	11.4	8.8	8.6	10.4	9.4
Services	8.9	9.0	9.9	9.3	10.6	11.0	11.1	10.0
Gross private domestic investment	-3.7	13.6	17.7	16.8	-2.3	-14.6	32.0	16.0
Residential structures	-3.4	35.5	25.1	6.6	-16.7	-7.1	30.1	17.1
Business fixed investment	1.6	3.6	12.3	16.4	9.7	-1.4	9.3	15.5
Gov't. purchases of goods & services	5.3	6.8	8.3	6.5	12.5	11.8	8.1	9.4
Federal	-1.9	.6	6.1	.1	9.2	11.5	6.9	8.3
State and local	11.6	11.6	9.8	10.8	14.5	11.9	8.8	10.1
GNP in constant (1972) dollars	-.3	3.0	5.7	5.5	-1.7	-1.8	6.2	4.7
Final purchases	.3	2.8	5.5	4.9	-1.1	-.1	4.3	4.6
Private	1.1	3.7	6.7	6.3	-1.7	-.7	5.1	5.1
GNP implicit deflator	5.4	5.1	4.1	5.8	10.0	9.3	5.3	5.6
Gross business product fixed weighted price index <sup>1/</sup>	4.4	4.4	3.3	5.7	10.2	9.3	4.8	5.3
Personal income	7.4	7.2	9.7	11.7	9.6	8.4	10.3	9.5
Wage and salary disbursements	6.2	6.0	9.4	10.7	9.1	5.5	10.4	9.9
Disposable income	8.8	8.3	7.9	12.5	9.0	10.0	9.8	9.5
Corporate profits before tax	-14.3	14.7	17.3	20.4	10.2	-10.3	27.6	15.0
Nonfarm payroll employment	.7	.4	3.5	4.3	2.0	-1.8	2.7	2.8
Manufacturing	-4.5	-3.6	2.7	5.2	-.5	-8.5	3.8	3.2
Industrial production	-3.0	1.7	9.2	8.4	-.4	-8.9	10.5	6.9
Housing starts, private	-2.7	43.4	15.1	-13.1	-34.6	-13.4	26.7	11.6
Sales new autos	-12.2	21.9	6.7	4.7	-22.5	-2.4	18.8	7.0
Domestic models	-15.8	21.9	7.4	3.8	-23.0	-5.0	24.3	6.8
Foreign models	15.3	21.9	3.2	9.9	-19.8	11.3	-5.1	7.3

<sup>1/</sup> Using expenditures in 1972 as weights.

## Comments on the Federal Sector Outlook

The Administration recently announced revised spending estimates for the third quarter of 1976, the transition quarter. Outlays are now forecast at between \$95 and \$96 billion, substantially below the \$102.1 billion figure projected by the Office of Management and Budget in its July "Mid-Session Budget Review." The expenditure totals for the second and third quarters of calendar 1976 combined show a spending shortfall of about \$10-\$15 billion below the level expected by OMB earlier this year. Approximately \$6 billion of this overestimate occurred in the defense budget, with spending in May, June and August fell far below expected rates. The remainder was due primarily to lower than anticipated increases in grants to state and local governments; savings in interest payments on the public debt; and special transactions in existing or financial assets, such as the larger than anticipated sale of Mid-Atlantic oil leases.

Reflecting these outlay shortfalls, NIA spending for the second and third quarters combined now appears lower than earlier expectations. Compared to staff estimates presented earlier this spring, this type of spending--which excludes financial transactions--now appears to be \$5 billion smaller, amounting to \$10 billion at an annual rate for each of the two quarters. The NIA shortfall appears to be concentrated in domestic transfers, grants, and interest outlays; only a small portion (\$1 billion at an annual rate for each of the two quarters) is reflected in the purchases estimate.

In fiscal year 1977, the staff now expects that unified outlays will total \$408 billion, about \$2 billion below the last Greenbook. Most of this decline is in the areas of interest payments on the public debt and grants to state and local governments. Projected receipts for fiscal year 1977 are essentially unchanged from last month's estimate of approximately \$356 billion and the deficit is forecast at about \$52 billion.

The full employment budget, as before, shows a sizable shift toward restraint in 1976:Q2 and little further change in the third quarter. On a calendar year basis the full employment budget after registering a \$10 billion deficit in 1975, moves to a \$2 billion deficit in 1976 and a \$2 billion surplus in 1977.

FEDERAL SECTOR ACCOUNTS  
(billions of dollars)

	Fiscal Year 1976*	Fiscal Year 1977 e/		CY 1976		F.R.B. estimates Calendar quarters; unadjusted data					
		Admin. est. 2/	Cong. est. 2/	F.R. Board	F.R. Board	1976		1977			
						I*	II*	III <sup>3/</sup>	IV	I	II
Unified budget receipts	300.0	352.5	362.5	355.6	317.2	66.9	93.6	82.2	74.5	79.0	108.3
Unified budget outlays	365.6	400.0	413.1	408.0	375.7	89.6	91.5	95.5	99.1	101.9	102.5
Surplus (+)/deficit (-), unified budget	-65.6	-47.5	-50.6	-52.4	-58.4	-22.7	2.2	-13.3	-24.6	-22.9	5.8
Surplus (+)/deficit(-), off-budget agencies <u>4/</u>	-8.0	-11.4	n.a.	-11.4	-10.2	-3.8	-.7	-3.1	-2.6	-3.7	-2.6
Means of financing combined deficits:											
Net borrowing from public	82.8	56.9	n.a.	56.9	69.3	24.1	9.4	17.9	17.9	22.2	2.8
Decrease in cash operating balance	-7.2	n.a.	n.a.	6.4	-.2	.4	-6.8	-2.6*	8.7	1.4	-5.0
Other <u>5/</u>	-1.9	n.a.	n.a.	.5	-.5	2.0	-4.0	.9	.6	3.0	-1.0
Cash operating balance, end of period	14.8	n.a.	n.a.	11.0	8.7	8.0	14.8	17.4*	8.7	7.3	12.3
Memo: Sponsored agency borrowing <u>6/</u>	3.5	10.8 <sup>7/</sup>	n.a.	n.a.	3.5	.3	.5	1.7	.9	1.2	1.5
<b>NIA Budget</b>						Seasonally adjusted, annual rates					
Receipts	311.4	n.a.	n.a.	357.3 <sup>8/</sup>	328.7	316.5	324.6	332.4	341.6	353.9	362.4
Expenditures	374.7	n.a.	n.a.	415.6	387.6	380.3	378.7	389.2	402.2	412.2	418.0
Purchases (total)	128.8	n.a.	n.a.	141.2	133.0	129.2	131.2	133.7	137.8	140.4	142.0
Defense	86.2	n.a.	n.a.	92.6	87.8	86.2	86.9	88.0	90.2	92.2	93.0
Non-defense	42.6	n.a.	n.a.	48.6	45.1	42.9	44.2	45.7	47.6	48.2	49.0
All other expenditures	245.9	n.a.	n.a.	274.4 <sup>8/</sup>	254.6	251.1	247.5	255.5	264.4	271.8	276.0
Surplus (+)/deficit (-)	-63.3	n.a.	n.a.	-58.3 <sup>8/</sup>	-58.9	-63.8	-54.1	-56.8	-60.6	-58.3	-55.6
High employment surplus (+)/deficit(-) (NIA basis) <u>9/</u>	-5.6	n.a.	n.a.	.3	-1.8	-9.2	2.8	1.7	-2.3	-1.7	3.3
	*actual	e--estimated		n.e.--not estimated		n.a.--not available				p--preliminary	

1/ Mid-Session Review of the 1977 Budget, July 16, 1976.

2/ Conference Report on Second Concurrent Resolution on the Budget, September 10, 1976.

3/ Fiscal year 1977 began on 10/1/76. The period July 1 to September 30 is a transition quarter between FY 76 and FY 77.

4/ Includes Federal Financing Bank, Postal Service, Export-Import Bank (prior to October, 1976), Rural Electrification and Telephone revolving fund, Housing for the Elderly or Handicapped Fund, and Pension Benefit Guaranty Corporation.

5/ Checks issued less checks paid, accrued items and other transactions.

6/ Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.

7/ Derived from Special Analyses, Budget of the United States Government, Fiscal Year 1977, January 21, 1976.

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 estimates now fully incorporate taxes on inventory profits beginning 1973.

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DOMESTIC FINANCIAL DEVELOPMENTS

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Summary. Credit demands in September remained relatively moderate, and market interest rates fluctuated in a narrow range over most of the month. More recently, however, interest rates have edged down in response to a slight easing in the Federal funds rate and a weakening of  $M_1$  growth. Short-term rates now are generally about 12 to 25 basis points and bond yields 5 to 20 basis points below levels prevailing at the time of the September FOMC meeting, and intermediate-term rates have declined somewhat more. Stock prices have come under considerable downward pressure recently, apparently the result of increasing doubts among some market participants about the durability and strength of the economic recovery.

Business demands for long-term funds picked up modestly in September. The volume of publicly offered bonds rose significantly from the depressed levels of the summer months, though remaining well below levels established earlier in the year. At the same time, private placements of bonds are estimated to have continued at about the pace of earlier months in the quarter. Stock issues, on the other hand, fell off slightly in September. Short-term business borrowing also declined in September as in August, as a further rise in business loans at banks was more than offset by a sharp decline in nonfinancial commercial paper. For the third quarter, short-term business indebtedness stayed essentially unchanged, in contrast to the modest advance recorded in the second quarter.

Demands for funds by other categories of borrowers were about unchanged in September. State and local governments continued to issue long-term bonds at an above average rate, and, at the same time, significantly increased their issuance of short-term debt. The Treasury also remained an active borrower, obtaining funds primarily through sales of intermediate-term coupon securities. Borrowing in the residential mortgage market continued at about the second quarter pace, and the advance of consumer credit in August--the latest month for which data are available--also was in line with gains recorded earlier this year.

Deposit growth at banks continued strong in September despite weak demand deposit expansion, as fund flows into consumer-type time deposits, especially savings deposits, remained relatively large. Banks used part of these incoming funds to make further retirements of CDs. But the bulk of incoming funds were channeled into consumer, real estate and business loans. Banks also apparently became somewhat more aggressive in seeking business loans by lowering their prime rates one-fourth per cent to 6-3/4 per cent and relaxing some non-price lending terms (see the Supplement for results of the latest Bank Lending Practices Survey).

Funds have also continued to pour into deposit accounts at the nonbank thrift institutions. With funds readily available, mortgage commitments at thrift institutions rose to a record level and rates on new mortgages edged down slightly.

Outlook. Aggregate credit demands appear likely to be only a little larger in the fourth quarter than in the third, and market interest rates may remain near current levels for some months to come. While the substantial buildup in the Treasury's balance in late September will help to hold down its financing activity, it nonetheless is still expected to need around \$18 billion of new money--compared with \$15.5 billion in the third quarter--to help cover substantial unified and off-budget agency deficits. State and local borrowing also appears likely to remain relatively large, as governmental units continue to take advantage of improved conditions in this market to finance programs that had been postponed in 1974 and 1975 because of unsettled market conditions. And growth in mortgages and consumer credit may also increase further in association with further expansion of economic activity.

In the business sector, credit demands are also likely to grow. Public offerings of bonds should rise well above the depressed third quarter level--though still remaining below that of the first half. And with the projected pick-up of economic activity, short-term credit demands may also expand somewhat.

With market rates remaining low relative to rates offered on deposits at financial institutions, the recent strong expansion in consumer-type deposits at banks and nonbank thrift institutions can be expected to continue. If funds flows remain strong, however, institutions may begin to trim advertising, and perhaps move down their deposit rates. Against this background, bank prime rates may also come under downward pressures, and rates on new mortgages might decline somewhat further.

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INTERNATIONAL DEVELOPMENTS

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Summary. Since mid-September the dollar has appreciated about 1/2 per cent on a weighted average basis against leading foreign currencies, largely as a counterpart to a decline of nearly 5 per cent by the pound against the dollar. The lira rate has been sustained recently by a temporary 10 per cent tax on foreign currency purchases. The EC snake came under severe pressure as a mark revaluation was anticipated following the October 3 German elections, but no revaluation took place and flows into marks have abated. The Mexican peso has been under renewed downward pressure, requiring substantial support from the Mexican authorities.

In the U.S. international accounts the merchandise trade balance registered a deficit of nearly \$10 billion (SAAR) in August, and about \$1 billion in July-August combined, about double the first-half rate. The main factor was the rising volumes of imports, including both fuels and other commodities, while export volumes rose more slowly. Bank-reported private capital flows, which had been inward on balance in July, shifted toward a moderate outflow in August. Most of the shift apparently represented month-end adjustments rather than a change in banks' behavior. One sizable change was a reduction in banks' outstanding credits to Japan in August, possibly representing the efforts of Japanese authorities to avoid further yen appreciation by limiting

borrowing from U.S. sources. Net outflows of capital related to transactions in securities were reduced in August as the volume of placements of new foreign bonds in the United States -- mostly Canadian -- dropped sharply from earlier record levels. Offsetting this to some extent, however, net foreign private dealings in U.S. corporate stocks resulted in a small net liquidation in August; net private foreign purchases had dropped off sharply after the first quarter when U.S. equity markets weakened. Net official purchases of U.S. corporate stocks by OPEC countries were also reduced.

Economic activity in most industrial countries abroad experienced a greater-than-expected slowdown, or in some cases even a halt, in the second quarter. Inflation rates are still high, and divergences are great, with consumer price increases at annual rates ranging from 1 per cent in Switzerland and 4-1/2 per cent in Germany to 12 per cent in the United Kingdom and 18 per cent in Italy. These divergences in inflation rates, and expectations that they might continue, have generated much of the pressure on weak currencies. In recent weeks the policy response to inflationary pressures, and to difficulties in maintaining margins in the EC snake, has been a considerable tightening of monetary policy plus special measures of various kinds in the more inflationary countries to damp consumer demand and support their currencies. Foreign interest rates, on the whole, have been rising relative to U.S. rates.

Outlook. Disappointing economic developments in most countries since the first quarter have resulted in somewhat greater uncertainty about the rate of economic expansion in the period ahead. Policy has generally remained firmly directed toward reducing inflation, however, and a number of countries with pressure on their currencies have recently tightened policies further. It is too early to judge the extent to which the economic outlook abroad is now weaker than a month ago, but we have adjusted our projections downward somewhat.

Projections of the U.S. trade balance for the period ahead have been revised to take account of the less expansive economic environment, as well as the large deficit registered in July-August. The result has been an estimate of a slightly larger deficit for this year than was estimated last month, and a larger deficit next year -- on the order of \$8-9 billion rather than the previous estimate of about \$7 billion. Projections of rising net receipts on military and services transactions would still yield a net surplus on goods and services combined. These estimates assume an increase of \$1.75 a barrel in the OPEC price of oil on January 1.

The weighted average value of the dollar against major foreign currencies has been quite steady in exchange markets since last April despite the rising trade deficit and a tendency toward relative easing of interest rates. Unless there are major new influences on the market in the period ahead, the average value of the dollar is not likely to move to a different level, though there may still be large shifts against particular currencies.

	1975	1976 <sup>P</sup>	1977 <sup>P</sup>	1976				1977 <sup>P</sup>			
				I	II	III <sup>P</sup>	IV <sup>P</sup>	I	II	III	IV
<b>Billions of dollars</b>											
Net Exports of Goods and Services (GNP basis net exports) <u>1/</u>	16.3 (20.5)	4.8 (8.7)	4.3 (9.9)	4.2 (8.4)	6.3 (9.3)	3.9 (8.1)	4.6 (8.9)	4.6 (9.4)	.7 (6.1)	4.9 (10.7)	7.5 (13.3)
Merchandise Trade Balance	9.0	-6.9	-8.4	-6.7	-5.1	-8.0	-8.0	-8.3	-11.9	-7.5	-5.5
Exports	107.1	114.9	129.0	107.3	113.8	118.7	119.7	122.6	127.0	131.0	135.6
Agricultural	22.2	23.2	22.8	21.3	23.5	25.0	23.0	22.5	22.8	22.7	23.0
Nonagricultural	84.8	91.7	106.3	86.1	90.3	93.7	96.7	100.1	104.2	108.3	112.6
Imports	98.1	121.8	137.4	114.0	118.9	126.7	127.7	130.9	138.9	138.5	141.1
Fuels	28.5	36.3	41.5	31.8	36.5	37.9	38.9	39.1	44.2	41.6	41.0
Nonfuels	69.5	85.6	95.9	82.3	82.5	88.8	88.8	91.8	94.7	96.9	100.1
Military and Service Transactions, net	7.3	11.7	12.7	10.9	11.4	11.9	12.6	12.9	12.6	12.4	13.0
Military transactions, net	-.9	.2	.7	--	-.1	.3	.5	.5	.6	.8	.8
Investment income, net	6.0	9.0	9.4	9.1	8.6	9.0	9.4	9.7	9.3	9.0	9.7
Other services, net	2.1	2.5	2.6	1.8	2.9	2.6	2.8	2.7	2.7	2.6	2.5
U.S. Current Account Balance <u>2/</u>	11.7	.7	.1	-.2	2.8	-.3	.4	.3	-3.6	.5	3.1
<b>Constant (1972) dollars</b>											
Merchandise exports (% change)	64.2 (-3.0)	66.8 (4.1)	71.6 (7.2)	63.3 (-19.0)	66.5 (21.6)	68.6 (13.5)	68.7 (.6)	69.8 (6.6)	71.0 (7.0)	72.2 (7.0)	73.6 (8.0)
Merchandise imports (% change)	51.3 (-12.4)	61.5 (19.9)	63.6 (3.4)	59.0 (40.0)	60.4 (9.8)	63.5 (22.2)	63.2 (-2.0)	63.2 --	64.2 (6.5)	63.1 (7.0)	63.4 (2.0)
<b>Foreign Outlook - Major Industrial Countries</b>											
Real GNP, % change <u>3/</u>	--	4.8	4.9	9.6	1.0	5.0	5.0	5.4	5.3	4.9	4.8
Wholesale Prices, % change <u>4/</u>	8.0	6.8	6.8	6.9	9.3	8.5	7.2	6.6	6.3	5.6	5.3

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 average of shares of Germany, Japan, Canada, and the United Kingdom in U.S. nonagricultural exports.

4/ Weighted by the shares of Germany, Japan, Canada, United Kingdom, France and Italy in the total manufactured goods exports of the six countries. Data are largely manufactured goods prices.

p/ Projected.