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CONFIDENTIAL (FR)

December 15, 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. Economic activity in the fourth quarter appears to be rising at about the reduced pace of the third quarter. There has been further evidence of the inventory backup that led to widespread production adjustments during the late summer and fall months. With consumer demand strengthening recently, however, excess stocks apparently are being worked down at the present time, and this should pave the way for improved industrial activity in coming months. But the sluggish growth of production, employment, and income since last spring seems to have adversely affected the outlook for business capital spending next year.

Industrial production is estimated to have risen 1-1/4 per cent in November. Somewhat more than half of the increase reflected the post-strike resumption of activity in autos and agricultural machinery. Apart from strike effects, increases in output were moderate but widespread.

There was a strong increase of total employment in November following two months of decline, but the labor force rose even more, and the unemployment rate moved up two-tenths further--to 8.1 per cent. Over the past half year, total employment has increased by only 430,000 and the unemployment rate has risen three-fourth of a point. Nonfarm payroll employment rose 150,000 (after strike adjustment) last month, with increases in the service sectors, construction and mining. In manufacturing, employment was unchanged, after allowing for the

return to work of strikers. The rise in the factory workweek, by 0.3 hours, partly reflected the end of the auto and agricultural machinery strikes. Factory employment and the length of the workweek in November were no higher than last spring.

Retail sales are estimated to have risen briskly (by 1.7 per cent) in November, following a strong gain in October (according to revised data). Sales increases last month were particularly large at stores selling furniture and appliances and general merchandise. The November level of retail sales, excluding autos and nonconsumer items, was 3-1/2 per cent above the third quarter average.

Unit sales of domestic models also improved in November, but they remained below the average of earlier this year, even after adjustment for strike effects. Sales of domestic units were at an 8.0 million seasonally adjusted annual rate, up from the strike-depressed 7.6 million rate in October. Shortages of some popular models continue to dampen sales last month, but the demand for domestic units has been relatively flat for the past half year or more. In the first ten days of December, auto sales were at an 8.7 million unit annual rate, close to the average earlier this year. Unit sales of foreign models dropped back to a 1-1/2 million annual rate in November from an average 1.8 million rate in the two previous months.

The book value of business inventories rose \$13.4 billion (annual rate) in October, about half the rapid September pace. The bulk of the slowdown was in trade, where auto stocks were run down

due to the strike and other components showed much smaller increases than in September. However, inventories continued to increase at a rapid pace in manufacturing during October. In contrast to earlier in the year, when excess stocks were principally in nondurable goods lines, the inventory problem now seems to be concentrated in durables. The stock-sales ratio for all manufacturing in October rose to the level of late 1975.

The outlook for capital spending appears to have weakened recently. Although orders for nondefense capital equipment have continued to advance strongly, the average increase in the past half year is substantially below the pace earlier in 1976. Other indicators of business capital outlays also suggest some weakening of spending intentions. The Commerce Department's latest survey of anticipated plant and equipment expenditures, conducted in late October and November, shows a strong gain for the current quarter, but essentially no increase in real terms in the first two quarters of 1977. Newly approved capital appropriations of the 1,000 largest manufacturing firms, which tend to lead spending by an average of about four quarters, also indicate less prospective strength. Excluding the volatile petroleum component, these appropriations declined by 18 per cent in the third quarter, following a sharp increase over the previous three quarters.

Residential construction activity, in contrast, continues to improve. Private housing starts in October, at 1.79 million units,

annual rate, were only slightly under the advanced September pace. Both single- and multifamily starts have been moving up; single-family starts rose to an annual rate of 1.33 million units in October, only 7 per cent below their January 1973 peak. Meanwhile, sales of both new and existing homes in October, although off from the September pace, remained quite strong.

Consumer prices rose 0.3 per cent in October, slightly under the rate of increase in recent months. Food prices rose at a moderate rate but there was a further large rise in energy prices. Services increased by 0.5 per cent, about equal to the average rise in the second and third quarters.

At wholesale, prices rose by 0.6 per cent in November. Farm and food prices changed little, but industrial commodities again increased rapidly (by 0.8 per cent). Over the past half year, the increase in industrial commodity prices has averaged about 10 per cent, annual rate, more than double the pace earlier in 1976. Fuels, metals, and lumber and wood products have paced the acceleration.

Outlook. Real GNP growth during the current quarter is now projected at about 3-1/2 per cent, annual rate, approximately the same as in the third quarter. Retail sales and residential construction appear to be showing significantly more strength this quarter than last. But this additional strength is likely to be offset by a slower rate of expansion in business fixed investment and by a decline in the rate of inventory investment. Real growth in Federal and State and local purchases is projected to remain sluggish this quarter.

The staff projections for 1977 incorporate new fiscal assumptions, as the incoming Administration appears to be leaning strongly in the direction of fiscal stimulus. We have assumed a \$15 billion stimulative package. Personal tax rates are assumed to be cut permanently with liabilities reduced by \$10 billion in calendar 1977. This would be accomplished by lower withholding rates during the last three quarters of 1977. We have also assumed a \$2 billion cut in corporate taxes through an extension of the surtax exemption to \$150,000. Additionally, we have assumed an increase of \$3 billion in government outlays, partly through expansion of public service jobs and partly by a speed-up and expansion of State and local construction grants. For fiscal 1977, total Federal budget outlays are now projected at about \$411 billion--some \$3 billion more than in the preceding Greenbook.

Our monetary policy assumptions continue to specify a growth path of 5-1/2 per cent for  $M_1$ , beginning in the third quarter of 1976. Given this assumption, short-term interest rates are expected to increase appreciably during 1977--but most of the rise would occur around mid-year or after, when economic expansion is expected to pick-up momentum.

For the four quarters of 1977, we now project an average rate of growth in real GNP of 5-1/2 per cent--about 1 percentage point more than last month's projection; reflecting the additional fiscal stimulus now assumed. For the first two quarters of 1977, the growth



rate in real GNP is expected to range between 4-1/2 and 5 per cent. Growth during this period seems likely to be held down by weakness in business capital outlays; however, we are assuming substantially larger increases in plant and equipment spending in early 1977 than reported in the latest Commerce Survey. On the other hand, the adjustment in inventories that has retarded production recently should act as less of a drag early next year. Moreover, economic growth in early 1977 should receive support from increased activity in housing and larger real purchases by both levels of government.

The pace of expansion is projected to quicken to the 6 to 6-1/2 per cent range during the second half of next year, when the impact of the tax cut on consumption becomes stronger and business investment in fixed capital and inventories seem likely to respond to the effects of an improving outlook.

Our projection suggests a decline in the unemployment rate from an estimated fourth quarter 1976 level of 8.0 per cent to 7.2 per cent by the last quarter of 1977.

We have retained for this projection the assumption of a 15 per cent increase in the OPEC price of crude oil on January 1; by and large our projections of price developments are similar to those of a month ago.

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

## STAFF GNP PROJECTIONS

	Per cent change, annual rate							
	Changes in nominal GNP (\$ billions)		Real GNP		Gross business product fixed-weighted price index		Unemployment rate (per cent)	
	11/10/76	12/15/76	11/10/76	12/15/76	11/10/76	12/15/76	11/10/76	12/15/76
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	176.4	175.6	6.2	6.1	4.6	4.6	7.6	7.7
1977	171.3	177.9	4.2	4.7	5.3	5.3	7.3	7.6
1976-I <u>1/</u>	48.0	48.0	9.2	9.2	3.7	3.7	7.6	7.6
1976-II <u>1/</u>	39.0	39.0	4.5	4.5	5.2	5.2	7.4	7.4
1976-III <u>1/</u>	34.5	33.2	4.0	3.8	4.4	4.3	7.8	7.8
1976-IV	39.9	39.5	3.3	3.5	5.2	5.2	7.7	8.0
1977-I	45.7	47.2	4.4	4.8	5.3	5.5	7.5	7.9
1977-II	41.7	44.8	4.4	5.1	5.2	5.0	7.4	7.7
1977-III	48.8	52.2	4.7	5.9	5.3	5.4	7.3	7.5
1977-IV	52.1	59.9	4.9	6.4	5.3	5.5	7.2	7.2
Change:								
75-II to								
76-II <u>1/</u>	192.9	192.9	7.0	7.0	5.6	5.6	-1.3	-1.3
75-IV to								
76-IV <u>1/</u>	161.4	159.7	5.2	5.2	4.7	4.6	-.8	-.5
76-II to								
77-II	161.8	164.7	4.0	4.3	5.1	5.0	.0	.3
76-IV to								
77-IV	188.3	204.1	4.6	5.5	5.3	5.4	-.5	-.8

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.)

	1976				1977			
	I	II	III	IV	Projected			
					I	II	III	IV
Gross National Product	1636.2	1675.2	1708.4	1747.9	1795.1	1839.9	1892.1	1952.0
Final purchases	1621.4	1659.2	1693.3	1740.9	1788.1	1831.2	1881.2	1937.5
Private	1266.7	1297.2	1323.7	1364.1	1402.9	1436.2	1475.8	1520.4
Excluding net exports	1258.3	1287.9	1320.3	1359.0	1395.7	1434.6	1473.5	1514.1
Personal consumption expenditures	1043.6	1064.7	1088.5	1117.5	1144.5	1173.8	1202.5	1233.3
Goods	580.5	589.8	599.4	615.9	630.9	647.2	662.9	680.0
Services	463.2	474.9	489.1	501.6	513.6	526.6	539.6	553.3
Gross private domestic investment	229.6	239.2	247.0	248.5	258.2	269.5	281.9	295.3
Residential construction	61.3	65.3	68.9	74.6	79.6	84.1	88.2	91.5
Business fixed investment	153.4	157.9	163.0	166.9	171.6	176.7	182.8	189.3
Change in business inventories	14.8	16.0	15.1	7.0	7.0	8.7	10.9	14.5
Nonfarm	12.7	17.3	15.6	8.0	7.5	8.7	10.9	14.5
Net exports of goods and services <sup>1/</sup>	8.4	9.3	3.4	5.1	7.2	1.6	2.3	6.3
Exports	154.1	160.3	166.3	168.3	173.7	178.9	184.4	190.2
Imports	145.7	151.0	162.9	163.2	166.5	177.3	182.1	183.9
Gov't. purchases of goods and services	354.7	362.0	369.6	376.8	385.2	395.0	405.4	417.1
Federal <sup>2/</sup>	129.2	131.2	134.5	138.0	140.5	142.9	145.9	150.6
State and local	225.5	230.9	235.0	238.8	244.7	252.1	259.9	266.5
Gross national product in constant (1972) dollars	1246.3	1260.0	1271.7	1282.6	1297.6	1313.7	1332.6	1353.3
Personal income	1331.3	1362.0	1386.0	1416.4	1451.6	1485.8	1523.3	1562.7
Wage and salary disbursements	861.5	881.1	897.8	917.2	938.8	961.4	984.7	1011.0
Disposable income	1147.6	1172.5	1190.2	1216.8	1245.9	1285.4	1316.6	1348.3
Saving rate (per cent)	6.9	7.1	6.4	6.0	6.0	6.5	6.5	6.4
Corporate profits with I.V.A. and C.C. Adj.	115.1	116.4	122.0	128.0	134.1	137.5	148.2	162.1
Corporate profits before tax	141.1	146.2	150.2	153.0	158.1	161.0	170.2	182.5
Federal government surplus or deficit (-) (N.I.A. basis)	-63.8	-54.1	-57.1	-60.8	-60.4	-72.6	-76.2	-71.0
High employment surplus or deficit (-)	-9.3	2.9	.3	-6	-1.5	-13.4	-18.8	-16.9
State and local government surplus or deficit (-) (N.I.A. basis)	12.2	9.2	12.7	15.1	14.8	17.2	21.0	20.9
Excluding social insurance funds	-.6	-3.8	-.5	1.6	1.0	3.1	6.6	6.2
Civilian labor force (millions)	93.6	94.5	95.3	95.7	96.1	96.6	97.1	97.5
Unemployment rate (per cent)	7.6	7.4	7.8	8.0	7.9	7.7	7.5	7.2
Nonfarm payroll employment (millions)	78.4	79.0	79.3	79.6	80.0	80.5	81.1	81.7
Manufacturing	18.8	19.0	19.0	19.0	19.2	19.4	19.6	19.9
Industrial production (1967=100)	127.0	129.4	131.0	131.7	133.5	135.8	138.5	141.5
Capacity utilization: all manufacturing (per cent)	79.0	80.2	80.8	80.5	80.9	81.6	83.1	83.8
Materials (per cent)	79.1	80.6	81.3	80.9	81.3	82.0	83.0	84.2
Housing starts, private (millions, A.R.)	1.40	1.43	1.59	1.65	1.70	1.75	1.85	1.85
Sales new autos, (millions, A.R.)	9.99	10.34	10.23	9.90	10.40	10.85	11.20	11.35
Domestic models	8.68	8.90	8.61	8.20	8.70	9.10	9.40	9.50
Foreign models	1.31	1.45	1.62	1.70	1.70	1.75	1.80	1.85

<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 FOMCCHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1976				1977			
	I	II	III	IV	Projected			
	I	II	III	IV	I	II	III	IV
-----Billions of Dollars-----								
Gross National Product	48.0	39.0	33.2	39.5	47.2	44.8	52.2	59.9
Inventory change	19.1	1.2	-9	-8.1	.0	1.7	2.2	3.6
Final purchases	28.9	37.8	34.1	47.6	47.2	43.1	50.0	56.3
Private	28.0	30.5	26.5	40.4	38.8	33.3	39.6	44.6
Net exports	-12.6	.9	-5.9	1.7	2.1	-5.6	.7	4.0
Excluding net exports	40.6	29.6	32.4	38.7	36.7	38.9	38.9	40.6
Personal consumption expenditures	31.6	21.1	23.8	29.0	27.0	29.3	28.7	30.8
Goods	17.1	9.3	9.6	16.5	15.0	16.3	15.7	17.1
Services	14.6	11.7	14.2	12.5	12.0	13.0	13.0	13.7
Residential fixed investment	4.3	4.0	3.6	5.7	5.0	4.5	4.1	3.3
Business fixed investment	4.7	4.5	5.1	3.9	4.7	5.1	6.1	6.5
Government	.9	7.3	7.6	7.2	8.4	9.8	10.4	11.7
Federal	-1.2	2.0	3.3	3.5	2.5	2.4	3.0	4.7
State and local	2.1	5.4	4.1	3.8	5.9	7.4	7.4	7.0
GNP in constant (1972) dollars	27.1	13.7	11.7	10.9	15.0	16.1	18.9	20.7
Final purchases	11.2	12.9	12.7	16.4	15.0	14.8	17.6	18.3
Private	14.5	11.2	10.8	16.6	13.8	12.0	14.7	16.5
-----In Per Cent Per Year <sup>1/</sup> -----								
Gross National Product	12.6	9.9	8.2	9.6	11.2	10.4	11.8	13.3
Final purchases	7.5	9.7	8.5	11.7	11.3	10.0	11.4	12.5
Private	9.4	10.0	8.4	12.8	11.9	9.8	11.5	12.6
Personal consumption expenditures	13.1	8.3	9.2	11.1	10.0	10.6	10.1	10.6
Goods	12.7	6.6	6.7	11.5	10.1	10.7	10.1	10.7
Services	13.7	10.5	12.5	10.6	9.9	10.5	10.2	10.5
Gross private domestic investment	68.9	17.9	13.8	2.5	16.6	18.7	19.7	20.4
Residential structures	34.0	28.3	24.3	37.4	29.6	24.6	21.0	15.8
Business fixed investment	13.3	12.3	13.5	9.9	11.7	12.4	14.5	15.0
Gov't. purchases of goods & services	1.0	8.6	8.6	8.1	9.2	10.6	11.0	12.1
Federal	-3.7	6.3	10.7	10.7	7.4	7.0	8.7	13.5
State and local	3.8	9.9	7.4	6.6	10.3	12.7	12.3	11.2
GNP in constant (1972) dollars	9.2	4.5	3.8	3.5	4.8	5.1	5.9	6.4
Final purchases	3.7	4.2	4.1	5.3	4.8	4.7	5.5	5.6
Private	6.2	4.7	4.5	6.9	5.6	4.8	5.7	6.4
GNP implicit deflator <sup>2/</sup>	3.2	5.2	4.2	5.9	6.2	5.1	5.6	6.5
Gross business product fixed-weighted price index <sup>3/</sup>	3.7	5.2	4.3	5.2	5.5	5.0	5.4	5.5
Personal income	10.1	9.5	7.2	9.1	10.3	9.8	10.5	10.8
Wage and salary disbursements	12.6	9.4	7.8	8.9	9.8	10.2	9.8	11.1
Disposable income	10.3	9.0	6.2	9.2	10.3	9.8	10.5	10.8
Corporate profits before tax	33.4	15.3	11.4	7.9	13.8	7.5	24.9	32.2
Nonfarm payroll employment	4.2	3.1	1.5	1.5	2.0	2.5	3.0	3.0
Manufacturing	6.6	4.3	.0	.0	4.3	4.2	4.2	6.3
Industrial production	12.6	7.8	5.0	2.2	5.6	7.0	8.2	8.8
Housing starts, private	9.1	8.9	52.8	16.0	12.7	12.3	24.9	.0
Sales new autos	39.0	14.8	-4.2	-12.3	21.8	18.5	13.5	5.5
Domestic models	48.0	10.5	-12.4	-17.7	26.7	19.7	13.9	4.3
Foreign models	-5.9	50.1	55.8	21.3	.0	12.3	11.9	11.6

<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, 5.4 per; 1977-I, 6.1 per cent; 1977-IV, 5.9 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	1691.9	1869.8
Final purchases	978.6	1057.1	1161.7	1288.6	1402.5	1531.0	1678.7	1859.5
Private	759.7	823.4	908.6	1019.1	1099.2	1192.0	1312.9	1458.8
Excluding net exports	755.8	821.8	911.9	1012.0	1091.7	1171.5	1306.4	1454.5
Personal consumption expenditures	618.8	668.2	733.0	809.9	887.5	973.2	1078.6	1188.5
Goods	349.6	374.8	410.5	457.5	497.8	540.8	596.4	655.2
Services	269.1	293.4	322.4	352.3	389.6	432.4	482.2	533.3
Gross private domestic investment	140.8	160.0	188.3	220.0	215.0	183.7	241.1	276.2
Residential construction	36.6	49.6	62.0	66.1	55.1	51.2	67.5	85.8
Business fixed investment	100.5	104.1	116.8	136.0	149.2	147.1	160.3	180.1
Change in business inventories	3.8	6.4	9.4	17.9	10.7	-14.6	13.2	10.3
Nonfarm	3.7	5.1	8.8	14.7	12.2	-17.6	13.4	10.4
Net exports of goods and services	3.9	1.6	-3.3	7.1	7.5	20.5	6.5	4.4
Exports	62.5	65.6	72.7	101.6	144.4	148.1	162.2	181.8
Imports	58.5	64.0	75.9	94.4	136.9	127.6	155.7	177.4
Gov't. purchases of goods and services	218.9	233.7	253.1	269.5	303.3	339.0	365.8	400.7
Federal	95.6	96.2	102.1	102.2	111.6	124.4	133.2	145.0
State and local	123.2	137.5	151.0	167.3	191.6	214.5	232.5	255.7
Gross national product in constant (1972) dollars	1075.3	1107.5	1171.1	1235.0	1214.0	1191.7	1265.1	1324.3
Personal income	801.3	859.1	942.5	1052.4	1153.3	1249.7	1373.9	1505.8
Wage and salary disbursements	546.5	579.4	633.8	701.3	765.0	806.7	889.4	974.1
Disposable income	685.9	742.8	801.3	901.7	982.9	1080.9	1181.8	1299.1
Saving rate (per cent)	7.4	7.7	6.2	7.8	7.3	7.8	6.6	6.4
Corporate profits with I.V.A. and C.C. Adj.	67.9	77.2	92.1	99.1	84.8	91.6	120.4	145.4
Corporate profits before tax	71.5	82.0	96.2	115.8	127.6	114.5	147.6	167.9
Federal government surplus or deficit (-) (N.I.A. basis)	-12.1	-22.0	-17.3	-6.7	-11.5	-71.2	-59.0	-70.0
High employment surplus or deficit (-)	6.5	-1.7	-1.0	6.6	26.3	-9.9	-1.7	-12.7
State and local government surplus or deficit (-) (N.I.A. basis)	2.8	3.7	13.7	13.0	7.3	6.9	12.4	18.5
Excluding social insurance funds	-4.0	-3.8	5.6	4.1	-2.8	-5.1	-.8	4.2
Civilian labor force (millions)	82.7	84.1	86.5	88.7	91.0	92.6	94.8	96.8
Unemployment rate (per cent)	4.9	5.9	5.6	4.9	5.6	8.5	7.7	7.6
Nonfarm payroll employment (millions)	70.9	71.2	73.7	76.9	78.4	77.0	79.1	80.8
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	137.3
Capacity utilization: all manufacturing (per cent)	79.2	78.0	83.1	87.5	84.2	73.6	80.1	82.3
Materials (per cent)	84.3	83.1	88.0	92.4	87.7	73.6	80.5	82.6
Housing starts, private (millions, A.R.)	1.43	2.05	2.36	2.05	1.34	1.16	1.52	1.79
Sales new autos (millions, A.R.)	8.40	10.24	10.93	11.42	8.91	8.66	10.12	10.95
Domestic models	7.12	8.68	9.32	9.65	7.49	7.08	8.60	9.17
Foreign models	1.28	1.56	1.61	1.77	1.42	1.58	1.52	1.77

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	175.6	177.9
Inventory change	-5.6	2.6	3.0	8.5	-7.2	-25.3	27.8	-2.9
Final purchases	52.4	78.5	104.6	126.9	113.9	128.5	147.7	180.8
Private	41.4	63.7	85.2	110.5	80.1	92.8	120.9	145.9
Net exports	2.1	-2.3	-4.9	10.4	.4	13.0	-14.0	-2.1
Excluding net exports	39.3	66.0	90.1	100.1	79.7	79.8	134.9	148.1
Personal consumption expenditures	39.1	49.4	64.8	76.9	77.6	85.7	105.4	109.9
Goods	17.1	25.2	35.7	47.0	40.3	43.0	55.6	58.8
Services	21.9	24.3	29.0	29.9	37.3	42.8	49.8	51.1
Residential fixed investment	-1.3	13.0	12.4	4.1	-11.0	-3.9	16.3	18.3
Business fixed investment	1.6	3.6	12.7	19.2	13.2	-2.1	13.2	19.8
Government	11.0	14.8	19.4	16.4	33.8	35.7	26.8	34.9
Federal	-1.9	.6	5.9	.1	9.4	12.8	8.8	11.8
State and local	12.8	14.3	13.5	16.3	24.3	22.9	18.0	23.2
GNP in constant (1972) dollars	-3.5	32.2	63.6	63.9	-21.0	-22.3	73.4	59.2
Final purchases	2.8	29.9	60.8	56.8	-13.0	-1.8	52.3	61.4
Private	9.3	30.7	57.1	57.4	-16.9	-6.4	49.3	54.9
-----In Per Cent Per Year-----								
Gross National Product	5.0	8.2	10.1	11.6	8.2	7.3	11.6	10.5
Final purchases	5.7	8.0	9.9	10.9	8.8	9.2	9.6	10.8
Private	5.8	8.4	10.3	12.2	7.9	8.4	10.1	11.1
Personal consumption expenditures	6.7	8.0	9.7	10.5	9.6	9.7	10.8	10.2
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	10.6
Gross private domestic investment	-3.7	13.6	17.7	16.8	-2.3	-14.6	31.2	14.6
Residential structures	-3.4	35.5	25.1	6.6	-16.7	-7.1	31.8	27.2
Business fixed investment	1.6	3.6	12.3	16.4	9.7	-1.4	9.0	12.3
Gov't. purchases of goods & services	5.3	6.8	8.3	6.5	12.5	11.8	7.9	9.5
Federal	-1.9	.6	6.1	.1	9.2	11.5	7.1	8.8
State and local	11.6	11.6	9.8	10.8	14.5	11.9	8.4	10.0
GNP in constant (1972) dollars	-.3	3.0	5.7	5.5	-1.7	-1.8	6.1	4.7
Final purchases	.3	2.8	5.5	4.9	-1.1	-.1	4.3	4.9
Private	1.1	3.7	6.7	6.3	-1.7	-.7	5.2	5.5
GNP implicit deflator	5.4	5.1	4.1	5.8	10.0	9.3	5.1	5.6
Gross business product fixed weighted price index <sup>1/</sup>	4.4	4.4	3.3	5.7	10.2	9.3	4.6	5.3
Personal income	7.4	7.2	9.7	11.7	9.6	8.4	9.9	9.6
Wage and salary disbursements	6.2	6.0	9.4	10.7	9.1	5.5	10.3	9.5
Disposable income	8.8	8.3	7.9	12.5	9.0	10.0	9.3	9.9
Corporate profits before tax	-14.3	14.7	17.3	20.4	10.2	-10.3	28.9	13.7
Nonfarm payroll employment	.7	.4	3.5	4.3	2.0	-1.8	2.7	2.1
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	5.8
Housing starts, private	-2.7	43.4	15.1	-13.1	-34.6	-13.4	31.0	17.8
Sales new autos	-12.2	21.9	6.7	4.5	-22.0	-2.8	16.9	8.2
Domestic models	-15.8	21.9	7.4	3.5	-22.4	-5.5	21.5	6.6
Foreign models	15.3	21.9	3.2	9.9	-19.8	11.3	-3.8	16.4

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

FEDERAL SECTOR ACCOUNTS  
(billions of dollars)

F.R.B. estimates

	Fiscal Year 1976*	Fiscal Year 1977 e/				CY 1976 F.R. Board	Calendar quarters; unadjusted data					
		Admin. est. 1/	Cong. est. 2/	F.R. Board	F.R. Board		1976			1977		
							II*	III*3/4/	IV	I	II	III
Unified budget receipts	300.0	352.5	362.5	344.6	315.6	93.6	81.8	73.2	79.1	102.6	89.8	
Unified budget outlays	365.6	400.0	413.1	410.6	372.6	91.5	94.5	97.1	100.8	104.7	108.0	
Surplus (+)/deficit(-), unified budget	-65.6	-47.5	-50.6	-66.0	-57.0	2.2	-12.7	-23.9	-21.7	-2.1	-18.2	
Surplus (+)/deficit(-), off-budget agencies <u>5/</u>	-8.0	-11.4	n.a.	-10.8	-8.1	-.7	-2.0	-1.5	-3.3	-1.3	-4.7	
Means of financing combined deficits:												
Net borrowing from public	82.8	56.9	n.a.	68.9	69.3	9.4	18.0	17.9	22.2	8.5	20.4	
Decrease in cash operating balance	-7.2	n.a.	n.a.	7.4	-2.3	-6.8	-2.6	6.6	2.9	-4.1	2.0	
Other <u>6/</u>	-1.9	n.a.	n.a.	.5	-1.7	-4.0	-.7	1.0	0.0	-1.0	.5	
Cash operating balance, end of period	14.8	n.a.	n.a.	10.0	10.8	14.8	17.4	10.8	7.9	12.0	10.0	
Memo: Sponsored agency borrowing <u>7/</u>	3.4	n.a.	n.a.	3.2	2.8	.5	1.7	.3	.5	1.4	1.1	
<b>NIA Budget</b>						Seasonally adjusted, annual rates						
Receipts	311.4	n.a.	n.a.	349.3 <sup>8/</sup>	328.9	324.6	334.0	340.5	350.7	348.7	360.6	
Outlays	374.7	n.a.	n.a.	417.6	387.9	378.7	391.1	401.3	411.1	421.3	436.6	
Purchases (total)	128.8	n.a.	n.a.	141.8	133.2	131.2	134.5	138.0	140.5	142.9	145.9	
Defense	86.2	n.a.	n.a.	93.0	88.0	86.9	88.5	90.4	92.1	93.5	95.9	
Non-defense	42.6	n.a.	n.a.	48.9	45.2	44.2	46.0	47.6	48.4	49.4	50.0	
All other expenditures	245.9	n.a.	n.a.	275.8 <sup>8/</sup>	254.7	247.5	256.6	263.3	270.6	278.4	290.7	
Surplus (+)/deficit (-)	-63.3	n.a.	n.a.	-68.3 <sup>8/</sup>	-58.9	-54.0	-57.1	-60.8	-60.4	-72.6	-76.0	
High employment surplus (+)/deficit(-) (NIA basis) <u>9/</u>	-5.6	n.a.	n.a.	-8.6	-1.7	2.9	.3	-.6	-1.5	-13.4	-18.8	
	*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/ NIA data are preliminary.

5/ 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.

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 estimates now fully incorporate taxes on inventory profits beginning 1973.

## Comments on the Federal Sector Outlook

The staff now estimates that the unified budget deficit for fiscal year 1977 will total \$66 billion, about \$13 billion higher than the last Greenbook--due mainly to our more stimulative fiscal policy assumptions. The assumed \$12 billion calendar year 1977 tax reduction is expected to lower revenues by approximately \$8 billion in the fiscal year ending September 30, 1977. Tax receipts in this fiscal year are now projected to be approximately \$345 billion, down from the \$355 billion estimate presented in the previous Greenbook, a shift which also reflects somewhat lower levels of corporate profits before tax.

On the expenditure side, our assumptions in regard to increased aid for public service employment, and for state and local construction grants raise fiscal year 1977 spending by almost \$2 billion. In addition, the higher levels in recent and near-term unemployment rates are expected to add \$1 billion to income security payments. However, the staff estimates that these outlays will start to decline by mid-1977, as the effects of the stimulative fiscal package begin to be exerted on the economy. Total outlays for FY 1977 are now assumed to be about \$411 billion.

For calendar year 1977, the staff now forecasts that the full employment budget--reflecting the more stimulative fiscal package--will register a \$13 billion deficit. This compares to the \$2 billion deficit projected for CY 1976.



Given the expected tax cut, the average effective withheld tax rate for calendar year 1977 is projected to be only marginally smaller than the withheld tax rate observed in 1975-III, the first full quarter after the Tax Reduction Act of 1975 became effective. According to these estimates the assumed \$10 billion cut in personal taxes serves mainly to return tax rates to their earlier levels, by offsetting the effects of progressivity in the tax structure. These effects otherwise would have edged tax rates higher, due to the rise in nominal incomes which have occurred since mid-1975.

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DOMESTIC FINANCIAL DEVELOPMENTS

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Summary. Developments over the period since the November FOMC meeting have been marked by a sizable rally in money and credit markets, propelled in part by easing actions of the Federal Reserve System. The discount rate was lowered by one quarter of a percentage point and the Federal funds rate declined by around 35 basis points. In addition, markets were influenced by the sluggish behavior of  $M_1$  and weakness in the real economy. Short-term interest rates generally have dropped about one-half percentage point over the past four weeks. The market apparently expects some further accommodative action by the System, as short rates have dropped further below the funds rate, and dealers have accumulated larger inventories of securities.

Easier market conditions also have been transmitted to intermediate and longer-term securities markets. Declines in intermediate-term yields have been about the same magnitude as those on short-term securities, while most long-term rates have fallen less sharply--on the order of 25 to 35 basis points.

Lower open-market yields have helped sustain fund inflows at depository institutions. The volume of residential mortgage lending has remained sizable, particularly at savings and loan associations, and commercial banks have continued to expand their holdings of real estate loans. Consumer instalment debt has continued to grow at a moderate rate.

In the public sector, Treasury debt offerings since the mid-November refunding have been occurring at a fairly substantial pace, but in line with earlier market expectations. State and local bond issues have been heavy, with volume buoyed by some accelerations of offerings to take advantage of lower rates.

Public offerings of corporate bonds in November were the lightest for any month in two years, but accelerations and increases in the size of issues previously scheduled have served to raise the calendar for December. In short-term markets, business borrowing--which had strengthened in October--remained fairly strong last month. The recent strengthening in flows of short-term business credit may have been associated with inventory accumulation and a tapering off of the balance sheet restructuring that has been in train for quite some time.

Outlook. Over the next few months, the present reduced level of long-term market rates may encourage a continued high volume of corporate bond offerings. Such a development would dampen the growth of outstanding short-term business credit, as would also any reduction in the pace of inventory accumulation. Nevertheless, banks might experience a moderate further expansion in business loans (abstracting from the expected drop in holdings of bankers' acceptances early next year) in light of their on-going easing of price and nonprice lending terms.

In the State and local sector also there may be some augmentation of long-term debt issuance to take advantage of favorable market conditions. Such offerings may be mainly a substitute for borrowings at the shorter end of the maturity spectrum, with little impact on over-all financing.

In the Federal sector, financing is expected to be modest during the remainder of this month. In the first quarter, the Treasury is projected to raise about \$22 billion in new money--slightly less than the total in the first quarter of 1976.

Current patterns of growth in consumer and mortgage credit may well continue for awhile. The flow of residential mortgage credit is likely to remain ample, given record amounts of outstanding commitments at S&L's. Moreover, primary mortgage rates have moved downward only sluggishly, and mortgages are now a relatively attractive investment for commercial banks and mutual savings banks. Depository institutions, however, will undoubtedly continue to reevaluate offering terms on deposits, and as such claims become relatively less attractive, deposit growth may be dampened somewhat.

Flows of funds from other institutional investors probably will not be greatly changed in the near future. Life as well as fire and casualty insurance companies likely will experience sustained strong cash flows, encouraging a continuance of heavy bond acquisitions.

On balance, there seems to be little reason to expect that rising credit demands will put upward pressures on the level of interest rates over the next few months. Some adjustments in the rate structure may well take place, however. Short-term market rates are low relative to the funds rate, as noted above, and--absent any further monetary action--some technical upward adjustments in Treasury bill and other short-term rates could develop. On the other hand, at the long-end of the market, the primary mortgage rate seems unsustainably high relative to other rates and is likely to come under downward pressure.

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INTERNATIONAL DEVELOPMENTS

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Summary. The weighted average value of the dollar against ten leading currencies declined slightly (0.5 per cent) in the five weeks since the last Green Book, continuing to hold close to the level reached last April. Major exchange rate movements were registered by sterling and the Canadian dollar: sterling rose by 3.5 per cent, mainly on the strength of expectations that the conditions associated with an IMF stand-by arrangement of \$3.9 billion would stabilize the U.K. economy and that other assistance for sterling might be made available; the Canadian dollar dropped over 6 per cent to 96 U.S. cents following the election of a separatist party in Quebec, but has since recovered to a level of about 98 U.S. cents. Among other currencies, the Australian dollar was devalued by 17.5 per cent on November 28, but has since been revalued twice by a total of 3-1/4 per cent as a large capital reflow occurred; the Mexican peso has risen to around 5 cents from a level of about 4 cents, with the foreign exchange market in Mexico partially closed since November 22; and the lira has held steady

The trade deficit in the U.S. international accounts registered a \$10 billion annual rate in October, somewhat under the third quarter rate. The physical volume of non-agricultural exports continued a decline that began about mid-year. This decline was partly offset by

some rise in export prices. Agricultural exports were a record in October, mainly based on a jump in exports of corn to areas of Europe hit by a drought earlier in the year. On the import side, October non-fuel imports were not much changed from the third quarter rate, and imports of fuels, though still very large, were down somewhat from the summer months

Bank-reported capital flows with private foreigners showed a net inflow in October after a continuous net outflow in the first three quarters amounting to nearly \$6.0 billion. The October net inflow reflected primarily a large increase in borrowing from Euro-market sources as conditions shifted toward making short-term Eurofunds relatively more attractive than CDs.

U.S. net purchases of new foreign securities were temporarily low in October, but are expected to reach \$2.5 billion in the fourth quarter -- about the same as the quarterly average for the year. Foreigners, apart from OPEC countries, were net sellers of U.S. corporate stocks in October.

In international capital markets activity continued at a high level into October. Combining the three main segments of the market -- medium-term Euro-credits, Euro-bonds, and foreign bonds -- total funds raised this year through October amounted to about \$48 billion, compared with about \$43 billion for all of 1975. Conditions in all of these markets have tended to ease since mid-year, and rates of borrowing have continued high for both industrial and developing countries, with some OPEC countries also raising substantial amounts.

Economic activity abroad continues to present a picture of sluggish recovery, with increasing scepticism that present policies will yield satisfactory growth rates in the year ahead. However, since in most countries inflation rates remain stubbornly high, authorities are reluctant to shift from a fiscal policy stance that is aimed at trimming the fiscal stimulus provided during the recession. In Italy and the United Kingdom, in particular, external pressures have led to efforts to cut budget deficits.

Outlook. Incoming data in the past month have pointed to a further cutback in expectations for economic growth in foreign industrial countries -- to a real GNP growth in 1977 of about 3.7 per cent. Moreover, there appears to be a growing disparity between the economic performance, especially price trends, of the stronger countries -- the U.S., Germany and Japan -- and the performance of Italy, the U.K. and France. Such disparities, if continued, suggest that further movements of exchange rates are likely; on balance the staff, and market futures rates, continue to expect the average value of the dollar to rise perhaps 5 per cent by the end of next year.

In terms of the outlook for the U.S. international accounts, the trade deficit is expected to widen to about \$12 billion next year compared to last month's estimate of about \$9 billion. The change reflects mainly a delay in the delivery of oil from Alaska, together with somewhat weaker demand abroad and the assumption that U.S. activity will receive a stimulus. However, the projection also allows for the fact that new export orders, especially for machinery, have been quite strong in July-October, despite the slowdown abroad.



	1975	1976 <sup>P</sup>	1977 <sup>P</sup>	1976				1977 <sup>P</sup>			
				I	II	III	IV <sup>P</sup>	I	II	III	IV
<b>Billions of dollars</b>											
Net Exports of Goods and Services (GNP basis of net exports) <u>1/</u>	16.3 (20.5)	3.2 (7.8)	.3 (6.7)	4.2 (8.4)	6.3 (9.3)	.3 <sup>P</sup> (3.4)	2.0 (5.1)	3.6 (7.2)	-2.5 (1.6)	-2.2 (2.3)	1.8 (6.3)
Merchandise Trade Balance	8.9	-8.5	-12.5	-6.7	-5.1	-11.6	-10.6	-9.3	-15.1	-14.6	-11.2
Exports	107.1	114.9	128.8	107.3	113.8	118.8	119.6	123.0	126.5	130.4	135.1
Agricultural	22.2	24.1	23.2	21.3	23.5	25.3	26.1	23.5	23.1	22.8	23.2
Nonagricultural	84.8	90.8	105.6	86.1	90.3	93.6	93.5	99.5	103.4	107.6	111.9
Imports	98.1	123.4	141.3	114.0	118.9	130.4	130.2	132.3	141.6	145.0	146.3
Fuels	28.5	36.9	42.8	31.8	36.5	39.9	39.3	38.4	44.6	44.8	43.2
Nonfuels	69.5	86.5	98.5	82.3	82.5	90.6	90.9	93.9	97.0	100.2	103.1
Military and Service Transactions, net	7.3	11.7	12.8	10.9	11.4	11.9 <sup>P</sup>	12.6	12.9	12.6	12.4	13.0
Military transactions, net	-.9	.2	.7	--	-.1	.3 <sup>P</sup>	.5	.5	.6	.8	.8
Investment income, net	6.0	9.0	9.4	9.1	8.6	9.0 <sup>P</sup>	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 <sup>P</sup>	2.8	2.7	2.7	2.6	2.5
U.S. Current Account Balance <u>2/</u>	11.7	-.9	-4.1	-.2	2.8	-3.9 <sup>P</sup>	-2.3	-.7	-6.8	-6.6	-2.6
<b>Constant (1972) dollars</b>											
Merchandise exports (% change, annual rates)	64.6 (-2.4)	66.8 (3.4)	71.5 (7.0)	63.3 (-19.3)	66.5 (22.0)	68.7 (13.9)	68.6 (-.4)	70.0 (8.2)	70.7 (4.1)	71.8 (6.6)	73.3 (8.7)
Merchandise imports (% change, annual rates)	51.3 (-12.5)	62.3 (21.4)	65.6 (5.3)	59.0 (44.8)	60.4 (10.0)	65.3 (36.6)	64.4 (-5.7)	63.9 (-3.2)	65.8 (12.6)	66.4 (3.6)	66.0 (-2.4)
<b>Foreign Outlook - Major Industrial Countries <u>3/</u></b>											
Real GNP, % change, annual rate	-1.1	4.7	3.7	7.8	2.9	2.2 <sup>P</sup>	3.3	3.8	4.3	4.7	4.6
Wholesale Prices, % change, A.R. <u>4/</u>	6.0	9.5	9.6	11.4	16.9	11.9	8.6	9.3	9.2	7.8	7.7

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 in dollar terms of the six countries.

4/ Data are largely manufactured goods prices.

P/ Projected