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CONFIDENTIAL (FR)

March 15, 1978

SUMMARY AND OUTLOOK

By the Staff
Board of Governors
of the Federal Reserve System

SUMMARY AND OUTLOOK

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary. Economic activity apparently strengthened somewhat in February despite continuance of severe weather and the coal strike. Employment rose considerably and the unemployment rate edged down. Industrial production and factory hours recovered somewhat from their depressed January levels, and retail sales posted a fractional gain. At the same time, the pace of inflation increased, mainly in response to sharply higher prices for agricultural products and foods.

Industrial production is estimated to have increased half a per cent last month, recouping much of the January decline. Automobile assemblies increased to an 8.2 million annual rate, recovering about one-third of the January decline, while most other product and industrial groupings registered moderate increases. Winter storms continued to damp growth of production in February and the coal strike appears to have had only small indirect effects.

Nonfarm payroll employment rose 350,000 between mid-January and mid-February, with one-third of the advance in manufacturing. The 100-day old coal strike appears to have had little secondary impact on employment, at least through early March, but curtailments of working hours to conserve electricity appear to be limiting production in the most affected 11-State area. The gain in employment, with little change in the labor force, was sufficient to bring a further decline in the unemployment rate to 6.1 per cent, its lowest level since October 1974 and 1-1/2 percentage points below February 1977.

Total retail sales increased a bit in February but still appeared depressed by the continuing severe weather. Excluding autos and building materials retail sales were up 2.2 per cent, recovering about two-thirds of the January decline. Unit sales of new domestic-type autos picked up somewhat last month, rising 500,000 to an 8.5 million annual rate, and rose further to a 9.3 unit rate early in March. So far this year, however, the average sales pace has been well below the 9.1 million units sold in 1977.

Indicators of business investment spending continue to suggest moderate growth in 1978. The February survey of anticipated outlays for plant and equipment showed planned spending for 1978 to be 10.9 per cent above last year, or about 2 percentage points less than the 1977 rise. The 1978 increase now anticipated is larger than that indicated by the November survey because of a shortfall of spending late last year. Among other investment indicators, new orders for nondefense capital goods fell about half as much in January as they had risen in December, while nonresidential construction contracts rose somewhat further to a level well above earlier levels. Total contracts and orders were down over the month but the level was still above the fourth quarter average. The book value of manufacturers' inventories rose at a \$9 billion annual rate in January as shipments declined in part because of bad weather.

State and local governments continue to follow conservative spending policies; employment has risen only moderately in recent months

and construction activity, which was hampered by bad weather in January, has shown little growth in the last year. Because of this conservative approach to program expansion, many States are experiencing large operational surpluses, and there is now a strong likelihood of significant tax relief in a number of States. At the Federal level, spending continues to fall below the path deemed by OMB to be consistent with the FY 1978 budget and the Administration has revised down its spending estimate for the fiscal year from \$462 to \$454 billion.

Wholesale prices for finished goods rose sharply in February--by 1.1 per cent--about twice as much as the recent monthly average. The acceleration was concentrated in foods. Price increases for nonfood finished goods continued rising at a relatively moderate rate, 0.4 per cent. Reflecting the recent run-up in food prices and the initial impact of large minimum wage and payroll tax increases, the Consumer Price Index rose 0.8 per cent in January--about twice the average monthly rise during the second half of last year.

Outlook. Incoming data since the last FOMC meeting have not changed the staff's assessment of economic expansion through mid-1979, but the current quarter now appears somewhat weaker. Real GNP growth during the first quarter of 1978 is estimated at about a 3-1/2 per cent annual rate--down from the 4-1/2 per cent indicated last month. Given current information on the value of retail sales, real personal consumption outlays during the quarter are unlikely to change much from the advanced fourth quarter level. Furthermore, construction interruptions,

presumably weather-related, appear to have been more widespread than believed earlier; State and local government spending as well as private construction outlays were substantially reduced early in the quarter. However, manufacturing employment and industrial production showed significant increases in February indicating faster inventory accumulation for the quarter than we had anticipated earlier.

Growth in the second and third quarters of 1978 is projected to be a little higher than indicated last month due to a stronger rebound now expected for final sales as the weather improves.

The staff continues to assume that the indirect effects of the coal strike will be minimal, as current coal shipments, remaining inventories, shifts to other fuels and purchases of electricity appear likely to be sufficient to avert serious production disruptions. However, continuation of the coal strike well into March means inventories of basic fuels are likely to run down nearly \$8 billion (annual rate)--considerably more than anticipated in the February Greenbook.

Our tax and monetary policy assumptions are basically unchanged this month. The projection continues to incorporate the effects of a \$25 billion tax cut--two-thirds to individuals--effective October 1, 1978. For monetary policy, M-1 growth is assumed to average 5-1/4 per cent through 1979-QII, with short-term interest rates rising during the remainder of this year, particularly during the spring months. Federal unified outlays in fiscal 1978, however, were reduced \$3-1/2 billion to \$455 billion, reflecting recent weakness in spending and the Administration's

outlay re-estimates. Because financial transactions account for part of the downward revision, the impact on real activity is estimated to be small. Over the entire six quarter projection period, real output growth is projected to average 4-1/2 per cent, annual rate, about the same as indicated in February's Greenbook. Through mid-1979, real business fixed investment is expected to grow at a 6 per cent annual rate--somewhat stronger than suggested by the Commerce Department Survey of planned expenditures but still less than the 1977 increase. Real consumption is also expected to rise less than in 1977, partly because of slower income growth and rising debt burdens. Real residential construction expenditures are projected to begin to decline in the third quarter of 1978 as tighter mortgage markets dampen housing starts and sales.

Economic growth in the 4-1/2 per cent zone is expected to generate a further large increase in employment. However, with labor force growth also expected to be rapid, the unemployment rate is projected to decline only moderately to about 5.7 per cent by mid-1979. Gains in productivity still appear likely to average 2-1/2 per cent (annual rate) and in hourly compensation 9 per cent (annual rate); thus, increases in unit labor costs would average about 6-1/2 per cent. Although projected domestic price increases have been scaled up slightly--reflecting both the recent further decline of the dollar in foreign exchange markets and somewhat larger rises in food prices early this year--the underlying rate of inflation is still expected to be about in line with the rise in unit labor costs.

Details of the staff projections are shown in detail in the tables that follow.

STAFF GNP PROJECTIONS

	Per cent changes, annual rate							
	Nominal GNP		Real GNP		Gross business product fixed-weighted price index		Unemployment rate (per cent)	
	2/22/78	3/15/78	2/22/78	3/15/78	2/22/78	3/15/78	2/22/78	3/15/78
1974 ^{1/}	8.1	8.1	-1.4	-1.4	10.4	10.4	5.6	5.6
1975 ^{1/}	8.2	8.2	-1.3	-1.3	9.5	9.5	8.5	8.5
1976 ^{1/}	11.6	11.6	6.0	6.0	5.4	5.4	7.7	7.7
1977 ^{1/}	10.8	10.8	4.9	4.9	6.0	6.0	7.0	7.0
1978	11.1	11.1	4.6	4.4	6.2	6.4	6.2	6.0
1977-III ^{1/}	10.2	10.2	5.1	5.1	5.0	5.0	6.9	6.9
1977-IV ^{1/}	10.4	10.4	4.0	4.0	5.5	5.5	6.6	6.6
1978-I	11.8	11.1	4.4	3.4	6.8	7.3	6.3	6.2
1978-II	11.0	11.6	4.6	5.0	6.4	6.7	6.2	6.0
1978-III	10.4	10.6	4.2	4.5	6.2	6.2	6.2	6.0
1978-IV	11.8	11.8	4.8	4.8	6.2	6.2	6.1	5.9
1979-I	11.9	11.7	5.0	4.9	6.7	6.7	6.0	5.8
1979-II	10.8	10.8	4.5	4.4	6.4	6.4	5.9	5.7
Change:								
76-IV to 77-IV ^{1/}	11.9	11.9	5.7	5.7	6.2	6.2	-1.2	-1.2
77-II to 78-II	10.8	10.8	4.5	4.4	5.9	6.1	-.9	-1.1
77-IV to 78-IV	11.3	11.3	4.5	4.4	6.4	6.6	-.5	-.7
78-II to 79-II	11.2	11.2	4.6	4.6	6.4	6.4	-.3	-.3

^{1/} Actual.

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

	1977		1978				1979	
	III	IV	I	II	III	Projected IV	I	II
Gross National Product	1915.9	1963.7	2016.1	2072.4	2125.5	2185.5	2246.9	2305.2
Final purchases	1892.2	1953.0	1998.9	2051.7	2102.5	2160.5	2218.6	2275.8
Private	1491.3	1539.6	1577.3	1620.0	1660.6	1705.7	1753.1	1799.7
Excluding net exports	1498.8	1554.7	1587.2	1630.7	1671.9	1716.9	1763.4	1808.7
Personal consumption expenditures	1218.9	1260.2	1282.7	1315.9	1349.5	1387.6	1426.3	1462.9
Goods	659.4	686.3	690.8	710.0	728.6	750.0	769.7	788.7
Services	559.5	573.9	591.9	605.9	620.9	637.6	656.6	674.2
Gross private domestic investment	303.6	305.2	321.7	335.5	345.4	354.3	365.4	375.2
Residential construction	92.5	99.6	103.6	106.6	107.6	108.1	109.1	110.6
Business fixed investment	187.5	194.9	200.9	208.2	214.8	221.2	228.0	235.2
Change in business inventories	23.6	10.7	17.2	20.7	23.0	25.0	28.3	29.4
Nonfarm	23.1	6.2	15.2	19.7	23.0	25.0	28.3	29.4
Net exports of goods and services ^{1/}	-7.5	-15.1	-9.9	-10.7	-11.3	-11.2	-10.3	-9.0
Exports	179.9	173.6	185.4	194.0	201.9	209.3	217.7	224.5
Imports	187.4	188.7	195.3	204.7	213.2	220.5	228.0	233.5
Gov't. purchases of goods and services	400.9	413.4	421.6	431.7	441.9	454.8	465.5	476.1
Federal ^{2/}	148.1	153.8	155.9	158.3	161.3	166.9	170.5	174.1
State and local	252.9	259.6	265.7	273.4	280.6	287.9	295.0	302.0
Gross national product in constant (1972) dollars	1347.4	1360.7	1372.0	1388.9	1404.2	1420.7	1437.8	1453.4
Personal income	1549.8	1602.8	1639.8	1681.2	1729.3	1777.0	1821.1	1864.5
Wage and salary disbursements	998.9	1028.5	1053.4	1079.2	1105.2	1135.6	1166.9	1193.4
Disposable income	1323.8	1368.2	1401.5	1434.6	1472.9	1527.1	1567.2	1602.2
Saving rate (per cent)	5.5	5.5	6.0	5.8	5.9	6.7	6.6	6.3
Corporate profits with I.V.A. and C.C. Adj.	149.0	143.6	147.2	154.0	154.8	163.6	162.4	166.6
Corporate profits before tax	172.8	177.1	183.2	190.5	191.9	201.4	200.7	205.4
Federal government surplus or deficit (-) (N.I.A. basis)	-58.9	-61.5	-56.3	-49.6	-46.4	-62.8	-55.9	-49.1
High employment surplus or deficit (-)	-20.4	-21.7	-17.5	-12.2	-7.9	-28.1	-20.5	-13.8
State and local government surplus or deficit (-) (N.I.A. basis)	32.9	31.6	29.8	28.2	26.1	26.2	24.9	22.9
Excluding social insurance funds	17.4	15.9	12.3	10.2	7.6	7.2	5.4	2.9
Civilian labor force (millions)	97.6	98.6	99.1	99.7	100.3	100.9	101.5	102.0
Unemployment rate (per cent)	6.9	6.6	6.2	6.0	6.0	5.9	5.8	5.7
Nonfarm payroll employment (millions)	82.5	83.2	84.0	84.6	85.2	85.8	86.5	87.1
Manufacturing	19.6	19.8	20.1	20.3	20.5	20.7	21.0	21.2
Industrial production (1967=100)	138.4	139.3	139.4	142.6	145.4	148.0	150.7	153.0
Capacity utilization: all manufacturing (per cent)	83.0	82.9	82.1	83.3	84.2	84.9	85.6	86.1
Materials (per cent)	82.3	82.2	81.1	82.6	83.6	84.6	85.5	86.2
Housing starts, private (millions, A.R.)	2.04	2.14	1.85	2.05	1.85	1.75	1.80	1.80
Sales new autos, (millions, A.R.)	10.92	10.75	10.50	10.85	10.90	11.05	11.10	10.95
Domestic models	8.88	8.77	8.40	8.75	8.90	9.10	9.15	9.10
Foreign models	2.04	1.98	2.10	2.10	2.00	1.95	1.95	1.85

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

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

CHANGES IN GROSS NATIONAL PRODUCT
 AND RELATED ITEMS

	1977		1978				1979	
	III	IV	Projected				I	II
			I	II	III	IV		
----- Billions of dollars -----								
Gross National Product	46.0	47.8	52.4	56.3	53.1	60.0	61.4	58.3
Inventory change	1.9	-12.9	6.5	3.5	2.3	2.0	3.3	1.1
Final purchases	44.0	60.8	45.9	52.8	50.8	58.0	58.1	57.2
Private	33.7	48.3	37.7	42.7	40.6	45.1	47.4	46.6
Net exports	2.2	-7.6	5.2	-.8	-.6	.1	.9	1.3
Excluding net exports	31.5	55.9	32.5	43.5	41.2	45.0	46.5	45.3
Personal consumption expenditures	24.9	41.3	22.5	33.2	33.6	38.1	38.7	36.6
Goods	6.4	26.9	4.5	19.2	18.6	21.4	19.7	19.0
Services	18.4	14.4	18.0	14.0	15.0	16.7	19.0	17.6
Residential fixed investment	1.7	7.1	4.0	3.0	1.0	.5	1.0	1.5
Business fixed investment	5.1	7.4	6.0	7.3	6.6	6.4	6.8	7.2
Government	10.3	12.5	8.2	10.1	10.2	12.9	10.7	10.6
Federal	4.5	5.7	2.1	2.4	3.0	5.6	3.6	3.6
State and local	5.9	6.7	6.1	7.7	7.2	7.3	7.1	7.0
GNP in constant (1972) dollars	16.7	13.3	11.3	16.9	15.3	16.5	17.1	15.6
Final purchases	14.3	22.0	7.2	14.7	13.7	15.4	15.2	14.9
Private	10.3	19.3	5.8	12.0	11.1	13.5	12.7	12.3
----- In Per Cent Per Year ^{1/} -----								
Gross National Product	10.2	10.4	11.1	11.6	10.6	11.8	11.7	10.8
Final purchases	9.9	13.5	9.7	11.0	10.3	11.5	11.2	10.7
Private	9.6	13.6	10.2	11.3	10.4	11.3	11.6	11.1
Personal consumption expenditures	8.6	14.3	7.3	10.8	10.6	11.8	11.6	10.7
Goods	4.0	17.3	2.6	11.6	10.9	12.3	10.9	10.2
Services	14.3	10.7	13.1	9.8	10.3	11.2	12.5	11.2
Gross private domestic investment	12.4	2.1	23.4	18.3	12.3	10.7	13.1	11.2
Residential structures	7.7	34.6	17.1	12.1	3.8	1.9	3.8	5.6
Business fixed investment	11.6	16.6	12.9	15.3	13.3	12.5	12.9	13.2
Gov't. purchases of goods and services	11.0	13.1	8.2	9.9	9.8	12.2	9.7	9.4
Federal	12.9	16.4	5.6	6.3	7.8	14.6	8.9	8.7
State and local	9.9	11.2	9.7	12.1	11.0	10.8	10.2	9.8
GNP in constant (1972) dollars	5.1	4.0	3.4	5.0	4.5	4.8	4.9	4.4
Final purchases	4.4	6.8	2.1	4.4	4.0	4.5	4.4	4.3
Private	4.0	7.5	2.2	4.5	4.1	5.0	4.6	4.4
GNP implicit deflator ^{2/}	4.8	6.1	7.5	6.3	5.9	6.7	6.5	6.1
Gross business product fixed-weight price index ^{3/}	5.0	5.5	7.3	6.7	6.2	6.2	6.7	6.4
Personal income	8.9	14.4	9.6	10.5	11.9	11.5	10.3	9.9
Wage and salary disbursements	7.5	12.4	10.0	10.2	10.0	11.5	11.5	9.4
Disposable income	10.0	14.1	10.1	9.8	11.1	15.6	10.9	9.2
Corporate profits before tax	-2.7	10.3	14.6	16.8	2.9	21.4	-1.4	9.7
Nonfarm payroll employment	3.3	3.2	4.1	2.7	2.6	3.0	3.3	2.8
Manufacturing	1.3	2.7	6.6	4.0	4.4	4.5	4.4	4.1
Nonfarm business sector								
Output per hour	3.8	.5	2.9	2.0	2.3	2.3	2.4	2.1
Compensation per hour	7.5	7.3	11.4	7.7	7.9	7.9	11.3	8.0
Unit labor costs	3.5	6.8	8.5	5.7	5.6	5.6	8.9	5.9
Industrial production	4.2	2.6	.3	9.5	8.0	7.6	7.4	6.2
Housing starts, private	23.1	21.6	-44.5	50.8	-33.7	-19.9	11.9	.0
Sales new autos	-24.1	-6.2	-9.0	14.0	1.9	5.6	1.8	-5.3
Domestic models	-18.4	-4.8	-16.0	17.7	7.0	9.3	2.2	-2.2
Foreign models	-43.9	-12.3	27.3	.0	-17.7	-9.6	.0	-19.0

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

^{2/} Excluding Federal pay increases rates of change are: 1977-IV, 5.4 per cent; 1978-I, 7.4 per cent; 1978-IV, 6.1 per cent; 1979-I, 6.5 per cent.

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

March 15, 1978

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U.S. II FOMCGROSS NATIONAL PRODUCT AND RELATED ITEMS
(Expenditures and income figures are billions of dollars)

	1971	1972	1973	1974	1975	1976	1977	Projected 1978
Gross National Product	1063.4	1171.1	1306.6	1412.9	1528.8	1706.5	1890.1	2099.9
Final purchases	1057.1	1161.7	1288.6	1404.0	1540.3	1693.1	1872.6	2078.4
Private	823.4	908.6	1019.1	1101.3	1201.4	1331.7	1477.7	1640.9
Excluding net exports	821.8	911.9	1012.0	1095.3	1181.0	1323.9	1487.8	1651.7
Personal consumption expenditures	668.2	733.0	809.9	889.6	980.4	1094.0	1211.4	1333.9
Goods	374.8	410.5	457.5	498.3	542.2	601.6	660.6	719.8
Services	293.4	322.4	352.3	391.3	438.2	492.3	550.8	614.1
Gross private domestic investment	160.0	188.3	220.0	214.6	189.1	243.3	293.9	339.2
Residential construction	49.6	62.0	66.1	55.1	51.5	68.0	91.0	106.5
Business fixed investment	104.1	116.8	136.0	150.6	149.1	161.9	185.5	211.3
Change in business inventories	6.4	9.4	17.9	8.9	-11.5	13.3	17.4	21.5
Nonfarm	5.1	8.8	14.7	10.8	-15.1	14.9	16.4	20.7
Net exports of goods and services	1.6	-3.3	7.1	6.0	20.4	7.8	-10.1	-10.8
Exports	65.6	72.7	101.6	137.9	147.3	162.9	175.5	197.6
Imports	64.0	75.9	94.4	131.9	126.9	155.1	185.6	208.4
Gov't. purchases of goods and services	233.7	253.1	269.5	302.7	338.9	361.4	394.9	437.5
Federal	96.2	102.1	102.2	111.1	123.3	130.1	145.5	160.6
State and local	137.5	151.0	167.3	191.5	215.6	231.2	249.5	276.9
s national product in constant (1972) dollars	1107.5	1171.1	1235.0	1217.8	1202.1	1274.7	1337.5	1396.5
Personal income	859.1	942.5	1052.4	1154.9	1253.4	1382.7	1536.7	1706.8
Wage and salary disbursements	579.4	633.8	701.3	764.6	805.7	891.8	989.9	1093.3
Disposable income	742.8	801.3	901.7	984.6	1084.4	1185.8	1309.2	1459.0
Saving rate (per cent)	7.7	6.2	7.8	7.3	7.4	5.6	5.1	6.1
Corporate profits with I.V.A. and C.C. Adj.	77.2	92.1	99.1	83.6	99.3	128.1	139.3	154.9
Corporate profits before tax	82.0	96.2	115.8	126.9	123.5	156.9	171.2	191.7
Federal government surplus or deficit (-) (N.I.A. basis)	-22.0	-17.3	-6.7	-10.7	-70.2	-54.0	-49.9	-53.8
High employment surplus or deficit (-)	-5.3	-5.9	-.7	17.1	-20.3	-10.4	-8.6	-16.4
State and local government surplus or deficit (-) (N.I.A. basis)	3.7	13.7	13.0	7.5	5.9	18.4	29.3	27.6
Excluding social insurance funds	-3.8	5.6	4.1	-2.9	-6.2	3.9	13.7	9.3
Civilian labor force (millions)	84.1	86.5	88.7	91.0	92.6	94.8	97.4	100.0
Unemployment rate (per cent)	5.9	5.6	4.9	5.6	8.5	7.7	7.0	6.0
Nonfarm payroll employment (millions)	71.2	73.7	76.9	78.4	77.1	79.4	82.1	84.9
Manufacturing	18.6	19.1	20.1	20.0	18.3	19.0	19.6	20.4
Industrial production (1967=100)	109.6	119.7	129.8	129.3	117.8	129.8	137.0	143.8
Capacity utilization: all manufacturing (per cent)	78.0	83.1	87.5	84.2	73.6	80.2	82.4	83.6
Materials (per cent)	83.1	88.0	92.4	87.7	73.6	80.4	81.9	83.0
Housing starts, private (millions, A.R.)	2.05	2.36	2.05	1.34	1.16	1.54	1.99	1.87
Sales new autos (millions, A.R.)	10.24	10.93	11.42	8.91	8.66	10.12	11.13	10.82
Domestic models	8.68	9.32	9.65	7.49	7.08	8.63	9.07	8.79
Foreign models	1.56	1.61	1.77	1.42	1.58	1.50	2.06	2.04

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CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1971	1972	1973	1974	1975	1976	1977	Projected 1978
----- Billions of Dollars -----								
Gross National Product	81.0	107.7	135.5	106.3	115.9	177.7	183.6	209.8
Inventory change	2.6	3.0	8.5	-9.0	-20.4	24.8	4.1	4.1
Final purchases	78.5	104.6	126.9	115.4	136.3	152.8	179.5	205.8
Private	63.7	85.2	110.5	82.2	100.1	130.3	146.0	163.2
Net exports	-2.3	-4.9	10.4	-1.1	14.4	-12.6	-17.9	-7
Excluding net exports	66.0	90.1	100.1	83.3	85.7	142.9	163.9	163.9
Personal consumption expenditures	49.4	64.8	76.9	79.7	90.8	113.6	117.4	122.5
Goods	25.2	35.7	47.0	40.8	43.9	59.4	59.0	59.2
Services	24.3	29.0	29.9	39.0	46.9	54.1	58.5	63.3
Residential fixed investment	13.0	12.4	4.1	-11.0	-3.6	16.5	23.0	15.5
Business fixed investment	3.6	12.7	19.2	14.6	-1.5	12.8	23.6	25.8
Government	14.8	19.4	16.4	33.2	36.2	22.5	33.5	42.6
Federal	.6	5.9	.1	8.9	12.2	6.8	15.4	15.1
State and local	14.3	13.5	16.3	24.2	24.1	15.6	18.3	27.4
GNP in constant (1972) dollars	32.2	63.6	63.9	-17.2	-15.7	72.6	62.8	59.0
Final purchases	29.9	60.8	56.8	-8.6	2.1	54.2	59.9	56.7
Private	30.7	57.1	57.4	-13.8	-3.2	52.8	53.3	45.8
----- In Per Cent Per Year -----								
Gross National Product	8.2	10.1	11.6	8.1	8.2	11.6	10.8	11.1
Final purchases	8.0	9.9	10.9	8.9	9.7	9.9	10.6	11.0
Private	8.4	10.3	12.2	8.1	9.1	10.8	11.0	11.0
Personal consumption expenditures	8.0	9.7	10.5	9.8	10.2	11.6	10.7	10.1
Goods	7.2	9.5	11.4	8.9	8.8	11.0	9.8	9.0
Services	9.0	9.9	9.3	11.1	12.0	12.4	11.9	11.5
Gross private domestic investment	13.6	17.7	16.8	-2.5	-11.9	28.7	20.8	15.4
Residential structures	35.5	25.1	6.6	-16.7	-6.5	32.2	33.7	17.0
Business fixed investment	3.6	12.3	16.4	10.8	-1.0	8.6	14.5	13.9
Gov't. purchases of goods and services	6.8	8.3	6.5	12.3	12.0	6.6	9.3	10.8
Federal	.6	6.1	.1	8.7	11.0	5.5	11.8	10.4
State and local	11.6	9.8	10.8	14.5	12.6	7.2	7.9	11.0
GNP in constant (1972) dollars	3.0	5.7	5.5	-1.4	-1.3	6.0	4.9	4.4
Final purchases	2.8	5.5	4.9	-.7	.2	4.5	4.7	4.3
Private	3.7	6.7	6.3	-1.4	-.3	5.6	5.3	4.3
GNP implicit deflator	5.1	4.1	5.8	9.7	9.6	5.3	5.6	6.4
Gross business product fixed-weighted index ^{1/}	4.4	3.3	5.7	10.4	9.5	5.4	6.0	6.4
Personal income	7.2	9.7	11.7	9.7	8.5	10.3	11.1	11.1
Wage and salary disbursements	6.0	9.4	10.7	9.0	5.4	10.7	11.0	10.4
Disposable income	8.3	7.9	12.5	9.2	10.1	9.4	10.4	11.4
Corporate profits before tax	14.7	17.3	20.4	9.6	-2.7	27.0	9.1	12.0
Nonfarm payroll employment	.4	3.5	4.3	2.0	-1.7	3.1	3.4	3.3
Manufacturing	-4.0	2.8	5.1	-.1	-8.5	3.3	3.2	4.3
Nonfarm business sector								
Output per hour	2.9	3.0	1.7	-2.9	1.6	4.1	2.1	2.1
Compensation per hour	6.6	5.8	7.8	9.4	9.6	8.7	8.7	8.5
Unit labor costs	3.5	2.7	6.0	12.7	7.9	4.5	6.4	6.3
Industrial production	1.7	9.2	8.4	-.4	-8.9	10.2	5.5	5.0
Housing starts	43.1	14.9	-13.2	-34.6	-13.3	32.5	29.2	-5.9
Sales new autos	21.9	6.8	-4.7	-14.5	-2.8	16.9	9.9	-2.8
Domestic models	21.9	7.4	3.5	-22.4	-5.5	21.9	5.1	-3.1
Foreign models	21.8	3.1	9.7	-19.9	11.4	-5.1	37.2	-.8

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

FEDERAL SECTOR ACCOUNTS
(billions of dollars)

March 15, 1978

	FY 1977*	FY 1978 e/		FY 1979 e/		CY77* F.R. Board	CY78e/ F.R. Board	F.R. Staff Estimates								
		Admin. 1/	F.R. Board 2/	Admin. 1/	F.R. Board			Calendar quarters; unadjusted data						1979		
								1977		1978		1978		1979		
								III*	IV*	I	II	III	IV	I	II	III
Unified budget receipts	356.9	400.5	398.7	439.8	438.5	365.2	407.5	91.3	84.5	86.1	122.5	105.7	93.2	97.0	132.7	115.6
Unified budget outlays	401.9	453.5	455.0	499.4	499.0	416.1	463.6	103.4	113.3	110.0	113.7	117.9	122.0	121.0	126.0	130.0
Surplus(+)/Deficit(-), unified budget	-45.0	-53.0	-56.3	-59.6	-60.5	-50.9	-56.1	-12.2	-28.8	-23.9	8.8	-12.2	-28.8	-24.0	6.7	-14.4
Surplus(+)/Deficit(-), off-budget agencies 3/	-8.7	-11.5	-10.4	-12.5	-11.5	-10.4	-10.7	-4.9	-1.3	-3.6	-1.1	-4.3	-1.7	-3.9	-1.3	-4.6
Means of financing combined deficits:																
Net borrowing from public	53.5	57.1	56.7	72.0	71.3	56.8	64.8	19.6 ^{8/}	20.7 ^{8/}	21.3	1.5	13.2	28.9	25.4	-3.5	20.5
Decrease in cash operating balance	-1.7	7.1	7.1	0.0	0.0	-0.6	0.3	-2.8 ^{8/}	6.8 ^{8/}	5.5	-9.2	4.0	0.0	0.0	0.0	0.0
Other 4/	1.9	0.3	2.6	0.1	0.7	5.3	1.6	0.4	2.6	0.7	0.0	-0.7	1.6	2.5	-1.9	-1.5
Cash operating balance, end of period	19.1	12.0	12.0	12.0	12.0	12.3	12.0	19.1 ^{8/}	12.3	6.8	16.0	12.0	12.0	12.0	12.0	12.0
Memo: Sponsored agency borrowing 5/	5.2	n.a.	18.4	n.a.	13.6	6.8	19.5	1.1	2.0	4.1	5.0	7.3	3.1	2.5	3.5	4.5
NIA Budget								Seasonally adjusted annual rates								
Receipts	361.9 ^{6/}	n.a.	403.4 ^{6/}	n.a.	n.e.	373.7	415.8	373.2	385.3	396.9	409.7	428.5	427.9	442.1	455.5	n.e.
Outlays	411.9	n.a.	458.5	n.a.	503.0	423.5	469.5	432.1	446.7	453.2	459.3	474.9	490.7	498.0	504.6	518.7
Purchases (total)	140.6	n.a.	157.3	n.a.	172.4	145.5	160.6	148.1	153.8	155.9	158.3	161.3	166.9	170.5	174.1	178.0
Defense	91.8	n.a.	99.5	n.a.	107.9	94.3	100.9	95.6	98.5	99.1	99.7	100.6	104.1	106.6	109.2	111.9
Non-defense	48.8	n.a.	57.8	n.a.	64.4	51.2	59.7	52.5	55.3	56.8	58.6	60.7	62.8	63.9	64.9	66.1
All other outlays	271.4 ^{6/}	n.a.	301.2 ^{6/}	n.a.	330.6	278.0	308.9	284.0	292.9	297.3	301.0	313.6	323.8	327.5	330.5	340.7
Surplus(+)/Deficit(-)	-50.0 ^{6/}	n.a.	-55.1 ^{6/}	n.a.	n.e.	-49.8	-53.7	-58.9	-61.4	-56.3	-49.6	-46.4	-62.8	-55.9	-49.1	n.e.
High Employment Surplus(+)/Deficit(-) (NEA basis) 7/	-5.0	n.a.	-14.9	n.a.	-17.2	-8.6	-16.4	-20.4	-21.7	-17.5	-12.2	-7.9	-28.1	-20.5	-13.8	-6.3
	*actual	e--estimated	r--revised	n.e.--not estimated	n.a.--not available	p--preliminary										

- 1/ The Budget of the United States Government, Fiscal Year 1979, January 1978 and OMB Current Budget Estimates, March 1978.
- 2/ The Second Concurrent Resolution on the Budget (September 15, 1977) set the Congressional receipt and outlay targets at \$397 and \$458.3 billion, respectively.
- 3/ Includes Federal Financing Bank, Postal Service, U.S. Railway Association, Rural Electrification and Telephone Revolving fund, Housing for the Elderly or Handicapped Fund (until October 1977), and Pension Benefit Guaranty Corporation.
- 4/ Checks issued less checks paid, accrued items and other transactions.
- 5/ Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.
- 6/ Quarterly average exceeds fiscal year total by \$1.6 billion for FY 1977 and by \$1.7 billion for FY 1978 due to spreading of wage base effect over calendar year.
- 7/ Estimated by F.R.B. staff.
- 8/ Includes \$2.5 billion of borrowing from the Federal Reserve on September 30 which was repaid October 4.

Comments on the Fiscal Policy Outlook

According to recent Treasury data, Federal spending during January and February appears to have been about \$2 billion below earlier agency estimates. The Office of Management and Budget now expects spending to increase less than anticipated earlier, and as a result has lowered its estimate of the fiscal year 1978 outlays from \$462 to \$453-1/2 billion. The Administration's revisions were spread through most of the budget's functional categories but adjustments were particularly large in defense, energy (petroleum storage), interest, construction grants and financial transactions, especially for the Export-Import Bank and for the foreign military sales trust fund.

Since the staff had anticipated about two-thirds of the overall shortfall, our current outlay revision was much less than the Administration's. However, the staff's current outlay forecast of \$455 billion is about \$1-1/2 billion above the Administration's most recent estimate, mainly because we expect outlays for farm aid and interest^{1/} to be higher than currently budgeted. The staff's receipts projection is essentially unchanged from last month at \$398-1/2 billion.

The staff now anticipates that the combined deficit (unified plus off-budget) in the current fiscal year will be around \$66-1/2 billion. The Treasury has already raised \$35 billion during this fiscal year,

^{1/} The revised budget assumes a constant 6.4 per cent bill rate for fiscal years 1978 and 1979.

including \$14-1/2 billion since January 1, 1978. Another \$8 to \$10 billion in additional new financing is expected in the market before the April 15 tax date. During the remainder of the second quarter, seasonally high tax receipts should enable the Treasury to pay down around \$8 to \$10 billion of marketable debt.

Fiscal year 1979 outlays now are projected at \$499 billion, about in line with the Administration's latest estimate. Our spending forecast, however, continues to differ somewhat in composition from that of the Administration. As in the current fiscal year, the staff expects that fiscal year 1979 outlays for interest and for farm price supports will be higher than currently budgeted. On the other hand, spending for a number of grant and transfer programs appears likely to be below Administration estimates. The staff continues to assume passage of a \$25 billion reduction (net) in personal and corporate taxes. Although our tax assumptions remain unchanged, the fiscal year 1979 receipts forecast has been revised upward \$3 billion to \$438-1/2 billion, mainly due to reestimates of tax refunds.

The full employment budget, which attempts to measure changes in discretionary fiscal policy, continues to show a large \$20 billion increase in the deficit for the fourth quarter of 1978, reflecting the implementation of the assumed tax cut.

DOMESTIC FINANCIAL DEVELOPMENTS

There has been no notable change in the structure of interest rates during the past few weeks, except for some decline in yields on shorter-dated Treasury bills associated with strong demand from foreign official institutions. Major factors affecting the public's expectations about monetary policy have tended to offset one another-- slower expansion of the economy and the monetary aggregates on one side, and pressure on the dollar and sharply rising price indexes on the other.

M-1 declined at a 4 per cent annual rate in February. Apart from the possible impacts of lagging tax refunds and imperfect seasonal adjustment, the February drop appears to reflect the slackening of economic expansion associated with the severe winter weather and the coal strike. M-2 and M-3 also decelerated last month, reflecting the drop in M-1 and slow growth in interest-bearing deposits subject to Federal rate ceilings. The strong competition from higher-yielding market instruments was evidenced by another large increase in the assets of money market mutual funds and by a substantial volume of noncompetitive tenders in Treasury bill auctions.

Under these circumstances, depository institutions have added further to their money market liabilities and other indebtedness in order to meet customers' demands for credit. Large time deposits at commercial banks increased \$6 billion in February, and nondeposit funds also rose markedly. The outstanding indebtedness of savings and loan associations to Home Loan Banks increased rapidly in February and in early March.

Bank credit expanded at a 10 per cent annual rate in February. Business loan growth remained rapid; expansion of consumer and mortgage loans is estimated to have slowed slightly, extending the trend of the past half year. In addition, banks added substantially to their holdings of Treasury securities--the first gain in 8 months. This probably was a transitory phenomenon, reflecting heavier than usual Federal financing during the month.

Outstanding commercial paper of nonfinancial firms declined in February, and total borrowing by such businesses at banks and in the commercial paper market continued at about its average pace since mid-1977. Public bond offerings remained at a relatively low level, and underwriters report that private placement activity has abated somewhat since year-end.

Net mortgage lending and outstanding commitments at S&L's declined appreciably in January. Inclement weather may have played a major part, but cash flow pressures appear to have prompted a firming in S&L lending policies since last fall. Origination of FHA/VA mortgages slowed in February, owing in considerable measure to the large discounts prevailing on such loans; a 1/4 percentage point increase at the end of the month in FHA/VA home mortgage ceilings to 8-3/4 per cent still left significant discounts. Reflecting the relatively attractive prices on commitments they had obtained earlier from FNMA, mortgage bankers stepped up their deliveries of FHA/VA mortgages to FNMA last month, while sharply decreasing their issuance of GNMA pass-throughs.

State and local bond issuance in February was somewhat less than in the preceding month, and municipal yields remained exceptionally low relative to rates on taxable securities. Treasury credit demands have continued sizable--although a bit below the staff's earlier expectations, because of lagging Federal outlays. Sponsored credit agency borrowing--primarily FHLB and FNMA--was heavy in February in both short- and long-term security markets.

Outlook. Private demands for credit appear to have eased somewhat in the current quarter, partly as a consequence of the transitory effects of the weather and the coal strike. If economic activity picks up as expected during the spring, it is likely that credit demands will begin to press harder on available supplies--assuming growth of the monetary aggregates within the ranges set by the FOMC.

In the nonfinancial corporate sector, the gap between capital expenditures and internal funds generated is projected to widen in the second quarter. Firms may increase their issuance of bonds, as well as expand their borrowing through commercial mortgages; the strong cash flows of life insurance companies and pension funds should enable them to supply a large proportion of these funds. Business borrowing at banks is expected to remain strong, and this, in conjunction with continued demands for residential mortgage and consumer credit, is likely to exert further pressure on bank liquidity positions.

Household demand for instalment credit may grow somewhat over the near-term as consumer spending strengthens again. In the home mortgage market, demands for credit should continue strong, but borrowers are likely to encounter rising interest rates and increasingly stringent nonprice terms as thrift institutions attempt to bring their lending commitments into a more comfortable alignment with their cash flow. Further reduction of liquid asset holdings--perhaps facilitated by a cut in FHLBB requirements--and continued heavy use of FHLB advances should permit S&L's to limit the decline in their lending. FNMA's net mortgage acquisitions may increase; outstanding standby purchase commitments have grown considerably of late. Reflecting their sizable lending, the FHLB System and FNMA will remain heavy borrowers in the months ahead.

The aggregate budgetary surplus of State and local governments is expected to diminish in the second quarter. The staff expects this to be reflected primarily in reduced liquid asset accumulation; bond issuance probably will remain around its recent more moderate level, while short-term borrowing will rise seasonally, led by the \$4 billion New York State spring financing operation.

Treasury financing demands, however, are likely to place less pressure on credit markets in the months immediately ahead than in the early part of the year. The Federal budget will swing into seasonal surplus in the second quarter, and although a moderate amount of new cash may be raised through regular coupon financings, this borrowing will be more than offset by a pay-down of cash management bills maturing shortly after the mid-April income tax date.

INTERNATIONAL DEVELOPMENTS

Summary. During the last three weeks several currencies came under strong pressure in the exchange markets and actions were taken by the U.S., German, Swiss and Japanese authorities to counter these pressures.

, the trade-weighted value of the dollar against major currencies rose slightly. The Japanese yen was in very strong demand in the period.

. On March 15 the Japanese authorities announced several measures intended to stem capital inflows. Earlier in the period the Swiss franc fell back sharply after tightening of measures to discourage capital inflows.

On March 13 the U.S. and German authorities announced agreement on measures to provide support for the dollar. These measures included a doubling of the swap line with the Bundesbank to \$4 billion, and arrangements to use SDR 600 million (about \$740 million) to acquire deutschmarks, if necessary, together with an indication of greater agreement on economic policies. Apparently more decisive actions were expected by the market and the immediate reaction was negative. Additional intervention for account of the System and the Treasury brought net U.S. sales of German marks for the period to \$567 million equivalent. Exchange market activity in the week of March 13 included some strengthening of the French and Italian currencies in response to political developments in those countries.

The U.S. trade deficit for January continued to be very large at about a \$37 billion annual rate on the international transactions basis. The interpretation of recent trade data has been complicated by the effects of a two-month dock strike ending November 20 and a change of the method for compiling these data. Nevertheless, it appears that U.S. exports continued through January to show no upward momentum, while imports continued to rise in line with U.S. economic activity.

Data reported on private banking transactions in January show a rise in net outflows - probably largely reflecting seasonal factors. Foreign lending by U.S. banks' domestic offices and foreign branches decelerated somewhat in the fourth quarter of 1977. The slowdown of lending during 1977 affected claims on most areas, and was noteworthy for two of the largest borrowers, Brazil and Mexico, whose external accounts have improved markedly.

Some signs of economic resurgence appeared in Germany and Japan in the fourth quarter of last year and early this year. So far, output growth remains generally sluggish in the other major foreign industrial countries. Inflation rates have continued the downtrend generally established in 1977, but rates of increase in consumer prices remain relatively high in most countries. Large current-account imbalances remain; while some countries have continued to reduce their deficits, Japan's current account in January again recorded a strong surplus.

Among major foreign countries trade developments last year were characterized by a cutback in import volumes while exports continued to grow, but at a reduced pace.

Outlook. Current projections of the U.S. trade and current account balances through the middle of next year are not much changed from those of a month ago -- the trade deficit for 1978 is estimated at \$33 billion and the current account deficit at \$21 billion, both up slightly from 1977. The trade and current account deficits are projected to level off midway through 1978. This projection reflects steady growth of the U.S. economy while activity abroad is expected to expand at higher rates than in 1977 and it also allows for the considerable depreciation of the dollar since last September. However, should the unexpectedly high rates of trade deficit recorded recently persist for another month or two, with little pick-up in exports in response to gains in economic activity abroad a significant change in the outlook for the international accounts would be indicated.

Reviewing exchange market developments in recent weeks, the staff has become increasingly impressed by the degree of market pessimism about the dollar. However, the staff does not anticipate a further substantial change in the average value of the dollar a year from now, though it does expect some further depreciation against a few strong currencies.

	1976	1977 ^P	1978 ^P	1977				1978 ^P				1979 ^P	
				I	II	III	IV ^P	I	II	III	IV	I	II
1. GNP NET EXPORTS - Intl Acct. data	7.7	-9.0	-8.1	-7.6	-9.1	-6.9	-12.5	-7.3	-8.1	-8.7	-8.6	-7.7	-6.4
2. (GNP net exports - GNP Acct. data) <u>1/</u>	(7.8)	(-10.1)	(-10.8)	(-8.2)	(-9.7)	(-7.5)	(-15.1*)	(-9.9)	(-10.7)	(-11.3)	(-11.2)	(-10.3)	(-9.0)
3. a) Merchandise Trade Balance	-9.3	-31.4*	-32.9	-28.6	-31.2	-30.2	-35.5*	-31.2	-32.4	-33.9	-34.4	-34.6	-33.7
4. Exports (excl. military)	114.7	120.4*	135.2	117.8	122.4	123.5	118.0*	126.5	132.6	138.1	143.4	149.1	154.5
5. Agricultural	23.4	24.3*	23.6	24.4	26.7	24.0	22.2*	23.5	23.4	23.6	23.9	24.1	24.3
6. Nonagricultural	91.3	96.1*	111.6	93.4	95.6	99.4	95.8*	103.0	109.2	114.5	119.5	125.0	130.2
7. Imports	124.0	151.8*	168.1	146.4	153.6	153.7	153.5*	157.7	165.0	172.0	177.8	183.7	188.2
8. Petroleum and petrol. products	34.6	44.8*	45.9	44.1	47.7	45.8	41.5*	41.7	44.8	47.9	49.4	51.0	51.3
9. Nonpetroleum	89.4	107.0*	122.2	102.4	105.9	107.9	112.0*	116.0	120.2	124.1	128.4	132.7	136.9
10. b) Military transactions, net <u>2/</u>	--	1.6	2.0	1.7	.8	1.9	1.8	2.0	2.0	2.0	2.0	2.0	2.0
11. c) Investment income, net <u>3/</u>	14.3	18.5	20.2	17.9	19.1	18.4	18.5	19.6	19.9	20.5	20.8	21.8	22.2
12. d) Other services, net <u>4/</u>	2.7	2.3	2.6	1.4	2.1	3.1	2.7	2.3	2.4	2.7	3.0	3.1	3.1
13. U.S. CURRENT ACCOUNT BALANCE	-1.4	-19.0	-20.7	-16.9	-18.6	-17.4	-23.5	-19.3	-20.7	-21.4	-21.7	-21.6	-20.5
14. a) GNP net exports (line 1.)	7.7	-9.0	-8.1	-7.6	-9.1	-6.9	-12.5	-7.3	-8.1	-8.7	-8.6	-7.7	-6.4
15. b) U.S. Govt & private transfers <u>5/</u>	-9.1	-10.0	-12.6	-9.3	-9.5	-10.5	-11.0	-12.0	-12.6	-12.7	-13.1	-13.9	-14.1
Constant (1972) dollars													
16. Merchandise exports (excl. military)	66.7	66.9	71.7	66.1	67.6	68.7	65.1	68.9	71.1	72.7	74.2	75.9	77.3
17. (% change, annual rates)	(3.4)	(0.3)	(7.2)	(-7.4)	(9.5)	(6.1)	(-22.5)	(25.8)	(13.0)	(9.5)	(8.7)	(9.1)	(7.8)
18. Merchandise imports	62.8	71.1	73.3	70.3	72.0	71.2	70.9	70.9	72.5	74.3	75.6	76.7	77.4
19. (% change, annual rates)	(22.5)	(13.2)	(3.1)	(28.2)	(10.0)	(-4.9)	(-1.6)	(0)	(10.0)	(10.0)	(7.4)	(5.7)	(3.7)
Foreign Outlook - Major Industrial Countries <u>6/</u>													
20. Real GNP, % change, annual rates	5.2	2.8	3.8	5.7	-0.4	1.2	3.7	4.9	4.9	4.5	4.5	4.5	4.5
21. Wholesale Prices, % change, A.R. <u>7/</u>	9.4	8.7	5.1	10.4	7.4	3.7	2.8	5.3	6.6	6.1	6.1	5.7	5.7

1/ Differs from Intl. Acct. data (line 1) in the inclusion of revisions and new data.

2/ Excludes grants to Israel under military assistance acts and exports financed by those grants.

3/ Excludes U.S. Govt. interest payments to foreigners, which are included in line 15.

4/ Includes travel, transportation, fees and royalties, and miscellaneous other service transactions.

5/ Includes U.S. Govt. grants, U.S. Govt. interest payments to foreigners, remittances and pensions, and exports to Israel financed by U.S. military assistance grants.

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

7/ Data are largely manufactured goods prices.

P/ Projected

e/ Estimated

* Published data.