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March 21, 1984

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee

By the staff of the Board of Governors of the Federal Reserve System

DOMESTIC NONFINANCIAL DEVELOPMENTS

Recent Developments. Economic activity appears to have expanded at a considerably more rapid rate in early 1984 than in the last quarter of 1983. Private domestic spending, especially for housing and automobiles, has been very strong, and there have been substantial gains in industrial production. Part of the surge in demand is being met by foreign supply, however, and it appears that the trade deficit is reaching a new record high. Inflation rates have moved up from last year, but the rise has been concentrated in the food sector. Wage increases have thus far remained moderate despite firming labor market conditions.

Industrial production rose 1.2 percent in both January and February, considerably above the monthly gains in the fourth quarter. Increases in output were widespread across products and materials. Production of all major categories of consumer goods expanded strongly, but auto output was about unchanged in February at an annual rate of 8 million units. Output of defense equipment and construction supplies increased rapidly in both months, and the increase in business equipment also was strong. In February the rate of capacity utilization in manufacturing rose to 81 percent, its highest level since May 1981.

The expansion in output in January and February generated substantial gains in employment. Payroll employment rose 385,000 in February, considerably above the 290,000 average monthly increase during the preceding six months. The factory workweek, which jumped half an hour in January, remained unchanged at its highest level since 1967. The strong growth in labor demand was associated with some speedup in labor force, growth,

reflecting higher participation of both teenagers and adult females. The civilian unemployment rate continued to fall 0.2 percentage point each month; at 7.8 percent in February, the jobless rate was nearly 3 percentage points below its peak in December 1982.

Reflecting both continuing high levels of consumer confidence and large gains in income, consumer spending continued at a high level through February. Retail sales soared 3.3 percent in January and fell back only slightly in February. The February sales pace was about 4 percent above the fourth-quarter average, with gains generally widespread across expenditure categories. Sales of domestic autos, which averaged nearly 8.5 million units at an annual rate for the two months, were especially strong. This pace, the best performance since 1979, was well above the 7.3 million unit selling rate in the fourth quarter of last year. Between January and February sales of foreign units declined from a 2.6 to 2.2 million unit annual rate, reflecting in part tight supplies of Japanese cars as the export-restraint year ends in March.

Housing activity has strengthened considerably since the beginning of the year. After jumping 17 percent in January, housing starts tacked on another 11 percent gain in February, reaching a 2.2 million unit annual rate, the highest monthly figure in six years. New building permits have exhibited nearly as much strength. Sales of new and existing homes also continued strong through January, and are now at their highest level since 1980. The rapidly expanding housing market reflects a number of factors: rising family income, demand that had been postponed during the recession, and the increasing use of adjustable-rate mortgages which often carry discounted initial rates.

Business fixed investment also appears to be increasing vigorously. Although shipments of nondefense capital goods fell 5.6 percent in January after two months of substantial increases, there was a huge rise in imports of capital goods in January, indicating that domestic demand for equipment is still rising. New orders for nondefense capital goods rose further. Nonresidential construction put in place also has been strong, rising 2.7 percent in December and 0.7 percent in January, with the expansion concentrated in commercial and industrial construction. Finally, compared with the autumn results, the latest surveys of investment plans show considerable upward revisions in spending plans for 1984.

With sales and shipments increasing briskly, inventory accumulation in January was again modest: manufacturing and trade inventories rose at an annual rate of \$5 billion in constant-dollar terms, less than the investment in the fourth quarter of last year. The accumulation has occurred mainly at trade outlets other than auto dealers; little restocking has taken place so far in this recovery in the manufacturing sector.

Wage increases have remained moderate in recent months. The index of hourly earnings for production workers rose only 3-1/4 percent at an annual rate in the three months ending in February. In 1983, this measure increased about 4 percent. Changes in payroll taxes for social security effective January 1 will add almost 2 percentage points (annual rate) to the first quarter's hourly compensation figure.

Inflation rates moved higher in early 1984. The PPI rose at a 6 percent annual rate in January and February, after being little changed

in the final months of 1983, while the CPI increased at a 7-1/2 percent annual rate in January, with sharply higher food prices a major factor. Excluding food and energy, the CPI rose at a 6-1/2 percent pace, somewhat above the nearly 5 percent increase during 1983.

Outlook. The staff estimates that real GNP will increase about 8 percent at an annual rate in the first quarter, an acceleration from the 5 percent rate of expansion in the final quarter of 1983. (The Commerce Department's flash estimate for first-quarter growth is 7-1/4 percent.) Spurred by exceptionally strong demand for autos, consumption spending appears to be expanding at about the same high rate as in the fourth quarter. Also, contributing to the sharp advance in output is a step-up in housing construction, which had fallen off somewhat last quarter. Business fixed investment is also expanding rapidly, although at less than the astonishing fourth-quarter pace. In addition, a sizable swing is projected in inventory investment in both the nonfarm and farm sectors, with the rise in private farm inventories offsetting a reduction in recorded federal spending as CCC stocks are released under the PIK program. A moderate growth in exports is projected to be more than offset by a rapid rise in imports, and therefore net exports are anticipated to continue to weaken.

The staff's assumptions about monetary policy are little changed since the last Greenbook. M1 and M2 are assumed to grow this year at rates around or a little above the midpoints of the FOMC's ranges, and then to slow a little over 1985. Because of the anticipated greater strength of aggregate demand in the economy in this forecast, interest

rates are expected to reach higher levels over the projection period than previously thought. For fiscal policy, the staff expects that on a unified budget basis the federal deficit will run about \$178 billion in fiscal year 1984 and roughly \$186 billion in fiscal year 1985. Deficit-reduction efforts are expected to have no real impact in the current fiscal year, but the budget estimate for fiscal 1985 assumes a \$20 billion package of revenue and spending measures.

After rising 6-1/4 percent during 1983, real GNP is expected to increase about 5-1/4 percent over the four quarters of 1984, a higher-than-average rate of expansion for a second year of recovery. The above-average growth is concentrated in the first half of the year reflecting the acceleration in spending on automobiles and housing and the recent very strong pace of business fixed investment. The swing in inventory investment also boosts the growth in output in the first half. With inventory investment and auto demand leveling off, and housing activity edging down in response to higher interest rates, output growth is expected to moderate considerably in the second half of this year and during 1985, when real GNP growth is projected to slow to about 3 percent. The impetus for continued expansion should come from business fixed investment, government purchases, and with rising world economic activity and an expected further decline of the dollar, from export demand. Consumption is expected to rise about in line with income.

The staff expects more rapid increases in wages and prices this year than last partly because of greatly diminished slack in labor and product markets. Also contributing to higher inflation are the large increase in

Social Security taxes, higher food prices, and the projected further depreciation of the dollar. The small size of projected increases in energy prices, by contrast, should help moderate the inflation rate. On balance, during 1984 the gross domestic business product (GDBP) fixed-weighted price index is projected to rise about 5 percent, compared with the rise of about 4-1/4 percent last year.

During 1985 the GDBP fixed-weighted price index is expected to rise about 5-3/4 percent as the unemployment rate is projected to be around 6-1/2 percent and the capacity utilization rate in manufacturing around 85 percent throughout the year. Hourly compensation is expected to accelerate to 6-1/2 percent after rising 5-3/4 percent this year. Rapidly rising import prices are projected to affect domestic inflation more significantly next year. In contrast, slowly rising energy prices are expected to hold down inflation, and no further food price shocks are projected. Excluding food and energy, the GDBP measure of inflation is expected to rise about 6 percent during next year, one percentage point above the expected increase this year.

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STAFF GNP PROJECTIONS

Percent changes, annual rate										
Nominal GNP		Real GNP		Gross domestic business product fixed-weighted price index				Unemployment rate (percent)		
				Total		Excluding food and energy				
1/25/84	3/21/84	1/25/84	3/21/84	1/25/84	3/21/84	1/25/84	3/21/84	1/25/84	3/21/84	
Annual changes:										
1982 <1>	4.0	4.0	-1.9	-1.9	6.0	6.0	6.9	6.9	9.7	9.7
1983 <1>	7.7	7.7	3.3	3.4	4.3	4.2	5.1	5.1	9.6	9.6
1984	9.7	10.8	5.1	6.3	4.7	4.7	4.8	4.8	7.7	7.2
1985	8.6	8.7	3.6	3.3	5.1	5.5	5.2	5.7	7.2	6.6
Quarterly changes:										
1983 Q1 <1>	8.2	8.2	2.6	2.6	3.6	3.6	6.7	6.7	10.4	10.4
Q2 <1>	13.3	13.3	9.7	9.7	4.1	4.1	3.5	3.5	10.1	10.1
Q3 <1>	11.5	11.5	7.6	7.6	4.7	4.7	5.6	5.6	9.4	9.4
Q4 <1>	8.6	9.1	4.5	5.0	4.5	4.1	5.0	4.4	8.5	8.5
1984 Q1	10.1	13.1	4.7	8.0	4.8	4.8	4.6	4.6	8.0	7.8
Q2	8.8	10.3	4.4	6.0	4.8	4.8	4.9	4.9	7.8	7.2
Q3	8.8	8.9	4.3	4.0	4.8	5.1	4.6	5.0	7.6	6.9
Q4	8.6	8.4	3.8	3.1	4.9	5.3	4.8	5.3	7.5	6.8
1985 Q1	8.8	8.7	3.4	3.1	5.0	5.4	5.2	5.7	7.4	6.7
Q2	8.4	8.1	3.4	2.7	5.2	5.6	5.3	5.9	7.3	6.6
Q3	8.4	8.8	3.1	2.9	5.3	5.9	5.6	6.2	7.1	6.5
Q4	8.4	8.9	2.9	2.8	5.4	6.1	5.9	6.4	7.0	6.5
Two-quarter changes: <2>										
1983 Q2 <1>	10.7	10.7	6.1	6.1	3.9	3.9	5.1	5.1	-1.5	-1.5
Q4 <1>	10.0	10.3	6.0	6.3	4.6	4.4	5.3	5.0	-1.6	-1.6
1984 Q2	9.4	11.7	4.6	7.0	4.8	4.8	4.7	4.7	-1.7	-1.3
Q4	8.7	8.6	4.0	3.6	4.9	5.2	4.7	5.2	-1.3	-1.4
1985 Q2	8.6	8.4	3.4	2.9	5.1	5.5	5.3	5.8	-1.2	-1.2
Q4	8.4	8.8	3.0	2.9	5.4	6.0	5.7	6.3	-1.3	-1.1
Four-quarter changes: <3>										
1982 Q4 <1>	2.6	2.6	-1.7	-1.7	4.7	4.7	5.4	5.4	2.4	2.4
1983 Q4 <1>	10.4	10.5	6.1	6.2	4.3	4.2	5.2	5.1	-2.1	-2.1
1984 Q4	9.1	10.2	4.3	5.3	4.8	5.0	4.7	5.0	-1.0	-1.7
1985 Q4	8.5	8.6	3.2	2.9	5.2	5.8	5.5	6.1	-1.5	-1.3

<1> Actual.

<2> Percent change from two quarters earlier.

<3> Percent change from four quarters earlier.

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CONFIDENTIAL - FR
CLASS II FOMC

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

	1982				1983			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	3021.4	3070.2	3090.7	3109.6	3171.5	3272.0	3362.2	3436.2
Final sales	3047.1	3081.4	3095.6	3165.9	3210.9	3286.6	3353.7	3416.6
Private	2417.3	2449.8	2439.9	2486.2	2533.5	2603.2	2655.4	2717.6
Domestic final purchases	2387.4	2416.5	2439.0	2480.6	2516.5	2611.7	2673.7	2743.7
Personal consumption expenditures	1938.9	1972.8	2008.8	2046.9	2073.0	2147.0	2181.1	2230.9
Goods	989.1	997.6	1010.0	1025.1	1035.6	1077.3	1097.6	1123.6
Services	949.7	975.2	998.9	1021.8	1037.4	1069.7	1083.5	1107.3
Gross private domestic investment	422.9	432.5	425.3	377.4	404.1	450.1	501.1	532.5
Residential structures	87.3	91.0	87.9	96.8	111.3	128.4	141.5	138.8
Business fixed investment	361.3	352.7	342.3	337.0	332.1	336.3	351.0	374.0
Change in business inventories	-25.7	-11.2	-4.9	-56.4	-39.4	-14.5	8.5	19.6
Nonfarm	-27.6	-8.8	-2.3	-53.7	-39.0	-10.3	18.4	19.7
Net exports of goods and services <1>	29.9	33.3	.9	5.6	17.0	-8.5	-18.3	-26.1
Exports	358.4	364.5	346.0	321.6	326.9	327.1	341.1	346.5
Imports	328.5	331.2	345.0	316.1	309.9	335.6	359.4	372.6
Gov't. purchases of goods and services	629.8	631.6	655.7	679.7	677.4	683.4	698.3	699.0
Federal <2>	249.7	244.1	261.7	279.2	273.5	273.7	278.1	274.1
State and local	380.0	387.5	394.0	400.5	404.0	409.7	420.2	424.9
Gross national product in constant (1972) dollars	1485.8	1489.3	1485.7	1480.7	1490.1	1525.1	1553.4	1572.5
Personal income	2528.1	2563.2	2591.3	2632.0	2657.7	2713.6	2761.9	2835.2
Wage and salary disbursements	1542.8	1563.8	1579.8	1586.0	1610.7	1648.4	1681.9	1717.3
Disposable personal income	2127.9	2159.0	2191.5	2227.8	2255.9	2301.0	2361.7	2423.9
Saving rate (percent)	6.1	5.9	5.6	5.4	5.4	4.0	4.9	5.2
Corporate profits with I.V.A. and C.C. Adj.	162.0	166.8	168.5	161.9	181.8	218.2	248.4	268.1
Corporate profits before tax	173.2	178.8	177.3	167.5	169.7	203.3	229.1	228.1
Federal government surplus or deficit (-) (N.I.A. basis)	-108.5	-113.2	-158.3	-208.2	-183.3	-166.1	-187.3	-189.9
High employment surplus or deficit (-) <3>	-38.1	-32.7	-64.9	-99.7	-72.3	-65.1	-101.7	-110.9
State and local government surplus or deficit(-) (N.I.A. basis)	28.8	32.0	31.3	32.9	40.4	51.7	55.5	58.1
Excluding social insurance funds	-3.5	-.8	-2.1	-1.2	5.5	16.1	18.9	20.8
Civilian labor force (millions)	109.4	110.2	110.5	110.8	110.7	111.3	112.1	112.0
Unemployment rate (percent)	8.8	9.4	10.0	10.6	10.4	10.1	9.4	8.5
Nonfarm payroll employment (millions)	90.3	89.9	89.3	88.8	88.8	89.5	90.3	91.3
Manufacturing	19.4	19.1	18.7	18.3	18.3	18.5	18.8	19.2
Industrial production (1967=100)	141.7	139.4	138.2	135.2	138.5	144.5	151.8	155.4
Capacity utilization: all manufacturing (percent)	72.9	71.6	71.1	69.0	70.7	73.9	77.4	78.9
Materials (percent)	73.0	70.7	69.4	67.2	70.1	73.5	77.5	79.6
Housing starts, private (million units, A.R.)	.88	.96	1.12	1.27	1.64	1.69	1.78	1.70
New auto sales (millions, A.R.)	8.12	7.53	7.78	8.57	8.46	9.10	9.22	9.94
Domestic models	5.90	5.53	5.56	6.08	6.06	6.81	6.92	7.29
Foreign models	2.22	1.99	2.22	2.49	2.40	2.28	2.31	2.65

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

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

<3> Estimates in table are evaluated at a 6.0 percent high employment unemployment rate.

March 21, 1984

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CLASS II FOMCPERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	1982				1983			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	-5.5	1.0	-1.0	-1.3	2.6	9.7	7.6	5.0
Final sales	-1.3	-0.8	-1.5	4.5	.6	6.8	5.1	3.7
Private	-1.6	.1	-4.0	3.0	3.0	8.8	5.3	5.5
Domestic final purchases	.0	.8	-.9	3.4	3.9	11.9	5.7	8.5
Personal consumption expenditures	2.4	3.1	.9	3.6	2.9	10.0	2.2	6.5
Goods	2.0	1.5	-.1	5.1	4.4	13.5	3.7	9.0
Services	2.9	4.7	2.1	1.9	1.4	6.4	.6	3.7
Gross private domestic investment	-34.1	3.4	-5.8	-34.6	28.6	49.8	45.1	27.6
Residential structures	-28.5	17.9	-13.0	53.2	57.3	79.5	35.9	-6.9
Business fixed investment	-5.9	-14.3	-8.8	-6.6	-1.5	7.9	18.7	27.2
Gov't. purchases of goods and services	-.2	-5.0	9.4	10.6	-8.8	-1.1	4.4	-3.9
Federal	.2	-14.0	26.3	28.3	-18.0	-2.8	4.6	-8.4
National defense	-1.3	13.0	14.0	5.1	6.5	7.4	.0	7.8
State and local	-.5	1.3	-.4	-.1	-1.8	.0	4.3	-.8
Disposable personal income	-3.4	1.9	-.3	2.6	2.9	3.5	6.5	8.0
<u>Current Dollars</u>								
Gross national product	-1.4	6.6	2.7	2.5	8.2	13.3	11.5	9.1
Final sales	3.9	4.6	1.9	9.4	5.8	9.8	8.4	7.7
Private	3.8	5.5	-1.6	7.8	7.8	11.5	8.3	9.7
Domestic final purchases	3.7	5.0	3.8	7.0	5.9	16.0	9.8	10.9
Personal consumption expenditures	7.5	7.2	7.5	7.8	5.2	15.1	6.5	9.4
Goods	4.4	3.5	5.1	6.1	4.2	17.1	7.8	9.8
Services	10.8	11.2	10.1	9.5	6.3	13.0	5.3	9.1
Gross private domestic investment	-37.8	9.5	-6.5	-38.0	31.5	53.9	53.6	27.5
Residential structures	-26.5	18.2	-13.0	46.9	75.3	76.7	47.5	-7.3
Business fixed investment	-6.7	-9.1	-11.3	-6.0	-5.7	5.1	18.8	28.8
Gov't. purchases of goods and services	4.6	1.2	16.1	15.5	-1.3	3.6	9.0	.4
Federal	2.1	-8.7	32.1	29.5	-8.0	.3	6.6	-5.6
National defense	3.5	18.0	20.8	16.5	7.8	10.7	3.6	10.5
State and local	6.2	8.1	6.8	6.8	3.5	5.8	10.7	4.6
Disposable personal income	1.4	6.0	6.1	6.8	5.1	8.2	11.0	10.9
Personal income	1.8	5.7	4.5	6.4	4.0	8.7	7.3	11.0
Wage and salary disbursements	3.2	5.6	4.2	1.6	6.4	9.7	8.4	8.7
Corporate profits with I.V.A. and C.C. Adj.	-49.3	12.4	4.1	-14.8	59.0	107.5	68.0	35.7
Corporate profits before tax	-59.6	13.6	-3.3	-20.3	5.4	106.0	61.3	-1.7
Nonfarm payroll employment	-3.0	-1.8	-2.7	-2.3	.1	2.9	3.6	4.9
Manufacturing	-9.5	-7.5	-7.7	-8.6	-.1	5.2	7.0	8.2
Nonfarm business sector								
Output per hour	.1	-.4	2.3	1.3	3.7	7.1	2.3	.9
Compensation per hour	10.0	5.8	7.2	5.8	6.8	4.3	3.8	4.4
Unit labor costs	9.9	6.2	4.7	4.4	3.0	-2.6	1.5	3.5
GNP implicit deflator <1>	4.3	5.6	3.7	3.8	5.5	3.3	3.6	3.9
Gross domestic business product								
fixed-weighted price index <2>	4.9	4.5	5.8	3.8	3.6	4.1	4.7	4.1
Excluding food and energy	5.8	6.4	5.4	3.9	6.7	3.5	5.6	4.4
Consumer price index (all urban)	3.8	5.5	7.3	1.5	.3	4.4	4.1	4.5
Industrial production	-11.8	-6.5	-3.4	-8.2	10.1	18.4	21.8	10.0

<1> Excluding the Federal pay increase, the rate of change in 1982-Q4 was 3.5 percent.

<2> Uses expenditures in 1972 as weights.

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CONFIDENTIAL - FR
CLASS II FOMC

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

	Projected							
	1984				1985			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	3543.7	3631.7	3710.1	3785.5	3865.2	3941.4	4025.1	4111.5
Final sales	3496.7	3585.4	3659.8	3740.5	3823.2	3902.4	3987.1	4073.5
Private	2785.3	2842.4	2896.9	2956.4	3017.0	3078.3	3144.1	3211.9
Domestic final purchases	2820.8	2893.8	2957.3	3020.9	3082.6	3143.2	3207.5	3271.9
Personal consumption expenditures	2284.5	2335.8	2384.8	2436.5	2484.0	2532.0	2582.0	2634.0
Goods	1157.7	1182.0	1203.0	1226.5	1246.5	1266.5	1286.5	1307.5
Services	1126.8	1153.8	1181.8	1210.0	1237.5	1265.5	1295.5	1326.5
Gross private domestic investment	583.3	604.3	622.8	629.4	640.6	650.2	663.5	675.9
Residential structures	149.5	158.2	159.3	157.7	158.7	158.5	160.6	161.3
Business fixed investment	386.8	399.8	413.2	426.7	439.9	452.7	464.9	476.6
Change in business inventories	47.0	46.3	50.3	45.0	42.0	39.0	38.0	38.0
Nonfarm	26.0	37.3	46.3	45.0	42.0	39.0	38.0	38.0
Net exports of goods and services <1>	-35.5	-51.4	-60.4	-64.5	-65.6	-64.9	-63.4	-60.0
Exports	360.1	371.0	380.7	393.7	408.7	422.6	438.6	456.6
Imports	395.6	422.4	441.1	458.2	474.3	487.5	502.0	516.6
Gov't. purchases of goods and services	711.4	743.0	762.9	784.1	806.2	824.1	843.0	861.6
Federal <2>	277.6	299.5	309.9	321.1	333.4	341.0	349.5	357.7
State and local	433.8	443.5	453.0	463.0	472.8	483.1	493.5	503.9
Gross national product in constant (1972) dollars	1602.9	1626.3	1642.4	1655.2	1667.8	1678.7	1690.8	1702.5
Personal income	2922.6	2977.4	3041.2	3107.8	3185.4	3248.4	3316.2	3381.8
Wage and salary disbursements	1759.4	1803.0	1844.9	1884.7	1926.3	1965.2	2004.4	2043.5
Disposable personal income	2498.2	2541.1	2594.1	2649.2	2715.9	2767.4	2823.2	2877.0
Saving rate (percent)	5.7	5.3	5.3	5.2	5.8	5.7	5.8	5.7
Corporate profits with I.V.A. and C.C. Adj.	278.2	281.1	285.0	288.2	283.6	286.7	297.1	309.1
Corporate profits before tax	240.5	242.4	243.3	243.5	234.9	234.0	240.4	247.4
Federal government surplus or deficit (-) (N.I.A. basis)	-174.8	-166.7	-167.0	-174.0	-184.0	-182.0	-182.5	-180.0
High employment surplus or deficit (-) <3>	-110.7	-113.0	-119.4	-129.1	-141.6	-140.2	-141.2	-138.0
State and local government surplus or deficit (-) (N.I.A. basis)	62.9	63.4	62.9	61.2	58.5	55.7	52.8	50.8
Excluding social insurance funds	24.5	24.5	23.3	20.9	17.6	14.2	10.7	8.0
Civilian labor force (millions)	112.6	113.2	113.8	114.4	114.9	115.4	115.9	116.4
Unemployment rate (percent)	7.8	7.2	6.9	6.8	6.7	6.6	6.5	6.5
Nonfarm payroll employment	92.2	93.3	94.3	95.0	95.8	96.4	97.0	97.6
Manufacturing	19.5	19.8	20.1	20.3	20.5	20.6	20.7	20.7
Industrial production (1967=100)	159.9	164.0	166.9	169.3	171.2	172.8	174.2	175.0
Capacity utilization: all manufacturing (percent)	80.9	82.6	83.6	84.3	84.8	85.0	85.2	85.2
Materials (percent)	81.6	83.5	84.8	85.9	86.5	86.9	87.2	87.4
Housing starts, private (million units, A.R.)	2.06	1.85	1.80	1.75	1.75	1.70	1.70	1.70
New auto sales (millions, A.R.)	10.75	10.70	10.75	11.10	11.05	11.25	11.45	11.60
Domestic models	8.45	8.30	8.20	8.50	8.60	8.70	8.80	8.90
Foreign models	2.30	2.40	2.55	2.60	2.45	2.55	2.65	2.70

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

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

<3> Estimates in table are evaluated at a 6.0 percent high employment unemployment rate.

CONFIDENTIAL - FR
CLASS II FOMCPERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	1984				Projected 1985			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	8.0	6.0	4.0	3.1	3.1	2.7	2.9	2.8
Final sales	4.7	6.6	3.7	3.8	3.5	3.0	3.1	2.9
Private	5.9	5.0	3.3	3.3	3.2	2.9	2.9	2.8
Domestic final purchases	7.9	5.5	3.3	3.1	3.0	2.5	2.5	2.2
Personal consumption expenditures	5.4	3.7	2.5	2.8	2.4	2.2	2.1	2.1
Goods	8.5	4.0	2.1	2.8	2.0	1.8	1.6	1.6
Services	2.0	3.4	3.1	2.9	2.7	2.6	2.6	2.5
Gross private domestic investment	42.5	8.6	8.2	.3	2.9	1.7	3.2	2.2
Residential structures	30.6	19.6	-2.4	-9.1	-2.9	-6.0	-.7	-4.3
Business fixed investment	15.6	11.0	9.6	8.6	8.0	6.9	5.7	4.5
Gov't. purchases of goods and services	-.2	13.8	5.5	6.0	4.8	3.6	3.7	3.3
Federal	-4.1	31.4	9.3	10.3	7.6	4.4	4.9	4.1
National defense	11.5	10.9	9.3	8.4	6.8	5.7	6.5	5.4
State and local	2.5	3.3	2.9	3.1	2.8	3.0	2.9	2.7
Disposable personal income	8.2	1.6	2.5	2.7	4.6	2.0	2.3	1.6
<u>Current Dollars</u>								
Gross national product	13.1	10.3	8.9	8.4	8.7	8.1	8.8	8.9
Final sales	9.7	10.5	8.6	9.1	9.1	8.5	9.0	9.0
Private	10.3	8.5	7.9	8.5	8.5	8.4	8.8	8.9
Domestic final purchases	11.7	10.8	9.1	8.9	8.4	8.1	8.4	8.3
Personal consumption expenditures	10.0	9.3	8.7	9.0	8.0	8.0	8.1	8.3
Goods	12.7	8.7	7.3	8.0	6.7	6.6	6.5	6.7
Services	7.2	9.9	10.1	9.9	9.4	9.4	9.8	9.9
Gross private domestic investment	44.0	15.2	12.8	4.3	7.3	6.1	8.4	7.7
Residential structures	34.5	25.4	2.8	-4.0	2.6	-.5	5.4	1.8
Business fixed investment	14.4	14.1	14.1	13.7	13.0	12.2	11.2	10.5
Gov't. purchases of goods and services	7.3	19.0	11.2	11.6	11.8	9.2	9.5	9.1
Federal	5.2	35.5	14.6	15.3	16.2	9.4	10.3	9.7
National defense	23.3	13.7	15.0	14.3	16.4	11.3	12.7	11.5
State and local	8.6	9.2	8.8	9.1	8.7	9.0	8.9	8.7
Disposable personal income	12.9	7.0	8.6	8.8	10.4	7.8	8.3	7.8
Personal income	12.9	7.7	8.8	9.1	10.4	8.2	8.6	8.2
Wage and salary disbursements	10.2	10.3	9.6	8.9	9.1	8.3	8.2	8.0
Corporate profits with I.V.A. and C.C. Adj.	-92.7	4.3	5.7	4.5	-6.2	4.4	15.3	17.1
Corporate profits before tax	23.6	3.2	1.5	.3	-13.4	-1.5	11.4	12.1
Nonfarm payroll employment	4.0	4.8	4.2	3.2	3.1	2.6	2.5	2.3
Manufacturing	6.8	6.9	5.8	4.7	3.2	2.2	1.4	.9
Nonfarm business sector								
Output per hour	1.8	1.4	.6	.1	.5	.3	.9	.8
Compensation per hour	6.1	5.5	5.8	5.9	6.5	6.2	6.4	6.5
Unit labor costs	4.3	4.0	5.2	5.8	6.0	5.9	5.5	5.7
GDP implicit deflator <1>	4.8	4.1	4.7	5.1	5.4	5.3	5.7	5.9
Gross domestic business product fixed-weighted price index <2>	4.8	4.8	5.1	5.3	5.4	5.6	5.9	6.1
Excluding food and energy	4.6	4.9	5.0	5.3	5.7	5.9	6.2	6.4
Consumer price index (all urban)	5.3	5.1	5.6	5.6	5.6	5.7	5.9	6.0
Industrial production	11.8	10.7	7.3	5.9	4.6	3.8	3.3	1.8

<1> Excluding Federal pay increases, the rate of change in 1984-Q1 is 4.4 percent and in 1985-Q1 is 5.1 percent.
 <2> Uses expenditures in 1972 as weights.

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CONFIDENTIAL - FR
CLASS II FOMCGROSS NATIONAL PRODUCT AND RELATED ITEMS
(Expenditures and income figures are billions of current dollars.)

	1978	1979	1980	1981	1982	1983	—Projected—	
							1984	1985
Gross national product	2163.9	2417.8	2631.7	2954.1	3073.0	3310.5	3667.7	3985.8
Final sales	2137.4	2403.5	2641.5	2935.6	3097.5	3316.9	3620.6	3946.5
Private	1705.5	1929.1	2103.7	2339.9	2448.3	2627.4	2870.2	3112.8
Domestic final purchases	1706.6	1915.9	2079.7	2313.6	2430.9	2636.4	2923.2	3176.3
Personal consumption expenditures	1346.5	1507.2	1668.1	1857.2	1991.9	2158.0	2360.4	2558.0
Goods	728.5	813.5	883.5	970.0	1005.5	1083.5	1192.3	1276.7
Services	618.0	693.7	784.5	887.1	986.4	1074.5	1168.1	1281.2
Gross private domestic investment	386.6	423.0	401.9	474.9	414.5	471.9	609.9	657.5
Residential construction	111.2	118.6	102.9	104.3	90.8	130.0	156.2	159.8
Business fixed investment	248.9	290.2	308.8	352.2	348.3	348.4	406.6	458.5
Change in business inventories	26.5	14.3	-9.8	18.5	-24.5	-6.4	47.1	39.3
Nonfarm	25.4	8.6	-4.5	10.9	-23.1	-2.8	38.6	39.3
Net exports of goods and services <1>	-1.1	13.2	23.9	26.3	17.4	-9.0	-52.9	-63.5
Exports	218.7	281.4	338.8	368.8	347.6	335.4	376.4	431.6
Imports	219.8	268.1	314.8	342.5	330.2	344.4	429.3	495.1
Gov't. purchases of goods and services	431.9	474.4	537.8	595.7	649.2	689.5	750.3	833.7
Federal <2>	153.6	168.3	197.0	229.2	258.7	274.8	302.0	345.4
State and local	278.3	306.0	340.8	366.5	390.5	414.7	448.3	488.3
Gross national product in constant (1972) dollars	1438.6	1479.4	1475.0	1513.8	1485.4	1535.3	1631.7	1685.0
Personal income	1732.7	1951.2	2165.3	2435.0	2578.6	2742.1	3012.2	3282.9
Wage and salary disbursements	1106.3	1237.6	1356.7	1493.2	1568.1	1664.6	1823.0	1984.8
Disposable personal income	1474.0	1650.2	1828.9	2047.6	2176.5	2335.6	2570.6	2795.9
Saving rate (percent)	6.1	5.9	6.0	6.6	5.8	4.9	5.4	5.7
Corporate profits with I.V.A. and C.C.Adj.	192.4	194.8	175.4	192.3	164.8	229.1	283.1	294.1
Corporate profits before tax	229.1	252.7	234.6	227.0	174.2	207.5	242.4	239.2
Federal government surplus or deficit(-) (N.I.A. basis)	-29.5	-16.1	-61.2	-62.2	-147.1	-181.6	-170.6	-182.2
High employment surplus or deficit(-)	-29.2	-18.6	-36.0	-26.0	-58.8	-87.5	-118.0	-140.2
State and local government surplus or deficit (-) (N.I.A. basis)	30.3	30.4	30.6	35.3	31.3	51.4	62.6	54.4
Excluding social insurance funds	10.0	6.6	3.5	4.4	-1.9	15.3	23.3	12.6
Civilian labor force (millions)	102.3	105.0	106.9	108.7	110.2	111.5	113.5	115.7
Unemployment rate (percent)	6.1	5.8	7.1	7.6	9.7	9.6	7.2	6.6
Nonfarm payroll employment (millions)	86.7	89.8	90.4	91.2	89.6	90.0	93.7	96.7
Manufacturing	20.5	21.0	20.3	20.2	18.9	18.7	19.9	20.6
Industrial production (1967=100)	146.1	152.5	147.0	150.9	138.6	147.6	165.0	173.3
Capacity utilization: all manufacturing (percent)	84.7	86.0	79.6	79.4	71.1	75.2	82.9	85.1
Materials (percent)	85.6	87.6	80.4	80.7	70.1	75.2	83.9	87.0
Housing starts, private (million units, A.R.)	2.00	1.72	1.30	1.10	1.06	1.70	1.87	1.71
New auto sales (millions, A.R.)	11.29	10.68	9.04	8.56	8.00	9.18	10.83	11.34
Domestic models	9.29	8.36	6.62	6.24	5.77	6.77	8.36	8.75
Foreign models	2.00	2.32	2.42	2.32	2.23	2.41	2.46	2.59

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

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

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

	1978	1979	1980	1981	1982	1983	—Projected—	
							1984	1985
<u>Constant (1972) Dollars</u>								
Gross national product	5.0	2.8	-.3	2.6	-1.9	3.4	6.3	3.3
Final sales	4.9	3.5	.5	1.8	-.7	2.8	4.9	3.6
Private	5.6	4.0	.1	2.0	-1.3	3.4	5.3	3.2
Domestic final purchases	5.5	2.9	-1.0	2.7	-.1	5.0	6.6	3.0
Personal consumption expenditures	4.5	2.7	.5	2.7	1.4	4.2	4.6	2.5
Goods	4.2	1.9	-1.4	2.1	.1	5.6	6.2	2.2
Services	4.8	3.7	2.7	3.3	2.9	2.7	2.9	2.8
Gross private domestic investment	10.5	-.2	-11.8	9.2	-14.5	12.6	25.5	3.2
Residential structures	2.8	-5.3	-20.3	-5.1	-15.4	39.4	16.0	-3.2
Business fixed investment	12.8	7.3	-2.4	5.2	-4.8	1.4	15.4	7.8
Gov't. purchases of goods and services	2.0	1.3	2.2	.8	1.8	.4	3.2	5.2
Federal	-.1	1.8	4.2	3.8	5.6	1.0	4.8	8.4
National defense	.4	2.6	3.9	5.2	7.1	6.9	8.4	7.3
State and local	3.3	1.1	1.0	-1.0	-.5	.1	2.1	3.0
Disposable personal income	4.9	2.7	.6	3.2	.5	3.2	5.3	2.8
<u>Current Dollars</u>								
Gross national product	12.8	11.7	8.8	12.2	4.0	7.7	10.8	8.7
Final sales	12.8	12.4	9.9	11.1	5.5	7.1	9.2	9.0
Private	13.6	13.1	9.0	11.2	4.6	7.3	9.2	8.5
Domestic final purchases	13.4	12.3	8.5	11.2	5.1	8.5	10.9	8.7
Personal consumption expenditures	11.8	11.9	10.7	11.3	7.3	8.3	9.4	8.4
Goods	10.9	11.7	8.6	9.8	3.7	7.8	10.0	7.1
Services	12.9	12.2	13.1	13.1	11.2	8.9	8.7	9.7
Gross private domestic investment	19.3	9.4	-5.0	18.2	-12.7	13.8	29.3	7.8
Residential structures	16.1	6.6	-13.2	1.4	-13.0	43.3	20.1	2.3
Business fixed investment	21.3	16.6	6.4	14.1	-1.1	.0	16.7	12.8
Gov't. purchases of goods and services	9.7	9.8	13.4	10.8	9.0	6.2	8.8	11.1
Federal	7.1	9.6	17.1	16.3	12.9	6.2	9.9	14.4
National defense	8.0	11.5	17.3	17.4	16.5	11.6	14.2	13.9
State and local	11.2	9.9	11.4	7.5	6.6	6.2	8.1	8.9
Disposable personal income	12.2	12.0	10.8	12.0	6.3	7.3	10.1	8.8
Personal income	12.5	12.6	11.0	12.5	5.9	6.3	9.9	9.0
Wage and salary disbursements:	12.5	11.9	9.6	10.1	5.0	6.2	9.5	8.9
Corporate profits with I.V.A. and C.C.Adj.	15.0	1.3	-9.9	9.6	-14.3	39.0	23.6	3.9
Corporate profits before tax	17.7	10.3	-7.1	-3.3	-23.2	19.1	16.8	-1.4
Nonfarm payroll employment	5.1	3.6	.6	.8	-1.7	.4	4.2	3.1
Manufacturing	4.2	2.6	-3.6	-.6	-6.5	-.9	6.7	3.4
Nonfarm business sector								
Output per hour	.6	-1.5	-.7	1.9	-.1	6.3	1.7	.5
Compensation per hour	8.6	9.0	10.4	9.8	7.8	11.3	5.2	6.2
Unit labor costs	8.0	10.7	11.1	7.7	7.9	4.8	3.5	5.6
GDP implicit deflator	7.4	8.6	9.2	9.4	6.0	4.2	4.2	5.2
Gross domestic business product								
fixed-weighted price index (1)	8.0	9.9	10.0	9.5	6.0	4.2	4.7	5.5
Excluding food and energy	7.8	8.6	8.5	9.3	6.9	5.1	4.8	5.7
Consumer price index (all urban)	7.6	11.3	13.5	10.3	6.1	3.2	5.0	5.7
Industrial production	5.8	4.4	-3.6	2.6	-8.1	6.4	11.8	5.0

(1) Uses expenditures in 1972 as weights.

March 21, 1984

FEDERAL SECTOR ACCOUNTS
(Billions of dollars)

	Fiscal Year 1983 ^a	FY1984 ^{b/2/}		FY1985 ^{b/2/}		CY1984 ^b		FRB staff estimates								
		Admin. 1/	FRB Staff	Admin. 1/	FRB Staff	CY 1983 ^a	FRB Staff	Calendar quarters; not seasonally adjusted								
								1983			1984			1985		
								IV ^a	I	II	III	IV	I	II	III	
Unified budget receipts	601	670	673	745	750	613	693	149	161	186	177	169	171	214	196	
Unified budget outlays	706	834	851	925	936	803	873	213	210	214	215	235	231	236	234	
Surplus/deficit(-), unified budget	-195	-164	-178	-180	-186	-190	-181	-63	-49	-28	-38	-66	-60	-21	-38	
Surplus/deficit(-), off-budget agencies ³	-12	-16	-12	-15	-15	-10	-16	1	-3	-5	-5	-3	-3	-5	-5	
Combined deficit to be financed	-208	-200	-190	-195	-201	-201	-196	-62	-52	-33	-43	-68	-62	-26	-43	
Means of financing combined deficits:																
Net borrowing from public	212	183	171	193	199	187	200	36	49	40	46	65	54	39	41	
Decrease in cash operating balance	-8	17	17	0	0	8	-3	25	-4	1	-5	5	5	-10	0	
Other ⁴	3	0	2	2	2	6	-1	1	7	-8	2	-2	4	-3	3	
Cash operating balance, end of period	37	20	20	20	20	12	15	12	16	15	20	15	10	20	20	
Memo: Sponsored agency borrowing ⁵	-3	38	15	41	18	1	15	3	3	5	6	4	4	5	5	
NIA Budget																
Receipts	631	691	699	779	776	645	721	658	692	713	731	748	768	785	804	
Expenditures	816	876	873	948	957	826	892	847	867	880	898	922	952	967	987	
Purchases	275	293	290	340	336	275	302	274	278	299	310	321	333	341	349	
Defense	197	224	220	257	253	200	229	206	217	225	233	240	250	257	264	
Nondefense	78	69	70	83	84	75	73	68	60	75	77	81	84	85	85	
All other expenditures	541	583	583	608	621	551	590	573	590	580	588	601	619	626	637	
Surplus/deficit(-)	-186	-184	-175	-169	-181	-182	-171	-190	-175	-167	-167	-174	-184	-182	-183	
High Employment (H.E.) surplus/deficit(-) evaluated as the unemployment rate of 6 percent	-85	n.a.	-113	n.a.	-138	-88	-118	-111	-111	-113	-119	-129	-142	-140	-141	
	*--actual					--estimated									n.a.--not available	

- Budget of the United States Government, Fiscal Year 1985 (February 1984).
- The CBO baseline budget estimates show revenues of \$463 billion and \$733 billion, outlays of \$852 billion and \$930 billion and deficits of \$189 billion and \$197 billion in fiscal years 1984 and 1985 respectively (An Analysis of the President's Budgetary Proposals, February 1984).

Note: Details may not add to totals due to rounding.

- Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, Rural Telephone Bank and Strategic Petroleum Reserve.
- Checks issued less checks paid, accrued items and other transactions.
- FRB staff estimates and actuals include Federal Home Loan Banks, FHLMC (excluding participation certificates), FIRMA (excluding mortgage-backed securities), Federal Land Banks, Federal Intermediate Credit Banks for Cooperatives, and Student Loan Marketing Association marketable debt on a payment basis. FRB and Administration estimates are not strictly comparable.

Recent Developments. Since the last FOMC meeting, interest rates have risen throughout the maturity spectrum. Short-term rates have reacted to incoming data suggesting a stronger economy than had been forecast, which dashed hopes of a near-term easing of reserve positions. The federal funds rate moved from the 9-3/8 to 9-1/2 percent area into the 9-1/2 to 9-3/4 percent area for most of the intermeeting period, with recent trading in the neighborhood of 10 percent. Other short-term market rates are up about 75 to 100 basis points, and very recently major banks raised their prime rates by 1/2 percentage point, to 11-1/2 percent. Long-term rates backed up about 80 basis points, amid renewed concerns about the outlook for inflation and pessimism regarding deficit reductions. Stock prices have declined further on balance over the intermeeting period.

M1 growth strengthened in the opening months of this year--to about an 8-1/2 percent average annual rate over January and February--from the subdued pace of the latter part of 1983. The recent pickup in M1 growth--which has placed this measure near the top part of its annual range--has been concentrated in its OCD component. It appears likely that M1 velocity has registered a sizable increase in the current quarter, as predicted by models of money demand in light of the acceleration of GNP growth and rising interest rates.

Despite the stronger expansion in its M1 component, M2 growth has moderated over the first two months of the year. Growth in M2 during January and February averaged 7 percent at an annual rate, placing this

measure in the center of the FOMC's annual range. The slowing of non-transactions M2 has been in core deposits, as larger inflows to MMDAs were more than offset by a sharp deceleration in small time deposit growth from the elevated pace of the second half of 1983 and by a faster runoff of savings deposits. Money market fund inflows, by contrast, picked up appreciably in early 1984.

With continued strong credit demands pressing against weaker growth of core deposits, depository institutions in the opening months of this year issued a substantial volume of managed liabilities in M3. Issuance of CDs by thrift institutions strengthened over the first two months of this year, evidently accompanying continued heavy acquisition of mortgage assets by S&Ls. With M3 expansion averaging 8 percent over January and February, this aggregate has expanded at an 8-3/4 percent rate since the fourth quarter of last year, leaving it near the upper end of its annual range.

Commercial bank credit continued to grow in January and February at around the brisk pace of last year's fourth quarter. Loan growth over those two months strengthened as it had done steadily over the last three quarters of 1983. The demand for business and real estate loans picked up from the fourth quarter while consumer loans continued to soar at the fourth-quarter pace. The growing commercial bank share of consumer lending reflects a greater willingness by banks to lend in this market as evidenced by more competitive bank lending rates.

Heavy borrowing by households in early 1984 has reflected a quickened pace of retail purchases, especially of automobiles, and strong

housing activity. Business borrowing has picked up in recent months--boosted in part by growing external financing needs, as growth in capital spending has outstripped improvement in internally generated funds. In addition, business credit demands have been enlarged by a curtailment of equity offerings--as stock prices have sagged--and, in February, by merger-related financing. Public bond offerings by non-financial corporations have risen somewhat from the meager volume of the fourth quarter of last year, but business borrowing continues to be concentrated in the short-term area, mostly from banks. Business loans (including those booked offshore) and commercial paper of nonfinancial firms grew at a 10 percent annual rate in January and an 18 percent rate in February, with nearly half of the February expansion accounted for by the financing of Texaco's acquisition of Getty Oil.

Although the federal deficit has narrowed somewhat in the current quarter, borrowing by the Treasury has risen from the fourth-quarter level which had been damped by a large cash balance runoff. In contrast, offerings of securities by state and local governments have moderated in the first quarter; issuance of private-purpose bonds has been dormant, pending congressional action on the status of such issues, and a pickup in electric utility revenue-bond offerings has provided only a partial offset in financing volume. Reflecting heavier borrowing by the private and Treasury sectors, aggregate domestic nonfinancial sector debt is estimated to have accelerated in the current quarter.

Outlook. Over the spring, heavy credit demands likely will accompany continued robust economic expansion, placing further upward

pressure on market rates of interest. Success in enacting significant deficit reduction measures could--through expectational effects--relieve some of this pressure, especially on intermediate- and long-term rates; the staff's forecast, however, does not assume such a dramatic development.

The Treasury will place substantial demands on credit markets over the second quarter, despite the seasonal pickup in receipts. Borrowing by the Treasury is expected to be around \$40 billion, primarily in marketable coupon issues, to finance a combined (on- and off-budget) deficit of about \$33 billion. Financing over this period may well be complicated by the current debt limit, which according to staff projections will be reached by mid-quarter. Meanwhile, borrowing by state and local governments over the spring is likely to remain near the reduced pace of recent months, in the absence of congressional action on private-purpose municipal securities.

Credit demands by businesses are expected to expand further over the coming months as the gap between capital spending and internal cash flow widens appreciably. External fund-raising by the business sector will also be boosted by additional large merger-related financing, although such activity should have only minimal effects on the overall availability and terms of credit. In the absence of a rally in the stock market, businesses will continue to raise the bulk of funds in credit markets, mostly through short-term borrowing. (Indeed, net equity issuance would remain deeply negative if giant merger deals continue to absorb large volumes of outstanding shares.)

Borrowing by households is expected to remain strong. The rapid pace of housing starts and record level of mortgage commitments at S&Ls suggest heavy mortgage borrowing, which is likely to continue to be concentrated in adjustable rate mortgages. Similarly, consumer installment borrowing is expected to remain robust in light of buoyant consumer spending.

Recent developments. The dollar's value against major foreign currencies declined without much interruption from the end of January into the first week of March -- falling about 7 percent on a weighted average basis. Since then the dollar has reversed about one-half of that decline. Early in the decline a major factor was the strong performance of the German mark, which had been falling through most of 1983 because of concerns about political stability and rising East-West tensions. These concerns were easing by February. An additional factor in the dollar's weakness was fear that the enlarged U.S. budget deficits would undercut efforts to resist inflation as the economy expands faster than expected. More recently the market seems to have been impressed by indications that monetary policy might be firming. Dollar interest rates have risen considerably against rates on foreign-currency assets.

Over the whole period since the end of January the dollar has depreciated 3 to 6 percent against the continental European currencies, and 2 to 3 percent against sterling and the yen. As noted, the German mark has been particularly strong since January, while sterling has been under some pressure, perhaps because of rising trade deficits and some cuts in interest rates. The yen registered a small but sharp upturn early in March.

Recovery abroad has continued and gathered some strength in several major industrial countries. Real GNP rose strongly in the fourth quarter of 1983 in the major industrial countries. The weighted average of fourth-quarter industrial production in the six major foreign countries was about 5 percent above the low-point a year ago, with January data pointing toward further gains. Japan, Germany and the United Kingdom are showing the strongest improvement, while Canada has slowed somewhat from its strong earlier performance and growth in France and Italy has remained weak. Unemployment rates abroad remain high despite recovering production. Several countries (France, Japan) are currently reporting record unemployment rates, and in others (Germany, United Kingdom) there is only slight improvement from the recent peaks of unemployment.

Inflation in the major industrial countries, measured on a year-over-year basis, reached its lowest rate since the early seventies by the fourth quarter of last year. Data for January and partial data for February suggest some renewed upward pressure, resulting in part from the continued effects of the strong dollar on import prices.

Recent policy actions have tended to confirm the generally restraining stance of foreign governments. The U.K. government budget for FY 1984/85 contains no net fiscal stimulus and lowered monetary targets. The governments of France and Italy as part of their

anti-inflation effort have attempted to tighten cost-of-living provisions in labor contracts, resulting in protests by labor.

U.S.-chartered banks' claims on non-OPEC developing countries increased \$2.3 billion in the fourth quarter of 1983, somewhat more than the very small quarterly increases earlier in the year. For 1983 as a whole claims rose only \$4.1 billion. In the fourth quarter, claims on most individual non-OPEC developing countries changed only slightly; there were no absolute declines in claims on any major borrowers. At the end of November, Brazil drew the remaining \$1.8 billion (\$.7 billion from U.S. banks) on the \$4.4 billion bank loan of February 1983, but the proceeds were almost entirely used up in repayment of the remaining \$1.2 billion balance on the late-1982 bridge loans (about one half for U.S. banks) and in paying off interest and other arrears. In November and December Mexico drew the remaining \$1.6 billion balance (\$.6 billion from U.S. banks) available from the \$5 billion loan of March 1983.

Most of the deeply indebted countries are maintaining satisfactory relations with the IMF and their bank creditors, though several have been unable to meet some of the criteria in their initial IMF programs. However, the Argentine and Philippine situations are less than satisfactory, and neither country has yet offered a revised program meeting IMF approval. Brazil, Mexico and Chile have succeeded in their negotiations for "new" bank credit and Peru has reached agreement on a rescheduling of bank debt for 1984-85. Argentina has been reluctant to use scarce reserves to meet scheduled interest payments, while Venezuela, which has sizable reserves, has resisted submitting its new economic program for IMF approval, though steps are being taken to deal with rising debt arrearages.

The U.S. merchandise trade deficit escalated to a record rate in January, following a reduced deficit rate registered in December. A moderate increase in the value of exports (both agricultural and manufactured goods) was swamped by a sharp increase in imports of a wide range of manufactures. Petroleum imports were below the fourth-quarter average in volume and price. Part of the January surge in imports of manufactures was probably temporary.

U.S. banks reported a net capital inflow from banks abroad between December and February, but at a considerably slower rate than the inflow in the fourth quarter of last year. Other small inflows in the recent period resulted from a decline in Eurodollar deposits of U.S. nonbanks, and some increase in loans to U.S. nonbanks from U.S. banks' branches abroad. Other inflows in the early months of the year will probably show up in direct investments, as U.S. corporations increased their borrowings in European security markets.

Outlook. Projections for both U.S. and foreign economic activity have been raised since January, though the U.S. revision is greater. Largely as a result of those changes the projections of both U.S. exports and imports have been raised, but with very little net effect on the projected trade and current account deficits. The projected trade deficits for 1984 and 1985 are \$105 billion and \$120 billion, respectively, with corresponding current account deficits of about \$80 billion and \$95 billion. The staff continues to project a depreciation of the dollar amounting to about 10 percent from the first-quarter average over the remainder of 1984, and a further 8 percent by the end of 1985.

MARCH 20, 1984

OUTLOOK FOR U.S. NET EXPORTS AND RELATED ITEMS
(BILLIONS OF DOLLARS, SEASONALLY ADJUSTED ANNUAL RATES)

	1983 ANN.	1984-P ANN.	1985-P ANN.	1983 Q3	1983 Q4	1984-P Q1	1984-P Q2	1984-P Q3	1984-P Q4	1985-P Q1	1985-P Q2	1985-P Q3	1985-P Q4
1. GNP NET EXPORTS													
CURRENT \$, NET EXPORTS OF G+S	-9.0	-53.0	-63.5	-18.3	-26.1	-35.5	-51.4	-60.4	-64.6	-65.6	-64.9	-63.4	-60.0
IMPORTS OF G+S	335.4	376.4	431.6	341.1	346.5	360.1	371.0	380.7	393.7	408.7	422.6	438.6	456.6
CONSTANT 72 \$, NET EXPORTS OF G+S	11.8	-3.9	-1.1	11.5	2.8	-3.0	-4.4	-4.4	-3.9	-3.1	-2.0	-0.6	1.4
IMPORTS OF G+S	138.7	147.8	159.2	140.7	140.6	143.8	146.7	148.8	152.0	155.0	157.5	160.5	164.0
TERMS OF TRADE (1972=100) 1/	89.2	90.1	87.8	87.2	91.2	93.0	90.5	88.9	88.1	87.9	87.8	87.7	87.6
2. U.S. MERCHANDISE TRADE BALANCE 2/													
EXPORTS (EXCL. MILITARY)	200.2	221.9	252.2	201.7	206.7	216.2	219.6	223.0	228.8	237.4	246.1	256.6	268.5
AGRICULTURAL	36.6	39.7	42.4	37.4	38.7	40.3	40.0	39.2	39.1	40.4	41.5	43.0	44.6
NONAGRICULTURAL	163.6	182.2	209.8	164.4	168.0	175.9	179.5	183.8	189.7	196.9	204.6	213.6	223.9
IMPORTS	260.8	327.6	372.4	274.4	281.9	303.0	322.9	336.5	348.1	358.4	367.2	377.0	387.2
PETROLEUM AND PRODUCTS	53.8	60.3	65.7	65.8	56.3	52.6	60.7	63.6	64.2	65.0	64.9	65.8	67.2
NONPETROLEUM	206.9	267.3	306.7	208.6	225.7	250.3	262.2	272.9	283.9	293.4	302.3	311.2	320.0
3. U.S. CURRENT ACCOUNT BALANCE													
OF WHICH: NET INVESTMENT INCOME	-48.8	-81.4	-95.8	-48.3	-61.2	-63.7	-78.9	-89.0	-94.2	-96.4	-96.8	-96.2	-93.8
	23.6	28.3	25.2	27.5	24.1	28.2	28.9	28.1	27.8	26.6	25.3	24.4	24.5
4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/													
REAL GNP, % CHANGE, ANNUAL RATES	1.4	2.7	2.6	2.3	3.8	2.6	2.5	2.5	2.6	2.7	2.6	2.5	2.7
CONSUMER PRICES, % CHANGE, ANNUAL RATES	5.7	5.3	5.0	5.3	5.5	5.2	5.3	5.0	5.1	5.0	5.1	4.8	4.9

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1/ GNP EXPORT IMPLICIT DEFLATOR DIVIDED BY GNP IMPORT IMPLICIT DEFLATOR

2/ INTERNATIONAL ACCOUNTS BASIS

3/ GEOMETRIC WEIGHTS USED TO AGGREGATE FOREIGN REAL GNP AND CONSUMER PRICES -- PERCENT SHARE IN TEN-COUNTRY TOTAL MULTILATERAL TRADE.

GERMANY (20.8%), JAPAN (13.6%), FRANCE (13.1%), UNITED KINGDOM (11.8%), CANADA (9.1%), ITALY (9.0%), THE NETHERLANDS (8.3%), BELGIUM (6.4%), SWEDEN (4.2%), SWITZERLAND (3.6%)

8/ PROJECTED