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Strictly Confidential (FR) Class II FOMC

Part 1

January 29, 1997

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Summary and Outlook

Prepared for the Federal Open Market Committee
By the staff of the Board of Governors of the Federal Reserve System

Strictly Confidential (FR) Class II FOMC

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SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee
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Summary

The economy closed out 1996 on a strong note. Our guess is that, on Friday, the Commerce Department will publish an advance estimate of fourth-quarter growth of real GDP around 3-1/2 percent; some private analysts are talking about even higher figures. In any case, we find ourselves faced once again with the question of whether an unexpected zig or zag is telling us something new about the underlying trend in activity.

Arguing against extrapolating the strength in the fourth quarter is the fact that much of the acceleration apparently was the result of a sudden burst of exports--one that, given reasonable assessments of underlying trends, most likely will be followed by only meager increases in the near term. Indeed, the recent appreciation of the dollar will likely exert a significant drag on our trade position in coming quarters. Consequently, we anticipate that net exports will fall substantially through this year--more than in our previous forecasts.

On the other side, however, the prospects for domestic spending appear at least as favorable as before. Households have experienced sizable gains in employment and income of late, and corporate profitability is high. Although bond yields have backed up further in recent weeks, credit conditions on the whole appear quite accommodative. Moreover, the striking further gains in the stock market have left Americans wealthier than we anticipated they would be at this point. Thus, we have raised our projection of the growth of private domestic demand in 1997, offsetting the greater negative effect of the external sector and keeping our forecast of real GDP growth this year at 2-1/4 percent. However, given the upside surprise of the fourth quarter, this means that the level of activity is consistently higher than before.

The higher level carries through 1998. We expect that our widening trade and current account deficit will contribute ultimately to a reversal of market sentiment and will depress the dollar, thereby helping to slow the growth in the trade gap. Given this pattern, we are now projecting that GDP growth will remain slightly above trend next year, at a tad more than 2 percent.

SUMMARY OF THE STAFF FORECAST
(Percentage change, Q4 to Q4, except as noted)

	1996	1997	1998
Real GDP	3.1	2.3	2.1
Previous	2.8	2.3	1.9
Gross domestic purchases	3.3	2.9	2.2
Previous	3.4	2.7	2.2
Consumer price index	3.1	2.6	3.0
Previous	3.2	2.7	2.7
Excluding food and energy	2.6	2.8	3.2
Previous	2.7	2.8	2.9
Level, end of period			
Unemployment rate	5.3	5.1	5.0
Previous	5.3	5.2	5.2

The upward revision to activity is mirrored in higher projected levels of resource utilization. Labor markets, of course, are already tight, and the latest statistics have confirmed the uptilt in compensation increases last year. With the unemployment rate projected to edge down to 5 percent and with the minimum wage jumping again later this year, we see labor cost inflation continuing to escalate. In addition, after a period in which declining prices for non-oil imports have damped inflation, this influence is likely to reverse by next year. More favorable movements in food and energy prices should restrain increases in the overall CPI, but we foresee core CPI inflation increasing from 2.6 percent during 1996 to 3.2 percent during 1998--an acceleration that would be a couple of tenths larger were it not for the effects of technical changes to the index over this period.

Key Background Factors in the Forecast

With this month's revisions, our forecast has edged further in the direction of a more cyclical pattern of inflationary overshooting, which typically has been followed by monetary tightening and then a period of weakness. Though our forecast is still well short of that scenario, we remain concerned that the greater risks may lie on that side.

However, financial market participants seem little afflicted with such concerns. The prevailing view is that, at worst, only the slightest tap on the monetary brakes will be necessary to keep inflation in check in a context of steady, moderate growth. Over the intermeeting period, longer-term interest rates have moved up another 1/4 percentage point in response to the surprising strength of the economy, but the yield curve is only a little steeper than "normal."

As at the time of the last Greenbook, we think the bond markets may benefit somewhat from developments in the fiscal sphere. But over the coming year, as inflationary pressures mount, markets should come increasingly to anticipate a tightening of monetary policy. On balance, we see no reason to predict any large, persistent deviations of bond yields from their current levels--and therefore rates in this forecast are notably higher than in the last, especially in 1998.

The recent rise in bond yields has had no perceptible effect on the stock market. The sustained stream of positive news on growth, inflation, and earnings has reinforced the optimism of equity investors and helped to extend the market rally. The 4 percent to 8 percent rise in stock prices since the last FOMC meeting has surprised us yet again, and we are loath to predict a meaningful setback without a turn in monetary policy--which is absent from this forecast, based as it is on a stable federal funds rate. We estimate that corporate profits came in stronger in the fourth quarter than we had projected and that earnings "momentum" will remain reasonably favorable in the near term. We now expect that stock prices will rise a bit further this year before running out of steam as flattening profits undermine optimistic share valuations.

The trade-weighted exchange value of the dollar, which has risen 4-3/4 percent further against the other G-10 currencies since the last FOMC meeting, has been boosted by market participants who see more signs of weakness in economic activity in a number of countries abroad than we do. Though we have assumed that these forces will persist for a while, we also believe that market participants will, over time, be swayed by the growing U.S. trade and current account deficits. We expect that the dollar, after holding around its current level into the second half of this year, will retrace its recent run-up, depreciating about 5 percent by the end of 1998. Our projection for foreign economic activity is unchanged; we still expect real growth abroad to average just under 4 percent this year and next, up from 3-1/2 percent during 1996.

In recent weeks, the spot price of West Texas intermediate crude oil has declined less than we had anticipated, and we now expect it to average $24 per barrel this quarter, $3 higher than we projected in December. World supplies have remained tight, in part because demand has been boosted by severe weather in Europe. Pressures on supplies should ease gradually by the spring, however, and the spot price is expected to stabilize at $20 per barrel--just a shade higher than previously assumed.

Regarding fiscal policy, we are projecting that the unified federal deficit for fiscal year 1997, $109 billion, will be little changed from the $107 billion recorded in fiscal 1996. Beyond that, we still anticipate that the Administration and the Congress will agree on a program promising budgetary balance by fiscal 2002. The package will probably contain a number of "gimmicks"--such as unspecified spending cuts and asset sales--but we are assuming that the plan will be credible enough to give a little further lift to the bond markets. For fiscal 1998, we have incorporated deficit-reduction measures totaling about $20 billion, enough to hold the unified deficit to $117 billion despite the slowdown in economic growth.

SUMMARY OF THE NEAR-TERM OUTLOOK FOR REAL GDP
(Percentage change at annual rates, except as noted)

	1996:Q4		1997:Q1	
	Dec. GB	Jan. GB	Dec. GB	Jan. GB
Real GDP	2.3	3.5	2.1	1.7
Consumer spending	3.2	3.0	3.4	3.5
Business fixed investment	5.0	2.7	4.1	6.0
Residential structures	-9.8	-8.3	-3.4	-6.6
Government spending	0.5	1.5	-1.1	-2.0
Change in billions of chained 1992 dollars				
Inventory investment	-7.2	-5.0	2.8	7.0
Net exports	6.5	29.4	-10.0	-23.1

Recent Developments and Prospects for the Current Quarter

Our forecast of a deceleration of real GDP from a growth rate of 3-1/2 percent last quarter to 1-3/4 percent this quarter rests almost entirely on analytical deduction. We have no hard economic data for January--other than the weekly unemployment insurance figures, which are notoriously unreliable at this time of year.

Even some potentially important December indicators, notably figures on international trade and inventories, have yet to come in.

The key features of our current-quarter forecast can be summarized briefly. As noted above, the most important factor in the projected downswing in growth is the behavior of net exports. We estimate that this component added about 1-3/4 percentage points to GDP growth in the fourth quarter and will subtract about 1-1/4 percentage points in the first. Some part of this swing is attributable to the residual seasonality in the data; other important considerations are the apparent bunching of some lumpy exports, the effects of the auto strikes, and an assessment of underlying trends.

Meanwhile, we are looking for a step-up in the growth of domestic purchases, from a 1-3/4 percent pace in the fourth quarter to a 3 percent rate in the current period. With federal purchases likely to be dropping sharply (because of a decline in military deliveries), private demand more than accounts for the projected gain.

Strong income, increased wealth, and upbeat sentiment should propel real consumer spending to another hefty advance. We expect the spending increase to be broadly based. Automakers are sweetening price incentives to ensure that their sales regain some of the ground lost last quarter when the strike and then production problems constrained supplies. In addition, sales of personal computers to households may rise with the arrival on the market of the new MMX-chip machines.

We are also projecting greater growth of business investment. For producers' durable equipment, the additional strength is expected to be in the high-tech areas. The sharp upswing in computer shipments in December supports the industry's view that the slippage in October-November was transitory. On the structures side, we have revised up our estimate of expenditures, although outlays are likely to be subdued after the huge increase in construction last fall. Finally, business inventory investment may rise a little with the rebuilding of auto dealers' stocks.

Although we think the demand for new homes is stabilizing, the fourth-quarter falloff in housing starts and permits suggests that residential investment will decline appreciably this quarter. Building in December appears to have been depressed by heavy precipitation; the flooding in the West and the freeze in the Midwest this month have probably delayed the makeup.

Net hiring is expected to slow somewhat this quarter--but much less so than growth of real GDP. The data on initial claims for unemployment insurance, the reports of hiring plans, and households' perceptions of conditions in the labor market suggest that labor demand is holding up quite well; in light of the reported difficulty in finding well-qualified workers, firms may hesitate to trim payrolls. Although the recent spurt in labor force participation could be extended, we think a brief pause is more likely and have allowed the momentum of hiring to show through in a slightly lower jobless rate.

NEAR-TERM OUTLOOK FOR INFLATION AND RESOURCE UTILIZATION
(Percentage change at annual rates, except as noted)

	1996:Q4		1997:Q1	
	Dec. GB	Jan. GB	Dec. GB	Jan. GB
Consumer price index	3.3	3.1	3.0	3.1
Excluding food and energy	2.7	2.7	2.7	2.3
Level (percent)				
Unemployment rate	5.3	5.3	5.2	5.2
Capacity utilization rate (manufacturing)	81.8	82.2	82.1	82.3
Level (dollars per barrel)				
WTI spot crude oil	24.60	24.70	21.00	24.00

Regarding inflation, rapidly rising energy prices last quarter pushed up the overall CPI. With the persistence of higher crude oil costs early this year, we expect another inflationary impulse from energy in the current quarter. Large increases in retail food prices also added to average CPI inflation last quarter; but prices at the crude level decelerated in December and, despite the recent freeze in Florida, continue, on balance, to be reasonably favorable. This suggests that consumer food prices will rise only moderately in the current quarter. At the core level, we see some risk that the higher costs of oil-related inputs and increased compensation rates could lead to a step-up in inflation in the near term. However, goods markets are showing no sign of imminent price acceleration, in part because of competition from imports, and we expect the core CPI to continue increasing only a couple of tenths a month this quarter.

The Outlook for the Economy beyond the Current Quarter

Growth of real GDP is now projected to average almost 2-1/2 percent during the latter three quarters of 1997 and then to be just over 2 percent during 1998--a growth path that, on net, is a bit higher than that in the December Greenbook. This trajectory is expected to result in a reduction of the unemployment rate to 5 percent by 1998. At the same time, the rate of manufacturing capacity utilization is anticipated to remain slightly above its longer-run average. Thus, in this forecast, both labor and industrial markets are expected to be on the tight side for the next two years, and we have allowed those pressures on resources to show through in a bit more of an upward tilt in inflation.

Consumer spending. Although consumer spending picked back up in the fourth quarter, the personal saving rate appears to have continued its upward drift. Future revisions of the NIPA could alter the picture considerably, but any revision would need to be very sizable to put the saving rate on the low trajectory that one might have expected in light of the enormous increase in stock market wealth.

Demographic and other factors could well be contributing to a tendency for higher saving; nevertheless, if this is the case, we still are puzzled why that tendency has become readily apparent only in the past two years. Perhaps the more public discussion of the strains in federal entitlement programs has played a role, and financial firms have done their best to drum up business by heightening concerns about the adequacy of saving for retirement more generally. In any event, the sensational returns in the stock market undoubtedly have provided those worried about their future financial needs an added incentive to act. Moreover, those households whose stock portfolios are held in retirement accounts may be less likely to cash in their chips and go shopping because of the tax penalties that they would face.

At the same time, we continue to find evidence, most recently in our 1995 Survey of Consumer Finances, to suggest that debt burdens may have been constraining spending. Between 1992 and 1995, the rise in debt burdens was greatest among lower-income households who tended to hold relatively few financial assets. These households are the ones who might have felt the pinch more recently when credit card issuers began to restrain new lines of credit.

Nonetheless, the influence of the debt factor on spending has probably been quite mild in the aggregate.

Our earlier forecast assumed a near-term correction in the stock market that implied a noticeable decline in the wealth-to-income ratio in 1997. That assumption had the effect of tempering the upside risk that consumer demand might take off as a consequence of advances in net worth. However, with our current projection of stock prices, the wealth-to-income ratio stays high until 1998 and then turns down only mildly. Moreover, better employment and income prospects, which are likely to keep consumer confidence high, suggest greater support for consumer demand.

Thus, in this forecast, real consumption expenditures are projected to grow slightly faster than real disposable income over the next two years, tilting the saving rate downward. Real PCE increases 3-1/4 percent during 1997 and 2-1/4 percent during 1998. Arguably, our projection still may not fully capture the upside potential for demand associated with the current wealth position of households.

Residential investment. The recent large month-to-month fluctuations in single-family starts during the fourth quarter have obscured the underlying direction of building. But permits, the generally more reliable series, have fluctuated little since September. Meanwhile, other market indicators have been mixed of late. On balance, we are left with the impression that demand for housing stabilized toward the end of 1996, leaving the bulk of the downturn in single-family starts behind us.

Looking ahead, we are projecting just a gradual further decline in new homebuilding over the forecast period: growth of jobs, income, and wealth moderate, but mortgage rates are expected to remain close to recent levels, thereby maintaining relatively favorable cash-flow affordability of home ownership. Starts, which totaled 1.09 million units (annual rate) in the fourth quarter of 1996, drift down to 1.08 million units this spring and 1.06 million units in 1998.

We are also projecting a mild decline in multifamily starts, from 310,000 in 1996 to 280,000 in 1998. Although in-migration is creating strong demand in some locales and the supply of financing is still ample, this market's broader supply-demand balance does not provide strong incentives for construction. In fact, in some parts of the country, manufactured homes, rather than apartments, have been growing in importance as the alternative to traditional single-family residences.

Business fixed investment. At the end of 1996, the fundamental forces shaping the environment for business investment--the user cost of capital goods, internal cash flow, and the output accelerator--were still positive. Moving into the projection period, these influences lose some thrust as flattening profits restrain increases in cash flow and as production and sales decelerate. As a result, growth of real business fixed investment declines from about 8-3/4 percent during 1996 to 6-1/4 percent in 1997 and 1998.

We expect slower spending for equipment to account for this deceleration, although several factors should keep equipment outlays rising at a moderate pace. Most important, declines in the prices of computers, while likely to be less steep than in 1996 (when the cost of memory chips collapsed), should still suffice to maintain growth in real outlays for computers at 20 percent or more. In addition, advances in cellular technology and expanding business uses of satellites should spur rapid growth in spending on telecommunications equipment. Finally, shipments of commercial aircraft to U.S. carriers should trend up as Boeing steps up production to fill orders out of its massive backlog.

For the first time in quite a while, the indicators for nonresidential investment appear relatively consistent, and we are now more confident that a forecast showing a moderate further expansion in this sector is reasonable. Revised data on construction contracts now show a clear uptrend in 1996. Moreover, the areas of relative strength in the contracts figures seem to line up well with reports that suburban and downtown commercial areas are experiencing low vacancy rates and that demand for new hotels has been strong. Real outlays are projected to rise 5 percent during 1997 and 3-1/2 percent during 1998. We sense only hints of speculative fever creeping into this sector; but considering the sector's past proclivities toward excess, the enthusiasm of the stock market recently for the shares of REITs, and the availability of financing from other sources, one might be concerned about the potential for a more dynamic upswing in nonresidential building.

Inventory investment. We estimate that nonfarm inventory accumulation amounted to about $28 billion (annual rate) in the fourth quarter, and we see investment remaining close to that pace on average over the projection period. This would keep aggregate inventory-sales ratios in the recent low range.

Within the nonfarm sector, motor vehicle dealers entered the year with lower stocks of many models than they would have liked. Manufacturers plan a step-up in production this quarter that should begin to restore the desired balance, but our forecast of sales points to an ongoing, modest need for accumulation into the summer. Apart from motor vehicles, stocks appear to have remained in reasonably good alignment with sales through last fall. However, the current rate of accumulation, appropriate when sales are rising so rapidly, will have to be trimmed somewhat in coming quarters as sales moderate.

In the farm sector, inventories shrank a bit last year but should increase somewhat this year and next--if, as we assume, crops are normal. However, the rebuilding of cattle inventories after last year's decline is expected to take considerably longer, extending into 1998 and beyond.

Government. After the spending for defense procurement returns to a more normal level this quarter, overall federal outlays for consumption and gross investment are projected to fall at an average rate of about 1 percent over the remainder of the calendar year. The decline in federal purchases is larger--4 percent--during 1998, when the initial installment of our assumed new round of budget-cutting efforts should begin to affect both defense and nondefense purchases.

Spending by state and local governments is projected to continue to rise at a moderate, 2-1/2 percent, pace over the forecast period. States are in reasonably good fiscal shape, and given our economic outlook, revenues should be growing at a healthy rate. However, these jurisdictions are remaining conservative in their plans for spending, preferring to keep voters happy by holding down taxes.

Net exports of goods and services. Because of the new path for the dollar, we now expect that exports will grow a bit more slowly for the rest of this year than they did in 1996 and that imports will accelerate further. All told, the decline in net exports during the final three quarters of 1997 shaves, on average, 1/2 percentage point (annual rate) from the growth of real GDP over the period. By 1998, this drag on domestic production from the external sector is expected to be stemmed by the lower dollar.

Export growth picks up a bit, returning to its 1996 pace, whereas import growth slows considerably. (A more detailed discussion of the prospects for net exports is contained in the *International Developments* section.)

Labor markets. As has been the case for some time, a key factor shaping the outlook for job market conditions and labor costs is the path for labor productivity. Measured productivity in the nonfarm business sector was reported to have been little changed during 1994 and 1995. Although we estimate that its growth picked up to 0.8 percent last year, its performance was still disappointing relative to our longstanding assumption that the underlying trend during the current expansion had remained at the 1.1 percent pace that prevailed during the 1980s. Taking cyclical influences into consideration as best we can, the current figures seem to indicate that the underlying trend in labor productivity in the 1990s has slowed noticeably, perhaps to around 3/4 percent per year. If we were to adopt that view, we would need to project a much tighter and more inflationary labor market than we have heretofore.

However, a somewhat more moderate response to the incoming data seems appropriate for a variety of reasons. We have difficulty accepting the notion that economic efficiency has performed so poorly when businesses have been restructuring, capital-labor ratios have been rising, and profitability has been well maintained. Notably, in the nonfinancial corporate sector, the reported performance of labor productivity in recent years looks markedly better than in the nonfarm business sector as a whole. The trend in productivity in the nonfinancial corporate sector has been stable since the early 1970s, which suggests that problems in output measurement outside the corporate sector could well be distorting the nonfarm business data. More generally, in recent years, the stronger estimated growth of gross domestic income--from which nonfinancial corporate output is derived--relative to gross domestic product--from which nonfarm business output is derived--could point to an upward revision to the latter series.

Certainly, revisions will be made to both sides of the ledger this summer when the Commerce Department incorporates more up-to-date source data on expenditures and income flows. We are reluctant to anticipate that the adjustment on the product side will be so large that it would erase all of the apparent deceleration in nonfarm business productivity in recent years. But we are persuaded by the economic arguments that output will be revised up to some extent over the 1994-96 period. As a middle ground, we have assumed that the revision will suffice to move the productivity trend for the 1990s up toward 0.9 percent per year, and this is the trend rate of growth that we have carried forward in the current projection. Of course, if our guess is correct, the upcoming NIPA revisions will still leave a gap between gross income and gross output; in the forecast, we have leaned in the direction of having that gap diminish over time, letting measured expenditures rise somewhat faster than income and narrowing the statistical discrepancy over the forecast period.

Our forecast has productivity growing just below trend over the next two years and the unemployment rate declining further. Payroll employment is projected to grow around 1-3/4 percent this year and close to 1-1/2 percent next year--a deceleration from last year's 2-1/4 percent pace; the growth of household employment is only a bit less. Job opportunities are likely to look sufficiently good to continue boosting labor force participation, and welfare reform may reinforce that tendency. We expect the participation rate to move up another 0.3 percentage point during the next two years. On balance, the unemployment rate is projected to decline to 5.1 percent by the end of this year and then to 5.0 percent in 1998.

THE OUTLOOK FOR THE LABOR MARKET
(Percentage change, Q4 to Q4, except as noted)

	1995	1996	1997	1998
Output per hour, nonfarm business sector	-.1	.8	.8	.8
Previous	-.1	.8	.9	1.0
Nonfarm payroll employment	2.0	2.2	1.7	1.4
Previous	2.0	2.1	1.4	1.1
Household employment	.6	2.1	1.5	1.3
Previous	.6	2.0	1.3	1.0
Labor force participation rate[1]	66.5	66.9	67.1	67.2
Previous	66.5	66.9	67.0	67.1

1. Average level for the fourth quarter.

Wages and prices. The upturn in the employment cost index for private industry compensation, from 2.6 percent in 1995 to 3.1 percent in 1996, confirms that labor markets have become sufficiently tight to generate ongoing upward pressure on labor costs. Although businesses profited from another year of slowly rising benefit costs in 1996, the combination of strong labor demand and a hike in the minimum wage pushed wages and salaries up almost 3-1/2 percent, a sharp acceleration from the 2-3/4 percent pace that prevailed during the preceding four years. By our estimates, the direct effect of the minimum wage probably represented at most only 0.2 percentage point of the pickup in wages and about 0.1 percentage point of the acceleration in the overall ECI.

We are projecting a further acceleration in ECI compensation, to 3-1/2 percent this year and 3-3/4 percent in 1998. To some extent, the bigger compensation increases in 1997 will mirror the larger increase in consumer prices over the past year, but they will also reflect the greater tightness of the labor market. Wages also will be boosted a bit in 1997 and 1998 by the next increment to the federal minimum.

Although we anticipate faster growth in benefit costs in 1997 and 1998 than in the past two years, we still expect that those increases will be smaller than the rise in wages. Surveys and anecdotal reports seem to confirm the quarterly pattern of ECI readings, which showed that the deceleration in health insurance costs ended last year. These sources also point to a step-up in premiums this year and possibly much larger increases in 1998 than we have forecast. The stories that insurers and providers are trying to rebuild profit margins seem plausible, particularly when viewed against a backdrop of demands for enhanced quality of service. However, at this juncture, we suspect that some of the more dramatic predictions of premium increases are overblown. Moreover, employers may still have some scope to make changes in coverage and to move workers to lower-cost plans. Nevertheless, if benefit costs were to accelerate rapidly, the increases could pose an upside risk to our overall compensation forecast because the tradeoff of benefit changes against wages is not tight in the short run.

With labor costs moving up a bit more rapidly in this forecast, we have raised our projection for core inflation. Moreover, the anticipated swing in non-oil import prices is more pronounced than before and leaves a greater imprint on the inflation forecast. We project that, after dropping 3 percent last year, non-oil import prices will fall 1 percent this year and then increase 2 percent in 1998--a swing large enough to make a significant contribution to the acceleration in core consumer prices over the period. All told, the officially reported core CPI, which rose 2.6 percent during 1996, is projected to be 2.8 percent during 1997 and 3.2 percent during 1998. As we noted earlier, that acceleration is smaller than it would have been in the absence of scheduled technical changes to the core CPI; we estimate that, without those changes, the index would show an additional 0.2 percentage point acceleration between 1996 and 1998 and that in 1998 a comparably measured core CPI would be rising at its fastest pace since 1991.

STAFF INFLATION PROJECTIONS
(Percentage change, Q4 to Q4, except as noted)

	1995	1996	1997	1998
Consumer price index	2.7	3.1	2.6	3.0
Previous	2.7	3.2	2.7	2.7
Food	2.6	4.2	2.4	2.9
Previous	2.6	4.2	2.8	2.7
Energy	-1.7	7.4	.8	.6
Previous	-1.7	7.4	.4	.9
Excluding food and energy	3.0	2.6	2.8	3.2
Previous	3.0	2.7	2.8	2.9
ECI for compensation of private industry workers[1]	2.6	3.1	3.5	3.7
Previous	2.6	3.0	3.4	3.6
Prices of non-oil merchandise imports	.8	-3.0	-1.0	1.9
Previous	.8	-2.9	-.4	.8
Memo:	------ percentage points -------			
Adjustment to the core CPI for technical changes	.1	.2	.3	.4
Previous	.1	.2	.3	.4

1. December to December.

As in our previous forecast, the overall CPI inflation outlook is more favorable than that for the core CPI because the recent sharp run-up in energy prices begins to reverse this spring. We project that, after rising at a 14-1/4 percent rate in the current quarter, the CPI for energy will drop at a rate of 4 to 5 percent for two quarters before leveling off. Clearly, the possibility that higher energy costs could persist beyond the winter poses an upside risk to our current forecast. Any additional unusual needs for heating oil production would further delay the building of stocks of gasoline and cause price pressures in that market segment this spring. We also continue to assume that harvests in this year and next will be ample enough to prevent a resurfacing of upward pressure on crop prices; thus, food prices are forecast to rise at rates just a shade below core inflation--2-1/2 percent during 1997 and just under 3 percent during 1998.

The overall CPI inflation, which averaged 3.1 percent during 1996, is projected to ease to 2.6 percent this year and then to increase to 3.0 percent during 1998. The chain-weighted price index for gross domestic product, which excludes the direct effect of changes in the cost of imports, is projected to accelerate from an estimated 2-1/4 percent in 1996 to about 2-3/4 percent in both 1997 and 1998.

Financial Markets

Our impression is that investors and lenders are operating increasingly on the basis of rosy projections and seeking less compensation for risk. This behavior is not entirely surprising after several years of cyclical improvement in the economy. Memories of past troubles tend to fade, and in the present case the optimism about the future has been enhanced by a perception among many investors that changes in the structure of the U.S. economy have made it inherently more stable. In addition, the perceived success of the Federal Reserve in fostering noninflationary growth appears to have enhanced confidence that it will be able to keep things on track should something untoward begin to develop.

Our baseline economic scenario for the next couple of years suggests that the day of reckoning may not be close at hand for those who have been incautious in their fund management. The mounting of inflationary pressures could lead to a greater souring of bond market sentiment by next year than we have anticipated, but that risk would seem limited in light of the fact that we are forecasting that headline CPI inflation will be running at 3 percent or less. As we've noted, flagging profit gains may undermine the rosy expectations underlying current stock market valuations, but we do not foresee--in an environment of stable short-term rates--a "correction" of such a magnitude that it will scare investors into a wholesale flight to the exits. If such a circumstance were to occur, it might, among other things, prompt some reflows into M2 assets. Without that development, and with little change predicted for interest rates, we expect that growth in M2 will tend to track nominal GDP.

Credit is likely to remain readily available to businesses, on attractive terms. The less robust profitability of the business sector may make lenders hesitant about reducing risk premiums still further; however, the macro environment looks favorable enough that we cannot assign a high probability to the kind of shock that would cause a significant tightening of terms or standards in the loan or securities markets. The requirements of nonfinancial corporations for external finance will probably expand as capital expenditures rise relative to cash flow. However, the projected financing gap is moderate by historical standards; in the aggregate, the ongoing net retirement of equity shares--in connection with corporate acquisitions and share repurchase programs--will continue to account for a large proportion of the business sector's borrowing activity. Banks are likely to provide a healthy share of the credit that businesses need for M&A or capital expenditures, but the bond market is projected to remain the more important source of debt financing, either directly or indirectly through the securitization of loans.

In the household sector, consumer debt growth is projected to moderate to 5-1/2 percent per year in 1997-98, from the 6-1/2 percent pace of late 1996. This slowing is a bit less than that in the last forecast, partly because of our reassessment of borrowing propensities in light of upward revisions to figures for the latter half of 1996 and partly in reflection of the greater projected strength of spending. Consumer loan delinquencies, especially in the credit card area, are likely to remain high enough to dissuade banks from resuming their earlier, more aggressive marketing and underwriting practices, but credit should continue to be readily available to the vast majority of households. In the mortgage market, debt growth may continue to be enhanced by the promotion of home equity loans; however, given the slackening in home construction and sales, overall home mortgage credit flows are projected to be in the same range as that experienced in recent quarters.

Net borrowing by states and localities appears to have moved back into positive territory. Debt retirements are waning with the completion of advance refundings of higher cost issues from the mid-

1980s, but they are not disappearing. Consequently, we see tax-exempt debt increasing only 2 to 2-1/2 percent a year during 1997 and 1998.

In total, the debt of domestic nonfinancial sectors is projected to grow about 5 percent this year and next, a little less than it grew in 1996 and a little above the pace of nominal GDP expansion. With depositories accounting for about the same share of overall credit flows, and further increasing their reliance on sources of funds in M3, we expect that M3 will continue to grow at a somewhat faster pace than M2.

Alternative Simulations

Our alternative simulations present the consequences of different assumptions about the federal funds rate. In the first simulation, increases in the funds rate begin immediately, and cumulate to 100 basis points by the end of this year. The higher level is maintained throughout 1998. Under this scenario, growth of real GDP this year is 0.4 percentage point less than in the baseline forecast, and during 1998 it is 0.8 percentage point lower than the baseline. The unemployment rate at the end of 1998 is 1/2 percentage point higher than in the baseline forecast. Given the additional slack, CPI inflation in the alternative simulation is fractionally lower during 1997 and 1/2 percentage point lower during 1998 than in the baseline forecast.

ALTERNATIVE FEDERAL FUNDS RATE ASSUMPTIONS
(Percentage change, Q4 to Q4, except as noted)

	1996	1997	1998
Real GDP			
Baseline	3.1	2.3	2.1
Higher funds rate	3.1	1.9	1.3
Lower funds rate	3.1	2.7	2.9
Civilian unemployment rate[1]			
Baseline	5.3	5.1	5.0
Higher funds rate	5.3	5.2	5.5
Lower funds rate	5.3	5.0	4.5
CPI			
Baseline	3.1	2.6	3.0
Higher funds rate	3.1	2.5	2.5
Lower funds rate	3.1	2.7	3.5

1. Average for the fourth quarter.

The second simulation assumes that the funds rate is lowered 100 basis points over the course of this year and then held steady during 1998. The economic effects of this alternative are symmetric to the alternative in which the funds rate was raised.

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January 29, 1997

STAFF PROJECTIONS OF CHANGES IN GDP, PRICES, AND UNEMPLOYMENT
(Percent, annual rate)

Interval	Nominal GDP		Real GDP		GDP Chain-weighted price index		Consumer price index[1]		Unemployment rate[2]	
	12/11/96	01/29/97	12/11/96	01/29/97	12/11/96	01/29/97	12/11/96	01/29/97	12/11/96	01/29/97
ANNUAL										
1994	5.8	5.8	3.5	3.5	2.3	2.3	2.6	2.6	6.1	6.1
1995	4.6	4.6	2.0	2.0	2.5	2.5	2.8	2.8	5.6	5.6
1996	4.4	4.5	2.4	2.4	2.2	2.2	2.9	2.9	5.4	5.4
1997	4.7	4.9	2.4	2.5	2.5	2.6	2.8	2.8	5.2	5.1
1998	4.3	4.6	2.1	2.2	2.5	2.6	2.7	2.8	5.2	5.0
QUARTERLY										
1995 Q1	3.8	3.8	0.4	0.4	3.3	3.3	2.7	2.7	5.5	5.5
Q2	3.1	3.1	0.7	0.7	2.4	2.4	3.5	3.5	5.7	5.6
Q3	6.0	6.0	3.8	3.8	2.1	2.1	2.1	2.1	5.6	5.7
Q4	2.3	2.3	0.3	0.3	2.1	2.1	2.4	2.4	5.5	5.6
1996 Q1	4.2	4.2	2.0	2.0	2.3	2.3	3.2	3.2	5.6	5.6
Q2	6.5	6.5	4.7	4.7	2.2	2.2	3.9	3.9	5.4	5.4
Q3	3.7	3.8	2.3	2.1	1.9	2.0	2.3	2.3	5.2	5.3
Q4	4.5	5.9	2.3	3.5	2.5	2.5	3.3	3.1	5.3	5.3
1997 Q1	5.3	4.6	2.1	1.7	3.2	3.2	3.0	3.1	5.2	5.2
Q2	4.5	4.9	2.3	2.4	2.3	2.7	2.3	2.3	5.2	5.1
Q3	4.3	4.4	2.3	2.4	2.3	2.2	2.6	2.3	5.2	5.1
Q4	4.3	4.6	2.2	2.4	2.3	2.3	2.7	2.8	5.2	5.1
1998 Q1	4.5	4.6	2.1	2.2	2.6	2.8	2.7	2.9	5.2	5.1
Q2	4.2	4.5	1.9	2.1	2.5	2.7	2.7	2.9	5.2	5.0
Q3	4.1	4.5	1.9	2.1	2.6	2.8	2.8	3.0	5.2	5.0
Q4	4.2	4.7	1.9	2.0	2.7	2.9	2.8	3.1	5.2	5.0
TWO-QUARTER[3]										
1995 Q2	3.5	3.5	0.6	0.6	2.9	2.9	3.2	3.2	0.1	0.0
Q4	4.1	4.1	2.0	2.0	2.1	2.1	2.2	2.2	-0.2	0.0
1996 Q2	5.4	5.4	3.3	3.3	2.2	2.2	3.5	3.5	-0.1	-0.2
Q4	4.1	4.9	2.3	2.8	2.2	2.2	2.8	2.7	-0.1	-0.1
1997 Q2	4.9	4.8	2.2	2.1	2.7	2.9	2.6	2.7	-0.1	-0.2
Q4	4.3	4.5	2.3	2.4	2.3	2.3	2.7	2.6	-0.0	-0.0
1998 Q2	4.3	4.6	2.0	2.1	2.6	2.7	2.7	2.9	0.0	-0.1
Q4	4.2	4.6	1.9	2.1	2.6	2.8	2.8	3.1	0.0	-0.0
FOUR-QUARTER[4]										
1994 Q4	5.9	5.9	3.5	3.5	2.3	2.3	2.6	2.6	-1.0	-1.0
1995 Q4	3.8	3.8	1.3	1.3	2.5	2.5	2.7	2.7	-0.1	0.0
1996 Q4	4.7	5.1	2.8	3.1	2.2	2.2	3.2	3.1	-0.2	-0.3
1997 Q4	4.6	4.6	2.3	2.3	2.5	2.6	2.7	2.6	-0.1	-0.2
1998 Q4	4.3	4.6	1.9	2.1	2.6	2.8	2.7	3.0	0.0	-0.1

1. For all urban consumers.
2. Level, except as noted.
3. Percent change from two quarters earlier; for unemployment rate, change in percentage points.
4. Percent change from four quarters earlier; for unemployment rate, change in percentage points.

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REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, ANNUAL VALUES
(Seasonally adjusted annual rate)

January 29, 1997

Item	Units[1]	1990	1991	1992	1993	1994	1995	1996	1997	1998
								- - - Projected - - -		
EXPENDITURES										
Nominal GDP	Bill. $	5743.8	5916.7	6244.4	6553.0	6935.7	7253.8	7578.8	7950.6	8315.3
Real GDP	Bill. Ch. $	6138.7	6079.0	6244.4	6386.4	6608.7	6742.9	6905.9	7081.7	7239.6
Real GDP	% change	-0.2	0.4	3.7	2.2	3.5	1.3	3.1	2.3	2.1
Gross domestic purchases		-0.8	-0.0	4.0	2.9	3.8	1.0	3.3	2.9	2.2
Final sales		0.6	-0.4	3.9	2.0	2.9	1.9	2.9	2.3	2.1
Priv. dom. final purchases		-0.6	-0.8	4.9	3.5	4.0	2.3	3.3	3.5	2.7
Personal cons. expenditures		0.5	-0.2	4.2	2.5	3.1	1.9	2.6	3.2	2.3
Durables		-3.2	-3.1	9.4	7.3	7.0	1.3	5.1	5.3	2.9
Nondurables		-0.5	-1.0	3.4	1.5	3.5	1.1	1.7	3.0	2.1
Services		2.0	0.9	3.6	2.1	2.0	2.4	2.5	2.8	2.3
Business fixed investment		-2.5	-6.0	5.5	8.5	10.1	6.4	8.7	6.2	6.2
Producers' dur. equipment		-2.0	-2.6	9.6	11.5	12.6	6.9	9.3	6.7	7.1
Nonres. structures		-3.5	-12.5	-3.4	1.6	3.6	5.1	7.1	5.0	3.5
Residential structures		-15.1	1.1	16.9	8.1	5.7	-1.5	2.1	-1.7	-0.4
Exports		7.2	8.6	4.1	4.8	9.9	7.4	6.9	5.6	7.1
Imports		0.5	4.1	7.4	10.5	11.8	4.2	8.9	9.8	7.2
Gov't. cons. & investment		2.6	-0.7	1.7	-0.5	0.0	-1.3	2.5	0.4	0.1
Federal		1.6	-3.1	1.3	-5.4	-3.1	-6.7	2.4	-3.3	-4.1
Defense		0.3	-5.3	-1.3	-6.8	-5.7	-6.8	1.7	-3.3	-4.4
State & local		3.3	1.0	2.0	3.1	2.2	2.1	2.5	2.5	2.4
Change in bus. inventories	Bill. Ch. $	10.4	-3.0	7.3	19.1	58.9	33.1	17.0	31.3	30.9
Nonfarm		7.8	-1.2	1.9	26.4	46.8	37.2	19.2	28.5	26.9
Net exports		-61.9	-22.3	-29.5	-72.0	-105.7	-107.6	-116.0	-145.3	-166.8
Nominal GDP	% change	4.4	3.8	6.3	4.8	5.9	3.8	5.1	4.6	4.6
EMPLOYMENT AND PRODUCTION										
Nonfarm payroll employment	Millions	109.4	108.3	108.6	110.7	114.2	117.2	119.5	121.8	123.6
Unemployment rate	%	5.6	6.8	7.5	6.9	6.1	5.6	5.4	5.1	5.0
Industrial prod. index	% change	-0.6	-0.0	3.9	3.0	5.7	1.8	3.7	2.9	3.0
Capacity util. rate - mfg.	%	81.4	78.0	79.5	80.8	83.1	83.1	82.1	82.2	82.4
Housing starts	Millions	1.19	1.01	1.20	1.29	1.46	1.35	1.46	1.38	1.34
Light motor vehicle sales		14.05	12.52	12.85	13.87	15.02	14.74	14.99	14.94	14.91
North Amer. produced		10.85	9.74	10.51	11.72	12.88	12.82	13.30	13.18	13.14
Other		3.20	2.77	2.34	2.15	2.13	1.91	1.69	1.76	1.77
INCOME AND SAVING										
Nominal GNP	Bill. $	5764.9	5932.4	6255.5	6563.5	6931.9	7246.7	7569.2	7930.6	8286.4
Nominal GNP	% change	4.6	3.5	6.2	4.7	5.7	3.9	5.0	4.5	4.5
Nominal personal income		6.4	3.7	7.3	3.6	5.2	5.6	5.7	4.8	4.9
Real disposable income		1.0	0.8	4.0	0.9	2.7	3.1	2.7	2.9	2.2
Personal saving rate	%	5.0	5.7	5.9	4.5	3.8	4.7	4.9	5.1	4.9
Corp. profits, IVA & CCAdj.	% change	6.2	3.9	12.7	19.9	11.3	7.2	6.7	3.4	1.3
Profit share of GNP	%	6.4	6.4	6.4	7.1	7.6	8.1	8.6	8.5	8.2
(excluding FR banks)	%	6.0	6.1	6.1	6.8	7.4	7.8	8.4	8.3	8.0
Federal surpl./deficit	Bill. $	-154.7	-196.0	-280.9	-255.6	-190.2	-161.7	-126.9	-127.5	-108.6
State & local surpl./def.		80.1	75.8	86.3	94.9	99.7	95.0	92.8	88.2	78.9
Ex. social ins. funds		20.2	11.5	18.3	28.0	36.9	36.8	36.9	33.6	25.1
PRICES AND COSTS										
GDP implicit deflator	% change	4.6	3.4	2.6	2.5	2.3	2.5	2.0	2.3	2.5
GDP chn.-wt. price index		4.7	3.3	2.6	2.5	2.3	2.5	2.2	2.6	2.8
Gross Domestic Purchases chn.-wt. price index		5.2	2.7	2.7	2.3	2.4	2.3	2.2	2.2	2.7
CPI		6.3	3.0	3.1	2.7	2.6	2.7	3.1	2.6	3.0
Ex. food and energy		5.3	4.4	3.5	3.1	2.8	3.0	2.6	2.8	3.2
ECI, hourly compensation[2]		4.6	4.4	3.5	3.6	3.1	2.6	3.1	3.5	3.7
Nonfarm business sector										
Output per hour		-0.6	2.2	3.6	-0.3	0.3	-0.1	0.8	0.8	0.8
Compensation per Hour		5.8	4.8	4.6	1.8	2.3	3.7	3.8	3.6	3.7
Unit labor cost		6.4	2.5	1.0	2.1	2.0	3.7	3.0	2.8	2.8

1. Changes are from fourth quarter to fourth quarter.
2. Private-industry workers.

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Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES
(Seasonally adjusted, annual rate except as noted)

January 29, 1997

Item	Units	1994 Q1	1994 Q2	1994 Q3	1994 Q4	1995 Q1	1995 Q2	1995 Q3	1995 Q4	1996 Q1	1996 Q2
EXPENDITURES											
Nominal GDP	Bill. $	6776.0	6890.5	6993.1	7083.2	7149.8	7204.9	7309.8	7350.6	7426.8	7545.1
Real GDP	Bill. Ch. $	6508.5	6587.6	6644.9	6693.9	6701.0	6713.5	6776.4	6780.7	6814.3	6892.6
Real GDP	% change	2.5	4.9	3.5	3.0	0.4	0.7	3.8	0.3	2.0	4.7
Gross domestic purchases		3.5	5.3	3.7	2.5	1.4	0.7	2.6	-0.7	3.0	5.2
Final sales		1.2	3.0	4.2	3.5	0.6	2.1	3.6	1.4	3.0	4.1
Priv. dom. final purchases		3.9	4.4	3.8	4.0	2.3	2.3	3.0	1.4	4.7	4.1
Personal cons. expenditures		2.8	3.5	2.8	3.1	1.0	3.1	2.4	1.1	3.5	3.4
Durables		5.8	4.3	5.6	12.4	-8.9	7.0	9.3	-1.0	8.2	11.4
Nondurables		3.9	3.2	3.8	3.2	2.4	1.8	0.5	-0.4	3.7	1.3
Services		1.6	3.5	1.6	1.2	2.4	3.0	2.0	2.3	2.4	2.7
Business fixed investment		7.3	7.1	13.8	12.2	15.4	3.5	4.9	2.5	11.6	3.8
Producers' dur. equipment		15.5	4.1	19.4	11.9	17.4	3.5	4.3	3.0	13.1	6.7
Nonres. structures		-11.8	15.7	0.2	13.0	9.9	3.4	6.3	1.0	7.7	-3.7
Residential structures		12.8	12.7	-1.8	-0.1	-6.3	-13.4	9.2	6.4	7.4	16.3
Exports		-1.5	15.9	9.7	16.5	2.6	5.9	10.7	10.7	1.8	5.6
Imports		8.2	18.4	10.7	10.3	11.2	4.5	-0.0	1.6	10.6	9.9
Gov't. cons. & investment		-4.3	-0.8	7.0	-1.4	-1.2	0.8	-0.6	-4.3	1.6	7.7
Federal		-11.4	-5.3	11.5	-5.9	-6.5	-1.4	-5.6	-13.2	6.0	9.4
Defense		-17.4	0.7	13.5	-16.1	-7.4	0.6	-7.6	-12.3	4.1	10.0
State & local		0.7	2.2	4.2	1.6	2.3	2.1	2.7	1.5	-0.9	6.7
Change in bus. inventories	Bill. Ch. $	40.5	74.5	64.5	56.1	54.5	30.5	33.0	14.6	-3.0	7.1
Nonfarm		29.7	54.0	50.5	53.0	57.4	33.7	38.6	19.0	2.9	11.7
Net exports		-99.3	-107.3	-111.7	-104.3	-122.5	-121.4	-101.6	-84.9	-104.0	-114.7
Nominal GDP	% change	5.3	6.9	6.1	5.3	3.8	3.1	6.0	2.3	4.2	6.5
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	112.6	113.7	114.7	115.6	116.5	117.0	117.4	117.9	118.5	119.3
Unemployment rate	%	6.6	6.2	6.0	5.6	5.5	5.6	5.7	5.6	5.6	5.4
Industrial prod. index	% change	6.2	6.7	4.4	5.6	3.9	-0.7	3.2	0.8	1.6	6.2
Capacity util. rate - mfg.	%	82.0	83.0	83.3	84.0	84.2	83.1	82.9	82.3	81.7	82.1
Housing starts	Millions	1.38	1.47	1.46	1.48	1.31	1.29	1.42	1.41	1.47	1.49
Light motor vehicle sales		15.07	14.85	14.99	15.16	14.56	14.44	15.04	14.92	15.18	15.13
North Amer. produced		12.94	12.69	12.79	13.12	12.52	12.46	13.18	13.13	13.49	13.41
Other		2.13	2.16	2.20	2.05	2.04	1.97	1.86	1.79	1.69	1.72
INCOME AND SAVING											
Nominal GNP	Bill. $	6781.0	6888.3	6987.0	7071.4	7146.8	7202.4	7293.4	7344.3	7426.6	7537.5
Nominal GNP	% change	5.4	6.5	5.9	4.9	4.3	3.1	5.1	2.8	4.6	6.1
Nominal personal income		-3.4	13.3	4.9	6.7	7.1	4.7	4.9	5.8	4.8	6.8
Real disposable income		-5.4	9.7	2.9	4.2	3.7	0.3	4.3	4.4	2.0	1.3
Personal saving rate	%	2.7	4.0	4.1	4.3	4.9	4.1	4.5	5.2	4.8	4.3
Corp. profits, IVA & CCAdj.	% change	-35.4	82.5	14.8	13.5	-7.4	1.7	40.8	-0.5	23.6	6.8
Profit share of GNP	%	6.8	7.8	7.9	8.1	7.8	7.8	8.4	8.3	8.7	8.7
(excluding FR banks)	%	6.5	7.5	7.7	7.8	7.5	7.5	8.1	8.0	8.4	8.4
Federal surpl./deficit	Bill. $	-212.7	-169.6	-188.5	-190.1	-172.6	-161.1	-158.5	-154.5	-155.2	-126.7
State & local surpl./def.		94.8	105.2	99.6	99.3	99.0	99.0	93.9	88.1	91.0	101.0
Ex. social ins. funds		29.0	41.1	37.9	39.4	40.2	40.9	35.8	30.5	34.1	44.6
PRICES AND COSTS											
GDP implicit deflator	% change	2.8	1.9	2.5	2.2	3.4	2.4	2.1	2.0	2.2	1.8
GDP chn.-wt. price index		2.9	1.9	2.4	2.1	3.3	2.4	2.1	2.1	2.3	2.2
Gross Domestic Purchases chn.-wt. price index		2.4	2.3	3.0	2.0	2.8	2.8	1.6	1.9	2.3	2.1
CPI		1.9	2.8	3.6	2.4	2.7	3.5	2.1	2.4	3.2	3.9
Ex. food and energy		2.9	2.9	3.1	2.3	3.3	3.3	2.8	2.7	2.7	2.7
ECI, hourly compensation[1]		3.0	3.4	3.3	2.3	2.9	2.9	2.6	2.6	2.9	3.2
Nonfarm business sector											
Output per hour		-1.8	1.0	1.7	0.4	-2.3	1.5	1.8	-1.2	1.9	0.6
Compensation per hour		2.9	1.3	1.8	3.3	2.9	4.0	3.7	4.0	3.4	3.9
Unit labor cost		4.9	0.3	0.1	2.9	5.3	2.5	1.9	5.2	1.5	3.3

1. Private-industry workers.

Strictly Confidential <FR>
Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES
(Seasonally adjusted, annual rate except as noted)

January 29, 1997

Item	Units	1996 Q3	- - - - - - - - - - - - - - - - Projected - - - - - - - - - - - - - - - - 1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3	1998 Q4
EXPENDITURES											
Nominal GDP	Bill. $	7616.3	7726.8	7814.0	7908.8	7994.6	8085.1	8177.3	8267.6	8359.9	8456.4
Real GDP	Bill. Ch. $	6928.4	6988.4	7017.8	7060.3	7102.9	7145.9	7184.0	7221.1	7258.2	7295.0
Real GDP	% change	2.1	3.5	1.7	2.4	2.4	2.4	2.2	2.1	2.1	2.0
Gross domestic purchases		3.3	1.8	3.0	2.9	3.3	2.4	2.4	2.3	2.5	1.6
Final sales		0.5	3.8	1.3	2.9	2.2	2.6	2.0	2.1	2.1	2.4
Priv. dom. final purchases		2.3	2.2	3.6	3.8	3.4	3.0	2.8	2.8	2.8	2.6
Personal cons. expenditures		0.5	3.0	3.5	3.4	3.1	2.7	2.4	2.3	2.2	2.2
Durables		-2.6	3.7	5.9	6.1	4.6	4.4	3.3	3.0	2.9	2.4
Nondurables		0.4	1.6	3.2	3.2	3.1	2.4	2.1	2.1	2.1	2.0
Services		1.3	3.6	3.2	2.9	2.7	2.5	2.3	2.3	2.2	2.2
Business fixed investment		17.5	2.7	6.0	6.9	6.0	6.0	6.0	6.3	6.1	6.3
Producers' dur. equipment		20.9	-2.0	6.2	7.7	6.4	6.5	6.8	7.1	7.2	7.5
Nonres. structures		8.4	17.1	5.6	5.0	5.0	4.5	3.9	4.0	3.1	3.0
Residential structures		-5.2	-8.3	-6.6	1.5	-1.6	0.2	-1.0	-1.0	-0.0	0.3
Exports		-0.9	22.6	1.8	7.3	2.1	11.4	4.3	9.2	2.9	12.3
Imports		9.3	5.7	11.6	9.9	8.2	9.6	5.9	9.5	5.8	7.7
Gov't. cons. & investment		-0.6	1.5	-2.0	1.3	1.7	0.7	-0.2	-0.0	1.3	-0.7
Federal		-3.5	-1.8	-9.4	-0.7	0.1	-2.7	-4.8	-4.5	-0.6	-6.2
Defense		-5.5	-1.3	-13.5	-0.6	0.7	0.7	-5.6	-6.2	-0.3	-5.5
State & local		1.1	3.5	2.6	2.4	2.5	2.6	2.4	2.5	2.3	2.4
Change in bus. inventories	Bill. Ch. $	34.5	29.5	36.4	28.4	31.8	28.5	31.9	32.3	32.9	26.5
Nonfarm		34.6	27.6	34.3	25.9	28.8	25.2	28.2	28.3	28.6	22.2
Net exports		-137.4	-108.1	-131.2	-139.7	-155.3	-155.2	-160.8	-165.2	-174.0	-167.3
Nominal GDP	% change	3.8	5.9	4.6	4.9	4.4	4.6	4.6	4.5	4.5	4.7
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	120.0	120.5	121.1	121.6	122.1	122.5	122.9	123.3	123.8	124.2
Unemployment rate	%	5.3	5.3	5.2	5.1	5.1	5.1	5.1	5.0	5.0	5.0
Industrial prod. index	% change	3.3	3.8	2.9	3.0	2.6	3.1	3.3	2.9	2.7	3.3
Capacity util. rate - mfg.	%	82.3	82.2	82.3	82.2	82.2	82.2	82.3	82.3	82.4	82.4
Housing starts	Millions	1.49	1.41	1.41	1.37	1.37	1.36	1.34	1.34	1.34	1.34
Light motor vehicle sales		14.95	14.69	14.91	15.01	14.92	14.92	14.91	14.91	14.91	14.91
North Amer. produced		13.30	12.99	13.15	13.25	13.16	13.15	13.14	13.14	13.14	13.14
Other		1.65	1.70	1.76	1.76	1.76	1.77	1.77	1.77	1.77	1.77
INCOME AND SAVING											
Nominal GNP	Bill. $	7598.9	7714.0	7800.5	7889.9	7972.2	8059.6	8152.0	8238.2	8329.4	8426.0
Nominal GNP	% change	3.3	6.2	4.6	4.7	4.2	4.5	4.7	4.3	4.5	4.7
Nominal personal income		5.7	5.4	5.0	5.0	4.6	4.4	5.1	4.7	4.6	5.1
Real disposable income		4.8	2.6	4.1	2.7	2.7	1.9	3.6	1.7	1.5	2.0
Personal saving rate	%	5.3	5.3	5.4	5.2	5.1	4.9	5.2	5.0	4.8	4.8
Corp. profits, IVA & CCAdj.	% change	3.3	-5.0	14.5	1.3	-0.7	-0.7	2.3	-0.3	2.7	0.3
Profit share of GNP	%	8.7	8.5	8.7	8.6	8.5	8.4	8.3	8.2	8.2	8.1
(excluding FR banks)	%	8.4	8.2	8.4	8.3	8.2	8.1	8.1	8.0	7.9	7.9
Federal surpl./deficit	Bill. $	-120.8	-104.8	-135.1	-128.9	-126.8	-119.2	-120.1	-111.6	-104.4	-98.4
State & local surpl./def.		89.2	90.1	92.2	90.5	87.9	82.4	81.2	80.2	79.2	75.2
Ex. social ins. funds		33.8	35.0	37.3	35.8	33.4	28.1	27.1	26.3	25.5	21.7
PRICES AND COSTS											
GDP implicit deflator	% change	1.7	2.4	2.8	2.4	1.9	2.1	2.4	2.4	2.4	2.6
GDP chn.-wt. price index		2.0	2.5	3.2	2.7	2.2	2.3	2.8	2.7	2.8	2.9
Gross Domestic Purchases chn.-wt. price index		1.9	2.6	2.7	2.0	1.9	2.3	2.8	2.7	2.7	2.8
CPI		2.3	3.1	3.1	2.3	2.3	2.8	2.9	2.9	3.0	3.1
Ex. food and energy		2.4	2.7	2.3	2.8	3.0	3.1	3.2	3.2	3.2	3.3
ECI, hourly compensation[1]		2.5	3.1	3.5	3.3	3.7	3.6	3.7	3.7	3.8	3.8
Nonfarm business sector											
Output per hour		-0.3	0.8	0.1	0.9	1.2	1.1	1.0	0.8	0.8	0.7
Compensation per hour		3.4	4.5	3.8	3.4	3.6	3.7	3.7	3.7	3.7	3.7
Unit labor cost		3.7	3.6	3.7	2.5	2.4	2.5	2.6	2.8	2.9	3.0

1. Private-industry workers.

Strictly Confidential <FR>
Class II FOMC

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

January 29, 1997

Item	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3	1998 Q4	96Q4/ 95Q4	97Q4/ 96Q4	98Q4/ 97Q4
Real GDP	3.5	1.7	2.4	2.4	2.4	2.2	2.1	2.1	2.0	3.1	2.3	2.1
Gross dom. purchases	1.8	3.0	2.9	3.3	2.4	2.5	2.3	2.6	1.7	3.4	2.9	2.3
Final sales	3.8	1.3	2.9	2.2	2.6	1.9	2.1	2.0	2.4	2.9	2.3	2.1
Priv. dom. final purchases	1.8	3.0	3.2	2.8	2.5	2.3	2.3	2.3	2.2	2.7	2.9	2.3
Personal cons. expenditures	2.0	2.4	2.3	2.1	1.8	1.6	1.6	1.5	1.5	1.8	2.1	1.6
Durables	0.3	0.5	0.5	0.4	0.4	0.3	0.3	0.3	0.2	0.4	0.5	0.3
Nondurables	0.3	0.7	0.7	0.6	0.5	0.4	0.4	0.4	0.4	0.4	0.6	0.4
Services	1.4	1.2	1.1	1.0	1.0	0.9	0.9	0.8	0.8	1.0	1.1	0.9
Business fixed investment	0.3	0.7	0.8	0.7	0.7	0.7	0.7	0.7	0.7	0.9	0.7	0.7
Producers' dur. equip.	-0.2	0.5	0.6	0.5	0.6	0.6	0.6	0.6	0.7	0.7	0.6	0.6
Nonres. structures	0.4	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.1
Residential structures	-0.3	-0.3	0.1	-0.1	0.0	-0.0	-0.0	-0.0	0.0	0.1	-0.1	-0.0
Net exports	1.7	-1.3	-0.5	-0.9	0.0	-0.3	-0.2	-0.5	0.4	-0.3	-0.7	-0.2
Exports	2.5	0.2	0.9	0.3	1.4	0.5	1.1	0.4	1.5	0.8	0.7	0.9
Imports	-0.8	-1.6	-1.4	-1.1	-1.4	-0.9	-1.4	-0.9	-1.2	-1.2	-1.4	-1.1
Government cons. & invest.	0.3	-0.4	0.2	0.3	0.1	-0.0	-0.0	0.2	-0.1	0.5	0.1	0.0
Federal	-0.1	-0.7	-0.0	0.0	-0.2	-0.3	-0.3	-0.0	-0.4	0.2	-0.2	-0.3
Defense	-0.1	-0.6	-0.0	0.0	0.0	-0.2	-0.3	-0.0	-0.2	0.1	-0.2	-0.2
Nondefense	-0.1	-0.0	-0.0	-0.0	-0.2	-0.1	-0.0	-0.0	-0.2	0.1	-0.1	-0.1
State and local	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Change in bus. inventories	-0.3	0.4	-0.5	0.2	-0.2	0.2	0.0	0.0	-0.4	0.2	-0.0	-0.0
Nonfarm	-0.4	0.4	-0.5	0.2	-0.2	0.2	0.0	0.0	-0.4	0.1	-0.0	-0.0
Farm	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0
GDP residual	-0.2	0.2	0.0	0.1	-0.0	0.0	0.0	0.1	-0.1	-0.0	0.1	0.0

Components may not sum to total due to rounding.

Strictly Confidential (FR)
Class II FOMC

STAFF PROJECTIONS OF FEDERAL SECTOR ACCOUNTS AND RELATED ITEMS
(Billions of dollars except as noted)

January 29, 1997

Item	Fiscal year[5]				1996				1997				1998			
	1995[a]	1996[a]	1997	1998	Q1[a]	Q2[a]	Q3[a]	Q4								
UNIFIED BUDGET					Not seasonally adjusted											
Receipts[1]	1355	1453	1525	1575	322	446	362	346	341	459	380	363	351	469	392	382
Outlays[1]	1519	1560	1634	1692	393	392	395	405	412	408	410	426	419	424	422	471
Surplus/deficit[1]	-164	-107	-109	-117	-72	54	-33	-59	-71	51	-31	-63	-68	45	-30	-89
On-budget	-226	-174	-184	-187	-84	14	-36	-76	-83	11	-36	-72	-81	2	-36	-101
Off-budget	62	67	75	69	12	39	2	18	12	40	5	8	12	43	6	11
Surplus excluding deposit insurance[2]	-182	-116	-118	-120	-75	52	-34	-65	-72	51	-32	-64	-69	44	-31	-90
Means of financing																
Borrowing	171	130	118	146	80	-23	39	49	58	-31	43	54	69	-25	48	73
Cash decrease	-2	-6	4	0	-1	-16	-6	11	13	-16	-4	10	10	-15	-5	10
Other[3]	-5	-16	-13	-29	-7	-14	0	-1	1	-5	-8	0	-11	-5	-13	6
Cash operating balance, end of period	38	44	40	40	22	38	44	33	20	36	40	30	20	35	40	30
NIPA FEDERAL SECTOR					Seasonally adjusted, annual rate											
Receipts	1459	1544	1625	1684	1523	1576	1582	1625	1606	1626	1645	1663	1672	1691	1711	1731
Expenditures	1629	1683	1749	1798	1678	1702	1703	1730	1741	1755	1772	1782	1792	1802	1815	1829
Consumption expend.	455	457	462	463	454	464	461	463	460	461	464	463	464	462	464	460
Defense	304	303	303	305	299	307	305	306	301	302	304	305	306	303	305	303
Nondefense	151	155	159	158	155	156	157	157	159	160	160	157	158	159	159	157
Other expenditures	1175	1226	1287	1335	1225	1239	1241	1267	1281	1294	1308	1319	1328	1340	1351	1369
Current account surplus	-171	-139	-124	-114	-155	-127	-121	-105	-135	-129	-127	-119	-120	-112	-104	-98
Gross investment	65	63	62	62	65	66	64	64	61	62	62	63	62	61	61	60
Current and capital account surplus	-236	-202	-186	-176	-220	-193	-185	-169	-196	-190	-189	-182	-182	-172	-166	-159
FISCAL INDICATORS[4]																
High-employment (HEB) surplus/deficit	-263	-237	-245	-249	-247	-233	-231	-222	-251	-251	-254	-253	-253	-247	-244	-241
Change in HEB, percent of potential GDP	0	-.4	.1	.1	.1	-.2	0	-.1	.4	0	0	0	0	-.1	0	0
Fiscal impetus (FI), percent, cal. year	-5.6	-1.6	-3.5	-5.5	1.3	1.8	-.2	-.8	-2.2	-.5	.1	-2.7	-1.8	-1.3	-.3	-2

1. OMB's July 1996 deficit estimates (assuming the enactment of the President's proposals) are $126 billion in FY97 and $94 billion in FY98. CBO's January 1997 baseline deficit estimates are $124 billion in FY97 and $120 billion in FY98. Budget receipts, outlays, and surplus/deficit include corresponding Social Security (OASDI) categories. The OASDI surplus is excluded from the on-budget deficit and shown separately as off-budget, as classified under current law. The Postal Service deficit is included in off-budget outlays beginning in FY90.

2. OMB's July 1996 deficit estimates (assuming the enactment of the President's proposals), excluding deposit insurance spending, are $134 billion in FY97 and $96 billion in FY98. CBO'S January 1997 baseline deficit estimates, excluding deposit insurance, are $136 billion in FY97 and $124 billion in FY98.

3. *Other means of financing* are checks issued less checks paid, accrued items, and changes in other financial assets and liabilities.

4. HEB is the NIPA current and capital account surplus in current dollars, with cyclically sensitive receipts and outlays adjusted to the level of potential output generated by 1.8 percent real growth and an associated unemployment rate of 6 percent. *Quarterly figures for change in HEB and FI are not at annual rates.* Change in HEB, as a percent of nominal potential GDP, is reversed in sign. FI is the weighted difference of discretionary changes in federal spending and taxes (in chained (1992) dollars), scaled by real federal consumption plus investment. For change in HEB and FI, negative values indicate restraint.

5. Fiscal 1995 data for the *unified budget come from OMB;* fiscal 1996 and quarterly data come from the Monthly Treasury Statement and may not sum to OMB fiscal year totals.

a--Actual.
b--Preliminary.

CHANGE IN DEBT OF THE DOMESTIC NONFINANCIAL SECTORS[1]
(Percent)

			Nonfederal						
				Households					
	Total	Federal government	Total	Total	Home mortgages	Consumer credit	Business	State and local governments	Memo: Nominal GDP
Year									
1986	12.1	13.6	11.7	11.4	13.8	9.2	12.2	10.8	5.0
1987	9.2	8.0	9.6	12.2	16.3	5.1	6.7	12.1	7.4
1988	9.0	8.0	9.3	9.6	10.9	8.6	9.7	6.5	7.6
1989	7.6	7.0	7.8	8.7	10.1	6.0	7.5	5.7	6.4
1990	6.6	11.0	5.3	7.9	10.1	2.0	3.1	4.9	4.4
1991	4.4	11.1	2.4	5.0	6.6	-1.7	-1.7	8.2	3.8
1992	4.8	10.9	2.8	5.2	6.1	0.6	0.5	2.0	6.3
1993	5.3	8.3	4.2	6.4	5.5	7.7	1.4	5.7	4.8
1994	5.0	4.7	5.1	8.7	6.7	14.6	3.6	-3.7	5.9
1995	5.5	4.1	6.0	8.2	6.3	14.3	6.2	-4.4	3.8
1996	5.3	4.0	5.8	7.6	7.5	8.3	5.2	-0.0	5.1
1997	4.9	3.3	5.5	5.9	6.3	5.6	5.9	2.1	4.6
1998	5.2	4.2	5.5	5.7	6.1	5.6	6.1	2.4	4.6
Quarter (seasonally adjusted annual rates)									
1995:1	6.4	7.1	6.2	8.2	6.5	13.9	6.9	-4.9	3.8
2	6.5	5.2	6.9	8.2	6.0	15.1	7.6	-0.8	3.1
3	4.3	2.4	4.9	8.8	7.1	14.7	4.4	-10.0	6.0
4	4.3	1.6	5.3	6.8	4.8	10.7	5.3	-1.9	2.3
1996:1	6.3	6.6	6.2	9.2	9.6	11.6	4.5	-1.2	4.2
2	4.9	1.7	6.1	7.7	7.2	7.5	4.8	2.8	6.5
3	4.8	4.3	4.9	6.5	6.4	6.7	6.0	-7.1	3.8
4	5.0	3.1	5.7	6.1	6.2	6.3	5.2	5.4	5.9
1997:1	5.0	3.5	5.5	5.9	6.2	5.5	6.0	1.6	4.6
2	4.7	1.8	5.7	5.9	6.1	5.5	5.7	4.4	4.9
3	4.9	4.2	5.1	5.8	6.2	5.5	5.7	-1.1	4.4
4	4.9	3.3	5.4	5.8	6.2	5.5	5.6	3.3	4.6

1. Data after 1996:Q3 are staff projections. Changes are measured from end of the preceding period to end of period indicated except for annual nominal GDP growth, which is calculated from Q4 to Q4.
On a monthly average basis, total debt grows 5.3 percent in 1996, 4.9 percent in 1997, and 5.1 percent in 1998.
Federal debt rises 3.8 percent in 1996, 3.2 percent in 1997, and 4.0 percent in 1998.
Nonfederal debt increases 5.8 percent in 1996, 5.5 percent in 1997, and 5.5 percent in 1998.

2.6.3 FOF

FLOW OF FUNDS PROJECTIONS: HIGHLIGHTS [1]
(Billions of dollars)

	Calendar year				1996		1997				1998	
	1995	1996	1997	1998	Q3	Q4	Q1	Q2	Q3	Q4	H1	H2
					Seasonally Adjusted Annual Rates							
Net funds raised by domestic nonfinancial sectors												
1 Total	646.6	669.5	635.0	722.3	551.0	660.1	661.0	618.5	618.3	642.1	700.5	744.1
2 Net equity issuance	-73.8	-73.1	-87.9	-76.4	-129.2	-62.0	-66.0	-74.0	-108.8	-102.8	-73.2	-79.6
3 Net debt issuance	720.4	742.6	722.9	798.7	680.2	722.1	727.0	692.5	727.1	744.9	773.7	823.7
Borrowing sectors												
Nonfinancial business												
4 Financing gap [2]	57.7	18.6	44.8	83.7	32.0	34.8	36.2	38.4	50.3	54.5	77.1	90.2
5 Net equity issuance	-73.8	-73.1	-87.9	-76.4	-129.2	-62.0	-66.0	-74.0	-108.8	-102.8	-73.2	-79.6
6 Credit market borrowing	241.5	217.2	255.7	281.6	255.9	224.1	261.2	254.2	254.1	253.2	274.6	288.5
Households												
7 Net borrowing, of which:	383.1	380.9	322.1	326.2	339.5	324.6	316.9	322.0	322.8	326.7	323.7	328.7
8 Home mortgages	198.4	253.9	228.9	235.2	223.7	220.2	225.2	225.2	230.2	235.2	235.2	235.2
9 Consumer credit	141.6	93.8	68.8	72.5	80.0	76.0	67.4	68.3	69.3	70.0	71.5	73.5
10 Debt/DPI (percent) [3]	91.0	93.5	94.6	95.5	94.0	94.3	94.1	94.4	94.7	95.1	95.2	95.7
State and local governments												
11 Net borrowing	-48.6	-0.5	22.0	25.7	-76.5	57.0	17.0	47.0	-11.4	35.4	33.1	18.4
12 Current surplus [4]	108.4	109.4	108.7	102.3	101.1	107.6	110.8	110.3	108.9	104.7	103.6	101.0
Federal government												
13 Net borrowing	144.4	145.0	123.1	165.3	161.3	116.5	131.9	69.3	161.6	129.6	142.3	188.2
14 Net borrowing (quarterly, n.s.a.)	144.4	145.0	123.1	165.3	39.3	48.7	57.6	-30.6	42.6	53.6	44.1	121.1
15 Unified deficit (quarterly, n.s.a.)	146.3	110.3	113.6	143.2	33.3	58.8	71.0	-51.4	30.9	63.2	23.6	119.6
16 Funds supplied by depository institutions	274.6	222.0	230.7	260.4	249.1	191.0	227.8	232.4	226.4	236.2	257.2	263.7
Memo: (percent of GDP)												
17 Domestic nonfinancial debt [3]	186.4	188.1	188.5	189.4	188.6	188.1	188.4	188.3	188.5	188.7	189.0	189.6
18 Domestic nonfinancial borrowing	9.9	9.8	9.1	9.6	8.9	9.3	9.3	8.8	9.1	9.2	9.4	9.8
19 Federal government [5]	2.0	1.9	1.5	2.0	2.1	1.5	1.7	0.9	2.0	1.6	1.7	2.2
20 Nonfederal	7.9	7.9	7.5	7.6	6.8	7.8	7.6	7.9	7.1	7.6	7.7	7.6

1. Data after 1996:Q3 are staff projections.
2. For corporations: Excess of capital expenditures over U.S. internal funds.
3. Average debt levels in the period (computed as the average of period-end debt positions) divided by nominal GDP.
4. NIPA surplus less changes in retirement fund assets plus consumption of fixed capital.
5. Excludes government-insured mortgage pool securities.

2.6.4 FOF

Recent Developments

Since the December FOMC meeting, the weighted-average foreign exchange value of the dollar has appreciated 4-3/4 percent in terms of the currencies of the other G-10 countries. The rise in the value of the dollar appears to reflect market perceptions of surprisingly strong growth in the United States and a risk of faltering growth in some other countries.

The dollar has risen 5-3/4 percent against the mark and most other ERM currencies over the intermeeting period. Data releases on employment and business sentiment in Germany and on manufacturing output and household spending in France disappointed market participants and contributed to downward pressure on those countries' currencies. Against the Japanese yen, the dollar has risen 6-3/4 percent. Recent Japanese data have suggested an improvement in economic activity in the fourth quarter from a nearly-flat third quarter, but the budget announced for the fiscal year beginning in April is more contractionary than anticipated. In addition, the sharp declines in Japanese stock prices (10 percent on the Topix since the December Greenbook) and the associated problems of Japanese banks have raised questions about the prospects for private spending, particularly investment. In contrast to most other G-10 countries, Canadian economic indicators have been more positive than expected, and the U.S. dollar has depreciated 1-1/2 percent in terms of the Canadian dollar.

The shifts in sentiment about the economic outlook in the United States and abroad have been reflected as well in the movements of long-term interest rates since the December FOMC meeting. After rising briefly in early January, rates on ten-year government securities abroad have moved down, on balance declining an average of 5 basis points. With the comparable U.S. rate rising 25 basis points, the interest differential has moved in favor of the dollar, consistent with the observed changes in exchange rates. Foreign short-term market rates of interest changed little over the period.

The dollar has depreciated 3/4 percent in nominal terms against the Mexican peso since the December meeting. In mid-January, Mexico repaid ahead of schedule the final $3.5 billion of outstanding obligations to the U.S. Treasury and $1.5 billion to the

IMF; these funds were borrowed during the 1994-95 financial crisis. Over the intermeeting period, Mexican short-term interest rates have declined nearly 5-1/2 percentage points.

. The Desk did not intervene.

Recent data suggest that during the fourth quarter the rate of real output growth in the continental European countries slowed, whereas it improved in Japan and remained healthy in the United Kingdom and Canada. In October and November, German industrial production averaged a little less than the third-quarter level, and unemployment continued to rise through December. However, new orders for manufactured goods remained at their previous high level in October/November. In contrast, in Japan industrial production in the fourth quarter and housing starts and machinery orders in October/November all improved noticeably. The ratio of job offers to applicants increased in both October and November from the third-quarter average. In Canada, retail sales rose sharply in October and November, and employment expanded further through December.

Consumer price inflation remains low or continues to slow in the major industrial countries. Most strikingly, in Italy it has improved to about 2-1/2 percent.

The nominal U.S. trade balance on goods and services improved considerably in October and remained about unchanged in November. For October and November combined, the trade deficit narrowed to about the same annual rate as in the first quarter of 1996. Exports of goods and services were about 5 percent higher than in the third quarter; exports of machinery and industrial supplies moved to record levels. On average, imports of goods and services in October and November were only slightly higher at an annual rate than in the third quarter. Reduced imports of automotive products from Canada (due to the GM strike) nearly offset increases in a wide range of other trade categories. After rising 2 percent during the third quarter, the quantity of oil imported fell 10.5 percent on average during October/November. Weaker consumption and normal seasonal stock drawdowns accounted for the lower oil imports, but preliminary statistics for December from the Department of Energy suggest some rebound.

Prices of nonagricultural exports moved up a bit, whereas prices of agricultural exports continued to decline. Prices of non-oil imports decreased slightly, on balance, in the fourth quarter, continuing a downward trend that began in late 1995.

The price of imported oil jumped 7 percent in October and remained at about that higher level through year-end; it rose 37 percent in the twelve months through December. Skirmishes in the Kurdish region of Northern Iraq, strikes in France that have interrupted refinery operations, and concern about the level of heating oil stocks because of extremely cold weather in Europe helped push up spot WTI prices in December. Deliveries of oil from Iraq put downward pressure on prices during January, offsetting the effect of the cold winter. The price of spot WTI remains quite volatile and is varying in the $23-$25 per barrel range.

SUMMARY OF STAFF PROJECTIONS
(Percent change from end of previous period)

	1996	1997			1998
	Q4	Q1	Q2	H2	
Foreign output	3.7	3.9	3.8	4.0	3.8
Previous	*3.5*	*4.0*	*3.7*	*3.8*	*3.7*
Real exports	22.6	1.8	7.3	6.6	7.1
Previous	*10.4*	*6.5*	*8.0*	*6.0*	*6.4*
Real imports	5.7	11.6	9.9	8.9	7.2
Previous	*5.9*	*10.0*	*9.5*	*9.0*	*7.5*

Outlook

The staff projects that total output in our major foreign trading partners (weighted by shares in U.S. nonagricultural exports) will grow at an annual rate of nearly 4 percent over the forecast period. The dollar is projected to remain around recent elevated levels in the near term but then to decline. After rising sharply in the fourth quarter of 1996, real exports of goods and services are projected to expand only slightly in the current quarter and then to resume moderate growth. Real imports, which will be supported by steady growth in U.S. real GDP and boosted in the near term by recent dollar appreciation, are projected to grow more rapidly than exports this year and at about the same rate as exports next year. As a consequence, net exports should make a negative contribution to real GDP growth of about 3/4 percentage point this year and about 1/4 percentage point next year.

The Dollar. We project that the foreign exchange value of the dollar in terms of the other G-10 currencies will remain essentially unchanged at its recent level through most of 1997, although in light of recent trends it could well move higher. The dollar eventually will weaken as market participants become aware of and concerned about widening U.S. and Japanese current account imbalances. For 1997 the specific path is above that in the previous Greenbook, but by the end of 1998 it is slightly below the endpoint projected in December. We expect that the CPI-adjusted value of the dollar in terms of the currencies of key developing countries will depreciate at a moderate rate throughout the forecast period.

Foreign G-7 countries. The staff forecasts that during 1997-98 real GDP in the foreign G-7 countries will grow on average at an annual rate of about 2-3/4 percent, unchanged from the previous Greenbook; small revisions to the outlooks for individual countries are offsetting. Real output growth in Germany is projected to remain weak through the current quarter, but to rebound later in the year as the expansion, which has so far been largely export-led, relies primarily on growth of domestic demand. In France, economic activity is expected to recover somewhat in the current quarter from an estimated decline in the fourth quarter of 1996 and to accelerate further later this year as investment strengthens. In both countries, fiscal restraint is planned for this year in order to lower the government deficit as a percent of GDP and to achieve the 3 percent reference value of the Maastricht Treaty. We have revised down our prediction for growth in Italy--to about 1 percent this year and 1-1/2 percent next year--as substantial additional fiscal restraint holds down growth in consumption and as recent appreciation of the lira in terms of other ERM currencies limits export growth.

Japanese real GDP is projected to grow a little less than 2 percent during 1997 and about 2-1/4 percent in 1998, a bit weaker overall than in our December forecast. The effects of significant fiscal contraction announced for this year should be partially offset by stronger net exports, given the recent further depreciation of the yen. For Canada, real GDP growth has been revised up to nearly 3-1/2 percent this year and 3-1/4 percent next year. Strength in consumption and private investment should continue through the forecast period; net exports should be about neutral. On average, consumer price inflation in the foreign G-7 countries is projected to remain low over the forecast period.

Our forecast incorporates the assumption of some upward adjustment of short-term market interest rates in the major foreign industrial countries by the end of the forecast period. In the near term, rates are assumed to change little except in Italy, where they are likely to move down further. Subsequently, the continued expansion of economic activity abroad should result in increases averaging about 1/2 percentage point. Long-term interest rates abroad are expected to remain about flat.

Other countries. Real GDP in our major trading partners in Latin America is expected to expand on average about 4-1/2 percent in 1997 and a little less in 1998. We expect that in Mexico the strong growth experienced during 1996 will continue this year, returning real GDP to its pre-crisis level by early 1997. While our growth forecast for Mexico is unchanged from the December Greenbook, we now project somewhat greater real appreciation of the peso which, in combination with the recovery in domestic demand, is projected to reduce significantly the trade surplus during 1997. Higher oil prices have continued to moderate the decline in real GDP in Venezuela during 1996 and have led us to raise our projection for growth in 1997 1 percentage point, to 4-1/2 percent; growth should slow in 1998 as oil prices decline from their recent peak. Our forecast for growth in Chile has been lowered 1 percentage point, to 5 percent; the slowdown is attributable in part to a tightening of monetary conditions and to the decline in copper prices.

Real output in our major trading partners in Asia is expected to expand at an annual rate of 7 percent in 1997 and 1998, slightly faster than in the previous Greenbook. Forecasts for growth in China, Hong Kong, and the Philippines have been raised because of stronger-than-anticipated activity toward the end of 1996 that is expected to continue into 1997. For South Korea, the forecast for growth in 1997 has been reduced a bit to reflect the labor unrest that may continue to simmer and will exert a negative impact on growth over the first half of the year that will not all be made up subsequently.

U.S. real exports and imports. We estimate that during the fourth quarter of 1996 real exports of goods and services grew more than 20 percent at an annual rate, substantially stronger growth than in previous quarters last year and than we projected in the December Greenbook. Trade data through November show rapid growth in all the major components of exports, and we have no basis for assuming that strength was not maintained through December. Exports of services, agricultural products, semiconductors, and a wide range of other merchandise, especially machinery, were robust. Some of the reported strength in fourth-quarter exports reflects residual seasonality in the data and some a bunching of high-value shipments. We estimate that real imports of goods and services in the fourth quarter grew 5.7 percent, annual rate, a bit less than projected in December, as the volume of oil imports decreased and growth of imports of semiconductors remained low. As a consequence, net exports are estimated to have made a positive 1.7 percentage point contribution to real GDP growth at an annual rate during 1996:Q4.

In the current quarter, the volume of exports of goods and services is expected to remain high but to grow only slightly, as the effects of transitory bunching of shipments in the fourth quarter is unwound. In addition, the slowdown in export growth reflects our projection of some downward pull in the first quarter because of residual seasonality in the data. With the level of U.S. economic activity now projected to be higher in the first quarter than forecast in the previous Greenbook, we have revised up our projection for the volume of imported goods and services and look for real net exports to subtract 1.3 percentage points at an annual rate from real GDP growth in the current quarter, somewhat more than projected in December.

Over the remainder of the forecast period, total real exports should grow at an annual rate of about 7 percent. Growth of the volume of nonagricultural exports other than computers and semiconductors should be supported by continued moderate output growth in our trading partners. However, the lagged effects of the recent dollar appreciation should restrain growth of these exports somewhat this year and more next year. The volumes of exports of computers and semiconductors are expected to continue growing rapidly. Service exports are forecast to strengthen a bit in 1998, largely reflecting a more rapid response of service exports to the dollar's projected decline than is the case for goods.

Total real imports of goods and services are projected to grow at an annual rate of about 9 percent during the final three quarters of this year and 7 percent during next year. The volume of non-oil imports other than computers and semiconductors is forecast to expand at an annual rate of more than 7 percent over the remainder of 1997 and then slow to about 4-1/2 percent in 1998. With non-oil import prices projected to decline further this year, relative prices should boost these imports in the near term but be about neutral in their effect next year. Growth of the volume of imported computers is expected to remain rapid while that of imported semiconductors, which actually was negative in mid-1996, is projected to rebound during the current quarter and should continue to be strong through the end of the forecast period.

We expect the quantity of oil imports to remain flat this quarter and then to rise during the remainder of the forecast period, as consumption expands with the increase in U.S. economic activity, and U.S. production declines.

Oil prices. The projected price of imported oil has been revised up about $2.75/b for the first quarter and nearly $1.50/b in the second quarter, reflecting the high spot oil prices that have prevailed through January. The price of imported oil is assumed to have peaked in 1996:Q4 and is projected to stabilize at a WTI price and oil import unit value of $19.75/b and $17.25/b, respectively, by the end of 1997. This end-point has been revised up from that in the December Greenbook because of the persistence of strong economic activity in the United States and the projected weakening of the dollar at the end of the forecast period.

Prices of non-oil imports and exports. Prices of agricultural exports are expected to continue to fall through the middle of this year and then to rise moderately in 1998 as more abundant supplies continue to move prices down from recent peaks for a time. Prices of nonagricultural exports are projected to be about flat on average this year but to move up somewhat next year in line with comparable U.S. producer prices. Prices of non-oil imports are projected to decline further this quarter and next, reflecting the strength in the dollar, and to rise modestly as the projected decline in the value of the dollar begins to show through.

SELECTED PRICE INDICATORS
(Percent change from end of previous period except as noted, AR)

	Projection					
	1996		1997			1998
	Q3	Q4	Q1	Q2	H2	
Ag. exports[1]	-13.0	-10.0	-9.2	-1.6	1.4	4.1
Nonag. exports[1]	-2.3	1.5	0.6	-1.1	0.4	1.6
Non-oil imports[1]	-3.0	-2.2	-4.0	-1.2	0.6	1.9
Oil imports (Q4 level, $/bl)	19.57	22.30	22.20	18.65	17.34	17.25

1. NIPA chain-weighted basis, including computers and semiconductors.

Nominal trade and current account balances. The nominal trade deficit on goods and services is estimated to have narrowed in the fourth quarter to $105 billion from its third-quarter level of $135 billion. During 1997 and 1998, the trade deficit is projected to resume widening, reaching about $135 billion in the fourth quarter of 1998. The balance on net investment income is expected to deteriorate further over the forecast period as well, reflecting growing U.S. net indebtedness. As a consequence, while the current account deficit is projected to have narrowed in the fourth quarter, we expect it to widen over the forecast period, bringing the average for 1998 to about $200 billion or 2.4 percent of GDP.

Alternative Simulation

Our alternative simulation explores the implication of leaving the dollar unchanged at its recent level over the entire forecast period. Federal Reserve policy is assumed to maintain an unchanged federal funds rate. Under this alternative path for the dollar, U.S. real GDP growth and inflation would be no different from the baseline this year. However, with the dollar remaining stronger throughout the forecast period, U.S. real output growth in 1998 would be lessened by 0.2 percentage points and consumer price inflation by 0.1 percentage points.

ALTERNATIVE EXCHANGE RATE PROJECTION
(Percent change, Q4 to Q4)

	1997	1998
Real GDP		
Baseline	2.3	2.1
Unchanged dollar	2.3	1.9
CPI		
Baseline	2.6	3.0
Unchanged dollar	2.6	2.9

OUTLOOK FOR FOREIGN REAL GDP AND CONSUMER PRICES: SELECTED COUNTRIES
(Percent, Q4 to Q4)

Measure and Country	1990	1991	1992	1993	1994	1995	---- Projected ---- 1996	1997	1998
REAL GDP									
Canada	-1.9	0.0	0.5	3.1	4.9	0.7	2.1	3.4	3.2
France	1.5	1.3	0.0	-0.6	4.2	0.4	1.8	2.5	2.3
Germany (1)	6.8	3.3	1.0	-0.4	3.7	1.1	2.2	2.1	2.3
Italy	0.5	1.9	-0.8	-0.0	2.6	2.3	0.6	1.1	1.5
Japan	5.1	2.5	0.1	0.4	0.8	2.6	2.7	1.9	2.3
United Kingdom	-0.7	-1.5	0.3	2.8	4.2	1.9	2.6	3.0	2.4
Average weighted by 1987-89 GDP	2.7	2.9	0.2	0.6	2.8	1.7	2.1	2.2	2.3
Average weighted by share of U.S. nonagricultural exports									
Total foreign	2.4	2.9	1.9	2.9	5.0	1.8	3.5	3.9	3.8
Foreign G-7	0.6	1.5	0.3	1.8	3.8	1.3	2.2	2.8	2.7
Developing Countries	6.0	6.1	4.8	5.3	6.9	2.4	5.6	6.0	5.9
CONSUMER PRICES									
Canada	4.9	4.1	1.8	1.8	0.0	2.1	2.0	1.5	1.4
France	3.5	3.0	1.8	2.1	1.6	1.9	1.7	1.6	1.7
Germany (1)	3.0	4.0	3.4	4.2	2.6	1.7	1.4	1.5	1.6
Italy	6.4	6.2	4.8	4.2	3.8	5.8	2.7	2.6	2.5
Japan	3.2	3.2	0.9	1.2	0.8	-0.8	0.1	1.4	0.2
United Kingdom (2)	9.2	5.7	3.7	2.7	2.2	2.9	3.2	2.7	3.0
Average weighted by 1987-89 GDP	4.7	4.4	2.4	2.5	1.8	1.7	1.5	1.8	1.5
Average weighted by share of U.S. non-oil imports	4.3	4.1	1.9	2.0	1.0	1.1	1.3	1.6	1.1

1. West German data through 1991, All German thereafter.
2. CPI excluding mortgage interest payments, which is the targeted inflation rate.

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OUTLOOK FOR FOREIGN REAL GDP AND CONSUMER PRICES: SELECTED COUNTRIES
(Percent, quarterly change at an annual rate)

	1996				Projected 1997				1998			
Measure and Country	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
REAL GDP												
Canada	1.1	1.2	3.3	3.0	3.9	3.1	3.3	3.4	3.1	3.1	3.3	3.4
France	4.9	-0.7	3.5	-0.3	1.0	2.8	3.2	3.0	2.5	2.3	2.2	2.1
Germany	-1.6	6.0	3.3	1.4	1.3	2.8	2.1	2.3	2.3	2.3	2.3	2.3
Italy	1.8	-1.6	2.4	-0.2	0.3	1.3	1.5	1.2	1.1	1.6	1.5	2.0
Japan	8.4	-1.1	0.4	3.3	3.0	0.8	2.0	1.8	1.9	2.7	2.4	2.3
United Kingdom	2.4	2.2	2.7	3.0	3.2	3.2	3.0	2.8	2.6	2.4	2.4	2.2
Average weighted by 1987-89 GDP	3.8	0.7	2.2	1.9	2.2	2.0	2.4	2.3	2.2	2.4	2.3	2.3
Average weighted by share of U.S. nonagricultural exports												
Total foreign	3.9	2.2	4.3	3.7	3.9	3.8	4.0	4.0	3.8	3.9	3.8	3.7
Foreign G-7	2.7	1.1	2.6	2.6	3.1	2.5	2.8	2.8	2.6	2.8	2.8	2.8
Developing Countries	6.9	2.8	7.1	5.5	5.9	6.0	6.0	6.0	5.9	5.9	5.8	5.8
CONSUMER PRICES (1)												
Canada	1.4	1.4	1.4	2.0	2.2	1.7	1.9	1.5	1.3	1.3	1.4	1.4
France	2.1	2.4	1.8	1.7	1.9	1.5	1.5	1.6	1.7	1.7	1.7	1.7
Germany	1.6	1.5	1.4	1.4	1.8	1.6	1.5	1.5	1.5	1.6	1.6	1.6
Italy	5.0	4.2	3.4	2.7	2.8	2.8	2.5	2.6	2.5	2.5	2.5	2.5
Japan	-0.3	0.1	0.0	0.1	0.0	1.5	1.5	1.4	1.5	0.1	0.2	0.2
United Kingdom (2)	2.9	2.8	2.9	3.2	3.2	3.0	2.8	2.7	2.7	2.8	3.0	3.0
Average weighted by 1987-89 GDP	1.7	1.7	1.5	1.5	1.6	1.9	1.9	1.8	1.8	1.4	1.5	1.5
Average weighted by share of U.S. non-oil imports	1.1	1.2	1.1	1.3	1.4	1.8	1.8	1.6	1.6	1.0	1.1	1.1

1. Year/Year changes.
2. CPI excluding mortgage interest payments, which is the targeted inflation rate.

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1990	1991	1992	1993	1994	1995	------ 1996	Projected 1997	------ 1998
NIPA REAL EXPORTS and IMPORTS									
	percentage point contribution to GDP growth, Q4/Q4								
Net Goods & Services	0.6	0.4	-0.4	-0.7	-0.4	0.3	-0.3	-0.7	-0.2
Exports of G&S	0.6	0.8	0.4	0.5	1.0	0.8	0.8	0.7	0.9
Imports of G&S	-0.0	-0.4	-0.8	-1.1	-1.4	-0.5	-1.2	-1.4	-1.1
	percent change, Q4/Q4								
Exports of G&S	7.2	8.6	4.1	4.8	9.9	7.4	6.9	5.6	7.1
Services	8.9	7.1	-0.9	3.9	4.8	5.1	2.8	2.6	4.3
Agricultural Goods	-7.3	10.1	10.4	-5.4	17.1	-3.1	1.9	-2.6	4.1
Computers	12.3	21.7	25.2	22.7	28.8	49.4	32.0	31.7	29.9
Semiconductors	61.5	41.8	64.8	45.1	68.7	29.7	5.9	23.3	26.2
Other Goods 1/	6.0	7.0	2.3	3.6	7.4	5.3	7.0	3.2	3.3
Imports of G&S	0.5	4.1	7.4	10.5	11.8	4.2	8.9	9.8	7.2
Services	5.8	-2.7	1.5	3.6	0.8	4.1	6.0	3.8	2.3
Oil	-15.8	8.1	12.1	10.1	-0.2	0.9	-0.0	7.8	4.2
Computers	2.9	35.9	45.1	38.8	37.3	43.8	22.4	27.4	23.9
Semiconductors	60.9	55.3	42.0	44.9	47.4	57.1	-13.8	29.9	28.6
Other Goods 2/	-0.3	2.5	5.4	9.4	12.5	-1.2	10.6	8.0	4.6
	in billions of chained 1992$								
Net Goods & Services	-61.9	-22.3	-29.5	-72.0	-105.7	-107.6	-116.0	-145.3	-166.8
Exports of G&S	564.4	599.9	639.4	658.2	712.0	775.4	824.8	882.3	941.7
Imports of G&S	626.3	622.2	668.9	730.3	817.6	883.0	940.9	1027.6	1108.5
	in billions of dollars								
US CURRENT ACCOUNT BALANCE	-94.7	-9.5	-62.6	-99.9	-148.4	-148.2	-163.6	-178.9	-201.4
Net Goods & Services (BOP)	-80.3	-29.9	-38.3	-72.0	-104.4	-105.1	-112.8	-119.9	-133.6
Exports of G&S (BOP)	536.8	580.7	617.7	643.0	698.3	786.5	836.3	884.3	944.6
Imports of G&S (BOP)	617.1	610.6	655.9	715.0	802.7	891.6	949.1	1004.2	1078.2
Net Investment Income	20.9	15.8	11.2	9.7	-4.2	-8.0	-10.3	-21.5	-30.3
Direct, Net	55.9	55.6	51.6	55.9	47.4	57.5	61.6	65.8	69.2
Portfolio, Net	-35.0	-39.8	-40.4	-46.2	-51.6	-65.5	-71.9	-87.3	-99.6
Net Transfers	-35.2	4.5	-35.5	-37.6	-39.9	-35.1	-40.4	-37.5	-37.5

1/ Merchandise exports excluding agricultural products, computers, and semiconductors.
2/ Merchandise imports excluding oil, computers, and semiconductors.

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1993				1994				1995			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
NIPA REAL EXPORTS and IMPORTS												
	percentage point contribution to GDP growth											
Net Goods & Services	-1.1	-0.5	-0.3	0.4	-1.1	0.1	1.2	1.0	-1.1	-0.6	-1.3	1.7
Exports of G&S	-0.2	1.6	1.0	1.7	0.3	0.7	1.2	1.2	0.2	0.7	-0.1	2.5
Imports of G&S	-0.9	-2.1	-1.3	-1.2	-1.4	-0.6	0.0	-0.2	-1.3	-1.3	-1.2	-0.8
	percent change, Q4/Q4											
Exports of G&S	-1.6	15.9	9.7	16.5	2.6	5.9	10.7	10.7	1.8	5.6	-0.9	22.6
Services	0.8	9.7	3.4	5.5	-1.1	4.0	18.7	-0.3	2.7	2.8	-3.8	10.0
Agricultural Goods	-24.4	6.8	43.0	62.9	-0.6	-19.8	16.4	-4.9	9.3	-33.7	8.7	36.9
Computers	24.5	16.6	27.6	48.6	33.0	30.1	79.0	61.0	58.7	21.0	18.3	33.5
Semiconductors	131.4	16.2	45.8	106.7	43.6	19.9	28.8	27.6	-0.0	-20.7	2.6	54.6
Other Goods 1/	-6.6	20.2	6.6	11.1	0.1	7.6	0.6	13.3	-4.2	13.8	-2.8	23.8
Imports of G&S	8.2	18.4	10.7	10.3	11.2	4.5	-0.0	1.6	10.6	9.9	9.3	5.7
Services	1.8	7.5	-1.6	-4.0	21.7	-6.7	5.8	-2.4	13.0	1.3	2.6	7.5
Oil	-8.6	27.2	33.5	-36.2	-2.4	5.3	22.0	-17.2	-22.2	59.9	7.0	-24.9
Computers	45.0	30.9	24.8	49.9	29.6	31.9	64.7	51.8	27.7	23.0	22.2	17.0
Semiconductors	65.3	7.3	43.4	85.8	49.3	61.0	76.4	43.6	4.6	-38.5	-19.0	6.1
Other Goods 2/	7.0	19.9	9.5	14.1	6.9	2.4	-10.9	-2.3	12.1	11.5	11.7	7.0
	in billions of chained 1992$											
Net Goods & Services	-99.3	-107.3	-111.7	-104.3	-122.5	-121.4	-101.6	-84.9	-104.0	-114.7	-137.4	-108.1
Exports of G&S	677.6	703.1	719.6	747.6	752.3	763.2	783.0	803.1	806.7	817.9	816.1	858.7
Imports of G&S	777.0	810.4	831.3	851.9	874.9	884.6	884.5	888.0	910.7	932.6	953.5	966.8
	in billions of dollars											
US CURRENT ACCOUNT BALANCE	-118.8	-144.1	-160.0	-170.6	-156.2	-163.9	-150.8	-121.7	-139.5	-160.8	-191.3	-162.7
Net Goods & Services (BOP)	-90.8	-103.5	-113.8	-109.4	-118.1	-127.3	-97.3	-77.6	-96.9	-114.3	-134.7	-105.4
Exports of G&S (BOP)	662.3	686.1	708.3	736.5	755.9	778.9	796.8	814.5	820.6	836.0	823.1	865.4
Imports of G&S (BOP)	753.1	789.6	822.1	845.9	874.0	906.2	894.2	892.0	917.5	950.3	957.8	970.9
Net Investment Income	4.7	-2.5	-6.4	-12.4	-3.6	-3.4	-17.4	-7.6	1.0	-9.1	-18.8	-14.2
Direct, Net	49.5	46.0	47.4	46.9	57.4	59.9	51.3	61.3	66.1	59.2	56.3	65.0
Portfolio, Net	-44.8	-48.5	-53.7	-59.3	-61.0	-63.3	-68.7	-68.9	-65.0	-68.3	-75.1	-79.2
Net Transfers	-32.7	-38.0	-39.9	-48.9	-34.6	-33.2	-36.0	-36.6	-43.6	-37.5	-37.7	-43.0

1/ Merchandise exports excluding agricultural products, computers, and semiconductors.
2/ Merchandise imports excluding oil, computers, and semiconductors.

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

				------- Projected	-------	-------	-------	-------	-------	-------	-------	-------
	1996				1997				1998			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
NIPA REAL EXPORTS and IMPORTS												
	percentage point contribution to GDP growth											
Net Goods & Services	-1.1	-0.6	-1.3	1.7	-1.3	-0.5	-0.9	0.0	-0.3	-0.2	-0.5	0.4
Exports of G&S	0.2	0.7	-0.1	2.5	0.2	0.9	0.3	1.4	0.5	1.1	0.4	1.5
Imports of G&S	-1.3	-1.3	-1.2	-0.8	-1.5	-1.4	-1.1	-1.4	-0.9	-1.4	-0.9	-1.2
	percent change, Q4/Q4											
Exports of G&S	1.8	5.6	-0.9	22.6	1.8	7.3	2.1	11.4	4.3	9.2	2.9	12.3
Services	2.7	2.8	-3.8	10.0	3.4	1.5	2.2	3.3	4.2	4.7	4.4	4.0
Agricultural Goods	9.3	-33.7	8.7	36.9	-23.8	4.5	8.5	4.1	4.1	4.1	4.1	4.1
Computers	58.7	21.0	18.3	33.5	33.5	31.1	31.1	31.1	29.9	29.9	29.9	29.9
Semiconductors	-0.0	-20.7	2.6	54.6	22.7	22.7	23.9	23.9	26.2	26.2	26.2	26.2
Other Goods 1/	-4.2	13.8	-2.8	23.8	-0.7	6.2	-4.0	12.2	-1.2	7.1	-4.4	12.5
Imports of G&S	10.6	9.9	9.3	5.7	11.6	9.9	8.2	9.6	5.9	9.5	5.8	7.7
Services	13.0	1.3	2.6	7.5	4.7	4.4	3.4	2.9	2.4	2.2	2.3	2.5
Oil	-22.2	59.9	7.0	-24.9	4.2	49.1	15.7	-24.8	3.7	41.4	14.6	-29.9
Computers	27.7	23.0	22.2	17.0	33.5	26.2	25.1	25.1	23.9	23.9	23.9	23.9
Semiconductors	4.6	-38.5	-19.0	6.1	33.5	28.6	28.6	28.6	28.6	28.6	28.6	28.6
Other Goods 2/	12.1	11.5	11.7	7.0	10.2	5.3	5.2	11.5	2.9	5.4	1.5	8.7
	in billions of chained 1992$											
Net Goods & Services	-104.0	-114.7	-137.4	-108.1	-131.2	-139.7	-155.3	-155.2	-160.8	-165.2	-174.0	-167.3
Exports of G&S	806.7	817.9	816.1	858.7	862.6	877.8	882.4	906.5	916.1	936.5	943.3	970.9
Imports of G&S	910.7	932.6	953.5	966.8	993.7	1017.5	1037.7	1061.7	1076.9	1101.7	1117.3	1138.3
	in billions of dollars											
US CURRENT ACCOUNT BALANCE	-139.5	-160.8	-191.3	-162.7	-169.1	-169.6	-182.6	-194.2	-189.5	-198.5	-208.3	-209.5
Net Goods & Services (BOP)	-96.9	-114.3	-134.7	-105.4	-119.2	-114.3	-123.8	-122.3	-127.8	-132.7	-141.3	-132.6
Exports of G&S (BOP)	820.6	836.0	823.1	865.4	867.2	879.9	882.8	907.4	917.6	939.3	946.3	975.3
Imports of G&S (BOP)	917.5	950.3	957.8	970.9	986.4	994.1	1006.5	1029.7	1045.4	1072.0	1087.6	1107.9
Net Investment Income	1.0	-9.1	-18.8	-14.2	-14.9	-20.3	-23.8	-27.0	-26.7	-30.8	-32.0	-31.9
Direct, Net	66.1	59.2	56.3	65.0	68.1	65.3	64.9	64.9	68.2	67.0	69.4	72.4
Portfolio, Net	-65.0	-68.3	-75.1	-79.2	-83.1	-85.6	-88.7	-91.9	-94.8	-97.9	-101.4	-104.3
Net Transfers	-43.6	-37.5	-37.7	-43.0	-35.0	-35.0	-35.0	-45.0	-35.0	-35.0	-35.0	-45.0

1/ Merchandise exports excluding agricultural products, computers, and semiconductors.
2/ Merchandise imports excluding oil, computers, and semiconductors.