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Strictly Confidential (FR) Class II FOMC

Part 1

September 23, 1998

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

September 23, 1998

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee
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Domestic Developments

Overview

The recent performance of the U.S. economy has not differed greatly from what we anticipated in the August Greenbook. Real GDP has evidently risen moderately in the third quarter. Domestic final demand appears still to be relatively robust, but manufacturing activity continues to be restrained by a deteriorating trade balance and by efforts to curb non-motor vehicle inventory accumulation. Labor markets have remained extremely tight overall, while indicators of inflation trends continue to be mixed.

But this has been a far from placid time. Indeed, the intermeeting period has been marked by financial tumult of such a magnitude as to significantly alter the outlook for the economy. Given the lags in the response of domestic demand to these shocks, the effects are not really apparent in the very near term path for real GDP, but they leave a considerable mark on the projected strength of activity in 1999. A deeper retrenchment in U.S. stock markets, more cautious credit provision, and more serious disruptions to economic growth abroad are now expected to combine to produce a sharper deceleration in output than we predicted in August: After rising at an annual rate of about 2-1/2 percent on average in the current half-year, real GDP is projected to increase just 1-1/4 percent over the four quarters of 1999. This pushes the unemployment rate up about 3/4 percentage point by the end of next year.

The outlook for aggregate demand would be still weaker had we not changed our monetary policy assumption. We have set aside our previous assumption of a stable federal funds rate and have instead anticipated that the System will ease money market conditions appreciably between now and next spring. The lower path for the federal funds rate exerts a significant influence on the trajectory of the economy in the latter half of 1999 and in 2000. With this Greenbook, we have extended our forecast through 2000 for the first time. The Fed easing, along with a diminishing drag from the external sector, helps to restore real GDP growth by the second half of 2000 to around the assumed 2-3/4 percent trend of potential output, stabilizing the jobless rate a touch below 5-1/2 percent.

The incoming information on labor cost trends has been ambiguous. However, we continue to think that compensation increases probably are flattening this year and will fall off some in 1999--reflecting not only the effects of weaker profits and of slower business expansion on commissions and bonuses but, more generally, the favorable trend of price expectations. Consumer prices have been held down this year

by the declining costs of oil and other materials, but in coming months, energy prices should turn up a bit, and the softening of the dollar on foreign exchange markets should lead to the firming of import prices. Thus, we continue to project a pickup in overall CPI inflation from just over 1-1/2 percent in the twelve months that ended in August to around 2 percent during 1999 and 2000.

Key Background Factors

As noted above, we have changed our monetary policy assumption this round, in anticipation of an appreciable decline in the federal funds rate between now and next spring. We chose the timing and dimension of the easing steps with an eye to bolstering demand enough that real GDP would again be rising at a moderate rate toward the end of the projection period and to preventing the unemployment rate from moving above our notional NAIRU. The assumed decline in the funds rate appears to be in the vicinity of what the market currently is anticipating.

In the August Greenbook, we indicated that the prevailing 5-1/2 percent funds rate would have been thought to be fairly restrictive were it not for the financial stimulus associated with a high stock market and aggressive lending. Those conditions have clearly changed in the intervening period. Even with monetary policy easing, we do not see financial markets returning to their previous accommodative state. Market participants will likely be licking their wounds for a while, and they will have to contend with an ongoing flow of sour economic news over the coming months.

That news will no doubt include negative reports on corporate profitability that should weigh on the stock market, where current expectations of earnings and notions of "normal" investment returns still seem out of touch with reality. Under the circumstances, we expect that major share price averages will slip back to the recent lows before staging a minimal recovery that begins next spring. This may still be a conservative prediction: In our projection, corporate profits decline 5-1/2 percent over 1999 before rebounding 4 percent in 2000. Consequently, price-earnings multiples will remain high by historical standards, leaving the market vulnerable to a considerably greater correction. As in the last Greenbook, we have chosen to address that downside risk through an alternative scenario using a model simulation described at the end of this section.

The shakiness of business conditions over the next several quarters is likely to affect credit markets along with the equity sector. Risk spreads on corporate bonds have widened dramatically in recent weeks--indeed, by more than would seem explicable by a reasoned reassessment of default risks per se. Rather, hit by losses

initially on "submerging" market investments and on other leveraged trading strategies, many of the players have sought to reduce their risk exposures; in the process, the corporate sector has been the victim of collateral damage, so to speak. We foresee some narrowing of corporate bond spreads as market participants regain their footing, but we do not expect them to approach the negligible risk premiums that prevailed before. On balance, given the greater economic adversities in this forecast and the renewed awareness of risk, we are anticipating a greater degree of restraint in private credit supplies than was built into our previous forecast--not only in the corporate bond markets but also in bank lending to businesses and, to a much lesser degree, to consumers.

We are assuming that after next spring, the federal funds rate will be steady through 2000. Given that the expectation of Fed easing is now so strongly held, we do not foresee much, if any, further decline in Treasury yields beyond the very short end. The yield curve should steepen as prospects for a pickup in economic activity are seen to improve and expectations regarding subsequent Fed action become neutral. On balance, we do not expect, over the next couple of years, to see any major departures in longer-term Treasury interest rates from the range established in the intermeeting period--but yields on higher-risk private bonds should come down a little as risk spreads narrow.

The dollar has depreciated substantially against the yen and key Continental currencies since the last FOMC meeting, but it has declined less in real terms as measured by our broad index of 29 foreign currencies. On this broader basis, we are projecting a 1 percent decline on the dollar in the fourth quarter as the Federal Reserve eases monetary policy. Thereafter, the broad real dollar index trends gradually lower--roughly 1 percent per year--over the remainder of the projection period.

Weighing heavily on financial markets in recent weeks has been renewed concern about the outlook for economic stability and growth in several parts of the world. Relative to our previous forecast, the largest changes in the outlook for foreign economic growth are in Latin America. However, we have also marked down our projections for growth in other areas. Overall, we now expect a slight contraction in foreign economic output over the second half of this year. We anticipate that, in 1999, continued weakness in output in Asia and in South America will hold growth of foreign real GDP to less than 1-1/2 percent--around 3/4 percentage point below our assumption in the August projection. We are expecting that, by 2000, foreign economic growth will pick up to 2-1/2 percent.

Over the past few months, OPEC and its allies appear to have been largely successful in achieving the production cuts that they pledged to implement in late June. As a result, progress has been made in reducing excess inventories of crude oil, and world oil prices have firmed. The spot price of WTI crude should average about $14.50 per barrel for September, and we expect it to climb somewhat above $16 per barrel by the first quarter of next year--a little higher than at the beginning of this year. Given prospects for world economic growth at the time of the August Greenbook, we projected that oil prices would continue to move up a bit further over the course of 1999. The current projection, however, embodies weaker world demand next year, and in that context, we now think it more likely that prices of crude oil will average $16 per barrel in 1999. We have assumed that oil prices will tick up to $16.50 per barrel in 2000 because of the continued weakening of the dollar.

Although the President's predicament has introduced some new political dynamics into the situation, the fiscal policy assumptions underlying our forecast have not changed. We have assumed that there will be no government shutdown and that efforts to push through some tax cuts or to raise spending above the caps will be rebuffed.[1] The changed economic projection and stock market path have led us to mark down our prediction for the federal budget surplus a bit. After reaching roughly $68 billion in the fiscal year now ending, the surplus is expected to shrink to around $56 billion in fiscal 1999, about $6 billion less than our August projection.[2] For fiscal 2000, we expect the surplus to fall slightly, to $52 billion. This trajectory is less favorable than that described by the CBO of late, and it may alter the rhetoric next year regarding the use of future government surpluses.

Recent Developments and the Near-Term Outlook

We now expect that real GDP will increase at an annual rate of around 2-1/2 percent in both the third and the fourth quarters--a projection marginally above that in the last Greenbook. As before, domestic final demand is projected to remain relatively strong--although not so strong as in the first half of the year: Domestic final sales are expected to be up at an annual rate of 3-3/4 percent, on average, this quarter and next, versus 6-3/4 percent during the first two quarters of the year. At the same time, we

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1. A temporary extension of funding for government operations, through October 9, was passed by the Congress last week. We assume that it will be signed and then followed by either another extension or, eventually, a resolution of 1999 appropriations.

2. The surplus now reported for fiscal 1998 is lower than we had expected because recent figures from OMB for September revealed losses from spectrum loans and higher expenditures for agricultural programs as a result of low commodity prices.

Summary of the Near-Term Outlook
(Percent change at annual rate except as noted)

Measure	1998:Q2		1998:Q3		1998:Q4	
	BEA prel.	Sept. GB	Aug. GB	Sept. GB	Aug. GB	Sept. GB
Real GDP	1.6	1.9	2.2	2.6	2.5	2.6
Private domestic final purchases	7.6	7.4	3.3	3.4	4.2	4.9
Personal consumption	5.8	5.9	3.6	3.5	3.1	3.4
Residential investment	14.8	15.5	8.5	10.9	2.7	5.3
Business fixed investment	12.6	12.7	-.6	.3	12.2	14.2
Government outlays for consumption and investment	3.6	3.6	1.4	2.1	2.7	1.5
	Change, billions of chained (1992) dollars					
Inventory investment	-52.3	-51.6	7.6	6.7	-8.2	-7.9
Net exports	-47.8	-45.9	-26.1	-20.7	-26.0	-30.2

anticipate a further drag from net exports, although it is only half as large as during the first two quarters of the year. We continue to anticipate that, while auto dealers will be restocking, other nonfarm businesses will be offsetting that impulse to produce by slowing their inventory investment from the unsustainable pace of the first half.

Real PCE is projected to rise at an annual rate of 3-1/2 percent in the third and fourth quarters, versus 6 percent in the first half. For the current quarter, the story is basically the drop-off in sales of new light motor vehicles owing to tight supplies and a payback after the spring incentive programs ended; retail trade figures through August point to another large increase in spending on other goods, and outlays for services have likely remained on a strong uptrend. Although anecdotes of individuals backing away from some discretionary purchases have already surfaced, we doubt that the turmoil in financial markets and the apparent ebbing in consumer confidence have much affected consumer demand in the aggregate to date. As we move through the next few months, however, the decline in household wealth and the deterioration in sentiment will likely hold spending in closer alignment with income trends than was the case earlier this year.

Housing demand--buoyed by gains in employment, income, and wealth and by the lowest interest rates on fixed-rate mortgages since 1993--also was robust this summer. Housing starts jumped in July, as single-family starts climbed to an annual rate of 1.30 million units and multifamily starts surged to more than 400,000 units.

Even given the favorable underlying conditions, the July figures looked a bit high, and we were not surprised to see starts drop back in August to 1.25 million units for singles and 370,000 for multis. We are looking for only a mild slackening in the pace of starts in the near term. Shortages of construction workers in a number of localities, along with the usual difficulties in obtaining building sites and regulatory clearances, probably have led to a backlog of deferred starts; at the same time, demand indicators have shown no significant softening yet, despite reports that some potential buyers have backed off from purchases because of stock market losses. Applications for loans for home purchase were still setting new highs through mid-September, and mortgage rates have come down considerably over the past few weeks. A further sharp increase in real residential investment expenditures is baked in the cake for the third quarter (our estimate is about 11 percent, annual rate); given lags from starts to construction, outlays will likely post a substantial, though smaller, advance in the fall quarter.

The quarterly pattern of increases in business fixed investment is expected to be uneven in the second half of the year. On average, the rise should be slower than it was over the first half--owing in part to decelerating output and weakening cash flow (especially in manufacturing). The flattening in BFI this quarter can be traced partly to a drop-off in business purchases of light motor vehicles as a result of the GM strikes; that drag should be reversed in the fourth quarter as supplies expand. Another negative this quarter is the expected decline in deliveries of aircraft to domestic buyers--a downswing that is mirrored in a pickup in aircraft exports. Otherwise, domestic purchases of business equipment, at present, still appear to be growing relatively rapidly, on balance. For nonresidential construction, we are projecting little change in outlays during the second half of this year. Further work on office and commercial projects should be a plus, but industrial building is falling, and the recent firming in oil prices does not appear to have been sufficient to stem a slide in outlays for domestic drilling structures.

July data on inventory investment in manufacturing and trade suggest that we were on the right track in expecting that firms--apart from motor vehicle distributors--would be trimming their rate of stock accumulation in the current quarter. At the same time, the sharp step-up in production after the GM strikes appears likely to yield a slight rise in vehicle inventories. On balance, the rate of nonfarm inventory investment may be a little higher in this quarter than in the last, contributing fractionally to the rise in real GDP. We expect a reversal of that contribution in the

fourth quarter, as a further slowing in non-vehicle inventory accumulation will bring the rate of increase in total nonfarm stocks down to around 2-1/2 percent.

The decline in real net exports over the second half of this year is expected to continue to be sizable, albeit about half as steep as in the first two quarters of the year. Nonagricultural exports held up surprisingly well in July, but we expect them to be falling for the remainder of the year. Net exports are projected to hold down the increase in real GDP almost 1 percentage point in the third quarter and then around 1-1/4 percentage points in the fourth quarter.

After having posted an outsized increase in the second quarter, real federal purchases should drop back a bit, on balance, during the second half of the year. Last quarter's figures were boosted by a surge in defense expenditures, which made up for the large decline that occurred in the first quarter. Real nondefense expenditures are projected to remain flat. At the same time, we are anticipating a pickup in spending at the state and local levels during the second half; preliminary numbers on construction in July were weak, but we expect that, especially given the financial health of these jurisdictions, expenditures will rise in coming months.

For a change, the incoming information from the labor market appears to line up reasonably well with our reading of the spending indicators. Hiring has slowed somewhat in recent months; private payroll gains averaged 180,000 per month in July and August, down from more than 220,000 per month during the first half of the year. The deceleration can be traced mainly to deeper cutbacks in manufacturing jobs. However, the recent low level of claims for unemployment benefits suggests that labor demand is hardly crumbling, and we are projecting only a gradual moderation in payroll growth over the remainder of the year.

Firms still have a good number of unfilled positions that they may seek to fill despite increased concerns about the business outlook. Complaints about shortages of workers remain numerous, and firms may not want to pass up opportunities to hire until activity deteriorates convincingly. If anything, the reports in the latest Beige Book suggest that more firms may be hiking pay substantially to attract or to retain workers. However, whether what is happening to pay is anything beyond the acceleration over the past year that has already been captured in the published aggregate wage statistics is difficult to judge. The only new data we have received since the last Greenbook are those for average hourly earnings in August; while wages by this measure were up 1/2 percent last month, the rise followed a couple of small increases and left the trend in wage inflation ambiguous. We are sticking with our forecast that ECI compensation will increase at a 3-3/4 percent rate in the third and

fourth quarters, holding the year-over-year change at about 3-1/2 percent, where it has been since last fall.

Our projection for the CPI over the second half of the year also is virtually unchanged, on balance, from the August Greenbook--with the core index rising at an annual rate of 2.1 percent and the overall index a couple of tenths less than that. We had expected that the decline in retail energy prices would extend into the current quarter, but it appears to have been steeper than we anticipated. And despite the recent upturn in the price of crude oil, we now expect that retail energy prices will rise only a little, on average, during the fourth quarter. On the other hand, our near-term projections for food prices are now a shade higher. For the core CPI, the August increase of 0.2 percent appears to have been influenced appreciably by increases for a couple of items that likely will not be repeated in September: A late Labor Day evidently delayed the usual back-to-school discounts on apparel, and the bimonthly sampling in some cities spread the backup in prices of motor vehicles after the expiration of the substantial June incentives into August.

The Outlook for the Economy in 1999 and 2000

The more adverse shocks to demand in this Greenbook have given our longer-term outlook a more cyclical cast--although that change has been considerably tempered by the revised policy assumption. We are now assuming a sharp step-down in the rate of increase in final sales early next year that engenders a very mild inventory imbalance. Real GDP is projected to increase at an annual rate of but 1 percent during the first half of 1999 and at just over a 1-1/2 percent pace in the second half. The effect of the slackening in resource utilization over the year on core inflation largely offsets the firming in non-oil import prices. The CPI is projected to rise 2.1 percent over the four quarters of the year, whereas the PCE chain-weighted price index should rise just over 1-1/2 percent.

The monetary easing that we have incorporated in the projection is expected to help boost the increase in real GDP in 2000 to an annual rate of around 2 percent in the first half of the year and to a rate of about 2-3/4 percent in the second half.[3] However, factoring in a rebound in growth of labor productivity, the unemployment rate is expected still to be almost 1 percentage point above its current level in 2000,

3. We built a Year 2000 wrinkle into our forecast. At the end of 1999, we expect to see some precautionary inventory accumulation in advance of potential production disruptions. Those additional stocks are drawn down in the first quarter of 2000. At the same time, we also allowed for some disruption of activity in the first quarter of 2000. Together, these two effects hold down the increase in real GDP in the first quarter of 2000, and output bounces back in the second quarter.

Summary of Staff Projections
(Percent change, compound annual rate)

Measure	1998:H2	1999:H1	1999:H2	2000
Real GDP	**2.6**	**.9**	**1.6**	**2.4**
Previous	2.3	1.3	2.0	. . .
Final sales	2.7	1.2	1.6	2.2
Previous	2.4	1.5	2.1	. . .
PCE	3.4	2.5	2.2	2.4
Previous	3.3	2.5	2.6	. . .
Residential investment	8.0	-6.1	-1.5	1.4
Previous	5.5	-4.1	-3.2	. . .
BFI	7.0	4.3	3.0	5.4
Previous	5.6	4.9	4.8	. . .
Government purchases	1.8	1.0	1.3	1.5
Previous	2.0	1.0	1.3	. . .
Exports	-2.3	.1	2.6	4.7
Previous	-1.4	1.9	4.1	. . .
Imports	6.6	6.8	5.3	6.6
Previous	7.5	7.3	5.7	. . .
	Change, billions of chained (1992) dollars			
Inventory change	-1.2	-14.9	.3	14.8
Previous	-.6	-10.0	-3.9	. . .
Net exports	-50.9	-41.9	-21.7	-41.7
Previous	-52.1	-36.2	-17.0	. . .

. . . Not applicable.

and despite sharply reduced expansion of manufacturing capacity, the utilization rate is anticipated to be noticeably below where it is now. In that environment, inflation in 2000 is expected to be unchanged from its pace in 1999.

Consumer spending. Clearly, one of the key elements in the outlook is our assessment of the prospects for the stock market and of the impact of declining share values on household spending patterns. We continue to believe that the outsized increase in consumer demand relative to income over the past few years was largely a result of the rise in household net worth, in which the stunning rise of share prices was the major driver. With the recent sharp decline in those prices, the ratio of net worth to income has dropped appreciably, and the additional stimulus from the "wealth

effect" should fade over the next few quarters. For this reason, our forecast shows the personal saving rate essentially stabilizing--at a very low level--as spending increases roughly in line with disposable income.

Given the increased and more direct role of equities in the finances of households (especially with so many individuals seemingly banking on their IRAs and 401(k) accounts for retirement security), one might wonder whether the market reversal could precipitate a more radical shift in savings propensities in the present case. The jury is still out on that question. The preliminary Michigan SRC survey for September did reveal some concern among households about the decline in the market and its consequences, but it provided no sign that respondents were alarmed enough to alter their spending habits radically. One reason may be that individuals seem to have retained their faith in the longer-term profitability of the stock market investments: Mutual fund customers have redeemed only modest portions of their equity fund holdings, and surveys indicate that they have maintained optimistic views of the longer-term returns on equity investments. The further slippage in the markets anticipated in this forecast should do little to alter this thinking--although a more sizable decline might exact a greater toll of confidence, possibly exaggerating the normal wealth effects on spending.

Be that as it may, we are projecting that real PCE will rise 2.4 percent in 1999. We are looking for a decided deceleration of spending on discretionary items in the nondurables and services categories. However, we also expect that demand for durable goods will moderate. Notably, purchases of motor vehicles, which have been strong for several years now, should slip, and a slackening of housing activity should take some of the steam out of the demand for furniture and appliances. The rise in PCE is projected to be moderate again in 2000; given our expectation that share prices will remained subdued, spending will do well to keep up with gains in income.

Housing. Starts of new homes are projected to fall back noticeably during 1999. Single-family starts are expected to drop to 1.18 million units next year after having averaged 1.25 million units in 1998. The negative effects of the drop in wealth and of slower employment and income gains will tend to outweigh the stimulus from lower mortgage interest rates. However, because the level of home construction would remain quite high, additions to supply would still be ample. Given the lack of pent-up demand, we are projecting single-family starts to be unchanged in 2000, despite improving job growth.

We also anticipate a weakening in the market for apartment units next year. This year has been another relatively strong one for multifamily starts, and those units

will be coming on the market at a time when demand from potential buyers and renters is easing. The effect of a backup in vacancy rates could be reinforced by a more cautious attitude among lenders. The flow of capital from REITs already has slackened as the equity market has turned negative on these entities this year. As a result, after having stayed at around 340,000 units for two consecutive years, multifamily starts probably will drop back to around 300,000 units next year before firming a bit in 2000.

Business fixed investment. Real business fixed investment is projected to decelerate further next year, rising 3-1/2 percent over the four quarters of 1999 after having increased at an average annual rate of 7 percent during the second half of 1998. The step-down occurs entirely in spending for producers' durable equipment. Underlying that deceleration is the slower trend in sales, a marked deterioration in corporate cash flow next year, and a less favorable external financing environment.

The slowing in real outlays for producers' durables is expected to be widespread by type of equipment. Even spending on computing equipment, which we expect will rise more than 60 percent in real terms in 1998, is not expected to be immune from prospective cutbacks in capital budgets. However, steeply falling prices along with a desire to take advantage of newly available features and to resolve Year 2000 problems should prop up spending somewhat--especially early in the year, before some firms suspend major system upgrades so that they can focus on final software fixes and testing. In nominal terms, we are projecting that outlays for computers will rise only a few percent next year, which when deflated translates into more than a 30 percent gain in real, quality-adjusted terms. Outlays for communications equipment also should post another sizable real increase in 1999, supported by the rapidly growing demand for the widening array of telecommunications services that are being offered at attractive prices. However, we expect to see cutbacks over the course of the year in deliveries of aircraft and motor vehicles to domestic firms and only a small increase in outlays for other types of equipment overall. Concerns in some manufacturing industries are expected to lead to a considerable reduction in their purchases of new equipment to curb the growth of excess, unprofitable capacity.

Nonresidential construction is expected to change little, on balance, over the projection period. Financing conditions have deteriorated considerably in the commercial sector. During 1999, the weaker rise in sales will put a damper on the desire to undertake new office and commercial projects, which have been this year's bright spots. However, with oil prices firming, we expect the recent sharp drop in

outlays for drilling and mining structures to stop. Industrial building, which has already fallen considerably this year, is projected to continue declining.

Business inventories. We are assuming that, by the end of this year, businesses (other than GM dealers, who are now restocking) will have significantly moderated the expansion of their inventories, leaving few, if any, noticeable imbalances as the new year begins. However, the marked deceleration of sales in 1999 will call for a further diminution in the pace of inventory accumulation. We would not be surprised to see some increase in inventory-sales ratios in the early part of the year, when final demand is particularly weak, but we are expecting the adjustments to occur quite quickly and have not anticipated any dramatic inventory dynamics. On net, the expected down-shifting in the rate of nonfarm inventory investment is projected to be a slight drag on real GDP next year. In 2000, inventories are assumed to rise roughly in line with sales and to make a marginally positive contribution to the increase in real GDP.

Farm inventories are expected to accumulate at a slower pace in 1999 as producers curb output in response to the lower prices that they have experienced this year and export demand stabilizes.

Government spending. Real federal purchases are projected to decline at an annual rate of 1-1/4 percent over the forecast period. This trajectory is consistent with the 1997 budget agreement, which set limits on discretionary spending and required that any changes to tax or mandatory outlay programs be deficit-neutral. Although nominal nondefense spending should increase a little, it is projected to slip gradually in real terms. Real defense spending is expected to fall at a rate of around 1-1/2 percent, on average, although the quarterly pattern likely will continue to be lumpy.

In the state and local sector, real purchases are projected to rise at a moderate, 2-3/4 percent, annual rate through 2000. These jurisdictions have seen their revenues outpace their expectations recently, but they have remained cautious about making major changes in their budget policies. Some politicians may yet succumb to the temptation to dip into mounting cash balances, but their appetite for cutting taxes or boosting spending should be lessened next year as they recognize that a weakening economy is cutting into revenues.

Net exports. With the revision to prospects for foreign GDP, we have marked down our expectations for real exports of goods and services; that increase is now just 1-1/4 percent next year. Export demand is expected to recover in 2000, pushing the volume up about 4-3/4 percent as foreign growth picks up and the real depreciation of

the dollar enhances U.S. competitiveness. Demand for imports is now expected to be weaker in 1999 in light of the slower projected growth of domestic activity. On net, the decline in real net exports next year is anticipated to subtract almost 3/4 percentage point from the increase in real GDP, less than half of its negative contribution this year. In 2000, the drag diminishes to less than 1/2 percentage point. (A more detailed discussion is contained in the *International Developments* section.)

Labor markets. Firms, confronted with pressures on their profit margins, undoubtedly are continuing to push for gains in efficiency, and we continue to believe that the underlying trend in labor productivity will be growing 1-3/4 percent a year over the projection period. However, as noted above, many businesses have been scrambling for workers, and they may continue to hire even as increases in output tail off in the period ahead. Consequently, we expect that labor productivity will rise at something less than the underlying trend pace during the current half-year and then lag still more during much of 1999, when economic activity turns distinctly subpar. In 2000, as output picks up and Year 2000 fixes are less of a drain, productivity should accelerate considerably; that year's gain is projected to be 2 percent.

The Outlook for the Labor Market
(Percent change, Q4 to Q4, except as noted)

Measure	1997	1998	1999	2000
Output per hour, nonfarm business	1.7	1.5	1.0	2.0
Previous	1.7	1.1	1.3	...
Nonfarm payroll employment	2.7	2.3	.7	.9
Previous	2.7	2.2	.8	...
Household employment survey	2.1	.9	.3	.6
Previous	2.1	.9	.4	...
Labor force participation rate[1]	67.1	66.9	66.8	66.8
Previous	67.1	67.0	66.9	...
Civilian unemployment rate[1]	4.7	4.5	5.2	5.4
Previous	4.7	4.6	5.1	...

1. Percent, average for the fourth quarter.
... Not applicable.

This pattern of labor productivity implies that variations in the growth of labor demand will be more muted than those in the growth of output. Nonetheless, net hiring is projected to be meager by the middle of next year before picking up as

activity accelerates later in 1999 and 2000. By the spring of 2000, however, the unemployment rate is expected to have risen to 5.4 percent, where we have it stabilizing.

Some side notes on the quite irregular quarterly pattern of labor market activity in 2000: Output per hour will mirror the temporary hesitation in the growth of real GDP resulting from the small, brief disruption of activity that we believe will accompany problems associated with the Millennium Bug in the first quarter of 2000; a rebound is expected in the subsequent quarter. And public payrolls will experience a bulge in the second quarter of 2000 when temporary workers are hired to conduct the decennial 2000 census.

Wages and prices. Given the easing of labor market pressures and the pricing environment that we are forecasting, we continue to expect that increases in labor compensation will level off in the near term and diminish over the next two years. The year-over-year change in ECI compensation is projected to remain around 3-1/2 percent during the next several quarters, 3.2 percent next year, and 2.9 percent in 2000. Over time, rising joblessness should restrain the size of pay increases. The deceleration in labor compensation is expected to occur in the wage and salary component of the index. In the nearer term, one factor is that the rising commissions of recent times--most notably in the finance and real estate sectors--will not be sustained. However, a noticeable step-up in the rate of increase in overall benefit costs is likely in 1999, largely because of the rising cost of health insurance. The large increases in premiums recently announced in the Federal Employee and CalPERS insurance programs underscore the pressures facing the health care industry: rapid increases in the costs of prescription drugs and the need simply to correct the underpricing of benefits that accompanied the earlier all-out competition for market share. In addition, lower stock values are likely to boost employer costs for defined benefit retirement plans. Some offset to these higher costs should come from smaller "nonproduction" bonus payments over the next several years. Indeed, businesses may benefit from a cooler labor market in ways that are not so obvious in the published data as the need to offer hiring bonuses and other costly inducements lessens. Although the recent slump in the stock market raises the risk that companies may not be able to get so much mileage from granting options, we are not anticipating that this will have much impact on aggregate wages and benefits--especially because many firms will respond by simply cutting strike prices or issuing more options.

We are projecting that core CPI inflation will drop to 2.1 percent in 1999, with the shift to "geo-means" in January accounting for all of the deceleration from the

Staff Inflation Projections
(Percent change, Q4 to Q4, except as noted)

Measure	1997	1998	1999	2000
Consumer price index	1.9	1.6	2.1	2.0
Previous	1.9	1.5	2.1	...
Food	1.7	1.8	1.3	1.5
Previous	1.7	1.7	1.3	...
Energy	-1.0	-8.0	4.1	1.6
Previous	-1.0	-7.2	3.9	...
Excluding food and energy	2.2	2.3	2.1	2.1
Previous	2.2	2.3	2.1	...
PCE chain-weighted price index	1.5	.9	1.6	1.5
Previous	1.5	.9	1.6	...
Excluding food and energy	1.6	1.3	1.5	1.5
Previous	1.6	1.3	1.5	...
GDP chain-weighted price index	1.7	1.0	1.5	1.5
Previous	1.7	1.1	1.5	...
ECI for compensation of private industry workers[1]	3.4	3.4	3.2	2.9
Previous	3.4	3.4	3.2	...
Prices of core non-oil merchandise imports	-.7	-2.7	.6	1.4
Previous	-.7	-2.9	1.1	...
	Percentage points			
MEMO: *Adjustments for technical changes to the CPI*[2]				
Core CPI	.2	.4	.6	.6

1. December to December.
2. Adjustments are calculated relative to the methodological structure of the CPI in 1994.
... Not applicable.

2.3 percent rate we expect will be recorded this year. The overall CPI is forecast to accelerate next year. Energy prices increase 4 percent, after having fallen 8 percent this year, and prices of non-oil imports turn upward. On a reported basis, the CPI inflation rate for 1999 is projected to be 2.1 percent, 1/2 percentage point more than this year, despite the technical changes in the index. We are also looking for pickups in inflation as measured by GDP-related indexes from current rates, but with numbers in those cases generally being in the lower, 1 to 1-1/2 percent, range.

The projected inflation rates for 1999 appear to be on the low side of prevailing expectations--at least as suggested by survey readings, if not by the spreads between nominal Treasuries and TIPS. The more favorable outcome should encourage a further decline in those expectations and help to mute inflationary tendencies in 2000. This factor, along with the reduced pressures on resources, should offset any impulse to U.S. inflation that might come from the effects of a modestly declining dollar on import prices. Consequently, we are projecting that prices overall will increase at about the same rate in 2000 as in 1999.

Money and Credit Flows

The expansion of the debt of the nonfinancial sectors this year, at 5-3/4 percent, is anticipated to outstrip the growth of nominal GDP, owing mainly to increased borrowing by the business and household sectors. However, over the next two years, growth of the debt aggregate should be reduced significantly as those sectors pull back somewhat in the face of weaker income growth and a slightly more restrictive credit supply environment. The slowdown is a bit more pronounced than projected in the previous Greenbook.

Borrowing by nonfinancial businesses is anticipated to slow substantially in coming quarters. As we move into 1999 and 2000, merger and acquisition activity is likely to tail off appreciably, and firms will be more cautious in their investment outlays, so that debt growth is expected to slow somewhat even as the generation of internal funds remains subdued. Less-receptive credit markets probably will play a role in encouraging this falloff in borrowing; the wider bond market spreads of late are expected to persist at least for a while before retracing a portion of their recent increases, and banks should follow suit by tightening standards and terms on business lending. Indeed, the results of the special survey of senior loan officers conducted this month suggests that process of bank tightening may already have begun. (The details of the survey results will be reported in the Greenbook *Supplement* on Friday.)

Household debt is expected to grow 8 percent this year. Attractive interest rates have spurred an increase in mortgage borrowing beyond that which is attributable to home purchases alone. The encouragement potential borrowers have had from lenders (and the tax code) to substitute home equity loans for consumer credit is only a part of that story. Possibly, optimistic views about prospective returns on stock market investments have fostered a tendency to borrow more heavily to cover expenditures; if so, recent and prospective equity price developments should lessen this enthusiasm for leverage. But the more important drag on household borrowing

growth over the next two years will be a moderation in the growth of spending. Although demand-side developments will be the dominant influence slowing debt growth, the weakening in the economy and rising unemployment may prompt lenders to tighten their underwriting standards. Investors in asset-backed securities are likely to continue to exhibit greater caution, which may leave an imprint on the pricing of consumer loans and subprime mortgages. On net, the increase in household debt over the next two years is expected to be down around 2-1/2 to 3 percentage points from its 1998 pace.

In the state and local government sector, the rise in debt should slow somewhat. Capital spending is projected to remain on a moderate track, but the opportunities to pre-refund debt are now more limited because of the large amount of activity that has already occurred (repeat advance refundings typically are not permitted). The continued federal surpluses mean that the Treasury will be retiring debt on balance, with nominal marketable securities running off at a pretty fast clip.

We are inclined to attribute a noticeable portion of the recent rapid growth of the monetary aggregates to redirection by households from the capital market toward safer and more liquid instruments. Supporting this notion, about two-thirds of the net increase in M2 over August and September was recorded in money market mutual funds, which mirrored a drying up of inflows to equity market funds. This reassessment of capital risk and increased risk aversion should continue in the months ahead and be sufficient to pull up M2 growth over the four quarters of 1998 to 8 percent, considerably faster than was expected at the time of the August FOMC meeting. However, given our working assumption of no large changes in stock prices in 1999 and 2000, those safe-haven inflows should abate. As a result, growth of M2 should step down over the next two years. M3 is anticipated to move in tandem, expanding at a 10 percent rate this year before decelerating considerably in 1999 and 2000, consistent with its longer-run tendency to expand faster than both M2 and nominal GDP.

Alternative Simulations

Our alternative model-based simulations present the implications, first, of unchanged System policy and, then, of two different scenarios for the stock market. In the first alternative, the federal funds rate remains constant at 5-1/2 percent through 2000, instead of declining over the next few quarters. In this scenario, the increase in real GDP is 1/2 percentage point below the baseline case next year and 3/4 percentage

Alternative Federal Funds Rate and Stock Market Assumptions
(Percent change, Q4 to Q4, except as noted)

Measure	1998	1999	2000
Real GDP			
Baseline	3.2	1.3	2.4
Unchanged funds rate	3.2	.8	1.6
Weaker stock prices	3.2	1.0	2.0
Constant stock market wealth-to-income ratio	3.2	1.7	2.9
Civilian unemployment rate[1]			
Baseline	4.5	5.2	5.4
Unchanged funds rate	4.5	5.4	5.9
Weaker stock prices	4.5	5.3	5.6
Constant stock market wealth-to-income ratio	4.5	5.1	5.1
CPI excluding food and energy			
Baseline	2.3	2.1	2.1
Unchanged funds rate	2.3	2.0	1.6
Weaker stock prices	2.3	2.1	2.0
Constant stock market wealth-to-income ratio	2.3	2.1	2.2

1. Average for the fourth quarter.

point lower in 2000--enough so that the unemployment rate would be approaching 6 percent by the end of the projection period. Inflation would be considerably lower--turning back downward in 2000--with the effects of the added slack being reinforced by a firmer dollar and a perception on the part of the public that the Federal Reserve was emphasizing the pursuit of price stability.

The second and third alternatives consider different paths for the stock market. The baseline for this Greenbook assumes that after having dropped a bit below the recent lows in the near term, share prices recover about 5 percent by early 2000. The second alternative takes the more pessimistic view that stock values drop about 10 percent below the recent low by the second quarter of next year and then move up only slightly in 2000 (essentially paralleling the baseline path). In this scenario, which we believe is quite plausible, sticking with the baseline interest rate path would result in 1/4 percentage point slower real GDP growth in 1999; the shortfall widens to almost 1/2 percentage point in 2000. The payoff in the form of lower inflation is relatively modest because, in the model's view, the public's perceptions of Federal Reserve objectives for inflation are little altered.

The third alternative assumes that the ratio of stock market wealth to income holds steady at its third-quarter average, rather than falling over the projection period. This avoids the negative wealth effect that is weighing on consumption in the baseline forecast and provides a lower cost of equity capital for businesses. The resultant difference in the pace of activity is significant, amounting to about 1/2 percentage point more in 1999 and again in 2000. The unemployment rate is around 5 percent in 2000, and inflation is a bit higher than in the baseline.

(Two additional alternative scenarios that consider risks in the global economy are presented at the end of the *International Developments* section.)

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September 23, 1998

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]	
		08/13/98	09/23/98	08/13/98	09/23/98	08/13/98	09/23/98	08/13/98	09/23/98	08/13/98	09/23/98
ANNUAL											
1996		5.4	5.4	3.4	3.4	1.9	1.9	3.0	3.0	5.4	5.4
1997		5.9	5.9	3.9	3.9	1.9	1.9	2.3	2.3	4.9	4.9
1998		4.5	4.6	3.4	3.5	1.1	1.1	1.6	1.6	4.6	4.5
1999		3.2	3.0	1.7	1.6	1.4	1.4	2.1	2.1	4.9	4.9
2000			3.4		1.9		1.5		2.0		5.4
QUARTERLY											
1997	Q1	7.2	7.2	4.2	4.2	2.8	2.8	2.0	2.0	5.3	5.3
	Q2	5.6	5.6	4.0	4.0	1.7	1.7	1.5	1.5	4.9	4.9
	Q3	5.4	5.4	4.2	4.2	1.2	1.2	1.8	1.8	4.9	4.9
	Q4	4.2	4.2	3.0	3.0	1.1	1.1	2.3	2.3	4.7	4.7
1998	Q1	6.4	6.4	5.5	5.5	0.9	0.9	0.5	0.5	4.7	4.7
	Q2	2.2	2.7	1.3	1.9	0.9	0.8	2.0	2.0	4.4	4.4
	Q3	3.6	4.2	2.2	2.6	1.4	1.5	1.7	1.9	4.5	4.5
	Q4	3.9	3.6	2.5	2.6	1.4	1.0	2.0	1.9	4.6	4.5
1999	Q1	3.0	2.7	1.2	0.9	1.7	1.8	2.4	2.4	4.7	4.7
	Q2	2.8	2.3	1.4	0.9	1.4	1.4	2.1	2.1	4.9	4.8
	Q3	3.2	2.8	1.8	1.4	1.4	1.4	2.0	2.0	5.0	5.0
	Q4	3.6	3.3	2.2	1.9	1.4	1.4	2.0	2.0	5.1	5.2
2000	Q1		2.9		1.3		1.6		2.0		5.3
	Q2		4.3		2.9		1.4		2.0		5.4
	Q3		4.1		2.7		1.4		2.0		5.4
	Q4		4.2		2.7		1.5		2.0		5.4
TWO-QUARTER[3]											
1997	Q2	6.4	6.4	4.1	4.1	2.2	2.2	1.8	1.8	-0.4	-0.4
	Q4	4.8	4.8	3.6	3.6	1.2	1.2	2.0	2.0	-0.2	-0.2
1998	Q2	4.3	4.5	3.4	3.7	0.9	0.8	1.2	1.2	-0.3	-0.3
	Q4	3.8	3.9	2.3	2.6	1.4	1.3	1.9	1.9	0.3	0.1
1999	Q2	2.9	2.5	1.3	0.9	1.6	1.6	2.2	2.2	0.3	0.3
	Q4	3.4	3.0	2.0	1.6	1.4	1.4	2.0	2.0	0.3	0.3
2000	Q2		3.6		2.1		1.5		2.0		0.2
	Q4		4.2		2.7		1.4		2.0		0.1
FOUR-QUARTER[4]											
1996	Q4	5.8	5.8	3.9	3.9	1.8	1.8	3.2	3.2	-0.3	-0.3
1997	Q4	5.6	5.6	3.8	3.8	1.7	1.7	1.9	1.9	-0.6	-0.6
1998	Q4	4.0	4.2	2.9	3.2	1.1	1.0	1.5	1.6	-0.1	-0.2
1999	Q4	3.1	2.8	1.7	1.3	1.5	1.5	2.1	2.1	0.5	0.6
2000	Q4		3.9		2.4		1.5		2.0		0.3

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)

September 23, 1998

Item	Units[1]	1992	1993	1994	1995	1996	1997	- - - Projected 1998	1999	2000 - - -
EXPENDITURES										
Nominal GDP	Bill. $	6244.4	6558.1	6947.0	7269.6	7661.6	8110.9	8488.1	8743.6	9043.2
Real GDP	Bill. Ch. $	6244.4	6389.6	6610.7	6761.7	6994.8	7269.8	7527.5	7648.7	7797.4
Real GDP	% change	3.6	2.4	3.3	2.1	3.9	3.8	3.2	1.3	2.4
Gross domestic purchases		4.0	3.0	3.6	1.6	4.2	4.4	4.8	1.9	2.7
Final sales		3.9	2.1	2.7	2.7	3.7	3.4	3.5	1.4	2.2
Priv. dom. final purchases		4.9	3.7	3.7	2.9	4.4	4.5	6.0	2.2	2.7
Personal cons. expenditures		4.2	2.7	3.1	2.6	3.3	3.7	4.7	2.4	2.4
Durables		9.4	7.4	6.3	4.5	5.8	7.4	7.5	3.2	4.5
Nondurables		3.4	1.6	3.0	1.7	2.8	2.0	4.6	1.7	1.8
Services		3.6	2.3	2.5	2.6	3.0	3.8	4.2	2.5	2.3
Business fixed investment		5.5	9.9	7.6	7.3	11.7	9.8	12.1	3.6	5.4
Producers' dur. equipment		9.6	12.2	10.2	9.1	11.8	12.7	17.6	5.1	7.3
Nonres. structures		-3.4	4.5	1.1	2.7	11.6	2.5	-1.8	-0.3	0.0
Residential structures		16.9	7.8	4.2	-1.4	5.4	4.2	11.7	-3.8	1.4
Exports		4.1	4.6	10.0	10.5	10.3	9.6	-3.8	1.3	4.7
Imports		7.4	10.2	12.3	5.6	11.8	14.0	9.5	6.1	6.6
Gov't. cons. & investment		1.7	-1.4	0.1	-0.9	2.1	1.4	1.3	1.2	1.5
Federal		1.3	-6.1	-3.9	-5.6	1.1	-0.6	-1.1	-1.7	-0.8
Defense		-1.3	-6.9	-6.0	-5.0	-0.1	-1.4	-3.5	-2.1	-0.7
State & local		2.0	2.0	2.7	2.1	2.8	2.6	2.6	2.7	2.6
Change in bus. inventories	Bill. Ch. $	7.0	22.1	60.6	27.7	30.0	63.2	54.1	24.8	33.2
Nonfarm		2.0	29.5	49.0	37.7	23.2	58.8	46.2	19.8	30.5
Net exports		-29.5	-70.2	-104.6	-96.5	-111.2	-136.1	-250.9	-341.2	-386.0
Nominal GDP	% change	6.3	5.0	5.8	4.2	5.8	5.6	4.2	2.8	3.9
EMPLOYMENT AND PRODUCTION										
Nonfarm payroll employment	Millions	108.6	110.7	114.1	117.2	119.6	122.7	125.8	127.3	128.4
Unemployment rate	%	7.5	6.9	6.1	5.6	5.4	4.9	4.5	4.9	5.4
Industrial prod. index	% change	3.7	3.3	6.5	3.3	4.2	5.8	1.9	0.4	2.8
Capacity util. rate - mfg.	%	79.4	80.5	82.5	82.8	81.4	81.7	80.5	78.6	78.7
Housing starts	Millions	1.20	1.29	1.46	1.35	1.48	1.47	1.59	1.48	1.50
Light motor vehicle sales		12.85	13.86	15.01	14.72	15.05	15.03	15.13	14.55	14.41
North Amer. produced		10.51	11.71	12.88	12.82	13.35	13.11	13.14	12.66	12.58
Other		2.34	2.15	2.13	1.90	1.70	1.92	1.99	1.89	1.83
INCOME AND SAVING										
Nominal GNP	Bill. $	6255.5	6576.8	6955.2	7287.1	7674.0	8102.9	8465.2	8704.1	8993.1
Nominal GNP	% change	6.2	5.1	5.7	4.4	5.6	5.2	4.1	2.6	3.8
Nominal personal income		7.2	4.0	5.2	4.6	5.9	5.4	4.9	3.1	3.7
Real disposable income		4.0	1.2	2.5	2.1	2.7	2.9	3.3	2.2	2.3
Personal saving rate	%	5.7	4.4	3.5	3.4	2.9	2.1	0.7	0.5	0.5
Corp. profits, IVA & CCAdj.	% change	11.3	19.0	14.1	14.6	7.7	7.7	-1.7	-5.5	4.0
Profit share of GNP	%	6.8	7.5	8.2	9.2	9.8	10.1	9.7	8.9	8.6
Excluding FR Banks		6.6	7.2	7.9	8.9	9.5	9.8	9.4	8.6	8.3
Federal surpl./deficit	Bill. $	-280.9	-250.7	-186.7	-174.4	-110.3	-21.1	71.3	45.7	50.0
State & local surpl./def.		86.3	87.4	96.8	111.7	122.6	134.1	143.7	149.0	145.9
Ex. social ins. funds		18.3	19.7	27.9	37.0	52.2	66.0	76.1	81.3	78.2
Gross natl. saving rate	%	14.5	14.4	15.5	16.3	16.6	17.4	17.3	16.3	16.0
Net natl. saving rate		3.7	3.7	4.7	5.8	6.3	7.3	7.3	6.2	5.9
PRICES AND COSTS										
GDP chn.-wt. price index	% change	2.6	2.6	2.5	2.1	1.8	1.7	1.0	1.5	1.5
Gross Domestic Purchases chn.-wt. price index		2.7	2.3	2.5	2.0	1.8	1.3	0.5	1.4	1.4
CPI		3.1	2.7	2.7	2.6	3.2	1.9	1.6	2.1	2.0
Ex. food and energy		3.5	3.1	2.8	3.1	2.6	2.2	2.3	2.1	2.1
ECI, hourly compensation[2]		3.5	3.6	3.1	2.6	3.1	3.4	3.4	3.2	2.9
Nonfarm business sector										
Output per hour		3.5	-0.4	0.1	1.2	2.1	1.7	1.5	1.0	2.0
Compensation per Hour		4.5	1.6	2.1	2.8	3.7	3.9	4.0	3.2	2.9
Unit labor cost		1.0	2.0	2.0	1.6	1.6	2.1	2.5	2.2	0.9

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

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

September 23, 1998

Item	Units	1996 Q1	1996 Q2	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2
EXPENDITURES											
Nominal GDP	Bill. $	7495.3	7629.2	7703.4	7818.4	7955.0	8063.4	8170.8	8254.5	8384.2	8439.6
Real GDP	Bill. Ch. $	6882.0	6983.9	7020.0	7093.1	7166.7	7236.5	7311.2	7364.6	7464.7	7499.6
Real GDP	% change	3.3	6.1	2.1	4.2	4.2	4.0	4.2	3.0	5.5	1.9
Gross domestic purchases		4.5	7.0	3.4	1.8	5.5	4.4	4.6	3.2	7.8	4.0
Final sales		3.6	5.4	0.9	5.1	2.9	2.7	5.8	2.1	4.3	4.5
Priv. dom. final purchases		5.1	6.1	3.1	3.3	4.6	3.3	7.2	2.9	8.5	7.4
Personal cons. expenditures		3.7	4.7	1.8	2.9	4.3	1.6	6.2	2.8	6.1	5.9
Durables		5.8	12.7	-1.9	7.2	12.3	-1.5	16.8	3.1	15.8	11.2
Nondurables		2.2	4.8	1.2	2.9	3.6	-0.2	5.1	-0.4	7.4	5.2
Services		4.0	3.0	3.0	2.0	3.1	3.2	4.7	4.3	3.5	5.2
Business fixed investment		13.1	11.0	14.2	8.8	7.0	14.0	17.0	1.8	22.2	12.7
Producers' dur. equipment		15.7	12.3	16.2	3.2	8.3	22.8	18.8	2.2	34.3	18.2
Nonres. structures		6.4	7.4	8.9	24.5	3.9	-6.2	12.4	0.9	-4.9	-1.1
Residential structures		9.3	19.5	-1.7	-3.9	3.1	6.1	-0.4	8.2	15.6	15.5
Exports		3.7	5.8	2.1	32.0	8.3	15.5	10.6	4.4	-2.8	-7.6
Imports		13.1	13.5	13.6	7.0	18.6	17.9	13.5	6.3	15.7	9.2
Gov't. cons. & investment		3.2	7.1	-1.6	0.0	2.1	2.1	1.4	0.1	-1.9	3.6
Federal		8.0	8.1	-4.7	-6.3	-2.7	3.6	-1.2	-2.1	-8.8	6.7
Defense		7.2	8.1	-6.3	-8.3	-9.9	9.1	-1.8	-2.0	-18.5	9.5
State & local		0.5	6.5	0.3	3.8	4.9	1.3	2.9	1.3	2.1	2.1
Change in bus. inventories	Bill. Ch. $	14.4	26.1	47.5	32.1	56.3	79.0	51.0	66.5	91.4	39.8
Nonfarm		10.4	15.2	38.6	28.7	56.2	72.1	44.0	62.7	85.9	31.3
Net exports		-95.5	-113.5	-140.1	-95.9	-121.5	-131.6	-142.4	-149.0	-198.5	-244.4
Nominal GDP	% change	5.7	7.3	3.9	6.1	7.2	5.6	5.4	4.2	6.4	2.7
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	118.5	119.3	120.0	120.7	121.5	122.3	123.0	123.9	124.8	125.5
Unemployment rate	%	5.6	5.4	5.3	5.3	5.3	4.9	4.9	4.7	4.7	4.4
Industrial prod. index	% change	2.0	7.5	3.6	3.8	5.2	4.6	6.0	7.2	1.2	1.7
Capacity util. rate - mfg.	%	81.0	81.6	81.5	81.4	81.6	81.5	81.6	82.2	81.6	80.8
Housing starts	Millions	1.47	1.49	1.49	1.42	1.47	1.46	1.45	1.53	1.58	1.57
Light motor vehicle sales		15.10	15.18	15.00	14.91	15.32	14.54	15.19	15.07	15.02	16.08
North Amer. produced		13.44	13.46	13.33	13.16	13.41	12.68	13.20	13.13	13.07	14.09
Other		1.66	1.72	1.68	1.76	1.92	1.86	1.99	1.94	1.95	1.99
INCOME AND SAVING											
Nominal GNP	Bill. $	7515.0	7643.3	7708.6	7829.0	7952.4	8062.3	8162.0	8234.9	8369.4	8421.0
Nominal GNP	% change	5.6	7.0	3.5	6.4	6.5	5.6	5.0	3.6	6.7	2.5
Nominal personal income		6.6	6.9	5.5	4.6	7.3	4.7	4.7	5.0	5.9	4.5
Real disposable income		2.9	2.1	4.4	1.3	3.3	2.9	2.4	2.9	4.0	2.9
Personal saving rate	%	3.2	2.6	3.1	2.6	2.4	2.6	1.7	1.7	1.2	0.5
Corp. profits, IVA & CCAdj.	% change	16.9	6.9	3.8	3.5	18.1	11.1	13.1	-9.2	4.2	-3.5
Profit share of GNP	%	9.8	9.8	9.8	9.7	10.0	10.1	10.3	10.0	9.9	9.8
Excluding FR Banks		9.5	9.5	9.5	9.5	9.7	9.8	10.0	9.7	9.6	9.5
Federal surpl./deficit	Bill. $	-150.1	-112.6	-100.1	-78.3	-51.2	-34.8	-0.3	2.2	58.8	73.3
State & local surpl./def.		117.3	129.1	122.3	121.7	128.4	130.1	136.6	141.4	140.2	135.0
Ex. social ins. funds		45.3	58.2	52.5	52.9	59.8	61.6	68.7	73.8	72.7	67.3
Gross natl. saving rate	%	16.4	16.4	16.8	16.7	17.0	17.6	17.5	17.3	17.7	17.2
Net natl. saving rate		6.0	6.2	6.6	6.5	7.0	7.6	7.5	7.3	7.8	7.2
PRICES AND COSTS											
GDP chn.-wt. price index	% change	2.2	1.4	1.8	1.6	2.8	1.7	1.2	1.1	0.9	0.8
Gross Domestic Purchases chn.-wt. price index		2.1	1.4	1.5	2.1	2.2	0.9	1.1	1.0	-0.2	0.4
CPI		3.2	3.7	2.6	3.3	2.0	1.5	1.8	2.3	0.5	2.0
Ex. food and energy		2.5	2.5	2.7	2.7	2.2	2.6	1.9	2.1	2.4	2.7
ECI, hourly compensation[1]		2.5	3.5	2.8	2.8	2.5	3.7	3.4	4.3	2.7	3.6
Nonfarm business sector											
Output per hour		4.1	3.0	0.0	1.2	0.5	1.8	3.6	0.9	3.5	0.6
Compensation per hour		2.6	5.2	3.7	3.3	4.0	2.6	3.9	4.9	4.6	4.0
Unit labor cost		-1.5	2.2	3.7	2.1	3.6	0.7	0.3	4.0	1.1	3.4

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)

September 23, 1998

Item	Units	Projected 1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2	2000 Q3	2000 Q4
EXPENDITURES											
Nominal GDP	Bill. $	8526.0	8602.3	8659.1	8708.2	8768.2	8839.0	8903.3	8997.6	9089.5	9182.5
Real GDP	Bill. Ch. $	7548.4	7597.2	7614.1	7630.6	7657.1	7693.0	7717.7	7772.7	7823.9	7875.5
Real GDP	% change	2.6	2.6	0.9	0.9	1.4	1.9	1.3	2.9	2.7	2.7
Gross domestic purchases		3.5	3.9	1.8	1.6	1.9	2.2	1.6	3.3	3.1	2.8
Final sales		2.3	3.0	1.3	1.2	1.5	1.7	1.4	2.3	2.3	2.7
Priv. dom. final purchases		3.4	4.9	2.7	2.0	2.1	2.2	2.0	3.0	3.0	2.9
Personal cons. expenditures		3.5	3.4	2.7	2.4	2.2	2.2	1.8	2.8	2.5	2.5
Durables		-3.7	7.7	3.6	3.3	2.7	3.2	3.2	5.5	4.6	4.8
Nondurables		3.6	2.2	1.8	1.7	1.8	1.7	1.7	1.7	1.9	1.9
Services		5.0	3.1	3.0	2.6	2.4	2.3	1.6	2.8	2.3	2.3
Business fixed investment		0.3	14.2	5.1	3.4	3.4	2.7	3.7	5.1	6.7	6.1
Producers' dur. equipment		0.8	19.7	7.3	4.7	4.6	3.7	5.3	6.9	9.0	8.2
Nonres. structures		-1.2	-0.1	-0.9	-0.1	-0.1	-0.1	-0.7	-0.0	0.4	0.4
Residential structures		10.9	5.3	-3.9	-8.2	-3.1	0.1	1.2	1.3	1.6	1.6
Exports		-1.7	-2.8	-0.8	0.9	2.3	2.9	3.8	4.6	5.0	5.3
Imports		5.5	7.7	6.8	6.9	5.9	4.7	5.5	7.6	7.6	5.6
Gov't. cons. & investment		2.1	1.5	0.2	1.9	1.6	1.1	0.2	1.7	1.4	2.6
Federal		-0.2	-1.7	-4.6	0.3	-0.7	-1.9	-4.4	-0.1	-1.0	2.4
Defense		-0.7	-2.0	-6.5	0.5	-1.0	-1.5	-6.3	0.4	-1.1	4.3
State & local		3.2	3.3	2.8	2.7	2.7	2.7	2.6	2.6	2.6	2.6
Change in bus. inventories	Bill. Ch. $	46.5	38.6	30.4	23.7	20.9	24.0	21.2	32.4	40.1	38.9
Nonfarm		37.5	29.9	23.1	18.1	16.7	21.1	18.5	29.7	37.4	36.3
Net exports		-265.1	-295.3	-318.0	-337.2	-350.5	-358.9	-367.7	-381.4	-394.5	-400.6
Nominal GDP	% change	4.2	3.6	2.7	2.3	2.8	3.3	2.9	4.3	4.1	4.2
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	126.1	126.7	126.9	127.2	127.4	127.6	127.9	128.5	128.5	128.8
Unemployment rate	%	4.5	4.5	4.7	4.8	5.0	5.2	5.3	5.4	5.4	5.4
Industrial prod. index	% change	1.0	3.6	-0.6	-0.7	0.8	2.3	1.0	3.5	3.4	3.2
Capacity util. rate - mfg.	%	79.9	79.8	79.1	78.6	78.3	78.4	78.2	78.6	78.9	79.1
Housing starts	Millions	1.63	1.57	1.50	1.46	1.47	1.48	1.50	1.50	1.50	1.50
Light motor vehicle sales		14.37	15.04	14.76	14.63	14.45	14.34	14.20	14.41	14.46	14.55
North Amer. produced		12.34	13.07	12.85	12.72	12.57	12.50	12.41	12.58	12.61	12.70
Other		2.04	1.97	1.91	1.91	1.88	1.84	1.79	1.83	1.85	1.85
INCOME AND SAVING											
Nominal GNP	Bill. $	8497.6	8573.0	8625.8	8671.2	8726.2	8793.4	8857.1	8949.3	9037.1	9128.7
Nominal GNP	% change	3.7	3.6	2.5	2.1	2.6	3.1	2.9	4.2	4.0	4.1
Nominal personal income		5.1	4.1	2.7	3.0	3.4	3.2	4.5	3.4	3.5	3.5
Real disposable income		3.7	2.5	4.1	1.3	1.7	1.5	4.2	1.6	1.7	1.7
Personal saving rate	%	0.6	0.4	0.8	0.5	0.4	0.2	0.8	0.5	0.4	0.2
Corp. profits, IVA & CCAdj.	% change	-5.6	-1.6	-7.8	-7.7	-5.2	-1.0	-9.8	10.6	8.1	8.5
Profit share of GNP	%	9.5	9.4	9.2	8.9	8.8	8.7	8.4	8.5	8.6	8.7
Excluding FR Banks		9.3	9.2	8.9	8.7	8.5	8.4	8.1	8.3	8.4	8.4
Federal surpl./deficit	Bill. $	80.5	72.5	44.6	44.7	48.1	45.4	36.3	48.2	59.0	56.7
State & local surpl./def.		146.5	153.2	152.6	149.5	146.3	147.7	145.2	145.9	146.0	146.5
Ex. social ins. funds		78.9	85.5	84.9	81.8	78.6	80.0	77.5	78.2	78.3	78.8
Gross natl. saving rate	%	17.3	17.0	16.7	16.4	16.2	15.9	16.0	16.0	16.0	15.9
Net natl. saving rate		7.3	7.0	6.7	6.3	6.0	5.8	5.8	5.9	5.9	5.8
PRICES AND COSTS											
GDP chn.-wt. price index	% change	1.5	1.0	1.8	1.4	1.4	1.4	1.6	1.4	1.4	1.5
Gross Domestic Purchases chn.-wt. price index		0.8	1.0	1.6	1.3	1.2	1.3	1.6	1.4	1.4	1.4
CPI		1.9	1.9	2.4	2.1	2.0	2.0	2.0	2.0	2.0	2.0
Ex. food and energy		2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
ECI, hourly compensation[1]		3.7	3.7	3.2	3.2	3.1	3.1	2.9	2.9	2.9	2.9
Nonfarm business sector											
Output per hour		0.8	1.4	1.0	0.8	0.9	1.5	1.1	2.7	2.2	2.0
Compensation per hour		3.8	3.7	3.6	3.2	3.1	3.1	3.3	2.8	2.8	2.8
Unit labor cost		3.0	2.3	2.6	2.4	2.2	1.6	2.2	0.1	0.6	0.8

1. Private-industry workers.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3	96Q4/ 95Q4	97Q4/ 96Q4	98Q4/ 97Q4
Real GDP	2.1	4.2	4.2	4.0	4.2	3.0	5.5	1.9	2.6	3.9	3.8	3.2
Gross dom. purchases	3.5	1.9	5.5	4.4	4.7	3.2	7.9	4.1	3.6	4.2	4.4	4.8
Final sales	0.9	5.1	2.9	2.7	5.7	2.1	4.3	4.5	2.3	3.7	3.3	3.5
Priv. dom. final purchases	2.5	2.7	3.8	2.7	5.9	2.4	7.0	6.1	2.9	3.6	3.7	5.0
Personal cons. expenditures	1.3	2.0	2.9	1.1	4.2	1.9	4.1	4.0	2.4	2.2	2.5	3.2
Durables	-0.2	0.6	1.0	-0.1	1.3	0.3	1.2	0.9	-0.3	0.5	0.6	0.6
Nondurables	0.2	0.6	0.7	0.0	1.0	-0.1	1.4	1.0	0.7	0.6	0.4	0.9
Services	1.2	0.8	1.2	1.3	1.9	1.7	1.4	2.0	2.0	1.2	1.5	1.7
Business fixed investment	1.4	0.9	0.7	1.4	1.7	0.2	2.2	1.3	0.0	1.2	1.0	1.3
Producers' dur. equip.	1.1	0.2	0.6	1.6	1.3	0.1	2.4	1.4	0.1	0.8	0.9	1.3
Nonres. structures	0.2	0.6	0.1	-0.2	0.4	0.0	-0.2	-0.0	-0.0	0.3	0.1	-0.1
Residential structures	-0.1	-0.2	0.1	0.2	0.0	0.3	0.6	0.6	0.5	0.2	0.2	0.5
Net exports	-1.3	2.4	-1.2	-0.5	-0.5	-0.3	-2.2	-2.1	-0.9	-0.3	-0.6	-1.7
Exports	0.2	3.2	1.0	1.8	1.2	0.5	-0.3	-0.9	-0.2	1.2	1.1	-0.4
Imports	-1.6	-0.9	-2.2	-2.2	-1.7	-0.8	-1.9	-1.2	-0.7	-1.4	-1.7	-1.2
Government cons. & invest.	-0.3	0.0	0.4	0.4	0.3	0.0	-0.3	0.6	0.4	0.4	0.3	0.2
Federal	-0.3	-0.4	-0.2	0.2	-0.1	-0.1	-0.6	0.4	-0.0	0.1	-0.0	-0.1
Defense	-0.3	-0.4	-0.5	0.4	-0.1	-0.1	-0.8	0.4	-0.0	-0.0	-0.1	-0.1
Nondefense	0.0	0.0	0.3	-0.2	0.0	-0.1	0.3	0.0	0.0	0.1	0.0	0.1
State and local	0.0	0.4	0.6	0.2	0.3	0.2	0.2	0.2	0.4	0.3	0.3	0.3
Change in bus. inventories	1.2	-0.8	1.3	1.3	-1.4	0.9	1.2	-2.5	0.3	0.2	0.5	-0.4
Nonfarm	1.3	-0.5	1.5	0.9	-1.5	1.0	1.2	-2.7	0.3	0.1	0.5	-0.4
Farm	-0.1	-0.3	-0.2	0.4	0.1	-0.1	0.0	0.2	0.0	0.0	0.0	0.1

Note. Components may not sum to totals because of rounding.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

September 23, 1998

Item	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2	2000 Q3	2000 Q4	98Q4/ 97Q4	99Q4/ 98Q4	0Q4/ 99Q4
Real GDP	2.6	0.9	0.9	1.4	1.9	1.3	2.9	2.7	2.7	3.2	1.3	2.4
Gross dom. purchases	3.9	1.9	1.7	1.9	2.2	1.6	3.4	3.1	2.9	4.8	1.9	2.7
Final sales	3.0	1.3	1.2	1.5	1.7	1.4	2.3	2.3	2.7	3.5	1.4	2.2
Priv. dom. final purchases	4.1	2.2	1.7	1.8	1.9	1.7	2.5	2.5	2.5	5.0	1.9	2.3
Personal cons. expenditures	2.3	1.8	1.7	1.5	1.6	1.2	1.9	1.7	1.7	3.2	1.6	1.7
Durables	0.6	0.3	0.3	0.2	0.3	0.3	0.4	0.4	0.4	0.6	0.3	0.4
Nondurables	0.4	0.3	0.3	0.4	0.3	0.3	0.3	0.4	0.4	0.9	0.3	0.4
Services	1.3	1.2	1.0	1.0	0.9	0.6	1.1	1.0	1.0	1.7	1.0	0.9
Business fixed investment	1.5	0.6	0.4	0.4	0.3	0.4	0.6	0.7	0.7	1.3	0.4	0.6
Producers' dur. equip.	1.5	0.6	0.4	0.4	0.3	0.4	0.6	0.7	0.7	1.3	0.4	0.6
Nonres. structures	-0.0	-0.0	-0.0	-0.0	-0.0	-0.0	-0.0	0.0	0.0	-0.1	-0.0	0.0
Residential structures	0.2	-0.2	-0.4	-0.1	0.0	0.1	0.1	0.1	0.1	0.5	-0.2	0.1
Net exports	-1.3	-1.0	-0.8	-0.5	-0.3	-0.3	-0.5	-0.5	-0.2	-1.7	-0.6	-0.4
Exports	-0.3	-0.1	0.1	0.2	0.3	0.4	0.5	0.5	0.6	-0.4	0.1	0.5
Imports	-1.0	-0.9	-0.9	-0.8	-0.6	-0.7	-1.0	-1.0	-0.8	-1.2	-0.8	-0.9
Government cons. & invest.	0.3	0.0	0.3	0.3	0.2	0.0	0.3	0.2	0.4	0.2	0.2	0.3
Federal	-0.1	-0.3	0.0	-0.0	-0.1	-0.3	-0.0	-0.1	0.1	-0.1	-0.1	-0.0
Defense	-0.1	-0.3	0.0	-0.0	-0.1	-0.2	0.0	-0.0	0.2	-0.1	-0.1	-0.0
Nondefense	-0.0	-0.0	0.0	0.0	-0.1	-0.0	-0.0	-0.0	-0.0	0.1	-0.0	-0.0
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	-0.4	-0.4	-0.3	-0.1	0.2	-0.1	0.5	0.4	-0.1	-0.4	-0.2	0.2
Nonfarm	-0.4	-0.3	-0.2	-0.1	0.2	-0.1	0.5	0.4	-0.1	-0.4	-0.1	0.2
Farm	0.0	-0.1	-0.1	-0.1	-0.1	-0.0	-0.0	-0.0	-0.0	0.1	-0.1	-0.0

Note. Components may not sum to totals because of rounding.

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

Item	Fiscal year[5]				1998				1999				2000			
	1997[a]	1998	1999	2000	Q1[a]	Q2[a]	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
UNIFIED BUDGET					Not seasonally adjusted											
Receipts[1]	1579	1721	1770	1806	378	544	412	411	388	541	431	412	407	549	438	419
Outlays[1]	1601	1653	1714	1754	409	407	411	472	397	421	425	443	448	432	431	453
Surplus/deficit[1]	-22	68	56	52	-30	137	1	-61	-8	120	6	-30	-41	117	7	-34
On-budget	-103	-37	-62	-74	-51	87	-7	-60	-62	66	-6	-65	-64	60	-5	-69
Off-budget	81	105	119	126	21	50	8	-1	54	53	12	35	23	56	11	34
Surplus excluding deposit insurance[2]	-36	63	52	48	-31	136	-1	-62	-9	119	5	-31	-42	116	6	-35
Means of financing																
Borrowing	38	-54	-36	-56	26	-82	-32	42	25	-105	2	20	31	-89	-17	19
Cash decrease	1	12	-8	0	4	-45	40	11	-4	-10	-5	10	10	-25	5	20
Other[3]	-17	-25	-12	4	0	-10	-9	8	-13	-5	-3	1	1	-3	6	-5
Cash operating balance, end of period	44	32	40	40	28	72	32	21	25	35	40	30	20	45	40	20
NIPA FEDERAL SECTOR					Seasonally adjusted annual rate											
Receipts	1687	1820	1869	1899	1809	1837	1870	1886	1854	1862	1873	1884	1883	1904	1924	1942
Expenditures	1728	1767	1816	1852	1750	1764	1789	1814	1809	1817	1825	1839	1847	1856	1865	1885
Consumption expend.	458	459	464	468	451	464	461	461	463	465	466	465	468	469	469	473
Defense	306	301	301	302	293	303	301	301	301	302	302	301	301	302	302	306
Nondefense	152	158	163	166	158	161	160	160	163	163	164	164	166	167	167	167
Other expenditures	1270	1308	1353	1384	1299	1300	1328	1353	1346	1352	1359	1374	1380	1387	1396	1412
Current account surplus	-41	54	52	47	59	73	80	72	45	45	48	45	36	48	59	57
Gross investment	61	59	59	57	61	56	60	60	59	59	59	58	57	57	57	58
Current and capital account surplus	-102	-6	-6	-10	-2	17	20	13	-14	-14	-10	-13	-21	-9	2	-1
FISCAL INDICATORS[4]																
High-employment (HEB) surplus/deficit	-163	-103	-90	-55	-102	-87	-83	-91	-103	-90	-75	-68	-65	-50	-37	-39
Change in HEB, percent of potential GDP	-.8	-.8	-.2	-.4	-.5	-.2	0	.1	.1	-.1	-.2	-.1	0	-.2	-.2	0
Fiscal impetus (FI), percent, cal. year	-2.1	-1.8	.2	-2.3	-2.1	1	1.7	-1.5	1	-.2	-.5	-1.2	-1.1	0	-.2	.6

1. OMB's May 1998 surplus estimates (assuming the enactment of the President's proposals) are $39 billion in FY98 and $54 billion in FY99. CBO's August 1998 baseline surplus estimates are $63 billion in FY98 and $80 billion in FY99. 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 May 1998 surplus estimates (assuming the enactment of the President's proposals), excluding deposit insurance spending, are $35 billion in FY98 and $51 billion in FY99 and CBO's August baseline estimates are $59 billion in FY98 and $76 billion in FY99.
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 associated with an unemployment rate of 6 percent. Real potential GDP growth is assumed to be 2.8 percent beginning 1995:Q3. 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 year data for the unified budget come from OMB; quarterly data come from the Monthly Treasury Statement and may not sum to OMB fiscal year totals.

a--Actual.
b--Preliminary.

Strictly Confidential Class II FOMC
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Change in Debt of the Domestic Nonfinancial Sectors
(Percent)

Period [1]	Total [2]	Federal government [3]	Nonfederal						Memo:
				Households					
			Total [4]	Total	Home mortgages	Consumer credit	Business	State and local governments	Nominal GDP
Year									
1990	6.4	11.0	5.2	7.5	9.6	1.5	3.1	5.0	4.4
1991	4.3	11.1	2.3	4.7	6.4	-1.3	-1.7	8.6	3.8
1992	4.6	10.9	2.6	4.3	5.2	0.5	0.8	2.2	6.3
1993	5.0	8.3	3.8	5.3	4.3	7.6	1.6	6.0	5.0
1994	4.6	4.7	4.6	7.5	5.8	14.5	4.0	-4.0	5.8
1995	5.4	4.1	5.9	7.8	5.5	14.1	6.6	-4.6	4.2
1996	5.3	4.0	5.8	7.8	8.0	7.9	5.1	-0.6	5.8
1997	5.3	0.6	7.0	6.8	7.5	4.3	7.6	5.3	5.6
1998	5.6	-1.2	7.8	8.0	8.9	3.8	8.3	4.8	4.2
1999	3.6	-1.6	5.2	5.5	6.3	1.8	5.1	4.3	2.8
2000	3.4	-1.5	4.8	4.9	5.3	1.9	4.9	3.8	3.9
Quarter									
1997:3	5.6	0.8	7.3	6.9	9.1	4.1	7.8	6.7	5.4
4	6.4	1.1	8.2	7.3	8.2	3.0	9.1	8.4	4.2
1998:1	6.0	-0.8	8.3	7.9	8.6	4.1	8.8	8.4	6.4
2	6.1	-1.8	8.6	8.5	9.3	4.6	9.5	5.7	2.7
3	4.6	-3.9	7.3	7.5	8.7	3.1	8.1	2.5	4.2
4	5.1	1.8	6.1	7.0	8.0	3.4	6.0	2.5	3.6
1999:1	4.1	-1.3	5.7	6.2	7.1	2.3	5.3	4.6	2.7
2	3.3	-2.8	5.2	5.6	6.3	2.0	4.9	4.4	2.3
3	3.5	-1.2	4.9	5.0	5.7	1.5	4.9	4.1	2.8
4	3.4	-0.9	4.7	4.8	5.5	1.4	4.8	3.9	3.3

Note. Quarterly data are at seasonally adjusted annual rates.

1. Data after 1998:Q2 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.
2. On a monthly average basis, total debt is projected to grow 5.7 percent in 1998 and 3.8 percent in 1999.
3. On a monthly average basis, federal debt is projected to grow -1.2 percent in 1998 and -1.2 percent in 1999.
4. On a monthly average basis, nonfederal debt is projected to grow 8.1 percent in 1998 and 5.4 percent in 1999.

2.6.3 FOF

Flow of Funds Proj..ions: Highlights
(Billions of dollars except as noted)

Category	Calendar year				Seasonally adjusted annual rates									
					1997		1998				1999			
	1997	1998	1999	2000	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net funds raised by domestic nonfinancial sectors														
1 Total	653.7	601.5	518.4	546.3	705.6	810.8	781.1	805.8	534.1	284.9	563.2	467.3	514.1	529.0
2 Net equity issuance	-114.6	-242.8	-64.0	-14.0	-124.0	-144.1	-138.0	-129.2	-182.0	-522.0	-88.0	-72.0	-56.0	-40.0
3 Net debt issuance	768.4	844.3	582.4	560.3	829.6	954.9	919.1	935.0	716.1	806.9	651.2	539.3	570.1	569.0
Borrowing sectors														
Nonfinancial business														
4 Financing gap [1]	73.8	111.0	136.7	163.3	50.8	82.8	118.5	103.0	98.4	124.3	127.8	133.1	139.5	146.6
5 Net equity issuance	-114.6	-242.8	-64.0	-14.0	-124.0	-144.1	-138.0	-129.2	-182.0	-522.0	-88.0	-72.0	-56.0	-40.0
6 Credit market borrowing	337.6	398.2	262.6	264.6	358.4	425.7	420.2	463.0	404.8	304.6	275.1	257.1	260.7	257.7
Households														
7 Net borrowing [2]	351.6	437.8	327.5	305.4	368.3	396.2	435.9	476.7	431.2	407.7	371.4	336.5	306.1	296.3
8 Home mortgages	261.3	336.0	258.2	232.1	326.9	302.0	322.2	359.1	341.2	321.7	289.7	263.7	243.7	235.7
9 Consumer credit	52.5	48.7	23.7	25.9	50.3	37.8	51.7	58.6	40.1	44.2	30.6	26.9	19.3	18.1
10 Debt/DPI (percent) [3]	91.9	94.9	97.2	98.5	92.1	92.8	93.6	94.7	95.4	96.2	96.4	97.2	97.7	98.1
State and local governments														
11 Net borrowing	56.1	54.2	50.5	46.8	72.6	92.3	94.3	64.9	28.8	28.8	53.8	51.8	49.8	46.8
12 Current surplus [4]	135.6	181.8	185.0	186.9	117.6	171.5	179.1	175.1	182.9	190.1	190.2	177.6	185.0	187.1
Federal government														
13 Net borrowing	23.1	-45.9	-58.3	-56.5	30.3	40.8	-31.3	-69.6	-148.7	65.8	-49.0	-106.0	-46.4	-31.7
14 Net borrowing (quarterly, n.s.a.)	23.1	-45.9	-58.3	-56.5	10.6	33.7	25.6	-81.5	-31.8	41.8	25.0	-104.6	1.7	19.5
15 Unified deficit (quarterly, n.s.a.)	2.4	-46.6	-87.2	-47.7	10.9	39.7	30.2	-136.9	-0.9	61.1	8.3	-119.6	-6.1	30.2
Depository institutions														
16 Funds supplied	336.9	259.3	221.0	230.7	204.4	472.9	323.4	160.9	303.7	249.3	220.3	211.9	222.3	229.5
Memo (percentage of GDP)														
17 Domestic nonfinancial debt [5]	182.8	184.2	186.9	187.1	182.0	182.8	182.8	184.3	184.9	185.4	186.3	187.0	187.3	187.4
18 Domestic nonfinancial borrowing	9.5	9.9	6.7	6.2	10.2	11.6	11.0	11.1	8.4	9.4	7.5	6.2	6.5	6.4
19 Federal government [6]	0.3	-0.5	-0.7	-0.6	0.4	0.5	-0.4	-0.8	-1.7	0.8	-0.6	-1.2	-0.5	-0.4
20 Nonfederal	9.2	10.5	7.3	6.8	9.8	11.1	11.3	11.9	10.1	8.6	8.1	7.4	7.0	6.8

Note. Data after 1998:Q2 are staff projections.
1. For corporations: Excess of capital expenditures over U.S. internal funds.
2. Includes change in liabilities not shown in lines 8 and 9.
3. Average debt levels in the period (computed as the average of period-end debt positions) divided by disposable personal income.
4. NIPA surplus less changes in retirement fund assets plus consumption of fixed capital.
5. Average debt levels in the period (computed as the average of period-end debt positions) divided by nominal GDP.
6. Excludes government-insured mortgage pool securities.

2.6.4 FOF

International Developments

Developments in international financial markets during the intermeeting period have confirmed our concerns that the actions taken by Russia just before the August FOMC meeting, to let the ruble depreciate and effectively default on its government debt, could have widespread negative repercussions. The reaction on the part of investors has been a general withdrawal from risk. In Latin America in particular, yield spreads and domestic interest rates soared, while stock markets declined sharply, with falling currencies or heavy outflows of private capital, especially from Brazil, Venezuela, and Mexico. In Europe, Japan, and North America, as well, equity markets have dropped substantially while government bond prices have jumped and corporate bond spreads have widened. The turmoil in financial markets has led us to revise down substantially our outlook for GDP growth in Latin America--an outlook that was anemic to begin with by recent historical standards--and moderately elsewhere. Everything else being equal, the resultant slowing of U.S. export growth in 1999 would have subtracted more than ¼ percentage point from our previous projection for U.S. GDP growth over the year ahead. However, other factors, including a lower path of the dollar associated with an assumed cut in U.S. interest rates, have a partly offsetting positive effect on the external sector.

Recent Developments

International financial markets. Financial meltdown in Russia proceeded fairly quickly after the government's actions on August 17, once investors realized fully that further international financial assistance for Russia would not be forthcoming any time soon. The ruble plunged and has fluctuated in a wide range between 8 and 22 per dollar (relative to its starting value of 6.2 rubles per dollar), ending the period around 15 per dollar. Foreign investors in ruble-denominated government debt appear to be facing very large losses on their holdings, although in recent days there have been hints that the terms of the forced restructuring may be amended. After several weeks of political uncertainty, a government is beginning to emerge under Prime Minister Primakov. Early pronouncements by the new (and former) head of the central bank, Viktor Geraschenko, suggest that the new government will depend heavily on the printing press both to finance wage arrears and to run off its debt.

Brazil was particularly vulnerable to the latest round of contagion, given its very large budget and external deficits and short-term debt. By early September, Brady bond spreads for Brazil had soared above their levels seen during the Mexican crisis in 1995, and domestic short-term interest rates were pushed up to between 40 percent and 50

percent in Brazil, Mexico, and Venezuela and to 15 percent in Argentina. The Mexican peso fell as much as 13 percent, and Brazil ran its reserves down from $68 billion in mid-August to less than $50 billion at present to maintain the *real*'s crawling peg. Pressure on these financial markets has eased somewhat over the past week and a half as a result of (1) a sharp increase in domestic interest rates, (2) a growing view in the market that international financial support would be made available to Brazil and Argentina if needed, and (3) talk of a cut in U.S. interest rates.

The events in Latin America have been accompanied by significant developments in international financial markets among the industrial countries. Since the August FOMC meeting, the dollar has depreciated sharply against the yen (6½ percent), the mark and most other continental European currencies (6 percent), and the pound (4 percent). Factors weighing on the dollar include the perception that the U.S. economy is more vulnerable than either Europe or Japan to a downturn in Latin America, growing expectations of a U.S. monetary easing, and uncertainty about the prospects for the Clinton presidency.

The yen strengthened through most of the intermeeting period despite further bad news about the Japanese banking system and economy, a cut in the Bank of Japan's call money rate from a bit below 50 basis points to 25 basis points, and a 6½ percent drop in the stock market as the Nikkei fell to a 12-year low. The yen's strength is puzzling. Market participants cited ongoing withdrawal of Japanese investments from emerging markets into yen (and in time for the September 30 end of the fiscal mid-year), as well as growing concern about U.S. and Japanese trade imbalances as reasons for the yen's appreciation. After having been deadlocked for most of the period, parties negotiating Japanese bank reform legislation appeared to reach an agreement on September 18, but disputes over the details arose subsequently. Reflecting both a flight to quality and a gloomier outlook for economic activity, the long-term government bond yield fell 40 basis points, but corporate bond spreads and the premium on interbank borrowing rates of Japanese banks widened somewhat.

Stock markets in the major European countries have fallen substantially over the intermeeting period and have lost 20 to 25 percent on balance since their peaks in July. Government bond yields have declined 25 to 55 basis points since mid-August and have moved below 4 percent in Germany for the first time in recent decades.

The dollar is little changed on balance against the Canadian dollar, which continued its recent downtrend early in the period but recovered after the Bank of Canada hiked its bank rate 100 basis points on August 27 in response to the currency's slide.

Canadian stock and bond markets have moved much the same as those in Europe and the United States over the period.

Financial markets in Asia, already having undergone a major downturn, were less affected by the developments in Russia and Latin America. Two actions worthy of note were massive intervention in the Hong Kong stock market by the Hong Kong Monetary Authority and the imposition of exchange controls in Malaysia. The HKMA spent an estimated $12½ billion in the stock market, which ended the period up 4 percent. With the imposition of exchange controls in Malaysia in early September, the currency was set at a 10 percent higher level than had prevailed in recent months. Malaysian interest rates have declined, and the stock market has risen on balance since the controls were imposed and banking supervision and regulation were relaxed.

On a trade-weighted average basis in terms of the major currencies, the dollar has declined about 4 percent since the August FOMC meeting. Against a broad weighted average the dollar is down only 2 percent, however, reflecting in large part the dollar's rise against the Mexican peso.

. The Desk did not intervene.

Economic activity abroad. The growth of total foreign real GDP (weighted by shares of U.S. nonagricultural exports) appears to have remained near zero in the second quarter, and early indications for the third quarter point to continued sluggishness. Japan's GDP showed another substantial decline, though the rate of descent slowed somewhat in the second quarter because of a steep drop in imports. Domestic demand fell at an annual rate of 6.2 percent in the second quarter, somewhat more than in the first quarter. A drop in industrial production and big declines in housing starts and machinery orders in July point to negative GDP growth for Japan again in the third quarter.

Real growth in Europe slowed in the second quarter as German GDP growth fell to only 0.4 percent (SAAR) because of the impact of a VAT increase and unusual weather. Recent indicators point to some rebound in the third quarter. Elsewhere in Europe, early indications are generally for some slowing of growth in the third quarter. Canadian growth should recover somewhat from a strike-depressed second quarter. Industrial countries showed a substantial slowing in growth of real exports during the first half of 1998 compared with 1997, and Japanese and U.K. exports recorded significantly negative growth rates. Twelve-month CPI inflation dipped to zero in Japan in July and August, was running in the neighborhood of ¾ to 1½ percent in continental Europe and Canada and slowed to the official target of 2½ percent in the United Kingdom in August.

Real output continued to spiral downward in Korea, Indonesia, Malaysia, and Thailand in the second quarter, although GDP in Korea and Malaysia appears to have declined more slowly than in the first quarter. The decline in the Philippines steepened from a moderate rate in the first quarter, and growth in Singapore turned negative. The countries for which data on industrial production are available through July or August (Korea, Malaysia, and Singapore) show continued weakness. Hong Kong recorded a sharp drop in real GDP in the first quarter; China and Taiwan showed slowing positive growth through the second quarter. The growth of China's industrial production held up at an annual rate of nearly 8 percent through August (12-month change), while Taiwan's continued at around 4 percent. The combined trade balance of Korea, Malaysia, Philippines, and Thailand was up $108 billion in the second quarter from a year earlier. We estimate that $25 billion of the adjustment has been in trade with the United States, primarily as a reduction in U.S. nominal exports.[1]

Output growth in Mexico and Argentina has slowed in recent months from last year's robust pace. In Mexico declining oil prices have forced some fiscal belt-tightening, and monetary conditions were tightened in response to increasing financial market turmoil earlier this year. Growth in Brazil is estimated to have picked up in the second quarter after its first-quarter plunge but appears to have turned negative again in the third quarter. While most of the Asian emerging market economies have moved significantly into external surplus this year, the major Latin American countries were still running relatively large current account deficits during the second quarter and into the third quarter. Twelve-month consumer price inflation remained high in Mexico through August (15 percent) but has declined in Brazil (to 4 percent) and remains around 1 percent in Argentina.

U.S. net exports and prices. The U.S. nominal trade deficit in goods and services narrowed slightly in July from the $174 billion (annual rate) deficit recorded in the second quarter. Both imports and exports declined, reflecting in part the effects of the GM strike on automotive trade with Canada and Mexico. The current account deficit widened to $226 billion, or 2.9 percent of GDP, in the second quarter.

U.S. export prices declined 3.1 percent at an annual rate in July-August relative to the second quarter, with declines concentrated in agricultural commodities, industrial materials, and computers. The price of non-oil imports fell 4.1 percent at an annual rate in July-August following similar declines in the first two quarters. These declines were

1. Given sharp declines in the prices of U.S. imports from key Asian countries, it appears that these imports have been rising significantly in real terms.

widespread across commodity categories, particularly industrial supplies, computers and semiconductors. Prices of imports from key Asian economies (whose exports are heavily weighted towards computers and semiconductors) declined while those from Europe and Canada were little changed.[2] The average price of imported oil dropped further in July-August. Unexpectedly large shipments from Iraq, market disappointment over the pace of production cutbacks from other OPEC producers, and weak oil demand -- especially in Asia -- all contributed to the decline in prices below $13.00 (WTI) in mid-August. Spot prices have rebounded since then largely because OPEC has intensified efforts to restrain production and because Iraq has announced that it will not be able to maintain its August export rates through the remainder of the year. Spot WTI is currently trading near $15.50 per barrel.

Outlook

The staff projects that foreign GDP (weighted by U.S. nonagricultural export shares), which declined slightly during the first half of this year, will decline further in the second half. Over the next two years, we see growth resuming with a gradual pickup to about 2½ percent by 2000, still well below the average rate during 1992-96. The projected growth performance for 1998-99 is easily the slowest two-year growth in the past three decades. Relative to the August forecast, we have subtracted about 1 percentage point from the growth of foreign GDP through the end of 1999 because of deep cuts in Latin American growth and smaller downward revisions elsewhere. We also see the risks surrounding this forecast as having widened further, and we outline those risks in more detail at the end of this outlook section.

We project the dollar to decline moderately in real terms against a broad set of currencies. This outlook is little changed from that in the August forecast as downward revisions in the path for the dollar in terms of major currencies is offset by upward revisions in terms of Latin American currencies. We now see real net exports subtracting about 1 percentage point from U.S. real GDP growth in the second half of 1998 and about ½ percentage point in1999 and 2000 somewhat more than in the August forecast. The lower foreign GDP growth reduces our projection for U.S. export growth enough to subtract 0.2 percentage point from U.S. GDP growth over the year ahead. In addition, U.S. import growth has been weakened slightly in light of the lower trajectory for U.S. GDP growth.

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2. The Asian economies covered by these data include Hong Kong, Korea, Singapore, and Taiwan.

Summary of Staff Projections
(Percentage change from end of previous period)

Measure	1997	Projection				
		1998			1999	2000
		H1	Q3	Q4		
Foreign output	4.0	.2	-.4	-.1	1.4	2.5
August	*3.9*	*-0.1*	*.5*	*1.1*	*2.1*	
Real exports	9.6	-5.2	-1.7	-2.8	1.3	4.7
August	*9.6*	*-5.8*	*-2.3*	*-.5*	*3.0*	
Real imports	14.0	12.4	5.5	7.7	6.1	6.6
August	*14.0*	*13.9*	*6.9*	*8.2*	*6.5*	

The dollar. We project that the trade-weighted exchange value of the dollar against the major foreign currencies will remain near its current level in coming weeks as market expectations are met for an easing in the very near term by the Federal Reserve. We assume that further cuts in U.S. short-term interest rates and, over time, growing concern about the U.S. external deficit, will cause the dollar to fall at an annual rate of about 4 percent against the euro during 1999 and 2000. The dollar should also decline, though more moderately, against the Canadian dollar as that currency regains some of the ground it has lost in recent months with the gradual pickup in global activity. There is considerable uncertainty about factors that will affect the dollar/yen exchange rate. We expect declining U.S. interest rates and growing concerns about diverging external balances in the United States and Japan to put downward pressure on the dollar. At the same time, chronic macroeconomic and financial sector problems in Japan will weigh on the yen. As a result, we are projecting the dollar to remain little changed against the yen while recognizing that the risk for large movements in either direction are substantial.

At the same time, our forecast has the real exchange value of the dollar little changed against emerging market currencies on average as increases in terms of Latin American currencies are offset by decreases against Asian currencies. We assume that the Mexican peso will decline significantly in the near term and that the Brazilian *real* will depreciate substantially in real terms over the forecast period as Brazil's currency peg succumbs to market pressures. We again project that Chinese authorities will allow some decline in the renminbi later next year and that the Argentine and Hong Kong currency pegs will hold. The projected appreciation of Asian currencies in real terms reflects inflation

rates that are higher in those countries than in the United States. On a broad weighted average basis, in real terms, the dollar falls 1 percent in the fourth quarter and another 2 percent over the next two years.

Activity in foreign industrial countries. The staff projects that real GDP growth in the foreign industrial countries will edge up from around 1½ percent in the third quarter to about 2 percent in the fourth quarter and that it will remain in that vicinity through 2000. This rate of growth is nearly ½ percent lower than that in the August forecast, reflecting downward revisions, especially in Europe and Canada, in response to the expected negative effects on spending of stock market corrections and weaker external demand resulting from the deteriorating outlook in Latin America and Eastern Europe and the slowing of growth in the United States.

Japan. We now expect Japanese GDP to show another substantial decline in the third quarter as fiscal measures are unlikely to show through significantly until later in the year. We project private domestic demand to continue declining through mid-1999 and to begin to turn up only very sluggishly in 2000. Nevertheless, we are projecting real GDP to expand at an annual rate of ¾ percent in the fourth quarter and about 1 percent in 1999 as a result of substantial fiscal stimulus now in train (and our assumption that a bit more is still to come) plus a small positive contribution from net exports. Absent further fiscal stimulus in 2000, GDP growth will remain around ½ percent as private demand picks up. Assuming growth of potential output in Japan remains about 1½ percent, this forecast implies an output gap of over 7 percent by the end of 2000.

Europe and Canada. Real output growth in Euroland is expected to remain around 2¼ to 2½ percent through the forecast period. Strength in domestic demand (supported by accommodative monetary policy) accounts for continued expansion as net exports are projected to make a negative contribution throughout the remainder of the forecast period. Real GDP growth in the United Kingdom and Canada is projected to slow over the next five quarters in response to recent monetary tightening and stock market declines and to pick up moderately in 2000.

Inflation. Consumer price inflation in the major foreign industrial countries (on a four-quarter basis and weighted by U.S. non-oil import shares) is projected to fall to just below ½ percent in the fourth quarter as Japanese prices fall 1 percent. We project the foreign average to rise to positive 1 percent by 2000 as Japanese inflation returns to zero. Inflation is expected to be low everywhere except in the United Kingdom, where it is anticipated to remain around 2½ percent.

Interest rates. This forecast incorporates the assumption that short-term market interest rates in Japan will remain very low over the forecast period. In coming months,

interest rates in Euroland will decline on average as rates converge at the current level of German rates (around 3½ percent) before the start of EMU. In light of the weaker outlook for growth in Europe, we have dropped our previous assumption that the ECB will tighten somewhat next year, and we now assume that monetary policy will remain accommodative over the forecast period with rates unchanged. We also assume that both Canadian and U.K. interest rates will decline by 100 to 150 basis points over the next two years as growth slows in those countries and (especially in the case of Canada) as U.S. rates are reduced.

Developing countries. Average real GDP of our major trading partners among developing countries is projected to decline at an annual rate of nearly 3 percent during the second half of 1998 and somewhat less in the first quarter of 1999 and to pick up but remain sluggish thereafter, with growth averaging a little over ¾ percent during 1999 and a bit less than 3 percent rate in 2000 -- only half the trend rate of recent years. This forecast represents a substantial downward revision from the previous projection because of a sharp markdown of our outlook for Latin America, especially Brazil and Argentina.

Latin America. Our best guess for Latin America is that real GDP will be depressed by diminished access to external borrowing and by the sharply higher interest rates and fiscal contractions put in place to bolster the confidence of international (and domestic) investors in these countries. Conditions in Latin American markets are expected to remain unsettled into next year; however, our forecast assumes that enough confidence will be restored to allow these countries to finance reduced though still negative current account balances.[3] Nevertheless, we project that the financial shock that has already occurred will cause GDP in Brazil and Argentina to decline at annual rates of 3 to 6 percent over the next several quarters. Venezuela will continue to be hit hard as well, but Mexico and Chile less so because their domestic policies and more flexible exchange rates have rendered them somewhat less vulnerable.

Asia. We project that real GDP in the Asian developing countries on average reach a trough in the first half of 1999 (mid-2000 for Indonesia) and will turn up slowly thereafter. Only China is expected to record significantly positive growth throughout the forecast period. Asian growth for 1998-99 has been marked down slightly since the last Greenbook.

Real net exports of goods and services. Trade data for June and July have led us to mark up the level of real exports of goods and services in the third quarter somewhat

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3. Our forecasts for Latin American growth and exchange rates are consistent with the current account deficits of these countries falling to half the levels we had projected earlier (and somewhat less than half their 1987 levels).

relative to the previous forecast. The decline in exports of machinery excluding computers and semiconductors in recent months has been less than we had expected. Beyond the third quarter, however, we have significantly reduced the growth of exports because of weaker GDP growth abroad. Latin America accounts for about 20 percent of U.S. exports, roughly the same as Asia excluding Japan. Exports of nonagricultural goods other than computers and semiconductors (core exports) are now projected to drop at an annual rate of 6 percent during the second half of this year and 2 percent during 1999. These exports should expand again in 2000, by nearly 3 percent, as GDP growth abroad picks up and the moderate decline in the dollar adds some stimulus to export demand. With exports of computers and semiconductors expected to continue growing at a much more rapid pace than other exports in real terms, total exports of goods and services should grow 2 to 3 percentage points faster than core exports over the forecast period.

We expect that the growth of imports of goods and services will slow noticeably over the year ahead from its rapid pace over the past several years as U.S. real GDP growth declines. Real imports of non-oil goods other than computers and semiconductors (core imports) should decelerate to an annual rate of growth of about 8 percent during the second half of this year from 13 percent over the past six quarters then slow to about 5 percent growth in 1999 and 2000. The moderate decline in the dollar over the forecast period should keep import growth steady as U.S. GDP growth recovers in 2000. Growth of imports of computers and semiconductors in real terms should remain rapid. The quantity of oil imports should decline during the second half of this year as inventories retreat from the current unusually high levels. We project that oil imports will rise a bit more rapidly than was forecast in August because of the adverse effect of low oil prices on U.S. oil production. Overall, real imports of goods and services are projected to expand at an annual rate of 6½ percent during the second half of this year and about 6 percent next year.

Oil prices. The staff has raised its projected path for the price of imported oil slightly in the near term to reflect recent increases in spot oil prices and anticipated further increases in response to production cuts by major oil producers. We project that the oil import price will rise from a little more than $11.50 per barrel in the third quarter to about $13.50 per barrel in 1999, and to $14 per barrel in 2000. This longer-term path is nearly $0.75 per barrel below the previous forecast largely because of the weaker outlook for global GDP growth.

Prices of non-oil imports and exports. We expect that the net appreciation of the dollar in recent quarters and declining world commodity prices through much of next year will continue to depress non-oil import prices of core goods through mid-1999. We project a rate of decline of nearly 3 percent in the second half of 1998 and no change in the first

half of 1999. As the effects of past appreciation of the dollar wane, and the dollar begins to depreciate, import prices should begin to rise slowly over the rest of the forecast period. Nonagricultural export prices for core goods are projected to decline slightly further in the second half of 1998 but to begin rising very slowly over the remainder of the forecast period, in line with comparable domestic prices.

Selected Trade Prices
(Percentage change from end of previous period except as noted; seasonally adjusted)

Trade category	1997	Projection				
		1998			1999	2000
		H1	Q3	Q4		
Exports						
Nonagricultural (core)	.5	-2.0	-.8	.1	1.2	1.3
Agricultural	-3.2	-10.9	-11.5	-11.4	1.7	2.0
Imports						
Non-oil (core)	-.7	-2.6	-3.8	-1.8	0.6	1.4
Oil (level, dollars per barrel)	17.72	12.51	11.64	12.75	13.50	14.00

NOTE. Prices for exports and non-oil imports of goods, excluding computers and semiconductors, are on a NIPA chain-weighted basis.

The price of imported oil for multiquarter periods is the price for the final quarter of the period.

Nominal trade and current account balances. The nominal trade deficit on goods and services is projected to widen significantly further over the forecast period, from about $175 billion in the second quarter of this year to nearly $290 billion in the fourth quarter of 2000. The deficit on net investment income also is projected to widen over the forecast period. As a result, the current account deficit is expected to grow from about $225 billion in the second quarter (2¾ percent of GDP) to an average of more than $360 billion for the year 2000 (4 percent of GDP, noticeably above the previous peak for this ratio that was reached in 1987).

Risks

The risks surrounding the international outlook are substantial and, if anything, have widened further as a result of recent events. We consider two alternative scenarios that highlight the potential implications of these risks for U.S. GDP and inflation. The first, labeled "pessimistic scenario" combines several somewhat interrelated developments abroad that could cause U.S. GDP to fall more than in our current baseline forecast. The

second, labeled "optimistic scenario" considers a combination of developments abroad that could raise U.S. GDP and exacerbate U.S. inflation pressures relative to the baseline.

Pessimistic scenario. In this scenario, we assume that (a) Japan either fails to reach an agreement on how to deal with its banking crisis or fails to implement a banking resolution agreement effectively, (b) Japanese fiscal expansion falls well short of current expectations, (c) Latin American financial markets continue in turmoil, as Brazil fails to make meaningful progress in reducing its budget deficit, international financial assistance falls well short of current market expectations, and as a result capital flight from Latin America persists through 1999, necessitating a reduction in these countries' current accounts to zero or in some cases into small surpluses, (d) negative reactions in Asian financial markets further depress GDP in those countries, (e) U.S. and European interest rates follow the paths assumed in the Greenbook forecast.

In this case, GDP growth in Japan and Latin America falls about 5 percentage points below baseline during 1999 and somewhat less during 2000; GDP growth in the rest of Asia falls half as much, and GDP growth in Europe falls a bit less than in the United States. U.S. GDP growth is reduced by 0.4percentage point relative to baseline during 1999, and by 0.3 percentage point during 2000. The dollar appreciates 4 percent in the near term and the U.S. inflation rate is reduced 0.2 percentage point for the next two years. In this simulation, the U.S. stock market falls endogenously by 2 percent. If the U.S. stock market were to fall by an additional10 percent (in excess of the model's prediction) in reaction to these events, the effects on U.S. GDP would be about twice as large. (See the results labeled "Pessimistic + Stock Market" in the table.)

Optimistic scenario. In this scenario, we assume that (a) Japan quickly reaches agreement on bank reform legislation and immediately begins effective implementation with generally positive response in Japanese and global financial markets, (b) Japanese fiscal stimulus shows through strongly and is augmented with additional legislation, (c) President Cardoso wins convincingly in the upcoming Brazilian election and undertakes large and credible fiscal correction, international financial assistance to Latin America is substantial, and Latin American financial markets recover strongly, with yield spreads and domestic interest rates falling sharply and allowing countries to continue to finance large current account deficits (though not as large as we had projected in August), (d) Asian financial markets rebound and activity picks up, (e) with emerging market jitters calmed, investors begin to focus on the outsized U.S. external deficit and the dollar falls10 percent against a broad range of currencies.

In this case, Japanese GDP growth rises about 2 percentage points above baseline in 1999 and 2000. GDP growth in Latin America and Asia rises several percentage points

above baseline but remains well below longer-term trend rates. The effect on Europe is small. U.S. GDP growth rises ¾ percentage point above baseline in 1999 and ½ percentage point in 2000. Consumer price inflation rises by roughly ½ percentage point during 1999 and 2000. Most of the effect on U.S. growth and inflation results directly from the decline in the dollar. If, in addition the U.S. stock market were to rebound strongly to these developments, the effects on U.S. GDP would be greater.

Alternative International Scenarios
(Percent change, Q4 to Q4)

Measure	1998	1999	2000
U.S. Real GDP			
Baseline	3.2	1.2	2.4
Pessimistic	3.2	0.8	2.1
Pessimistic + Stock Market*	3.2	0.5	1.8
Optimistic	3.3	2.0	2.8
U.S. CPI ex. food and energy			
Baseline	2.3	2.1	2.1
Pessimistic	2.3	1.9	1.9
Pessimistic + Stock Market*	2.3	1.9	1.8
Optimistic	2.3	2.7	2.6

* U.S. stock market falls an additional 10 percent.

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

Measure and country	1992	1993	1994	1995	1996	1997	-----Projected---- 1998	1999	2000
REAL GDP									
Canada	0.9	3.1	4.5	0.8	2.0	4.0	2.5	2.2	2.5
Japan	0.1	0.5	0.8	2.4	3.4	-0.4	-2.6	0.9	0.6
United Kingdom	0.4	2.7	4.9	2.0	2.9	2.9	1.5	1.7	2.3
Euro-11 Average (1)	0.1	-0.1	3.4	1.3	1.9	3.0	2.5	2.3	2.4
of which:									
France	-0.1	-0.5	4.1	0.3	2.4	3.0	2.2	1.9	2.0
Germany (2)	0.9	-0.2	3.4	0.0	2.1	2.3	2.3	2.0	2.2
Italy	-0.8	0.1	2.5	2.6	-0.2	2.8	1.4	2.0	2.3
Foreign G-7 Average weighted by 1991 GDP	0.2	0.6	2.8	1.5	2.3	1.8	0.4	1.6	1.7
Average weighted by share of U.S. nonagricultural exports									
Total foreign	2.3	3.4	5.0	1.8	4.1	4.0	-0.2	1.4	2.5
Foreign G-7	0.5	1.9	3.6	1.2	2.3	2.8	1.3	1.8	2.1
Developing Countries	5.2	6.1	7.2	2.5	6.8	5.4	-2.9	0.8	2.9
CONSUMER PRICES									
Canada	1.8	1.8	-0.0	2.1	2.0	1.0	1.3	1.6	1.5
Japan	0.9	1.2	0.8	-0.8	0.1	2.1	-1.0	-0.3	0.1
United Kingdom (3)	3.7	2.7	2.2	2.9	3.2	2.8	2.6	3.0	2.7
Euro-11 Average (4)	NA	NA	NA	2.7	2.0	1.4	1.3	1.5	1.5
of which:									
France	1.8	2.1	1.6	1.9	1.7	1.2	0.9	1.0	1.0
Germany (2)	3.4	4.2	2.6	1.7	1.4	1.8	0.8	1.2	1.5
Italy	4.9	4.1	3.8	5.9	2.7	1.6	1.7	1.8	1.8
Foreign G-7 Average weighted by 1991 GDP	2.4	2.5	1.8	1.6	1.5	1.8	0.6	1.0	1.2
Average weighted by share of U.S. non-oil imports	1.9	2.0	1.0	1.1	1.3	1.7	0.4	0.9	1.0

1. Includes all of the European Union countries except the United Kingdom, Denmark, Sweden, and Greece; weighted by GDP.
2. CPI excluding mortgage interest payments which is the targeted inflation rate.
3. Harmonized CPI's for the Euro-11, weighted by shares in final consumption of households converted to a common currency using estimated PPP exchange rates.

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

					Projected							
	1998				1999				2000			
Measure and country	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
REAL GDP												
Canada	3.4	1.8	2.5	2.3	2.2	2.2	2.2	2.2	2.2	2.4	2.6	2.8
Japan	-5.2	-3.3	-2.7	0.8	0.8	1.1	0.9	0.7	0.3	0.5	0.7	0.9
United Kingdom	2.2	2.0	0.9	1.0	1.4	1.6	1.8	2.0	2.1	2.3	2.5	2.5
Euro-11 Average (1)	3.3	2.1	2.5	2.0	2.3	2.3	2.3	2.4	2.4	2.4	2.4	2.4
of which:												
France	2.5	2.8	1.8	1.8	1.8	1.8	2.0	2.0	2.0	2.0	2.0	2.0
Germany	5.9	0.4	1.3	1.6	1.8	2.0	2.0	2.1	2.1	2.2	2.3	2.3
Italy	-0.5	1.7	3.5	1.0	2.0	2.0	2.0	2.0	2.3	2.3	2.3	2.3
Foreign G-7 Average weighted by 1991 GDP	0.1	-0.0	0.4	1.3	1.5	1.6	1.6	1.6	1.5	1.6	1.8	1.8
Average weighted by share of U.S. nonagricultural exports												
Total foreign	-0.8	0.4	-0.4	-0.1	0.5	1.3	1.8	2.1	2.2	2.4	2.6	2.7
Foreign G-7	1.6	0.7	1.2	1.7	1.8	1.9	1.9	1.9	1.8	2.0	2.1	2.3
Developing Countries	-4.7	-1.1	-3.0	-2.6	-1.2	0.6	1.6	2.3	2.5	2.7	3.0	3.2
CONSUMER PRICES (2)												
Canada	1.0	1.0	1.1	1.3	1.5	1.6	1.6	1.6	1.5	1.5	1.5	1.5
Japan	2.1	0.6	0.0	-1.0	-1.0	-1.0	-0.7	-0.3	0.0	0.0	0.1	0.1
United Kingdom (3)	2.5	3.0	2.6	2.6	2.9	2.9	3.0	3.0	2.9	2.8	2.8	2.7
Euro-11 Average (4)	1.2	1.5	1.4	1.3	1.4	1.3	1.3	1.5	1.5	1.5	1.5	1.5
of which:												
France	0.7	1.0	1.0	0.9	0.9	0.9	0.9	1.0	1.0	1.0	1.0	1.0
Germany	1.2	1.3	0.8	0.8	0.9	1.0	1.1	1.2	1.3	1.4	1.5	1.5
Italy	1.7	1.8	1.8	1.7	1.7	1.7	1.7	1.8	1.8	1.8	1.8	1.8
Foreign G-7 Average weighted by 1991 GDP	1.6	1.3	1.0	0.6	0.7	0.7	0.8	1.0	1.1	1.1	1.2	1.2
Average weighted by share of U.S. non-oil imports	1.6	1.1	0.8	0.4	0.5	0.6	0.7	0.9	1.0	1.0	1.0	1.0

1. Includes all of the European Union countries except the United Kingdom, Denmark, Sweden, and Greece; weighted by GDP.
2. Percent change from same period a year earlier.
3. CPI excluding mortgage interest payments which is the targeted inflation rate.
4. Harmonized CPI's for the Euro-11, weighted by shares in final consumption of households converted to a common currency using estimated PPP exchange rates.

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1992	1993	1994	1995	1996	1997	------ Projected ------ 1998	1999	2000
NIPA REAL EXPORTS and IMPORTS									
	Percentage point contribution to GDP growth, Q4/Q4								
Net Goods & Services	-0.4	-0.6	-0.4	0.5	-0.3	-0.6	-1.7	-0.6	-0.4
Exports of G&S	0.4	0.5	1.0	1.1	1.2	1.1	-0.4	0.1	0.5
Imports of G&S	-0.8	-1.1	-1.4	-0.7	-1.4	-1.7	-1.2	-0.8	-0.9
	Percentage change, Q4/Q4								
Exports of G&S	4.1	4.6	10.0	10.5	10.3	9.6	-3.8	1.3	4.7
Services	-0.9	4.1	6.0	9.8	7.5	1.5	-1.1	1.7	3.0
Agricultural Goods	10.4	-5.5	16.6	-4.3	4.8	2.8	-5.3	1.5	1.5
Computers	25.2	23.7	32.0	55.5	35.9	40.7	9.0	26.6	28.3
Semiconductors	64.8	32.9	66.9	79.6	46.2	21.0	-0.8	16.9	21.3
Other Goods 1/	2.3	3.6	7.0	5.8	8.0	11.6	-6.2	-1.9	2.9
Imports of G&S	7.4	10.2	12.3	5.6	11.8	14.0	9.5	6.1	6.6
Services	1.4	3.2	1.4	6.1	5.5	12.4	2.5	1.3	2.7
Oil	12.1	10.1	-0.2	2.4	7.9	4.0	1.0	3.2	6.1
Computers	45.1	39.3	44.8	48.1	24.4	30.3	31.1	30.2	29.9
Semiconductors	42.0	34.2	54.5	92.4	57.6	32.7	-7.3	21.8	25.3
Other Goods 2/	5.4	9.5	12.2	-1.2	10.4	13.0	10.7	4.8	4.8
	Billions of chained 1992 dollars								
Net Goods & Services	-29.5	-70.2	-104.6	-96.5	-111.2	-136.1	-250.9	-341.2	-386.0
Exports of G&S	639.4	658.2	712.4	792.6	860.0	970.0	973.4	965.3	1000.6
Imports of G&S	669.0	728.4	817.0	889.0	971.2	1106.1	1224.3	1306.5	1386.7
	Billions of dollars								
US CURRENT ACCOUNT BALANCE	-51.4	-86.1	-123.8	-115.3	-134.9	-155.2	-233.7	-319.0	-364.1
Net Goods & Services (BOP)	-38.7	-71.9	-100.9	-99.9	-108.6	-110.2	-175.4	-243.2	-277.6
Exports of G&S (BOP)	617.3	643.2	703.8	795.6	850.8	937.6	920.7	905.4	938.8
Imports of G&S (BOP)	656.0	715.2	804.7	895.5	959.3	1047.8	1096.1	1148.6	1216.4
Net Investment Income	22.5	23.9	16.5	19.3	14.2	-5.3	-17.2	-34.1	-44.8
Direct, Net	51.6	55.7	51.8	63.0	66.2	63.7	57.5	49.2	55.9
Portfolio, Net	-29.1	-31.7	-35.3	-43.7	-51.9	-69.1	-74.8	-83.2	-100.7
Net Transfers	-35.2	-38.1	-39.4	-34.6	-40.6	-39.7	-41.1	-41.8	-41.8

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1995				1996				1997			
	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	-0.2	-0.3	1.6	0.7	-1.1	-1.0	-1.4	2.4	-1.3	-0.4	-0.5	-0.3
Exports of G&S	1.0	0.6	1.9	1.1	0.4	0.6	0.2	3.2	0.9	1.7	1.2	0.5
Imports of G&S	-1.2	-0.9	-0.3	-0.4	-1.5	-1.6	-1.6	-0.9	-2.2	-2.2	-1.7	-0.8
Percentage change from previous period, SAAR												
Exports of G&S	9.2	5.4	17.8	10.2	3.7	5.8	2.1	32.0	8.3	15.5	10.6	4.4
Services	9.1	2.9	21.7	6.4	-4.0	10.3	-9.9	39.8	-6.7	11.8	5.9	-4.0
Agricultural Goods	1.8	-13.4	5.0	-9.4	22.6	-32.8	-1.6	48.7	-16.1	-7.8	8.7	32.8
Computers	36.4	33.8	86.6	71.6	57.6	24.7	27.7	35.9	70.2	78.7	41.9	-9.2
Semiconductors	72.0	100.8	96.2	53.6	23.8	29.7	30.2	118.6	41.3	17.3	32.3	-2.2
Other Goods 1/	4.3	1.4	9.4	8.1	0.1	6.0	5.7	21.3	13.8	15.6	9.2	8.0
Imports of G&S	9.8	7.2	2.0	3.5	13.1	13.5	13.6	7.0	18.6	17.9	13.5	6.3
Services	20.5	-3.3	3.1	5.5	9.2	4.3	9.9	-1.1	17.8	10.6	15.8	5.8
Oil	-11.4	15.4	31.4	-18.2	-9.8	68.9	3.5	-14.0	-8.2	37.0	6.0	-12.2
Computers	15.4	51.6	62.7	69.3	22.5	22.9	18.8	33.8	54.5	39.0	30.6	2.9
Semiconductors	37.1	105.5	128.2	113.3	38.7	8.9	50.1	172.1	89.0	16.0	20.3	17.6
Other Goods 2/	7.2	1.5	-8.8	-3.8	13.9	10.5	13.5	4.2	16.2	16.1	11.8	8.1
Billions of chained 1992 dollars, SAAR												
Net Goods & Services	-109.5	-114.7	-86.8	-74.8	-95.5	-113.5	-140.1	-95.9	-121.5	-131.6	-142.4	-149.0
Exports of G&S	763.9	774.0	806.3	826.1	833.6	845.5	849.9	911.1	929.4	963.6	988.1	998.8
Imports of G&S	873.4	888.7	893.1	900.9	929.1	958.9	990.0	1007.0	1050.9	1095.2	1130.5	1147.8
Billions of dollars, SAAR												
US CURRENT ACCOUNT BALANCE	-123.7	-134.2	-115.5	-87.7	-112.9	-132.0	-161.6	-133.2	-148.0	-140.4	-152.4	-180.2
Net Goods & Services (BOP)	-109.3	-125.8	-90.0	-74.5	-92.4	-112.8	-132.3	-96.8	-112.5	-106.1	-108.4	-113.8
Exports of G&S (BOP)	765.4	782.0	809.7	825.6	833.6	845.3	837.5	886.7	904.7	936.1	951.7	957.8
Imports of G&S (BOP)	874.7	907.7	899.7	900.1	926.0	958.2	969.8	983.5	1017.3	1042.1	1060.1	1071.7
Net Investment Income	20.1	24.0	10.2	22.7	21.4	15.9	6.9	12.7	0.1	1.8	-6.2	-17.0
Direct, Net	59.9	67.2	56.5	68.3	64.8	64.4	61.9	73.6	64.2	69.6	65.5	55.6
Portfolio, Net	-39.8	-43.2	-46.2	-45.5	-43.3	-48.5	-55.0	-60.9	-64.2	-67.8	-71.7	-72.6
Net Transfers	-34.5	-32.4	-35.8	-35.9	-41.9	-35.1	-36.2	-49.1	-35.5	-36.1	-37.8	-49.3

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1998				Projected 1999				2000			
	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	-2.3	-2.1	-0.9	-1.3	-1.0	-0.8	-0.5	-0.3	-0.3	-0.5	-0.5	-0.2
Exports of G&S	-0.3	-0.9	-0.2	-0.3	-0.1	0.1	0.2	0.3	0.4	0.5	0.5	0.6
Imports of G&S	-1.9	-1.2	-0.7	-1.0	-0.9	-0.9	-0.8	-0.6	-0.7	-1.0	-1.0	-0.8
Percentage change from previous period, SAAR												
Exports of G&S	-2.8	-7.6	-1.7	-2.8	-0.8	0.9	2.3	2.9	3.8	4.6	5.0	5.3
Services	-1.2	2.0	-2.8	-2.2	0.1	1.7	2.5	2.4	2.5	3.2	3.1	3.1
Agricultural Goods	-9.9	-23.5	14.7	1.6	1.6	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Computers	-15.5	8.9	21.5	26.2	26.2	26.2	26.7	27.2	27.7	28.2	28.6	28.6
Semiconductors	-2.0	-18.2	7.4	12.6	14.8	15.9	17.9	19.3	20.4	21.6	21.6	21.6
Other Goods 1/	-1.6	-11.1	-5.0	-6.8	-4.6	-2.5	-0.8	0.3	1.7	2.6	3.5	4.0
Imports of G&S	15.7	9.2	5.5	7.7	6.8	6.9	5.9	4.7	5.5	7.6	7.6	5.6
Services	9.3	-0.5	-0.1	1.6	1.0	0.3	1.5	2.2	1.6	3.3	3.0	3.0
Oil	8.8	40.8	-13.2	-21.7	-6.3	35.0	9.6	-18.3	7.0	25.6	14.3	-17.6
Computers	38.8	22.9	29.6	33.5	33.5	31.1	28.6	27.4	26.2	31.1	31.1	31.1
Semiconductors	9.9	-29.5	-18.5	17.0	19.3	21.6	22.7	23.9	25.3	25.3	25.3	25.3
Other Goods 2/	16.1	10.6	7.4	8.9	6.4	4.2	4.1	4.5	3.7	4.8	5.5	5.2
Billions of chained 1992 dollars, SAAR												
Net Goods & Services	-198.5	-244.4	-265.1	-295.3	-318.0	-337.2	-350.5	-358.9	-367.7	-381.4	-394.5	-400.6
Exports of G&S	991.9	972.4	968.1	961.2	959.3	961.5	966.8	973.8	982.9	994.0	1006.2	1019.4
Imports of G&S	1190.4	1216.8	1233.3	1256.5	1277.3	1298.6	1317.4	1332.7	1350.5	1375.4	1400.7	1420.1
Billions of dollars, SAAR												
US CURRENT ACCOUNT BALANCE	-186.9	-224.5	-242.3	-281.0	-293.0	-311.2	-325.6	-346.1	-343.0	-357.0	-370.4	-386.0
Net Goods & Services (BOP)	-140.0	-174.3	-180.3	-207.1	-226.2	-240.6	-250.1	-255.9	-263.2	-275.0	-284.4	-287.6
Exports of G&S (BOP)	946.2	921.1	913.6	901.9	900.2	901.9	906.7	912.9	921.9	932.5	944.2	956.7
Imports of G&S (BOP)	1086.2	1095.4	1093.9	1108.9	1126.4	1142.4	1156.7	1168.9	1185.1	1207.5	1228.7	1244.3
Net Investment Income	-9.0	-13.0	-23.0	-23.9	-27.8	-31.6	-36.6	-40.2	-40.8	-42.9	-46.9	-48.4
Direct, Net	62.4	61.0	53.7	53.1	49.9	49.1	48.2	49.5	53.4	55.5	56.1	58.8
Portfolio, Net	-71.3	-74.0	-76.7	-77.0	-77.8	-80.7	-84.8	-89.7	-94.2	-98.4	-103.0	-107.3
Net Transfers	-37.9	-37.3	-39.0	-50.0	-39.0	-39.0	-39.0	-50.0	-39.0	-39.0	-39.0	-50.0

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