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## **Part 1**

January 28, 1999

# **CURRENT ECONOMIC AND FINANCIAL CONDITIONS**

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## **Summary and Outlook**

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

Strictly Confidential (FR) Class II FOMC

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January 28, 1999

## **SUMMARY AND OUTLOOK**

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## Domestic Developments

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The BEA will publish its advance estimate of fourth-quarter GDP growth tomorrow. Our guess is that it will report a real increase of around 5 percent. Every major segment of private domestic spending appears to have surpassed our expectations and so, too, have net exports. Meanwhile, wages and prices have performed about as we predicted, with inflation showing no signs of picking up despite extremely taut labor markets and a downturn in the dollar since last summer.

Can the good times continue to roll? Perhaps they can, for at least a while. However, ultimately the constraints on the supply side of the economy would stand in the way of a lengthy extension of the 3-3/4 to 4 percent real GDP growth trend that we have observed in the past three years. The recent performance of labor productivity has supported our assessment that the underlying pace of improvement picked up at the middle of the decade, but it would require some greater optimism to anticipate a further significant acceleration in the period ahead. Thus, a continuation of output gains even approaching those we have been enjoying probably would require that the jobless rate fall considerably further. We have strong doubts that such a development could be achieved without a quite marked intensification of inflationary pressures.

In our current forecast, there is no direct test of that assertion because we still anticipate a substantial moderation in the pace of economic expansion this year. In the near term, this reflects, in part, the unwinding of some special factors that elevated activity in late 1998--namely, unusually favorable weather and an auto strike rebound. Of greater fundamental importance is our view that the bull market in U.S. equities probably has run its course. In the forecast, the consequent decline in the household wealth-income ratio gradually takes the steam out of aggregate demand. Along the way, the accelerator effects that have boosted investment over the past few years also wane.

We are predicting that real GDP growth will drop off to about 2-1/2 percent, on average, this year and next. Owing to the initial conditions of greater demand momentum and a higher stock market level, this is a significantly stronger output path than in the last Greenbook--probably strong enough to prevent the unemployment rate from rising appreciably, in contrast to our prior forecasts. With this additional tautness in the labor market, and with higher factory utilization rates as well, there is a bit more acceleration in wages and prices in this forecast, although from marginally more favorable initial levels. Oil prices are still the biggest factor in a projected step-up in inflation over the next two years: The CPI moves up from a 1.5 percent rise in 1998 to a 2.6 percent advance in 2000, on a consistently measured basis.

### Key Background Factors

Financial conditions became increasingly supportive of growth over the intermeeting period. Stock prices hit record highs in the middle of January, and subsequent "profit taking" eroded only a portion of those gains. Perhaps because it had been so much feared, the anticipated year-end scramble for funds proved to be a non-event, and thus far the news of presidential impeachment, military action against Iraq, and currency crisis in Brazil have caused only a ripple in financial markets. Commercial paper spreads have returned to essentially their earlier narrow dimension; and though the January survey of senior loan officers shows some further firming of terms since November, there was little additional tightening of standards in C&I lending. In the bond markets, Treasury yields are little changed, on balance, since the December FOMC meeting, and quality spreads on corporates have narrowed a tad.

The federal funds rate is assumed to remain at 4-3/4 percent over the projection period. However, we anticipate Treasury bond yields will drift up some from current levels as safe-haven demands ebb and as continued tight labor markets and increased inflation dispel any lingering hopes of Federal Reserve easing. In contrast, we expect little change in rates on corporate bonds and mortgages, as currently wide quality spreads narrow a bit more.

In the equity markets, we have seen new signs of speculative froth in the form of the astonishing run-up in the "Internet" stocks. But share prices more generally have continued to defy the gravitational pull of traditional valuation standards; rather than slipping with the publication of quarterly earnings reports that looked good only against downgraded expectations, share prices overall have risen considerably further in the past several weeks, once again in marked contradiction of our previous forecast path. Stocks thus look still more overvalued, given what we think are the prospects for corporate earnings. The market would seem ripe for a significant correction. But chastened by bitter experience, and in the absence of an assumption of a tightening in monetary policy, we have anticipated only a sideways movement in equity prices over the next two years, rather than a drop. As a result, the wealth-to-income ratio, though declining, is at an appreciably higher level throughout this projection than in the last.

The turmoil in Brazil, especially, has necessitated a reassessment of the international influences in our forecast. We see a rocky road ahead for Brazil; the outlook there has substantial uncertainties, but our baseline forecast assumes that the nominal exchange rate of the *real* against the dollar stabilizes later this year at a much lower level than before its float in mid-January. On the way, monetary and fiscal stringency produces a deeper

recession than in our last forecast. The steeper drop in activity in Brazil and the associated financial market dislocations will tend to have adverse effects on other economies, especially in Latin America. However, financial spillovers to emerging economies outside the region have thus far been rather mild, and we are assuming that this pattern will continue to hold.

The economic outlook for Europe and Japan is a little softer in this Greenbook; in non-Japan Asia, incoming indicators actually have been a bit more positive on net than we had expected. But, as a result of the weaker forecast for Latin America, foreign real GDP growth--weighted across countries according to the importance in U.S. exports--now is projected to rise only 1 percent in 1999, 3/4 percentage point less than anticipated in the last forecast. Growth is projected to pick up to a 2-1/4 percent pace in 2000, as recovery commences in Latin America and growth firms in emerging Asian countries.

On foreign exchange markets, the dollar is little changed, on balance, against the yen over the intermeeting period, but it has strengthened slightly against the euro. We are projecting that the dollar will depreciate gradually over the forecast period against the currencies of the major industrial nations. Given developments in Latin America, however, the broad index of the dollar is expected to rise further in real terms this year before retreating somewhat late in 1999 and in 2000 when inflation picks up in Latin America. On balance, the real value of the dollar now is expected to be little changed over 1999-2000, rather than falling 1-1/2 percent as forecast in the December Greenbook.

With the onset of colder weather in North America, crude oil prices have firmed this month; the spot price of West Texas intermediate is expected to average \$13.25 in the first quarter as a whole, versus \$12.90 in the fourth quarter. That price is projected to rise to \$16 per barrel by early next year, as demand grows and OPEC and other producers succeed in limiting their output somewhat. The price holds at \$16 for the remainder of 2000.

Fiscal policy is expected to be an essentially neutral influence on aggregate demand. Proposals to reform the social security system or to reduce income taxes are now on the table, but in the present political climate these initiatives do not appear likely to lead to quick action. As a result, our key fiscal assumptions are unchanged in this Greenbook. With the stronger economy and higher wealth generating substantial additional revenues, our revised forecast shows the unified surplus at \$101 billion in fiscal 1999 and \$144 billion in fiscal 2000.

### Recent Developments and the Outlook for the Current Quarter

As noted, GDP growth in the fourth quarter appears to have been remarkably rapid, outstripping even the brisk trend of previous quarters. A part of the story was the surge in motor vehicle assemblies, which contributed about 1-1/2 percentage points to the GDP gain; GM's post-strike efforts to recapture market share led to an intensification of price competition that, against a backdrop of basically strong demand, helped push sales to levels that took even the automakers by surprise.

Total consumer spending probably increased about 4-3/4 percent (annual rate) in the fourth quarter. Excluding motor vehicles, PCE rose at an annual rate of 3 percent or so--a considerable increment, but one that pales in comparison with the blistering 5-1/2 percent pace of the first three quarters of last year. Motor vehicles were also an important contributor to the re-acceleration of spending on producers' durable equipment in the final quarter of 1998; in addition, outlays for computers and communications equipment continued to post impressive increases. Construction expenditures were up appreciably: Warm weather and strong underlying fundamentals contributed to a jump in housing starts and a double-digit gain in residential investment, while outlays for nonresidential structures probably ticked up.

### Summary of the Near-Term Outlook

(Percent change at annual rate except as noted)

Measure	1998:Q4		1999:Q1	
	Dec. GB	Jan. GB	Dec. GB	Jan. GB
<b>Real GDP</b>	3.1	5.0	2.5	2.7
Private domestic final purchases	5.5	6.3	3.4	3.2
Personal consumption	4.1	4.7	3.1	2.7
Residential investment	10.5	12.5	4.7	7.9
Business fixed investment	12.2	14.0	4.6	4.5
Government outlays for consumption and investment	2.8	3.1	1.6	.8
	Change, billions of chained (1992) dollars			
Inventory investment	-24.2	-17.4	-.2	20.3
Net exports	-16.8	-2.0	-14.9	-26.5

Although source data are still far from complete, those we do have suggest that inventory investment slowed in the fourth quarter. Our guess is that nonfarm stock accumulation subsided enough to subtract 3/4 percentage point from GDP growth. The pace of accumulation--about 2-1/2 percent--would be well under that of final sales, and our sense is that inventories are viewed as excessive in only a few segments of the nonfarm economy.

Turning to the current quarter, we are projecting that real GDP will slow to a 2-3/4 percent pace. Unfortunately, hard data are virtually nonexistent at this point. One shred of information we have is schedules for motor vehicle assemblies, which suggest that the output of cars and trucks will level off this quarter, eliminating the boost to output growth that occurred in the fourth quarter.

A decline in net exports is projected to subtract more than a percentage point from the growth of real GDP in the first quarter; net exports were a neutral influence in the fourth quarter. Although exports of computers and semiconductors continue to grow rapidly in the first quarter, other merchandise exports drop at a double-digit pace as shipments of vehicle parts to Canadian assembly operations fall back from elevated post-strike levels. Imports of semiconductors are forecast to turn up in the first quarter in light of strong demand; again reflecting in part the influence of the auto industry, other merchandise imports should be about flat overall.

After having risen 6-1/2 percent over 1998, private domestic final purchases are projected to increase a "mere" 3-1/4 percent in the current quarter. After the surge in the fourth quarter, we expect some payback in the sales of light vehicles. Outside of motor vehicles, consumer spending is expected to grow a little more than in the fall quarter. The recent strength in employment and the further accretion of wealth in the stock market clearly have left households in good spirits and disposed to spend. Reports from retailers are quite upbeat with regard to early January sales, one element being the belated demand for winter merchandise as low temperatures and snow finally arrived.

Housing starts are expected to be essentially unchanged at a 1.68 million unit pace in the first quarter. However, given normal production lags, the rise of starts since last summer should hold the growth of residential investment this quarter to within a few percentage points of the brisk fourth-quarter pace.

Real business fixed investment probably will post a much milder advance this quarter than in the last. Besides the drop-back in purchases of motor vehicles, deliveries of commercial jets to domestic airlines should decline considerably. However, other producers' durables appear to be on a solid

growth trajectory, judging by recent orders data from domestic manufacturers of nondefense capital goods. An ongoing decline in industrial building and oil drilling likely will pull down outlays for nonresidential structures.

Inventory investment may increase this quarter, because of efforts to rebuild skimpy auto dealer stocks. Outside of the motor vehicle sector, we expect inventory accumulation to remain moderate, as some of the industries with overhangs, such as steel and chemicals, work those down.

The output growth we are forecasting should suffice to generate further payroll expansion this quarter; however, the January increase probably will be relatively modest because less favorable weather will cause a drop in seasonally adjusted construction jobs.

Inflation still seems to be well damped at this point, though the near-term readings on core prices may be lifted by the "special factors" of tobacco and postage increases. The CPI less food and energy is forecast to rise at an annual rate of 2-3/4 percent in the first quarter--almost 1/2 percentage point faster than the pace in the preceding half year. Similarly, core PCE prices are projected to accelerate to a 1-3/4 percent annual rate in the first quarter from a pace of around 1 percent in the second half. We expect that the increase in the ECI for private industry compensation will pick back up from the 3 percent annual rate of the fourth quarter: Smaller bonuses in the financial sector offset only part of the anticipated step-up in health insurance costs and the additional wage pressures of a very tight labor market.

#### **The Outlook for Economic Activity beyond the Current Quarter**

Real GDP is projected to grow at an average pace of just over 2-1/2 percent in 1999 and 2000. The slowdown from the torrid rate of the past three years is concentrated in private domestic final purchases: PDPF decelerates from a 6-1/2 percent increase in 1998 to 3-1/2 percent this year and 3 percent in 2000. Latin American economic difficulties will intensify the deterioration in our net export position in the near term, but over the next two years the firming in overall foreign activity and the depreciation of the dollar should diminish the drag on U.S. GDP growth from the external sector.

**Consumer spending.** Consumer demand is expected to continue providing impetus to economic expansion, though not to the degree we saw last year. Real PCE is projected to grow 3-1/2 percent in 1999 and 2-3/4 percent in 2000, compared with 5-1/4 percent in 1998. Given the magnitude of the rise in the stock market in recent years and the normal lags between changes in the wealth-income ratio and consumption, equity prices are expected to have a positive effect for a while longer. However, the net stimulus wanes as time

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

Measure	1997	1998	1999	2000
<b>Real GDP</b>	3.8	4.0	2.6	2.4
Previous	3.8	3.6	2.1	2.3
Final sales	3.4	4.4	2.5	2.4
Previous	3.4	4.1	2.0	2.2
PCE	3.7	5.2	3.5	2.8
Previous	3.7	5.1	2.7	2.5
Residential investment	4.2	13.2	.2	-2.2
Previous	4.2	12.6	-1.2	-.6
BFI	9.8	11.8	5.8	5.8
Previous	9.8	11.4	4.1	5.1
Government purchases	1.4	1.6	1.4	1.8
Previous	1.4	1.6	1.3	1.5
Exports	9.6	.7	.2	4.4
Previous	9.6	-2.8	2.5	4.8
Imports	14.0	10.4	6.1	6.7
Previous	14.0	8.5	5.9	6.2
	Change, billions of chained (1992) dollars			
Inventory change	34.4	-28.3	4.0	-.7
Previous	34.4	-34.8	7.7	3.4
Net exports	-53.1	-112.0	-75.2	-46.1
Previous	-53.1	-125.7	-49.3	-34.4

passes: Based on our rules of thumb, the wealth effect contributed 1 percentage point to the growth in consumption in 1998 and is projected to add 1/2 percentage point in 1999 and to subtract a tenth in 2000. As a result, increases in PCE outstrip the gains in disposable personal income, and the personal saving rate ends up in marginally negative territory over much of the 1999-2000 period.

Some analysts would say that the continuation of zero personal saving constitutes a downside risk to the consumption forecast. We do not find that argument compelling. Among other things, the NIPA saving concept is a byproduct of an accounting scheme that is not designed to capture all the elements of household finances that influence spending. And the

measurement of the saving rate is imprecise and subject to revision--implying that it can be dangerous to put great stock in the indicated level. The low personal saving rate might be seen as part of a broader national saving imbalance, mirrored in an ultimately unsustainable trend in our external position, but that certainly is not a clear guide for a short-run forecast of consumer spending. And individuals may be undersaving currently if a stock market bubble has given them an exaggerated view of their lifetime financial resources. A collapse of the bubble could produce a marked weakening of spending.<sup>1</sup>

In any event, expenditures on durable goods are expected to register an especially sharp deceleration. Spending in this category has risen 25 percent over the past three years--and stocks now are probably both considerably larger and growing at an appreciable pace. Further increases in households' perceptions of their "permanent" incomes could elevate the targeted levels for these stocks, but given our projection of current incomes and wealth, this is unlikely to be so powerful an impetus to demand as it has been to date. For example, we anticipate that sales of new light motor vehicles, which reached a twelve-year high of 15-1/2 million units in 1998, will slip to about 15 million units in 2000. Continuing product innovation and declining prices should keep sales of electronic gear moving briskly upward in real terms, but even with these goods some deceleration should be expected. Less robust discretionary spending on items such as restaurant meals, luxury apparel, and travel also is expected to contribute to slower growth in purchases of nondurable goods and services.<sup>2</sup>

**Residential investment.** Rapid growth of employment and real incomes, rising household net worth, and the decline in mortgage rates propelled housing construction to an impressive gain in 1998. At 1.62 million units, housing starts registered the best annual performance since 1987.

Despite that high level of activity, builders reportedly still have sizable backlogs of orders, and these should help to sustain the volume of new construction starts even as the fundamentals of the sector begin to weaken

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1. Were the stock market to rise above the level assumed in our forecast, we would have no hesitation in projecting a more negative saving rate. It has been suggested that there might be a break point at zero because the representative household can get down to zero simply by spending all its income, but it must borrow or sell assets to push the saving rate below zero; however, the NIPA numbers do not really correspond to the cash flows of households, and consumers have many ways to liquefy their labor or property wealth.

2. As the millennium approaches, we expect households to increase their precautionary purchases of non-perishables, and we have boosted consumer spending slightly in 1998:Q4 to account for this effect.

over the coming months. A moderation of job and income gains and a halt to the rise in stock market wealth will eventually leave some imprint on housing demand, despite a continuation of attractive mortgage rates.

In the single-family market, starts are expected to drop back this quarter from the weather-aided high of late 1998 and to drift gradually lower thereafter. Single-family starts for 1999 as a whole still match last year's total of 1.27 million units, but starts fall to 1.22 million units in 2000. These are both quite hefty numbers, especially coming after several years of building that has propelled the national homeownership rate to new highs. However, there is no reason to think that the homeownership rate cannot rise still further, and moreover, the combination of changes in tax laws, higher wealth, and a growing middle-age population probably is stimulating demand for second homes.

Our forecast for the multifamily sector has a similar contour, with starts matching the level of 1998 this year before dropping off in 2000. The turmoil in financial markets this past summer did little to sidetrack the construction of multifamily properties. With vacancy rates low in many localities and real rents rising, financing has still been available for developers from a variety of sources, and we do not see any deterioration in prospect.

**Business fixed investment.** Real BFI appears to have risen at a 6-1/2 percent annual rate over the past two quarters--not slow, but well below the average pace of the prior few years. This may well have been the first stage of the natural ebbing of the "accelerator" effect, as GDP growth has been on a pretty steady path since 1996 and capacity growth is already appreciable at the prevailing level of investment. Going forward, the accelerator should become a still greater drag, and a squeeze on corporate profit margins will be curbing cash flow growth. Indeed, our forecast for capital spending would be weaker than it is were it not for our expectation that technological innovations will continue to afford firms opportunities for cost-saving capital-labor substitutions and also force them to update their facilities to produce new products. Thus, after averaging growth of 11 percent per year over 1996-1998, we expect real BFI to increase just under 6 percent in both 1999 and 2000.

Equipment spending should be the major swing factor in this downshift. We project that real PDE will rise 8-1/2 percent this year--half the extraordinary 1998 pace--and 7-3/4 percent in 2000. Gross business purchases of computers are projected to grow very rapidly, but less steeply than last year. In part this will reflect the general moderation in capital investment, but in addition, price declines may not be so sharp as they were last year. Y2K

considerations may produce some waves in the trajectory of computer purchases: Replacement of old machines is probably getting an extra boost from remediation programs currently, but later this year some businesses--especially large firms--will wish to stabilize their systems and free their IT staffs from installation work as they complete final searches for any remaining millennium bugs. Elsewhere in the high-tech sector, the demand for communications equipment is expected to continue growing at a double-digit pace, stimulated by the expansion of wireless phone networks, growing competition in local and long-distance telephone markets, and the need for infrastructure investment to support the explosive growth of the Internet.

In the transportation sector, we are looking for an absolute decline in the pace of equipment spending. Given the large order backlogs, shipments of heavy trucks are likely to remain at a high level for quite a while longer, but we anticipate a significant falloff in business purchases of cars and light trucks, in large measure reflecting a slower pace of consumer leasing activity--which is counted as PDE in the NIPAs. Similarly, in the aircraft industry, Boeing production schedules suggest that domestic airlines will take delivery of a reduced number of planes in 1999 and 2000.

Orders for other types of equipment have been quite strong in recent months--some of that strength being in longer-lead-time items such as power-generating equipment that should be delivered in late 1999 and 2000. However, overall, excess capacity and pressures on profits and cash flows will put a significant damper on capital spending, especially in manufacturing and agriculture.

Prospects for investment in nonresidential structures remain weak. In the industrial sector, firms have already been trimming their spending on new plants, and that trend should continue, given already ample capacity in many sectors. With an abundance of retail space available, the decline in other commercial structures is likely to continue, and the projected rise in oil prices will not be enough to reverse the decline in domestic exploration and drilling. Conditions in office-space markets differ considerably from area to area, but vacancy rates and other indicators suggest that there is economic room for a further increase in overall construction; projects reportedly have been receiving greater scrutiny from lenders, but financing should not be a problem for sound undertakings. Also on the plus side, shortages of generating capacity are prompting increases in spending by electric utilities. Because of these cross currents, we are projecting that aggregate real NRS will move little one way or the other over the next two years.

**Business inventories.** As noted earlier, we are estimating that nonfarm inventories rose only moderately in the fourth quarter. With stocks for the most part at reasonably comfortable levels, and with businesses already anticipating some deceleration of sales, there would appear to be little reason to anticipate a dynamic role for inventory investment in the outlook for economic activity. We have, however, once again built into our forecast a zig-zag in the pace of stocking to reflect the likelihood that businesses will want to build up supplies of some items by the end of the year as a hedge against Y2K-related disruptions. While this process could start earlier, we have assumed that the phenomenon will largely be a fourth-quarter story. The boost to GDP growth is less than a percentage point in that period, and it is more than reversed in the first quarter of 2000, when producers actually experience a few glitches.

In the farm sector, we are assuming that inventory accumulation will slow over 1999 and 2000, partly as a consequence of producers' responses to the negative price signals they have been receiving. Just how far that slowing will go is unclear at this point, with the normal inertia of farm supply perhaps being reinforced by the ambiguity of the federal government's recent reaction to strains in the sector. Our assumption is that the spirit of the Freedom to Farm Act will survive, and that producers will not delay adjustments unduly in hopes of a non-market reprieve.

**Government spending.** Real federal purchases are forecast to fall 1-3/4 percent this year and 1/2 percent in 2000. Defense spending is expected to fall in both years. The strikes against Iraq--even if continued on the recent scale--are unlikely to have a material effect on procurement of munitions within the projection period. Nondefense expenditures are essentially flat this year but fall 3/4 percent in 2000.

We have strengthened the path of state and local purchases in this Greenbook. Real spending now is forecast to rise 3 percent in 1999 and 2000--almost 1/2 percentage point more than in the last forecast. The financial position of most state governments has continued to improve--and will be enhanced over the coming years by moneys from the tobacco settlement. Although many states have been inclined to salt away some of their revenue surprises in rainy day funds, surpluses have now risen to such high levels that some increase in spending is likely to be almost irresistible. Investment spending is expected to be the fastest growing component, lifted in part by the new federal funds for highway construction. In contrast, states and municipalities are expected to keep a fairly tight rein on consumption outlays--mainly through restraint on the size of their workforces.

**Net exports.** Real exports of goods and services are forecast to rise 1/4 percent this year--a pace slightly below that in 1998. Increases are concentrated in computers and semiconductors, whereas other nonagricultural merchandise exports are projected to fall. Real exports increase 4-1/2 percent in 2000, as the pickup in foreign economic activity and the abatement of negative effects of earlier dollar appreciation boost the demand for U.S. products. Real imports of goods and services are expected to rise a still brisk 6 percent this year and 6-3/4 percent in 2000, reflecting steep uptrends in computers and semiconductors and the high income-elasticity of demand for other non-oil imports in this country. On balance, having subtracted 1-1/4 percentage points from real GDP growth in 1998, the drag from real net exports is projected to diminish to 3/4 percentage point this year and less than 1/2 percentage point in 2000. (A fuller discussion of the forecast for net exports is contained in the International Developments section.)

**Labor markets.** Labor productivity in the nonfarm business sector now appears to have risen rapidly in the fourth quarter of 1998 and about 2-1/2 percent for the year as a whole. Given the strength in the economy, a portion of this increase likely reflected "cyclical" influences; indeed, our models still generate an underlying productivity trend of 1-3/4 percent per year for the period since 1995, our standing assumption. But the recent performance is more impressive when one considers that many firms have had to divert worker hours to Y2K repairs. That thought, and the notion that

**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	2.4	1.4	1.8
Previous	1.7	1.8	1.3	1.9
Nonfarm payroll employment	2.7	2.3	1.7	1.2
Previous	2.7	2.3	1.3	.8
Employment, household survey	2.1	1.3	1.3	.9
Previous	2.1	1.2	.8	.5
Labor force participation rate <sup>1</sup>	67.1	67.1	67.2	67.2
Previous	67.1	67.1	67.0	66.9
Civilian unemployment rate <sup>1</sup>	4.7	4.4	4.3	4.4
Previous	4.7	4.5	4.7	4.9

1. Percent, average for the fourth quarter.

businesses have become adamant in cost control and more efficient in varying employment and hours, have led us to a marginally more optimistic view of productivity prospects. Growth in output per hour averages about 1.6 percent in 1999 and 2000, just a shade below trend, despite the significant slackening in GDP growth.

With firms maintaining this tight grip on payrolls, we expect increases in employment to diminish fairly promptly as output growth slows. After an increase of 2-1/4 percent in 1998, the growth in nonfarm payrolls slips to 1-3/4 percent this year and 1-1/4 percent in 2000. (In terms of monthly employment changes, this implies a moderation from an average of 240,000 per month in 1998 to about 175,000 in 1999 and 125,000 in 2000.) In view of the still abundant job opportunities, we have anticipated that the recent higher level of labor force participation will be sustained through the projection period; this represents a return to our earlier assessment of the trend, which we abandoned when the rate persistently fell short of our expectations after last winter. Welfare reform should help to buoy the participation rate, though there is some pessimism that the remaining recipients can be readily moved into jobs.

#### **The Outlook for Wages and Prices**

Recent anecdotal and statistical information has continued to portray the pattern that we have observed for some time: Tight labor markets are forcing firms to raise wage rates substantially in real terms, while competitive pressures are keeping prices pinned down, especially in markets for internationally traded goods. Going forward, the story is likely to be more of the same, although with some firms finding a tad more pricing leverage as the recent bottoming out of non-oil import prices evolves into a gradual uptrend.

The fourth-quarter ECI report showed less of an increase in hourly compensation than we expected. However, with the projection now showing no easing of the prevailing labor market tautness, we have raised our forecast of ECI compensation slightly for 1999 and 2000. Now, rather than decelerating from the 1998 pace, we foresee stability at about 3-1/2 percent this year and an uptick to 3-3/4 percent in 2000.

This forecast remains a somewhat awkward compromise between two basic models of wage determination. In one view, overly tight labor markets tend to generate ever larger increases in nominal wage inflation, with no direct influence from what is happening to prices and thus to real wages. In the other view, nominal wages are directly linked to prices, so that a lower rate of price inflation tends to hold down nominal wage increases, even though excess demand for labor does push up real wage increases. We have leaned

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

Measure	1997	1998	1999	2000
Consumer price index	1.9	1.5	2.3	2.4
Previous	1.9	1.6	2.3	2.2
Food	1.7	2.3	1.7	2.1
Previous	1.7	2.3	1.3	1.8
Energy	-1.0	-9.0	3.0	1.4
Previous	-1.0	-9.0	3.7	1.1
Excluding food and energy	2.2	2.4	2.3	2.6
Previous	2.2	2.4	2.3	2.3
PCE chain-weighted price index	1.5	.8	1.7	1.9
Previous	1.5	.8	1.7	1.7
Excluding food and energy	1.6	1.2	1.6	1.8
Previous	1.6	1.2	1.7	1.7
GDP chain-weighted price index	1.7	.9	1.5	1.9
Previous	1.7	.9	1.5	1.7
ECI for compensation of private industry workers <sup>1</sup>	3.4	3.5	3.5	3.7
Previous	3.4	3.6	3.3	3.3
Prices of core non-oil merchandise imports	-.7	-2.0	1.5	1.4
Previous	-.7	-2.0	1.5	1.4
	Percentage points			
MEMO: <i>Adjustments for technical     changes to the CPI</i> <sup>2</sup>				
Core CPI	.2	.4	.6	.6

1. December to December.

2. Adjustments are calculated relative to the methodological structure of the CPI in 1994.

in the direction of the “wage-price” model in our forecast because it has performed better over the years and has greater intuitive appeal: Employers’ and employees’ perceptions of appropriate wage increments undoubtedly are influenced to some degree by the rate of increase in the cost of living; in a small percentage of cases, there is still a contractual link.

But, in addition, we continue to note that a disproportionate share of the acceleration of compensation has occurred in commissions and bonuses (mainly for sales workers and in finance, insurance, and real estate) which bodes well for a moderating influence on overall pay gains as activity turns less robust. Indeed, reports from Wall Street suggest that bonuses will be down considerably, year-over-year, in the first quarter. Moreover, the broader adoption of "flexible pay" schemes suggests that there is a greater potential now than in the past for firms to respond quickly to the pressure on profits by trimming compensation gains. These considerations provide an offset to the likely compensation-raising effect of the step-up in health insurance premium costs that began to appear in 1998 and is reportedly going to be much more important this year and next.

On the price side, too, there is more than one way of looking at the inflationary tendencies. The low unemployment rate and the pressures of labor costs on profitability suggest that prices should be accelerating. Moreover, firmer non-oil import prices and the upturn in oil prices should have an inflationary effect. On the other hand, there are scarcely any signs at this point that prices are accelerating (aside from drugs--that is, tobacco and pharmaceuticals) and the performance of inflation would seem to be more in line with what one might expect if the more relevant measure of resource pressures is manufacturing capacity utilization. We have attempted to blend all these factors in formulating our forecast, ultimately giving preponderant weight to the extraordinary tightness of the labor market and to the turn in the dollar and import prices.

The bottom line is that we have prices accelerating substantially in 1999 and a little further in 2000. The upturn in oil prices leads to a considerable positive swing in retail energy prices in the next few quarters, a movement only marginally offset by some slackening in food price increases. Core consumer price increases, as measured by the CPI excluding food and energy, pick up from 2.4 percent in 1998 to 2.8 percent in 2000, on a consistently measured basis (that is, adding back in 0.2 percentage point for the damping effect of the switch this month to geometric mean weighting). The rate of increase in core PCE prices is forecast to rise from 1.2 percent in 1998 to 1.8 percent in 2000; the larger acceleration than in the core CPI reflects a return to more normal rates of increase in the prices of imputed financial services (which are outside the scope of the CPI) and a bigger contribution from rising health care costs (which have a larger weight in PCE).

Looking at the overall CPI, we project a pickup from the 1.5 percent increase in 1998 to 2.6 percent in 2000. We are expecting that the GDP chain price index will accelerate from just under 1 percent in 1998 to just under 2 percent

next year. The persistent gap primarily reflects the continuing relative price declines for private investment goods, especially computing equipment.

### **Money and Credit Flows**

The aggregate debt of domestic nonfinancial sectors is estimated to have grown at a 6-1/2 percent rate in the fourth quarter, lifting growth for the year to 6-1/4 percent--the fastest increase since 1990; in real terms, the rise last year was the most rapid in more than a decade. Households, businesses, and state and local governments all experienced a pickup in debt growth, with the market turmoil during the late summer and fall putting no discernible dent in the pace of total borrowing. We anticipate that nonfinancial debt growth will step down to just below 5 percent this year and to 4-1/4 percent in 2000, as federal debt contracts more rapidly than it did last year and debt growth gradually slows in each of the major nonfederal sectors. This projection implies only a small further rise in the ratio of total nonfinancial debt to nominal GDP, which jumped last year after an extended period of rough stability.

Judging from the still-wide yield spreads between corporate bonds and Treasuries, investors appear to be placing sizable odds on another market disruption or a severe worsening of credit quality. There are hints that corporate financial positions have weakened a bit of late, and we would not be surprised to see some further deterioration, given our forecast of slower economic growth and lower profits. But we think the market has priced in an overly bearish outlook for credit performance and thus expect risk spreads to narrow somewhat as the year unfolds--though to nowhere near the levels prevailing in the first half of 1998. We also expect banks to maintain tighter terms and standards on business loans than they had in place six months ago, but not to tighten much further. Consequently, we do not envision any constriction of credit that would greatly restrain business spending.

Nonfinancial business debt expanded more than 9 percent in 1998, boosted in part by the heavy volume of corporate bond issuance before midyear, as firms took advantage of the extremely receptive conditions in financial markets. In effect, some firms "pre-funded" their anticipated longer-term financing requirements, and we would expect the pace of bond offerings to move lower this year. Debt growth also should be tempered by the reduced reliance on credit for financing large mergers; although merger activity is still expected to be robust, the recently announced megadeals have been almost entirely structured as stock swaps. As a partial offset to these influences, the gap between capital spending and internal cash flow is expected to widen, increasing the demand for external finance. All told, we project that

nonfinancial business debt will grow at a rate of about 6-1/2 percent over the forecast period.

After increasing almost 9 percent last year, household debt is expected to rise 8 percent this year and about 7 percent in 2000. The gradual slowdown stems from the anticipated deceleration in outlays for durable goods and the slower pace of home sales. This projection keeps household debt growing faster than disposable income, causing the debt-service burden to rise over the forecast period, though the increase is tempered by the continued shift from consumer credit to longer-maturity mortgage debt. Despite the higher debt burden, we do not foresee the type of adverse income shock that would prompt serious payment difficulties and lead to a widespread tightening of credit conditions.

The debt of state and local governments, which expanded more than 7 percent in 1998, is projected to grow more moderately this year and next. Debt growth last year was boosted by a heavy flow of advance refundings, as governmental units moved to lock in long-term interest rates that touched the lowest levels since 1993. With fewer bonds now eligible for refunding, this component of bond issuance should be more subdued going forward. Nonetheless, issuance to fund new capital projects should remain strong, consistent with our outlook for substantial state and local expenditures on infrastructure.

The growth of the broad monetary aggregates over 1998 substantially exceeded their annual ranges, with M2 increasing 8-3/4 percent and M3 increasing 11 percent. The aggregates should decelerate this year, and partial data for January provide a sliver of support for this view. The case for slower growth in M2 continues to reflect factors we have cited for some time: the unwinding of safe-haven and liquidity demands, the projected downshift in nominal GDP growth, and the waning effect of last fall's policy easings on M2 opportunity costs. Although M3 should continue to grow more rapidly than M2, its increase is also projected to moderate, in part because of the slower expansion of bank credit. The velocities of both aggregates are expected to continue trending down through 2000, but at a pace that diminishes over time.

Clearly, in the forecasts of the monetary aggregates and other credit market developments, we are anticipating that--though the financial markets will have to digest some additional bad international news in the coming months--any disturbances will be less disruptive than those of the past year or two. In part, this projection reflects the judgment that the markets will be less stunned by the misfortunes contemplated here and, furthermore, that the markets will

be better prepared to absorb any shocks by dint of the deleveraging of positions that has occurred since last summer.

### Alternative Simulations

We have generated two alternative simulations for this Greenbook: A tighter monetary policy scenario and a higher stock market scenario.

In the tighter monetary policy scenario, the federal funds rate is raised 100 basis points between March and October and then held at that higher level for the balance of the projection period. Under these assumptions, real GDP growth is reduced 0.2 percentage point this year and 1.1 percent percentage points in 2000. The unemployment rate rises to close to 5 percent by the end of next year, and inflation in 2000 ends up 1/2 percentage point lower than in the baseline.

In the higher stock market simulation, the Wilshire 5000 is assumed to rise at a 10 percent annual rate from here. In this scenario, growth is slightly faster this year and about 1/2 percentage point more rapid in 2000. The unemployment rate edges down to 4.2 percent this year and holds at that level in 2000. Nonetheless, the effect of higher utilization rates on inflation is relatively muted: The core CPI in 2000 is only 0.1 percentage point higher than in the baseline--in part because, in contrast to the tightening of monetary policy in the first simulation, expectations about inflation are not quickly altered.

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

Measure	1999	2000
<i>Real GDP</i>		
Baseline	2.6	2.4
Tighter policy	2.4	1.3
Higher stock prices	2.8	3.0
<i>Civilian unemployment rate<sup>1</sup></i>		
Baseline	4.3	4.4
Tighter policy	4.4	4.9
Higher stock prices	4.2	4.2
<i>CPI excluding food and energy</i>		
Baseline	2.3	2.6
Tighter policy	2.3	2.1
Higher stock prices	2.3	2.7

1. Average for the fourth quarter.

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

January 28, 1999

Interval	Nominal GDP		Real GDP		GDP chain-weighted price index		Consumer price index <sup>1</sup>		Unemployment rate <sup>2</sup>		
	12/16/98	01/28/99	12/16/98	01/28/99	12/16/98	01/28/99	12/16/98	01/28/99	12/16/98	01/28/99	
<b>ANNUAL</b>											
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	4.8	4.9	3.7	3.8	1.0	1.0	1.6	1.6	4.5	4.5	
1999	3.8	4.5	2.5	3.1	1.3	1.3	2.2	2.1	4.5	4.3	
2000	3.6	4.1	2.0	2.3	1.6	1.8	2.2	2.4	4.8	4.4	
<b>QUARTERLY</b>											
1997	Q1	7.2	7.2	4.2	4.2	2.8	2.8	2.0	2.0	5.3	5.2
	Q2	5.6	5.6	4.0	4.0	1.7	1.7	1.5	1.5	4.9	5.0
	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	4.6
	Q2	2.7	2.7	1.8	1.8	0.9	0.9	2.0	2.0	4.4	4.4
	Q3	4.7	4.7	3.8	3.7	0.8	1.0	1.7	1.7	4.6	4.5
	Q4	4.2	6.0	3.1	5.0	1.0	1.0	2.0	2.0	4.5	4.4
1999	Q1	4.5	4.4	2.5	2.7	1.9	1.7	2.3	2.1	4.4	4.3
	Q2	3.0	3.9	1.7	2.4	1.3	1.4	2.4	2.4	4.5	4.3
	Q3	3.2	3.8	1.8	2.2	1.4	1.5	2.2	2.3	4.6	4.3
	Q4	3.6	4.5	2.2	2.9	1.4	1.5	2.2	2.3	4.7	4.3
2000	Q1	2.9	3.2	0.9	1.0	2.0	2.2	2.2	2.5	4.8	4.3
	Q2	4.5	4.8	2.8	3.0	1.6	1.8	2.2	2.4	4.8	4.4
	Q3	4.3	4.3	2.6	2.4	1.6	1.8	2.2	2.4	4.9	4.4
	Q4	4.3	4.8	2.7	2.9	1.6	1.8	2.2	2.4	4.9	4.4
<b>TWO-QUARTER<sup>3</sup></b>											
1997	Q2	6.4	6.4	4.1	4.1	2.2	2.2	1.8	1.8	-0.4	-0.3
	Q4	4.8	4.8	3.6	3.6	1.2	1.2	2.0	2.0	-0.2	-0.3
1998	Q2	4.6	4.6	3.7	3.7	0.9	0.9	1.2	1.2	-0.3	-0.3
	Q4	4.4	5.4	3.5	4.3	0.9	1.0	1.9	1.9	0.1	0.0
1999	Q2	3.7	4.1	2.1	2.5	1.6	1.6	2.3	2.3	-0.0	-0.1
	Q4	3.4	4.1	2.0	2.6	1.4	1.5	2.2	2.3	0.2	-0.0
2000	Q2	3.7	4.0	1.9	2.0	1.8	2.0	2.2	2.4	0.1	0.1
	Q4	4.3	4.6	2.6	2.7	1.6	1.8	2.2	2.4	0.1	-0.0
<b>FOUR-QUARTER<sup>4</sup></b>											
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	4.5	5.0	3.6	4.0	0.9	0.9	1.6	1.5	-0.2	-0.3
1999	Q4	3.6	4.1	2.1	2.6	1.5	1.5	2.3	2.3	0.2	-0.1
2000	Q4	4.0	4.3	2.3	2.4	1.7	1.9	2.2	2.4	0.2	0.1

1. For all urban consumers.

2. Level, except as noted.

3. Percent change from two quarters earlier; for unemployment rate, change in percentage points.

4. Percent change from four quarters earlier; for unemployment rate, change in percentage points.

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Class II FOMCREAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, ANNUAL VALUES  
(Seasonally adjusted annual rate)

January 28, 1999

Item	Units <sup>1</sup>	- - - Projected - - -								
		1992	1993	1994	1995	1996	1997	1998	1999	2000
<b>EXPENDITURES</b>										
Nominal GDP	Bill. \$	6244.4	6558.1	6947.0	7269.6	7661.6	8110.9	8506.7	8886.7	9251.4
Real GDP	Bill. Ch. \$	6244.4	6389.6	6610.7	6761.7	6994.8	7269.8	7547.2	7779.3	7957.2
Real GDP	% change	3.6	2.4	3.3	2.1	3.9	3.8	4.0	2.6	2.4
Gross domestic purchases		4.0	3.0	3.6	1.6	4.2	4.4	5.2	3.3	2.7
Final sales		3.9	2.1	2.7	2.7	3.7	3.4	4.4	2.5	2.4
Priv. dcm. final purchases		4.9	3.7	3.7	2.9	4.4	4.5	6.5	3.6	2.9
Personal cons. expenditures		4.2	2.7	3.1	2.6	3.3	3.7	5.2	3.5	2.8
Durables		9.4	7.4	6.3	4.5	5.8	7.4	12.6	3.6	3.5
Nondurables		3.4	1.6	3.0	1.7	2.8	2.0	4.5	3.5	2.3
Services		3.6	2.3	2.5	2.6	3.0	3.8	4.1	3.5	2.9
Business fixed investment		5.5	9.9	7.6	7.3	11.7	9.8	11.8	5.8	5.8
Producers' dur. equipment		9.6	12.2	10.2	9.1	11.8	12.7	16.8	8.4	7.7
Nonres. structures		-3.4	4.5	1.1	2.7	11.6	2.5	-0.9	-1.4	0.6
Residential structures		16.9	7.8	4.2	-1.4	5.4	4.2	13.2	0.2	-2.2
Exports		4.1	4.6	10.0	10.5	10.3	9.6	0.7	0.2	4.4
Imports		7.4	10.2	12.3	5.6	11.8	14.0	10.4	6.1	6.7
Gov't. cons. & investment		1.7	-1.4	0.1	-0.9	2.1	1.4	1.6	1.4	1.8
Federal		1.3	-6.1	-3.9	-5.6	1.1	-0.6	0.4	-1.7	-0.6
Defense		-1.3	-6.9	-6.0	-5.0	-0.1	-1.4	-1.9	-2.5	-0.5
State & local		2.0	2.0	2.7	2.1	2.8	2.6	2.3	3.1	3.1
Change in bus. inventories	Bill. Ch. \$	7.0	22.1	60.6	27.7	30.0	63.2	55.9	44.4	36.2
Nonfarm		2.0	29.5	49.0	37.7	23.2	58.8	48.2	39.4	33.7
Net exports		-29.5	-70.2	-104.6	-96.5	-111.2	-136.1	-240.9	-316.0	-370.8
Nominal GDP	% change	6.3	5.0	5.8	4.2	5.8	5.6	5.0	4.1	4.3
<b>EMPLOYMENT AND PRODUCTION</b>										
Nonfarm payroll employment	Millions	108.6	110.7	114.1	117.2	119.6	122.7	125.8	128.2	130.0
Unemployment rate	%	7.5	6.9	6.1	5.6	5.4	4.9	4.5	4.3	4.4
Industrial prod. index	% change	3.6	3.3	6.5	3.5	5.3	6.6	2.1	3.0	2.4
Capacity util. rate - mfg.	%	79.5	80.5	82.5	82.7	81.4	82.0	80.9	79.9	80.1
Housing starts	Millions	1.20	1.29	1.46	1.35	1.48	1.47	1.62	1.61	1.54
Light motor vehicle sales		12.85	13.86	15.01	14.72	15.05	15.02	15.50	15.30	14.95
North Amer. produced		10.51	11.71	12.88	12.82	13.35	13.09	13.47	13.28	13.04
Other		2.34	2.15	2.13	1.90	1.70	1.92	2.04	2.02	1.92
<b>INCOME AND SAVING</b>										
Nominal GNP	Bill. \$	6255.5	6576.8	6955.2	7287.1	7674.0	8102.9	8484.1	8844.0	9189.3
Nominal GNP	% change	6.2	5.1	5.7	4.4	5.6	5.2	4.8	3.9	4.2
Nominal personal income		7.2	4.0	5.2	4.6	5.9	5.4	5.1	4.3	4.5
Real disposable income		4.0	1.2	2.5	2.1	2.7	2.9	3.6	2.9	2.7
Personal saving rate	%	5.7	4.4	3.5	3.4	2.9	2.1	0.5	0.2	-0.1
Corp. profits, IVA & CCAdj.	% change	11.3	19.0	14.1	14.6	7.7	7.7	2.6	-3.9	1.7
Profit share of GNP	%	6.8	7.5	8.2	9.2	9.8	10.1	9.8	9.3	8.8
Excluding FR Banks		6.6	7.2	7.9	8.9	9.5	9.8	9.5	9.0	8.5
Federal surpl./deficit	Bill. \$	-280.9	-250.7	-186.7	-174.4	-110.3	-21.1	78.5	106.8	141.7
State & local surpl./def.		86.3	87.4	96.8	111.7	122.6	134.1	147.9	156.8	164.0
Ex. social ins. funds		18.3	19.7	27.9	37.0	52.2	66.0	80.4	89.3	96.5
Gross natl. saving rate	%	14.5	14.4	15.5	16.3	16.6	17.4	17.4	17.0	16.7
Net natl. saving rate		3.7	3.7	4.7	5.8	6.3	7.3	7.4	7.1	6.8
<b>PRICES AND COSTS</b>										
GDP chn.-wt. price index	% change	2.6	2.6	2.5	2.1	1.8	1.7	0.9	1.5	1.9
Gross Domestic Purchases		2.7	2.3	2.5	2.0	1.8	1.3	0.5	1.5	1.8
chn.-wt. price index		3.1	2.7	2.7	2.6	3.2	1.9	1.5	2.3	2.4
CPI		3.5	3.1	2.8	3.1	2.6	2.2	2.4	2.3	2.6
Ex. food and energy										
ECI, hourly compensation <sup>2</sup>		3.5	3.6	3.1	2.6	3.1	3.4	3.5	3.5	3.7
Nonfarm business sector										
Output per hour		3.5	-0.4	0.1	1.2	2.1	1.7	2.4	1.4	1.8
Compensation per Hour		4.5	1.6	2.1	2.8	3.7	3.9	4.0	3.9	4.0
Unit labor cost		1.0	2.0	2.0	1.6	1.6	2.1	1.5	2.5	2.3

1. Changes are from fourth quarter to fourth quarter.

2. Private-industry workers.

Strictly Confidential <FR>  
Class II FOMCREAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES  
(Seasonally adjusted, annual rate except as noted)

January 28, 1999

Item	Units	1996 Q1	1996 Q2	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2
<b>EXPENDITURES</b>											
Nominal GDP	Bill. \$	7495.3	7629.2	7703.4	7818.4	7955.0	8063.4	8170.8	8254.5	8384.2	8440.6
Real GDP	Bill. Ch. \$	6882.0	6983.9	7020.0	7093.1	7166.7	7236.5	7311.2	7364.6	7464.7	7498.6
Real GDP	% change	3.3	6.1	2.1	4.2	4.2	4.0	4.2	3.0	5.5	1.8
Gross domestic purchases		4.5	7.0	3.4	1.8	5.5	4.4	4.6	3.2	7.8	3.9
Final sales		3.6	5.4	0.9	5.1	2.9	2.7	5.8	2.1	4.3	4.6
Priv. dom. final purchases		5.1	6.2	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	6.1
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	5.3
Services		4.0	3.0	3.0	2.0	3.1	3.2	4.7	4.3	3.5	5.4
Business fixed investment		13.1	11.0	14.2	8.8	7.0	14.0	17.0	1.8	22.2	12.8
Producers' dur. equipment		15.7	12.3	16.2	3.2	8.3	22.8	18.8	2.2	34.3	18.8
Nonres. structures		6.4	7.4	8.9	24.5	3.9	-6.2	12.4	0.9	-4.9	-2.3
Residential structures		9.3	19.5	-1.7	-3.9	3.1	6.1	-0.4	8.2	15.6	15.0
Exports		3.7	5.8	2.1	32.0	8.3	15.5	10.6	4.4	-2.8	-7.7
Imports		13.1	13.5	13.6	7.0	18.6	17.9	13.5	6.3	15.7	9.3
Gov't. cons. & investment		3.2	7.1	-1.6	0.0	2.1	2.1	1.4	0.1	-1.9	3.7
Federal		8.0	8.1	-4.7	-6.3	-2.7	3.6	-1.2	-2.1	-8.8	7.3
Defense		7.2	8.1	-6.3	-8.3	-9.9	9.1	-1.8	-2.0	-18.5	9.9
State & local		0.5	6.5	0.3	3.8	4.9	1.3	2.9	1.3	2.1	1.8
Change in bus. inventories	Bill. Ch. \$	14.4	26.1	47.5	32.1	56.3	79.0	51.0	66.5	91.4	38.2
Nonfarm		10.4	15.2	38.6	28.7	56.2	72.1	44.0	62.7	85.9	29.9
Net exports		-95.5	-113.5	-140.1	-95.9	-121.5	-131.6	-142.4	-149.0	-198.5	-245.2
Nominal GDP	% change	5.7	7.3	3.9	6.1	7.2	5.6	5.4	4.2	6.4	2.7
<b>EMPLOYMENT AND PRODUCTION</b>											
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	%	5.5	5.5	5.3	5.3	5.2	5.0	4.9	4.7	4.6	4.4
Industrial prod. index	% change	2.8	9.6	5.5	3.5	6.6	6.0	7.2	6.6	1.6	2.8
Capacity util. rate - mfg.	%	80.9	81.6	81.8	81.3	81.6	81.7	82.1	82.5	81.8	81.2
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	15.02	15.07	16.08
North Amer. produced		13.44	13.46	13.33	13.16	13.41	12.68	13.20	13.08	13.12	14.09
Other		1.66	1.72	1.68	1.76	1.92	1.86	1.99	1.94	1.95	1.99
<b>INCOME AND SAVING</b>											
Nominal GNP	Bill. \$	7515.0	7643.3	7708.6	7829.0	7952.4	8062.3	8162.0	8234.9	8369.4	8421.8
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	2.6
Personal saving rate	%	3.2	2.6	3.1	2.6	2.4	2.6	1.7	1.7	1.2	0.4
Corp. profits, IVA & CCAdj.	% change	16.9	6.9	3.8	3.5	18.1	11.1	13.1	-9.2	4.2	-4.1
Profit share of GNP	%	9.8	9.8	9.8	9.7	10.0	10.1	10.3	10.0	9.9	9.7
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	74.4
State & local surpl./def.		117.3	129.1	122.3	121.7	128.4	130.1	136.6	141.4	140.2	141.3
Ex. social ins. funds		45.3	58.2	52.5	52.9	59.8	61.6	68.7	73.8	72.7	73.6
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
<b>PRICES AND COSTS</b>											
GDP chn.-wt. price index	% change	2.2	1.4	1.8	1.6	2.8	1.7	1.2	1.1	0.9	0.9
Gross Domestic Purchases		2.1	1.4	1.5	2.1	2.2	0.9	1.1	1.0	-0.2	0.4
chn.-wt. price index		3.2	3.7	2.6	3.3	2.0	1.5	1.8	2.3	0.5	2.0
CPI		2.5	2.5	2.7	2.7	2.2	2.6	1.9	2.1	2.4	2.6
Ex. food and energy											
ECI, hourly compensation <sup>1</sup>		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	0.3
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	3.7

1. Private-industry workers.

Strictly Confidential <FR>  
Class II FOMCREAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES  
(Seasonally adjusted, annual rate except as noted)

January 28, 1999

Item	Units	----- Projected -----									
		1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2	2000 Q3	2000 Q4
<b>EXPENDITURES</b>											
Nominal GDP	Bill. \$	8537.9	8664.1	8758.5	8841.7	8924.2	9022.2	9093.9	9202.2	9299.4	9410.0
Real GDP	Bill. Ch. \$	7566.5	7659.0	7709.5	7755.0	7798.1	7854.5	7874.5	7933.6	7981.3	8039.4
Real GDP	% change	3.7	5.0	2.7	2.4	2.2	2.9	1.0	3.0	2.4	2.9
Gross domestic purchases		4.2	4.8	3.8	3.3	2.8	3.1	1.6	3.5	2.8	2.9
Final sales		2.8	5.9	1.7	3.3	2.4	2.7	1.7	2.6	2.4	2.8
Priv. dom. final purchases		3.7	6.3	3.2	4.8	3.3	3.2	2.4	3.2	3.0	3.1
Personal cons. expenditures		4.1	4.7	2.7	4.2	3.5	3.5	2.5	3.2	2.7	2.8
Durables		2.4	22.2	-3.9	9.7	3.9	5.0	3.6	3.3	3.0	4.0
Nondurables		2.1	3.3	3.1	3.6	3.5	3.7	2.4	2.4	2.3	2.3
Services		5.4	2.0	4.0	3.4	3.3	3.1	2.3	3.6	2.8	2.8
Business fixed investment		-0.7	14.0	4.5	9.7	5.0	4.2	4.3	5.2	6.8	7.0
Producers' dur. equipment		-1.0	18.0	7.5	13.7	7.0	5.8	5.9	6.9	9.0	9.0
Nonres. structures		0.2	3.5	-3.6	-1.0	-0.5	-0.3	-0.1	0.4	0.6	1.4
Residential structures		9.9	12.5	7.9	0.9	-3.5	-4.2	-4.2	-2.0	-1.8	-1.0
Exports		-2.8	18.0	-6.7	0.8	2.3	4.8	0.5	4.2	5.3	7.8
Imports		2.3	14.7	3.0	8.5	7.0	6.0	5.4	7.9	7.5	6.2
Gov't. cons. & investment		1.5	3.1	0.8	2.0	1.6	1.4	2.2	2.8	1.6	0.9
Federal		-1.4	5.1	-3.5	-0.1	-1.2	-1.9	0.3	2.3	-1.4	-3.4
Defense		4.3	-0.9	-6.5	0.1	-1.6	-1.8	-1.3	-1.0	0.0	0.4
State & local		3.1	2.3	3.2	3.1	3.1	3.1	3.1	3.1	3.1	3.1
Change in bus. inventories	Bill. Ch. \$	55.7	38.2	58.6	39.8	36.8	42.3	27.7	36.9	38.7	41.6
Nonfarm		47.0	30.0	51.3	34.3	32.7	39.4	25.1	34.3	36.1	39.2
Net exports		-259.0	-261.0	-287.5	-311.8	-328.4	-336.2	-352.5	-368.2	-380.4	-382.3
Nominal GDP	% change	4.7	6.0	4.4	3.9	3.8	4.5	3.2	4.8	4.3	4.8
<b>EMPLOYMENT AND PRODUCTION</b>											
Nonfarm payroll employment	Millions	126.1	126.8	127.5	128.0	128.4	128.9	129.4	130.0	130.1	130.4
Unemployment rate	%	4.5	4.4	4.3	4.3	4.3	4.3	4.3	4.4	4.4	4.4
Industrial prod. index	% change	0.9	3.2	2.3	3.0	3.0	3.7	0.8	2.8	2.8	3.2
Capacity util. rate - mfg.	%	80.2	80.2	79.8	79.8	79.9	80.2	79.8	80.0	80.1	80.3
Housing starts	Millions	1.63	1.69	1.68	1.64	1.59	1.55	1.54	1.54	1.53	1.53
Light motor vehicle sales		14.55	16.31	15.06	15.61	15.30	15.23	15.10	15.00	14.85	14.86
North Amer. produced		12.55	14.11	12.98	13.57	13.31	13.27	13.19	13.09	12.93	12.93
Other		2.01	2.20	2.08	2.04	1.99	1.96	1.91	1.91	1.92	1.93
<b>INCOME AND SAVING</b>											
Nominal GNP	Bill. \$	8510.9	8634.2	8724.4	8803.1	8878.9	8969.6	9035.6	9140.8	9236.0	9344.6
Nominal GNP	% change	4.3	5.9	4.2	3.7	3.5	4.2	3.0	4.7	4.2	4.8
Nominal personal income		4.5	5.7	5.2	3.7	4.1	4.2	5.6	4.3	3.9	4.2
Real disposable income		3.2	4.5	5.5	1.7	2.1	2.2	4.7	2.2	1.8	2.1
Personal saving rate	%	0.2	0.2	0.9	0.3	-0.0	-0.3	0.2	-0.0	-0.2	-0.4
Corp. profits, IVA & CCAdj.	% change	3.2	7.6	-3.5	-4.8	-5.9	-1.5	-11.4	7.6	6.3	5.5
Profit share of GNP	%	9.7	9.8	9.6	9.4	9.1	9.0	8.7	8.7	8.8	8.8
Excluding FR Banks	%	9.4	9.5	9.3	9.1	8.9	8.7	8.4	8.5	8.5	8.5
Federal surpl./deficit	Bill. \$	92.0	88.7	82.4	102.1	116.5	126.2	115.4	133.2	153.0	165.3
State & local surpl./def.		148.7	161.6	155.5	156.5	155.6	159.5	162.9	163.7	164.0	165.2
Ex. social ins. funds		81.3	94.1	88.0	89.0	88.1	92.0	95.4	96.2	96.5	97.7
Gross natl. saving rate	%	17.3	17.3	17.5	17.1	16.8	16.6	16.6	16.6	16.7	16.7
Net natl. saving rate		7.3	7.4	7.6	7.2	6.9	6.7	6.8	6.8	6.9	6.9
<b>PRICES AND COSTS</b>											
GDP chn.-wt. price index	% change	1.0	1.0	1.7	1.4	1.5	1.5	2.2	1.8	1.8	1.8
Gross Domestic Purchases											
chn.-wt. price index		0.7	0.9	1.5	1.5	1.5	1.5	2.1	1.6	1.7	1.7
CPI		1.7	2.0	2.1	2.4	2.3	2.3	2.5	2.4	2.4	2.4
Ex. food and energy		2.3	2.3	2.7	2.1	2.2	2.3	2.6	2.6	2.6	2.6
ECI, hourly compensation <sup>1</sup>		4.4	2.9	3.2	3.5	3.6	3.6	3.6	3.7	3.7	4.0
Nonfarm business sector											
Output per hour		3.0	3.0	1.3	1.4	1.2	1.6	-0.4	2.5	2.3	2.7
Compensation per hour		4.1	3.4	4.2	3.8	3.8	3.8	4.4	3.8	3.8	4.2
Unit labor cost		1.1	0.4	2.9	2.4	2.6	2.1	4.8	1.3	1.5	1.5

1. Private-industry workers.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

January 28, 1999

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	1.8	3.7	3.9	3.8	4.0
Gross dom. purchases	3.5	1.9	5.5	4.4	4.7	3.2	7.9	4.0	4.3	4.2	4.4	5.2
Final sales	0.9	5.1	2.9	2.7	5.7	2.1	4.3	4.6	2.8	3.7	3.3	4.4
Priv. dom. final purchases	2.5	2.7	3.8	2.7	5.9	2.4	7.0	6.1	3.1	3.6	3.7	5.3
Personal cons. expenditures	1.3	2.0	2.9	1.1	4.2	1.9	4.1	4.1	2.8	2.2	2.5	3.5
Durables	-0.2	0.6	1.0	-0.1	1.3	0.3	1.2	0.9	0.2	0.5	0.6	1.0
Nondurables	0.2	0.6	0.7	-0.0	1.0	-0.1	1.4	1.0	0.4	0.6	0.4	0.9
Services	1.2	0.8	1.2	1.3	1.9	1.7	1.4	2.1	2.2	1.2	1.5	1.6
Business fixed investment	1.4	0.9	0.7	1.4	1.7	0.2	2.2	1.4	-0.1	1.2	1.0	1.2
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	-0.1	0.0	0.3	0.1	-0.0
Residential structures	-0.1	-0.2	0.1	0.2	-0.0	0.3	0.6	0.6	0.4	0.2	0.2	0.5
Net exports	-1.3	2.4	-1.2	-0.5	-0.5	-0.3	-2.2	-2.1	-0.6	-0.3	-0.6	-1.2
Exports	0.2	3.2	1.0	1.8	1.2	0.5	-0.3	-0.9	-0.3	1.2	1.1	0.1
Imports	-1.6	-0.9	-2.2	-2.2	-1.7	-0.8	-1.9	-1.2	-0.3	-1.4	-1.7	-1.3
Government cons. & invest.	-0.3	0.0	0.4	0.4	0.3	0.0	-0.3	0.6	0.3	0.4	0.3	0.3
Federal	-0.3	-0.4	-0.2	0.2	-0.1	-0.1	-0.6	0.4	-0.1	0.1	-0.0	0.0
Defense	-0.3	-0.4	-0.5	0.4	-0.1	-0.1	-0.8	0.4	0.2	-0.0	-0.1	-0.1
Nondefense	0.0	0.0	0.3	-0.2	0.0	-0.1	0.3	0.1	-0.3	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	-2.7	0.9	0.2	0.5	-0.4
Nonfarm	1.3	-0.5	1.5	0.9	-1.5	1.0	1.2	-2.8	0.9	0.1	0.5	-0.4
Farm	-0.1	-0.3	-0.2	0.4	0.1	-0.1	0.0	0.1	0.0	0.0	0.0	0.1

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

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	5.0	2.7	2.4	2.2	2.9	1.0	3.0	2.4	2.9	4.0	2.6	2.4
Gross dom. purchases	4.9	3.8	3.4	2.9	3.2	1.7	3.6	2.9	3.0	5.2	3.3	2.8
Final sales	5.9	1.7	3.3	2.4	2.7	1.7	2.6	2.3	2.8	4.4	2.5	2.4
Priv. dom. final purchases	5.3	2.7	4.0	2.8	2.7	2.0	2.7	2.5	2.7	5.3	3.0	2.5
Personal cons. expenditures	3.2	1.9	2.9	2.4	2.4	1.7	2.2	1.8	1.9	3.5	2.4	1.9
Durables	1.7	-0.3	0.8	0.3	0.4	0.3	0.3	0.2	0.3	1.0	0.3	0.3
Nondurables	0.6	0.6	0.7	0.7	0.7	0.5	0.5	0.4	0.4	0.9	0.7	0.5
Services	0.8	1.6	1.4	1.4	1.3	0.9	1.5	1.1	1.1	1.6	1.4	1.2
Business fixed investment	1.5	0.5	1.0	0.5	0.5	0.5	0.6	0.7	0.8	1.2	0.6	0.6
Producers' dur. equip.	1.4	0.6	1.1	0.6	0.5	0.5	0.6	0.7	0.7	1.3	0.7	0.6
Nonres. structures	0.1	-0.1	-0.0	-0.0	-0.0	-0.0	0.0	0.0	0.0	-0.0	-0.0	0.0
Residential structures	0.5	0.3	0.0	-0.2	-0.2	-0.2	-0.1	-0.1	-0.0	0.5	0.0	-0.1
Net exports	0.1	-1.1	-1.0	-0.7	-0.3	-0.6	-0.6	-0.4	-0.0	-1.2	-0.8	-0.4
Exports	1.9	-0.8	0.1	0.3	0.5	0.1	0.4	0.6	0.8	0.1	0.0	0.5
Imports	-1.8	-0.4	-1.1	-0.9	-0.8	-0.7	-1.0	-1.0	-0.8	-1.3	-0.8	-0.9
Government cons. & invest.	0.5	0.1	0.3	0.3	0.2	0.4	0.5	0.3	0.2	0.3	0.3	0.3
Federal	0.3	-0.2	-0.0	-0.1	-0.1	0.0	0.1	-0.1	-0.2	0.0	-0.1	-0.0
Defense	-0.0	-0.3	0.0	-0.1	-0.1	-0.0	-0.0	0.0	0.0	-0.1	-0.1	-0.0
Nondefense	0.3	0.0	-0.0	-0.0	-0.0	0.1	0.2	-0.1	-0.2	0.1	-0.0	-0.0
State and local	0.3	0.4	0.3	0.4	0.3	0.4	0.4	0.4	0.4	0.3	0.4	0.4
Change in bus. inventories	-0.8	1.0	-0.9	-0.1	0.3	-0.7	0.4	0.1	0.1	-0.4	0.0	-0.0
Nonfarm	-0.8	1.0	-0.8	-0.1	0.3	-0.7	0.4	0.1	0.1	-0.4	0.1	-0.0
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.

Item	Fiscal year <sup>5</sup>				1998				1999				2000			
	1997 <sup>a</sup>	1998 <sup>a</sup>	1999	2000	Q1 <sup>a</sup>	Q2 <sup>a</sup>	Q3 <sup>a</sup>	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>UNIFIED BUDGET</b>																
Not seasonally adjusted																
Receipts <sup>1</sup>	1579	1721	1802	1888	378	544	412	413	399	550	440	428	423	578	459	444
Outlays <sup>1</sup>	1601	1651	1701	1745	409	407	409	468	392	422	419	444	445	434	422	451
Surplus/deficit <sup>1</sup>	-22	70	101	144	-30	137	3	-55	7	128	20	-16	-21	143	37	-7
On-budget	-103	-29	-28	0	-53	87	3	-58	-49	71	9	-56	-49	81	25	-51
Off-budget	81	99	128	143	22	50	0	3	56	57	11	40	27	63	13	44
Surplus excluding deposit insurance <sup>2</sup>	-36	66	95	140	-31	136	2	-57	6	127	19	-16	-22	142	36	-8
<b>Means of financing</b>																
Borrowing	38	-51	-83	-148	26	-82	-29	32	3	-108	-11	5	11	-116	-48	-8
Cash decrease	1	5	-1	0	4	-45	33	21	-2	-14	-6	10	10	-25	5	20
Other <sup>3</sup>	-17	-24	-16	4	0	-10	-8	1	-8	-6	-3	1	1	-3	6	-5
Cash operating balance, end of period	44	39	40	40	28	72	39	18	19	34	40	30	20	45	40	20
Seasonally adjusted annual rate																
Receipts	1687	1818	1907	1982	1809	1838	1859	1888	1892	1914	1934	1958	1965	1991	2015	2040
Expenditures	1728	1761	1810	1850	1750	1764	1767	1800	1810	1812	1818	1831	1849	1858	1862	1875
Consumption expend.	458	458	470	481	451	464	459	467	471	472	471	470	482	487	486	482
Defense	306	301	304	308	293	303	303	304	304	305	304	303	309	309	310	311
Nondefense	152	157	166	173	158	161	156	163	167	167	167	167	173	177	176	172
Other expenditures	1270	1303	1340	1369	1299	1300	1308	1333	1339	1341	1346	1361	1367	1371	1376	1393
Current account surplus	-41	57	97	132	59	74	92	89	82	102	116	126	115	133	153	165
Gross investment	61	60	59	58	61	57	61	60	59	59	59	58	58	58	58	58
Current and capital account surplus	-102	-3	38	74	-2	18	31	28	24	43	58	68	57	75	95	107
<b>FISCAL INDICATORS<sup>4</sup></b>																
High-employment (HEB) surplus/deficit	-163	-101	-85	-43	-103	-85	-77	-94	-100	-81	-65	-56	-58	-40	-18	-7
Change in HEB, percent of potential GDP	-.8	-.8	-.2	-.5	-.5	-.2	-.1	.2	.1	-.2	-.2	-.1	0	-.2	-.2	-.1
Fiscal impetus (FI), percent, cal. year	-2.1	-1.8	2.2	-.7	-2.1	1.1	.4	.6	1.9	-.2	-.6	-.7	.1	.5	-.4	-.6

1. OMB's May 1998 surplus estimates (assuming the enactment of the President's proposals) are \$39 billion in FY98, \$54 billion in FY99 and \$61 billion in FY00. CBO's August 1998 baseline surplus estimates are \$63 billion in FY98, \$80 billion in FY99 and \$79 billion in FY00. 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, \$51 billion in FY99 and \$58 billion in FY00, and CBO's August baseline estimates are \$59 billion in FY98, \$76 billion in FY99 and \$76 billion in FY00.

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.

Change in Debt of the Domestic Nonfinancial Sectors  
(Percent)

Period <sup>1</sup>	Total <sup>2</sup>	Federal government <sup>3</sup>	Nonfederal						Memo: Nominal GDP
			Total <sup>4</sup>	Households			Business	State and local governments	
				Total	Home mortgages	Consumer credit			
<i>Year</i>									
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	5.8	7.7	5.5	14.1	6.7	-4.6	4.2
1996	5.3	4.0	5.8	7.7	8.0	7.9	5.2	-0.6	5.8
1997	5.3	0.6	7.0	6.9	7.5	4.3	7.5	5.3	5.6
1998	6.3	-1.4	8.9	8.7	9.2	6.2	9.5	7.2	5.0
1999	4.9	-2.9	7.3	8.0	8.6	5.6	6.9	5.5	4.1
2000	4.2	-4.4	6.5	7.1	7.7	4.0	6.3	5.0	4.3
<i>Quarter</i>									
1997:3	5.6	0.8	7.3	6.8	9.1	4.1	7.9	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	8.4	4.5	8.7	8.4	6.4
2	6.1	-1.9	8.6	8.4	9.1	5.1	9.4	6.9	2.7
3	5.9	-3.6	8.9	8.2	9.1	6.7	10.4	6.3	4.7
4	6.6	0.7	8.4	9.1	9.1	8.0	8.1	6.5	6.0
1999:1	5.0	-3.7	7.6	8.3	8.7	6.0	7.2	5.6	4.4
2	4.7	-3.2	7.0	7.9	8.4	6.0	6.4	5.3	3.9
3	4.8	-2.6	7.0	7.5	8.1	5.0	6.8	5.3	3.8
4	4.8	-2.5	6.9	7.4	8.0	5.0	6.6	5.2	4.5

Note. Quarterly data are at seasonally adjusted annual rates.

1. Data after 1998:Q3 are staff projections. Changes are measured from end of the preceding period to end of period indicated except for annual nominal GDP growth, which is calculated from Q4 to Q4.

2. On a monthly average basis, total debt is estimated to have grown 6.3 percent in 1998 and is projected to grow 5.2 percent in 1999 and 4.2 percent in 2000.

3. On a monthly average basis, federal debt is estimated to have grown -1.2 percent in 1998 and is projected to grow -2.6 percent in 1999 and -4.3 percent in 2000.

4. On a monthly average basis, nonfederal debt is estimated to have grown 8.8 percent in 1998 and is projected to grow 7.5 percent in 1999 and 6.6 percent in 2000.

Flow of Funds Projections: Highlights  
(Billions of dollars except as noted)

Category	Calendar year				Seasonally adjusted annual rates									
					1998				1999				2000	
	1997	1998	1999	2000	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	H1	H2
<i>Net funds raised by domestic nonfinancial sectors</i>														
1 Total	655.1	696.6	647.1	653.2	780.0	806.1	626.2	574.2	707.3	553.2	581.6	746.5	685.3	621.1
2 Net equity issuance	-114.4	-261.6	-149.0	-56.5	-139.2	-129.1	-299.2	-479.0	-96.0	-218.0	-218.0	-64.0	-63.0	-50.0
3 Net debt issuance	769.6	958.2	796.1	709.7	919.2	935.2	925.3	1053.2	803.3	771.2	799.6	810.5	748.3	671.1
<i>Borrowing sectors</i>														
<i>Nonfinancial business</i>														
4 Financing gap <sup>1</sup>	74.3	103.3	139.0	163.7	119.1	97.2	100.7	96.1	123.7	130.8	142.2	159.2	157.4	170.0
5 Net equity issuance	-114.4	-261.6	-149.0	-56.5	-139.2	-129.1	-299.2	-479.0	-96.0	-218.0	-218.0	-64.0	-63.0	-50.0
6 Credit market borrowing	334.8	452.2	362.2	351.4	417.8	457.4	517.9	415.6	375.8	340.7	366.7	365.7	350.6	352.1
<i>Households</i>														
7 Net borrowing <sup>2</sup>	355.6	478.1	479.2	456.5	437.2	469.8	471.2	534.3	498.4	483.4	465.1	470.1	463.8	449.3
8 Home mortgages	261.9	347.4	352.2	344.9	316.1	351.7	356.2	365.7	357.7	352.7	348.8	349.6	346.0	343.8
9 Consumer credit	52.5	78.6	75.4	57.2	57.3	65.1	86.7	105.3	80.6	81.8	69.2	70.0	61.3	53.1
10 Debt/DPI (percent) <sup>3</sup>	91.8	95.2	98.3	101.0	93.6	94.7	95.6	96.3	96.8	97.9	98.8	99.7	100.3	101.8
<i>State and local governments</i>														
11 Net borrowing	56.1	80.5	65.4	62.8	94.3	78.9	72.7	76.3	66.7	65.0	65.0	65.0	61.8	63.8
12 Current surplus <sup>4</sup>	135.6	184.6	189.6	199.3	179.1	169.4	191.5	198.4	187.9	183.5	191.2	195.8	198.5	200.1
<i>Federal government</i>														
13 Net borrowing	23.1	-52.6	-110.7	-160.9	-30.0	-70.9	-136.5	27.0	-137.6	-117.8	-97.2	-90.2	-127.8	-194.0
14 Net borrowing (quarterly, n.s.a.)	23.1	-52.6	-110.7	-160.9	25.9	-81.8	-28.8	32.1	2.9	-107.5	-11.0	4.9	-104.7	-56.2
15 Unified deficit (quarterly, n.s.a.)	2.4	-54.7	-139.9	-152.2	30.2	-136.9	-3.0	55.0	-7.3	-128.1	-20.2	15.6	-121.9	-30.3
<i>Depository institutions</i>														
16 Funds supplied	336.3	299.2	322.2	281.6	319.5	147.0	301.1	429.3	341.5	323.1	324.7	299.4	283.9	279.4
<i>Memo (percentage of GDP)</i>														
17 Domestic nonfinancial debt <sup>5</sup>	182.8	184.4	186.4	187.2	182.8	184.3	184.9	185.1	185.7	186.2	186.7	186.9	187.5	187.1
18 Domestic nonfinancial borrowing	9.5	11.3	9.0	7.7	11.0	11.1	10.8	12.2	9.2	8.7	9.0	9.0	8.2	7.2
19 Federal government <sup>6</sup>	0.3	-0.6	-1.2	-1.7	-0.4	-0.8	-1.6	0.3	-1.6	-1.3	-1.1	-1.0	-1.4	-2.1
20 Nonfederal	9.2	11.9	10.2	9.4	11.3	11.9	12.4	11.8	10.7	10.1	10.0	10.0	9.6	9.2

Note. Data after 1998:Q3 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.

## International Developments

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The staff projects that net exports will exert a greater drag on the U.S. economy during the forecast period than had been projected for the December Greenbook. Factors that have contributed to our reassessment include a considerably weaker outlook for Brazil; slower growth in the rest of Latin America; a stronger U.S. dollar, especially against currencies of emerging-market economies; and stronger U.S. growth. The depressing influence of net exports is still expected to wane during the forecast period.

Turmoil from events in Brazil has dominated international developments in the intermeeting period. So far, contagion from Brazil's problems has not been significant for countries outside Latin America, but the Brazilian situation is still highly uncertain and remains a key source of risk, not only for that country and others in the region but also for financial markets throughout the rest of the world. In Asia, there are signs that emerging-market economies hit by earlier crises may be bottoming out and even beginning to turn upward, but strengthening of the yen and higher long-term interest rates have damped Japan's prospects for recovery. In Europe, more signs of slower growth have increased pressure on the new European central bank for a near-term easing.

### Recent Developments

**International financial markets.** Since the December FOMC meeting, the dollar has appreciated about 1-3/4 percent on a weighted-average basis against a broad group of currencies. The largest gains have come against currencies of some emerging-market countries, as the economic crisis in Brazil has been a focus of market attention for much of the period. After several developments in Brazil had cast doubt on prospects for successful reform, the floating of the *real* on January 15 brought a lull in pressure on Brazilian financial markets. However, sizable outflows through the foreign exchange markets have continued. The latest decline of the *real* versus the dollar has brought the cumulative fall against the dollar during the period to over 35 percent. Following the devaluation of the *real*, the Mexican peso declined sharply but subsequently recovered most of its losses and now is down about 4 percent over the intermeeting period. Yield spreads for Brazilian Brady bonds are up about 300 basis points, and those of most other Latin American countries are up to a lesser extent. The influence of Brazil's problems on financial markets in emerging Asia have been largely contained so far, but these markets have been sensitive to sporadic rumors of possible devaluations in Hong Kong and China.

During the intermeeting period, the dollar is about unchanged on average against the major currencies. In early January, a steep decline in the dollar's value against the yen to its lowest level in two years was reversed after heavy intervention by the Bank of Japan. Initial appreciation of the euro after its fairly smooth introduction at the beginning of this month was offset by indications of a

weaker outlook in the euro area and growing conviction in the markets that the new European central bank may have to ease sooner than thought previously. As a result, the dollar is up on balance 2-1/4 percent so far this year against the new currency, and euro-denominated long-term government bond yields are down as much as 25 basis points. The dollar also has appreciated nearly 2-1/2 percent versus sterling, as the Bank of England cut official rates once again amid evidence of ongoing weakness in the U.K. economy. The dollar lost 1-1/2 percent against the Canadian currency, however, as energy prices turned up and signs of increased economic strength emerged in Canada.

**Economic activity abroad.** Economic activity appears to have weakened in most of the major foreign industrial countries. In Japan, the slightly brighter picture suggested by recent consumption indicators most likely arose from special factors and is not expected to persist, especially in view of deteriorating labor market conditions--including a record-high unemployment rate of 4.4 percent. Other indicators from the fourth quarter point to another contraction with negative momentum going forward. Evidence of a slowdown in the euro area has been most apparent in Germany (including weakness in November data for industrial production, orders, and business confidence), but signs of slower growth have emerged in other key euro-area countries as well. Business confidence elsewhere in the euro area also slipped sharply in the fourth quarter. Fourth-quarter data for the United Kingdom (including retail sales and a preliminary estimate of GDP growth at only 0.7 percent, s.a.a.r.) also have been soft. In contrast, Canada appears to be making a solid recovery from the effects of strikes in 1998.

Latest price data give no indication of inflationary pressure in foreign industrial countries. Twelve-month consumer price inflation in Japan moved up sharply in December to 0.7 percent, but the increase was due to special factors (largely the impact of typhoons on food supplies). The underlying trend of Japanese prices is still negative, and recent yen appreciation may have exerted additional downward pressure. Euro-area consumer prices (on a harmonized basis) have been rising at an average rate of only 1 percent, with the latest German and French CPI inflation at 1/2 percent or less. Since mid-year, U.K. inflation has been about 2-1/2 percent, the Bank of England's official target. At 1 percent, Canadian inflation is at the bottom end of the Bank of Canada's target range.

The recent turmoil in Latin American markets associated with the floating of the Brazilian *real* has come against a backdrop of weakening economic activity, in part the consequence of higher interest rates that had been raised to defend currencies. Third-quarter GDP fell about 6 percent (s.a.a.r.) in Brazil and quite likely contracted by a similar amount in the fourth quarter. Since the float, one-month interest rates in Brazil have moved up to more than 40 percent, with

overnight rates rising somewhat less. High interest rates not only have put the brakes on activity but also have compounded the task of reducing the budget deficit, because much of the outstanding stock of government debt is indexed to the overnight rate.

Growth also seems to have slowed sharply in Argentina and in Venezuela. After a robust third-quarter, the Mexican economy appears to have decelerated--and may even have contracted. Despite slower import growth as activity has weakened, trade deficits in all these countries have remained substantial because of adverse effects of lower commodity prices. Inflation has remained low in Argentina but has been much higher in Mexico and Venezuela (about 20 and 30 percent, respectively, in the fourth quarter). Inflation is expected to rise sharply in Brazil in response to the *real's* devaluation.

There are further signs that Korea may be starting to recover, including the second consecutive month of year-over-year increases in industrial production in December. Other ASEAN economies may be nearing troughs, although activity is still at depressed levels. Trade balances across the region have improved sharply during the past year owing primarily to reductions in imports, while export revenues have remained weak. Inflation in these countries generally has stabilized, but in many cases it is above pre-crisis rates. Increased investment by state-owned enterprises appears to have boosted Chinese growth. Russia has missed a payment on its debt to London Club creditors, and its latest draft budget falls well short of what the IMF has indicated is required to win further assistance.

**U.S. net exports and prices.** Although the November U.S. trade deficit in goods and services widened somewhat to \$15.5 billion, the combined October-November deficit was smaller than the third-quarter average. Exports in almost all major product categories declined in November from peak levels. An exception was automotive exports to Canada, which rose sharply. In October-November, however, the value of total U.S. exports was about 5 percent higher than the third-quarter average (not at an annual rate). Automotive, aircraft, and services exports were particularly strong. There were gains in shipments to Canada, Europe, and Asia--including China, Korea, and Taiwan--but exports to Latin America declined. After a slight rise in November, the combined October-November level of imports was about 3 percent higher than in the third quarter, supported by strong increases in automotive products from Canada and Mexico and in imported computers.

Prices of non-oil imports leveled off in December after edging up in October and November. In the fourth quarter, non-oil import prices fell only 1/2 percent (s.a.a.r.) from their third-quarter level, the smallest decline in two years. Prices

of imported “core” goods (which exclude agricultural products, computers, and semiconductors) rose 1/2 percent, the first increase since 1996:Q1. There were increases in all major categories of core goods except computers and non-oil industrial supplies. Prices of exported core goods decreased 1 percent in the fourth quarter, the smallest decline in a year. Total export prices were down 2 percent.

The spot price of West Texas intermediate (WTI) crude oil fell from \$12.94 per barrel in November to \$11.28 in December, driven by unexpectedly strong Iraqi exports as well as unseasonably warm weather and high inventories. Since then, the spot WTI price has moved back above \$12 per barrel.

### **Outlook**

The staff expects foreign real GDP (weighted by U.S. nonagricultural export shares) to grow only 0.9 percent during 1999, about the same pace as that in the second half of last year, and roughly half the 1.6 percent rate projected in the December Greenbook for 1999. Most of the change is the result of a substantial downward revision of our outlook for Latin American economies affected by the crisis in Brazil. Real GDP in Latin America now is projected to decline 2-1/2 percent (compared with our December forecast of positive 1 percent). Growth of foreign real GDP is projected to recover to about 2-1/4 percent during 2000, as Asian economies strengthen and most Latin American countries rebound. However, in light of the relatively contained global financial market reaction so far to developments in Brazil, we have not incorporated in the Greenbook forecast extreme contagion elsewhere in Latin America and have not assumed any significant spillovers to the emerging Asian economies. We project that U.S. real net exports will decline enough to subtract about 3/4 percentage point from U.S. GDP growth in 1999 and about 1/2 percentage point from growth in 2000.

**Summary of Staff Projections**  
(Percent change from end of previous period)

Measure	1998		Projection			
	H1	Q3	1998	1999		2000
			Q4	H1	H2	
Foreign output	-1	1.1	.9	.4	1.3	2.2
<i>December GB</i>	.0	1.3	.3	1.2	2.0	2.3
Real exports	-5.3	-2.8	18.0	-3.0	3.5	4.4
<i>December GB</i>	-5.3	-3.0	2.7	1.6	3.4	4.8
Real imports	12.5	2.3	14.7	5.7	6.5	6.7
<i>December GB</i>	12.5	1.8	7.8	6.6	5.3	6.2

**The dollar.** We continue to expect that expanding current account imbalances in the United States and Japan--as well as the large euro-area current account surplus--will exert downward pressure on the dollar over the forecast period. Accordingly, despite some projected easing of monetary policy in Europe (compared with a stance by the Federal Reserve that is assumed to be unchanged), the dollar is projected to decline 1/2 percent against the euro in 1999 and 2-1/2 percent in 2000. The dollar is assumed to remain flat against the yen at a level somewhat below its current value, as continuing uncertainty about prospects for recovery in Japan offset pressures from current account imbalances. Projected upward movement of commodity prices should support appreciation of the Canadian currency against the U.S. dollar--about 3-1/2 percent in 1999 and 2 percent more in 2000. We project, on balance, that the trade-weighted foreign exchange value of the dollar against the major currencies will decline 2-1/2 percent in 1999 and another 1-1/2 percent in 2000.

Against the currencies of a broad group of U.S. trading partners, the real exchange value of the dollar is projected to move up in the near term. The Brazilian *real* is assumed to move to a rate of 2 *real*/dollar shortly and remain at that level for the rest of the forecast period. As inflation in Brazil picks up later this year, we project the price-adjusted value of the *real* to rise. We are projecting a more modest depreciation of the Mexican peso in price-adjusted terms over the next two quarters that is sustained over the remainder of the forecast period. On balance, we expect that the price-adjusted value of the broad index will gain about 1/2 percent in 1999 and edge back a bit in 2000. As in the previous Greenbook forecast, we assume that Chinese authorities will begin to allow some modest depreciation of the renminbi at some point during the

forecast period, and we continue to assume that the Argentine and Hong Kong currency pegs will hold.

**Activity in foreign industrial countries.** Real GDP growth in foreign industrial countries is projected to rise from an annual rate of about 1-3/4 percent in the first half of this year to nearly 2 percent in the second half and in 2000--about unchanged from the December Greenbook projection. Recent data indicate a softer outlook for the euro area, where we expect growth to be close to 2 percent this year (about 1/4 percentage point less than forecast in December), with only a modest pickup in 2000. As a result, the euro-area output gap is expected to widen somewhat over the forecast period. Canada should register growth near 2-1/2 percent this year and in 2000. We have strengthened our forecast for Canadian growth this year by about 1/4 percentage point in view of recent signs of stronger activity as well as the more robust U.S. outlook.

The forecast for Japanese growth remains weak, although the outlook for the main components of GDP have been adjusted somewhat. The fiscal year 1999 budget apparently will generate a stronger fiscal impulse than had been expected previously, but recent data--including a record-high unemployment rate--suggest that private demand is slumping badly. Higher long-term interest rates, the stronger value of the yen, and continued worries about Japan's banking and financial problems likely will forestall any emergence of sustained recovery of private demand during the forecast period. These factors roughly offset one another in their impact on the 1999 outlook, but the forecast for growth in 2000 has been marked down about 1/4 percentage point. We estimate that Japanese GDP will register another sharp decline in 1999:Q1, and project that the economy will contract about 1/2 percent in both 1999 and 2000.

**Inflation.** Consumer price inflation in foreign industrial countries (on a four-quarter basis and weighted by U.S. non-oil import shares) is projected to be about 1/2 percent this year and to edge up to about 3/4 percent in 2000. These rates are slightly lower than those forecast for the December Greenbook and reflect a downward revision of the inflation outlook for Japan. We now expect Japanese consumer prices to fall at an annual rate of about 1-1/2 percent during the forecast period.

**Interest rates.** Signs of weaker activity in the euro area, as well as comments by euro-area monetary policy officials suggesting a greater willingness to accept an easing, have prompted a downward revision of the projected path for short-term euro-denominated interest rates. Short-term euro rates are expected to move down about 25 basis points during the first half of 1999, as the ESCB cuts its key policy rate by a similar amount sometime before midyear. The path for euro-denominated long-term interest rates has been lowered somewhat as

well, reflecting both recent market developments and the expected shift in the ESCB policy stance. Further declines in both official and market rates in the United Kingdom are expected in view of the weak U.K. outlook. In Japan, we anticipate that yen-denominated long-term rates will stay near their present level of 1-3/4 percent over most of the forecast period--about 65 basis points higher than projected for the previous Greenbook. This change reflects increases that occurred mainly in late December owing in part to the greater degree of fiscal stimulus in the 1999 budget.

**Other countries.** The outlook for growth in the major developing-country trading partners of the United States has been revised down significantly from the December Greenbook, reflecting the deteriorating situation in Brazil and its expected spillover to other emerging-market countries, especially those in Latin America. We now project that real GDP in the major developing countries will contract about 1/4 percent in 1999, compared with our projection of about 1-1/4 percent positive growth in the December Greenbook. In 2000, average growth in the developing countries is expected to recover to about 2-3/4 percent.

In Brazil, anticipated fallout from the collapse of the exchange rate--including continued high real interest rates, heightened economic uncertainty, a greater burden of payments on foreign-currency denominated debt, and severe pressures on the financial system--is projected to cause a nearly 8 percent fall in real GDP in 1999 (versus the roughly 3-1/4 percent fall projected in December). GDP in Argentina is expected to decline nearly 5 percent this year, reflecting the effects of higher real interest rates needed to defend the dollar peg and loss of exports to Brazil. Smaller declines in output this year are also expected in Mexico and Venezuela. In Latin America as a whole, real GDP is projected to contract 2-1/2 percent in 1999, down from a projection of about 1 percent positive growth in the December Greenbook. For 2000, we anticipate that growth in Latin America will recover to a rate of about 2 percent. Exchange rate depreciations in Brazil and other Latin American countries, especially Mexico, have boosted our projection of inflation in the region for 1999 to about 20 percent, with a deceleration to less than 15 percent in 2000.

Latest data tend to confirm our view that activity is bottoming out in the emerging Asian economies that suffered sharp declines in output last year. The Asian outlook has been marked down slightly from the December Greenbook, reflecting some anticipated adverse financial market spillover from the situation in Brazil and other Latin American countries. Nevertheless, we expect that, on average, real GDP growth in those countries will turn slightly positive in the first half of 1999 and reach 2 percent by the end of the year, with further acceleration in 2000.

**Real exports and imports of goods and services.** Recent monthly trade data have led us to raise our estimate of real exports of goods and services for the fourth quarter of last year. With exports revised up more than imports, we now project that real net exports will make essentially no contribution to GDP growth in the quarter, in contrast to the moderate negative contribution projected in December.

Looking beyond the fourth quarter, we have reduced our forecast for growth of real exports in light of our projection of weaker foreign growth this year and a stronger dollar than we predicted in the December Greenbook. Total exports are expected to decline at an annual rate of 3 percent in the first half of 1999 but to recover thereafter, reaching a nearly 4-1/2 percent growth rate in 2000. Exports of core goods (goods excluding agricultural products, computers, and semiconductors) will lag behind this pace.

After increasing at a brisk pace of over 14 percent (annual rate) in the fourth quarter of 1998, real imports of goods and services are expected to advance at a slower pace this year and next. We are now projecting total imports to increase at an annual rate of about 6 percent in 1999 and 6-3/4 percent in 2000. These are modest upward revisions from December, reflecting primarily the impact of a stronger outlook for the dollar and higher projected U.S. growth. Owing to the effects of low oil prices on domestic production, oil imports are estimated to have increased in the fourth quarter, and they should continue to rise throughout 1999 and 2000.

**Oil prices.** The staff has raised slightly the expected price of imported oil in the current quarter to reflect recent market developments, including supply disruptions from Nigeria, Russia, and Mexico. Thereafter in 1999, the projected path for the price of imported oil has been lowered because of our weaker outlook for foreign economic activity and a stronger dollar. Higher inventories and more production from Iraq than expected previously also will put downward pressure on oil prices. After a decline from an estimated price of \$11.42 per barrel in the fourth quarter, the staff projects that the price of imported oil will increase steadily from around \$10.50 in the current quarter to about \$13.00 in the fourth quarter of this year. For 2000, the staff predicts an oil import price of \$13.50 per barrel, a projection unchanged from the December Greenbook.

### Selected Trade Prices

(Percent change from end of previous period  
except as noted; seasonally adjusted)

Trade category	1998		Projection				2000
			1998	1999			
	H1	Q3	Q4	H1	H2		
<i>Exports</i>							
Nonagricultural (core)	-2.1	-2.3	-1.1	1.4	1.8	1.7	
Agricultural	-11.0	-7.8	-7.2	1.6	1.6	2.0	
<i>Imports</i>							
Non-oil (core)	-2.6	-3.1	.4	1.8	1.3	1.4	
Oil (level, dollars per barrel)	12.51	11.59	11.40	11.61	12.97	13.50	

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.

**Prices of non-oil imports and exports.** After recording negative rates for the past three years, core import price inflation should increase to 1-3/4 percent (s.a.a.r.) in the first half of 1999 and then slow to 1-1/2 percent in 2000 as the effects of dollar depreciation wane. Some delayed effects from earlier dollar appreciation may tend to counteract the passthrough of more recent dollar weakness to import prices. Movements of commodity prices should be smaller than in 1998. After falling more than 13 percent last year and contributing importantly to lower import prices, commodity prices are expected to increase about 2 percent in 1999 and 2000, with little projected impact on prices of core imports. After falling about 1 percent in the fourth quarter, core export prices are expected to rise at an annual rate of about 1-1/2 percent.

**Nominal trade and current account balances.** The nominal trade deficit for goods and services is projected to widen significantly during the forecast period, from about \$180 billion (annual rate) in the fourth quarter of 1998 to about \$275 billion in 2000. The deficit for net investment income also is projected to widen. As a result, the current account deficit is expected to expand from a \$255 billion annual rate in the fourth quarter of last year (3 percent of GDP) to \$375 billion for the year 2000 (4 percent of GDP and nearly 1/2 percentage point above the previous peak for this ratio reached in 1987).

### **Risks to the Foreign Outlook**

Although the Brazilian government has taken several significant steps to deal with Brazil's long-term fiscal problems, the situation there remains tenuous. Investor confidence about the government's ability to meet its economic policy objectives appeared to have been restored to some degree by the floating of the *real* in mid-January, but financial market pressures have returned. The staff's current outlook has been modified to incorporate the resulting decline of the *real* and other related developments that had been part of a worse-case scenario prepared for the December Greenbook.

Our current outlook has significant risks on both sides. It is closer to a balanced view than the December Greenbook forecast, which assumed Brazil's peg would hold. In our baseline forecast this time, we have assumed that fiscal restraint, higher interest rates, larger debt burden, and market disruptions contribute to a sharp contraction of GDP in Brazil this year, with a further modest decline in 2000. Other countries in Latin America are projected to experience negative spillover effects, while effects elsewhere are fairly modest. In particular, contagion to Asian emerging economies and other potentially vulnerable countries is assumed to be limited.

Two plausible alternative scenarios from the wide range of possible outcomes provide a sense of the risks to the outlook. (Neither case represents a "worst" or a "best" outcome.) The implications of these alternatives for U.S. real GDP and consumer prices are summarized in the table below. In the more pessimistic scenario, the severe Brazilian contraction worsens with more contagion to other emerging markets in Latin America and Asia. Risk spreads widen and equity markets in industrial countries experience significant declines with depressing effects on growth. In contrast, in an optimistic scenario, the Brazilian Congress and other authorities exhibit enough fiscal restraint to reassure markets. The *real* bounces back, allowing nominal and real interest rates to decline in Brazil and growth to begin to recover--with commensurate effects in the rest of Latin America. Other countries, including emerging economies in Asia and industrial countries, experience some positive spillovers including a boost to equity prices.

**Impact of Alternative Assumptions**

(Percent change, Q4 to Q4)

Measure	1999	2000
<i>U.S. real GDP</i>		
Baseline	2.6	2.4
Pessimistic Brazil <sup>1</sup>	1.8	1.5
Optimistic Brazil <sup>2</sup>	3.1	2.9
<i>U.S. CPI excluding food and energy</i>		
Baseline	2.3	2.4
Pessimistic Brazil <sup>1</sup>	2.1	1.9
Optimistic Brazil <sup>2</sup>	2.4	2.6

NOTE. All simulations assume fixed federal funds rate.

1. Assumes U.S. stock market falls an additional 20 percent.

2. Assumes U.S. stock market rises an additional 10 percent.

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
<b>REAL GDP (1)</b>									
-----									
Total foreign	2.2	3.3	5.1	2.0	4.1	4.1	0.5	0.9	2.2
Industrial Countries	0.7	1.8	4.0	1.7	2.6	3.3	1.6	1.8	1.9
of which:									
Canada	0.9	2.9	5.5	1.1	1.7	4.4	2.3	2.5	2.4
Japan	0.1	0.5	0.9	2.5	5.1	-0.8	-2.7	-0.6	-0.4
United Kingdom	0.7	3.2	4.6	1.9	2.6	4.0	1.6	1.0	2.0
Euro-11	0.1	-0.1	3.4	1.3	1.9	3.1	2.5	2.1	2.2
Germany	0.9	-0.2	3.4	0.0	2.1	2.3	2.4	1.9	2.3
Developing Countries	4.6	5.4	6.8	2.5	6.3	5.1	-1.0	-0.3	2.7
Asia	6.8	8.2	8.6	6.7	7.0	5.0	-3.2	1.0	3.1
Korea	2.4	8.1	9.5	7.3	7.1	3.9	-6.6	1.0	3.1
China	15.0	12.0	14.8	8.1	9.4	7.9	9.2	5.9	6.8
Latin America	3.0	2.6	5.6	-4.1	6.2	5.9	1.5	-2.4	2.2
Mexico	2.8	1.9	5.2	-7.0	7.1	6.7	3.2	-0.9	2.7
Brazil	0.1	4.4	9.6	-1.5	5.0	1.6	-1.0	-7.8	-1.0
<b>CONSUMER PRICES (2)</b>									
-----									
Industrial Countries	2.0	2.1	1.1	1.3	1.5	1.6	1.0	0.5	0.7
of which:									
Canada	1.8	1.8	-0.0	2.1	2.0	1.0	1.1	1.3	1.5
Japan	0.9	1.2	0.8	-0.8	0.1	2.1	0.7	-2.0	-1.4
United Kingdom (3)	3.7	2.7	2.2	2.9	3.2	2.8	2.6	2.4	2.5
Euro-11 (4)	NA	NA	NA	2.7	2.0	1.4	0.9	1.4	1.4
Germany	3.4	4.2	2.6	1.7	1.4	1.8	0.6	1.1	1.2
Developing Countries	21.7	24.8	23.1	17.0	11.2	6.9	8.9	8.9	7.7
Asia	5.5	7.7	10.8	6.4	4.8	2.8	4.6	2.6	4.4
Korea	4.7	5.5	5.8	4.4	5.1	5.0	6.0	3.0	2.6
China	8.2	17.1	26.9	11.1	7.0	1.0	-1.1	0.1	3.6
Latin America	72.4	74.5	54.6	42.2	26.0	15.6	15.7	20.5	13.4
Mexico	13.2	8.6	6.9	48.8	28.1	17.2	17.6	20.5	13.5
Brazil	1150.1	2321.7	1237.1	22.5	10.5	4.2	2.7	24.6	12.7

1. Foreign GDP aggregates calculated using shares of U.S. non-agricultural exports.
2. Foreign CPI aggregates calculated using shares of U.S. non-oil imports.
3. CPI excluding mortgage interest payments, which is the targeted inflation rate.
4. Harmonized CPI's, 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 changes)

Measure and country	1998				----- Projected -----				2000			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
REAL GDP (1)	----- Quarterly changes at an annual rate -----											
Total foreign	-0.9	0.8	1.1	0.9	0.3	0.5	1.1	1.5	1.6	2.2	2.4	2.6
Industrial Countries	1.9	1.2	1.3	1.9	1.7	1.7	1.7	2.0	1.4	1.9	2.1	2.2
of which:												
Canada	3.1	1.4	1.8	3.0	2.6	2.4	2.4	2.7	2.0	2.4	2.6	2.8
Japan	-4.8	-2.9	-2.6	-0.5	-1.1	-0.6	-0.6	-0.2	-1.3	-0.2	-0.0	-0.0
United Kingdom	1.9	2.0	1.6	0.7	0.9	0.9	1.0	1.4	1.4	1.9	2.4	2.4
Euro-11	3.2	2.3	2.7	1.6	1.8	2.0	2.1	2.4	1.7	2.3	2.3	2.3
Germany	5.9	0.2	3.5	0.2	1.0	1.8	2.3	2.6	1.9	2.4	2.4	2.4
Developing Countries	-4.6	0.2	0.8	-0.5	-1.5	-0.9	0.3	0.9	2.0	2.6	2.9	3.1
Asia	-9.8	-3.3	-0.3	0.9	-0.2	0.6	1.4	2.2	2.2	2.9	3.5	3.8
Korea	-22.8	-5.1	2.3	1.5	0.5	0.5	1.0	2.0	1.7	2.5	3.5	4.5
China	7.2	6.6	10.8	12.4	5.2	6.0	6.0	6.5	6.3	7.0	7.0	7.0
Latin America	1.0	4.7	2.7	-2.4	-3.8	-3.4	-1.4	-1.0	1.9	2.3	2.3	2.3
Mexico	1.0	6.1	7.7	-1.6	-2.0	-1.6	0.1	-0.0	2.5	2.8	2.9	2.8
Brazil	2.1	5.4	-5.9	-5.0	-10.0	-10.0	-6.0	-5.0	-1.0	-1.0	-1.0	-1.0
CONSUMER PRICES (2)	----- Four-quarter changes -----											
Industrial Countries	1.4	1.1	0.8	1.0	0.9	0.6	0.6	0.5	0.5	0.5	0.7	0.7
of which:												
Canada	1.0	1.0	0.9	1.1	1.2	1.2	1.3	1.3	1.4	1.4	1.5	1.5
Japan	2.1	0.6	-0.1	0.7	-0.2	-1.1	-1.4	-2.0	-2.0	-2.0	-1.5	-1.4
United Kingdom (3)	2.5	3.0	2.6	2.6	2.5	2.4	2.4	2.4	2.5	2.4	2.5	2.5
Euro-11 (4)	1.2	1.5	1.2	0.9	1.2	1.2	1.3	1.4	1.4	1.4	1.4	1.4
Germany	1.2	1.3	0.8	0.6	0.7	0.9	1.0	1.1	1.2	1.2	1.2	1.2
Developing Countries	7.3	7.6	8.0	8.9	8.7	9.3	9.4	8.9	8.3	7.8	7.7	7.7
Asia	4.2	4.7	4.6	4.6	3.1	2.8	2.5	2.6	3.3	3.6	4.0	4.4
Korea	8.9	8.2	7.0	6.0	1.1	1.7	2.7	3.0	3.3	3.1	2.8	2.6
China	0.4	-0.9	-1.4	-1.1	-0.5	0.9	0.8	0.1	0.6	1.4	2.4	3.6
Latin America	14.1	14.2	14.3	15.7	17.9	20.2	21.4	20.5	16.8	14.7	13.9	13.4
Mexico	15.3	15.1	15.6	17.6	19.9	21.7	22.2	20.5	16.4	14.7	14.1	13.5
Brazil	4.4	4.5	3.6	2.7	6.2	14.0	20.6	24.6	21.9	15.3	12.7	12.7

1. Foreign GDP aggregates calculated using shares of U.S. non-agricultural exports.
2. Foreign CPI aggregates calculated using shares of U.S. non-oil imports.
3. CPI excluding mortgage interest payments, which is the targeted inflation rate.
4. Harmonized CPI's, 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	----- 1998	Projected 1999	----- 2000
<b>NIPA REAL EXPORTS and IMPORTS</b>									
Percentage point contribution to GDP growth, Q4/Q4									
Net Goods & Services	-0.4	-0.6	-0.4	0.5	-0.3	-0.6	-1.2	-0.8	-0.4
Exports of G&S	0.4	0.5	1.0	1.1	1.2	1.1	0.1	0.0	0.5
Imports of G&S	-0.8	-1.1	-1.4	-0.7	-1.4	-1.7	-1.3	-0.8	-0.9
Percentage change, Q4/Q4									
Exports of G&S	4.1	4.6	10.0	10.5	10.3	9.6	0.7	0.2	4.4
Services	-0.9	4.1	6.0	9.8	7.5	1.5	-0.3	0.6	1.9
Agricultural Goods	10.4	-5.5	16.6	-4.3	4.8	2.8	-3.4	-9.2	0.2
Computers	25.2	23.7	32.0	55.5	35.9	40.7	5.9	24.2	28.2
Semiconductors	64.8	32.9	66.9	79.6	46.2	21.0	6.8	21.6	23.6
Other Goods 1/	2.3	3.6	7.0	5.8	8.0	11.6	0.9	-2.4	2.6
Imports of G&S	7.4	10.2	12.3	5.6	11.8	14.0	10.4	6.1	6.7
Services	1.4	3.2	1.4	6.1	5.5	12.4	3.8	3.4	3.1
Oil	12.1	10.1	-0.2	2.4	7.9	4.0	9.6	1.1	5.1
Computers	45.1	39.3	44.8	48.1	24.4	30.3	29.1	28.5	28.4
Semiconductors	42.0	34.2	54.5	92.4	57.6	32.7	-8.3	26.2	27.4
Other Goods 2/	5.4	9.5	12.2	-1.2	10.4	13.0	11.2	4.4	4.9
Billions of chained 1992 dollars									
Net Goods & Services	-29.5	-70.2	-104.6	-96.5	-111.2	-136.1	-240.9	-316.0	-370.8
Exports of G&S	639.4	658.2	712.4	792.6	860.0	970.0	983.8	996.1	1028.8
Imports of G&S	669.0	728.4	817.0	889.0	971.2	1106.1	1224.8	1312.1	1399.7
Billions of dollars									
US CURRENT ACCOUNT BALANCE	-51.4	-86.1	-123.8	-115.3	-134.9	-155.2	-229.0	-309.6	-374.1
Net Goods & Services (BOP)	-38.7	-71.9	-100.9	-99.9	-108.6	-110.2	-170.2	-230.4	-275.5
Exports of G&S (BOP)	617.3	643.2	703.8	795.6	850.8	937.6	931.6	938.0	975.8
Imports of G&S (BOP)	656.0	715.2	804.7	895.5	959.3	1047.8	1101.8	1168.4	1251.4
Net Investment Income	22.5	23.9	16.5	19.3	14.2	-5.3	-17.2	-37.4	-56.8
Direct, Net	51.6	55.7	51.8	63.0	66.2	63.7	56.8	41.2	38.8
Portfolio, Net	-29.1	-31.7	-35.3	-43.7	-51.9	-69.1	-74.1	-78.6	-95.7
Net Transfers	-35.2	-38.1	-39.4	-34.6	-40.6	-39.7	-41.5	-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
<b>NIPA REAL EXPORTS and IMPORTS</b>												
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	8.1
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 -----				----- 2000 -----			
	1998		1999		1999		2000		2000		2000	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>NIPA REAL EXPORTS and IMPORTS</b>												
	Percentage point contribution to GDP growth											
Net Goods & Services	-2.3	-2.1	-0.6	0.1	-1.1	-1.0	-0.7	-0.3	-0.6	-0.6	-0.4	-0.0
Exports of G&S	-0.3	-0.9	-0.3	1.9	-0.8	0.1	0.3	0.5	0.1	0.4	0.6	0.8
Imports of G&S	-1.9	-1.2	-0.3	-1.8	-0.4	-1.1	-0.9	-0.8	-0.7	-1.0	-1.0	-0.8
	Percentage change from previous period, SAAR											
Exports of G&S	-2.8	-7.7	-2.8	18.0	-6.7	0.8	2.3	4.8	0.5	4.2	5.3	7.8
Services	-1.2	1.7	-10.4	9.9	-0.2	0.8	0.7	0.9	1.1	2.1	2.2	2.4
Agricultural Goods	-9.9	-23.4	-14.5	47.7	-34.7	-7.8	11.2	1.7	-6.8	-2.7	8.3	2.6
Computers	-15.5	8.7	20.6	13.6	20.4	23.9	26.2	26.2	27.2	28.2	28.6	28.6
Semiconductors	-2.0	-18.7	29.6	26.2	21.6	21.6	21.6	21.6	22.7	23.9	23.9	23.9
Other Goods 1/	-1.7	-11.0	-1.2	19.7	-10.5	-1.6	-0.8	4.1	-2.8	2.4	3.3	8.0
Imports of G&S	15.7	9.3	2.3	14.7	3.0	8.5	7.0	6.0	5.4	7.9	7.5	6.2
Services	9.3	-0.6	-0.6	7.7	2.1	3.4	3.8	4.4	1.6	4.2	3.0	3.7
Oil	8.8	41.4	-5.7	-0.4	-18.2	40.1	10.1	-17.2	0.2	28.8	13.0	-16.3
Computers	38.8	22.4	9.8	49.1	31.1	29.1	27.7	26.3	26.3	28.7	29.1	29.6
Semiconductors	9.9	-28.0	-10.4	0.0	26.2	26.2	26.2	26.2	26.7	27.2	27.7	28.2
Other Goods 2/	16.1	10.7	3.4	15.3	1.3	5.7	5.1	5.5	3.9	4.8	5.5	5.5
	Billions of chained 1992 dollars, SAAR											
Net Goods & Services	-198.5	-245.2	-259.0	-261.0	-287.5	-311.8	-328.4	-336.2	-352.5	-368.2	-380.4	-382.3
Exports of G&S	991.9	972.1	965.3	1006.0	988.8	990.9	996.6	1008.2	1009.6	1019.9	1033.2	1052.6
Imports of G&S	1190.4	1217.3	1224.3	1267.0	1276.3	1302.7	1325.0	1344.4	1362.1	1388.1	1413.6	1434.9
	Billions of dollars, SAAR											
US CURRENT ACCOUNT BALANCE	-186.9	-226.8	-246.0	-256.2	-271.4	-299.9	-321.0	-346.2	-355.2	-370.4	-380.3	-390.7
Net Goods & Services (BOP)	-140.0	-175.5	-183.8	-181.6	-203.5	-227.5	-241.9	-248.8	-263.2	-275.2	-283.1	-280.6
Exports of G&S (BOP)	946.2	922.3	909.8	948.1	928.4	932.2	939.5	952.0	955.0	966.5	980.7	1001.2
Imports of G&S (BOP)	1086.2	1097.8	1093.6	1129.7	1131.9	1159.7	1181.4	1200.8	1218.2	1241.7	1263.8	1281.8
Net Investment Income	-9.0	-13.5	-21.8	-24.6	-28.8	-33.3	-40.1	-47.4	-53.0	-56.2	-58.2	-60.1
Direct, Net	62.4	60.7	54.7	49.6	45.1	43.0	39.7	37.1	36.3	37.2	39.7	42.1
Portfolio, Net	-71.3	-74.2	-76.6	-74.2	-73.9	-76.3	-79.8	-84.6	-89.2	-93.3	-97.9	-102.2
Net Transfers	-37.9	-37.8	-40.3	-50.0	-39.0	-39.0	-39.0	-50.0	-39.0	-39.0	-39.0	-50.0

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