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CONFIDENTIAL (FR)

February 11, 1976

SUMMARY AND OUTLOOK

By the Staff  
Board of Governors  
of the Federal Reserve System

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## **SUMMARY AND OUTLOOK**

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DOMESTIC NONFINANCIAL DEVELOPMENTS

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Summary. The year-end acceleration of economic activity has been extended into January. Consumer confidence has improved and retail sales have remained at advanced levels. Industrial production continued to rise last month; employment increased strongly, and the unemployment rate moved sharply downward. Conditions in financial markets remain relatively easy, and the general atmosphere seems conducive to a good rate of economic expansion over the next several quarters. However, there has been no evidence as yet of a strong upturn of business capital spending.

Industrial production is estimated to have risen by more than 1/2 a per cent in January. Gains last month were apparently widespread, with the strongest increase in production of nondurable materials, where inventories had been run down. Smaller gains occurred in production of consumer goods and business equipment.

Nonfarm payroll employment in January expanded by 360,000-- following a 210,000 rise in December. In addition, the factory workweek was increased by one-tenth of an hour, after a four-tenths rise in the previous month. Total employment as measured by the household series rose 800,000, and the unemployment rate was reduced by half a point to 7.3 per cent. The unusual strength of labor market data in January may result partly from difficulties of seasonal adjustment, but there has clearly been further improvement in labor market conditions.

Consumer markets remained relatively bouyant in January. Retail sales excluding autos and nonconsumption items increased by 0.3 per cent further following a strong (but downward revised) December increase. Gains in January occurred in furniture and appliances, food and apparel outlets.

Unit sales of autos also rose further in January--to an 8.4 million annual rate for domestic-type models, up from 8.2 million in December. Some of the strength of domestic cars was at the expense of imports, whose sales fell to a 1.2 million annual rate, or 13 per cent of the market. In 1975, unit sales of imports totaled 1.6 million, accounting for 18 per cent of sales.

The Conference Board reported a further strong improvement of consumer confidence in early December. Consumers were more optimistic about current employment and business conditions, as well as about the outlook for 6 months ahead.

Housing starts in December edged off for the second month in a row. For the fourth quarter as a whole, however, starts averaged 1.37 million units, 9 per cent above the third quarter and 40 per cent above the first quarter trough. Moreover, loan commitments at savings and loan associations have moved higher; mortgage interest rates have edged down; home sales have risen; and vacancy rates are down--all suggesting further improvement in residential construction activity in upcoming quarters.

Nonfarm inventories apparently were still being liquidated toward year end, although at a slower rate than earlier. The book value of manufacturers' inventories rose at a \$1-1/2 billion annual rate in December, about the same as for the fourth quarter as a whole, compared to a \$6-1/2 billion rate of decline in the third quarter. Manufacturers' inventories of nondurables have been reduced to quite a low level, and attempts are being made to build stocks. But inventory-shipments ratios remain quite high for durables, and liquidation of those goods is continuing. Meanwhile, in retail trade--where stocks are also quite low--the strength of sales in December may have resulted in an unintended further reduction of inventories, suggesting continuing improvement in orders and production in coming months.

Business demand for capital appears to have bottomed out, but there is still no convincing evidence that a substantial upturn is in the making. In real terms, business fixed investment increased in the fourth quarter, due partly to large shipments of farm machinery and increased construction expenditures on the Alaskan pipeline. However, there has been no significant increase yet in real orders for non-defense capital goods (down 2.8 per cent in December and only 5 per cent above their March low) or in contracts for commercial and industrial buildings (little above their first quarter low).

The outlook for inflation has shown little change in recent months. The hourly earnings index continues to move erratically, with a 9 per cent increase in January--reflecting, in part, an increase in the minimum wage--following no change in December. On average, wages rose at about an 8 per cent annual rate during 1975.

Growth of productivity in the private nonfarm economy halted in the fourth quarter, as the rate of expansion of economic activity moderated. As a result, unit labor costs rose by a 6-1/2 per cent annual rate. Productivity gains will almost certainly speed up again, but are not likely to be as large as the third-quarter surge. Consequently, unit labor costs will again be exerting considerable upward pressure on prices.

The easing of farm and food prices has taken some of the pressure off over-all prices at both wholesale and retail in the past few months. Excluding food and energy, consumer prices in December rose at a 6.8 per cent rate--about equal to the average for 1975 as a whole. Wholesale prices of industrial commodities rose at a 7-1/2 per cent rate in December, about the same as in the previous month.

Outlook. The staff GNP projection has been extended through the middle of 1977, and now incorporates fiscal assumptions that take the new FY 1977 Budget into account.

As regards Federal spending, our assumptions are consistent with budget outlays of around \$410 billion in FY 1977, some \$16 billion

larger than the outlays recommended by the President. We expect effective resistance in the Congress to portions of the proposed spending cuts, especially in the area of health, manpower, education and income security. Nevertheless, we have assumed that spending will be held some \$5 billion below the total that would be consistent with maintenance of all currently legislated programs. The result is to reduce projected Federal spending during CY 1976 by about \$2-1/2 billion from the previous Greenbook.

If the projected excess of expenditures over the Budget actually develops, the President may resist the \$10 billion income tax cut scheduled for July 1976. We have therefore assumed continuation of current income tax provisions throughout the projection period. In regard to payroll taxes, our projection is consistent with proposed budget increases for social security and unemployment insurance amounting to almost \$8 billion, annual rate, effective in January 1977.

On balance, the projected divergences from the Budget in receipts and expenditures are partially offsetting, and thus the projected staff deficit, on a full employment basis, is only some \$5 billion larger than that in the Budget Document. Our assumptions imply a shift from a full employment deficit of \$10 billion in CY 1975, to a \$7 billion deficit in CY 1976, and a \$9 billion surplus (annual rate) in the 1st half of CY 1977.

The assumptions for monetary policy include an  $M_1$  growth rate that averages 6 per cent annual rate over the projection period.



Short-term interest rates are expected to mark their lows during the current quarter, but the cyclical rise thereafter is projected to be gradual--moving the commercial paper rate from about 5 per cent presently to around 3 per cent in early 1977. Long-term rates are expected to stay fairly close to current levels.

The staff has revised upward its projection for growth in real GNP during the current quarter to an annual rate of 6-1/2 per cent. The added strength is principally accounted for by a larger swing from liquidation of nonfarm inventories in the fourth quarter to accumulation in the first, and by increased outlays for consumer durables.

We expect these elements of increased strength to carry over into subsequent quarters, with consumption bolstered both by large gains in income and by a reduction in the savings rate from 8.2 per cent last quarter to about 7-1/4 per cent by mid-1977--an assumption that seems justified by improving consumer wealth positions and strengthening consumer confidence. On average, real consumption is projected to advance at around a 5 per cent annual rate over the next six quarters.

Inventory investment is also expected to provide more thrust over the remainder of this year, as businesses move to rebuild inventories depleted by the recent strong rise of sales. Projections for other sectors of demand have been altered only a little. In the case of business fixed investment, orders and shipments suggest only moderate

gains in real capital spending over the near term. But with consumer demand increasing steadily, profits still improving, and financial markets accomodative, we expect a stronger gain in plant and equipment expenditures to develop toward the end of 1976 and into early 1977. In the case of residential construction, the rise in housing starts is still projected to slow as this year progresses and to level out at an annual rate of 1.8 million during the first half of 1977. Net exports are projected to decline during the projection period as the recovery generates rising imports.

On balance, real GNP growth is now projected to average around a 5-1/2 per cent annual rate. On a year-over-year basis, this would mean a rise in real GNP of 6.3 per cent in 1976. With this more rapid rate of economic expansion and with recent evidence of improvement in the labor market, the unemployment rate is now projected to move down to 7-1/4 per cent by year-end, and to reach 7 per cent in the second quarter of 1977.

The price outlook has not changed significantly since last month, and the additional strength in real activity we project is not expected to alter the behavior of prices materially. Thus, we are still projecting the fixed-weighted price index for gross private product to advance at about a 5-1/2 per cent rate during 1976, and just a little higher in early 1977.

Details on these projections are presented in the tables that follow.

## STAFF GNP PROJECTIONS

	Changes in nominal GNP (\$ billions)		Per cent change, annual rate					
			Real GNP		Gross private product fixed weighted price index		Unemployment rate (per cent)	
	1/14/76	2/11/76	1/14/76	2/11/76	1/14/76	2/11/76	1/14/76	2/11/76
1972 <u>1/</u>	107.7	107.7	5.7	5.7	3.3	3.3	5.6	5.6
1973 <u>1/</u>	135.2	135.2	5.3	5.3	6.3	6.3	4.9	4.9
1974 <u>1/</u>	100.6	100.6	-1.8	-1.8	11.4	11.4	5.6	5.6
1975 <u>1/</u>	92.9	92.9	-2.0	-2.0	n.a.	n.a.	8.5	8.5
1976	175.0	186.4	5.6	6.3	n.a.	n.a.	8.0	7.6
1975-I <u>1/</u>	-7.7	-7.7	-9.2	-9.2	7.7	7.7	8.3	8.1
II <u>1/</u>	27.0	27.0	3.3	3.3	5.5	5.5	8.9	8.7
III <u>1/</u>	67.9	67.9	11.9	11.9	7.3	7.3	8.4	8.6
IV <u>1/</u>	47.9	44.7	6.1	5.4	5.9	5.9	8.4	8.5
1976-I	37.0	44.9	4.5	6.5	5.6	5.8	8.2	7.9
II	40.3	44.3	4.5	5.5	5.6	5.6	8.1	7.6
III	41.0	44.6	4.3	5.1	5.6	5.6	7.9	7.4
IV	42.5	47.0	4.0	5.0	5.5	5.5	7.9	7.3
1977-I	n.a.	46.8	n.a.	5.4	n.a.	5.7	n.a.	7.2
II	n.a.	47.3	n.a.	5.5	n.a.	5.7	n.a.	7.1
Change:								
74-IV to								
75-IV <u>1/</u>	135.1	131.9	2.7	2.6	6.6	6.6	1.8	1.8
75-II to								
76-II	193.1	201.8	6.7	7.3	6.1	6.2	-.8	-1.1
75-IV to								
76-IV	160.8	120.8	4.3	5.5	5.6	5.6	-.5	-1.2
76-II to								
77-II	n.a.	185.7	n.a.	5.2	n.a.	5.6	n.a.	-.5

1/ Actual

NOTE: Changes in GNP, nominal and real, are based on the revised estimates, but changes in gross private product fixed weighted price index are based on the former series. Unemployment rates and changes therein for 2/11/76 projection reflect the revised series (new seasonal factors); for 1/14/76 the figures are based on former series.

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

	1975		1976				1977	
	III	IV	Projected		III	IV	I	II
Gross National Product	1528.5	1573.2	1618.1	1662.4	1707.0	1754.0	1800.8	1848.1
Final purchases	1530.6	1573.4	1611.8	1653.4	1696.0	1740.0	1782.8	1826.1
Private	1196.5	1229.6	1262.2	1296.6	1331.6	1365.9	1401.5	1438.4
Excluding net exports	1174.4	1207.2	1243.7	1279.3	1315.8	1351.2	1388.9	1427.9
Personal consumption expenditures	977.4	998.7	1025.4	1052.8	1079.3	1106.1	1135.1	1164.6
Durable goods	131.8	136.1	141.9	148.0	154.4	161.2	169.0	176.8
Nondurable goods	416.4	424.8	436.3	448.3	459.4	469.9	480.9	492.4
Services	429.2	437.7	447.2	456.5	465.5	475.0	485.2	495.4
Gross private domestic investment	194.9	208.3	224.6	235.5	247.5	259.1	271.8	285.3
Residential construction	50.4	55.7	60.1	64.1	69.1	71.7	73.4	74.9
Business fixed investment	146.7	152.7	156.7	160.9	165.9	171.9	178.9	186.9
Change in business inventories	-2.1	-.2	7.8	10.5	12.5	15.5	19.5	23.5
Nonfarm	-5.7	-5.7	6.8	11.5	13.5	16.5	19.5	23.5
Net exports of goods and services <sup>1/</sup>	22.1	22.4	18.5	17.3	15.8	14.7	12.6	10.5
Exports	148.5	151.9	154.5	158.0	161.3	165.0	168.7	173.3
Imports	126.4	129.4	136.0	140.7	145.5	150.3	156.1	162.8
Gov't. purchases of goods and services	334.1	343.8	349.6	356.8	364.4	374.1	381.3	387.7
Federal	124.2	129.8	131.5	133.2	135.3	139.1	140.7	141.5
Defense	84.9	87.4	88.2	89.4	90.6	92.9	94.1	94.4
Other	39.3	42.3	43.3	43.8	44.7	46.2	46.6	47.1
State and local	209.9	214.1	218.1	223.6	229.1	235.0	240.6	246.2
Gross national product in constant (1972) dollars	1201.5	1217.4	1236.7	1253.4	1268.9	1284.9	1301.8	1319.2
GNP implicit deflator (1972 = 100)	127.2	129.2	130.8	132.6	134.5	136.5	138.3	140.1
Personal income	1261.7	1294.8	1327.9	1358.0	1391.6	1424.7	1458.8	1490.9
Wage and salary disbursements	807.3	830.5	851.9	873.0	894.4	918.7	941.6	964.3
Disposable income	1087.1	1114.4	1145.5	1170.2	1197.6	1225.2	1255.9	1282.7
Personal saving	85.9	91.3	95.6	92.7	93.5	94.2	95.8	93.1
Saving rate (per cent)	7.9	8.2	8.3	7.9	7.8	7.7	7.6	7.3
Corporate profits with I.V.A. and C.C. Adj.	113.1	120.3	123.3	132.7	138.8	145.9	147.6	156.8
Corporate profits w/I.V.A., without C.C. Adj.	119.6	128.9	131.3	140.2	145.8	152.6	154.1	163.3
Corporate profits before taxes	129.5	144.7	145.3	152.7	156.8	162.1	163.1	171.8
Federal government receipts and expenditures, (N.I.A. basis)								
Receipts	293.3	304.9	313.2	323.9	334.5	344.8	359.4	370.1
Expenditures	363.8	374.2	382.6	390.2	399.5	406.8	416.0	420.2
Surplus or deficit (-)	-70.5	-69.3	-69.3	-66.3	-65.0	-62.0	-56.5	-50.0
High employment surplus or deficit (-)	-6.7	-7.3	-11.9	-8.8	-7.0	-2.0	5.3	12.3
State and local government surplus or deficit (-) (N.I.A. basis)	12.9	12.3	12.6	12.5	13.2	12.1	12.1	11.7
Civilian labor force (millions)	93.1	93.2	93.7	94.1	94.5	95.0	95.4	96.0
Unemployment rate (per cent)	8.6	8.5	7.9	7.6	7.4	7.3	7.2	7.1
Nonfarm payroll employment (millions)	77.0	77.6	78.4	79.1	79.6	80.1	80.5	81.2
Manufacturing	18.3	18.5	18.8	19.1	19.3	19.5	19.7	19.9
Industrial production (1967 = 100)	114.2	117.5	120.8	123.6	125.9	128.3	130.7	133.4
Capacity utilization, mfg. (per cent)	69.0	70.8	72.2	73.3	74.1	74.8	75.6	76.6
Major materials (per cent)	78.0	80.8	82.3	83.4	84.3	85.1	85.9	86.9
Housing starts, private (millions, A.R.)	1.26	1.37	1.50	1.65	1.70	1.75	1.80	1.80
Sales new autos (millions, A.R.)	9.21	9.20	9.65	9.85	10.00	10.20	10.50	10.70
Domestic models	7.52	7.87	8.25	8.35	8.50	8.70	8.90	9.10
Foreign models	1.69	1.33	1.40	1.50	1.50	1.50	1.60	1.60
<sup>1/</sup> Net exports <sup>2/</sup> of g.&s. (Bal. of paymts)	18.0 <sub>3/</sub>	16.5 <sub>3/</sub>	11.8	10.2	8.7	7.6	5.5	3.4
Exports <sup>2/</sup>	148.7 <sup>2/</sup>	152.6 <sup>2/</sup>	154.7	158.2	161.5	165.2	168.9	173.5
Imports	130.7	136.1	142.9	148.0	152.8	157.6	163.4	170.1

<sup>2/</sup> Federal government N.I.A. receipts in 1975-II reflects the \$8.1 billion rebate of 1974 individual income taxes and in 1975-III and following quarters the \$9.3 billion reduction in 1975 individual income taxes; the withholding rates associated with the latter reduction are assumed to be continued in 1976. Includes \$.3 billion, annual rate of shipments of military equipment and supplies to Israel which are not included in GNP exports.

CHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1975		1976				1977	
	III	IV	I	II	Projected		I	II
					III	IV		
Gross National Product	67.9	44.7	44.9	44.3	44.6	47.0	46.8	47.3
Inventory change	27.5	1.9	6.5	2.7	2.0	3.0	4.0	4.0
Final purchases	40.4	42.8	38.4	41.6	42.6	44.0	42.8	43.3
Private	31.0	33.1	32.6	34.4	35.0	34.3	35.6	36.9
Net exports	-2.1	.3	-3.9	-1.2	-1.5	-1.1	-2.1	-2.1
Excluding net exports	33.1	32.8	36.5	35.6	36.5	35.4	37.7	39.0
Personal consumption expenditures	27.1	21.3	26.7	27.4	26.5	26.8	29.0	29.5
Durable goods	8.0	4.3	5.8	6.1	6.4	6.8	7.8	7.8
Nondurable goods	11.6	8.4	11.5	12.0	11.1	10.5	11.0	11.5
Services	7.6	8.5	9.5	9.3	9.0	9.5	10.2	10.2
Residential fixed investment	5.4	5.3	4.4	4.0	5.0	2.6	1.7	1.5
Business fixed investment	.6	6.0	4.0	4.2	5.0	6.0	7.0	8.0
Government	9.4	9.7	5.8	7.2	7.6	9.7	7.2	6.4
Federal	5.0	5.6	1.7	1.7	2.1	3.8	1.6	.8
State and local	4.4	4.2	4.0	5.5	5.5	5.9	5.6	5.6
GNP in constant (1972) dollars	33.4	15.9	19.3	16.7	15.5	16.0	16.9	17.4
Final purchases	13.5	14.9	13.5	15.2	14.9	14.2	14.1	14.6
Private	9.7	12.5	11.8	13.3	13.1	12.4	13.1	13.8
	-----In Per Cent Per Year <sup>1/</sup> -----							
Gross National Product	19.9	12.2	11.9	11.4	11.2	11.5	11.1	10.9
Final purchases	11.3	11.7	10.1	10.7	10.7	10.8	10.2	10.1
Private	11.1	11.5	11.0	11.4	11.2	10.7	10.8	11.0
Personal consumption expenditures	11.9	9.0	11.1	11.1	10.5	10.3	10.9	10.8
Durable goods	28.5	13.7	18.2	18.3	18.5	18.8	20.8	19.8
Nondurable goods	12.0	8.3	11.3	11.5	10.3	9.5	9.7	9.9
Services	7.4	8.2	9.0	8.6	8.1	8.4	8.9	8.7
Gross private domestic investment	112.6	30.5	31.6	21.0	22.1	20.2	21.2	21.5
Residential structures	57.4	49.2	35.5	29.4	35.0	15.9	9.8	8.4
Business fixed investment	1.7	17.4	10.9	11.2	13.0	15.3	17.3	19.1
Gov't purchases of goods & services	12.1	12.1	6.9	8.5	8.8	11.1	7.9	6.9
Federal	17.9	19.3	5.3	6.5	11.7	5.3	4.7	2.3
Defense	14.4	12.3	3.7	5.6	5.5	10.5	5.3	1.3
Other	25.9	34.2	9.8	4.7	8.5	14.1	3.5	4.4
State and local	8.8	8.2	7.7	10.5	10.2	10.7	9.9	9.6
GNP in constant (1972) dollars	11.9	5.4	6.5	5.5	5.0	5.1	5.4	5.5
Final purchases	4.6	5.1	4.5	5.0	4.9	4.6	4.5	4.6
Private	4.2	5.4	5.0	5.6	5.4	5.1	5.3	5.5
GNP implicit deflator <sup>2/</sup>	7.2	6.4	5.0	5.6	5.9	6.1	5.5	5.3
Private GNP fixed weighted index <sup>3/</sup>	7.3	5.9	5.8	5.6	5.6	5.5	5.7	5.7
Personal income	13.0	10.9	10.6	9.4	10.3	9.9	9.9	9.1
Wage and salary disbursements	10.4	12.0	10.7	10.3	10.2	11.3	10.3	10.0
Disposable income	2.0	10.4	11.6	8.9	9.7	9.5	10.4	8.8
Corporate profits before tax	105.2	55.9	1.7	22.0	11.2	14.2	2.5	23.1
Federal Government receipts and expenditures (N.I.A. basis)								
Receipts	89.1	16.8	11.3	14.4	13.7	12.9	18.0	12.5
Expenditures	13.7	11.9	9.3	8.2	9.9	7.5	9.4	4.1
Nonfarm payroll employment	3.2	3.2	4.2	3.6	2.6	2.5	2.0	3.5
Manufacturing	4.5	4.4	6.6	6.5	4.3	4.2	4.2	4.1
Industrial production	14.5	12.1	11.7	9.6	7.7	7.8	7.7	8.5
Housing starts, private	92.3	39.8	43.7	46.4	12.7	12.3	11.9	.0
Sales new autos	84.7	-.4	21.0	8.6	6.2	8.2	12.3	7.8
Domestic models	99.2	20.0	20.8	4.9	7.4	9.7	9.5	9.3
Foreign models	34.3	-61.6	22.8	31.8	.0	.0	29.5	.0

<sup>1/</sup> Percentage rates are annual rates compounded quarterly.<sup>2/</sup> Excluding Federal pay increases rates of change are: 1975-IV, 5.8 per cent; 1976-I, 5.0 per cent; 1976-IV, 5.4 per cent; 1977-I, 5.4 per cent.<sup>3/</sup> Using expenditures in 1967 as weights.

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

	1969	1970	1971	1972	1973	1974	1975	Projected 1976
Gross National Product	935.5	982.4	1063.4	1171.1	1306.3	1406.9	1499.0	1685.4
Final purchases	926.1	978.6	1057.0	1161.7	1288.8	1397.2	1513.2	1675.3
Private	718.2	759.7	823.3	908.6	1018.9	1096.1	1182.3	1314.1
Excluding net exports	716.4	755.8	821.7	911.9	1011.5	1088.4	1160.8	1297.5
Personal consumption expenditures	579.7	618.8	668.2	733.0	808.5	885.9	963.2	1065.9
Durable goods	85.5	84.9	97.1	111.2	122.9	121.9	127.7	151.4
Nondurable goods	247.0	264.7	277.7	299.3	334.4	375.7	410.0	453.5
Services	247.2	269.1	293.4	322.4	315.3	388.3	425.5	461.1
Gross private domestic investment	146.2	140.8	160.0	188.3	220.5	212.2	183.3	241.7
Residential construction	37.9	36.6	49.6	62.0	66.5	54.6	48.8	66.3
Business fixed investment	98.9	100.5	104.1	116.8	136.5	147.9	148.7	163.9
Change in business inventories	9.4	3.8	6.4	9.4	17.5	9.7	-14.2	11.6
Nonfarm	9.2	3.7	5.1	8.8	14.1	11.6	-16.1	12.1
Net exports of goods and services <sup>1/</sup>	1.8	3.9	1.6	-3.3	7.4	7.7	21.5	16.6
Exports	54.7	62.5	65.6	72.7	101.5	144.2	147.3	159.7
Imports	52.9	58.5	64.0	75.9	94.2	136.5	125.8	143.1
Gov't. purchases of goods and services	207.9	218.9	233.7	253.1	269.9	301.1	330.9	361.2
Federal	97.5	95.6	96.2	102.1	102.0	111.7	123.1	134.8
Defense	76.3	73.5	70.2	73.5	73.4	77.4	84.0	90.3
Other	21.2	22.1	26.0	28.6	28.6	34.3	39.2	44.5
State and local	110.4	123.2	137.5	151.0	168.0	189.4	207.8	226.5
Gross national product in constant (1972) dollars	1078.8	1075.3	1107.5	1171.1	1233.4	1210.7	1186.4	1261.0
GNP implicit deflator (1972=100)	86.7	91.4	96.0	100.0	105.9	116.2	126.4	133.6
Personal income	745.8	801.3	859.1	942.5	1054.3	1154.7	1246.0	1375.6
Wage and salary disbursements	514.6	546.5	579.4	633.8	701.0	763.6	801.6	884.3
Disposable income	630.4	685.9	742.8	801.3	903.1	983.6	1076.8	1184.6
Personal saving	35.1	50.6	57.3	49.4	72.7	74.0	89.6	94.0
Saving rate (per cent)	5.6	7.4	7.7	6.2	8.0	7.5	8.3	7.9
Corporate profits with I.V.A. and C.C.Adj.	81.4	67.9	77.2	92.1	100.2	91.3	102.1	135.2
Corporate profits with I.V.A., without C.C.Adj.	77.9	66.4	76.9	85.6	98.6	93.6	108.3	142.5
Corporate profits before tax	83.4	71.5	82.0	96.2	117.0	132.1	119.8	154.2
Federal government receipts and expenditures, (N.I.A. basis)								
Receipts <sup>2/</sup>	197.0	192.1	198.6	227.5	257.9	288.4	283.5	329.1
Expenditures	188.4	204.2	220.6	224.7	264.8	300.1	356.9	394.8
Surplus or deficit (-) <sup>2/</sup>	-8.5	-12.1	-22.0	-17.3	-6.9	-11.7	-73.4	-64.2
High employment surplus or deficit (-)	13.4	6.5	-1.7	-1.0	4.3	18.0	-9.9	-7.4
State and local government surplus or deficit (-) (N.I.A. basis)	2.1	2.8	3.7	13.7	12.9	8.1	9.9	12.6
Civilian labor force (millions)	77.9	78.6	79.1	81.7	84.4	85.9	92.7	94.3
Unemployment rate (per cent)	3.5	4.9	5.9	5.6	4.9	5.6	8.5	7.6
Nonfarm payroll employment (millions)	70.4	70.9	71.2	73.7	76.9	78.4	77.0	79.3
Manufacturing	20.2	19.3	18.6	19.1	20.1	20.0	18.4	19.2
Industrial production (1967=100)	110.7	106.6	106.8	115.2	125.6	124.8	113.4	124.7
Capacity utilization, mfg. (per cent)	86.5	78.3	75.0	78.6	83.0	78.9	68.7	73.6
Major materials (per cent)	90.0	86.2	85.3	89.6	93.0	87.0	74.9	83.8
Housing starts, private (millions, A.R.)	1.47	1.43	2.05	2.36	2.05	1.34	1.18	1.65
Sales new autos (millions, A.R.)	9.57	8.40	10.24	10.93	11.44	8.87	8.66	9.93
Domestic models	8.46	7.12	8.68	9.32	9.67	7.45	7.08	8.45
Foreign models	1.11	1.28	1.56	1.61	1.77	1.42	1.58	1.48
<sup>1/</sup> Net exports of g. & s. (Bal. of paymts)	1.0	3.0	-2	-5.9	4.2	3.8	16.8	9.6
Exports	54.7	62.4	65.5	72.6	102.1 <sup>3/</sup>	144.4 <sup>3/</sup>	146.7 <sup>3/</sup>	160.0
Imports	53.6	59.5	65.8	78.5	97.9	140.6	130.8	150.4

<sup>2/</sup> Federal government N.I.A. receipts in 1975-II reflect the \$8.1 billion rebate of 1974 individual income taxes and in 1975-III and following quarters the \$9.3 billion reduction in 1975 individual income taxes; the withholding rates associated with the latter reduction are assumed to be continued in 1976.

<sup>3/</sup> Includes \$3 billion, annual rate of shipments of military equipment and supplies to Israel which are not included in GNP exports.

CHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1969	1970	1971	1972	1973	1974	1975	Projected 1976
Gross National Product	67.0	46.9	81.0	107.7	135.2	100.6	92.1	186.4
Inventory change	1.7	-5.6	2.6	3.0	8.1	-7.8	-23.9	24.3
Final purchases	65.3	52.5	78.4	104.7	127.1	108.4	116.0	162.1
Private	56.1	41.5	63.6	85.3	110.3	77.2	86.2	131.8
Net exports	-.5	2.1	-2.3	-4.9	10.7	.3	13.8	-4.9
Excluding net exports	56.6	39.4	65.9	90.2	99.6	76.9	72.4	136.7
Personal consumption expenditures	43.8	39.1	49.4	64.8	75.5	77.4	77.3	104.2
Durable goods	5.5	-.6	12.2	14.1	11.7	-1.0	5.8	24.2
Nondurable goods	16.6	17.7	13.0	21.6	35.1	41.3	34.3	44.5
Services	21.6	21.9	24.3	29.0	28.9	37.0	37.2	35.6
Residential fixed investment	3.4	-1.3	13.0	12.4	4.5	-11.9	-5.8	17.5
Business fixed investment	9.6	1.6	3.6	12.7	19.7	11.4	.8	15.2
Government	9.2	11.0	14.8	19.4	16.8	31.2	29.8	30.3
Federal	-.5	-1.9	.6	5.9	-.1	9.7	11.4	11.7
State and local	9.7	12.8	14.3	13.5	17.0	21.4	18.4	18.7
GNP in constant (1972) dollars	27.0	-3.5	32.2	63.6	62.3	-22.7	-24.3	74.7
Final purchases	25.1	2.8	29.9	60.8	55.7	-14.4	-6.5	57.7
Private	27.6	9.3	30.7	57.1	56.3	-16.2	-9.6	49.5
	-----In Per Cent Per Year-----							
Gross national product	7.7	5.0	8.2	10.1	11.5	7.7	6.5	12.4
Final purchases	7.6	5.7	8.0	9.9	10.9	8.4	8.3	10.7
Private	8.5	5.8	8.4	10.4	12.1	7.6	7.9	11.1
Personal consumption expenditures	8.2	6.7	8.0	9.7	10.3	9.6	8.7	10.7
Durable goods	6.9	-.7	14.4	14.5	10.5	-.8	4.8	18.6
Nondurable goods	7.2	7.2	4.9	7.8	11.7	12.4	9.1	10.6
Services	9.6	8.9	9.0	9.9	9.0	10.5	9.6	8.4
Gross private domestic investment	11.2	-3.7	13.6	17.7	17.1	-3.8	-13.6	31.9
Residential structures	9.9	-3.4	35.5	25.0	7.3	-17.9	-10.6	35.9
Business fixed investment	10.8	1.6	3.6	12.2	16.9	8.4	.5	10.2
Gov't. purchases of goods & services	4.6	5.3	6.8	8.3	6.6	11.6	9.9	9.2
Federal	-.5	-1.9	.6	6.1	.1	9.5	10.2	9.5
Defense	-.8	-3.7	-4.5	4.7	-.1	5.4	8.5	7.5
Other	.0	4.2	17.6	10.0	.0	19.9	14.3	13.5
State and local	9.6	11.6	11.6	9.8	11.3	12.7	9.7	9.0
GNP in constant (1972) dollars	2.6	-.3	3.0	5.7	5.3	-1.8	-2.0	6.3
Final purchases	2.4	.3	2.8	5.5	4.8	-1.2	-.5	4.8
Private	3.5	1.1	3.7	6.7	6.2	-1.7	-1.0	5.3
GNP implicit deflator	5.0	5.4	5.0	4.2	5.9	9.7	8.8	5.7
Private GNP fixed weighted index <sup>1/</sup>	5.0	5.4	4.9	4.1	6.4	10.8	6.6	5.6
Personal income	8.8	7.4	7.2	9.7	11.9	9.5	7.9	10.4
Wage and salary disbursements	9.6	6.2	6.0	9.4	10.6	8.9	5.0	10.3
Disposable income	7.2	8.8	8.3	7.9	12.7	8.9	9.5	10.0
Corporate profits before tax	-2.6	-14.3	14.7	17.3	21.6	12.9	-9.3	28.7
Federal Government receipts and expenditures (N.I.A. basis)								
Receipts	12.8	-2.5	3.4	14.6	13.4	11.8	-1.7	16.1
Expenditures	4.3	8.4	8.0	10.9	8.2	13.3	18.9	10.6
Nonfarm payroll employment	3.5	.7	.4	3.5	4.3	2.0	-1.8	3.0
Manufacturing	2.0	-4.5	-3.6	2.7	5.2	.5	-8.0	4.3
Industrial production	4.7	-3.7	.2	7.9	9.0	-.6	-9.1	10.0
Housing starts, private	-2.6	-2.7	43.4	15.1	-13.1	-34.6	-11.9	39.8
Sales new autos	-.7	-12.2	21.9	6.7	4.7	-22.5	-2.4	14.7
Domestic models	-1.9	-15.8	21.9	7.4	3.8	-23.0	-5.0	19.4
Foreign models	8.8	15.3	21.9	3.2	9.9	-19.8	11.3	-6.3

<sup>1/</sup> Using expenditures in 1967 as weights.

DOMESTIC FINANCIAL DEVELOPMENTS

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Summary. In the weeks since the last FOMC meeting, expectations of further declines in market rates of interest evaporated with indications of increased strength in economic activity along with stability in the Federal funds rate. Moreover, financial market participants apparently have interpreted the Chairman's testimony before Congress as confirmation that the slow growth in  $M_1$  in recent months was unlikely to produce further easing in money market conditions. Consequently, the strong rally in financial markets since the turn of the year came to a halt in late January but most market rates of interest remain near the levels prevailing at the time of the January FOMC meeting.

Recent low rates of interest have resulted in a near record increase in savings deposits at commercial banks. Such deposits have been particularly attractive relative to Treasury bills on which yields have been below the savings deposit ceiling rate. The increased demand for savings deposits in January was broadly based, but about one-sixth of the growth was accounted for by businesses which could not, until recently, hold such deposits. Banks permitted large negotiable CDs to run off in volume in January, given the increase in other deposit flows and modest loan growth.

Business loans at banks in January provided some hint of a rise in demand for funds--after adjusting for the December buildup



and January drop in bank holdings of acceptances. Commercial paper issued by nonfinancial firms also rose appreciably in January, a means of financing which remains very attractive on a cost basis compared to bank loans. The spread favoring the paper market widened since late December as the drop in paper rates was greater than the 1/2 percentage point decline to 6.75 per cent in the prime rate.

At thrift institutions deposit growth also expanded considerably in January. Savings and loan associations--the dominant suppliers of residential mortgage loans--repaid about \$700 million of borrowings from the FHLBanks and apparently also continued to take a large volume of mortgage loans into their portfolios. Outstanding mortgage commitments at S&L's continued to rise, and the \$18.2 billion level at year-end was the highest in almost 2-1/2 years. Interest rates on commitments for conventional home mortgages have declined about 15 basis points since mid-January and are now about 40 basis points below the recent high in October.

In long-term securities markets, the improved environment was accompanied by a strong flow of new offerings. Corporate bond volume rose in the latter part of January as a result of several large offerings induced by lower interest rates. While corporate issues were readily distributed at lower rates, the municipal market was somewhat less receptive to new offerings at prevailing lower yields, and underwriters now hold a substantial volume of unsold

bonds. The Treasury market absorbed a substantial volume of new offerings in the Treasury's February refunding and new borrowing operation. In particular, huge demands developed for the 7-year note with an 8 per cent coupon; the Treasury awarded \$6 billion of these instruments instead of the \$3.5 billion originally planned, and raised about \$5 billion of new cash in the operation as a whole.

Outlook. The continued expansion of economic activity is likely to be associated with further increases in private credit demands in coming months. In addition, the Treasury will be a substantial borrower until mid-April, perhaps requiring about \$12-15 billion of new cash over this period. Hence, it appears some upward pressures on short-term rates could begin to develop in the near term.

Larger demands for credit by households are likely to be generated by rising consumer expenditures and by increased housing market activity. Businesses, too, probably will require some increase in external financing as additional nominal expenditures on inventories and capital investment tend to outpace growth in cash flow. Many firms still desire to restructure balance sheets, and corporate issuance of bonds is thus expected to be sizable, although well below the record volume last year; the higher level of equity prices presently also has enhanced the prospects for raising funds in the equity market. Furthermore, demands for funds in long-term markets are likely to be supplemented by enlarged foreign borrowing in domestic markets, given the cost and ability to float large, long-term offerings.

Prospective supplies of funds appear ample enough to avoid significant stresses and strains in financial markets over the next few months. In particular, the depository institutions have achieved comfortable liquidity positions and deposit flows are likely to remain sizable even with some rise in market rates of interest. However, the recent very large net inflows of time and savings deposits other than large CDs at banks and thrift institutions are not likely to be sustained, if market rates increase as projected--though the expected large volume of tax refunds this year will help to sustain deposit growth.

The mortgage market seems likely to be a continuing beneficiary of the more ebullient atmosphere in financial markets this year. With appreciable deposit growth, and prepayment penalties increasingly inhibiting further sizable paydowns of FHLBank borrowing, thrift institutions probably will continue to seek new commitments aggressively. Mortgage rates in the conventional market could edge a little lower than present levels and the FHA-VA ceiling rate might be reduced.

In the municipal market there continue to be considerable uncertainties over the New York State and State agency financing difficulties. There are also other major governmental units that have come under a cloud. Even so, the receptivity of the market to lower-grade issues has improved some this year and there may be further progress in this direction assuming the New York State problem can be resolved satisfactorily.

INTERNATIONAL DEVELOPMENTS

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Summary. Following several months of relatively calm conditions, exchange markets since mid-January have been unsettled at times. The disturbances focused on the European currencies, however, and not on the U.S. dollar. On balance the weighted-average value of the U.S. dollar rose about 1/2 per cent during the past four weeks,

Since the Bank of Italy withdrew from the foreign exchange market on January 21, the lira has declined by about 9 per cent against the U.S. dollar, and slightly more against a weighted average of all major currencies. This action by the Bank of Italy followed the severe depletion of Italy's foreign exchange reserves, as the Italian authorities had attempted to peg the lira's effective exchange rate in the wake of the political hiatus caused by the fall of the government of Premier Moro on January 7 and growing pressures on the lira.

Reflecting rumors of a realignment within the EC snake, the French franc came under pressure following the start of the lira crisis and again after the Spanish peseta was devalued by 11 per cent on February 9.

As a by-product of the pressures that developed within the snake, , the German mark rose by about 2-1/2 per cent against the dollar, and the System over the past two weeks has sold about \$100 million in marks out of balances and by drawing on the swap line with the Bundesbank.

Data on U.S. international transactions in the fourth quarter of 1975 show a substantial U.S. trade surplus at about an \$8 billion annual rate (balance-of-payments basis) for the second consecutive quarter, although the trade surplus for December was at a somewhat lower rate. U.S. exports and imports rose in value for the second quarter in a row with most of the rise accounted for by increases in volume. The pick-up in imports reflected primarily the upturn in the U.S. economy, while the increase in exports can be attributed to improving economic conditions abroad.

The latest data confirm earlier indications that an upturn in economic activity had begun in most major foreign industrial countries by late 1975. The strength and sustainability of the rise in the rate of economic activity abroad are, however, still in question for most countries. In Japan, which earlier had shown strong signs of recovery, recent data suggest that the upturn may have stalled. Moreover, in Italy an upturn may not even have started. The recovery in Germany, although modest, is the strongest among the major foreign industrial countries.

Meanwhile, in the fourth quarter of 1975 a shift occurred to a net outflow of U.S. private capital on bank-reported transactions and transactions in securities. The net outflow was nearly \$4 billion

(quarterly rate) compared with a net inflow of \$3.5 billion in the third quarter. This shift was accompanied by a \$7.4 billion swing in U.S. liabilities to official agencies of countries other than members of OPEC (from a large \$6.3 billion decrease in the third quarter to a \$1.1 billion increase in the fourth quarter). In addition, there was little further change in the dollar's average value, and the differential between foreign and U.S. interest rates widened. Bank-reported claims on foreigners rose by more than \$4.5 billion in the fourth quarter of 1975. Over the same period, new foreign bond issues in the U.S. market amounted to a record \$2.6 billion--including a record \$1.3 billion in Canadian issues--and the rate of net foreign purchases of U.S. stocks rose to over \$1.5 billion.

U.S. liabilities to OPEC rose in the fourth quarter of 1975 at about half the rate of the third quarter. For 1975 as a whole, OPEC holdings of U.S. assets rose about \$6 billion compared with an increase of over \$11 billion in 1974. The investible surplus of OPEC declined by about 40 per cent in 1975, with a larger proportion of it going into assets with longer maturities.

Outlook. We still forecast only a slow pick-up in economic activity abroad with year-over-year increases in real GNP for the major foreign countries ranging from 1 to 4-1/2 per cent. Given the stronger outlook for U.S. economic activity, we now expect a slightly sharper drop in the U.S. trade balance in 1976 than was shown in last month's green book. We expect the U.S. trade balance to move gradually from a surplus of over \$8 billion at an annual rate in the fourth quarter of 1975 to a

deficit of about \$7 billion in the second quarter of 1977. On a balance-of-payments basis, net exports of goods and services will be in surplus by about \$3.5 billion at an annual rate at the end of the forecast period, since net service receipts are projected to rise steadily.

This forecast is generally in line with the projections of most observers, and we do not expect a marked difference to develop between the patterns of interest rate movements here and abroad over the next six quarters; therefore, we see no pronounced tendency for the dollar to appreciate or depreciate on average over that period. This outlook could change, however, if the intervention by foreign central banks results in asymmetrical purchases or sales of U.S. dollars on a substantial scale or if unanticipated changes occur in underlying economic factors.