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## **Part 1**

June 24, 1998

# **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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June 24, 1998

## **SUMMARY AND OUTLOOK**

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## Domestic Developments

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### Overview

The striking cross-currents affecting the U.S. and other economies have left the financial markets uncertain and volatile in recent weeks--and made it difficult to decide how our forecast should be modified. In the end, the outlook we are describing in this Greenbook is the same in its broad contours as that presented in May: We are still looking at a decided deceleration in activity in the current quarter and growth at a subpar pace through 1999. And, with labor markets remaining very tight through next year, and with some heretofore helpful "special" factors turning unfavorable, price inflation still is projected to trend upward.

We estimate that growth of real GDP will come in somewhere in the neighborhood of 2 percent at an annual rate in the second quarter, off sharply from the more than 5 percent first-quarter pace the Commerce Department is likely to announce tomorrow. The major element in this slowing is a substantial moderation in inventory investment from the inordinate pace of the first quarter; even with this drop-off, however, stocks are still growing rapidly, and we therefore anticipate that a further downshift in the pace of accumulation will be restraining production over the second half of the year as well. Meanwhile, the incoming bad news on the performance of the Asian economies and, relatedly, on the U.S. trade balance has also led us to anticipate an ongoing drag from the external sector--not so marked as in the first half of the year, but more than in our previous forecast. These forces should contribute to a slowing in the growth of payrolls and labor income, in turn contributing to a deceleration in domestic final demand; that deceleration is in time reinforced by a further weakening of the stock market associated with the deterioration in corporate profitability that now seems to be in train.

Our deceleration story might be more persuasive if we could already point to an incipient weakening in labor demand. But, with payroll increases of 300,000 per month in April and May, about the only hint we have of a softening is the reported slippage in the average workweek of production workers this spring--a pretty thin statistical reed. Our low GDP prediction implicitly includes a pause in productivity growth after the first-quarter surge--plausible, but far from a sure thing.

Be that as it may, with GDP growth running at about 2 percent on average over the next year and a half, as we are projecting, employment gains will slow and the unemployment rate almost surely will creep upward. However, we see the

jobless rate remaining below 5 percent, suggesting that workers will retain sufficient market leverage to secure further sizable gains in real compensation per hour. We expect that the emerging cost pressures will manifest themselves on the price side as well, and that the overall CPI inflation rate will increase to about 2-1/4 percent in 1999, versus 1.7 percent in the past twelve months--despite a few tenths worth of damping influence from technical changes to the index.

### **Key Background Factors**

We have again conditioned our baseline forecast on the assumption that the federal funds rate will remain near 5-1/2 percent through 1999. In recent weeks, bond yields have eased somewhat--absolutely and relative to our expectations--as the developments in Asia have prompted some flight to dollar assets and allayed concerns that the Federal Reserve might tighten money market conditions. Although our forecast anticipates that international safe-haven considerations will become less important as time passes, a growing perception that the economic expansion has moderated should maintain a firm tone to the bond markets. We don't foresee long-term yields returning to the upper part of the recent range on a persistent basis until next year.

Our forecast anticipates only a modest further decline in share prices over the next couple of quarters and no change during 1999. We continue to harbor considerable doubt about the rationality of current equity valuations, and we therefore would not be surprised to see a considerably deeper correction as profits fail to meet the rosy predictions of private analysts. But the market has given ground only grudgingly in response to the negative news of recent months, and the economic scenario we are describing does not include any events that would obviously force investors imbued with the buy-on-dips/hold-for-the-long-term mentality to abandon their optimism.

Discretionary fiscal policy is expected to have an essentially neutral influence on aggregate demand going forward. Although the House and Senate have put very different fiscal year 1999 budget proposals on the table, we assume that the final legislation will have little net effect on the federal surplus. The incoming information on receipts and expenditures has led us to raise our estimate of the budget surplus for fiscal 1998 a bit further, to around \$63 billion. We anticipate that in fiscal 1999 the surplus will edge down to \$53 billion, reflecting the projected slowing in the economy. Recent developments suggest that we have been correct

not to incorporate any tobacco legislation in our fiscal assumptions; if anything does happen on that front, the net budgetary effects are unlikely to be large during the forecast period.

With evidence of a further--and probably more prolonged--deterioration in the Asian economies and indications of mounting difficulties in Russia and Brazil, we have marked down considerably the outlook for economic growth abroad. We now expect that foreign GDP, on an export-weighted basis, will increase around 1 percent this year, with outright declines forecast for Japan and for many other Asian economies; the overall projected growth rate is about half as much as we thought previously. In 1999, foreign growth is expected to move up to roughly 2-1/2 percent, 1/2 percentage point below the May Greenbook forecast.

The dollar appreciated sharply against the other major currencies on a weighted average (narrow index) basis between the May FOMC meeting and the middle of June but has since declined and is now up a little more than 1 percent on balance. We expect the dollar to depreciate almost 4 percent from its current level by the end of 1999. Compared with the May forecast, the level of the dollar is about 2 percent higher in the near term, reflecting recent developments, but is projected to reach a similar level by the end of next year.

Despite the production cuts agreed upon in March by the major petroleum-exporting countries, slackening demand--particularly in Asia--has caused crude oil prices to fall back in recent weeks, dropping at times below \$12 per barrel. The spot price for West Texas intermediate crude currently stands at \$14.50 per barrel, slightly below the May average.<sup>1</sup> In response to the weakness in crude prices, we anticipate that exporters will reduce oil production significantly further. We thus are projecting that spot WTI prices will rise to \$16 per barrel by the beginning of next year, only \$0.50 below the level assumed in the May Greenbook.

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

The labor market and expenditure indicators are presenting a mixed message about the strength of activity this quarter. Therefore, our prediction of a 2 percent

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1. The average level of WTI prices during the intermeeting period may overstate the weakness in oil markets because stocks in the United States have been at an extraordinarily high level. This situation has led to a significant discounting of WTI relative to other grades of crude oil. For example, prices of Brent crude have averaged about \$0.35 per barrel less than WTI in recent weeks, compared with an average differential of \$1.50 per barrel over the past two years.

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

Measure	1998:Q1			1998:Q2	
	May GB	BEA <sup>1</sup>	June GB	May GB	June GB
<b>Real GDP</b>	5.2	4.8	5.4	2.5	2.0
Private domestic final purchases	8.0	7.9	8.2	6.1	6.2
Personal consumption expenditures	5.8	6.1	6.1	5.2	5.2
Residential investment	17.6	16.1	16.5	12.7	12.1
Business fixed investment	17.7	17.2	18.2	9.0	10.2
Government outlays for consumption and investment	-2.8	-3.0	-3.2	3.7	6.1
	Change, billions of chained (1992) dollars				
Inventory investment	29.0	26.7	29.7	-45.3	-51.1
Net exports	-48.8	-55.6	-48.8	-17.7	-35.0

1. Preliminary release published on May 28.

annual rate of real GDP growth, though not out of line with many private forecasts, is not offered with much confidence.

The plunge in the unemployment rate suggests, via Okun's law, another increase in real GDP on the order of 5 percent. Experience, however, tells us that this is not a very reliable indicator of quarter-to-quarter changes. Hours data generally are a more useful guide at this point, and we are estimating that aggregate hours in the nonfarm business sector will increase 2 percent at an annual rate this quarter.<sup>2</sup> We are anticipating in our forecast that output per hour will be flat, for two reasons: The GM strike is likely to subtract about 1/2 percentage point from GDP growth, though the loss of hours will not be picked up in the June labor market survey; and more fundamentally, the rapid GDP growth of the past several quarters probably has lifted labor productivity well above the underlying trend and some reversion is to be expected as firms gradually bring their staffing levels and workweeks into more normal alignment with activity.

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2. Aggregate private production-worker hours are anticipated to rise just 1/2 percent (annual rate) in the current quarter. The gap between the projected growth in production-worker hours and that in nonfarm business hours reflects the significantly larger gains in recent months in hours of nonproduction/supervisory workers and the self-employed.

On the expenditure side, our second-quarter story is much the same as it was in the last Greenbook, with the growth in GDP being held down by a sharp slowing in the pace of inventory investment and a further decline in net exports. Domestic final sales are continuing to grow rapidly, at about the same pace as that in the first quarter.

Real personal consumption expenditures appear likely to register a 5 percent annual rate of advance--impressive, but off from the 6 percent pace of the previous quarter. Retail sales posted big increases in April and May. If the hefty gains in employment, income, and wealth were not enough to put households in a mood to spend, the enhanced incentives offered by auto manufacturers competing for market share have given a further boost to light vehicle sales since late April.

Residential investment also is likely to decelerate somewhat in the current quarter, but we are still looking for a real increase on the order of 12 percent. With all the fundamentals, including mortgage rates, highly favorable, the demand for new homes evidently has increased even further. However, starts have edged off slightly in the past couple of months, as builders reportedly have encountered some difficulty in assembling construction crews in a very tight labor market.

Likewise, the prospect this quarter for business fixed investment appears to be one of reduced double-digit growth in real outlays. Nonresidential building is showing long-overdue signs of life, with a considerable uptick in construction put in place through April, but real purchases of producers' durable equipment are projected to rise at less than half the outsized 27 percent annual rate of the first quarter. The shipments and orders figures reported by domestic manufacturers through May indicate a much smaller advance in real outlays for information-processing equipment this period, and deliveries of commercial jets to domestic airlines appear slated to be about flat after jumping in the first three months of the year.

The May Monthly Treasury Statement suggests that defense purchases are retracing most of the surprisingly steep first-quarter drop, so total federal purchases may be up around 10 percent (annual rate) in real terms this quarter. In the state and local sector, purchases appear poised to rise perhaps 3-3/4 percent this quarter, after a meager 3/4 percent increase in the first quarter. Employment growth in this sector has picked up in recent months, and the latest data on construction spending showed a rebound in April from a weak first-quarter level.

Real net exports are anticipated to subtract about 1-1/2 percentage points from GDP growth this quarter. The drag from the external sector is much smaller than that in the first quarter, but twice what we had projected in the previous Greenbook. To



some extent, the greater projected decline in net exports this quarter reflects an upward revision to exports in the first quarter--largely the result of revised seasonal factors.

We indicated in the last Greenbook that inventory investment in the first quarter--now estimated to have been more than \$100 billion (annual rate)--appeared improbably large. It still looks like more than can be squared with other evidence, including the lack of more than isolated reports of inventory overhangs. But we have yet to find any statistical flaws and thus are taking the numbers at face value. In the current quarter, available information suggests that petroleum inventories have continued to grow, but less than in the first quarter. Motor vehicle stocks are being depleted by the combination of strong sales and GM production shortfalls. And, outside of motor vehicles, the April figures suggest that the pace of inventory accumulation in manufacturing and trade was well below that earlier in the year; indeed, to get to the level of inventory investment implicit in our 2 percent GDP forecast, we have had to assume more sizable increases in these categories for May and June. Even with that "plug," overall inventory investment is projected to subtract about 2-1/2 percentage points from GDP growth this quarter.

As for prices, the incoming data were a bit less favorable in May than we had anticipated, and we now project that the overall CPI will increase 2 percent at an annual rate in the current quarter, about 1/2 percentage point above our previous forecast. Part of the surprise was in food, where an increase in fresh vegetable prices in May is likely to be reversed in coming months. However, the core CPI also is projected to rise somewhat more--around 2-3/4 percent--as motor vehicle prices reportedly fell only slightly last month despite the introduction of new manufacturers' incentives, and rents and cigarette prices continued to increase more rapidly than we were anticipating. On the wage side, recent increases in average hourly earnings have been about in line with our expectations of a gradual pickup in nominal pay gains. Although we continue to hear widespread reports of labor shortages, many employers appear to have responded by using narrowly targeted larger wage hikes or by letting positions go unfilled.

#### **The Outlook for the Economy beyond the Current Quarter**

On the assumption that the GM labor disputes will be settled in the next couple of weeks, we expect that a recovery in vehicle production will give a boost to GDP growth in the coming months. But the ongoing downshift in net exports and non-auto inventory investment is likely to continue weighing heavily on activity, and we have

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

Measure	1998:H1	1998:H2	1999
<b>Real GDP</b>	<b>3.7</b>	<b>1.8</b>	<b>2.0</b>
Previous	3.9	1.8	2.3
Final sales	4.2	2.4	2.1
Previous	4.2	2.8	2.3
PCE	5.7	3.6	2.6
Previous	5.5	3.6	2.6
Residential investment	14.3	-.8	-2.8
Previous	15.1	-2.1	-2.4
BFI	14.1	6.7	6.1
Previous	13.3	6.8	6.9
Government purchases	1.4	.6	.9
Previous	.4	1.3	.9
Exports	-2.2	1.0	3.8
Previous	-1.1	3.6	5.0
Imports	13.0	7.7	6.5
Previous	10.9	7.6	7.0
	Change, billions of chained (1992) dollars		
Inventory change	-21.4	-20.7	-9.5
Previous	-16.3	-35.9	.2
Net exports	-83.8	-41.2	-45.0
Previous	-66.6	-32.6	-37.7

GDP growth remaining sluggish in the second half of the year. Although the direct drags from these two sectors are projected to abate in 1999, the lagging multiplier-accelerator effects will tend to damp demand growth next year, as will the anticipated decline in the ratio of household wealth to income. On average, we are projecting that real GDP will grow at an annual rate of just under 2 percent over the next six quarters, more than 1/2 percentage point slower than the estimated rise in potential output.

That differential implies an easing of the pressures in the labor market, but a sub-5 percent unemployment rate can scarcely be characterized as slack conditions. Moreover, oil prices are expected to recover some of their marked decline of the past

year, as are non-oil import prices, given the anticipated behavior of the dollar. However, competitive forces are likely to remain a significant constraint on pricing in many product markets. In particular, unless manufacturing investment falls more rapidly than we are projecting, excess capacity in many industries will put a cap on pricing power. Further large real compensation gains for workers are thus likely to be reflected in some squeeze on average profit margins rather than in a more-pronounced nominal wage-price spiral.

**Consumer spending.** Growth in real personal consumption expenditures is projected to slow to about 3-1/2 percent at an annual rate in the second half of this year from the 5-1/2 percent pace of the first half. Even this reduced pace is substantial, however, and it would leave the growth of spending for the year as a whole well in excess of income gains. We believe that the major force behind this surge in demand is the run-up in household wealth--most important, the capital gains on share holdings but with some contribution from rising housing equity as well. In addition, the opportunity to refinance mortgages at lower interest rates has provided households with some additional spendable cash flow--and, in many instances, the opportunity to reduce financial uncertainty by shifting from adjustable-rate to fixed-rate mortgage debt. Given our forecasts for financial variables, we expect spending to move into closer alignment with the growth of labor income over the next year and a half, and with employment growth slowing, this leads us to predict that real PCE will increase 2-1/2 percent during 1999.

Among the major components of consumer spending, outlays for durables are expected to show the steepest deceleration over the latter part of this year, from a double-digit pace in the first half to about 3-1/2 percent at an annual rate in the second. Sales of light motor vehicles account for much of this slowing: With the Big-Three coupon incentives scheduled to expire at the beginning of July and with Japanese producers apparently raising margins rather than cutting prices in response to the depreciation of the yen, unit sales are projected to drop below 15 million in the third quarter and to slow to a pace of 14-1/2 million by the end of 1999. Meanwhile, rapidly declining prices should continue to lift the demand for electronic goods, and the healthy pace of home sales should support spending on other household durables for a while. Outlays for services are also projected to remain relatively robust over the second half; the estimated strength in travel and other discretionary service outlays this year is entirely consistent with what we would expect to occur when consumers are feeling well-off. As the bloom begins to come off the stock market in the coming

months and jobs become a bit less abundant, confidence is likely to suffer somewhat, and spending should slow pretty much across the board in 1999.

**Residential investment.** As we suggested in our discussion of the current quarter, there may be a bit of a backlog developing in the single-family housing market, as builders struggle to keep up with a heavy demand. The backlog should provide some momentum to starts even as demand begins to wane with the slackening of employment and income growth. Consequently, we see single-family starts holding through the summer near the strong 1.23 million-1.24 million unit pace of the first five months of the year.

By the end of this year and in 1999, the deterioration in the fundamentals underlying demand, including some backup in mortgage rates, is expected to leave its mark on building activity. But with the cash-flow affordability of home ownership remaining extraordinarily favorable, that mark should not be a very deep one. At 1.13 million units, the volume of single-family starts projected for 1999 is equal to that for 1997--still a good year by historical standards. We believe that the oncoming supply should be sufficient to prevent a further acceleration of house prices in the aggregate, although there will undoubtedly be some hot markets that experience notable appreciation.

In the multifamily sector, starts are expected to move up a bit in coming months. The recent buildup in the backlog of permits is a positive indicator in this regard; in addition, declining vacancies and an ample supply of financing are providing considerable impetus to construction. Consequently, despite the slowing economy, we project that starts will average 320,000 units at an annual rate over the remainder of the forecast period, close to their current pace.

When one adds in a substantial volume of manufactured housing, the additions to the stock of dwelling units are expected to remain high relative to notional demographic trends. However, those trends are difficult to pinpoint and are quite elastic in the short run. Thus, we do not share the view of some private analysts that building activity is due for a sharp near-term setback because of excess supply.

**Business fixed investment.** Growth in real business fixed investment is projected to slow to 6-3/4 percent (annual rate) over the second half of this year from a robust pace of 14 percent in the first half. Financing costs are expected to remain low, and prices of high-tech equipment are projected to decline further. However, the deceleration in business activity should lower sales expectations and restrain cash flow, reducing the incentive to invest in new capital--particularly in industries where heavy

investment in recent years has led to sizable increases in capacity. These macro influences become even more pronounced in 1999, and thus growth in business fixed investment is projected to slow further, to around 6 percent.

After rising at what appears likely to be almost a 20 percent annual rate in the first half of this year, equipment spending is forecast to increase about 8 percent in the second half and 7-1/2 percent in 1999. Growth of real computer outlays is projected to drop back further from its astonishing 100 percent first-quarter pace, but with an unrelenting supply of new products, and with declining prices continuing to spur demand, this "slowdown" still is expected to leave purchases rising 30 percent next year. Spending on communication equipment is also expected to be brisk over the next six quarters, reflecting the significant advances being made in wireless communications and other efforts to capitalize on the opportunities presented by technological and regulatory changes. In contrast, outlays for many other types of equipment are expected to slow sharply, or even decline, in coming quarters. In particular, we anticipate that motor vehicle purchases will edge off from their high current levels as business activity decelerates. In addition, investment in basic industrial equipment will likely be curtailed by the emergence of more widespread excess capacity in the manufacturing sector; in fact, we have cut back our projection of factory capacity growth in 1999 to "just" 2 percent, but owing largely to the weaker trade outlook, utilization is nonetheless expected to drop below 80 percent.

After a puzzling string of declines in late 1997 and early 1998, investment in nonresidential structures appears to have turned up recently, and we are projecting further increases in construction over the projection period--around 3-1/2 percent at an annual rate in the second half of this year and 2-1/2 percent in 1999. Office buildings and other commercial properties--for which rents and prices appear to be rising--are expected to account for much of the overall gain. In contrast, spending on industrial buildings is projected to decline over the projection period, reflecting the efforts to trim capacity growth in manufacturing.

**Business inventories.** Even if our estimate of a large negative swing in nonfarm inventory investment this quarter is on the mark, stocks would still be growing at a 3-3/4 percent annual rate--in excess of the sustainable trend of real sales. Thus, although overhangs of undesired stocks are evident only in a few areas, we anticipate that, in the aggregate, firms will want to reduce the pace of accumulation further. We expect that the adjustment in the pace of nonfarm investment will be

fully accomplished by the end of the year and that inventories will not be a major factor in the dynamics of the economy in 1999.

In agriculture, crop conditions have been slipping in some regions of the country, and concerns about the weather have heightened in recent days, just as some of the key crops are about to enter the most critical phase of their annual production cycles. These developments have led us to trim a little from our projection of farm output. Nonetheless, given the sluggish outlook for exports, we still anticipate that the harvests will be large enough to generate further additions to the stockpiles of crops, though not quite so much as was expected in the last Greenbook.

**Government spending.** Real federal consumption and investment expenditures are projected to fall 2-1/4 percent at an annual rate, on average, over the next six quarters. Defense purchases are expected to decline roughly 3 percent at an annual rate, on average, over this period, while real nondefense purchases should be relatively flat, given that the discretionary caps imply a small increase in nominal spending.

As noted earlier, real purchases by state and local governments are projected to jump a little this quarter, after a winter lull. Over the next year and a half, growth is expected to run at an average annual rate of about 2-1/2 percent--a moderate advance that certainly will not strain the financial resources of the sector. The fiscal positions of most states have been much improved by positive revenue surprises, and with the recently signed federal transportation bill providing renewed funding for infrastructure, we anticipate that construction spending will pick up somewhat in coming quarters. More generally, however, state legislatures have been relatively conservative in approving new spending increases, instead enacting small tax cuts or caching revenue windfalls in "rainy day" funds. We see no reason to expect this tendency to change over the forecast period, especially given the projected deceleration in economic activity.

**Net exports.** Given our assumption of a higher exchange value for the dollar and indications of significantly more serious problems in Asia and in some emerging economies elsewhere, we are forecasting a somewhat greater deterioration in our external balances than in the May Greenbook. In particular, our projection for the growth of real exports of goods and services has been revised down to 1 percent at an annual rate over the second half of this year and to only 3-3/4 percent in 1999. The effects of the higher dollar on imports are about offset by the slight downward revision to U.S. activity, and thus the projected increase in real imports--7-3/4 percent at an annual rate in the second half of this year and 6-1/2 percent in 1999--is about the

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

Measure	1997	1998	1999
Output per hour, nonfarm business <sup>1</sup>	1.8	1.3	1.4
Previous	2.3	1.0	1.6
Nonfarm payroll employment	2.7	2.0	.9
Previous	2.5	1.7	1.2
Household employment survey	2.1	1.4	.5
Previous	2.1	1.3	.9
Labor force participation rate <sup>2</sup>	67.1	67.1	67.1
Previous	67.1	67.2	67.2
Civilian unemployment rate <sup>2</sup>	4.7	4.4	4.9
Previous	4.7	4.5	4.8

1. Corrected by FRB staff for length-of-pay-period problem.

2. Percent, average for the fourth quarter.

same as in our previous forecast. On balance, net exports are now projected to reduce real U.S. GDP growth about 1-1/2 percentage points in 1998 and 1/2 percentage point in 1999—a quarter point more, on average, than in the last Greenbook. (A more detailed discussion is contained in the *International Developments* section.)

**Labor markets.** There have been ongoing anecdotes about employers having to scramble—and, in some cases, to lower their standards—to add to their work forces in this tight labor market. In all probability, many employers have yet to meet their hiring goals, and thus payroll gains in the near term are projected to diminish only a little from the 250,000 per month pace posted thus far this year. Eventually, however, the deceleration in business activity should damp employers' enthusiasm for adding workers, and thus job growth is anticipated to drop to less than 150,000 per month by the end of this year and to around 100,000 per month in 1999. With employment growth falling below its trend rate, the unemployment rate rises in 1999, approaching 5 percent by the end of the year.

Reflecting the presumed lag between output growth and employment growth implicit in our analysis, we are projecting a sharp diminution in labor productivity gains. Output per hour in the nonfarm business sector, which we expect will be up at close to a 2 percent annual rate in the first half of this year (corrected for length-of-pay-period effects), is projected to rise only 1 percent over the second half. As firms

get their work forces into alignment with ongoing levels of production, productivity growth picks up again in 1999. However, the need to divert labor resources to addressing Year 2000 problems is expected to hold next year's gains a bit below trend as well.<sup>3</sup>

**Wages and prices.** We have raised our inflation forecast a touch relative to the May Greenbook. The unemployment rate this year is projected to be a tenth below our previous forecast, suggesting some additional upward pressures from tighter labor markets. Moreover, incoming data are giving greater hints that demand pressures are starting to show through to prices, especially for services. Lower crude oil prices and steeper declines in other import prices provide some offset in the near term, but these favorable influences wane over 1999.

We have added a little to our forecast of compensation inflation in the next couple of quarters, given the greater near-term tightness of the labor market and the larger increases in prices of late. We have also responded, in part, to anecdotal reports of bigger pay hikes. But, for all practical purposes, our projection for the ECI still can be described as showing a flat path for compensation increases at about 3-1/2 percent per annum--the pace recorded over the year ended in March. As in previous Greenbooks, increases in nominal compensation are expected to be damped by the low rates of overall price inflation; in real terms (measured in product prices), compensation gains are projected to remain well above the trend growth rate of productivity. An additional consideration, once again, is the notion that the wider use of "flexible" pay structures will make compensation increases more sensitive to the slowing in the pace of economic growth, both through the commission component of wages and through the "nonproduction bonus" component of benefits. In our forecast, a deceleration of bonuses prevents a larger pickup in overall benefit costs associated with the acceleration in health insurance costs that we are projecting.<sup>4</sup>

On the price side, core consumer prices are projected to increase 2.3 percent in both 1998 and 1999, 1/10 point more than in the May Greenbook. Adjusting for technical changes, the core CPI accelerates 0.6 percentage point between 1997 and

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3. As in the last Greenbook, we are assuming that the trend rate of productivity growth is 1.5 percent per year *on a consistently measured basis*. Allowing for the effects of technical changes in the CPI, the trend estimates are 1.6 percent in 1998 and 1.8 percent in 1999.

4. As an indication of the direction in which health insurance costs are headed, the California Public Employees Retirement System (CalPERS) and Kaiser Permanente HMO recently reached an agreement that will raise health insurance premiums in 1999 by 10-3/4 percent for active employees. The size of this increase reflects, in part, ongoing financial difficulties at Kaiser, and our forecast is for employer health insurance costs overall to rise about 6 percent next year.



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

Measure	1997	1998	1999
Consumer price index	1.9	1.7	2.2
Previous	1.9	1.6	2.1
Food	1.7	1.4	2.0
Previous	1.7	1.3	1.7
Energy	-1.0	-5.3	1.7
Previous	-1.0	-4.4	1.1
Excluding food and energy	2.2	2.3	2.3
Previous	2.2	2.2	2.2
PCE chain-weighted price index	1.5	1.3	1.9
Previous	1.5	1.4	1.8
Excluding food and energy	1.5	1.7	1.9
Previous	1.5	1.7	1.8
GDP chain-weighted price index	1.8	1.5	1.7
Previous	1.8	1.5	1.7
ECI for compensation of private industry workers <sup>1</sup>	3.4	3.6	3.5
Previous	3.4	3.4	3.4
Prices of core non-oil merchandise imports	-.8	-2.3	1.6
Previous	-.8	-1.7	1.3
	Percentage points		
<i>MEMO: Adjustments for technical changes to the CPI<sup>2</sup></i>			
Core CPI	.2	.4	.7
Core PCE	.1	.1	.4
GDP chain price index	.1	.1	.2

1. December to December.

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

1999. It is tempting to discount some of the recent bad news on prices as indicative of factors unrelated to the high level of activity and labor cost pressures. The brisk rise in cigarette prices is an obvious case, and pharmaceutical price hikes may not be a product of purely cyclical factors. But, at bottom, we believe that it would be dangerous to slice and dice the overall CPI and set these items off to the side, when

aggregate demand is so strong and labor cost pressures would seem to be tilted toward a pickup in inflation.

We may not have seen all the disinflationary effects of the recent international developments. Business contacts suggest that lower-priced materials and merchandise will be arriving from abroad in coming months. In our forecast, non-oil import prices are projected to exert a bit more restraint on goods prices over the second half of this year than in the May Greenbook. In 1999, though, the expected depreciation of the dollar is anticipated to lead to some rise in these prices, contributing to that year's acceleration in the core CPI on a consistently measured basis.

The total CPI is projected to increase 1.7 percent this year and 2.2 percent in 1999. Retail energy prices, which fell sharply over the first five months of the year, are expected to move up along with oil prices in coming quarters, but they still end the year 5-1/2 percent lower than in the fourth quarter of 1997. Energy prices are forecast to rise about 1-3/4 percent in 1999. In conjunction with the lowering of the forecasts of farm output and farm inventory change, we have nudged up our projection for consumer food prices, more so in 1999 than in 1998. With futures prices for livestock exhibiting renewed weakness since mid-May, we continue to think that the rise in food prices this year will be appreciably less than the rise in core inflation. Next year, however, the gap between core inflation and food inflation seems likely to narrow. Livestock production apparently is headed for a slowdown in 1999, and the recent upswing in crop prices, while still of moderate proportions as of this writing, will likely exacerbate the production slowdown to some degree.

### **Money and Credit Flows**

Domestic nonfinancial sector debt posted a 6-1/4 percent (annual rate) increase in the first quarter, but growth appears to have dropped back in the second quarter to a pace of about 4-3/4 percent. A contraction in federal government debt accounts for most of the slowing. Net borrowing by the private sectors and by state and local governments appears to have moderated only a bit in recent months, and the staff forecast anticipates little further diminution in debt growth for these sectors in coming quarters. Overall, total debt is expected to rise 5-1/2 percent this year on a month-average basis, placing it a little above the mid-point of the FOMC monitoring range, and to rise 4-1/2 percent in 1999. In both 1998 and 1999, the expansion of total debt is the better part of a percentage point faster than the projected growth of nominal GDP.

Business debt is forecast to expand briskly, albeit at somewhat less than the 8-1/4 percent annual rate estimated for the first half of this year. The weakening of corporate profits in the projection implies that further increases in nominal capital spending will necessitate an increased reliance on external funds. The greater pressures on internal funds likely will lead to some slackening in the pace of share repurchases and merger activity. Banks may continue to add appreciably to their C&I loan portfolios, but the bond markets are expected to remain the primary funding source for corporate borrowers--whether through direct issues or through securitized loans. Although the yield curve may steepen slightly, and risk spreads may widen a bit on bonds as profitability deteriorates, firms likely will continue to find markets generally receptive to long-term offerings.

Household debt growth is also expected to remain high and to outpace personal income growth over the next year and a half. Households, like many businesses, have been able to lower interest costs and stretch out maturities of their debt. As a result, borrowing of late does not appear to have resulted in a rise in debt payment burdens, at least in the aggregate, and such burdens are expected to remain about unchanged through 1999. Moreover, evidence continues to mount that the deterioration in the quality of consumer credit has been stemmed or, in the cases where problems appeared to be the most severe (for example, auto finance companies), reversed to some degree. As a result, we do not anticipate any significant further pull-back on the part of lenders, especially in light of continued solid growth of household income and tight labor markets.

The expansion of home mortgage debt should tend to be damped by the projected leveling of nominal construction outlays, but cutting against that probably will be continuing growth in the home equity loan business. The rising trend of home prices is providing more equity to tap, through either home equity loans or cash-out refinancings, and is also making mortgage credit look less risky to lenders. Consumer credit growth is expected to edge off further in coming quarters, owing in part to the ongoing substitution of mortgage debt for higher-rate credit card and other installment debt.

Special factors that have lifted state and local government borrowing in recent quarters--namely advance refunding of higher-cost debt and public takeover of a utility--are likely to wane. Nonetheless, the combination of low municipal bond rates and sound financial conditions of state and local governments appears to be stimulating funding for capital projects, and we expect debt growth for the sector to

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

Measure	1997	1998	1999
<i>Real GDP</i>			
Baseline	3.7	2.7	2.0
Higher funds rate	3.7	2.6	1.3
Lower funds rate	3.7	2.8	2.7
Constant stock market wealth-to-income ratio	3.7	2.8	2.3
<i>Civilian unemployment rate<sup>1</sup></i>			
Baseline	4.7	4.4	4.9
Higher funds rate	4.7	4.4	5.2
Lower funds rate	4.7	4.4	4.6
Constant stock market wealth-to-income ratio	4.7	4.4	4.8
<i>CPI excluding food and energy</i>			
Baseline	2.2	2.3	2.3
Higher funds rate	2.2	2.3	2.0
Lower funds rate	2.2	2.3	2.6
Constant stock market wealth-to-income ratio	2.2	2.3	2.3

1. Average for the fourth quarter.

level off at around 5 percent in coming quarters. Federal government debt, in contrast, is expected to shrink at an average 1-3/4 percent annual rate over the next year and a half.

The recent slowing of M2 growth is projected to extend into the second half of the year. As a result, the declines in M2 velocity of late are projected to abate, and M2 growth falls roughly in line with GDP growth by the end of this year. M3 expansion is projected to remain faster than income growth, owing both to the rapid rise of institutional money market accounts favored by business treasurers and to the need by banks to fund strong growth of depository credit.

### Alternative Simulations

Our alternative, model-based simulations assess the implications of different assumptions about interest rates and the stock market. In the first alternative, the federal funds rate rises 25 basis points per quarter beginning in the third quarter of

this year, reaching 100 basis points above the baseline in the second quarter of 1999; the funds rate is assumed to remain at that level thereafter. This tightening of policy reduces real GDP growth 0.1 percentage point in the second half of this year and 0.7 percentage point in 1999. As a result, the unemployment rate rises above 5 percent by the end of next year, reducing the pressures on resource utilization. The increase in the core CPI next year is 0.3 percent below the baseline forecast, essentially eliminating the acceleration when core prices are measured on a consistent basis. The second, symmetric, alternative assumes a 100-basis-point decline in the funds rate between now and the second quarter of 1999. In this scenario, the unemployment rate remains near 4-1/2 percent throughout the projection period, and core consumer price inflation rises to 2.6 percent in 1999.

The third alternative assumes that the stock market wealth-to-income ratio holds steady over the projection period, rather than declining as we are anticipating in the baseline forecast. In this scenario, real GDP growth is 0.1 percentage point higher in the baseline forecast this year and 0.3 percentage point higher in 1999. The unemployment rate is slightly lower next year in this simulation, but not by enough to have a noticeable effect on core CPI inflation.

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

June 24, 1998

Interval	Nominal GDP		Real GDP		GDP chain-weighted price index		Consumer price index <sup>1</sup>		Unemployment rate <sup>2</sup>		
	05/14/98	06/24/98	05/14/98	06/24/98	05/14/98	06/24/98	05/14/98	06/24/98	05/14/98	06/24/98	
<b>ANNUAL</b>											
1995	4.6	4.6	2.0	2.0	2.5	2.5	2.8	2.8	5.6	5.6	
1996	5.1	5.1	2.8	2.8	2.3	2.3	3.0	3.0	5.4	5.4	
1997	5.8	5.8	3.8	3.8	2.0	2.0	2.3	2.3	4.9	4.9	
1998	4.8	4.8	3.4	3.3	1.4	1.4	1.6	1.6	4.5	4.4	
1999	3.8	3.5	2.1	1.8	1.7	1.7	2.1	2.2	4.7	4.7	
<b>QUARTERLY</b>											
1996	Q1	4.7	4.7	1.8	1.8	2.8	2.8	3.2	3.2	5.6	5.6
	Q2	7.7	7.7	6.0	6.0	1.9	1.9	3.7	3.7	5.4	5.4
	Q3	3.6	3.6	1.0	1.0	2.7	2.7	2.6	2.6	5.3	5.3
	Q4	6.2	6.2	4.3	4.3	1.9	1.9	3.3	3.3	5.3	5.3
1997	Q1	7.4	7.4	4.9	4.9	2.4	2.4	2.0	2.0	5.3	5.3
	Q2	5.2	5.2	3.3	3.3	1.8	1.8	1.5	1.5	4.9	4.9
	Q3	4.6	4.6	3.1	3.1	1.4	1.4	1.8	1.8	4.9	4.9
	Q4	5.2	5.2	3.7	3.7	1.4	1.4	2.3	2.3	4.7	4.7
1998	Q1	6.1	6.5	5.2	5.4	0.9	1.0	0.5	0.5	4.7	4.7
	Q2	4.2	3.7	2.5	2.0	1.6	1.7	1.6	2.0	4.4	4.3
	Q3	3.6	3.6	1.8	2.0	1.7	1.6	2.3	2.0	4.5	4.3
	Q4	3.5	3.4	1.8	1.7	1.7	1.7	2.1	2.2	4.5	4.4
1999	Q1	4.0	3.4	2.0	1.5	1.9	1.9	2.1	2.4	4.6	4.6
	Q2	3.8	3.4	2.2	1.8	1.6	1.6	2.1	2.2	4.7	4.7
	Q3	4.0	3.9	2.3	2.2	1.6	1.6	2.1	2.2	4.7	4.8
	Q4	4.1	4.0	2.4	2.3	1.6	1.7	2.1	2.2	4.8	4.9
<b>TWO-QUARTER<sup>3</sup></b>											
1996	Q2	6.2	6.2	3.8	3.8	2.3	2.3	3.5	3.5	-0.2	-0.2
	Q4	4.9	4.9	2.7	2.7	2.3	2.3	2.9	2.9	-0.1	-0.1
1997	Q2	6.3	6.3	4.1	4.1	2.1	2.1	1.8	1.8	-0.4	-0.4
	Q4	4.9	4.9	3.4	3.4	1.4	1.4	2.0	2.0	-0.2	-0.2
1998	Q2	5.1	5.1	3.9	3.7	1.3	1.4	1.1	1.3	-0.3	-0.4
	Q4	3.5	3.5	1.8	1.8	1.7	1.6	2.2	2.1	0.1	0.1
1999	Q2	3.9	3.4	2.1	1.6	1.7	1.8	2.1	2.3	0.2	0.3
	Q4	4.0	4.0	2.4	2.3	1.6	1.6	2.1	2.2	0.1	0.2
<b>FOUR-QUARTER<sup>4</sup></b>											
1995	Q4	4.0	4.0	1.6	1.6	2.4	2.4	2.6	2.6	0.0	0.0
1996	Q4	5.6	5.6	3.2	3.2	2.3	2.3	3.2	3.2	-0.3	-0.3
1997	Q4	5.6	5.6	3.7	3.7	1.8	1.8	1.9	1.9	-0.6	-0.6
1998	Q4	4.3	4.3	2.8	2.7	1.5	1.5	1.6	1.7	-0.2	-0.3
1999	Q4	4.0	3.7	2.3	2.0	1.7	1.7	2.1	2.2	0.3	0.5

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.

Item	Units <sup>1</sup>	- Projected -								
		1991	1992	1993	1994	1995	1996	1997	1998	1999
<b>EXPENDITURES</b>										
Nominal GDP	Bill. \$	5916.7	6244.4	6558.1	6947.0	7265.4	7636.0	8079.9	8468.8	8768.3
Real GDP	Bill. Ch. \$	6079.4	6244.4	6389.6	6610.7	6742.1	6928.4	7188.8	7429.1	7563.2
Real GDP	% change	0.4	3.6	2.4	3.3	1.6	3.2	3.7	2.7	2.0
Gross domestic purchases		0.0	4.0	3.0	3.6	1.2	3.6	4.3	4.1	2.3
Final sales		-0.4	3.9	2.1	2.7	2.2	3.1	3.1	3.3	2.1
Priv. dom. final purchases		-0.8	4.9	3.7	3.7	2.5	3.8	4.3	5.5	2.8
Personal cons. expenditures		-0.2	4.2	2.7	3.1	2.2	2.7	3.6	4.6	2.6
Durables		-3.1	9.4	7.4	6.3	3.0	3.9	6.8	7.6	3.0
Nondurables		-1.0	3.4	1.6	3.0	1.0	1.8	1.4	4.1	1.8
Services		0.9	3.6	2.3	2.5	2.7	2.8	4.0	4.3	2.9
Business fixed investment		-6.0	5.5	9.9	7.6	6.5	11.7	9.0	10.3	6.1
Producers' dur. equipment		-2.6	9.6	12.2	10.2	8.3	12.2	12.9	13.3	7.5
Nonres. structures		-12.5	-3.4	4.5	1.1	2.0	10.3	-0.7	2.5	2.5
Residential structures		1.1	16.9	7.8	4.2	-1.9	3.9	5.6	6.5	-2.8
Exports		8.6	4.1	4.6	10.0	10.3	9.3	10.2	-0.6	3.8
Imports		4.1	7.4	10.2	12.3	5.6	11.8	14.4	10.3	6.5
Gov't. cons. & investment		-0.7	1.7	-1.4	0.1	-1.4	2.0	1.0	1.0	0.9
Federal		-3.1	1.3	-6.1	-3.9	-6.0	1.5	-0.7	-1.6	-1.9
Defense		-5.3	-1.3	-6.9	-6.0	-5.9	1.1	-0.8	-4.1	-2.4
State & local		1.0	2.0	2.0	2.7	1.4	2.2	2.0	2.4	2.4
Change in bus. inventories	Bill. Ch. \$	-3.0	7.0	22.1	60.6	27.3	25.0	65.7	59.3	26.5
Nonfarm		-1.2	2.0	29.5	49.0	35.7	22.5	57.8	52.1	21.3
Net exports		-22.3	-29.5	-70.2	-104.6	-98.8	-114.4	-146.5	-250.3	-316.3
Nominal GDP	% change	3.8	6.3	5.0	5.8	4.0	5.6	5.6	4.3	3.7
<b>EMPLOYMENT AND PRODUCTION</b>										
Nonfarm payroll employment	Millions	108.3	108.6	110.7	114.1	117.2	119.6	122.7	125.7	127.1
Unemployment rate	%	6.8	7.5	6.9	6.1	5.6	5.4	4.9	4.4	4.7
Industrial prod. index	% change	-0.0	3.7	3.3	6.5	3.3	4.2	5.8	1.6	1.7
Capacity util. rate - mfg.	%	77.9	79.4	80.5	82.5	82.8	81.4	81.7	80.5	79.6
Housing starts	Millions	1.01	1.20	1.29	1.46	1.35	1.48	1.47	1.55	1.45
Light motor vehicle sales		12.53	12.86	13.88	15.03	14.74	15.06	15.06	15.14	14.66
North Amer. produced		9.74	10.51	11.71	12.88	12.82	13.34	13.12	13.18	12.78
Other		2.78	2.35	2.16	2.14	1.91	1.71	1.94	1.97	1.89
<b>INCOME AND SAVING</b>										
Nominal GNP	Bill. \$	5932.4	6255.5	6576.8	6955.2	7270.6	7637.7	8060.1	8440.9	8726.9
Nominal GNP	% change	3.5	6.2	5.1	5.7	4.1	5.5	5.2	4.1	3.6
Nominal personal income		3.7	7.3	4.2	5.1	5.2	5.8	6.0	4.7	3.9
Real disposable income		0.8	4.0	1.5	2.4	2.4	2.0	3.7	2.8	2.6
Personal saving rate	%	6.0	6.2	5.1	4.2	4.8	4.3	3.9	2.9	2.7
Corp. profits, IVA & CCAadj.	% change	4.5	11.3	19.0	14.1	11.0	9.1	9.4	-3.3	0.3
Profit share of GNP	%	6.9	6.8	7.5	8.2	8.9	9.6	10.0	9.6	9.0
Excluding FR Banks		6.6	6.6	7.2	7.9	8.6	9.3	9.7	9.3	8.8
Federal surpl./deficit	Bill. \$	-196.0	-280.9	-250.7	-186.7	-174.4	-110.5	-28.8	61.9	35.0
State & local surpl./def.		75.8	86.3	87.4	96.8	103.1	105.3	107.8	114.6	116.4
Ex. social ins. funds		11.5	18.3	19.7	27.9	32.5	34.1	36.3	42.8	44.5
Gross natl. saving rate	%	15.7	14.5	14.4	15.5	16.0	16.6	17.3	17.4	16.5
Net natl. saving rate		4.8	3.7	3.7	4.7	5.5	6.4	7.3	7.5	6.5
<b>PRICES AND COSTS</b>										
GDP chn.-wt. price index	% change	3.3	2.6	2.6	2.5	2.4	2.3	1.8	1.5	1.7
Gross Domestic Purchases										
chn.-wt. price index		2.7	2.7	2.3	2.5	2.3	2.3	1.3	1.0	1.7
CPI		3.0	3.1	2.7	2.7	2.6	3.2	1.9	1.7	2.2
Ex. food and energy		4.4	3.5	3.1	2.8	3.1	2.6	2.2	2.3	2.3
ECI, hourly compensation <sup>2</sup>		4.4	3.5	3.6	3.1	2.6	3.1	3.4	3.6	3.5
Nonfarm business sector										
Output per hour		2.2	3.5	-0.2	-0.1	0.6	1.7	2.1	0.7	1.4
Compensation per Hour		4.8	4.5	1.8	1.9	3.1	3.9	4.1	4.0	3.5
Unit labor cost		2.5	1.0	2.0	2.0	2.4	2.2	2.0	3.3	2.2

1. Changes are from fourth quarter to fourth quarter.

2. Private-industry workers.

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

June 24, 1998

Item	Units	1995 Q1	1995 Q2	1995 Q3	1995 Q4	1996 Q1	1996 Q2	1996 Q3	1996 Q4	1997 Q1	1997 Q2
<b>EXPENDITURES</b>											
Nominal GDP	Bill. \$	7168.9	7209.5	7301.3	7381.9	7467.5	7607.7	7676.0	7792.9	7933.6	8034.3
Real GDP	Bill. Ch. \$	6703.7	6708.8	6759.2	6796.5	6826.4	6926.0	6943.8	7017.4	7101.6	7159.6
Real GDP	% change	0.9	0.3	3.0	2.2	1.8	6.0	1.0	4.3	4.9	3.3
Gross domestic purchases		1.3	0.2	1.9	1.3	3.1	6.5	2.4	2.5	5.9	3.7
Final sales		1.8	1.9	3.3	2.0	2.6	5.2	0.2	4.5	3.0	2.5
Priv. dom. final purchases		2.5	2.2	2.7	2.5	4.4	5.5	2.1	3.2	5.1	2.9
Personal cons. expenditures		1.5	2.9	2.6	1.8	3.1	3.7	0.5	3.3	5.3	0.9
Durables		-3.0	3.9	9.3	2.0	4.8	9.7	-1.9	3.5	14.1	-5.4
Nondurables		1.7	0.9	0.7	0.7	1.7	2.6	0.6	2.1	4.7	-2.1
Services		2.4	3.7	2.2	2.3	3.5	3.1	1.0	3.9	3.9	3.9
Business fixed investment		14.2	5.7	1.6	4.9	11.7	13.0	16.5	5.9	4.1	14.6
Producers' dur. equipment		16.1	6.2	2.0	9.4	13.1	14.9	19.1	2.6	6.7	23.0
Nonres. structures		9.5	4.3	0.7	-5.8	8.2	7.9	10.0	15.3	-2.1	-4.7
Residential structures		-7.0	-15.5	8.4	8.5	8.3	17.9	-4.5	-4.3	3.3	7.4
Exports		7.2	9.3	13.5	11.5	1.7	9.6	1.9	25.5	9.9	18.4
Imports		10.0	7.7	2.3	2.4	13.1	14.1	13.2	6.8	17.9	20.5
Gov't. cons. & investment		0.6	-0.1	-0.7	-5.4	1.8	7.2	-1.1	0.1	-0.4	3.1
Federal		-1.1	-4.5	-1.3	-16.4	7.5	8.8	-4.2	-5.2	-5.8	6.6
Defense		-1.1	-1.6	-4.0	-15.9	6.1	11.0	-4.6	-7.1	-11.8	7.5
State & local		1.7	2.6	-0.4	1.9	-1.4	6.3	0.7	3.3	2.7	1.2
Change in bus. inventories	Bill. Ch. \$	48.5	21.6	17.0	22.2	8.0	21.3	37.9	32.9	63.7	77.6
Nonfarm		54.7	34.0	29.6	24.4	14.5	17.3	31.6	26.5	58.3	70.1
Net exports		-113.5	-112.8	-92.9	-76.1	-100.8	-112.6	-138.9	-105.6	-126.3	-136.6
Nominal GDP	% change	4.2	2.3	5.2	4.5	4.7	7.7	3.6	6.2	7.4	5.2
<b>EMPLOYMENT AND PRODUCTION</b>											
Nonfarm payroll employment	Millions	116.5	116.9	117.4	117.9	118.5	119.3	120.0	120.7	121.5	122.3
Unemployment rate	%	5.5	5.7	5.7	5.6	5.6	5.4	5.3	5.3	5.3	4.9
Industrial prod. index	% change	5.9	1.6	4.5	1.1	2.0	7.5	3.6	3.8	5.2	4.6
Capacity util. rate - mfg.	%	83.8	82.9	82.6	81.8	81.0	81.6	81.5	81.4	81.6	81.5
Housing starts	Millions	1.32	1.29	1.42	1.42	1.47	1.49	1.49	1.42	1.47	1.46
Light motor vehicle sales		14.68	14.43	14.87	14.96	15.04	15.14	15.08	14.96	15.27	14.51
North Amer. produced		12.66	12.46	13.00	13.18	13.38	13.43	13.38	13.18	13.34	12.67
Other		2.02	1.97	1.87	1.78	1.67	1.71	1.70	1.77	1.92	1.85
<b>INCOME AND SAVING</b>											
Nominal GNP	Bill. \$	7175.1	7220.6	7298.3	7388.5	7475.3	7610.5	7669.1	7796.1	7919.2	8013.6
Real GNP	% change	4.5	2.6	4.4	5.0	4.8	7.4	3.1	6.8	6.5	4.9
Nominal personal income		7.4	4.1	4.3	5.1	6.8	6.6	5.1	4.8	8.0	5.0
Real disposable income		4.5	0.2	2.6	2.5	3.5	1.1	2.7	0.7	4.6	3.1
Personal saving rate	%	5.3	4.6	4.5	4.6	4.7	4.1	4.5	3.9	3.7	4.2
Corp. profits, IVA & CCAdj.	% change	-2.9	10.0	31.7	7.9	20.0	12.1	0.6	4.5	18.1	8.2
Profit share of GNP	%	8.5	8.7	9.2	9.3	9.6	9.7	9.6	9.6	9.8	9.9
Excluding FR Banks		8.2	8.4	8.9	9.0	9.3	9.4	9.4	9.3	9.6	9.6
Federal surpl./deficit	Bill. \$	-191.5	-179.5	-176.5	-150.2	-153.6	-111.6	-99.5	-77.1	-55.5	-36.8
State & local surpl./def.		107.7	105.6	101.1	97.8	104.1	114.4	102.6	100.4	104.7	104.9
Ex. social ins. funds		37.7	35.3	30.3	26.8	33.2	43.1	31.1	28.9	33.5	33.3
Gross natl. saving rate	%	15.8	15.7	16.0	16.6	16.3	16.5	16.9	16.7	16.8	17.4
Net natl. saving rate		5.4	5.1	5.5	6.0	6.0	6.4	6.7	6.6	6.7	7.4
<b>PRICES AND COSTS</b>											
GDP chn.-wt. price index	% change	3.3	2.1	2.0	2.1	2.8	1.9	2.7	1.9	2.4	1.8
Gross Domestic Purchases											
chn.-wt. price index		3.0	2.5	1.7	1.9	2.7	1.8	2.4	2.4	1.9	0.8
CPI		2.7	3.5	2.1	2.4	3.2	3.7	2.6	3.3	2.0	1.5
Ex. food and energy		3.3	3.3	2.8	3.0	2.5	2.5	2.7	2.7	2.2	2.6
ECI, hourly compensation <sup>1</sup>		2.9	2.6	2.6	2.9	2.5	3.5	2.8	2.8	2.5	3.7
Nonfarm business sector											
Output per hour		-1.8	0.8	1.4	2.2	2.8	2.9	-0.7	1.9	1.1	2.3
Compensation per hour		2.3	3.1	3.1	3.7	3.9	5.1	3.3	3.4	4.3	3.2
Unit labor cost		4.2	2.3	1.7	1.4	1.0	2.2	4.0	1.5	3.1	0.9

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)

June 24, 1998

em	Units	----- Projected -----									
		1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4
<b>EXPENDITURES</b>											
Nominal GDP	Bill. \$	8124.3	8227.4	8357.1	8432.8	8507.3	8577.9	8649.7	8722.9	8806.4	8894.1
Real GDP	Bill. Ch. \$	7214.0	7280.0	7376.2	7412.2	7448.7	7479.3	7506.4	7539.6	7581.4	7625.5
Real GDP	% change	3.1	3.7	5.4	2.0	2.0	1.7	1.5	1.8	2.2	2.3
Gross domestic purchases		4.3	3.4	7.6	3.5	2.9	2.4	2.0	2.3	2.6	2.5
Final sales		4.7	2.3	3.8	4.6	2.2	2.5	1.6	1.9	2.3	2.5
Priv. dom. final purchases		7.1	2.3	8.2	6.2	4.0	3.5	2.6	2.6	2.9	3.1
Personal cons. expenditures		5.6	2.5	6.1	5.2	3.8	3.3	2.6	2.5	2.6	2.7
Durables		18.4	1.9	15.8	8.2	1.9	5.1	2.7	2.6	3.3	3.4
Nondurables		4.3	-1.2	6.6	4.4	3.0	2.4	1.8	1.8	1.8	1.9
Services		3.9	4.4	4.0	5.1	4.7	3.4	3.0	2.9	2.9	2.9
Business fixed investment		19.2	-0.8	18.2	10.2	6.8	6.6	6.0	6.2	6.3	6.2
Producers' dur. equipment		24.1	-0.3	27.0	11.7	7.8	7.9	7.1	7.5	7.7	7.6
Nonres. structures		6.7	-2.3	-2.9	6.2	4.0	2.9	2.8	2.7	2.4	2.3
Residential structures		2.7	9.1	16.5	12.1	-0.5	-1.1	-6.9	-4.8	-0.4	1.3
Exports		4.4	8.3	-1.2	-3.2	0.3	1.7	2.4	3.6	4.4	4.9
Imports		14.6	5.3	16.9	9.3	8.1	7.3	6.4	7.8	6.6	5.3
Gov't. cons. & investment		1.1	0.3	-3.2	6.1	-0.7	1.9	-0.1	1.6	1.3	0.7
Federal		-1.1	-2.3	-9.8	10.4	-6.7	0.7	-4.6	0.3	-0.8	-2.3
Defense		1.2	1.0	-18.4	13.8	-10.3	1.6	-6.4	0.4	-1.3	-2.1
State & local		2.3	1.8	0.7	3.8	2.7	2.6	2.4	2.3	2.4	2.4
Change in bus. inventories	Bill. Ch. \$	47.5	74.0	103.8	52.6	48.8	31.9	29.7	27.7	26.2	22.4
Nonfarm		38.3	64.5	94.8	45.2	42.2	26.1	24.2	22.5	21.0	17.3
Net exports		-164.1	-159.1	-207.9	-242.9	-266.2	-284.1	-298.2	-313.7	-324.0	-329.1
Nominal GDP	% change	4.6	5.2	6.5	3.7	3.6	3.4	3.4	3.4	3.9	4.0
<b>EMPLOYMENT AND PRODUCTION</b>											
Nonfarm payroll employment	Millions	123.0	123.9	124.8	125.5	126.1	126.5	126.7	127.0	127.2	127.6
Unemployment rate	%	4.9	4.7	4.7	4.3	4.3	4.4	4.6	4.7	4.8	4.9
Industrial prod. index	% change	6.0	7.2	1.0	1.8	1.6	1.8	1.5	1.6	1.8	2.1
Capacity util. rate - mfg.	%	81.6	82.2	81.5	80.6	80.0	79.8	79.6	79.6	79.6	79.6
Housing starts	Millions	1.45	1.53	1.58	1.55	1.56	1.50	1.45	1.45	1.45	1.45
Light motor vehicle sales		15.34	15.10	15.01	15.67	14.90	14.99	14.86	14.66	14.59	14.54
North Amer. produced		13.31	13.14	13.05	13.71	12.93	13.02	12.95	12.76	12.71	12.69
Other		2.03	1.96	1.97	1.96	1.98	1.97	1.91	1.90	1.88	1.85
<b>INCOME AND SAVING</b>											
Nominal GNP	Bill. \$	8103.5	8204.2	8338.6	8407.4	8473.3	8544.3	8613.3	8684.5	8761.5	8848.2
Nominal GNP	% change	4.6	5.1	6.7	3.3	3.2	3.4	3.3	3.3	3.6	4.0
Nominal personal income		4.6	6.3	6.6	4.4	4.2	3.7	3.8	3.8	4.0	3.9
Real disposable income		2.6	4.5	4.7	2.5	2.4	1.5	5.2	1.8	1.9	1.8
Personal saving rate	%	3.5	3.9	3.7	3.1	2.7	2.3	2.9	2.8	2.6	2.4
Corp. profits, IVA & CCAadj.	% change	17.2	-4.4	7.6	-7.0	-9.2	-3.6	-2.1	-2.8	1.7	4.8
Profit share of GNP	%	10.2	10.0	10.0	9.7	9.4	9.3	9.1	9.0	9.0	9.0
Excluding FR Banks		9.9	9.7	9.7	9.5	9.2	9.0	8.9	8.7	8.7	8.7
Federal surpl./deficit	Bill. \$	-10.8	-12.1	54.2	56.6	73.6	63.4	26.8	31.5	40.5	41.2
State & local surpl./def.		111.4	110.1	108.6	117.4	116.2	116.2	115.4	116.5	116.0	117.5
Ex. social ins. funds		40.0	38.6	36.8	45.6	44.4	44.4	43.5	44.6	44.1	45.6
Gross natl. saving rate	%	17.4	17.5	18.1	17.5	17.3	16.7	16.7	16.5	16.5	16.3
Net natl. saving rate		7.5	7.5	8.2	7.7	7.3	6.7	6.7	6.5	6.4	6.3
<b>PRICES AND COSTS</b>											
GDP chn.-wt. price index	% change	1.4	1.4	1.0	1.7	1.6	1.7	1.9	1.6	1.6	1.7
Gross Domestic Purchases		1.3	1.4	0.1	1.0	1.2	1.7	1.9	1.6	1.6	1.6
chn.-wt. price index		1.8	2.3	0.5	2.0	2.0	2.2	2.4	2.2	2.2	2.2
CPI		1.9	2.1	2.4	2.7	2.2	2.1	2.3	2.3	2.3	2.3
Ex. food and energy		3.4	4.3	2.7	4.0	3.9	3.9	3.4	3.5	3.5	3.5
ECI, hourly compensation <sup>1</sup>		3.6	1.4	0.9	0.0	0.7	1.1	0.9	1.1	1.7	1.7
Nonfarm business sector		3.8	5.2	4.2	3.9	3.9	3.9	3.5	3.5	3.5	3.5
Output per hour		0.2	3.8	3.3	4.0	3.3	2.9	2.6	2.4	1.8	1.9
Compensation per hour											
Unit labor cost											

1. Private-industry workers.

Item	1995 Q3	1995 Q4	1996 Q1	1996 Q2	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	95Q4/ 94Q4	96Q4/ 95Q4	97Q4/ 96Q4
Real GDP	3.0	2.2	1.8	6.0	1.0	4.3	4.9	3.3	3.1	1.6	3.2	3.7
Gross dom. purchases	1.9	1.3	3.1	6.6	2.4	2.5	6.0	3.7	4.4	1.2	3.6	4.4
Final sales	3.3	1.9	2.6	5.2	0.2	4.5	3.0	2.5	4.7	2.2	3.1	3.1
Priv. dom. final purchases	2.3	2.0	3.6	4.5	1.7	2.7	4.2	2.4	5.8	2.0	3.1	3.6
Personal cons. expenditures	1.8	1.2	2.1	2.5	0.4	2.2	3.6	0.6	3.8	1.5	1.8	2.4
Durables	0.7	0.2	0.4	0.8	-0.2	0.3	1.1	-0.5	1.4	0.2	0.3	0.5
Nondurables	0.1	0.1	0.4	0.5	0.1	0.4	0.9	-0.4	0.8	0.2	0.4	0.3
Services	0.9	0.9	1.4	1.2	0.4	1.5	1.5	1.5	1.5	1.0	1.1	1.6
Business fixed investment	0.2	0.5	1.1	1.3	1.6	0.6	0.4	1.4	1.9	0.6	1.1	0.9
Producers' dur. equip.	0.1	0.6	0.9	1.0	1.3	0.2	0.5	1.6	1.7	0.6	0.9	0.9
Nonres. structures	0.0	-0.2	0.2	0.2	0.3	0.4	-0.1	-0.1	0.2	0.1	0.3	-0.0
Residential structures	0.3	0.3	0.3	0.7	-0.2	-0.2	0.1	0.3	0.1	-0.1	0.2	0.2
Net exports	1.1	1.0	-1.3	-0.6	-1.4	1.8	-1.0	-0.4	-1.3	0.4	-0.4	-0.6
Exports	1.4	1.2	0.2	1.1	0.2	2.7	1.1	2.0	0.5	1.1	1.0	1.2
Imports	-0.2	-0.3	-1.5	-1.7	-1.6	-0.8	-2.1	-2.5	-1.7	-0.7	-1.4	-1.8
Government cons. & invest.	-0.1	-1.0	0.3	1.3	-0.2	0.0	-0.1	0.6	0.2	-0.3	0.4	0.2
Federal	-0.1	-1.2	0.5	0.6	-0.3	-0.4	-0.4	0.4	-0.1	-0.4	0.1	-0.0
Defense	-0.2	-0.8	0.3	0.5	-0.2	-0.3	-0.6	0.3	0.1	-0.3	0.0	-0.0
Nondefense	0.1	-0.4	0.2	0.1	-0.1	0.0	0.2	0.1	-0.1	-0.2	0.1	-0.0
State and local	0.0	0.2	-0.2	0.7	0.1	0.4	0.3	0.1	0.3	0.2	0.3	0.2
Change in bus. inventories	-0.2	0.3	-0.8	0.7	0.8	-0.2	1.8	0.8	-1.6	-0.6	0.1	0.5
Nonfarm	-0.2	-0.3	-0.6	0.1	0.8	-0.2	1.8	0.7	-1.7	-0.5	0.0	0.5
Farm	0.0	0.6	-0.2	0.5	0.1	-0.1	0.0	0.1	0.1	-0.1	0.1	0.0

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

Item	1997 Q4	1998 Q1	1998 Q2	1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	97Q4/ 96Q4	98Q4/ 97Q4	99Q4/ 98Q4
Real GDP	3.7	5.4	2.0	2.0	1.7	1.5	1.8	2.2	2.3	3.7	2.7	2.0
Gross dom. purchases	3.4	7.7	3.5	3.0	2.4	2.0	2.4	2.6	2.5	4.4	4.1	2.4
Final sales	2.3	3.8	4.6	2.2	2.5	1.6	1.9	2.3	2.5	3.1	3.3	2.1
Priv. dom. final purchases	1.9	6.7	5.1	3.3	2.9	2.2	2.2	2.5	2.6	3.6	4.5	2.3
Personal cons. expenditures	1.7	4.1	3.5	2.6	2.3	1.8	1.7	1.8	1.8	2.4	3.1	1.8
Durables	0.2	1.2	0.7	0.2	0.4	0.2	0.2	0.3	0.3	0.5	0.6	0.2
Nondurables	-0.2	1.3	0.8	0.6	0.5	0.4	0.3	0.4	0.4	0.3	0.8	0.4
Services	1.8	1.6	2.0	1.9	1.4	1.2	1.2	1.2	1.2	1.6	1.7	1.2
Business fixed investment	-0.1	1.8	1.1	0.7	0.7	0.6	0.7	0.7	0.7	0.9	1.1	0.7
Producers' dur. equip.	0.0	1.9	0.9	0.6	0.6	0.6	0.6	0.6	0.6	0.9	1.0	0.6
Nonres. structures	-0.1	-0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	-0.0	0.1	0.1
Residential structures	0.4	0.6	0.5	-0.0	-0.0	-0.3	-0.2	-0.0	0.1	0.2	0.3	-0.1
Net exports	0.3	-2.2	-1.5	-1.0	-0.7	-0.6	-0.6	-0.4	-0.2	-0.6	-1.4	-0.4
Exports	1.0	-0.1	-0.4	0.0	0.2	0.3	0.4	0.5	0.5	1.2	-0.1	0.4
Imports	-0.7	-2.1	-1.2	-1.0	-0.9	-0.8	-1.0	-0.9	-0.7	-1.8	-1.3	-0.9
Government cons. & invest.	0.1	-0.6	1.0	-0.1	0.3	-0.0	0.3	0.2	0.1	0.2	0.2	0.2
Federal	-0.1	-0.7	0.6	-0.4	0.0	-0.3	0.0	-0.1	-0.1	-0.0	-0.1	-0.1
Defense	0.0	-0.9	0.5	-0.4	0.1	-0.3	0.0	-0.1	-0.1	-0.0	-0.2	-0.1
Nondefense	-0.2	0.2	0.1	0.0	-0.0	-0.0	0.0	0.0	-0.1	-0.0	0.1	-0.0
State and local	0.2	0.1	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.3	0.3
Change in bus. inventories	1.4	1.5	-2.5	-0.2	-0.8	-0.1	-0.1	-0.1	-0.2	0.5	-0.5	-0.1
Nonfarm	1.4	1.6	-2.5	-0.1	-0.8	-0.1	-0.1	-0.1	-0.2	0.5	-0.5	-0.1
Farm	0.0	-0.0	-0.0	-0.0	-0.0	-0.0	-0.0	0.0	0.0	0.0	-0.0	-0.0

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

Item	Fiscal year <sup>5</sup>				1997				1998				1999			
	1996 <sup>a</sup>	1997 <sup>a</sup>	1998	1999	Q1 <sup>a</sup>	Q2 <sup>a</sup>	Q3 <sup>a</sup>	Q4 <sup>a</sup>	Q1 <sup>b</sup>	Q2	Q3	Q4	Q1	Q2	Q3	Q4
UNIFIED BUDGET																
Not seasonally adjusted																
Receipts <sup>1</sup>	1453	1579	1715	1767	349	496	387	386	378	543	406	417	383	538	429	422
Outlays <sup>1</sup>	1561	1601	1652	1714	401	396	398	426	409	406	411	464	398	424	428	440
Surplus/deficit <sup>1</sup>	-107	-22	63	53	-52	100	-11	-40	-30	138	-5	-47	-15	114	1	-19
On-budget	-174	-103	-36	-65	-69	61	-19	-66	-51	95	-14	-48	-67	61	-12	-56
Off-budget	67	81	98	119	17	39	8	26	21	43	9	1	52	53	13	37
Surplus excluding deposit insurance <sup>2</sup>	-116	-36	58	49	-56	97	-12	-41	-31	136	-7	-48	-16	113	0	-20
Means of financing																
Borrowing	130	38	-49	-49	48	-69	11	34	26	-84	-25	30	8	-96	9	6
Cash decrease	-6	1	4	0	-1	-18	8	12	4	-48	36	4	16	-15	-5	10
Other <sup>3</sup>	-16	-17	-17	-4	5	-13	-7	-6	0	-6	-5	13	-9	-3	-5	2
Cash operating balance, end of period	44	44	40	40	33	51	44	32	28	76	40	36	20	35	40	30
NIPA FEDERAL SECTOR																
Seasonally adjusted annual rate																
Receipts	1550	1692	1823	1866	1675	1709	1742	1767	1816	1845	1863	1876	1847	1862	1879	1896
Expenditures	1679	1737	1780	1825	1731	1746	1753	1780	1761	1789	1790	1813	1820	1830	1839	1855
Consumption expend.	447	460	464	469	458	464	465	468	457	469	464	466	468	470	471	470
Defense	302	309	308	308	306	311	312	314	301	312	306	308	308	309	309	308
Nondefense	145	151	156	161	152	153	153	154	155	157	158	158	161	161	162	162
Other expenditures	1232	1277	1315	1357	1273	1282	1288	1311	1305	1320	1326	1347	1352	1360	1368	1385
Current account surplus	-129	-45	43	41	-56	-37	-11	-12	54	57	74	63	27	32	40	41
Gross investment	69	61	60	59	58	62	61	59	59	61	59	60	59	59	59	59
Current and capital account surplus	-197	-106	-16	-18	-114	-99	-72	-71	-5	-5	14	4	-32	-27	-18	-17
FISCAL INDICATORS <sup>4</sup>																
High-employment (HEB) surplus/deficit	-220	-164	-119	-116	-167	-164	-144	-155	-107	-115	-97	-105	-130	-120	-108	-105
Change in HEB, percent of potential GDP	-.7	-.7	-.6	0	-.2	0	-.2	.1	-.6	.1	-.2	.1	.3	-.1	-.1	0
Fiscal impetus (FI), percent, cal. year	-2.3	-1.9	-1.6	-.5	-1.1	1.5	.2	-1.7	-2.3	3.5	-1.7	-.9	.9	-.2	-.5	-1.4

1. OMB's May 1998 surplus estimates (assuming the enactment of the President's proposals) are \$39 billion in FY98 and \$54 billion in FY99. In May 1998, CBO revised its surplus estimates to a range of \$43 billion to \$63 billion for FY98 and a range of \$30 billion to \$40 billion for FY99. Budget receipts, outlays, and surplus/deficit include corresponding social security (OASDI) categories. The OASDI surplus is excluded from the on-budget deficit and shown separately as off-budget, as classified under current law. The Postal Service deficit is included in off-budget outlays beginning in FY90.

2. OMB's May 1998 surplus estimates (assuming the enactment of the President's proposals), excluding deposit insurance spending, are \$35 billion in FY98 and \$51 billion in FY99.

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 rise from 2.3 percent in 1996 to 2.5 percent in 1999, reflecting CPI modifications. Quarterly figures for change in HEB and FI are not at annual rates. Change in HEB, as a percent of nominal potential GDP, is reversed in sign. FI is the weighted difference of discretionary changes in federal spending and taxes in chained (1992) dollars, scaled by real federal consumption plus investment. For change in HEB and FI, negative values indicate restraint.

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

a--Actual.

b--Preliminary.

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>									
1989	7.3	7.0	7.3	8.6	9.9	6.0	6.7	5.6	6.4
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	0.7	2.9	6.3
1993	5.0	8.3	3.8	5.2	4.3	7.6	1.4	6.7	5.0
1994	4.6	4.7	4.6	7.5	5.8	14.5	3.7	-2.7	5.8
1995	5.4	4.1	5.9	7.8	5.5	14.1	6.3	-3.1	4.0
1996	5.3	4.0	5.8	7.8	8.0	7.9	4.7	1.3	5.6
1997	5.3	0.6	6.9	6.8	7.5	4.3	7.1	7.0	5.6
1998	5.3	-1.5	7.5	7.4	8.2	4.1	7.7	7.5	4.3
1999	4.4	-1.9	6.4	6.5	7.5	3.2	6.6	5.1	3.7
<i>Quarter</i>									
1997:3	5.3	0.8	6.9	7.2	9.4	4.1	6.9	5.4	4.6
4	6.2	1.1	8.0	7.2	8.2	2.3	8.8	8.3	5.2
1998:1	6.2	-0.8	8.5	7.8	8.2	4.5	8.9	10.3	6.5
2	4.8	-3.7	7.6	7.3	8.1	4.1	7.6	8.7	3.7
3	4.4	-2.8	6.7	6.9	7.9	3.8	6.8	5.3	3.6
4	5.3	1.4	6.5	6.6	7.7	3.7	6.9	5.0	3.4
1999:1	4.4	-2.3	6.4	6.6	7.5	3.5	6.6	5.1	3.4
2	3.7	-5.2	6.3	6.4	7.3	3.4	6.6	5.0	3.4
3	4.9	0.8	6.1	6.2	7.1	3.0	6.3	4.9	3.9
4	4.4	-1.2	6.0	6.0	7.0	2.7	6.3	4.9	4.0

Note. Quarterly data are at seasonally adjusted annual rates.

1. Data after 1998:Q1 are staff projections. Changes are measured from end of the preceding period to end of period indicated except for annual nominal GDP growth, which is calculated from Q4 to Q4.

2. On a monthly average basis, total debt is projected to grow 5.4 percent in 1998 and 4.6 percent in 1999.

3. On a monthly average basis, federal debt is projected to grow -1.5 percent in 1998 and -1.3 percent in 1999.

4. On a monthly average basis, nonfederal debt is projected to grow 7.7 percent in 1998 and 6.4 percent in 1999.

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

Category	Calendar year				Seasonally adjusted annual rates									
					1997		1998				1999			
	1996	1997	1998	1999	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<i>Net funds raised by domestic nonfinancial sectors</i>														
1 Total	663.6	649.4	679.6	618.4	703.7	789.2	831.6	657.8	571.3	657.9	606.0	502.4	720.8	644.3
2 Net equity issuance	-64.2	-114.8	-122.9	-90.0	-83.2	-144.1	-109.6	-82.0	-118.0	-182.0	-98.0	-94.0	-86.0	-82.0
3 Net debt issuance	727.8	764.2	802.5	708.4	786.9	933.4	941.2	739.8	689.3	839.9	704.0	596.4	806.8	726.3
<i>Borrowing sectors</i>														
<i>Nonfinancial business</i>														
4 Financing gap <sup>1</sup>	6.8	48.2	75.6	81.4	25.3	54.0	82.4	58.6	88.1	73.4	72.6	81.1	84.0	87.9
5 Net equity issuance	-64.2	-114.8	-122.9	-90.0	-83.2	-144.1	-109.6	-82.0	-118.0	-182.0	-98.0	-94.0	-86.0	-82.0
6 Credit market borrowing	195.8	311.3	364.1	334.1	311.6	406.0	419.7	363.0	332.4	341.1	332.1	338.1	332.1	334.1
<i>Households</i>														
7 Net borrowing <sup>2</sup>	372.7	350.3	404.3	381.4	381.4	388.0	426.9	411.8	395.0	383.5	392.1	385.1	377.6	371.1
8 Home mortgages	261.0	262.2	309.8	304.2	337.7	303.4	307.5	312.9	311.8	306.9	307.4	304.4	301.4	303.4
9 Consumer credit	88.8	52.5	51.6	42.1	50.5	28.8	56.9	52.0	49.5	47.8	46.0	45.0	40.5	37.0
10 Debt/DPI (percent) <sup>3</sup>	88.7	90.4	92.6	94.7	90.6	90.9	91.5	92.3	93.1	93.9	93.8	94.5	95.1	95.7
<i>State and local governments</i>														
11 Net borrowing	14.3	79.5	90.9	65.9	63.6	98.6	124.6	107.4	67.8	63.9	65.9	65.9	65.9	65.9
12 Current surplus <sup>4</sup>	123.2	107.0	106.8	109.6	89.9	137.7	125.2	101.6	100.2	100.1	119.0	109.8	119.2	90.4
<i>Federal government</i>														
13 Net borrowing	145.0	23.1	-56.7	-73.0	30.3	40.8	-30.0	-142.4	-105.8	51.4	-86.0	-192.7	31.3	-44.7
14 Net borrowing (quarterly, n.s.a.)	145.0	23.1	-56.7	-73.0	10.6	33.7	25.9	-83.7	-25.3	30.4	8.0	-96.3	9.0	6.3
15 Unified deficit (quarterly, n.s.a.)	110.9	2.4	-55.3	-81.4	10.9	39.7	30.2	-137.6	5.1	47.1	15.1	-114.3	-1.0	18.8
<i>Depository institutions</i>														
16 Funds supplied	232.9	336.9	275.5	279.9	188.9	476.0	316.8	218.7	278.5	287.9	276.9	277.9	281.9	282.9
<i>Memo (percentage of GDP)</i>														
17 Domestic nonfinancial debt <sup>5</sup>	184.4	183.5	184.3	186.7	183.1	183.5	183.4	184.3	184.7	185.4	186.1	186.4	186.7	187.0
18 Domestic nonfinancial borrowing	9.5	9.5	9.5	8.1	9.7	11.3	11.3	8.8	8.1	9.8	8.1	6.8	9.2	8.2
19 Federal government <sup>6</sup>	1.9	0.3	-0.7	-0.8	0.4	0.5	-0.4	-1.7	-1.2	0.6	-1.0	-2.2	0.4	-0.5
20 Nonfederal	7.6	9.2	10.1	8.9	9.3	10.8	11.6	10.5	9.3	9.2	9.1	9.0	8.8	8.7

Note. Data after 1998:Q1 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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### Recent Developments

Recent developments abroad have been dominated by continued disappointing news from Asia. Export-weighted foreign GDP growth came to a standstill in the first quarter, and we expect only a small improvement in the second quarter. This performance is considerably weaker than anticipated in the May Greenbook, with the downward revisions concentrated in the Asian economies. The U.S. trade deficit has continued to widen, reflecting the decline in demand from Asia and the strength of the dollar.

The dollar appreciated sharply against the other major currencies on a weighted average basis between the May FOMC meeting and the middle of June but has since declined and is now up a little more than 1 percent on balance. The recent movements in the foreign exchange value of the dollar have largely reflected changes in the yen, which reached an eight-year low against the dollar on June 15 in response to additional negative data on the Japanese economy and to intensified pessimism about the ability of Japanese authorities to deal with the country's financial sector problems. The yen weakness also put considerable pressure on other Asian currencies, notably the Hong Kong dollar and the Chinese renminbi. The yen appreciated sharply following coordinated intervention by U.S. and Japanese authorities on June 17, including sales of \$833 million against yen from the accounts of the Treasury and the System. (This was the first U.S. operation since August 1995.)

The sizable impact of the intervention appeared to be related to Secretary Rubin's statement that U.S. participation was "in the context of Japan's plans to strengthen its economy." However, the market was subsequently disappointed when there were no immediate follow-up actions; the yen weakened again and is now about 3 percent lower against the dollar than it was at the time of the last FOMC meeting. Japanese long-term interest rates mirrored the movements in the dollar-yen rate. The Nikkei equity price index was relatively stable over the intermeeting period.

The dollar has shown little net change since the May FOMC meeting against the mark and other continental European currencies, as long-term rates in these countries fell in conjunction with U.S. long rates while short-term rates changed little. In contrast, sterling has appreciated nearly 3 percent relative to the dollar in response to recent information suggesting that the economy is not slowing as much as had been anticipated. Concern that U.K. inflation may be rising prompted a surprise 25-basis-

point increase in official rates on June 4, and markets appear to be anticipating another rate hike in the near future. The Canadian dollar reached a new low in response to further weakness in prices of the commodities that make up a large share of Canadian exports. Canadian stock prices have also fallen, nearly 7 percent. Movements in equity prices in the European countries have been mixed; prices have fallen in the United Kingdom and Italy and have risen in Germany and France.

The broad nominal index of the dollar is up about 1½ percent since the May FOMC meeting partly as a result of a 2 percent appreciation relative to the emerging market currencies. The Indonesian rupiah firmed early in the period following the resignation of President Suharto but then weakened in conjunction with the yen, as did the currencies of several of the other Asian developing countries. Although these currencies later rallied along with the yen, the rupiah is down more than 20 percent on balance, while most of the other currencies have shown much smaller net changes. The Mexican peso has depreciated about 4 percent relative to the dollar in part in response to declining oil prices. Equity prices in most emerging market economies continued to fall over the intermeeting period.

Japanese real GDP shrank at an annual rate of 5.3 percent in the first quarter, the second consecutive quarter of negative growth. Recent indicators on household spending and industrial production point to yet another decline in output in the second quarter, despite an expected boost from public construction spending as the latest fiscal stimulus package comes on line. Forward-looking indicators of private demand, such as machinery orders and business confidence, have fallen sharply in recent months as well.

A slowdown in export growth in the first quarter in the major continental European countries indicates some spillover from the Asian crises, although strong domestic demand helped sustain real GDP growth. Both consumption and investment posted solid gains in France and Germany, and early second-quarter indicators, including French consumption of manufactured products and German orders for manufactured goods, have shown further increases. Real GDP in Italy contracted slightly in the first quarter as net exports fell sharply, but domestic demand rose as a result of a hefty gain in business investment. Unemployment rates have dropped in nearly all of the euro-area countries in recent months, contributing to a continued rise in consumer confidence. Business confidence in the region, which had been rising steadily for more than a year, has dipped slightly in the last few months largely because of a deterioration in export orders, but it remains at a relatively high level.



The drop in Asian demand along with the strength of sterling has helped to curb the hard-charging U.K. economy in recent months, and business confidence has fallen sharply. However, growth of consumer demand remains robust; consumption rose at an annual rate of 4 percent in the first quarter, and retail sales were up sharply further in May. The strength of the domestic economy has been reflected in falling unemployment and rising wage growth.

The Canadian economy has also been resilient so far this year in the face of the Asian crises and the severe January ice storm, supported by strong export demand from the United States and a declining Canadian dollar. Although domestic demand paused in the first quarter after more than a year of rapid gains, the fundamental factors favor a rebound, given that employment and income growth have remained strong and capacity utilization is at its highest level in nearly twenty years. Nonetheless, the weakness in Asia, along with resulting lower commodity prices, has led to some tempering of the very optimistic business outlook.

Inflation remains low in most of the major foreign industrial countries, aided by falling oil prices and some remaining economic slack. Only in the United Kingdom is there serious concern about an acceleration in prices in the near-term. Although the recent increase in U.K. inflation to more than 3 percent largely reflected a transitory surge in food prices and the timing of recent budgetary measures, underlying inflation remains above the target of 2½ percent and wage pressures are increasing.

In marked contrast to the recent generally favorable developments in Europe and Canada, real GDP in the Asian developing economies plunged an estimated 9 percent at an annual rate in the first quarter, with declines in excess of 20 percent in Korea, Malaysia, and Indonesia. Less dramatic but still hefty contractions occurred in Hong Kong and Thailand. Real GDP growth in China also appears to have slowed, but remained positive. Twelve-month inflation soared to more than 50 percent in Indonesia in April and picked up, although to much lower levels, in the other front-line economies.

Economic performance diverged sharply across the Latin American countries in the first quarter, with Mexico, Argentina, and Chile continuing to expand at healthy rates while the Brazilian and Venezuelan economies appear to have contracted. Although falling oil production has contributed to some moderation in Mexican growth so far this year, there is little evidence so far of a dramatic slowdown. Brazil continues to suffer the effects of financial market contagion from Asia; although the overnight interest rate has been reduced considerably since last fall, it is still in excess

of 20 percent. Russian financial markets also remain under pressure because of internal financial problems, including continued weakness in tax revenues and associated large budget deficits, as well as Asian contagion.

The nominal U.S. trade deficit in goods and services widened further in April following a substantial deterioration in the first quarter; the April deficit at an annual rate was about \$35 billion larger than the first-quarter average. Exports fell in April to a level about 2 percent below the first-quarter average, with about half of the decline attributable to aircraft and the rest spread among several other categories. Thus far this year, the decline in exports has been more than accounted for by a fall in shipments to Asia. Imports also fell in April, although by less than exports, but they were up moderately relative to the first quarter, particularly in the consumer goods category.

Oil imports rose sharply in April, mostly because of an acceleration in stockbuilding, although consumption was also surprisingly strong. Preliminary Department of Energy statistics indicate that oil imports were high again in May because of a large accumulation of stocks, while oil consumption returned to its April rate.

The price of imported oil rose slightly in April and May, but it remained more than 30 percent below its peak in the fall of last year, reflecting increased supply from the OPEC countries, resumption of oil exports from Iraq, weak demand from Asia, and plentiful inventories following the mild winter. West Texas intermediate spot prices, which had risen from less than \$13 per barrel in March to trade in a range of \$14.75 to \$16.50 per barrel during April, briefly plunged below \$12 per barrel in June in response to reports of surprisingly high levels of world oil stocks and a sharp downward revision in the figures for oil consumption in Asia during the first quarter. The spot price has rebounded on news of further cuts in production by major oil producers and is currently just under \$15 per barrel.

Prices of U.S. non-oil imports declined in April-May on average about 3¼ percent at an annual rate from the first-quarter, reflecting both the continued strength of the dollar as well as weakness in non-oil commodity prices. Export prices rose in May as a result of an increase in prices of agricultural exports, but they were down about 2½ percent at an annual rate relative to the first quarter for April-May on average.

### Outlook

Growth in total foreign real GDP (weighted by shares of U.S. nonagricultural exports) is expected to show only a small rebound in the second quarter following a stagnant first quarter, to remain quite weak throughout the rest of this year, and to pick up only moderately in 1999. This forecast is considerably lower than that in the May Greenbook mainly because of a much gloomier outlook for Asia. The dollar is expected to depreciate slightly in real terms over the forecast period against an average of 29 currencies, principally reflecting modest nominal depreciation against most major currencies as well as higher inflation in the Asian developing economies than in the United States. Compared with the May Greenbook, the path of the dollar is about 3 percent higher over the forecast period. As a result of the less optimistic outlook for foreign growth as well as the stronger dollar, exports are now expected to fall about ½ percent (Q4/Q4) in 1998. The downward revision to our projection for exports reduces the contribution of real net exports to GDP growth this year to -1.4 percentage point, compared with -1.0 percentage point in the May Greenbook. However, the staff still expects the contribution of net exports to be less negative next year (-0.4 percentage point), as the effect of the past appreciation of the dollar wears off, foreign growth improves somewhat, and U.S. growth slows.

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

Measure	1997	Projection			
		1998			1999
		Q1	Q2	H2	
Foreign output	3.8	-0.3	0.8	1.7	2.6
<i>May</i>	4.0	1.5	2.2	2.5	3.0
Real exports	10.2	-1.2	-3.2	1.0	3.8
<i>May</i>	10.2	-4.3	2.2	3.6	5.0
Real imports	14.4	16.9	9.3	7.7	6.5
<i>May</i>	14.4	13.8	8.0	7.6	7.0

**The dollar.** We project that the dollar will depreciate almost 4 percent from its current level on balance against the major foreign currencies that make up the staff's narrow exchange-rate index by the end of 1999. Compared with the May forecast, the level of the dollar is about 2 percent higher in the near-term, reflecting recent developments, but is projected to reach a similar level by the end of next year. The yen is forecast to remain around its recent level through 1998 and to appreciate somewhat

during 1999 as fiscal stimulus takes hold, progress is made in resolving Japan's financial sector difficulties, and market participants increasingly focus on widening Japanese and U.S. external imbalances. Against the mark and the other continental European currencies, the dollar is expected to depreciate slightly over the forecast period as EMU developments continue on track and the prospective euro currencies benefit from a further unwinding of risk premiums as a result. We continue to assume that the Bundesbank will not tighten policy this year. The ECB is expected to raise rates next year by 50 basis points as activity in Euroland continues to strengthen.

The dollar's exchange value against the 29 currencies in the staff's broad exchange-rate index is projected to depreciate about 2 percent in real terms over the forecast period, as inflation rates move higher in the Asian countries most affected by the crises. This rate of depreciation is somewhat less than that projected in the May Greenbook in response to a downward revision to the pace of both economic activity and inflation in the Asian developing economies. We continue to project that the Chinese renminbi will remain unchanged against the dollar through the end of this year and subsequently will depreciate moderately, that the Hong Kong dollar's peg will hold, and that the Mexican peso will remain about unchanged in real terms.

**Foreign industrial countries.** Real GDP growth in the foreign G-7 countries, weighted by shares in U.S. nonagricultural exports, is expected to average about 2 percent in the second quarter, up from the first quarter pace of 1½ percent. Growth in these countries is expected to firm to about 2¼ percent (annual rate) over the rest of the forecast period. This projection is about ½ percentage point lower than in the last Greenbook for 1998 and also is slightly lower for 1999, with the downward revision owing entirely to a weaker outlook for Japan.

Real GDP in Japan is expected to fall 1 percent in 1998 (Q4/Q4) after contracting about ½ percent in 1997. Although GDP growth is expected to rebound somewhat in the second half of this year as a result of fiscal stimulus, growth is expected to drop back to about ½ percent in 1999 as the contribution from fiscal policy fades. Private domestic demand is expected to contract through 1998 and continue to be depressed by consumer and business pessimism during 1999.

Our projection for moderate growth in the rest of the major foreign industrial countries this year and next is little changed from the last Greenbook. For Euroland, growth is expected to continue at an annual rate of about 2¾ percent in the second half of this year as robust domestic demand growth offsets the impact of the Asian crises on net exports. The pace of expansion should improve to about 3 percent next year as the drag from net exports lessens. Growth in the United Kingdom is projected to slow

markedly this year in response to monetary tightening and the strength of sterling and to remain slightly below potential next year, easing some of the current inflationary pressure. Canadian growth is also expected to slow over the forecast period as consumer spending decelerates to a pace more in line with income growth, and investment growth is curbed by the past year's increases in interest rates.

Average consumer price inflation in the foreign G-7 countries (weighted by shares of U.S. bilateral imports) is projected to drop back to 1 percent this year as the effect of last year's Japanese VAT increase drops out of the calculation of twelve-month changes. Prices in Japan are expected to remain unchanged over the forecast period. Inflation rates in Euroland and Canada are projected to increase a little from current very low rates as growth picks up, but they should remain below 2 percent through the end of next year. Inflation in the United Kingdom is expected to average about  $2\frac{3}{4}$  percent over the forecast period, a little above the government's target.

As in the previous forecast, we assume that German short-term interest rates will change little over the course of this year, while rates in the other EMU countries should continue to converge to the German level. Next year, rates in Euroland are expected to rise 50 basis points. We have revised up our projection for U.K. interest rates in response to the recent strength in consumer demand and higher-than-expected inflation in May and are now showing one more 25-basis-point increase this year. We still expect rates to be reduced about 75 basis points over the course of next year as the economy cools. We are also assuming that Japanese short-term interest rates will be reduced to 25 basis points in response to weakening economic conditions. Long-term interest rates abroad are expected to change little on average this year and to edge up a little next year along with the general pickup in activity.

**Other countries.** The real GDP of major developing-country trading partners of the United States is projected to decrease about  $1\frac{1}{2}$  percent on average during 1998, a marked reduction from the May Greenbook. This downward revision is concentrated in the Asian countries and results from very weak first-quarter data and subsequent developments that point to a more protracted resolution of the crises in many of these countries. We now project that real GDP in the Asian developing countries will fall about 4 percent on average in 1998, including significant output declines in Indonesia, Malaysia, Korea, Thailand, and Hong Kong. Domestic demand in these countries is likely to be greatly restrained by continued volatility in currency and equity markets and weak financial sectors. Improvements in net exports over the remainder of this year should provide only a partial offset. We project that growth in most of these countries will recover in 1999, but to rates well below recent trends. Inflation in the Asian

developing countries is projected to rise significantly in 1998, reflecting the substantial depreciations of their currencies late last year and early this year.

Our forecast for real growth in Latin America during 1998 has been marked down about  $\frac{1}{2}$  percentage point to  $2\frac{1}{2}$  percent, reflecting some further spillover effects from the Asian crises on these countries. Growth in these countries is still expected to recover to about 4 percent next year, while inflation in most of them should continue to trend down.

**Real exports and imports of goods and services.** We have reduced our projection for U.S. export growth in response to the weaker outlook for foreign activity and the higher path of the dollar.<sup>1</sup> Exports of nonagricultural goods other than computers and semiconductors (core exports) are now projected to continue to fall over the rest of this year and to show only a small increase next year. Exports of services follow a roughly similar pattern to core exports. We continue to project rapid growth of real exports of computers and semiconductors, although at rates slower this year than last year. Overall, exports of goods and services are now expected to decline about  $\frac{1}{2}$  percent this year and to rise  $3\frac{3}{4}$  percent next year, compared with the May Greenbook projection for growth of about  $1\frac{1}{4}$  percent for this year and 5 percent for next year.

Imports of goods and services are projected to increase  $10\frac{1}{4}$  percent in 1998 and  $6\frac{1}{2}$  percent in 1999. The diminishing effect of the past appreciation of the dollar as well as slower growth in the U.S. economy should reduce growth of imports of core goods and services over the forecast period. Growth in imports of computers and semiconductors is projected to diminish somewhat, although the average pace should remain quite high. We expect the quantity of oil imports to change during the forecast period in line with movements in oil consumption.

**Oil prices.** We have lowered our projected path for the price of imported oil relative to the May Greenbook forecast by nearly \$1.00 per barrel in 1998 and \$0.50 per barrel in 1999 primarily as a result of our downward revision to the outlook for oil demand in Asia. After declining to \$12.25 per barrel during the second quarter, we project that the oil import unit value will rise to \$13.50 per barrel by the end of this year and will remain near that level through the end of 1999. This projection assumes that OPEC and non-OPEC producers will cut back production sufficiently so that the market will be able to absorb additional shipments from Iraq at a price for WTI near \$16.00 per barrel next year. There is considerable risk to this forecast. On the one

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1. The latest BEA revision to the trade data incorporates seasonal adjustment for more components of exports than was the case previously. As a consequence, residual seasonality has been largely eliminated from the quarterly pattern of export growth.

hand, if producers are unable to sustain the lower rate of production, then spot WTI could fall as low as \$11.00 per barrel in the near term. On the other hand, if Iraqi oil is withheld from the market again—especially near the end of the year when Iraq may be exporting as much as 2.0 mb/d—spot WTI could rise above \$20 per barrel.

**Prices of non-oil imports and exports.** Our forecasts for other merchandise trade prices are generally little changed from the May Greenbook. Prices of imports of non-oil goods other than computers and semiconductors (core imports) have continued to decline so far in the second quarter in response to the strength of the dollar and decreases in non-oil commodity prices. We expect a small further decline in import prices in the third quarter, followed by moderate increases over the forecast period as the dollar reverses some of its recent gains and commodity prices stabilize. Prices of core goods exports are also estimated to have fallen in the second quarter and are expected to ease further in the third quarter, but to firm toward the end of the year and then rise in line with comparable U.S. domestic prices.

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

Trade category	1997	Projection			
		1998			1999
		Q1	Q2	H2	
<i>Exports</i>					
Nonagricultural (core)	0.5	-2.4	-1.9	-0.1	1.2
Agricultural	-3.1	-16.5	-7.8	-3.1	2.0
<i>Imports</i>					
Non-oil (core)	-0.8	-3.5	-2.6	-1.6	1.6
Oil (level, dollars per barrel)	17.72	13.89	12.29	12.81	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.

**Nominal trade and current account balances.** The nominal trade deficit in goods and services is expected to continue to deteriorate over the forecast period, reaching over \$225 billion by the end of 1999. We also expect the deficit in net investment income to widen. As a result, the current account deficit is projected to increase from \$190 billion in the first quarter of 1998 to about \$300 billion for 1999, nearly 3½ percent of GDP.

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

Measure and country	1991	1992	1993	1994	1995	1996	----- Projected -----		
							1997	1998	1999
<b>REAL GDP</b>									
Canada	-0.3	0.9	3.1	4.5	0.8	2.0	4.0	3.3	2.7
Japan	2.5	0.1	0.5	0.8	2.4	3.4	-0.4	-1.0	0.4
United Kingdom	-1.6	0.4	2.7	4.9	2.0	2.9	2.9	2.0	2.0
Euro-11 Average (1)	2.1	0.1	-0.1	3.4	1.5	1.9	3.0	2.7	3.0
of which:									
France	1.4	-0.1	-0.5	4.1	0.3	2.3	3.1	2.4	2.7
Germany (2)	3.3	0.9	-0.2	3.4	0.7	2.1	2.3	2.5	2.9
Italy	1.9	-0.8	0.1	2.5	2.6	-0.2	2.6	2.1	2.9
Foreign G-7 Average weighted by 1991 GDP	1.7	0.2	0.6	2.8	1.7	2.3	1.8	1.3	1.9
Average weighted by share of U.S. nonagricultural exports									
Total foreign	3.3	2.3	3.4	5.0	1.9	4.1	3.8	0.9	2.6
Foreign G-7	0.8	0.5	1.9	3.6	1.3	2.3	2.8	2.1	2.2
Developing Countries	6.7	5.2	6.1	7.1	2.6	6.8	5.2	-1.4	3.0
<b>CONSUMER PRICES</b>									
Canada	4.1	1.8	1.8	-0.0	2.1	2.0	1.0	1.6	1.8
Japan	3.2	0.9	1.2	0.8	-0.8	0.1	2.1	0.0	0.0
United Kingdom (3)	5.7	3.7	2.7	2.2	2.9	3.2	2.8	2.9	2.8
Euro-11 Average (4)	NA	NA	NA	NA	2.7	2.0	1.4	1.7	1.9
of which:									
France	3.0	1.8	2.1	1.6	1.9	1.7	1.2	1.3	1.6
Germany (2)	4.0	3.4	4.2	2.6	1.7	1.4	1.8	1.5	1.8
Italy	6.1	4.9	4.1	3.8	5.9	2.7	1.6	1.8	2.0
Foreign G-7 Average weighted by 1991 GDP	4.1	2.4	2.5	1.8	1.6	1.5	1.8	1.2	1.3
Average weighted by share of U.S. non-oil imports	3.9	1.9	2.0	1.0	1.1	1.3	1.7	1.0	1.2

1. Includes all of the European Union countries except the United Kingdom, Denmark, Sweden, and Greece; weighted by GDP.
2. West German data through 1991; all Germany thereafter.
3. CPI excluding mortgage interest payments which is the targeted inflation rate.
4. Harmonized CPI's for the Euro-11, weighted by shares in final consumption of households converted to a common currency using estimated PPP exchange rates.



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

Measure and country	1997				----- 1998 -----				Projected ----- 1999 -----			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>REAL GDP</b>												
Canada	4.8	4.2	4.3	2.8	3.7	3.6	3.1	2.8	2.8	2.7	2.7	2.7
Japan	8.3	-10.6	3.2	-1.5	-5.3	-2.4	1.5	2.4	0.1	0.3	0.5	0.7
United Kingdom	2.1	3.5	3.6	2.5	2.0	2.3	1.8	1.7	1.8	1.8	2.1	2.1
Euro-11 Average (1)	1.5	5.1	3.2	2.1	2.6	2.7	2.8	2.7	2.8	2.8	3.1	3.1
of which:												
France	0.9	4.7	3.7	3.2	2.2	2.6	2.3	2.3	2.5	2.6	2.8	2.8
Germany	1.3	3.9	2.9	1.2	3.9	1.1	2.6	2.6	2.7	2.8	3.1	3.1
Italy	0.2	8.0	1.9	0.7	-0.4	4.1	2.5	2.5	2.5	2.5	3.4	3.4
Foreign G-7 Average weighted by 1991 GDP	3.7	-0.5	3.1	0.8	-0.3	0.9	2.1	2.4	1.7	1.8	2.1	2.2
Average weighted by share of U.S. nonagricultural exports												
Total foreign	5.2	3.7	4.5	2.0	-0.3	0.8	1.4	1.9	2.3	2.6	2.8	2.9
Foreign G-7	4.5	1.1	3.8	1.7	1.5	2.0	2.5	2.5	2.1	2.2	2.2	2.3
Developing Countries	6.7	6.5	5.7	2.1	-3.9	-1.6	-0.6	0.6	2.2	3.0	3.4	3.5
<b>CONSUMER PRICES (2)</b>												
Canada	2.1	1.6	1.7	1.0	1.0	1.2	1.4	1.6	1.7	1.7	1.8	1.8
Japan	0.0	1.5	1.7	2.1	2.1	0.5	0.0	0.0	-0.0	0.0	0.0	0.0
United Kingdom (3)	2.9	2.6	2.8	2.8	2.5	3.2	3.0	2.9	2.9	2.6	2.8	2.8
Euro-11 Average (4)	1.7	1.2	1.5	1.4	1.2	1.5	1.6	1.7	1.8	1.8	1.9	1.9
of which:												
France	1.5	0.9	1.3	1.2	0.7	1.0	1.3	1.3	1.4	1.5	1.6	1.6
Germany	1.7	1.6	1.9	1.8	1.2	1.4	1.4	1.5	1.7	1.8	1.8	1.8
Italy	2.4	1.6	1.5	1.6	1.7	1.8	1.8	1.8	2.1	2.0	2.0	2.0
Foreign G-7 Average weighted by 1991 GDP	1.4	1.6	1.8	1.8	1.6	1.3	1.2	1.2	1.3	1.3	1.3	1.3
Average weighted by share of U.S. non-oil imports	1.3	1.6	1.8	1.7	1.6	1.1	1.0	1.0	1.1	1.1	1.2	1.2

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1991	1992	1993	1994	1995	1996	--- Projected --- 1997	1998	1999
<b>NIPA REAL EXPORTS and IMPORTS</b>									
Percentage point contribution to GDP growth, Q4/Q4									
Net Goods & Services	0.4	-0.4	-0.6	-0.4	0.4	-0.4	-0.6	-1.4	-0.4
Exports of G&S	0.8	0.4	0.5	1.0	1.1	1.0	1.2	-0.1	0.4
Imports of G&S	-0.4	-0.8	-1.1	-1.4	-0.7	-1.4	-1.8	-1.3	-0.9
Percentage change, Q4/Q4									
Exports of G&S	8.6	4.1	4.6	10.0	10.3	9.3	10.2	-0.6	3.8
Services	7.1	-0.9	4.1	6.0	9.0	4.7	2.1	0.3	3.0
Agricultural Goods	10.1	10.4	-5.5	16.6	-3.4	5.7	2.5	-7.1	1.7
Computers	21.7	25.2	23.7	32.0	55.7	33.8	48.0	19.6	29.9
Semiconductors	41.8	64.8	32.9	66.9	80.4	45.9	21.4	8.7	30.2
Other Goods 1/	7.0	2.3	3.6	6.9	5.7	7.7	11.6	-2.5	0.9
Imports of G&S	4.1	7.4	10.2	12.3	5.6	11.8	14.4	10.3	6.5
Services	-2.7	1.4	3.2	1.4	7.3	5.0	10.6	4.4	2.3
Oil	8.1	12.1	10.1	-0.2	1.5	8.3	5.5	1.8	2.3
Computers	35.9	45.1	39.3	44.8	46.2	23.6	44.5	35.1	25.6
Semiconductors	55.3	42.0	34.2	54.5	92.7	57.9	32.6	10.1	31.0
Other Goods 2/	2.5	5.4	9.5	12.2	-1.3	10.6	12.9	10.3	5.2
Billions of chained 1992 dollars									
Net Goods & Services	-22.3	-29.5	-70.2	-104.6	-98.8	-114.4	-146.5	-250.3	-316.3
Exports of G&S	599.9	639.4	658.2	712.4	791.2	857.0	962.7	985.0	1007.5
Imports of G&S	622.2	669.0	728.4	817.0	890.1	971.5	1109.2	1235.3	1323.8
Billions of dollars									
US CURRENT ACCOUNT BALANCE	-4.4	-51.4	-86.1	-123.8	-115.3	-134.9	-155.2	-228.0	-293.9
Net Goods & Services (BOP)	-30.9	-38.7	-71.9	-100.9	-99.9	-108.6	-110.2	-164.9	-216.8
Exports of G&S (BOP)	581.2	617.3	643.2	703.8	795.6	850.8	937.6	931.4	945.8
Imports of G&S (BOP)	612.2	656.0	715.2	804.8	895.5	959.3	1047.8	1096.4	1162.5
Net Investment Income	21.5	22.5	23.9	16.5	19.3	14.2	-5.3	-21.8	-35.3
Direct, Net	55.6	51.6	55.7	51.8	63.0	66.2	63.7	55.2	54.7
Portfolio, Net	-34.1	-29.1	-31.7	-35.3	-43.7	-51.9	-69.1	-77.0	-90.1
Net Transfers	5.0	-35.2	-38.1	-39.4	-34.6	-40.6	-39.7	-41.2	-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

	1994				1995				1996			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
NIPA REAL EXPORTS and IMPORTS												
	Percentage point contribution to GDP growth											
Net Goods & Services	-1.0	-0.3	-0.4	0.3	-0.4	0.1	1.2	1.0	-1.3	-0.6	-1.4	1.8
Exports of G&S	-0.2	1.7	1.1	1.5	0.8	1.0	1.4	1.3	0.2	1.1	0.2	2.6
Imports of G&S	-0.8	-2.0	-1.5	-1.2	-1.2	-0.9	-0.3	-0.3	-1.5	-1.7	-1.6	-0.8
	Percentage change from previous period, SAAR											
Exports of G&S	-1.8	17.7	10.6	14.7	7.2	9.3	13.5	11.5	1.7	9.6	1.9	25.5
Services	2.4	12.9	2.0	6.9	6.0	3.8	20.3	6.6	-3.8	9.7	0.3	13.5
Agricultural Goods	-25.2	8.1	45.3	57.2	-1.3	-17.5	19.7	-10.7	12.5	-34.3	13.1	49.2
Computers	21.4	24.3	35.5	48.4	34.9	41.0	89.6	63.1	46.2	31.8	29.2	28.7
Semiconductors	111.8	23.4	65.9	79.1	72.0	97.0	100.3	56.2	19.9	28.3	37.6	113.8
Other Goods 1/	-6.8	20.3	7.4	8.6	2.9	8.1	0.9	10.9	-1.3	13.2	-2.9	24.2
Imports of G&S	7.6	19.0	13.1	9.9	10.0	7.7	2.3	2.4	13.1	14.1	13.2	6.8
Services	2.7	4.1	-0.4	-0.9	24.4	-4.0	8.4	2.2	14.6	2.7	1.2	2.1
Oil	-8.6	27.2	33.5	-36.2	-8.1	12.5	28.0	-19.7	-7.6	67.2	10.6	-19.6
Computers	32.9	48.3	42.3	57.0	8.1	57.3	65.8	61.8	6.4	30.7	26.9	32.0
Semiconductors	60.7	23.7	74.4	64.3	29.6	108.0	157.1	98.8	30.4	10.3	75.5	146.4
Other Goods 2/	6.8	19.6	10.3	12.5	7.3	2.2	-10.0	-3.7	14.5	11.1	12.4	4.6
	Billions of chained 1992 dollars, SAAR											
Net Goods & Services	-97.6	-103.9	-111.1	-105.9	-113.5	-112.8	-92.9	-76.1	-100.8	-112.6	-138.9	-105.6
Exports of G&S	676.0	704.1	722.1	747.3	760.4	777.4	802.4	824.6	828.2	847.4	851.4	901.1
Imports of G&S	773.6	808.0	833.2	853.2	873.9	890.3	895.4	900.7	929.0	960.0	990.2	1006.6
	Billions of dollars, SAAR											
US CURRENT ACCOUNT BALANCE	-97.3	-118.5	-135.9	-143.7	-123.7	-134.2	-115.5	-87.7	-112.8	-132.1	-161.6	-133.1
Net Goods & Services (BOP)	-85.9	-97.3	-111.2	-109.2	-109.3	-125.8	-90.0	-74.5	-92.4	-112.8	-132.3	-96.8
Exports of G&S (BOP)	668.0	693.1	714.3	740.0	765.4	782.0	809.7	825.6	833.6	845.3	837.5	886.7
Imports of G&S (BOP)	753.9	790.5	825.5	849.1	874.7	907.7	899.7	900.1	926.0	958.2	969.8	983.5
Net Investment Income	20.8	16.3	14.6	14.2	20.1	24.0	10.2	22.7	21.5	15.8	6.9	12.8
Direct, Net	52.3	49.5	52.2	53.2	59.9	67.2	56.5	68.3	64.8	64.3	61.8	73.7
Portfolio, Net	-31.5	-33.1	-37.5	-39.0	-39.8	-43.2	-46.2	-45.5	-43.3	-48.5	-55.0	-60.9
Net Transfers	-32.1	-37.5	-39.2	-48.7	-34.5	-32.4	-35.8	-35.9	-41.9	-35.1	-36.2	-49.1

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

OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	----- Projected -----											
	1997				1998				1999			
	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	-1.0	-0.4	-1.3	0.3	-2.2	-1.5	-1.0	-0.7	-0.6	-0.6	-0.4	-0.2
Exports of G&S	1.1	2.0	0.5	1.0	-0.1	-0.4	0.0	0.2	0.3	0.4	0.5	0.5
Imports of G&S	-2.1	-2.5	-1.8	-0.7	-2.1	-1.2	-1.0	-0.9	-0.8	-1.0	-0.9	-0.7
	Percentage change from previous period, SAAR											
Exports of G&S	9.9	18.4	4.4	8.3	-1.2	-3.2	0.3	1.7	2.4	3.6	4.4	4.9
Services	3.7	3.2	7.2	-5.1	-0.4	2.0	-1.4	1.0	2.1	3.3	3.4	3.3
Agricultural Goods	-27.6	-4.2	20.6	31.9	-9.2	-20.6	1.7	1.6	1.6	1.7	1.7	1.7
Computers	72.3	84.3	61.5	-6.5	12.1	14.7	23.9	28.7	31.1	31.1	28.7	28.7
Semiconductors	39.0	15.7	38.8	-2.6	-1.7	-5.4	17.0	28.6	29.6	30.0	30.5	30.5
Other Goods 1/	12.4	25.0	-4.6	15.7	-1.8	-5.0	-1.6	-1.4	-1.1	0.4	1.7	2.7
Imports of G&S	17.9	20.5	14.6	5.3	16.9	9.3	8.1	7.3	6.4	7.8	6.6	5.3
Services	24.2	8.9	10.1	0.3	9.2	2.7	3.8	2.1	1.9	1.9	2.4	2.9
Oil	-10.8	44.5	6.3	-9.5	9.1	27.3	-12.6	-11.6	-9.6	35.9	8.4	-17.8
Computers	51.3	71.1	53.0	10.0	62.7	23.9	28.6	28.6	27.4	25.1	25.1	25.1
Semiconductors	71.2	19.3	44.3	5.0	6.0	-9.6	19.2	28.6	31.0	31.0	31.0	31.0
Other Goods 2/	15.3	17.1	11.8	7.6	16.4	9.4	8.5	7.2	5.9	5.1	4.9	5.0
	Billions of chained 1992 dollars, SAAR											
Net Goods & Services	-126.3	-136.6	-164.1	-159.1	-207.9	-242.9	-266.2	-284.1	-298.2	-313.7	-324.0	-329.1
Exports of G&S	922.7	962.5	973.0	992.7	989.6	981.6	982.4	986.6	992.4	1001.3	1012.1	1024.4
Imports of G&S	1048.9	1099.1	1137.1	1151.8	1197.5	1224.5	1248.6	1270.7	1290.6	1315.0	1336.1	1353.5
	Billions of dollars, SAAR											
US CURRENT ACCOUNT BALANCE	-147.9	-140.5	-152.4	-180.1	-188.8	-218.1	-239.1	-266.0	-270.8	-286.4	-301.6	-316.5
Net Goods & Services (BOP)	-112.5	-106.1	-108.4	-113.8	-139.4	-159.8	-172.1	-188.4	-201.5	-215.0	-223.8	-226.7
Exports of G&S (BOP)	904.7	936.1	951.7	957.8	945.6	928.9	924.2	927.1	932.3	940.1	949.8	960.9
Imports of G&S (BOP)	1017.3	1042.1	1060.1	1071.7	1085.1	1088.7	1096.2	1115.5	1133.8	1155.1	1173.6	1187.6
Net Investment Income	0.1	1.7	-6.2	-16.9	-12.4	-19.2	-28.0	-27.6	-30.3	-32.4	-38.8	-39.8
Direct, Net	64.3	69.5	65.5	55.7	61.8	55.9	49.8	53.3	53.7	55.2	53.2	56.8
Portfolio, Net	-64.2	-67.8	-71.7	-72.6	-74.2	-75.1	-77.8	-80.9	-84.0	-87.6	-92.0	-96.6
Net Transfers	-35.5	-36.1	-37.8	-49.3	-36.9	-39.0	-39.0	-50.0	-39.0	-39.0	-39.0	-50.0

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