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CONFIDENTIAL (FR)

November 10, 1976

SUMMARY AND OUTLOOK

By the Staff  
Board of Governors  
of the Federal Reserve System

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## **SUMMARY AND OUTLOOK**

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DOMESTIC NONFINANCIAL DEVELOPMENTS

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Summary. Economic growth has slowed further over the past month or two from the reduced pace of the previous half year. Industrial production apparently declined in October, there was little evidence of strength in the demand for labor, and the unemployment rate remained on the high plateau of the prior three months. It now appears that imbalances between inventories and sales have spread. On the positive side, retail sales moved up in October, and indicators of business capital spending point to further expansion of these outlays next year. It is not clear to what extent the prolonged pause may be adversely affecting business investment intentions.

Industrial production appears to have declined somewhat in October, the first drop in 19 months. With the late settlement of the auto strike, assemblies at Ford remained depressed, and there was little evidence of significant strength in other sectors. Business equipment production was about unchanged, and output of farm equipment declined as a result of a strike. Over all, production of materials remained unchanged, although raw steel output was reduced somewhat.

Labor demand remained sluggish in October. After adjustment for strikes, payroll employment rose modestly (by 40,000), with job increases in State and local government, trade, and services. However, manufacturing employment declined by 45,000 (strike adjusted). The factory workweek edged up by 0.1 hour, remaining almost half an hour below the July level. Total hours of work in factories declined by

nearly 1 per cent, reflecting both increased strike activity and small but widespread job reductions.

The total unemployment rate edged up to 7.9 per cent in October. Both total employment and the civilian labor force have changed little on balance over the past several months, after having risen sharply earlier in the year.

Total retail sales are estimated from weekly data to have increased by nearly 1 per cent in October, as compared to the 0.1 per cent September rise. Excluding autos and nonconsumption items, sales increased by about half a per cent, off from the 0.8 per cent September rise. There was significant growth in apparel sales, and in furniture and appliances sales.

Unit sales of domestic autos in October dropped to a 7.6 million annual rate, about half million below the September pace. Shortages resulting from the Ford strike were a problem and there were production scheduling difficulties reported at GM. Even allowing for strike effects, sales of all domestic models probably have been somewhat below the average rate of the past half year. Sales of foreign models, however, have picked up recently and are now at their highest rate in the past few years.

Although businessmen have apparently been attempting to keep inventories under tight control, the book value of manufacturing stocks increased at a \$16 billion rate in September, somewhat more than

the recent average rate of gain. The inventory-sales ratio rose-- more for durables than for nondurables.

New information bearing on future capital spending still gives reason for optimism. New orders for nondefense capital equipment rose by 3 per cent in September. These orders have increased in eight of the last nine months for which data are available and in real terms are almost 15 per cent above the level at the end of last year. Recent survey results also suggest a continued expansion of plant and equipment spending in 1977. The McGraw-Hill survey, conducted in early October, indicates planned outlays about 13 per cent above those of 1976, about in line with the results of the earlier Merrill-Lynch survey. In real terms, the McGraw-Hill survey suggests an increase of about 6 per cent from 1976.

The outlook for residential construction activity continues to strengthen. Private housing starts increased sharply further in September to a 1.8 million annual rate, and sales of both new and existing homes rose strongly. For the third quarter as a whole, starts averaged 10 per cent above the second quarter. The spurt in starts in September--heavily in multifamily units--largely reflects efforts by HUD to advance the timing of Federally-subsidized and insured housing, and starts may well have declined again in October. But mortgage and other real estate developments suggest continued improvement of housing production through the end of the year and on into 1977.

Consumer prices in September rose 0.4 per cent, slightly less rapidly than in the previous four months. The improvement was due largely to stability in food prices (reflecting declines in meats) as well as moderation of price increases for some other nondurable goods as well as durables. Energy prices continued to rise sharply, although at a somewhat less rapid pace than in August.

Wholesale prices rose 0.6 per cent in October, off from 0.9 per cent rate in September. Prices of farm products declined, but industrial prices rose 1.0 per cent in October, the most rapid rise in a year. The largest increases were in fuels and power, motor vehicles, and lumber. Excluding the energy group, industrial prices were up 0.7 per cent --about a quarter of this rise was due to increased prices of the 1977 model cars. However, there is no clear cut evidence of an intensification of underlying pressures of costs on prices. Although the hourly earnings index rose more rapidly in October than September, the increase so far this year still averages about 6-3/4 per cent annual rate. Moreover, sensitive industrial commodity prices have edged off over the past several weeks.

Outlook. The monetary policy assumption underlying our current projection is consistent with the FOMC's new long-range targets for the monetary aggregates. We assume a long-run growth rate of 5-1/2 per cent for  $M_1$ , beginning in the third quarter. Given the weaker outlook for economic activity, upward pressures on short-term interest rates are expected to be quite moderate--with the Treasury bill rate rising by only 1 to 1-1/2 percentage points by year-end 1977. No new

fiscal policy initiatives have been incorporated in this projection. We continue to project Federal budget outlays in FY 1977 at a level of \$408 billion, which is \$8 billion higher than the Administration's Mid-Year Budget Review but \$5 billion less than the Congressional target. Recent spending shortfalls are not expected to result in a compensatory bulge during the current fiscal year.

With widespread inventory adjustments still underway, the staff has reduced substantially its estimate of real GNP growth for the fourth quarter of this year. We are now estimating a rise of 3.3 per cent at an annual rate, compared with the 5 per cent rate estimated last month. Real final sales during the current quarter are expected to advance by about 4-1/2 per cent at an annual rate, close to the pace that has prevailed since the recovery began.

We believe the prolonged pause has reduced somewhat the strength of underlying expansive forces. Growth of real GNP is now projected at an annual rate of about 4-1/2 per cent for the four quarters of 1977, 0.3 per cent less than in the last Greenbook. Although we are less optimistic than formerly about the outlook for business fixed investment in 1977, we still expect the rise to be somewhat greater than the rate of increase indicated by recent surveys, and to strengthen as the year progresses. This strengthening should be reflected in some pick-up in the over-all tempo of economic activity during the latter half of next year.

The slower rate of real GNP growth projected for 1977 also reflects some dampening of consumer spending propensities. The personal saving rate is projected to remain at about the 6-1/2 per cent rate of the past quarter--rather than gradually declining as had been expected earlier. We also expect a continued attitude of caution on the part of business with regard to inventory investment. Residential construction, on the other hand, is now projected to be stronger for most of 1977 than in last month's Greenbook. Based largely on more ample expected supplies of mortgage funds from the thrift institutions, housing starts are now seen as edging up throughout 1977, reaching a level of 1.8 million units late next year.

With the projected average rate of real economic expansion over the next five quarters down to slightly under 4-1/2 per cent, only modest improvement in the rate of unemployment can be expected. The rate is now projected to drop to about 7-1/4 per cent by the fourth quarter of 1977.

We are currently projecting a marginally slower rate of price increase toward the end of 1977 than we did a month ago, reflecting the weaker markets now expected. On the average, prices of all goods and services are expected to advance at an annual rate

of 5-1/4 per cent during this and the next four quarters. This estimate includes an allowance for a 15 per cent increase in OPEC oil prices. Labor compensation is projected to increase at an annual rate of around 7-1/2 per cent and productivity to advance at a 2 to 2-1/2 per cent rate; competitive forces are expected to limit average price increases to about the rate of increase in labor costs.

Details on the staff projection are shown in the tables that follow.

## STAFF GNP PROJECTIONS

	Per cent change, annual rate							
	Changes in nominal GNP (\$ billions)		Real GNP		Gross business product fixed-weighted price index		Unemployment rate (per cent)	
	10/13/76	11/10/76	10/13/76	11/10/76	10/13/76	11/10/76	10/13/76	11/10/76
1973 <u>1/</u>	135.5	135.5	5.5	5.5	5.7	5.7	4.9	4.9
1974 <u>1/</u>	106.6	106.6	-1.7	-1.7	10.2	10.2	5.6	5.6
1975 <u>1/</u>	103.1	103.1	-1.8	-1.8	9.3	9.3	8.5	8.5
1976	178.2	176.4	6.2	6.2	4.8	4.6	7.6	7.6
1977	178.6	171.3	4.7	4.2	5.3	5.3	7.0	7.3
1976-I <u>1/</u>	48.0	48.0	9.2	9.2	3.7	3.7	7.6	7.6
1976-II <u>1/</u>	39.0	39.0	4.5	4.5	5.2	5.2	7.4	7.4
1976-III <u>1/</u>	34.4	34.5	3.3	4.0	5.0	4.4	7.8	7.8
1976-IV	47.4	39.9	5.1	3.3	5.4	5.2	7.5	7.7
1977-I	46.6	45.7	5.0	4.4	5.1	5.3	7.2	7.5
1977-II	42.3	41.7	4.8	4.4	5.1	5.2	7.0	7.4
1977-III	49.7	48.8	4.9	4.7	5.5	5.3	6.9	7.3
1977-IV	51.9	52.1	4.9	4.9	5.5	5.3	6.8	7.2
Change:								
75-II to								
76-II <u>1/</u>	192.9	192.9	7.0	7.0	5.6	5.6	-1.3	-1.3
75-IV to								
76-IV <u>1/</u>	168.8	161.4	5.5	5.2	4.8	4.7	-1.0	-1.8
76-II to								
77-II	170.7	161.8	4.5	4.0	5.2	5.1	-.4	.0
76-IV to								
77-IV	190.5	188.3	4.9	4.6	5.3	5.3	-.7	-.5

1/ Actual

November 10, 1976

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

	1976				1977			
	I	II	III	IV	Projected			
	I	II	III	IV	I	II	III	IV
Gross National Product	1636.2	1675.2	1709.7	1749.6	1795.3	1837.0	1885.8	1937.9
Final purchases	1621.4	1659.2	1695.4	1739.7	1784.4	1823.6	1871.9	1922.5
Private	1266.7	1297.2	1325.9	1361.5	1397.5	1428.6	1468.1	1507.9
Excluding net exports	1258.3	1287.9	1320.0	1354.1	1387.8	1422.6	1457.4	1493.7
Personal consumption expenditures	1043.6	1064.7	1088.9	1113.9	1139.2	1165.0	1190.6	1216.9
Goods	580.5	589.8	600.8	613.8	627.1	640.7	653.8	667.3
Services	463.2	474.9	488.1	500.1	512.1	524.3	536.8	549.6
Gross private domestic investment	229.6	239.2	245.5	250.1	259.5	271.0	280.7	292.2
Residential construction	61.3	65.3	68.7	72.9	76.1	79.6	82.6	85.6
Business fixed investment	153.4	157.9	162.5	167.3	172.5	178.0	184.2	191.2
Change in business inventories	14.8	16.0	14.4	9.9	10.9	13.4	13.9	15.4
Nonfarm	12.7	17.3	15.4	10.9	11.4	13.4	13.9	15.4
Net exports of goods and services <sup>1/</sup>	8.4	9.3	5.9	7.4	9.7	6.0	10.7	14.2
Exports	154.1	160.3	166.2	168.1	172.9	178.6	184.7	190.3
Imports	145.7	151.0	160.3	160.7	163.2	172.6	174.0	176.1
Gov't. purchases of goods and services	354.7	362.0	369.5	378.2	386.9	395.0	403.8	414.6
Federal <sup>2/</sup>	129.2	131.2	134.4	137.9	140.0	142.4	145.4	150.1
State and local	225.5	230.9	235.1	240.3	246.9	252.6	258.4	264.5
Gross national product in constant (1972) dollars	1246.3	1260.0	1272.2	1282.7	1296.5	1310.5	1325.6	1341.6
Personal income	1331.3	1362.0	1386.2	1415.7	1449.8	1480.9	1515.4	1549.7
Wage and salary disbursements	861.5	881.1	897.7	917.2	938.3	958.1	979.1	1003.3
Disposable income	1147.6	1172.5	1190.4	1217.8	1246.5	1272.4	1301.1	1329.8
Saving rate (per cent)	6.9	7.1	6.4	6.4	6.5	6.4	6.4	6.5
Corporate profits with I.V.A. and C.C. Adj.	115.1	116.4	124.9	130.6	136.5	141.1	152.2	163.6
Corporate profits before tax	141.1	146.2	153.3	155.6	160.5	164.6	174.2	184.0
Federal government surplus or deficit (-) (N.I.A. basis)	-63.8	-54.1	-54.9	-60.7	-58.5	-57.9	-59.2	-57.0
High employment surplus or deficit (-)	-9.2	2.7	.4	-.8	1.0	4.7	3.0	4.8
State and local government surplus or deficit (-) (N.I.A. basis)	12.2	9.2	12.2	13.9	12.6	13.4	15.3	15.2
Excluding social insurance funds	-.6	-3.8	-1.0	.4	-1.2	-.7	.9	.5
Civilian labor force (millions)	93.6	94.5	95.3	95.5	95.8	96.4	96.8	97.2
Unemployment rate (per cent)	7.6	7.4	7.8	7.7	7.5	7.4	7.3	7.2
Nonfarm payroll employment (millions)	78.4	78.9	79.4	79.6	80.0	80.5	80.9	81.5
Manufacturing	18.8	19.0	19.0	19.1	19.3	19.5	19.6	19.7
Industrial production (1967=100)	127.0	129.4	131.1	132.0	133.7	135.9	137.8	140.0
Capacity utilization: all manufacturing (per cent)	72.1	73.0	73.6	73.7	74.2	74.9	75.4	76.2
Materials (per cent)	78.9	80.4	81.3	81.5	82.0	83.0	83.5	84.3
Housing starts, private (millions, A.R.)	1.40	1.43	1.58	1.58	1.63	1.70	1.75	1.80
Sales new autos, (millions, A.R.)	9.99	10.34	10.23	10.35	11.00	11.20	11.25	11.35
Domestic models	8.68	8.90	8.61	8.60	9.20	9.40	9.45	9.50
Foreign models	1.31	1.45	1.62	1.75	1.80	1.80	1.80	1.85

1/ Balance of payments data and projection underlying these estimates are shown in the International Developments section of this part of the Greenbook.

2/ Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

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CHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1976				1977			
	I	II	III	IV	Projected			
	I	II	III	IV	I	II	III	IV
-----Billions of Dollars-----								
Gross National Product	48.0	39.0	34.5	39.9	45.7	41.7	48.8	52.1
Inventory change	19.1	1.2	-1.6	-4.5	1.0	2.5	.5	1.5
Final purchases	28.9	37.8	36.2	44.3	44.7	39.2	48.3	50.6
Private	28.0	30.5	28.7	35.6	36.0	31.1	39.5	39.8
Net exports	-12.6	.9	-3.4	1.5	2.3	-3.7	4.7	3.5
Excluding net exports	40.6	29.6	32.1	34.1	33.7	34.8	34.8	36.3
Personal consumption expenditures	31.6	21.1	24.2	25.0	25.3	25.8	24.6	26.3
Goods	17.1	9.3	11.0	13.0	13.3	13.6	13.1	13.5
Services	14.6	11.7	13.2	12.0	12.0	12.2	12.5	12.8
Residential fixed investment	4.3	4.0	3.4	4.2	3.2	3.5	3.0	3.0
Business fixed investment	4.7	4.5	4.6	4.8	5.2	5.5	6.2	7.0
Government	.9	7.3	7.5	8.7	8.7	8.1	8.8	10.8
Federal	-1.2	2.0	3.2	3.5	2.1	2.4	3.0	4.7
State and local	2.1	5.4	4.2	5.2	6.6	5.7	5.8	6.1
GNP in constant (1972) dollars	27.1	13.7	12.2	10.5	13.8	14.0	15.1	16.0
Final purchases	11.2	12.9	13.6	13.6	13.4	11.4	15.5	15.0
Private	14.5	11.2	11.6	12.7	11.9	10.0	13.7	13.7
-----In Per Cent Per Year 1/-----								
Gross National Product	12.6	9.9	8.5	9.7	10.9	9.6	11.1	11.5
Final purchases	7.5	9.7	9.0	10.9	10.7	9.1	11.0	11.3
Private	9.4	10.0	9.1	11.2	11.0	9.2	11.5	11.3
Personal consumption expenditures	13.1	8.3	9.4	9.5	9.4	9.4	9.1	9.1
Goods	12.7	6.6	7.7	8.9	9.0	9.0	8.4	8.5
Services	13.7	10.5	11.6	10.2	9.9	9.9	9.9	9.9
Gross private domestic investment	68.9	17.9	10.9	7.7	15.9	18.9	15.1	17.4
Residential structures	34.0	28.3	22.4	27.1	18.7	19.7	15.9	15.3
Business fixed investment	13.3	12.3	12.0	12.5	13.0	13.4	14.7	16.1
Gov't. purchases of goods & services	1.0	8.6	8.5	9.8	9.5	8.6	9.2	11.1
Federal	-3.7	6.3	10.1	10.9	6.2	7.9	8.7	13.6
State and local	3.8	7.9	7.6	9.1	11.4	9.6	9.5	9.6
GNP in constant (1972) dollars	9.2	4.5	4.0	3.3	4.4	4.4	4.7	4.9
Final purchases	3.7	4.2	4.4	4.4	4.3	3.6	4.8	4.6
Private	6.2	4.7	4.8	5.2	4.8	4.0	5.4	5.4
GNP implicit deflator 2/	3.2	5.2	4.4	6.1	6.2	5.0	6.1	6.3
Gross business product fixed-weighted price index 3/	3.7	5.2	4.4	5.2	5.3	5.0	5.3	5.3
Personal income	10.1	9.5	7.3	8.8	10.0	8.9	9.6	9.4
Wage and salary disbursements	12.6	9.4	7.8	9.0	9.5	8.7	9.1	10.3
Disposable income	10.3	9.0	6.2	9.5	10.0	8.9	9.6	9.4
Corporate profits before tax	33.4	15.3	20.9	6.3	13.0	10.7	25.4	24.7
Nonfarm payroll employment	4.2	2.6	2.6	1.0	2.0	2.5	2.0	3.0
Manufacturing	6.6	4.3	.0	2.1	4.3	4.2	2.1	2.1
Industrial production	12.6	7.8	5.4	2.8	5.3	6.7	5.8	6.6
Housing starts, private	9.1	8.9	49.0	.0	13.3	18.3	12.3	11.9
Sales new autos	38.4	14.8	-4.2	4.8	27.6	7.5	1.8	3.6
Domestic models	48.0	10.5	-12.4	-5	31.0	9.0	2.1	2.1
Foreign models	-5.9	50.1	55.8	36.2	11.9	.0	.0	11.6

1/ Percentage rates are annual rates compounded quarterly.

2/ Excluding Federal pay increases rates of change are: 1976-I, 3.0 per cent; 1976-IV, 5.6 per cent; 1977-I, 6.1 per cent; 1977-IV, 5.7 per cent.

3/ Using expenditures in 1972 as weights.

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CLASS II FOMC

GROSS NATIONAL PRODUCT AND RELATED ITEMS  
(Expenditures and income figures are billions of dollars)

	1970	1971	1972	1973	1974	1975	Projected	
							1976	1977
Gross National Product	982.4	1063.4	1171.1	1306.6	1413.2	1516.3	1692.7	1864.0
Final purchases	978.6	1057.1	1161.7	1288.6	1402.5	1531.0	1678.9	1850.6
Private	759.7	823.4	908.6	1019.1	1099.2	1192.0	1312.8	1450.5
Excluding net exports	755.8	821.8	911.9	1012.0	1091.7	1171.5	1305.1	1440.4
Personal consumption expenditures	618.8	668.2	733.0	809.9	887.5	973.2	1077.8	1177.9
Goods	349.6	374.8	410.5	457.5	497.8	540.8	596.2	647.2
Services	269.1	293.4	322.4	352.3	389.6	432.4	481.6	530.7
Gross private domestic investment	140.8	160.0	188.3	220.0	215.0	183.7	241.1	275.8
Residential construction	36.6	49.6	62.0	66.1	55.1	51.2	67.0	81.0
Business fixed investment	100.5	104.1	116.8	136.0	149.2	147.1	160.3	181.5
Change in business inventories	3.8	6.4	9.4	17.9	10.7	-14.6	13.8	13.4
Nonfarm	3.7	5.1	8.8	14.7	12.2	-17.6	14.1	13.5
Net exports of goods and services	3.9	1.6	-3.3	7.1	7.5	20.5	7.7	10.2
Exports	62.5	65.6	72.7	101.6	144.4	148.1	162.2	181.6
Imports	58.5	64.0	75.9	94.4	136.9	127.6	154.4	171.5
Gov't. purchases of goods and services	218.9	233.7	253.1	269.5	303.3	339.0	366.1	400.1
Federal	95.6	96.2	102.1	102.2	111.6	124.4	133.2	144.5
State and local	123.2	137.5	151.0	167.3	191.6	214.5	232.9	255.6
Gross national product in constant (1972) dollars	1075.3	1107.5	1171.1	1235.0	1214.0	1191.7	1265.3	1318.6
Personal income	801.3	859.1	942.5	1052.4	1153.3	1249.7	1373.8	1499.0
Wage and salary disbursements	546.5	579.4	633.8	701.3	765.0	806.7	889.4	969.7
Disposable income	685.9	742.8	801.3	901.7	982.9	1080.9	1182.1	1287.5
Saving rate (per cent)	7.4	7.7	6.2	7.8	7.3	7.8	6.7	6.4
Corporate profits with I.V.A. and C.C. Adj.	67.9	77.2	92.1	99.1	84.8	91.6	121.8	148.3
Corporate profits before tax	71.5	82.0	96.2	115.8	127.6	114.5	149.1	170.8
Federal government surplus or deficit (-) (N.I.A. basis)	-12.1	-22.0	-17.3	-6.7	-11.5	-71.2	-58.4	-58.2
High employment surplus or deficit (-)	6.5	-1.7	-1.0	6.6	26.3	-9.8	-1.7	3.4
State and local government surplus or deficit (-) (N.I.A. basis)	2.8	3.7	13.7	13.0	7.3	6.9	11.9	14.1
Excluding social insurance funds	-4.0	-3.8	5.6	4.1	-2.8	-5.1	-1.3	-1
Civilian labor force (millions)	82.7	84.1	86.5	88.7	91.0	92.6	94.7	96.5
Unemployment rate (per cent)	4.9	5.9	5.6	4.9	5.6	8.5	7.6	7.3
Nonfarm payroll employment (millions)	70.9	71.2	73.7	76.9	78.4	77.0	79.1	80.7
Manufacturing	19.3	18.6	19.1	20.1	20.0	18.3	19.0	19.5
Industrial production (1967=100)	107.8	109.6	119.7	129.8	129.3	117.8	129.9	136.9
Capacity utilization: all manufacturing (per cent)	78.3	75.0	78.6	83.0	78.9	68.7	73.1	75.2
Materials (per cent)	84.3	83.1	88.0	92.5	87.7	73.5	80.5	83.2
Housing starts, private (millions, A.R.)	1.43	2.05	2.36	2.05	1.34	1.16	1.50	1.72
Sales new autos (millions, A.R.)	8.40	10.24	10.93	11.44	8.87	8.66	10.23	11.20
Domestic models	7.12	8.68	9.32	9.67	7.45	7.08	8.70	9.39
Foreign models	1.28	1.56	1.61	1.77	1.42	1.58	1.53	1.81

November 10, 1976

CONFIDENTIAL - FR  
CLASS II FCMCCHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1970	1971	1972	1973	1974	1975	Projected	
							1976	1977
-----Billions of Dollars-----								
Gross National Product	46.9	81.0	107.7	135.5	106.6	103.1	176.4	171.3
Inventory change	-5.6	2.6	3.0	8.5	-7.2	-25.3	28.4	-.4
Final purchases	52.4	78.5	104.6	126.9	113.9	128.5	147.9	171.7
Private	41.4	63.7	85.2	110.5	80.1	92.8	120.8	137.7
Net exports	2.1	-2.3	-4.9	10.4	.4	13.0	-12.8	2.5
Excluding net exports	39.3	66.0	90.1	100.1	79.7	79.8	133.6	135.3
Personal consumption expenditures	39.1	49.4	64.8	76.9	77.6	85.7	104.6	100.1
Goods	17.1	25.2	35.7	47.0	40.3	43.0	55.4	51.0
Services	21.9	24.3	29.0	29.9	37.3	42.8	49.2	49.1
Residential fixed investment	-1.3	13.0	12.4	4.1	-11.0	-3.9	15.8	14.0
Business fixed investment	1.6	3.6	12.7	19.2	13.2	-2.1	13.2	21.2
Government	11.0	14.8	19.4	16.4	33.8	35.7	27.1	34.0
Federal	-1.9	.6	5.9	.1	9.4	12.8	8.8	11.3
State and local	12.8	14.3	13.5	16.3	24.3	22.9	18.4	22.7
GNP in constant (1972) dollars	-3.5	32.2	63.6	63.9	-21.0	-22.3	73.6	53.3
Final purchases	2.8	29.9	60.8	56.8	-13.0	-1.8	52.1	53.7
Private	9.3	30.7	57.1	57.4	-16.9	-6.4	48.7	47.8
-----In Per Cent Per Year-----								
Gross National Product	5.0	8.2	10.1	11.6	8.2	7.3	11.6	10.1
Final purchases	5.7	8.0	9.9	10.9	8.8	9.2	9.7	10.2
Private	5.8	8.4	10.3	12.2	7.9	8.4	10.1	10.5
Personal consumption expenditures	6.7	8.0	9.7	10.5	9.6	9.7	10.7	9.3
Goods	5.1	7.2	9.5	11.4	8.8	8.6	10.2	8.6
Services	8.9	9.0	9.9	9.3	10.6	11.0	11.4	10.2
Gross private domestic investment	-3.7	13.6	17.7	16.8	-2.3	-14.6	31.2	14.4
Residential structures	-3.4	35.5	25.1	6.6	-16.7	-7.1	30.9	20.8
Business fixed investment	1.6	3.6	12.3	16.4	9.7	-1.4	9.0	13.2
Gov't. purchases of goods & services	5.3	6.8	8.3	6.5	12.5	11.8	8.0	9.3
Federal	-1.9	.6	6.1	.1	9.2	11.5	7.1	8.5
State and local	11.6	11.6	9.8	10.8	14.5	11.9	8.6	9.7
GNP in constant (1972) dollars	-.3	3.0	5.7	5.5	-1.7	-1.8	6.2	4.2
Final purchases	.3	2.8	5.5	4.9	-1.1	-.1	4.3	4.3
Private	1.1	3.7	6.7	6.3	-1.7	-.7	5.2	4.8
GNP implicit deflator	5.4	5.1	4.1	5.8	10.0	9.3	5.2	5.7
Gross business product fixed weighted price index <sup>1/</sup>	4.4	4.4	3.3	5.7	10.2	9.3	4.6	5.3
Personal income	7.4	7.2	9.7	11.7	9.6	8.4	9.9	9.1
Wage and salary disbursements	6.2	6.0	9.4	10.7	9.1	5.5	10.3	9.0
Disposable income	8.8	8.3	7.9	12.5	9.0	13.0	9.4	8.9
Corporate profits before tax	-14.3	14.7	17.3	20.4	10.2	-10.3	30.2	14.6
Nonfarm payroll employment	.7	.4	3.5	4.3	2.0	-1.8	2.7	2.0
Manufacturing	-4.5	-3.6	2.7	5.2	-.5	-8.5	3.8	2.6
Industrial production	-3.0	1.7	9.2	8.4	-.4	-8.9	10.3	5.4
Housing starts, private	-2.7	43.4	15.1	-13.1	-34.6	-13.4	29.3	14.7
Sales new autos	-12.2	21.9	6.7	4.7	-22.5	-2.4	18.1	9.5
Domestic models	-15.8	21.9	7.4	3.8	-23.0	-5.0	22.9	7.9
Foreign models	15.3	21.9	3.2	9.9	-19.8	11.3	-3.2	18.3

<sup>1/</sup> Using expenditures in 1972 as weights.

FEDERAL SECTOR ACCOUNTS  
(billions of dollars)

	Fiscal Year 1976*	Fiscal Year 1977 e/			CY 1976 F.R. Board	F.R.B. estimates Calendar quarters; unadjusted data					
		Admin. est. 1/	Cong. est. 2/	F.R. Board		1976			1977		
						II*	III* 3/4/	IV	I	II	III
Unified budget receipts	300.0	352.5	362.5	354.8	317.1	93.6	81.8	74.8	78.8	107.8	93.4
Unified budget outlays	365.6	400.0	413.1	408.0	373.2	91.5	94.5	97.7	101.6	103.5	105.2
Surplus (+)/Deficit (-), unified budget	-65.6	-47.5	-50.6	-53.2	-56.1	2.2	-12.7	-22.9	-22.7	4.3	-11.8
Surplus (+), Deficit (-), off-budget agencies 5/	-8.0	-11.4	n.a.	-10.8	-7.8	-.7	-2.0	-1.3	-3.7	-.9	-4.9
Means of financing combined deficits:											
Net borrowing from public	82.8	56.9	n.a.	56.9	67.7	9.4	18.0	16.2	22.2	1.0	17.5
Decrease in cash operating balance	-7.2	n.a.	n.a.	6.6	-1.5	-6.8	-2.6	7.4	1.1	-3.4	1.5
Other 6/	-1.9	n.a.	n.a.	.5	-2.1	-4.0	-.7	.6	3.0	-1.0	-2.1
Cash operating balance, end of period	14.8	n.a.	n.a.	10.8	10.0	14.8	17.4	10.0	8.9	12.3	10.8
Memo: Sponsored agency borrowing 7/	3.5	10.8 <sup>8/</sup>	n.a.	4.0	3.2	.5	1.8	.6	.7	1.4	1.4
<u>NIA Budget</u>						Seasonally adjusted, annual rates					
Receipts	311.4	n.a.	n.a.	355.0 <sup>9/</sup>	329.3	324.6	335.6	340.4	351.6	360.0	371.3 <sup>13/</sup>
Outlays	374.7	n.a.	n.a.	414.9	387.6	378.7	390.5	401.1	410.1	417.9	430.5
Purchases (total)	128.8	n.a.	n.a.	141.4	133.2	131.2	134.4	137.9	140.0	142.4	145.4
Defense	86.2	n.a.	n.a.	92.8	88.0	86.9	88.6	90.3	91.8	93.4	95.8
Non-defense	42.6	n.a.	n.a.	48.6	45.1	44.2	45.7	47.6	48.2	49.0	49.6
All other expenditures	245.9	n.a.	n.a.	273.5 <sup>9/</sup>	254.4	247.5	256.1	263.2	270.1	275.5	285.1
Surplus (+)/Deficit (-)	-63.3	n.a.	n.a.	-59.9 <sup>9/</sup>	-58.4	-54.1	-54.9	-60.7	-58.5	-57.9	-59.2
High Employment surplus (+)/deficit (-) (NIA basis) 10/	-5.6	n.a.	n.a.	2.0	-1.7	2.7	.4	-.8	1.0	4.7	3.0
	*actual	e--estimated	n.e.--not estimated			n.a.--not available			p--preliminary		

- 1/ Mid-Session Review of the 1977 Budget, July 16, 1976.  
2/ Conference Report on Second Concurrent Resolution on the Budget, September 10, 1976.  
3/ Fiscal year 1977 began on 10/1/76. The period July 1 to September 30 is a transition quarter between FY 76 and FY 77.  
4/ NIA data are preliminary.  
5/ Includes Federal Financing Bank, Postal Service, Export-Import Bank (prior to October, 1976), Rural Electrification and Telephone revolving fund, Housing for the Elderly or Handicapped Fund, and Pension Benefit Guaranty Corporation.  
6/ Checks issued less checks paid, accrued items and other transactions.  
7/ Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.  
8/ Derived from Special Analyses, Budget of the United States Government, Fiscal Year 1977, January 21, 1976.  
9/ Quarterly average exceeds fiscal year total by \$.8 billion for FY 1977 due to spreading of wage base effect over calendar year.  
10/ Estimated by F.R.B. staff. The high employment budget estimates now fully incorporate taxes on inventory profits beginning 1973.

## COMMENTS ON THE FEDERAL SECTOR OUTLOOK

The staff's projection of Federal spending is essentially unchanged for the last Greenbook, as mentioned above.

Although we have not incorporated new initiatives on the tax side, several previously enacted tax changes will take effect on January 1st:

	<u>Annual Revenue Gain</u> <u>(\$ billion)</u>
Social security wage base will increase from \$15,300 per taxpayer to \$16,500	2.1
Unemployment insurance tax rate will rise from 0.5 to 0.7 per cent of covered payroll	0.7

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DOMESTIC FINANCIAL DEVELOPMENTS

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Summary. In October short-term business credit expansion was the most rapid since August 1974, as a sharp increase in business loans was accompanied by only a small decline in outstanding non-financial commercial paper. There is no clear reason for so rapid an expansion in business loans. Bankers contacted attributed the strength to selected local influences, and believe that no fundamental strengthening has occurred in credit demands. The staff also is of the opinion that October business loan growth is not indicative of a basic change in the underlying strength of business loan demand. It may, however, be reflective of inventory accumulation associated with continued softness of final demands, and perhaps with a moderation of business efforts to restructure balance sheets, either of which could continue to provide a fillip to business loan demands in the near-term.

Capital markets absorbed an increased volume of corporate and State and local bonds at declining yields through mid-October. However, with market concern that monetary policy would not ease further in light of the October strength in the monetary aggregates, several aggressively priced issues did not sell well--and yields backed up about 5 to 10 basis points. Prices of the two longer-term issues offered in the current Treasury refunding are now somewhat below their issue prices in the late October auctions. In short-term markets, changing expectations about the outlook for monetary policy similarly led to some backup in yields.

Market rates of interest generally have remained below offering rates on interest bearing deposits and inflows to banks and thrift institutions have continued sizable. At commercial banks, such inflows were large enough to finance the sharp expansion of loans and still permit a further run-off of negotiable CD's, although total security holdings of banks declined somewhat for the first time since January 1975. Savings and loan associations--with loan commitments at record levels--continue to be the major mortgage lenders, while GNMA-guaranteed mortgage-backed security issues have remained large. Since the last FOMC meeting, FNMA secondary mortgage yields edged down to the lowest level since March 1974, and rates in the primary market have declined 10 basis points. However, home mortgage rates in the primary market have declined only about 25 basis points this year as the demand for such credit has remained unusually strong, in large part reflecting sales of existing homes and indications that homeowners have been liquidating some of their equity.

Outlook. Staff projections for weaker economic expansion this quarter and next suggest little growth of total credit demands. The forward calendar of corporate bond offerings for the balance of this year is relatively modest by recent standards, though it is difficult to disentangle the degree to which this reflects reduced financing needs, a moderation of efforts to restructure balance sheets, and/or changing borrower expectations with regard to the

level of future interest rates. In any event, the staff believes that corporate demands on capital markets are in the process of moderating--notably in the public bond market--and that a larger proportion of business financing needs may be directed to banks and the commercial paper market. The somewhat greater emphasis on short-term credit demands, however, is likely to be offset in part by business efforts to limit growth in inventory positions, suggesting that short-term business credit expansion will remain relatively modest.

Growth in consumer instalment credit is expected to remain near current levels given the projected expansion in consumption expenditures. However, mortgage debt is projected to expand at a rapid pace in view of historically high outstanding levels of mortgage commitments, the expected continued large inflows to thrift institutions, and rising demands to finance growth in construction and property transfer. Indeed, with market rates projected to remain generally below the levels on depositary claims, deposit inflows are expected to remain at a pace sufficient to bring some further downward pressure on mortgage rates. Moreover, over the next few months, banks and thrift institutions might be expected to reduce promotion and advertising of longer-term high-rate deposits, shave offering rates, and some institutions may cease offering the longest-term deposits.

Borrowing by the public sector is anticipated to remain fairly large. State and local governments appear, in part, still to be adjusting credit demands to distortions caused by the New York crisis last year. With the longer-term market now more receptive, local governmental units are taking the opportunity to fund short-term debt and reactivate earlier borrowing plans. Thus, there have been no signs of abatement in the recent high volume of bond offerings. Staff estimates indicate that the Treasury will borrow another \$7 billion before year-end.

On balance, over the next few months--with over-all credit demands expected to be somewhat more moderate than earlier anticipated, and with institutional investors continuing to experience sizable inflows of funds--upward interest rate pressures are likely to be limited.

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INTERNATIONAL DEVELOPMENTS

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Summary. In the four weeks since the last green book, the trade-weighted average value of the dollar against the major foreign currencies has increased by about one half of a per cent. The British pound has been increasingly buffeted by rumors about U.K. economic policies and possible international arrangements covering sterling balances; the pound dropped 5 per cent against the dollar to \$1.57 late in October before rebounding to above \$1.63 more recently. In the face of on-again-off-again exchange controls, the lira declined over the period by about 3 per cent against the dollar. On October 18, a small realignment of parities within the EC snake occurred; this realignment was followed by even smaller movements in actual market exchange rates. Over the period, the snake currencies rose by one per cent against the dollar. Finally, in the face of mounting reserve losses, the Bank of Mexico refloated the peso on October 25 and subsequently has held it at 50 per cent below its August 31 parity of U.S. \$0.08 per peso.

The economic recovery in the major foreign industrial countries continues to be slow and uneven. Each of them experienced either a slowdown or negative growth starting in the second or third quarter of this year. On a weighted-average basis, industrial production for these countries in August was 2.8 per cent below the peak recorded in the fourth quarter of 1973 and 9.4 per cent above

the trough in the second quarter of 1975. No country has taken steps to stimulate its economy since the recent pause began.

Despite the slowdown in the pace of economic activity abroad, the value of U.S. exports rose 4-1/2 per cent in the third quarter of 1976, compared with a 6 per cent rise in the second quarter. September exports were essentially flat. Third-quarter imports rose by over 9 per cent with equal percentage increases in fuel and non-fuel imports; the increase in non-fuel imports continued in September. Fuel imports remain above the level required to maintain current consumption rates; this phenomenon presumably reflects purchases in anticipation of an OPEC price hike on January 1, 1977. As a result of the rapid increase in imports, the third-quarter trade deficit doubled to \$11.5 billion (seasonally adjusted annual rate).

In the third quarter, the rate of net bank-reported private capital outflows at \$0.6 billion (quarterly rate) was about half that in the second quarter. However, new issues of foreign bonds in U.S. markets doubled to over \$3 billion after a brief lull in the second quarter. It is expected that in the fourth quarter of 1976 new foreign bond issues will be between \$2.5 billion and \$3 billion.

Outlook. The staff continues to project for the next five quarters a modest increase in the rate of economic growth in the major foreign industrial countries, with real GNP growth averaging about 4-3/4 per cent. This outlook combined with recent

increases in export orders indicates a continued moderate expansion in U.S. exports. With high rates of oil imports anticipated to continue through the end of 1976, we now expect a somewhat larger trade deficit for 1976 as a whole than was projected in last month's green book. We expect, moreover, only small changes in the trade deficit through mid-1977 when Alaskan oil should begin to bring about a reduction.

For 1977 as a whole, the staff projects a trade deficit of \$9 billion, about the same rate as we now expect for 1976 as a whole but below the third-quarter rate. From the third quarter of 1976 to the fourth quarter of 1977, rising net receipts on military and services transactions are expected to add slightly to the \$5 billion, positive swing in net exports of merchandise and result in a \$6-7 billion swing in net exports of goods and services and in the current account balance.

The staff anticipates that on a weighted-average basis the dollar will appreciate over the forecast period by, perhaps, five per cent, declining slightly against the mark and Swiss franc and rising substantially against the pound and, especially, the lira. This judgment is consistent with expected divergences in inflation rates and the structure of forward rates in exchange markets.

	1975	1976 <sup>P</sup>	1977 <sup>P</sup>	1976				1977 <sup>P</sup>			
				I	II	III <sup>P</sup>	IV <sup>P</sup>	I	II	III	IV
<u>Billions of dollars</u>											
Net Exports of Goods and Services (GNP basis of net exports) <u>1/</u>	16.3 (20.5)	3.2 (7.8)	3.7 (10.1)	4.2 (8.4)	6.3 (9.3)	.4 (5.9)	1.9 (7.4)	3.7 (9.7)	-.5 (6.0)	3.8 (10.7)	7.3 (14.2)
Merchandise Trade Balance	8.9	-8.5	-9.1	-6.7	-5.1	-11.5	-10.7	-9.2	-13.1	-8.6	-5.7
Exports	107.1	114.8	128.6	107.3	113.8	118.7	119.4	122.2	126.2	130.7	135.2
Agricultural	22.2	23.3	23.0	21.3	23.5	25.3	23.1	22.7	22.8	23.1	23.3
Nonagricultural	84.8	91.5	105.6	86.1	90.3	93.4	96.3	99.5	103.4	107.6	111.9
Imports	98.1	123.3	137.7	114.0	118.9	130.2	130.1	131.4	139.3	139.3	140.9
Fuels	28.5	37.0	41.0	31.8	36.5	39.9	39.6	38.5	43.8	41.1	40.4
Nonfuels	69.5	86.3	96.7	82.3	82.5	90.3	90.5	92.9	95.5	98.2	100.5
Military and Service Transactions, net	7.3	11.7	12.8	10.9	11.4	11.9	12.6	12.9	12.6	12.4	13.0
Military transactions, net	-.9	.2	.7	--	-.1	.3	.5	.5	.6	.8	.8
Investment income, net	6.0	9.0	9.4	9.1	8.6	9.0	9.4	9.7	9.3	9.0	9.7
Other services, net	2.1	2.5	2.6	1.8	2.9	2.6	2.8	2.7	2.7	2.6	2.5
U.S. Current Account Balance <u>2/</u>	11.7	-.9	-.7	-.2	+2.8	-3.8	-2.3	-.6	-4.8	-.6	+2.9
<u>Constant (1972) dollars</u>											
Merchandise exports (% change, annual rates)	64.6 (-2.4)	66.8 (3.4)	71.4 (6.9)	63.3 (-19.3)	66.5 (22.0)	68.6 (13.4)	68.5 (-.6)	69.6 (6.6)	70.6 (5.7)	71.9 (7.4)	73.3 (7.8)
Merchandise imports (% change, annual rates)	51.3 (-12.5)	62.2 (21.2)	63.9 (2.7)	59.0 (44.8)	60.4 (10.0)	65.2 (35.5)	64.4 (-4.9)	63.5 (-5.7)	64.7 (7.8)	63.8 (-5.7)	63.6 (-1.2)
<u>Foreign Outlook - Major Industrial Countries <u>3/</u></u>											
Real GNP, % change, annual rate	--	4.9	4.2	8.8	2.8	2.7	3.8	4.7	4.7	4.9	4.7
Wholesale Prices, % change, A.R. <u>4/</u>	6.0	9.5	9.0	11.4	16.9	11.8	8.7	8.4	8.4	6.9	6.3

1/ The GNP account excludes from service imports, U.S. Government interest payments to foreigners (\$4.5 billion in 1975), and excludes from exports, military shipments to Israel under cash grant programs (\$340 million in 1975).

2/ Includes goods and services plus private and official remittances and pensions and U.S. Government grants.

3/ Weighted by the shares of Canada, France, Germany, Italy, Japan and the United Kingdom in the sum of the real GNP in dollar terms of the six countries.

4/ Data are largely manufactured goods prices.

P/ Projected.