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CONFIDENTIAL (FR)

January 12, 1977

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. A substantial cutback in the rate of inventory investment, together with a slowdown in the growth of business capital outlays, appears to have retarded the rate of economic expansion somewhat further in the last quarter of 1976. During the course of the fourth quarter, however, the tempo of activity quickened. Retail sales rose sharply in December, following strong gains in the two earlier months. And with the overhang of excess inventories reduced, improvement in the production of consumer and related goods seems very likely. However, plans for business fixed capital outlays weakened during the prolonged period of slow growth of production, employment and income, and these outlays may continue to provide only modest support to overall economic growth until well into 1977.

Nonfarm payroll employment rose by 230,000, adjusted for strikes in December, following a strike-adjusted November rise of 126,000. Most of the December job increase was in the service producing industries, but manufacturing employment edged ahead by 30,000, strike adjusted. The unemployment rate dropped 0.2 to 7.9 per cent, as the labor force remained unchanged, while employment rose.

Based on very fragmentary data, it appears that industrial production rose moderately last month. Auto assemblies were up strongly, as producers attempted to meet demands for popular mid- and large-size models, and employment increases suggest production gains in other sectors.

Retail sales are reported to have risen by 3 per cent in December, the third consecutive large monthly increase. This strength of retail buying confirmed recent survey reports of improved consumer confidence. Sales gains in December were particularly large for autos but sizable increases occurred at some other major types of stores. Excluding autos and nonconsumption items, the December rise was almost 2 per cent, and for the fourth quarter as a whole these sales were 3-1/4 per cent above the third quarter average--the best gain in a year and a half.

Unit sales of domestic autos last month totaled 9.3 million, annual rate--the highest monthly sales pace in over three years. The strength in sales of the popular intermediate and larger models was supported by increased supplies. Sales of small models improved more moderately despite the rebate programs. Sales of imports remained at the 1-1/2 million unit annual rate of November--down from the third quarter sales pace which had been stimulated by special sales incentives.

In contrast to the improvement evident in consumer markets, business attitudes toward investment in both fixed capital and inventories remain extremely cautious. Manufacturers' stocks had backed up substantially in September and October but with production curtailed in these months, and shipments up strongly in November, the book value of these inventories rose by only \$2.9 billion, annual rate, in November. There was an actual liquidation of nondurable goods, but

the larger adjustment occurred at durable goods producers. After having risen since mid-year, the inventory-sales ratio for durable manufacturing declined in November to around its first quarter 1976 level; the ratio for nondurables edged off, but remained above the level early in the year.

New figures for capital spending confirm the weakening tendencies evident in earlier data. In November, current dollar shipments of nondefense capital goods and sales of trucks were essentially unchanged, and there was only a modest rise in non-residential construction outlays. Additionally, new orders for nondefense capital goods dropped sharply, as did contracts for construction of commercial and industrial facilities measured in floor space.

The Commerce November survey of anticipated plant and equipment spending indicated a strong fourth quarter of 1976, but a weak first half of 1977; the apparent shortfall in outlays last quarter may reflect some postponement of spending into early 1977. The latest Commerce survey--taken in December--reports an 11.3 per cent increase for 1977 as a whole, and appears consistent with stronger gains in capital spending as the year progresses.

Residential construction remains a relatively bright spot. Although private housing starts edged down somewhat further in November from the very high September rate, for the fourth quarter as a whole they should average about 1.7 million, annual rate--7 per cent above

the third quarter and the highest figure in about three years. Single-family starts appear likely to average about 1-1/4 million units, at annual rates, in the fourth quarter, only 7 per cent below the cyclical peak in 1973. Sales of new and existing homes in November remained strong.

With food prices down and energy items rising more moderately, the overall CPI rose only 0.3 per cent in November and October, slightly under the average rise over the first three quarters. Excluding food and energy items, the November rise in consumer prices was 0.5 per cent, about equal to the average rise earlier in 1976.

The wholesale price index for industrial commodities rose 0.3 per cent in December after much larger increases over the prior three months. The improvement primarily reflected a decline in fuel and power prices. Because of a large rise for farm and food products, the overall wholesale price index rose 0.9 per cent.

Outlook. The staff has reduced its estimate of real GNP growth for the fourth quarter of 1976 to 2.8 per cent, annual rate, compared with the 3.9 per cent rate of the third quarter. The further slowdown in the fourth quarter mainly reflects a large projected decline in the rate of inventory investment, together with slower growth of business fixed investment. These developments more than offset the greater real strength evident in consumer expenditures and housing.

The staff projections for 1977 calendar year include changes in our fiscal assumptions. The specifics of the stimulative fiscal package that we incorporated in the last Greenbook have been altered somewhat to conform more closely to the spirit of the recommendations of the new Administration. We now assume a \$10 billion rebate paid in the second quarter and a \$4 billion permanent tax cut for individuals. We continue to assume a \$2 billion tax cut for corporations and a \$3 billion increase in CY 1977 Federal spending for public service jobs and State and local construction.

Our monetary policy assumptions continue to specify a growth path of 5-1/2 per cent for  $M_1$ , with the base period now shifted forward to the fourth quarter of 1976. We still expect a cyclical upturn in interest rates, particularly short-term rates, with increased pressures most evident in the second half of 1977.

For the four quarters of 1977, we now project an average rate of growth in real GNP of about 5-3/4 per cent, slightly more than last month. The stepped-up rate of expansion projected for the first quarter of 1977 mainly reflects a leveling out of inventory investment, following a sharp decline in the fourth quarter. Economic growth is projected to strengthen appreciably further in the second quarter, as the tax rebate stimulates consumption expenditures. Real GNP growth is projected to average nearly 6 per cent annual rate during the latter half of 1977, with substantial support provided by resumption of a more rapid rate of growth in capital spending and gains in inventory investment.

During the second half of the year the growth in consumption is expected to moderate somewhat, but retail sales should be relatively well sustained by strengthening gains in employment and wage and salary income as well as by the delayed effects of the rebate. Personal saving is expected to rise sharply in the second quarter, at the time of the rebate, and to fall thereafter to about a 6-1/4 per cent rate by year end. For 1977 as a whole, however, the saving rate averages a bit higher than in the past few quarters.

Expansion of GNP at the projected rate would imply a moderate decline in the unemployment rate to close to 7 per cent by the fourth quarter of 1977, even with relatively strong gains in the labor force.

Our price projections have been shaded down slightly, mainly because the decisions by the oil exporting countries now suggest a less unfavorable outlook for imported crude oil prices. Our assumption now is that these prices will rise about 5 per cent by the second quarter of 1977, and move up another 2 to 3 per cent over the remainder of the year. The fixed-weighted price index for gross business product is now projected to moderate to about a 5 per cent rate in the second half of 1977.

## 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)	
	12/15/76	1/12/77	12/15/76	1/12/77	12/15/76	1/12/77	12/15/76	1/12/77
1973 <sup>1/</sup>	135.5	135.5	5.5	5.5	5.7	5.7	4.9	4.9
1974 <sup>1/</sup>	106.6	106.6	-1.7	-1.7	10.2	10.2	5.6	5.6
1975 <sup>1/</sup>	103.1	103.1	-1.8	-1.8	9.3	9.3	8.5	8.5
1976	175.6	175.5	6.1	6.1	4.6	4.6	7.7	7.7
1977	177.9	179.2	4.7	4.9	5.3	5.2	7.6	7.5
1976-I <sup>1/</sup>	48.0	48.0	9.2	9.2	3.7	3.7	7.6	7.6
1976-II <sup>1/</sup>	39.0	39.0	4.5	4.5	5.2	5.2	7.4	7.4
1976-III <sup>1/</sup>	33.2	34.6	3.8	3.9	4.3	4.3	7.8	7.8
1976-IV	39.5	36.3	3.5	2.8	5.2	5.2	8.0	8.0
1977-I	47.2	46.6	4.8	5.0	5.5	5.5	7.9	7.9
1977-II	44.8	51.1	5.1	6.5	5.0	5.4	7.7	7.6
1977-III	52.2	52.4	5.9	6.1	5.4	5.0	7.5	7.3
1977-IV	59.9	55.1	6.4	5.7	5.5	5.0	7.2	7.1
Change:								
75-II to 76-II <sup>1/</sup>	192.9	192.9	7.0	7.0	5.6	5.6	-1.3	-1.3
75-IV to 76-IV <sup>1/</sup>	159.7	157.9	5.2	5.1	4.6	4.6	-.5	-.5
76-II to 77-II	164.7	168.6	4.3	4.6	5.0	5.1	.3	.2
76-IV to 77-IV	204.1	205.2	5.5	5.8	5.4	5.2	-.8	-.9

<sup>1/</sup> Actual.

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

	1976				1977			
	I	II	III	IV	I	II	III	IV
Gross National Product	1636.2	1675.2	1709.8	1746.1	1792.7	1843.8	1896.2	1951.3
Final purchases	1621.4	1659.2	1694.7	1739.9	1785.7	1832.8	1880.9	1932.3
Private	1266.7	1297.2	1325.1	1363.3	1401.7	1438.9	1476.2	1516.1
Excluding net exports	1258.3	1287.9	1320.4	1359.7	1397.2	1439.0	1476.2	1513.1
Personal consumption expenditures	1043.6	1064.7	1088.5	1119.0	1147.1	1180.3	1207.3	1234.3
Goods	580.5	589.8	599.4	617.4	633.1	652.8	666.8	681.8
Services	463.2	474.9	489.1	501.6	514.0	527.5	540.5	552.5
Gross private domestic investment	229.6	239.2	247.0	246.9	257.1	269.7	284.2	297.8
Residential construction	61.3	65.3	68.9	75.2	80.4	84.7	88.6	91.8
Business fixed investment	153.4	157.9	163.0	165.5	169.7	174.0	180.3	187.0
Change in business inventories	14.8	16.0	15.1	6.2	7.0	11.0	15.3	19.0
Nonfarm	12.7	17.3	15.6	7.0	7.5	11.0	15.3	19.0
Net exports of goods and services <sup>1/</sup>	8.4	9.3	4.7	3.6	4.5	-1.1	.0	3.0
Exports	154.1	160.3	167.7	166.9	172.8	178.5	183.9	188.9
Imports	145.7	151.0	163.0	163.3	168.3	178.6	183.9	185.9
Gov't. purchases of goods and services	354.7	362.0	369.6	376.6	384.0	393.9	404.7	416.2
Federal <sup>2/</sup>	129.2	131.2	134.5	138.5	140.9	143.2	146.2	150.9
State and local	225.5	230.9	235.0	238.1	243.1	250.7	258.5	265.3
Gross national product in constant (1972) dollars	1246.3	1260.0	1272.2	1281.0	1296.6	1317.4	1337.1	1355.8
Personal income	1331.3	1362.0	1386.0	1419.4	1455.3	1499.2	1529.7	1570.0
Wage and salary disbursements	861.5	881.1	897.8	921.1	943.3	967.8	993.0	1019.8
Disposable income	1147.6	1172.5	1190.2	1219.1	1248.8	1321.8	1313.9	1346.3
Saving rate (per cent)	6.9	7.1	6.4	6.0	6.0	8.6	6.0	6.2
Corporate profits with I.V.A. and C.C. Adj.	115.1	116.4	122.0	123.8	129.0	137.0	147.0	156.4
Corporate profits before tax	141.1	146.2	150.2	157.2	163.0	169.0	176.5	183.4
Federal government surplus or deficit (-) (N.I.A. basis)	-63.8	-54.1	-57.4	-59.0	-57.5	-100.9	-65.0	-62.7
High employment surplus or deficit (-) <sup>3/</sup>	-18.1	-8.6	-9.9	-10.8	-6.7	-45.8	-20.5	-20.8
State and local government surplus or deficit (-) (N.I.A. basis)	12.2	9.2	12.7	17.3	17.1	20.0	22.8	21.7
Excluding social insurance funds	-6	-3.8	-6	3.8	3.3	5.9	8.4	7.0
Civilian labor force (millions)	93.6	94.5	95.3	95.7	96.2	96.8	97.3	97.7
Unemployment rate (per cent)	7.6	7.4	7.8	8.0	7.9	7.6	7.3	7.1
Nonfarm payroll employment (millions)	78.4	79.0	79.3	79.7	80.1	80.9	81.5	82.1
Manufacturing	18.8	19.0	19.0	19.0	19.2	19.5	19.7	20.0
Industrial production (1967=100)	127.0	129.4	131.0	131.7	133.8	137.2	140.1	142.9
Capacity utilization: all manufacturing (per cent)	79.0	80.2	80.8	80.5	81.1	82.5	84.2	84.7
Materials (per cent)	79.1	80.6	81.3	80.9	81.5	82.9	84.1	85.1
Housing starts, private (millions, A.R.)	1.40	1.43	1.59	1.70	1.70	1.75	1.85	1.85
Sales new autos, (millions, A.R.)	9.99	10.34	10.23	9.93	10.35	10.90	11.20	11.35
Domestic models	8.68	8.90	8.61	8.32	8.75	9.25	9.50	9.60
Foreign models	1.31	1.45	1.62	1.61	1.60	1.65	1.70	1.75

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

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

vised series - see comments in Federal Sector Outlook of Part I.

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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	34.6	36.3	46.6	51.1	52.4	55.1
Inventory change	19.1	1.2	-.9	-8.9	.8	4.0	4.3	3.7
Final purchases	28.9	37.8	35.5	45.2	45.8	47.1	48.1	51.4
Private	28.0	30.5	27.9	38.2	38.4	37.2	37.3	39.9
Net exports	-12.6	.9	-4.6	-1.1	.9	-4.6	.1	3.0
Excluding net exports	40.6	29.6	32.5	39.3	37.5	41.8	37.2	36.9
Personal consumption expenditures	31.6	21.1	23.8	30.5	28.1	33.2	27.0	27.0
Goods	17.1	9.3	9.6	18.0	15.7	19.7	14.0	15.0
Services	14.6	11.7	14.2	12.5	12.4	13.5	13.0	12.0
Residential fixed investment	4.3	4.0	3.6	6.3	5.2	4.3	3.9	3.2
Business fixed investment	4.7	4.5	5.1	2.5	4.2	4.3	6.3	6.7
Government	.9	7.3	7.6	7.0	7.4	9.9	10.8	11.5
Federal	-1.2	2.0	3.3	4.0	2.4	2.3	3.0	4.7
State and local	2.1	5.4	4.1	3.1	5.0	7.6	7.8	6.8
GNP in constant (1972) dollars	27.1	13.7	12.2	8.8	15.6	20.8	19.7	18.7
Final purchases	11.2	12.9	13.2	14.8	15.2	17.9	17.0	16.2
Private	14.5	11.2	11.3	15.0	14.4	14.7	13.6	14.4
	-----In Per Cent Per Year <sup>1/</sup> -----							
Gross National Product	12.6	9.9	8.5	8.8	11.1	11.9	11.9	12.1
Final purchases	7.5	9.7	8.8	11.1	11.0	11.0	10.9	11.4
Private	9.4	10.0	8.9	12.0	11.8	11.0	10.8	11.3
Personal consumption expenditures	13.1	8.3	9.2	11.7	10.4	12.1	9.5	9.2
Goods	12.7	6.6	6.7	12.6	10.6	13.0	8.9	9.3
Services	13.7	10.5	12.5	10.6	10.3	10.9	10.2	9.2
Gross private domestic investment	68.9	17.9	13.8	-.2	17.6	21.1	23.3	20.6
Residential structures	34.0	28.3	24.3	41.9	30.7	23.2	19.7	15.2
Business fixed investment	13.3	12.3	13.5	6.3	10.5	10.5	15.3	15.7
Gov't. purchases of goods & services	1.0	8.6	8.6	7.8	8.1	10.7	11.4	11.9
Federal	-3.7	6.3	10.7	12.3	7.1	6.7	8.6	13.5
State and local	3.8	9.9	7.4	5.3	8.7	13.1	13.0	10.9
GNP in constant (1972) dollars	9.2	4.5	3.9	2.8	5.0	6.5	6.1	5.7
Final purchases	3.7	4.2	4.3	4.8	4.8	5.7	5.3	5.0
Private	6.2	4.7	4.7	6.2	5.8	5.9	5.3	5.5
GNP implicit deflator <sup>2/</sup>	3.2	5.2	4.4	5.8	5.8	5.0	5.4	6.1
Gross business product fixed-weighted price index <sup>3/</sup>	3.7	5.2	4.3	5.2	5.5	5.4	5.0	5.0
Personal income	10.1	9.5	7.2	10.0	10.5	12.6	8.4	10.9
Wage and salary disbursements	12.6	9.4	7.8	10.8	10.0	10.8	10.8	11.2
Disposable income	10.3	9.0	6.2	10.1	10.5	12.6	8.4	10.9
Corporate profits before tax	33.4	15.3	11.4	20.0	15.6	15.5	19.0	16.5
Nonfarm payroll employment	4.2	3.1	1.5	2.0	2.0	4.1	3.0	3.0
Manufacturing	6.6	4.3	.0	.0	4.3	6.4	4.2	6.2
Industrial production	12.6	7.8	5.0	2.2	6.6	10.5	8.8	8.1
Housing starts, private	9.1	8.9	52.8	30.7	.0	12.3	24.9	.0
Sales new autos	39.0	14.8	-4.2	-11.2	18.0	23.0	11.5	5.5
Domestic models	48.0	10.5	-12.4	-12.8	22.3	24.9	11.3	4.3
Foreign models	-5.9	50.1	55.8	-2.4	-2.5	13.1	12.7	12.3

<sup>1/</sup> Percentage rates are annual rates compounded quarterly.

<sup>2/</sup> Excluding Federal pay increases rates of change are: 1976-I, 3.0 per cent; 1976-IV, 5.3 per cent; 1977-I, 5.7 per cent; 1977-IV, 5.5 per cent.

<sup>3/</sup> Using expenditures in 1972 as weights.

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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	1691.8	1871.0
Final purchases	978.6	1057.1	1161.7	1288.6	1402.5	1531.0	1678.8	1857.9
Private	759.7	823.4	908.6	1019.1	1099.2	1192.0	1313.1	1458.2
Excluding net exports	755.8	821.8	911.9	1012.0	1091.7	1171.5	1306.6	1456.4
Personal consumption expenditures	618.8	668.2	733.0	809.9	887.5	973.2	1078.9	1192.2
Goods	349.6	374.8	410.5	457.5	497.8	540.8	596.8	658.6
Services	269.1	293.4	322.4	352.3	389.6	432.4	482.2	533.6
Gross private domestic investment	140.8	160.0	188.3	220.0	215.0	183.7	240.7	277.2
Residential construction	36.6	49.6	62.0	66.1	55.1	51.2	67.7	86.4
Business fixed investment	100.5	104.1	116.8	136.0	149.2	147.1	160.0	177.7
Change in business inventories	3.8	6.4	9.4	17.9	10.7	-14.6	13.0	13.1
Nonfarm	3.7	5.1	8.8	14.7	12.2	-17.6	13.1	13.2
Net exports of goods and services	3.9	1.6	-3.3	7.1	7.5	20.5	6.5	1.9
Exports	62.5	65.6	72.7	101.6	144.4	148.1	162.2	181.0
Imports	58.5	64.0	75.9	94.4	136.9	127.6	155.7	179.2
Gov't. purchases of goods and services	218.9	233.7	253.1	269.5	303.3	339.0	365.7	399.7
Federal	95.6	96.2	102.1	102.2	111.6	124.4	133.3	145.3
State and local	123.2	137.5	151.0	167.3	191.6	214.5	232.4	254.4
Gross national product in constant (1972) dollars	1075.3	1107.5	1171.1	1235.0	1214.0	1191.7	1264.9	1326.7
Personal income	801.3	859.1	942.5	1052.4	1153.3	1249.7	1374.7	1513.5
Wage and salary disbursements	546.5	579.4	633.8	701.3	765.0	806.7	890.4	981.0
Disposable income	685.9	742.8	801.3	901.7	982.9	1080.9	1182.4	1307.7
Saving rate (per cent)	7.4	7.7	6.2	7.8	7.3	7.8	6.6	6.7
Corporate profits with I.V.A. and C.C. Adj.	67.9	77.2	92.1	99.1	84.8	91.6	119.3	142.3
Corporate profits before tax	71.5	82.0	96.2	115.8	127.6	114.5	148.7	172.9
Federal government surplus or deficit (-) (N.I.A. basis)	-12.1	-22.0	-17.3	-6.7	-11.5	-71.2	-58.6	-71.5
High employment surplus or deficit (-)	3.0	-5.7	-5.9	-7	16.8	-17.2	-11.8	-23.5
State and local government surplus or deficit (-) (N.I.A. basis)	2.8	3.7	13.7	13.0	7.3	6.9	12.9	20.4
Excluding social insurance funds	-4.0	-3.8	5.6	4.1	-2.8	-5.1	-3	6.2
Civilian labor force (millions)	82.7	84.1	86.5	88.7	91.0	92.6	94.8	97.0
Unemployment rate (per cent)	4.9	5.9	5.6	4.9	5.6	8.5	7.7	7.5
Nonfarm payroll employment (millions)	70.9	71.2	73.7	76.9	78.4	77.0	79.1	81.2
Manufacturing	19.3	18.6	19.1	20.1	20.0	18.3	19.0	19.6
Industrial production (1967=100)	107.8	109.6	119.7	129.8	129.3	117.8	129.8	138.5
Capacity utilization: all manufacturing (per cent)	79.2	78.0	83.1	87.5	84.2	73.6	80.1	83.1
Materials (per cent)	84.3	83.1	88.0	92.4	87.7	73.6	80.5	83.4
Housing starts, private (millions, A.R.)	1.43	2.05	2.36	2.05	1.34	1.16	1.53	1.79
Sales new autos (millions, A.R.)	8.40	10.24	10.93	11.42	8.91	8.66	10.12	10.95
Domestic models	7.12	8.68	9.32	9.65	7.49	7.08	8.63	9.27
Foreign models	1.28	1.56	1.61	1.77	1.42	1.58	1.50	1.67

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CHANGES 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	175.5	179.2
Inventory change	-5.6	2.6	3.0	8.5	-7.2	-25.3	27.6	.1
Final purchases	52.4	78.5	104.6	126.9	113.9	128.5	147.8	179.1
Private	41.4	63.7	85.2	110.5	80.1	92.8	121.1	145.1
Net exports	2.1	-2.3	-4.9	10.4	.4	13.0	-14.0	-4.6
Excluding net exports	39.3	66.0	90.1	100.1	79.7	79.8	135.1	149.8
Personal consumption expenditures	39.1	49.4	64.8	76.9	77.6	85.7	105.7	113.3
Goods	17.1	25.2	35.7	47.0	40.3	43.0	56.0	61.8
Services	21.9	24.3	29.0	29.9	37.3	42.8	49.8	51.4
Residential fixed investment	-1.3	13.0	12.4	4.1	-11.0	-3.9	16.5	18.7
Business fixed investment	1.6	3.6	12.7	19.2	13.2	-2.1	12.9	17.7
Government	11.0	14.8	19.4	16.4	33.8	35.7	26.7	34.0
Federal	-1.9	.6	5.9	.1	9.4	12.8	8.9	12.0
State and local	12.8	14.3	13.5	16.3	24.3	22.9	17.9	22.0
GNP in constant (1972) dollars	-3.5	32.2	63.6	63.9	-21.0	-22.3	73.2	61.8
Final purchases	2.8	29.9	60.8	56.8	-13.0	-1.8	52.2	62.1
Private	9.3	30.7	57.1	57.4	-16.9	-6.4	49.1	55.5
-----In Per Cent Per Year-----								
Gross National Product	5.0	8.2	10.1	11.6	8.2	7.3	11.6	10.6
Final purchases	5.7	8.0	9.9	10.9	8.8	9.2	9.7	10.7
Private	5.8	8.4	10.3	12.2	7.9	8.4	10.2	11.1
Personal consumption expenditures	6.7	8.0	9.7	10.5	9.6	9.7	10.9	10.5
Goods	5.1	7.2	9.5	11.4	8.8	8.6	10.4	10.4
Services	8.9	9.0	9.9	9.3	10.6	11.0	11.5	10.7
As private domestic investment	-3.7	13.6	17.7	16.8	-2.3	-14.6	31.0	15.2
Residential structures	-3.4	35.5	25.1	6.6	-16.7	-7.1	32.2	27.7
Business fixed investment	1.6	3.6	12.3	16.4	9.7	-1.4	8.8	11.1
Gov't. purchases of goods & services	5.3	6.8	8.3	6.5	12.5	11.8	7.9	9.3
Federal	-1.9	.6	6.1	.1	9.2	11.5	7.2	9.0
State and local	11.6	11.6	9.8	10.8	14.5	11.9	8.3	9.5
GNP in constant (1972) dollars	-3	3.0	5.7	5.5	-1.7	-1.8	6.1	4.9
Final purchases	3	2.8	5.5	4.9	-1.1	-.1	4.3	4.9
Private	1.1	3.7	6.7	6.3	-1.7	-.7	5.2	5.6
GNP implicit deflator	5.4	5.1	4.1	5.8	10.0	9.3	5.2	5.4
Gross business product fixed weighted price index <sup>1/</sup>	4.4	4.4	3.3	5.7	10.2	9.3	4.6	5.2
Personal income	7.4	7.2	9.7	11.7	9.6	8.4	10.0	10.1
Wage and salary disbursements	6.2	6.0	9.4	10.7	9.1	5.5	10.4	10.2
Disposable income	8.8	8.3	7.9	12.5	9.0	10.0	9.4	10.6
Corporate profits before tax	-14.3	14.7	17.3	20.4	10.2	-10.3	29.9	16.3
Nonfarm payroll employment	.7	.4	3.5	4.3	2.0	-1.8	2.7	2.7
Manufacturing	-4.5	-3.6	2.7	5.2	-.5	-8.5	3.8	3.2
Industrial production	-3.0	1.7	9.2	8.4	-.4	-8.9	10.2	6.7
Housing starts, private	-2.7	43.4	15.1	-13.1	-34.6	-13.4	31.9	16.8
Sales new autos	-12.2	21.9	6.7	4.5	-22.0	-2.8	16.9	8.2
Domestic models	-15.8	21.9	7.4	3.5	-22.4	-5.5	21.9	7.4
Foreign models	15.3	21.9	3.2	9.9	-19.8	11.3	-5.1	11.3

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

FEDERAL SECTOR ACCOUNTS  
(billions of dollars)

	F.R.B. staff estimates										
	Fiscal Year 1977 e/			CY 1976	CY 1977	Calendar quarters; unadjusted data					
	Admin. est. 1/	Cong. est. 2/	F.R. Board	F.R. Board	F.R. Board	1976 III*3/	IV	I	II	III	IV
Unified budget receipts	352.5	362.5	342.9	318.9	351.3	81.8	76.5	77.9	97.0	91.4	85.0
Unified budget outlays	400.0	413.1	413.7	373.2	424.8	94.5	97.7	100.7	106.7	108.6	108.8
Surplus (+)/Deficit(-), unified budget	-47.5	-50.6	-70.8	-54.3	-73.5	-12.7	-21.2	-22.8	-9.7	-17.2	-23.8
Surplus (+)/Deficit(-), off-budget agencies 4/	-11.4	n.a.	-10.8	-8.2	-10.5	-2.0	-1.6	-3.5	-1.2	-4.6	-1.2
Means of financing combined deficits:											
Net borrowing from public	56.9	n.a.	77.3	69.0	85.0	18.0	17.6	24.2	15.6	10.9	25.3
Decrease in cash operating balance	n.a.	n.a.	7.4	-3.3	1.7	-2.6	5.7	2.1	-2.3	1.9	0.0
Other 5/	n.a.	n.a.	-3.0	-3.2	-2.8	-7	-5	--	-2.5	--	-3
Cash operating balance, end of period	n.a.	n.a.	10.0	11.7	10.0	17.4	11.7	9.6	11.9	10.0	10.0
Memo: Sponsored agency borrowing 6/	n.a.	n.a.	2.4	2.9	n.a.	1.7	.3	.6	.7	.8	n.a.
<b>NIA Budget</b>						<b>Seasonally adjusted, annual rates</b>					
Receipts	n.a.	n.a.	349.4 <sup>7/</sup>	329.5	360.7	333.8	343.3	353.9	330.3	373.3	385.5
Outlays	n.a.	n.a.	420.6	388.1	432.1	391.1	402.3	411.4	430.5	438.3	448.4
Purchases (total)	n.a.	n.a.	142.2	133.3	145.3	134.5	138.5	140.9	143.2	146.2	150.9
Defense	n.a.	n.a.	93.1	88.1	95.1	88.5	90.6	92.2	93.5	95.9	98.9
Non-defense	n.a.	n.a.	49.2	45.3	50.2	46.0	47.9	48.7	49.7	50.3	52.0
All other expenditures	n.a.	n.a.	278.4 <sup>7/</sup>	254.8	286.8	256.6	263.8	270.5	287.3	292.1	297.5
Surplus (+)/Deficit(-)	n.a.	n.a.	-71.2 <sup>7/</sup>	-58.6	-71.4	-57.3	-59.0	-57.5	-100.2	-65.0	-62.9
High Employment Surplus (+)/Deficit(-) (NIA basis) 8/	n.a.	n.a.	-21.0	-11.8	-23.5	-9.9	-10.8	-6.7	-45.8	-20.5	-20.8
	*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/ 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 Funds, and Pension Benefit Guaranty Corporation.

5/ Checks issued less checks paid, accrued items and other transactions.

6/ Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.

7/ Quarterly average exceeds fiscal year total by \$.8 billion for FY 1977 due to spreading of wage base effect over calendar year.

8/ Estimated by F.R.B. staff. The high employment budget forecast now incorporates the Council of Economic Advisers revised estimates of potential GNP and also fully incorporates taxes on inventory profits beginning 1973.

## Comments on the Federal Sector Outlook

The staff now forecasts that the fiscal year 1977 deficit will total \$71 billion, about \$5 billion larger than last month. Projected outlays in the current fiscal year have been revised upward from \$411 to \$414 billion. Approximately \$2 billion of this increase results from our assumption of a payment to social security recipients in connection with the one-time tax rebate recently recommended by the incoming Administration. The remaining outlay increase--about \$1 billion--reflects a somewhat higher level of spending in the last two months than was previously anticipated by the staff. Our assumptions concerning an additional \$3 billion spending boost in CY 1977 for public service jobs, public works and countercyclical revenue sharing remain unchanged.

On the receipts side, the staff assumes an \$8 billion rebate on individuals' 1976 income tax liabilities, all of which, including the additional funds for social security recipients, is assumed to be paid in the second quarter. In addition, we now project a smaller permanent tax cut for individuals that would amount to \$4 billion during calendar year 1977. The assumption of a \$2 billion corporate tax cut remains unchanged from the last Greenbook.

Finally, the staff this month has revised its full employment budget in order to incorporate new computations for potential GNP, prepared by the Council of Economic Advisers and to be published in the near future. The Council has lowered full employment GNP as

a result of the slower growth in labor productivity that has prevailed since 1966. Also in view of demographic changes in the labor force, the concept of "full employment" for 1976 has been revised from an unemployment rate of 4 per cent to a rate of 4.9 per cent. These factors reduce the estimate of potential GNP in 1976 by about 4 per cent and imply lower potential tax receipts and thus an increase in the full employment budget deficit of some \$16 billion.

However, the increase in the full employment deficit shown in this Greenbook is only about \$10 billion for 1976 because revisions in tax rates have also been introduced at this time. More specifically, the July 1976 NIA revisions suggested the need for a corporate tax rate adjustment. As a result, the deficit for 1976 is now calculated to be \$11.8 billion, as against the \$1.7 billion shown in the last Greenbook. While this is a large revision in the level of the full employment deficit, quarter to quarter changes in the old and new series tend to be quite similar. Most economists have emphasized these movements as the best indicator of changes in fiscal policy. For CY 1977, we are now projecting a \$12 billion increase in the full employment deficit (to a level of \$23-1/2 billion), reflecting in part the stimulative policy package that has been incorporated in the staff's forecast.

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DOMESTIC FINANCIAL DEVELOPMENTS

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Summary. Financial developments during the inter-meeting period have been dominated by a change in market expectations about monetary policy. Short-term interest rates at the time of the December FOMC meeting were at levels that suggested market expectations of a further easing of monetary policy. But the subsequent stability in the Federal funds rate, the strengthening in recent economic indicators, and more recently the proposed fiscal stimulus, have led to increases in short-term market interest rates ranging up to three-eighths of a percentage point from their mid-December levels.

In long-term markets, with yields at their lowest levels in about three years, the forward calendar of new corporate and State and local bonds has begun to mount, following the seasonal lull in offerings over the turn of the year. However, the initial market impact of the increasing prospective supply was limited by aggressive underwriter pricing and the large continued demand for longer-term securities by institutional investors. But most recently, yields on long-term securities also have risen along with the back-up in short-term rates. Treasury bond yields are currently about 20 basis points above, and other bond yields are slightly above, their levels at the time of the last FOMC meeting.

The step-up in business loan expansion at banks earlier this fall recently has tapered off. This slower growth in bank loans, and total short-term business borrowing, may reflect the reduced rate of

inventory accumulation--especially in manufacturing--as the quarter progressed.

Despite rate cutting on time deposits--and some scattered reductions in offering rates on savings deposits--deposits still remain attractive relative to market securities and inflows have remained large at thrifts and commercial banks. S&L's have continued to increase their commitments to the residential mortgage market, and as other market rates have declined, commercial and savings banks also appear to have increased somewhat their acquisitions of conventional home mortgages. While the conventional mortgage rate has been relatively sticky, most recently there have been some indications that this rate, too, has begun to adjust downward.

Outlook. The demands for funds in securities markets in coming months are expected to be sizable. Treasury and agency net cash borrowings over the first quarter are projected to total nearly \$24 billion (\$22 billion marketable). Moreover, both corporations and State and local governments are being attracted to the bond markets by the current relatively low level of yields, with underwriters reportedly advising their clients that interest costs will move higher as the year progresses. The forward calendar for publicly offered corporate bonds in January and February already exceeds by almost 50 per cent the pace of such offerings in early

1976 and privately placed issues also are expected to remain about as large as last year.<sup>1/</sup>

With the financing gap of businesses (capital and inventory outlays less internal funds generation) remaining quite modest in the aggregate, the large corporate capital market financing can be expected to limit growth in business loans at banks this winter. However, the stimulative impact of the new Administration's fiscal package and large corporate tax payments to cover remaining 1976 tax liabilities may add to short-term credit demands this spring.<sup>2/</sup>

Although market rates may back up a bit more in the near-term in adjustment to expectations of more buoyant economic conditions and greater total credit demands, the staff anticipates that in the next several months long-term yields are likely to fluctuate in a narrow range. Institutional investors, particularly life insurance companies and savings banks, have sizable funds for corporate bond investments, while fire and casualty insurance companies and commercial

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<sup>1/</sup> At the current level of market yields, about \$2-1/2 billion of high-coupon corporate bonds are vulnerable to call for refunding. The January calendar includes about \$215 million of such advance refundings. In addition, about \$425 million of AT&T (and subsidiary) bonds are being called and not refunded this month.

<sup>2/</sup> In March and June most corporations are scheduled to make final payments on their 1976 tax liabilities and in April their first payment on 1977 estimated tax liabilities. In the second quarter of 1977 total payments will exceed accruals of tax liability on current income by almost \$8 billion, some \$3 billion more than in 1976. Thus, tax payments may marginally increase business credit demands this spring.

banks are expected to remain large buyers of tax-exempt bonds. The conventional home mortgage rate may be subject to some further downward pressure as both commercial and savings banks are increasingly attracted to the mortgage market by the relatively high level of yields. Shorter-term yields, on the other hand, may be subject to moderate upward rate pressures later this winter and in the spring as the economy picks up from its recent more sluggish pace.

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INTERNATIONAL DEVELOPMENTS

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Summary: In the four weeks since the last green book, the U.S. dollar on a trade-weighted basis has declined further by about 1/2 per cent. By early January, the decline had reached about 1.2 per cent

. Subsequently, however, the dollar strengthened against all major foreign currencies, as U.S. market interest rates rose absolutely and relative to European interest rates and the details of the new administration's fiscal program became known.

The pound sterling has risen by almost 2 per cent against the dollar over the past four weeks. It was buoyed first by the successful completion of negotiations for a \$3.9 billion stand-by arrangement with the IMF and related financial arrangements. On January 10, sterling rose temporarily with the announcement from the BIS of agreement on a \$3 billion medium-term facility to offset, under specified conditions, reductions in official sterling balances; on the following day sterling dropped back sharply. Under the agreement on sterling balances, the British will seek an orderly reduction in the reserve currency role of sterling and will fund a portion of official sterling balances through foreign currency bonds placed with official holders. To the extent that the BIS cannot from its own resources provide financing to the British for reductions in official sterling holdings (valued at \$3.8 billion on September 30, 1976), the United States and other countries will provide a back-up facility. The U.S. share will be \$1 billion.

Despite the continued evidence of a slowdown in economic activity abroad, no major shifts in the stance of domestic monetary policy have occurred in major foreign countries since September. However, short-term interest rates in most foreign countries have declined recently from earlier highs reached, in most cases, in response to exchange-market pressures. The preceding decline in U.S. interest rates may have permitted these countries to tolerate a reduction in domestic interest rates a bit earlier than they had planned or hoped. Except in Italy and France, two countries where inflationary pressures remain severe, long-term interest rates have also declined somewhat over the past several months.

Recent data on U.S. international transactions show a rise in the U.S. trade deficit in November. The October-November deficit, however, was about at the 1976 third-quarter rate of \$12 billion. Agricultural exports for the two months were below the record rate in the third quarter, while non-agricultural exports were also down somewhat, reflecting the pause in expansion abroad. The recent decline in exports of machinery is, however, surprising given the recent strength of new export orders for these goods. Non-fuel imports declined in October and November as expected given the slowdown in domestic economic growth and the lingering influence of the Ford strike. After a dip in October, imports of fuels reached a record high of 8.8 million barrels a day in November. The average price, \$12.34 per barrel, was about 1 per cent above the average for the third quarter.

Bank-reported capital transactions, which have been highly variable, shifted to a sizeable net outflow in November, following a net inflow in October. For the two months combined, the net outflow was close to the average rate in the first two quarters of 1976 and up from the rate in the third quarter. New issues of foreign bonds in the United States in the fourth quarter of 1976 were at about their yearly average of \$2.5 billion per quarter, but declined somewhat in January in the face of a heavy volume of new issues of U.S. corporate bonds.

Newly available data on military and service transactions show the surplus in these accounts rose to \$15.6 billion at an annual rate in the third quarter of 1976 from a revised \$12.3 billion in the second quarter and \$7.3 billion for all of 1975. This latter rise reflects a \$2.3 billion swing in net military transactions and a \$4.8 billion increase in net investment receipts.

Outlook. The expected growth of real GNP in the major foreign industrial countries in 1977 over 1976 has been reduced to 3.3 per cent in this month's green book from our projection of 3.7 per cent last month. On the basis of this change and the continued weakness of actual exports, 1977 U.S. exports are now projected to be about \$2 billion lower than was expected last month. With an outlook now for slightly higher U.S. imports in 1977, the merchandise trade deficit is projected to be about \$15-1/2 billion in 1977, about \$3 billion larger than was projected last month. The deficit will decline to slightly under \$15 billion (annual rate) in the fourth quarter as Alaskan oil begins to reduce

the oil-import bill. However, because of the stronger picture for net military and services transactions the outlook for net exports of goods and services and the U.S. current account is essentially unchanged from that in last month's green book.

The staff expects that by early 1978 the weighted-average value of the dollar will have risen by, perhaps, 5 per cent from its present level. This outlook is consistent with, inter alia, one-year forward exchange rates observed in the market.

	1975	1976 <sup>P</sup> 1977 <sup>P</sup>		1 9 7 6				1 9 7 7 <sup>P</sup>			
				I	II	III	IV <sup>P</sup>	I	II	III	IV
<b>Billions of dollars</b>											
Net Exports of Goods and Services (GNP basis of net exports) <u>1/</u>	16.3 (20.5)	4.2 (6.5)	-.1 (1.9)	4.2 (8.4)	6.9 (9.3)	3.5 (4.7)	2.4 (3.6)	3.1 (4.5)	-2.0 (-.1)	-2.3 (--)	.7 (3.0)
Merchandise Trade Balance (excl. military)	8.9	-9.4	-15.5	-6.7	-5.4	-12.1	-13.1	-12.4	-17.3	-17.6	-14.9
Exports (excl. military)	107.1	114.1	126.7	107.3	113.7	118.3	117.0	120.9	124.8	128.5	132.5
Agricultural	22.2	23.5	23.2	21.3	23.4	25.4	24.0	22.5	23.1	23.3	23.7
Nonagricultural	84.8	90.6	103.5	86.1	90.3	93.0	93.0	98.4	101.7	105.2	108.8
Imports	98.1	123.5	142.2	114.0	119.1	130.5	130.1	133.3	142.1	146.1	147.4
Fuels	28.5	37.1	42.4	31.8	36.5	40.1	39.8	38.5	43.8	44.3	43.0
Nonfuels	69.5	86.4	99.8	82.3	82.6	90.4	90.3	94.8	98.3	101.8	104.4
Military and Service Transactions, net	7.3	13.6	15.4	10.9	12.3	15.6	15.5	15.5	15.3	15.3	15.6
Military transactions, net	-.9	.6	1.5	--	-.6	1.5	1.4	1.4	1.5	1.5	1.6
Investment income, net	6.0	10.4	11.9	9.1	9.8	10.8	11.9	11.9	12.0	11.9	12.0
Other services, net	2.1	2.6	2.0	1.8	3.1	3.3	2.2	2.2	1.8	1.9	2.0
U.S. Current Account Balance <u>2/</u>	11.7	-.9	-4.8	-.2	3.3	-4.2	-2.1	-1.5	-6.6	-7.0	-4.0
<b>Constant (1972) dollars</b>											
Merchandise exports (excl. military) (% change, annual rates)	64.6 (-2.4)	66.1 (2.3)	69.6 (5.3)	63.3 (-19.3)	66.5 (21.6)	68.4 (11.7)	66.3 (-13.0)	68.2 (11.7)	69.1 (5.3)	70.0 (5.3)	71.2 (7.0)
Merchandise imports (% change, annual rates)	51.3 (-12.5)	62.2 (21.3)	67.0 (7.7)	59.0 (44.8)	60.5 (10.8)	65.4 (36.6)	64.0 (-8.7)	64.5 (2.8)	67.4 (19.0)	68.2 (7.8)	67.8 (-2.3)
<b>Foreign Outlook - Major Industrial Countries <u>3/</u></b>											
Real GNP, % change, annual rate	-1.1	4.5	3.3	8.1	2.8	2.1	1.8	3.3	4.2	5.0	5.1
Wholesale Prices, % change, A.R. <u>4/</u>	6.0	9.4	9.5	11.4	16.9	11.9	7.4	10.0	9.1	7.6	7.6

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