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# Part 1

November 9, 1977

## 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

CONFIDENTIAL (FR)

November 9, 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. Recent economic indicators suggest a somewhat more rapid pace of activity in the fourth quarter than the reduced third quarter rate. Consumer demand appears to have picked up, and residential construction remains buoyant. There are also signs of continued advance in capital outlays. However, industrial production and employment rose only moderately in October and private surveys of business fixed investment plans indicate smaller gains for 1978 than this year. At the same time, finished goods prices at wholesale rose sharply in October, possibly presaging a larger price rise at retail following the small increases in August and September.

Retail sales are estimated on the basis of weekly data to have moved up sharply in October, after several months of lackluster performance. Purchases at general merchandise, furniture and appliance, and food stores appear to have moved up quite sharply. Unit auto sales also increased somewhat in October; sales of domestic models, which may have been adversely affected in September by the delayed availability of 1978 models, rose to a 9.1 million unit annual rate. Sales of foreign autos edged down to a 1.8 million unit annual rate, reportedly because of depleted inventories of some popular models.

Industrial production is tentatively estimated to have increased by one-quarter to one-half per cent in October. Employment growth slowed and the unemployment rate edged back up to 7.0 per cent, the

seventh consecutive month at about that level. The increase in nonfarm payroll employment totaled only 120,000 (165,000 after allowance for increased strike activity); the service-producing industries showed smaller gains, and layoffs in the steel industry and strikes at aerospace firms more than offset moderate job rises in most other sectors of manufacturing. The average workweek in manufacturing edged back up to 40.3 hours.

Residential building activity has continued at a robust pace. Total private housing starts were at a 2.04 million unit annual rate in September--about the same as the third quarter average, which was almost 8 per cent above the second quarter. Single family starts continued near a record rate of 1.5 million while multi-family starts moved somewhat lower. Continued strength in demand is evidenced by the very strong sales pace of new and existing houses during the quarter. Moreover, vacancy rates remain historically quite low.

On the basis of incomplete data, the Commerce Department estimated that nonfarm inventory accumulation (GNP basis) in the third quarter was slightly reduced from the second quarter pace. Book value data indicate a relatively slow rate of increase at manufacturers early in the third quarter. In September, however, accumulation picked up, largely reflecting faster growth for nondurables, especially food and related products. Accumulation at trade establishments was exceptionally large in August.

Indicators of business fixed investment activity continue mixed. New orders for nondefense capital goods rose 8.7 per cent in September but for the third quarter as a whole these orders were off marginally from the second quarter rate. However, the machinery component of such orders--generally a better indicator of future trends in business fixed investment than the total--was up about 5-1/2 per cent from the second quarter. In addition, construction contracts for commercial and industrial buildings (measured in square feet) rose sharply in the third quarter, to their highest level since 1974, with both components showing strong gains.

At the same time, the McGraw-Hill capital spending survey--generally considered the most reliable of the private surveys--indicated an increase of only 11 per cent in 1978. The survey suggested continued strength for most durable manufacturers. However, little increase was indicated for petroleum and the rise planned by electric utilities was significantly under the 1977 increase. An overall rise of this magnitude would result in a smaller increase in business fixed investment in real terms than this year's likely gain of about 8-3/4 per cent.

Increases in government spending contributed substantially to the growth of real output in the third quarter, as implementation of public service employment programs contributed to a large gain in State and local employment. State and local construction activity was apparently little changed between the second and third quarter, however, despite substantial disbursements of Federal funds under the Public Works Program.

Retail price increases have been smaller recently than during the first half of the year. The Consumer Price Index rose only 0.3 per cent in September--about the same as in August--as both food and non-food commodities rose modestly and prices of services increased at a slower pace than earlier in the year. In October, however, wholesale prices rose 0.8 per cent, as prices of farm products and processed feeds increased sharply after declining for four months. Among industrial commodities, there were large price rises for a number of producer finished goods (trucks, aircraft and some machinery items). In addition, prices of consumer nonfood finished goods registered another sizable increase last month.

Outlook. The staff estimate of real growth in the fourth quarter has been revised down slightly. Inventory investment, which was somewhat greater in the third quarter than the staff had previously assumed, is now expected to show a smaller rise in the fourth quarter. But consumption outlays appear likely to be a bit stronger, and on balance we now anticipate an increase in real GNP at an annual rate of 5 per cent.

The fiscal and monetary policy assumptions underlying the forecast are unchanged from those incorporated last month. The deficit expected for fiscal year 1978 remains a shade below \$59 billion and the full employment budget still is expected to move toward balance by the end of the year. Growth of  $M_1$  is still assumed to average 5-1/4 per cent

through 1978-QIII and short-term interest rates are projected to move upward through the second half of next year.

Real GNP growth during 1978 is now expected to average nearly 4-1/2 per cent--fractionally lower than last month's projection, with the rate of increase close to 4 per cent toward year end. In large part, the moderation during the year reflects a slowing of growth of residential construction activity. We still assume a fairly steady growth in real business fixed investment outlays, but the projection of capital spending has been trimmed back a bit in light of our assessment of recent indicators. In response to a slowing of income growth, real consumption is projected to increase at an average annual rate of 3-3/4 per cent during 1978. In this circumstance, the savings rate is projected to average about 6-1/4 per cent next year, a significant increase from the low rate early this year.

Output growth now indicated for 1978 implies relatively little improvement in the unemployment rate--now projected to average 6.6 per cent late next year. Productivity gains are still projected to average about 2 per cent next year and labor cost and general price increases are expected to average around 6-1/2 per cent for 1978.

Details of the staff projections are shown in the tables that follow.

## STAFF GNP PROJECTIONS

	Per cent changes, annual rate							
	Nominal GNP		Real GNP		Gross business product fixed-weighted price index		Unemployment rate (per cent)	
	10/12/77	11/9/77	10/12/77	11/9/77	10/12/77	11/9/77	10/12/77	11/9/77
1974 <sup>1/</sup>	8.1	8.1	-1.4	-1.4	10.4	10.4	5.6	5.6
1975 <sup>1/</sup>	8.2	8.2	-1.3	-1.3	9.5	9.5	8.5	8.5
1976 <sup>1/</sup>	11.6	11.6	6.0	6.0	5.4	5.4	7.7	7.7
1977	10.8	10.7	4.8	4.8	6.0	6.0	7.1	7.1
1978	11.3	11.2	4.7	4.6	6.4	6.3	6.6	6.6
1977-I <sup>1/</sup>	13.2	13.2	7.5	7.5	6.8	6.8	7.4	7.4
1977-II <sup>1/</sup>	13.7	13.7	6.2	6.2	7.5	7.5	7.0	7.0
1977-III <sup>1/</sup>	9.2	9.2	3.8	3.8	5.3	5.2	7.0	7.0
1977-IV	12.4	12.1	5.2	5.0	6.0	6.0	6.9	6.9
1978-I	11.4	11.4	4.8	4.7	6.8	6.8	6.7	6.7
1978-II	11.2	10.9	4.7	4.5	6.5	6.5	6.7	6.7
1978-III	10.6	10.5	4.3	4.2	6.2	6.2	6.6	6.6
1978-IV	11.3	11.3	4.3	4.1	6.3	6.3	6.6	6.6
Change:								
76-II to 77-II <sup>1/</sup>	10.5	10.5	4.7	4.7	6.1	6.1	-.4	-.4
76-IV to 77-IV	12.1	12.0	5.7	5.6	6.4	6.4	-1.0	-1.0
77-II to 78-II	11.0	10.9	4.6	4.5	6.1	6.1	-.3	-.3
77-IV to 78-IV	11.1	11.0	4.5	4.4	6.4	6.4	-.3	-.3

<sup>1/</sup> Actual.

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

	1977				1978			
	I	II	III	IV	Projected			
	I	II	III	IV	I	II	III	IV
Gross National Product	1810.8	1869.9	1911.3	1966.8	2020.7	2073.5	2125.7	2183.5
Final purchases	1797.0	1848.2	1891.5	1945.7	2002.1	2049.7	2100.5	2156.1
Private	1422.1	1457.6	1485.9	1526.2	1572.2	1609.4	1649.4	1691.6
Excluding net exports	1430.3	1467.3	1497.5	1539.3	1583.7	1625.1	1665.8	1708.2
Personal consumption expenditures	1172.4	1194.0	1216.7	1246.7	1279.4	1310.9	1342.0	1375.0
Goods	643.6	653.0	654.9	669.9	687.6	704.1	720.7	738.5
Services	528.8	541.1	561.8	576.8	591.8	606.8	621.3	636.5
Gross private domestic investment	271.8	294.9	300.6	313.7	322.9	338.0	349.0	360.6
Residential construction	81.0	90.8	93.1	99.1	104.6	108.1	111.1	113.6
Business fixed investment	177.0	182.4	187.7	193.5	199.7	206.1	212.7	219.6
Change in business inventories	13.8	21.7	19.8	21.1	18.6	23.8	25.2	27.4
Nonfarm	14.1	22.4	19.3	20.8	18.6	23.8	25.2	27.4
Net exports of goods and services <sup>1/</sup>	-8.2	-9.7	-11.6	-13.1	-11.5	-15.7	-16.4	-16.6
Exports	170.4	178.1	174.9	173.9	186.6	192.1	198.6	204.3
Imports	178.6	187.7	186.6	187.1	198.2	207.9	215.1	221.0
Gov't. purchases of goods and services	374.9	390.6	405.6	419.5	429.9	440.3	451.1	464.5
Federal <sup>2/</sup>	136.3	143.6	151.5	157.6	160.2	163.0	166.3	172.2
State and local	238.5	247.0	254.1	261.9	269.7	277.3	284.8	292.3
Gross national product in constant (1972) dollars	1311.0	1330.7	1343.2	1359.6	1375.3	1390.6	1404.8	1419.1
Personal income	1476.8	1517.2	1548.3	1597.7	1635.5	1675.8	1724.0	1770.2
Wage and salary disbursements	951.3	980.9	997.1	1025.3	1053.3	1077.8	1103.8	1133.2
Disposable income	1252.4	1292.5	1320.5	1363.1	1401.2	1433.4	1467.0	1503.4
Saving rate (per cent)	4.1	5.3	5.5	6.2	6.4	6.2	6.2	6.2
Corporate profits with I.V.A. and C.C. Adj.	125.4	140.2	147.2	153.7	150.4	156.2	159.7	165.6
Corporate profits before tax	161.7	174.0	171.2	185.7	182.7	188.7	192.2	198.1
Federal government surplus or deficit (-) (N.I.A. basis)	-38.8	-40.3	-59.3	-59.6	-54.6	-49.3	-43.3	-40.8
High employment surplus or deficit (-)	9.4	-5	-18.5	-19.9	-12.7	-7.7	-2.3	-2
State and local government surplus or deficit (-) (N.I.A. basis)	27.3	25.4	30.6	28.0	25.8	25.1	23.7	21.7
Excluding social insurance funds	11.9	10.0	15.1	10.9	8.3	7.1	5.2	2.7
Civilian labor force (millions)	96.1	97.2	97.6	98.2	98.7	99.3	99.9	100.4
Unemployment rate (per cent)	7.4	7.0	7.0	6.9	6.7	6.7	6.6	6.6
Nonfarm payroll employment (millions)	80.9	81.9	82.5	83.1	83.7	84.3	84.9	85.4
Manufacturing	19.3	19.6	19.6	19.7	19.9	20.1	20.3	20.5
Industrial production (1967=100)	133.6	137.0	138.6	140.0	142.5	145.1	147.4	149.7
Capacity utilization: all manufacturing (per cent)	81.2	82.7	83.0	83.0	83.7	84.4	84.9	85.3
Materials (per cent)	80.4	82.6	82.8	83.0	83.9	84.7	85.3	86.0
Housing starts, private (millions, A.R.)	1.76	1.91	2.05	2.15	2.20	2.10	2.05	2.00
Sales new autos, (millions, A.R.)	11.12	11.70	10.92	11.20	11.35	11.40	11.40	11.40
Domestic models	9.28	9.34	8.88	9.20	9.45	9.50	9.50	9.50
Foreign models	1.84	2.36	2.04	2.00	1.90	1.90	1.90	1.90

<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.

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CHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1977				1978			
	I	II	III	IV	Projected			
	I	II	III	IV	I	II	III	IV
	-----Billions of dollars-----							
Gross National Product	55.4	59.1	41.4	55.5	53.9	52.8	52.2	57.8
Inventory change	14.7	7.9	-1.9	1.3	-2.5	5.2	1.4	2.2
Final purchases	40.7	51.2	43.3	54.2	56.4	47.6	50.8	55.6
Private	35.8	35.5	28.3	40.3	46.0	37.2	40.0	42.2
Net exports	-11.2	-1.5	-1.9	-1.5	1.6	-4.2	-.7	-.2
Excluding net exports	47.0	37.0	30.2	41.8	44.4	41.4	40.7	42.4
Personal consumption expenditures	33.4	21.6	22.7	30.0	32.7	31.5	31.1	33.0
Goods	18.5	9.4	1.9	15.0	17.7	16.5	16.6	17.8
Services	14.9	12.3	20.7	15.0	15.0	15.0	14.5	15.2
Residential fixed investment	4.3	9.8	2.3	6.0	5.5	3.5	3.0	2.5
Business fixed investment	9.4	5.4	5.3	5.8	6.2	6.4	6.6	6.9
Government	4.9	15.7	15.0	13.9	10.4	10.4	10.8	13.4
Federal	2.1	7.3	7.9	6.1	2.6	2.8	3.3	5.9
State and local	2.7	8.5	7.1	7.8	7.8	7.6	7.5	7.5
GNP in constant (1972) dollars	23.6	19.7	12.5	16.5	15.6	15.3	14.2	14.3
Final purchases	12.0	16.3	12.6	15.6	16.8	11.9	13.6	12.8
Private	13.3	9.6	5.6	12.5	14.0	9.2	10.8	11.3
	-----In Per Cent Per Year <sup>1/</sup> -----							
Gross National Product	13.2	13.7	9.2	12.1	11.4	10.9	10.5	11.3
Final purchases	9.6	11.9	9.7	12.0	12.1	9.9	10.3	11.0
Private	10.7	10.4	8.0	11.3	12.6	9.8	10.3	10.6
Personal consumption expenditures	12.2	7.6	7.8	10.2	10.9	10.2	9.8	10.2
Goods	12.4	6.0	1.2	9.5	11.0	9.9	9.8	10.3
Services	12.0	9.6	16.2	11.1	10.8	10.5	9.9	10.2
Gross private domestic investment	55.5	38.6	8.0	18.6	12.3	20.1	13.7	14.0
Residential structures	24.2	57.9	10.8	28.4	24.1	14.1	11.6	9.3
Business fixed investment	24.5	12.8	12.0	12.9	13.4	13.4	13.4	13.6
Gov't. purchases of goods and services	5.4	17.9	16.3	14.4	10.3	10.0	10.2	12.4
Federal	6.6	23.3	23.8	17.1	6.8	7.2	8.3	15.0
State and local	4.7	14.9	12.1	12.9	12.5	11.8	11.3	11.0
GNP in constant (1972) dollars	7.5	6.2	3.8	5.0	4.7	4.5	4.2	4.1
Final purchases	3.8	5.1	3.9	4.8	5.1	3.6	4.0	3.7
Private	5.3	3.8	2.2	4.8	5.4	3.4	4.0	4.2
GNP implicit deflator <sup>2/</sup>	5.3	7.1	5.1	6.8	6.4	6.1	6.0	6.9
Gross business product fixed-weighted price index <sup>3/</sup>	6.8	7.5	5.2	6.0	6.8	6.5	6.2	6.3
Personal income	13.1	11.4	8.5	13.4	9.8	10.2	12.0	11.2
Wage and salary disbursements	12.7	13.0	6.8	11.8	11.4	9.6	10.0	11.1
Disposable income	10.1	13.4	9.0	13.5	11.6	9.5	9.7	10.3
Corporate profits before tax	19.1	34.1	-6.3	38.6	-6.3	13.6	7.8	12.8
Nonfarm payroll employment	4.3	4.9	3.2	2.7	3.0	2.6	2.9	2.7
Manufacturing	5.3	6.4	1.1	1.6	4.5	4.8	3.5	3.6
Nonfarm business sector								
Output per hour	4.8	7	3.5	2.2	2.2	2.2	2.0	2.0
Compensation per hour	11.4	7.5	7.4	7.7	11.2	7.8	7.9	7.9
Unit labor costs	6.3	6.8	3.7	5.5	9.0	5.6	5.9	5.9
Industrial production	6.2	10.6	4.8	4.1	7.5	7.4	6.4	6.3
Housing starts, private	-2.6	37.7	34.8	20.5	9.6	-17.0	-9.2	-9.4
Sales new autos	53.4	22.5	-24.1	10.5	5.5	1.8	.0	.0
Domestic models	55.1	2.6	-18.4	15.2	11.3	2.1	.0	.0
Foreign models	45.2	170.5	-43.9	-8.2	-18.5	.0	.0	.0

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

<sup>2/</sup> Excluding Federal pay increases rates of change are: 1977-I, 5.3 per cent; 1977-IV, 6.1 per cent; 1978-I, 6.4 per cent; 1978-IV, 6.2 per cent.

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

November 9, 1977

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CLASS II FOMCGROSS NATIONAL PRODUCT AND RELATED ITEMS  
(Expenditures and income figures are billions of dollars)

	1971	1972	1973	1974	1975	1976	1977	1978
Gross National Product	1063.4	1171.1	1306.6	1412.9	1528.8	1706.5	1889.7	2100.8
Final purchases	1057.1	1161.7	1288.6	1404.0	1540.3	1693.1	1870.6	2077.1
Private	823.4	908.6	1019.1	1101.3	1201.4	1331.7	1473.0	1630.6
Excluding net exports	821.8	911.9	1012.0	1095.3	1181.0	1323.9	1483.6	1645.7
Personal consumption expenditures	668.2	733.0	809.9	889.6	980.4	1093.9	1207.4	1326.8
Goods	374.8	410.5	457.5	498.3	542.2	601.6	655.4	712.7
Services	293.4	322.4	352.3	391.3	438.2	492.3	552.1	614.1
Gross private domestic investment	160.0	188.3	220.0	214.6	189.1	243.3	295.3	342.6
Residential construction	49.6	62.0	66.1	55.1	51.5	68.0	91.0	109.3
Business fixed investment	104.1	116.8	136.0	150.6	149.1	161.9	185.2	209.5
Change in business inventories	6.4	9.4	17.9	8.9	-11.5	13.3	19.1	23.7
Nonfarm	5.1	8.8	14.7	10.8	-15.1	14.9	19.1	23.7
Net exports of goods and services	1.6	-3.3	7.1	6.0	20.4	7.8	-10.7	-15.1
Exports	65.6	72.7	101.6	137.9	147.3	162.9	174.3	195.4
Imports	64.0	75.9	94.4	131.9	126.9	155.1	185.0	210.5
Gov't. purchases of goods and services	233.7	253.1	269.5	302.7	338.9	361.4	397.7	446.4
Federal	96.2	102.1	102.2	111.1	123.3	130.1	147.2	165.4
State and local	137.5	151.0	167.3	191.5	215.6	231.2	250.4	281.0
Gross national product in constant (1972) dollars	1107.5	1171.1	1235.0	1217.8	1202.1	1274.7	1336.1	1397.5
Personal income	859.1	942.5	1052.4	1154.9	1253.4	1382.7	1535.0	1701.4
Wage and salary disbursements	579.4	633.8	701.3	764.6	805.7	891.8	988.7	1092.0
Disposable income	742.8	801.3	901.7	984.6	1084.4	1185.8	1307.1	1451.2
Saving rate (per cent)	7.7	6.2	7.8	7.3	7.4	5.6	5.3	6.2
Corporate profits with I.V.A. and C.C. Adj.	77.2	92.1	99.1	83.6	99.3	128.1	141.6	158.0
Corporate profits before tax	82.0	96.2	115.8	126.9	123.5	156.9	173.2	190.4
Federal government surplus or deficit (-) (N.I.A. basis)	-22.0	-17.3	-6.7	-10.7	-70.2	-54.0	-49.5	-47.0
High employment surplus or deficit (-)	-5.3	-5.9	-7	17.1	-20.3	-10.4	-7.4	-5.7
State and local government surplus or deficit (-) (N.I.A. basis)	3.7	13.7	13.0	7.5	5.9	18.4	27.8	24.1
Excluding social insurance funds	-3.8	5.6	4.1	-2.9	-6.2	3.9	12.0	5.8
Civilian labor force (millions)	84.1	86.5	88.7	91.0	92.6	94.8	97.3	99.6
Unemployment rate (per cent)	6.0	5.6	4.9	5.6	8.5	7.7	7.1	6.6
Nonfarm payroll employment (millions)	71.2	73.7	76.9	78.4	77.1	79.4	82.1	84.6
Manufacturing	18.6	19.1	20.1	20.0	18.3	19.0	19.6	20.2
Industrial production (1967=100)	109.6	119.7	129.8	129.3	117.8	129.8	137.3	146.2
Capacity utilization: all manufacturing (per cent)	78.0	83.1	87.5	84.2	73.6	80.2	82.5	84.6
Materials (per cent)	83.1	88.0	92.4	87.7	73.6	80.4	82.2	85.0
Housing starts, private (millions, A.R.)	2.05	2.36	2.05	1.34	1.16	1.54	1.97	2.09
Sales new autos (millions, A.R.)	10.24	10.93	11.42	8.91	8.66	10.12	11.24	11.39
Domestic models	8.68	9.32	9.65	7.49	7.08	8.63	9.18	9.49
Foreign models	1.56	1.61	1.77	1.42	1.58	1.50	2.06	1.90

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CHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1971	1972	1973	1974	1975	1976	1977	1978
-----Billions of Dollars-----								
Gross National Product	81.0	107.7	135.5	106.3	115.9	177.7	183.2	211.1
Inventory change	2.6	3.0	8.5	-9.0	-20.4	24.8	5.8	4.7
Final purchases	78.5	104.6	126.9	115.4	136.3	152.8	177.5	206.4
Private	63.7	85.2	110.5	82.2	100.1	130.3	141.3	157.6
Net exports	-2.3	-4.9	10.4	-1.1	14.4	-12.6	-18.5	-4.4
Excluding net exports	66.0	90.1	100.1	83.3	85.7	142.9	159.7	162.1
Personal consumption expenditures	49.4	64.8	76.9	79.7	90.8	113.5	113.5	119.4
Goods	25.2	35.7	47.0	40.8	43.9	59.4	53.8	57.3
Services	24.3	29.0	29.9	39.0	46.9	54.1	59.8	62.0
Residential fixed investment	13.0	12.4	4.1	-11.0	-3.6	16.5	23.0	18.3
Business fixed investment	3.6	12.7	19.2	14.6	-1.5	12.8	23.3	24.4
Government	14.8	19.4	16.4	33.2	36.2	22.5	36.3	48.7
Federal	.6	5.9	.1	8.9	12.2	6.8	17.1	18.2
State and local	14.3	13.5	16.3	24.2	24.1	15.6	19.2	30.6
GNP in constant (1972) dollars	32.2	63.6	63.9	-17.2	-15.7	72.6	61.4	61.3
Final purchases	29.9	60.8	56.8	-8.6	2.1	54.2	57.4	57.7
Private	30.7	57.1	57.4	-13.8	-3.2	52.8	49.3	43.6
-----In Per Cent Per Year-----								
Gross National Product	8.2	10.1	11.6	8.1	8.2	11.6	10.7	11.2
Final purchases	8.0	9.9	10.9	8.9	9.7	9.9	10.5	11.0
Private	8.4	10.3	12.2	8.1	9.1	10.8	10.6	10.7
Personal consumption expenditures	8.0	9.7	10.5	9.8	10.2	11.6	10.4	9.9
Goods	7.2	9.5	11.4	8.9	8.8	11.0	8.9	8.7
Services	9.0	9.9	9.3	11.1	12.0	12.4	12.1	11.2
Gross private domestic investment	13.6	17.7	16.8	-2.5	-11.9	28.7	21.4	16.0
Residential structures	35.5	25.1	6.6	-16.7	-6.5	32.2	33.8	20.2
Business fixed investment	3.6	12.3	16.4	10.8	-1.0	8.6	14.4	13.1
Gov't. purchases of goods and services	6.8	8.3	6.5	12.3	12.0	6.6	10.0	12.2
Federal	.6	6.1	.1	8.7	11.0	5.5	13.1	12.3
State and local	11.6	9.8	10.8	14.5	12.6	7.2	8.3	12.2
GNP in constant (1972) dollars	3.0	5.7	5.5	-1.4	-1.3	6.0	4.8	4.6
Final purchases	2.8	5.5	4.9	-.7	.2	4.5	4.5	4.4
Private	3.7	6.7	6.3	-1.4	-.3	5.6	4.9	4.2
GNP implicit deflator	5.1	4.1	5.8	9.7	9.6	5.3	5.6	6.3
Gross business product fixed-weighted price index <sup>1/</sup>	4.4	3.3	5.7	10.4	9.5	5.4	6.0	6.3
Personal income	7.2	9.7	11.7	9.7	8.5	10.3	11.0	10.8
Wage and salary disbursements	6.0	9.4	10.7	9.0	5.4	10.7	10.9	10.4
Disposable income	8.3	7.9	12.5	9.2	10.1	9.4	10.2	11.0
Corporate profits before tax	14.7	17.3	20.4	9.6	-2.7	27.0	10.4	9.9
Nonfarm payroll employment	.4	3.5	4.3	2.0	-1.7	3.1	3.4	3.0
Manufacturing	-4.0	2.8	5.1	-1	-8.5	3.3	3.2	3.5
Nonfarm business sector								
Output per hour	2.9	3.0	1.7	-2.9	1.6	4.1	2.2	2.2
Compensation per hour	6.6	5.8	7.8	9.4	9.6	8.7	8.7	8.6
Unit labor costs	3.5	2.7	6.0	12.7	7.9	4.5	6.4	6.3
Industrial production	1.7	9.2	8.4	-.4	-8.9	10.2	5.8	6.5
Housing starts	43.1	14.9	-13.2	-34.6	-13.3	32.6	27.8	6.3
Sales new autos	21.9	6.8	-4.7	-14.5	-2.8	16.9	11.0	1.4
Domestic models	21.9	7.4	3.5	-22.4	-5.5	21.9	6.4	3.4
Foreign models	21.8	3.1	9.7	-19.9	11.4	-5.1	37.6	-7.8

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

FEDERAL SECTOR ACCOUNTS  
(billions of dollars)

	Fiscal Year 1977*	FY 1978 e/			CY 1976 *	CY 1977 e/		Calendar quarters; unadjusted data						
		Admin. est. 1/	F.R. Board	Cong. est. 2/		F.R. Board	1977				1978			
							I*	II*	III*	IV	I	II	III	
Unified budget receipts	356.9	401.4	397.0	397.0	317.6	367.2	79.0	110.5	91.3	86.4	86.4	119.8	104.4	
Unified budget outlays	401.9	462.9	455.5	458.3	374.2	411.7	97.6	101.8	103.4	108.9	109.3	115.3	122.0	
Surplus(+)/Deficit(-), unified budget	-45.0	-61.5	-58.5	-61.3	-56.6	-44.5	-18.7	8.6	-12.2	-22.5	-22.9	4.5	-17.6	
Surplus(+)/Deficit(-), off-budget agencies 3/	-8.7	-7.7	-10.9	n.a.	-5.7	-11.4	-4.3	.1	-4.9	-2.3	-3.0	-0.9	-4.7	
Means of financing combined deficits:														
Net borrowing from public	53.5	n.a.	62.4	n.a.	69.0	54.1	17.6	-1.1	19.6 <sup>8/</sup>	18.0 <sup>8/</sup>	23.5	-2.1	23.0	
Decrease in cash operating balance	-1.7	n.a.	7.1	n.a.	-3.2	-0.3	2.6	-7.2	-2.8 <sup>8/</sup>	7.1 <sup>8/</sup>	0	0	0	
Other 4/	1.9	n.a.	-0.2	n.a.	-3.5	2.4	2.7	-4	0.4	-0.3	2.3	-1.5	-0.7	
Cash operating balance, end of period	19.1	n.a.	12.0	n.a.	11.7	12.0	9.0	16.3	19.1 <sup>8/</sup>	12.0	12.0	12.0	12.0	
Memo: Sponsored agency borrowing 5/	6.1	n.a.	n.e.	n.a.	2.9	7.2	.7	3.0	2.0	1.5	2.8	n.e.	n.e.	
<u>NIA Budget</u>							<u>Seasonally adjusted annual rates</u>							
Receipts	362.7 <sup>6/</sup>	415.3	409.3 <sup>6/</sup>	n.a.	332.3	374.9	364.9	371.2	374.6e	388.9	402.7	415.7	434.2	
Outlays	412.4p	469.3	462.1	n.a.	386.3	424.5	403.7	411.5	434.0p	448.6	457.3	465.0	477.5	
Purchases (total)	141.4p	163.5	161.8	n.a.	130.1	147.3	136.3	143.6	151.5p	157.6	160.2	163.0	166.3	
Defense	92.2p	105.2	103.6	n.a.	86.8	95.4	89.7	93.4	97.3p	101.1	102.8	104.5	106.1	
Non-defense	49.2p	58.3	58.2	n.a.	43.3	51.9	46.7	50.2	54.2p	56.5	57.4	58.5	60.2	
All other outlays	271.0p	305.8	300.3 <sup>6/</sup>	n.a.	256.2	277.2	267.4	267.9	282.5p	291.0	297.1	302.0	311.2	
Surplus(+)/Deficit(-)	-49.7 <sup>8/</sup>	-54.0	-52.8 <sup>6/</sup>	n.a.	-54.0	-49.5	-38.8	-40.3	-59.4e	-59.6	-54.6	-49.3	-43.3	
High Employment Surplus(+)/Deficit (NIA basis) 7/	-4.3	n.a.	-10.7	n.a.	-10.4	-7.4	9.5	-0.5	-18.5	-19.9	-12.7	-7.7	-2.3	
	*actual	e--estimated	r--revised	n.e.--not estimated			n.a.--not available				p--preliminary			

1/ OMB Mid-Session Review of the 1978 Budget, (July 1, 1977).

2/ Congress' Second Concurrent Resolution on the Budget (September 15, 1977).

3/ Includes Federal Financing Bank, Postal Service, U.S. Railway Association, Rural Electrification and Telephone Revolving fund, Housing for the Elderly or Handicapped Fund, and Pension Benefit Guaranty Corporation.

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

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

6/ Quarterly average exceeds fiscal year total by \$1.1 billion for FY 1977 and FY 1978 due to spreading of wage base effect over calendar year.

7/ Estimated by F.R.B. staff.

8/ Includes \$2.5 billion of borrowing from the Federal Reserve on September 30 which was repaid October 4.

## Comments on the Federal Sector Outlook

The fiscal policy outlook continues to incorporate key assumptions about energy policy and social security tax changes, each of which currently are being reviewed by Congressional Conference Committees. Our energy assumptions continue to conform to the House bill which includes a crude oil equalization tax taking effect in early 1978. The added revenues from this tax--\$4.5 billion in calendar year 1978<sup>1/</sup>--are assumed to be fully returned to individuals and corporations in the form of per capita rebates and energy conservation tax credits.

With respect to social security taxes, we are still assuming only the currently scheduled increases (on January 1, 1978) in both the wage base ceiling--from \$16,500 to \$17,700--and the combined payroll tax rate--from 11.7 per cent to 12.1 per cent. These changes are expected to raise around \$7.0 billion in new revenues during calendar year 1978. The staff has assumed that any additional increases in the wage base and tax rate--currently under consideration by a Conference Committee--will be delayed until January 1, 1979, as recommended by the Senate.

Given the above assumptions, the staff projects that unified budget receipts for fiscal year 1978 will be \$397 billion and that

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<sup>1/</sup> This estimate is on a calendar year 1978 liability basis and is the relevant figure for the NIA forecast.

outlays will be \$455.5 billion, both about unchanged from last month. The unified budget deficit for fiscal year 1978 is thus projected by the staff to be \$58-1/2 billion, and the total amount that needs to be financed (unified plus off-budget) is estimated at around \$69 billion. About three-fourths of these borrowing needs are expected to occur in the current quarter and in the first quarter of 1978. After allowing for a rundown in the end of September cash balance of \$7 billion and for anticipated sales of nonmarketable issues totalling \$6 billion,<sup>2/</sup> marketable borrowing by the Treasury during this period is projected to be \$37-\$39 billion, at least \$10 billion more than in the same period last year. Borrowing requirements of this magnitude probably will necessitate the issuance of Treasury bills--either late in this quarter or early in the next--in order to augment the new cash raised through the regular note cycles and mid-quarter refundings.

The high employment budget, after registering a modest surplus in the first half of calendar year 1977, continues to show a swing to deficit in 1977 H:2 (\$19 billion) and 1978 H:1 (\$10 billion). This movement reflects the faster pace of public employment and public works spending and the higher refunds resulting from the 1977 Tax Act. With no new fiscal initiatives and continued growth in receipts, the high employment deficit is projected to decline to \$5 billion in the last half of 1978.

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<sup>2/</sup> Excludes repayment of \$2.5 billion of special borrowing from the Federal Reserve.

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DOMESTIC FINANCIAL DEVELOPMENTS

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Summary. Growth in the major monetary aggregates picked up further in October as the rate of expansion in  $M_1$  surged to an estimated 12.3 per cent annual rate. The rate of increase in the time and savings deposit component of  $M_2$  changed little, while thrift institution deposit flows slowed from their advanced pace of the last few months.

Short-term interest rates have moved downward, on balance, since the last FOMC meeting, as market participants revised their expectations in the light of the recent relative stability in the Federal funds rate. Intermediate- and long-term rates, though, have moved upward by as much as 15 basis points, partly in response to the Treasury's announcement of plans to continue debt lengthening and of larger than generally expected financing requirements through the first quarter of 1978. Most major stock prices indexes, in addition, have retreated around one per cent since the last FOMC meeting.

Aggregate credit flows, meanwhile, continued at close to the very high levels of recent months. Total funds raised by nonfinancial businesses in October may have picked up moderately as short- and intermediate-term borrowings accelerated, while public bond offerings moved somewhat lower. Household borrowing showed no appreciable slackening, with mortgage flows evidently remaining around the advanced third quarter pace and growth in consumer instalment credit probably rebounding from a slower September rate.

In the public sector, security offerings by the Treasury rose somewhat in October, particularly toward the end of the month, and on into November in conjunction with the mid-quarter refunding. The Treasury at the refunding raised \$4.1 billion in cash through auctions of 3- and 10-year notes, and thirty year bonds.<sup>1/</sup> State and local debt issues were somewhat lower in October, as short-term offerings declined and a swollen calendar of long-term issues was trimmed when tax-exempt yields backed up temporarily.

Outlook. Aggregate credit flows over the next few months are expected to remain around their current strong pace. Although Treasury borrowing is likely to pick up moderately, State and local debt offerings should abate somewhat from their recent exceptional volume, as the attractiveness of advance refundings diminishes.

Private credit flows in total are expected to remain relatively robust into early next year. Demands for funds by households, given current economic projections, will probably decline somewhat from the advanced pace in the third quarter. But the gap between business capital outlays and internally generated funds is expected to widen in response to increased capital spending.

Longer-term bond issues of corporations and governments are likely to be absorbed at around current interest rate levels by

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<sup>1/</sup> These figures exclude \$700 million sold to foreign official institutions.

continued, sizable supplies of funds from insurance companies, pension funds, and trust accounts. Demands on banks for credit probably will exceed inflows of funds from demand and small-denomination time and saving deposits, given short-term market rates at least as high as those currently prevailing. Thus, commercial banks can be expected not only to continue to liquidate Treasury securities but also, as in recent weeks, to rely more heavily on managed liabilities such as large denomination CD's.

Deposit inflows to thrift institutions are projected to be slower in the months ahead than during the summer and early fall, when the expansion in deposits had been exceptionally rapid for a period of rising interest rates. Inflows, of course, would tend to slow more if interest rates increase further as a result of stronger credit demands or restraints on bank reserve growth in the face of large demands for money. As thrift institution liquidity declines, increased reliance will be placed on Federal financial support of thrift institutions and the mortgage market. Consequently, Federal agency issues--particularly of those of the FHLBanks and FNMA--are expected to rise significantly. Mortgage lending conditions generally are likely to tighten, and the increase in mortgage debt outstanding may begin to decelerate by early next year.

INTERNATIONAL DEVELOPMENTS

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Summary. On a trade-weighted basis the average value of the dollar has declined about 1-1/4 per cent against leading currencies since the last green book, mainly reflecting upward movements of the Japanese yen, the Swiss franc, and the U.K. pound. The Canadian dollar, however, declined further against the U.S. dollar and other currencies. Continued weakness of the U.S. dollar reflects heightened awareness of the size of the prospective U.S. deficit on current account and the unsettling effects of attitudes about the dollar and other currencies expressed by various official sources.

On October 31 the pound sterling was allowed to float upward

. Since floating, the pound has appreciated a net 2-1/2 per cent against the dollar,

. The Japanese yen appreciated a further 4 per cent during the past four weeks, following a 4 per cent appreciation in the preceding two weeks,

The U.S. trade balance in September improved somewhat to a \$24 billion deficit, at an annual rate, resulting in a \$30 billion deficit rate for the third quarter. A sharp rise in exports in September to a considerable extent reflected temporary factors such as anticipation of the longshoremen's strike on the East and Gulf Coasts which began

October 1, and a rebound of coal and other exports from an unusually low August rate. Imports in September were up a little, mainly because of large petroleum imports as stocks here were raised further. The current account deficit in the third quarter is estimated at about an \$18 billion annual rate -- about the same as in the second quarter.

Reported capital flows (private and official) in the third quarter were a net inflow of about \$11.7 billion, more than double the net inflow in the second quarter. However, the bank-reported inflow in September seems to have been exaggerated by end-of-month discrepancies, so that the actual net inflow was probably closer to \$10 billion. This smaller figure about equals the estimated amount needed to finance the current account deficit and other capital flows not yet reported, so the large net receipts in the errors and omissions that have characterized the U.S. international accounts since the end of 1974 may have disappeared, at least temporarily.

The bulk of the reported capital inflow in the third quarter, as in the first half of the year, was accounted for by large increases in U.S. assets held by foreign official accounts --

. U.S. banking offices  
also registered a net inflow in the third quarter, the recorded net

inflow in September was over \$4 billion but, as noted above, there is evidence that about half of this was associated with month-end discrepancies in accounting.

Net inflows of capital to the U.S. through banks since early in the year are consistent with the relative rise in interest rates on dollar-denominated assets.

Activity in international capital markets slowed a bit in the third quarter. Total borrowing of \$13.3 billion was recorded in the Euro-credit, Euro-bond, and foreign bond markets -- about 15 per cent under the rate in the second quarter and under the quarterly average of 1976. Borrowing in the Euro-credit market by non-oil developing countries appears to be down considerably from last year's rate. As usual, interest rates in these markets have tended to rise in sympathy with U.S. rates, but spreads in the Euro-credit market have been reduced by intense competition.

With economic activity still lagging in industrial countries, monetary policy abroad has generally been aimed at accommodating any strengthening of demand, while fiscal policy, at least in the major economies, has been gradually and cautiously shifted to stimulate growth. Such fiscal policy initiatives have recently been taken in Canada, France, Germany, Japan, and the United Kingdom. Smaller countries have combined

attempts to raise employment with efforts to minimize budget deficits, make the tax system more progressive, and reduce imports.

Outlook. Though economic policies abroad are increasingly aimed at raising growth rates, the measures taken so far are not expected to achieve more than a moderate year-over-year gain in foreign economic activity from the unexpectedly depressed level of this year. In the absence of significant change in the outlook for economic activity in the U.S. and abroad the projection of the U.S. current-account deficit for 1978 has been changed only marginally -- to about \$24 billion from last month's estimate of about \$26 billion. For 1977 the deficit has been scaled down a little to \$18 billion. For both years projected imports were reduced somewhat.

Financing of the current-account deficit is likely to shift increasingly to private flows through banking markets if official market intervention is now reduced because floating has become more general. Depending on relative conditions in credit markets, and also on the host of other factors that color expectations about exchange rates, such inflows could occur without much further change in the average exchange value of the dollar. However, some further small depreciation is expected by the staff over the next year, with continued gains by the German mark, Japanese yen, and Swiss franc more than matching declines of some other currencies against the dollar.

	1976	1977 <sup>P</sup>	1978 <sup>P</sup>	1976		1977				1978 <sup>P</sup>			
				III	IV	I	II	III <sup>P</sup>	IV <sup>P</sup>	I	II	III	IV
1. GNP NET EXPORTS - Intl Acct. data	7.7	-8.6	-11.8	7.8	2.9	-7.4	-8.7	-8.4	-9.9	-8.3	-12.6	-13.2	-13.4
2. (GNP net exports - GNP acct. data) <u>1/</u>	(7.8)	(-10.7)	(-15.1)	(7.9)	(3.0)	(-8.2)	(-9.7)	(-11.6)*	(-13.1)	(-11.5)	(-15.7)	(-16.4)	(-16.6)
3. a) Merchandise Trade Balance	-9.3	-30.5	-36.6	-11.2	-14.4	-28.4	-31.4	-30.3*	-31.8	-31.9	-36.9	-38.6	-39.1
4. Exports (excl. military)	114.7	120.8	136.3	118.4	118.8	117.8	122.0	122.9*	120.5	129.6	133.5	138.6	143.4
5. Agricultural	23.4	24.2	22.7	25.0	23.5	24.5	26.8	23.9*	21.6	22.1	22.3	23.0	23.4
6. Nonagricultural	91.3	96.6	113.6	93.5	95.3	93.4	95.2	99.1*	98.9	107.5	111.2	115.6	120.0
7. Imports	124.0	151.3	172.9	129.6	133.2	146.2	153.4	153.2*	152.3	161.5	170.4	177.2	182.5
8. Petroleum and petrol. products	34.6	45.9	49.0	37.6	37.4	44.1	47.7	45.8*	45.8	44.9	49.4	51.0	50.7
9. Nonpetroleum	89.4	105.4	123.9	92.0	95.9	102.1	105.7	107.4*	106.5	116.6	121.0	126.2	131.8
10. b) Military transactions, net <u>2/</u>	--	1.6	1.6	.6	.5	1.7	1.5	1.6	1.5	1.6	1.6	1.6	1.6
11. c) Investment income, net <u>3/</u>	14.3	18.5	21.2	15.3	14.4	17.9	18.7	18.5	18.7	20.2	20.9	21.8	21.9
12. d) Other services, net <u>4/</u>	2.7	1.8	2.0	3.1	2.4	1.4	2.5	1.8	1.7	1.8	1.8	2.0	2.2
13. U.S. CURRENT ACCOUNT BALANCE <u>2/</u>	-1.0	-18.2	-24.3	-1.6	-6.0	-16.5	-17.8	-18.1	-20.3	-20.3	-25.0	-25.8	-26.0
14. a) GNP net exports (line 1.)	7.7	-8.6	-11.8	7.8	2.9	-7.4	-8.7	-8.4	-9.9	-8.3	-12.6	-13.2	-13.4
15. b) U.S. Govt & private transfers <u>5/</u>	-8.7	-9.6	-12.5	-9.3	-8.9	-9.0	-9.1	-9.7	-10.4	-12.0	-12.4	-12.6	-12.6
<u>Constant (1972) dollars</u>													
16. Merchandise exports (excl. military)	56.7	67.3	72.6	68.4	67.3	66.1	67.4	68.4	67.0	71.0	71.7	73.1	74.4
17. (% change, annual rates)	(3.4)	(0.8)	(7.8)	(13.0)	(-6.6)	(-7.4)	(8.2)	(5.7)	(-8.2)	(25.8)	(4.1)	(8.2)	(7.4)
18. Merchandise imports	62.8	70.9	76.0	64.9	66.1	70.2	72.0	71.1	70.1	72.9	75.4	77.3	78.5
19. (% change, annual rates)	(22.5)	(13.0)	(7.2)	(29.1)	(7.4)	(27.2)	(10.4)	(-5.3)	(-5.7)	(17.0)	(14.3)	(10.4)	(6.6)
<u>Foreign Outlook - Major Industrial Countries <u>6/</u></u>													
20. Real GNP, % change, annual rates	5.2	3.2	4.5	1.6	2.9	5.3	-.8	2.9	5.3	4.9	5.3	5.3	4.9
21. Wholesale Prices, % change, A.R. <u>7/</u>	9.5	8.8	6.0	11.7	8.7	10.4	7.4	3.9	5.7	6.1	6.1	6.6	7.0

1/ Lags Intl. Acct. data (line 1) in the inclusion of revisions and new data.

2/ Excludes grants to Israel under military assistance acts and exports financed by those grants.

3/ Excludes U.S. Govt. interest payments to foreigners, which are included in line 15.

4/ Includes travel, transportation, fees and royalties, and miscellaneous other service transactions.

5/ Includes U.S. Govt grants, U.S. Govt interest payments to foreigners, and remittances and pensions.

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

7/ Data are largely manufactured goods prices.

P/ Projected.

e/ Estimated.

\* Published data.