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CONFIDENTIAL (FR)

January 3, 1980

SUMMARY AND OUTLOOK

By the Staff
Board of Governors
of the Federal Reserve System

SUMMARY AND OUTLOOK

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary

Incoming information suggests that the economy expanded somewhat further in the fourth quarter, bolstered largely by consumer spending outside the auto sector. At the same time, increasing weakness became evident in housing and, to a lesser extent, in business investment. The inflation rate continued very high.

The demand for labor remained quite strong through November. According to the survey of establishments, nonfarm employment rose substantially in both October and November with hiring concentrated in the trade and services sector. Total payroll employment increased 220,000 in November, while manufacturing employment was unchanged, following declines in the preceding three months. The unemployment rate edged lower to 5.8 percent, within the 5-3/4 to 6 percent range that has prevailed for more than a year.

Industrial production declined 1/2 percent in November, reflecting a sharp curtailment in the output of motor vehicles and smaller cutbacks of home goods and construction supplies. Total industrial production was at about the same level in November as at the end of 1978; since then the capacity utilization rate in manufacturing declined about 2-1/2 percentage points to 84-1/2 percent.

Unit auto sales of domestic models slowed a bit further in November to an annual rate of 6.9 million units, the lowest monthly rate since 1975. The rate for foreign models was a bit stronger at 2.6 million units. Total auto sales thus were about the same as in October despite reintroduction of some rebates for large 1979 models.

Nonauto retail sales are reported to have risen 1.7 percent in nominal terms in November. Fragmentary reports for December show a mixed picture. These sales had increased swiftly in late summer, but had changed little during October. In November sales at general merchandise and apparel stores were especially strong.

More restricted availability of credit and rising mortgage interest rates appear to have slowed housing activity in the fourth quarter. Total housing starts, which had been on a fairly high plateau for much of 1979, were down 14 percent in November, following an 8 percent drop in October. Permits also declined substantially, and so did home sales during November according to industry sources. Some measures of house prices also have moved down in recent months.

Growth in business equipment spending has slowed recently. In November the value of shipments of nondefense capital goods declined, partly as the result of strikes, following two months of no change. In both October and November sales of heavy-weight trucks were below their third-quarter pace. Expenditures for nonresidential construction moved higher in October, but edged down in November.

Recent commitments for capital spending suggest some further slowing of outlays in the near term. New orders for nondefense capital goods in constant dollars, while little changed in November, have been on a general downtrend since early 1979, as have been contracts for business construction. In contrast to these developments, the Commerce Department October/November survey suggests that plant and equipment spending will continue to grow strongly through the first half of 1980. These results should be viewed with caution, however, because the track

record of the November survey has been uneven and because the 1980 investment outlook previously reported by two private surveys was considerably weaker.

Inventory investment also has tended to slow since early summer. The pace has been erratic, however: after an unusually small increase in the book value of stocks during September, inventory building increased to an annual rate of \$50 billion in October. Much of the pick-up was at the retail level, where automobile dealers experienced an increase in stocks, following two months of considerable reductions. Total retail stocks increased at a \$17 billion annual rate in October, offsetting a decline in September of similar magnitude. Manufacturing inventories rose further, but at a somewhat slower rate than their sales.

Recent price measures indicated that inflation continued through November at about the same rapid pace that has prevailed since the beginning of 1979. While inflation rates for energy items recently have abated markedly, the higher level of these prices is still being diffused throughout the economy. Moreover, oil companies have recently announced price increases for petroleum products in response to further hikes in world oil prices. In addition, the costs of shelter--for both renters and homeowners--have risen more sharply in recent months. Increases in homeownership costs, as measured by the CPI, were particularly large in October and November, and were a major factor keeping the rise in the CPI at 1 percent in these months.

Wage increases continued to run considerably below the inflation rates, whether measured by the CPI or other consumption price indexes. While wage rates advanced a bit faster in November, the annual rate of

increase for the first 11 months of 1979 was about 8 percent compared with 8-1/2 percent during 1978.

Outlook

Real gross national product is now estimated to have risen at an annual rate of about 1-1/2 percent in the fourth quarter, a substantially stronger performance than was anticipated at the time of the November FOMC meeting. Although auto sales appear to have weakened as expected, there was surprising strength in the other components of consumption, and the quarterly saving rate is estimated to have dipped below 4 percent for only the fourth time since World War II. Outlays for residential and business fixed investment appear to have declined in real terms during the fourth quarter in line with earlier projections.

With this Greenbook, the staff projections have been extended through 1981. The fiscal policy assumptions have been modified to include a tax on windfall oil profits along the lines indicated by the congressional conference committee; this bill is estimated to yield receipts of \$5 billion in FY 1980 and \$13 billion in FY 1981. No other new discretionary tax actions are assumed in this projection. Projected outlays for FY 1980 have been raised somewhat to \$552 billion. These additional outlays offset most of the receipts from the windfall tax; the projected unified budget deficit for FY 1980 has now been reduced from \$42 billion to \$38 billion. In FY 1981, the deficit is projected to narrow to around \$30 billion, as outlays increase about 11 percent but receipts are bolstered by an \$18 billion hike in the social security tax rate and wage base.

On the monetary side, M-1 is still assumed to increase 6 percent during 1980 and this rate of growth has been extended through 1981. Demands for credit are likely to ease as the economy weakens, and in this setting market interest rates are expected to decline moderately through mid-1980. Around the beginning of 1981, as economic recovery begins, interest rates are expected to start edging up again.

The staff has changed its assumptions with regard to oil prices in line with recent and prospective developments. The average price per barrel of imported crude is now estimated to have been \$23.50 in the fourth quarter of 1979; it is assumed to rise 32 percent during 1980 to about \$31 per barrel by the fourth quarter, nearly \$3 more than was assumed in the November Greenbook. A further 13 percent price increase is assumed over the four quarters of 1981.

Starting from a higher year-end level, real GNP is now projected to fall 2-1/4 percent during 1980, nearly 1 percentage point more than shown in November. The recent strength in consumer activity is not expected to persist into 1980. In view of current and prospective declines in business and housing outlays, real personal income is also likely to decline. In addition, tighter credit and the recent fall in personal saving will further restrain household spending. The staff now expects a somewhat larger retrenchment in real consumer spending during 1980.

The contour of the staff projection outside the consumption area remains generally similar. The tighter financial conditions of the past few months are likely to have their greatest impact on housing construction in the first half of 1980. Business fixed investment will be damped

over a longer period; in real terms it is projected to decline by about 3-1/2 percent over the four quarters of 1980, partly in response to declining final sales. Firms also are expected to move quickly to trim inventories in order to prevent buildups of stocks as sales decline.

The reduction in labor demand associated with these developments is anticipated to raise the unemployment rate to 8-1/4 percent by the end of 1980. Hourly compensation, however, is unlikely to slow in 1980 from the surprisingly moderate 1979 increase; the effects of a weaker labor market are expected to be offset by the lagged response of wages to the 1979 inflation surge. Inflation, as measured by the fixed-weighted price index for gross domestic business product, is expected to rise to nearly 11 percent, at an annual rate, in the first half of 1980, because of large increases in energy prices and some food price pressures as well. As the influence of these factors abates in the second half, inflation is projected to slow to an annual rate of about 9-1/2 percent.

The staff is projecting only a sluggish recovery for 1981. The outlook is influenced substantially by the assumption of an increasingly restrictive fiscal stance coupled with continued moderate growth of the monetary aggregates. Housing activity, reflecting underlying strength in demand, is expected to be the only sector with vigorous expansion starting from a trough in mid-1980. Without additional major new sources of income growth, we expect consumption and business investment outlays to be sluggish. Consequently, real GNP is projected to be up only about 1-1/4 percent over the four quarters of 1981. This rate of GNP growth is likely to generate little expansion of employment and the unemployment

rate is expected to rise further. The overall inflation rate is projected to slow to about 8-1/4 percent by the latter half of the year.

Detailed data for these projections are shown in the tables that follow.

STAFF GNP PROJECTIONS

Percent changes, annual rate										
	Nominal GNP		Real GNP		Gross domestic business product fixed-weighted price index				Unemployment rate (percent)	
					Total		Excluding food and energy			
	11/14/79	1/3/80	11/14/79	1/3/80	11/14/79	1/3/80	11/14/79	1/3/80	11/14/79	1/3/80
1978 ^{1/}	12.0	12.0	4.4	4.4	7.6	7.6	7.2	7.2	6.0	6.0
1979	11.0	11.4	1.9	2.3	9.7	9.7	8.1	8.2	5.9	5.8
1980	7.5	7.8	-1.7	-1.3	9.9	10.2	7.7	8.1	7.9	7.4
1981		9.3		.2		9.1		8.1		8.6
1979-Q1 ^{1/}	10.6	10.6	1.1	1.1	10.0	10.0	7.7	7.7	5.7	5.7
1979-Q2 ^{1/}	6.7	6.7	-2.3	-2.3	10.1	10.1	7.9	7.9	5.7	5.7
1979-Q3 ^{1/}	11.0	12.0	2.4	3.1	10.0	10.4	7.0	7.6	5.8	5.8
1979-Q4	7.0	10.7	-2.7	1.5	10.0	9.6	7.7	8.1	6.3	5.9
1980-Q1	5.7	4.7	-3.8	-3.7	10.2	10.5	7.7	7.8	7.1	6.6
1980-Q2	6.7	6.0	-2.5	-3.4	10.1	11.0	8.1	8.6	7.9	7.2
1980-Q3	8.8	8.0	.0	-1.6	9.0	9.5	7.9	8.4	8.2	7.8
1980-Q4	10.1	9.4	.8	-.3	8.9	9.3	7.7	8.3	8.4	8.1
1981-Q1		9.5		.4		9.3		8.3		8.3
1981-Q2		10.0		1.2		8.9		7.9		8.5
1981-Q3		10.0		1.6		8.3		7.3		8.7
1981-Q4		10.8		2.0		8.3		7.3		8.8
Half-year changes: ^{2/}										
1979-Q4	9.0	11.4	-.2	2.3	10.0	9.9	7.3	7.9	.6	.2
1980-Q2	6.2	5.4	-3.1	-3.5	10.1	10.7	7.9	8.2	1.6	1.3
1980-Q4	9.4	8.7	.4	-1.0	8.9	9.4	7.8	8.4	.5	.9
1981-Q2		9.8		.8		9.1		8.1		.4
1981-Q4		10.4		1.8		8.2		7.3		.3
Yearly changes: ^{3/}										
1978-Q4 ^{1/}	13.4	13.4	4.8	4.8	8.6	8.6	8.1	8.1	-.8	-.8
1979-Q4	8.3	10.0	-.4	.9	10.0	10.0	7.6	7.8	.5	.1
1980-Q4	7.8	7.0	-1.4	-2.3	9.5	10.0	7.8	8.3	2.1	2.2
1981-Q4		10.1		1.3		8.7		7.7		.7

^{1/} Actual.^{2/} Percent change from two quarters earlier.^{3/} Percent change from four quarters earlier.

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

	1980				1981			
	Q1	Q2	Q3	Projected Q4	Q1	Q2	Q3	Q4
Gross national product	2488.0	2524.8	2574.0	2632.3	2692.9	2758.0	2824.5	2898.1
Final purchases	2486.5	2529.3	2577.5	2634.3	2689.9	2752.0	2815.5	2888.1
Private	1974.7	2006.5	2043.7	2085.9	2129.9	2179.7	2230.9	2287.4
Excluding net exports	1980.2	2006.9	2039.2	2081.1	2126.8	2177.5	2229.5	2286.4
Personal consumption expenditures	1604.5	1632.1	1657.1	1688.1	1721.4	1757.2	1794.4	1836.1
Goods	845.3	852.1	857.1	868.1	880.4	894.7	909.9	928.6
Services	759.2	780.0	800.0	820.0	841.0	862.5	884.5	907.5
Gross private domestic investment	377.2	370.3	378.6	391.0	408.4	426.3	444.1	460.3
Residential construction	110.0	107.0	111.0	117.5	125.0	134.5	143.5	152.5
Business fixed investment	265.7	267.8	271.1	275.5	280.4	285.8	291.6	297.8
Change in business inventories	1.5	-4.5	-3.5	-2.0	3.0	6.0	9.0	10.0
Nonfarm	1.5	-4.5	-3.5	-2.0	3.0	6.0	9.0	10.0
Net exports of goods and services ^{1/}	-5.5	-4.4	4.5	4.9	3.1	2.2	1.4	1.0
Exports	292.8	297.1	301.0	305.7	311.5	318.3	326.7	336.5
Imports	298.3	297.5	296.4	300.9	308.4	316.1	325.3	335.5
Gov't. purchases of goods and services	511.8	522.8	533.8	548.4	560.0	572.3	584.6	600.7
Federal ^{2/}	181.4	185.4	189.5	197.0	201.5	206.0	210.3	218.5
State and local	330.4	337.4	344.3	351.4	358.5	366.3	374.3	382.2
Gross national product in constant (1972) dollars	1425.4	1413.2	1407.6	1406.4	1407.7	1411.8	1417.5	1424.6
Personal income	2046.0	2085.0	2132.7	2182.2	2223.0	2270.3	2330.3	2384.7
Wage and salary disbursements	1287.4	1303.1	1317.1	1345.5	1374.4	1401.3	1430.6	1464.3
Disposable personal income	1720.6	1752.3	1792.2	1830.8	1858.2	1894.8	1942.6	1982.9
Saving rate (percent)	4.2	4.3	4.9	5.1	4.7	4.5	4.9	4.7
Corporate profits with I.V.A. and C.C. Adj.	161.3	155.1	163.6	166.0	159.1	167.5	174.3	182.5
Corporate profits before tax	222.9	212.9	219.8	221.7	214.5	222.6	229.1	235.0
Federal government surplus or deficit (-) (N.I.A. basis)	-23.3	-30.5	-41.6	-42.2	-21.9	-14.3	-15.7	-8.8
High employment surplus or deficit (-)	33.3	42.8	44.2	52.9	84.2	98.7	102.6	113.5
State and local government surplus or deficit (-) (N.I.A. basis)	20.1	17.9	15.7	14.6	13.2	11.4	10.0	9.6
Excluding social insurance funds	-8.2	-11.0	-13.7	-15.4	-17.4	-19.8	-21.8	-22.8
Civilian labor force (millions)	104.2	104.6	104.9	105.2	105.5	105.8	106.1	106.4
Unemployment rate (percent)	6.6	7.2	7.8	8.1	8.3	8.5	8.7	8.8
Nonfarm payroll employment (millions)	89.8	89.4	89.0	88.8	88.7	88.8	88.9	89.0
Manufacturing	20.5	20.2	19.9	19.7	19.6	19.5	19.4	19.4
Industrial production (1967=100)	150.8	149.3	148.8	148.7	149.0	149.4	150.1	150.8
Capacity utilization: all mfg. (percent)	83.1	81.6	80.5	79.9	79.5	79.2	79.0	78.9
Materials (percent)	83.8	81.4	79.9	79.1	78.6	78.2	77.9	77.8
Housing starts, private (million units, A.R.)	1.30	1.40	1.55	1.65	1.75	1.80	1.90	2.00
New autos sales, (millions, A.R.)	9.20	9.10	9.20	9.20	9.30	9.40	9.60	9.90
Domestic models	7.00	7.00	7.10	7.05	7.10	7.15	7.30	7.50
Foreign models	2.20	2.10	2.10	2.15	2.20	2.25	2.30	2.40

^{1/} Balance of payments data and details 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.

January 3, 1980

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CLASS II FOMCPERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	1980				Projected		1981	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) dollars</u>								
Gross national product	-3.7	-3.4	-1.6	-.3	.4	1.2	1.6	2.0
Final purchases	-3.2	-2.6	-1.7	-.5	-.3	.7	1.2	1.9
Private	-4.2	-3.3	-2.4	-.9	-.6	.5	1.1	2.0
Excluding net exports	-5.0	-4.3	-2.7	-.8	-.3	.7	1.3	2.1
Personal consumption expenditures	-3.7	-3.3	-3.0	-1.4	-1.1	-.3	.4	1.3
Goods	-7.7	-7.3	-6.4	-3.3	-3.0	-1.8	-1.2	.4
Services	1.1	1.3	.8	.8	.9	1.3	2.0	2.2
Gross private domestic investment	-14.2	-14.2	-.3	3.6	8.6	8.9	8.3	6.3
Residential structures	-27.2	-19.0	4.8	13.6	17.0	23.0	19.4	17.6
Business fixed investment	-4.2	-5.1	-3.3	-1.7	-1.3	-.1	.3	1.1
Gov't. purchases of goods and services	1.2	.8	1.0	1.1	.9	1.6	1.4	1.3
Federal	3.1	2.2	2.8	2.6	2.4	3.2	2.3	2.4
State and local	.2	.0	.0	.2	.0	.6	.9	.7
Disposable personal income	-1.3	-3.4	.5	-.5	-2.9	-.8	2.0	.3
<u>Current dollars</u>								
Gross national product	4.7	6.0	8.0	9.4	9.5	10.0	10.0	10.8
Final purchases	5.4	7.1	7.9	9.1	8.7	9.6	9.6	10.7
Private	4.3	6.6	7.6	8.5	8.7	9.7	9.7	10.5
Excluding net exports	5.1	5.5	6.6	8.5	9.1	9.9	9.9	10.6
Personal consumption expenditures	7.2	7.1	6.3	7.7	8.1	8.6	8.7	9.6
Goods	2.6	3.3	2.4	5.2	5.8	6.7	7.0	8.5
Services	12.6	11.4	10.7	10.4	10.6	10.6	10.6	10.8
Gross private domestic investment	-7.3	-7.1	9.3	13.8	19.0	18.7	17.8	15.4
Residential structures	-19.1	-10.5	15.8	25.6	28.1	34.0	29.6	27.5
Business fixed investment	4.3	3.2	5.0	6.7	7.3	7.9	8.4	8.8
Gov't. purchases of goods and services	9.7	8.9	8.7	11.4	8.7	9.1	8.9	11.5
Federal	10.1	9.1	9.1	16.8	9.5	9.2	8.6	16.5
State and local	9.5	8.7	8.4	8.5	8.3	9.0	9.0	8.7
Disposable personal income	9.7	7.6	9.4	8.9	6.1	8.1	10.5	8.6
Personal income	8.8	7.8	9.5	9.6	7.7	8.8	11.0	9.7
Wage and salary disbursements	5.8	5.0	4.4	8.9	8.9	8.1	8.6	9.9
Corporate profits with IVA & C.C. Adj.	-42.1	-14.5	23.8	6.0	-15.6	22.9	17.3	20.2
Corporate profits before tax	-36.8	-16.8	13.6	3.5	-12.4	16.0	12.3	10.6
Nonfarm payroll employment	-1.3	-2.0	-1.9	-.9	-.1	.4	.3	.5
Manufacturing	-7.2	-6.2	-4.5	-4.2	-2.4	-2.0	-.9	-.6
Nonfarm business sector	-1.6	-.5	1.0	.8	.7	1.0	1.1	1.4
Output per hour	10.3	9.0	9.3	9.3	12.0	8.3	9.0	9.0
Compensation per hour	12.1	9.5	8.2	8.4	11.2	7.2	7.8	7.5
Unit labor costs								
GNP implicit deflator ^{1/}	8.7	9.7	9.8	9.7	9.1	8.8	8.3	8.6
Gross domestic business product								
fixed-weighted price index ^{2/}	10.5	11.0	9.5	9.3	9.3	8.9	8.3	8.3
Excluding food and energy	7.8	8.6	8.4	8.3	8.3	7.9	7.3	7.3
Consumer price index (all urban)	15.6	11.5	8.3	9.2	9.5	9.4	9.0	9.0
Industrial production	-2.2	-3.8	-1.4	-.4	.9	1.2	1.9	1.8

^{1/} Excluding Federal pay increases, the rates of change are: 1980-Q1, 3.7 percent; 1980-Q4, 9.2 percent; 1981-Q1, 9.1 percent; 1981-Q4, 8.1 percent.

^{2/} Uses expenditures in 1972 as weights.

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

	1978				1979			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Projected Q4
Gross national product	2011.3	2104.2	2159.6	2235.2	2292.1	2329.3	2396.5	2459.5
Final purchases	1988.5	2078.4	2139.5	2214.5	2272.9	2296.4	2381.9	2454.0
Private	1569.1	1650.1	1698.6	1760.7	1812.8	1829.8	1904.1	1953.9
Excluding net exports	1591.3	1657.7	1705.4	1765.2	1808.8	1837.9	1906.4	1955.7
Personal consumption expenditures	1287.2	1331.2	1369.3	1415.4	1454.2	1475.9	1528.6	1576.8
Goods	691.2	722.1	740.2	770.2	784.9	789.9	818.1	839.8
Services	596.0	609.1	629.1	645.1	669.3	686.0	710.6	737.0
Gross private domestic investment	327.0	352.3	356.2	370.5	373.8	395.4	392.3	384.4
Residential construction	100.5	107.7	110.2	113.7	111.2	112.9	116.0	116.0
Business fixed investment	203.7	218.8	225.9	236.1	243.4	249.1	261.8	262.9
Change in business inventories	22.8	25.8	20.0	20.6	19.1	33.4	14.5	5.5
Nonfarm	22.0	25.3	18.5	19.3	18.8	32.6	12.6	2.0
Net exports of goods and services ^{1/}	-22.2	-7.6	-6.8	-4.5	4.0	-8.1	-2.3	-1.8
Exports	184.4	205.7	213.8	224.9	238.5	243.7	267.3	285.6
Imports	206.6	213.3	220.6	229.4	234.4	251.9	269.5	287.4
Gov't. purchases of goods and services	419.4	428.3	440.9	453.8	460.1	466.6	477.8	500.1
Federal ^{2/}	150.9	148.2	152.3	159.0	163.6	161.7	162.9	177.1
State and local	268.5	280.1	288.6	294.8	296.5	304.9	314.9	323.0
Gross national product in constant (1972) dollar	1367.8	1395.2	1407.3	1426.6	1430.6	1422.3	1433.3	1438.8
Personal income	1634.8	1689.3	1742.5	1803.1	1852.6	1892.5	1946.6	2003.5
Wage and salary disbursements	1052.0	1090.0	1116.8	1154.3	1189.3	1212.4	1238.1	1269.4
Disposable personal income	1395.0	1437.3	1476.5	1524.8	1572.2	1601.7	1640.0	1681.2
Saving rate (percent)	5.3	5.0	4.8	4.7	5.0	5.4	4.3	3.7
Corporate profits with I.V.A. and G.C. Adj.	141.2	169.4	175.2	184.8	178.9	176.6	180.8	184.9
Corporate profits before tax	177.5	207.2	212.0	227.4	233.3	227.9	242.3	250.0
Federal government surplus or deficit (-) (N.I.A. basis)	-49.4	-24.6	-20.4	-16.3	-11.7	-7.0	-11.3	-10.4
High employment surplus or deficit (-)	-20.4	-4.7	-1.0	-0.8	7.9	20.2	18.7	26.7
State and local government surplus or deficit (-) (N.I.A. basis)	30.2	29.6	22.7	27.1	27.6	19.7	25.3	23.6
Excluding social insurance funds	7.9	6.5	-0.9	3.3	2.6	-6.3	-1.8	-4.1
Civilian labor force (millions)	99.3	100.1	100.8	101.5	102.5	102.3	103.2	103.7
Unemployment rate (percent)	6.2	6.0	6.0	5.8	5.7	5.7	5.8	5.9
Nonfarm payroll employment (millions)	84.8	86.3	86.9	87.8	88.7	89.4	89.8	90.1
Manufacturing	20.2	20.4	20.5	20.8	21.0	21.1	21.0	20.9
Industrial production (1967=100)	140.8	145.1	147.9	150.7	152.2	151.9	152.3	151.6
Capacity utilization: all mfg. (percent)	82.0	83.9	85.2	86.4	86.7	85.9	85.4	84.3
Materials (percent)	82.6	85.0	86.4	88.2	88.0	87.3	87.1	85.9
Housing starts, private (million units, A.R.)	1.81	2.10	2.04	2.08	1.62	1.83	1.83	1.56
New autos sales, (millions, A.R.)	10.80	12.12	11.16	11.07	11.55	10.66	10.77	9.40
Domestic models	8.80	10.01	9.19	9.06	9.13	8.00	8.49	7.20
Foreign models	2.00	2.11	1.98	2.00	2.42	2.66	2.28	2.20

^{1/} Balance of payments data and details 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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CONFIDENTIAL - FR
CLASS II FOMCPERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	1978				1979			Projected Q4
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	
<u>Constant (1972) dollars</u>								
Gross national product	1.9	8.3	3.5	5.6	1.1	-2.3	3.1	1.5
Final purchases	.4	8.7	4.6	5.7	1.1	-3.9	6.4	2.8
Private	1.8	10.7	4.4	6.7	1.8	-4.1	7.8	2.2
Excluding net exports	1.0	7.9	4.1	6.9	.4	-2.9	5.3	1.1
Personal consumption expenditures	.8	5.6	4.8	6.8	.6	-2.9	4.9	2.9
Goods	-4.7	9.2	4.2	9.9	-4.4	-7.3	6.0	1.2
Services	7.9	1.4	5.5	3.2	7.1	2.5	3.6	4.8
Gross private domestic investment	12.3	15.7	-5.0	6.6	-5	8.5	-12.8	-14.2
Residential structures	-4.7	11.0	-4.9	-1.1	-14.3	-7.2	-1.5	-9.1
Business fixed investment	4.6	23.2	3.9	11.3	4.8	-8	10.7	-6.1
Gov't. purchases of goods and services	-1.2	.9	5.0	1.8	-1.8	-3.3	1.0	5.4
Federal	-7.4	-12.3	8.2	3.2	7.2	-11.3	-2.6	14.3
State and local	2.7	9.3	3.3	1.0	-6.6	1.6	3.1	.7
Disposable personal income	2.0	4.0	4.2	6.4	2.1	-1.4	.2	.4
<u>Current dollars</u>								
Gross national product	8.4	19.8	10.9	14.8	10.6	6.7	11.9	10.9
Final purchases	7.5	19.3	12.3	14.8	11.0	4.2	15.8	12.7
Private	7.7	22.3	12.3	15.4	12.4	3.8	17.3	10.9
Excluding net exports	8.8	17.8	12.0	14.8	10.3	6.6	15.8	10.7
Personal consumption expenditures	9.0	14.4	11.9	14.2	11.4	6.1	15.0	13.2
Goods	3.3	19.1	10.4	17.2	7.9	2.6	13.1	11.1
Services	16.1	9.1	13.8	10.6	15.8	10.4	15.1	15.7
Gross private domestic investment	13.3	34.8	4.5	17.1	3.6	25.2	-3.0	-7.8
Residential structures	2.4	32.0	9.5	13.5	-8.5	6.1	11.7	.0
Business fixed investment	10.6	33.3	13.7	19.3	12.9	9.6	22.0	1.8
Gov't. purchases of goods and services	6.5	8.8	12.3	12.2	5.6	5.8	10.0	20.0
Federal	-9	-7.0	11.7	18.7	12.1	-4.6	3.1	39.7
State and local	11.1	18.5	12.6	8.9	2.3	11.8	13.8	10.7
Disposable personal income	10.3	12.7	11.4	13.8	13.0	7.7	9.9	10.4
Personal income	10.0	14.0	13.2	14.7	11.4	8.9	11.9	12.2
Wage and salary disbursements	11.7	15.3	10.2	14.1	12.7	8.0	8.8	10.5
Corporate profits with IVA & C.C. Adj.	-27.5	107.2	14.4	23.8	-12.2	-5.0	9.9	9.4
Corporate profits before tax	-11.5	85.7	9.6	32.4	10.8	-8.9	27.8	13.6
Nonfarm payroll employment	4.6	7.1	2.8	4.4	4.3	2.9	1.8	1.7
Manufacturing	5.8	3.8	1.3	5.5	5.0	.8	-1.3	-2.5
Nonfarm business sector								
Output per hour	-9	1.9	2.7	.8	-3.2	-4.1	-7	1.0
Compensation per hour	11.4	7.5	8.8	8.8	10.4	7.9	8.5	8.4
Unit labor costs	12.4	5.4	6.0	8.0	14.0	12.5	9.3	7.3
GNP implicit deflator ^{1/}	6.3	10.6	7.2	8.7	9.3	9.3	8.5	9.3
Gross domestic business product								
fixed-weighted price index ^{2/}	6.6	10.5	8.8	8.7	10.0	10.1	10.4	9.6
Excluding food and energy	5.5	9.4	8.9	8.7	7.7	7.9	7.6	8.1
Consumer price index (all urban)	7.8	10.2	8.8	9.1	11.1	13.6	12.9	13.0
Industrial production	1.4	12.8	7.9	7.8	4.0	-8	1.1	-1.8

^{1/} Excluding Federal pay increases, rates of change were: 1978-Q1, 6.3 percent; 1978-Q4, 8.1 percent; 1979-Q1, 9.3 percent; 1979-Q4, 8.6 percent.

^{2/} Uses expenditures in 1972 as weights.

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CONFIDENTIAL - FR
CLASS II FOMCGROSS NATIONAL PRODUCT AND RELATED ITEMS
(Expenditures and income figures are billions of current dollars.)

	1974	1975	1976	1977	1978	Projected		
						1979	1980	1981
Gross national product	1412.9	1528.8	1702.2	1899.5	2127.6	2369.5	2554.8	2793.4
Final purchases	1404.0	1539.6	1692.1	1877.6	2105.2	2351.3	2556.9	2786.4
Private	1101.3	1201.2	1330.8	1481.4	1669.6	1875.2	2027.7	2207.0
Excluding net exports	1095.3	1180.8	1322.8	1491.3	1679.9	1877.2	2026.8	2205.0
Personal consumption expenditures	889.6	979.1	1089.9	1210.0	1350.8	1508.9	1645.4	1777.3
Goods	498.3	541.5	601.3	660.1	730.9	808.2	855.6	903.4
Services	391.3	437.5	488.5	549.8	619.8	700.7	789.8	873.9
Gross private domestic investment	214.6	190.9	243.0	303.3	351.5	386.5	379.3	434.8
Residential construction	55.1	51.5	68.1	91.9	108.0	114.0	111.4	138.9
Business fixed investment	150.6	150.2	164.9	189.4	221.1	254.3	270.0	288.9
Change in business inventories	8.9	-10.7	10.0	21.9	22.3	18.1	-2.1	7.0
Nonfarm	10.8	-14.3	12.1	20.7	21.3	16.5	-2.1	7.0
Net exports of goods and services ^{1/}	6.0	20.4	8.0	-9.9	-10.3	-2.0	.9	1.9
Exports	137.9	147.3	163.3	175.9	207.2	258.8	299.2	232.2
Imports	131.9	126.9	155.4	185.8	217.5	260.8	298.3	321.3
Gov't. purchases of goods and services	302.7	338.4	361.3	396.2	435.6	476.1	529.2	579.4
Federal ^{2/}	111.1	123.1	129.7	144.4	152.6	166.3	188.3	209.1
State and local	191.5	215.4	231.6	251.8	283.0	309.8	340.9	370.3
Gross national product in constant (1972) dollars	1217.8	1202.3	1273.0	1340.5	1399.2	1413.3	1413.2	1415.4
Personal income	1154.9	1255.5	1381.6	1531.6	1717.4	1923.8	2111.5	2302.1
Wage and salary disbursements	764.6	805.9	890.0	984.0	1103.3	1227.3	1313.3	1417.8
Disposable personal income	984.6	1086.7	1184.5	1305.1	1458.4	1623.8	1774.0	1919.6
Saving rate (percent)	7.3	7.7	5.8	5.0	4.9	4.6	4.6	4.7
Corporate profits with I.V.A. and C.C. Adj.	83.6	95.9	126.8	150.0	167.7	180.3	161.3	170.8
Corporate profits before tax	126.9	120.4	156.0	177.1	206.0	238.4	219.3	225.3
Federal government surplus or deficit (N.I.A. basis)	-10.7	-70.6	-53.6	-46.3	-27.7	-10.1	-34.4	-15.2
High employment surplus or deficit (-)	14.9	-27.4	-20.2	-19.0	-6.7	18.4	43.3	99.7
State and local government surplus or deficit (-) (N.I.A. basis)	7.6	6.2	17.9	26.8	27.4	24.1	17.1	11.1
Excluding social insurance funds	-2.9	-6.2	2.3	7.3	4.2	-2.4	-12.1	-20.4
Civilian labor force (millions)	91.0	92.6	94.8	97.4	100.4	102.9	104.8	106.0
Unemployment rate (percent)	5.6	8.5	7.7	7.0	6.0	5.8	7.4	8.6
Nonfarm payroll employment (millions)	78.3	77.0	79.4	82.4	86.4	89.5	89.2	88.9
Manufacturing	20.1	18.3	19.0	19.7	20.5	21.0	20.1	19.5
Industrial production (1967=100)	129.3	117.8	130.5	138.2	146.1	152.0	149.4	149.8
Capacity utilization: all manufacturing (percent)	83.8	72.9	79.5	81.9	84.4	85.6	81.3	79.1
Materials (percent)	87.1	73.4	81.1	82.7	85.6	87.1	81.0	78.1
Housing starts, private (million units, A.R.)	1.34	1.16	1.54	1.99	2.02	1.71	1.47	1.86
New auto sales, (millions, A.R.)	8.91	8.66	10.12	11.13	11.29	10.59	9.17	9.55
Domestic models	7.49	7.08	8.63	9.07	9.27	8.20	7.04	7.26
Foreign models	1.42	1.58	1.50	2.06	2.02	2.39	2.14	2.29

^{1/} Balance of payments data 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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CONFIDENTIAL - FR
CLASS II FOMCPERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1974	1975	1976	1977	1978	Projected		
						1979	1980	1981
<u>Constant (1972) dollars</u>								
Gross national product	-1.4	-1.3	5.9	5.3	4.4	2.3	-1.3	-.2
Final purchases	-.7	.2	4.5	4.8	4.4	2.6	-.5	-.2
Private	-1.4	-.3	5.6	5.6	5.0	3.2	-1.0	-.5
Excluding net exports	-2.3	-1.0	6.5	6.2	5.0	2.5	-1.8	-.4
Personal consumption expenditures	-.9	1.8	5.9	5.0	4.5	2.6	-1.1	-1.1
Goods	-3.4	.7	6.9	5.1	4.1	1.1	-3.9	-3.2
Services	2.3	3.2	4.8	4.9	5.1	4.3	2.2	1.2
Gross private domestic investment	-11.4	-22.3	21.6	15.4	7.1	.2	-10.1	4.9
Residential structures	-24.6	-13.9	23.3	20.7	4.2	-6.0	-12.1	13.7
Business fixed investment	-.3	-13.0	4.8	8.6	8.4	5.9	-2.5	-1.3
Gov't. purchases of goods and services	2.1	1.9	.2	2.0	1.8	.4	1.6	1.2
Federal	-.8	.7	-.2	4.4	-2.0	.7	3.1	2.6
State and local	3.8	2.6	.5	.6	4.0	.2	.7	.3
Disposable personal income	-1.5	2.1	3.7	4.2	4.6	2.2	-.9	-.9
<u>Current dollars</u>								
Gross national product	8.1	8.2	11.3	11.6	12.0	11.4	7.8	9.3
Final purchases	8.9	9.7	9.9	11.0	12.1	11.7	8.7	9.0
Private	8.1	9.1	10.8	11.3	12.7	12.3	8.1	8.8
Excluding net exports	8.2	7.8	12.0	12.7	12.6	11.7	8.0	8.8
Personal consumption expenditures	9.8	10.1	11.3	11.0	11.6	11.7	9.1	8.0
Goods	8.9	8.7	11.0	9.8	10.7	10.6	5.9	5.6
Services	11.1	11.8	11.7	12.5	12.7	13.1	12.7	10.6
Gross private domestic investment	-2.5	-11.0	27.3	24.8	15.9	10.0	-1.9	14.6
Residential structures	-16.7	-6.5	32.3	35.0	17.5	5.6	-2.3	24.7
Business fixed investment	10.8	-.3	9.8	14.9	16.7	15.0	6.2	7.0
Gov't. purchases of goods and services	12.3	11.8	6.8	9.7	9.9	9.3	11.1	9.5
Federal	8.7	10.7	5.4	11.3	5.7	9.0	13.2	11.0
State and local	14.5	12.5	7.5	8.7	12.4	9.5	10.0	8.6
Disposable personal income	9.2	10.4	9.0	10.2	11.7	11.3	9.2	8.2
Personal income	9.7	8.7	10.0	10.9	12.1	12.0	9.8	9.0
Wage and salary disbursements	9.0	5.4	10.4	10.6	12.1	11.2	7.0	8.0
Corporate profits with IVA & C.C. Adj.	-15.6	14.7	32.2	18.3	11.8	7.5	-10.4	5.8
Corporate profits before tax	9.6	-5.1	29.6	13.5	16.3	15.7	-8.0	2.7
Nonfarm payroll employment	2.0	-1.7	3.1	3.8	4.9	3.5	-.3	-.4
Manufacturing	-.4	-8.7	3.7	3.6	4.0	2.5	-4.4	-2.9
Nonfarm business sector								
Output per hour	-2.9	1.9	3.5	1.8	.5	-1.0	-.5	.8
Compensation per hour	9.4	9.9	8.3	8.0	8.6	8.9	9.1	9.7
Unit labor costs	12.7	7.8	4.7	6.3	8.0	10.0	9.7	8.8
GNP implicit deflator	9.7	9.6	5.2	6.0	7.3	8.9	9.2	9.1
Gross domestic business product								
fixed-weighted price index ^{1/}	10.4	9.4	5.3	6.2	7.6	9.7	10.2	9.1
Excluding food and energy	8.1	9.5	5.8	6.3	7.2	8.2	8.1	8.1
Consumer price index (all urban)	11.0	9.1	5.8	6.5	7.7	11.2	12.5	9.3
Industrial production	-.4	-8.9	10.8	5.9	5.7	4.0	-1.7	.3

^{1/} Uses expenditures in 1972 weights.

FEDERAL SECTOR ACCOUNTS
(billions of dollars)

January 3, 1980

	Fiscal Year 1979*	FY 1980 e/3/					FY 1981e/ CY79e/					FRB Staff Estimates				
		Admin.		F.R.		F.R.		F.R.		F.R.		Calendar quarters; unadjusted data				
		1/2/	Board	Board	Board	Board	Board	1978	1979				1980			
	IV*	I*	II*	III*	IV	I	II	III	IV							
Unified budget receipts	465.9	513.9	514.2	581.5	480.4	526.5	99.5	102.1	144.4	119.9	114.0	112.3	152.0	135.8	126.4	
Unified budget outlays	493.2 ^{4/}	547.1	552.0	612.0	509.2	566.9	123.2	122.6	123.1	124.4	139.1	134.6	137.7	140.6	154.0	
Surplus(+)/Deficit(-), unified budget	-27.3	-33.2	-37.8	-30.5	-28.8	-40.4	-23.7	-20.5	21.4	-4.5	-25.1	-22.3	14.3	-4.8	-27.6	
Surplus(+)/Deficit(-), off-budget agencies ^{7/}	-12.4	-20.0 ^{5/}	-17.8	n.a.	-14.1	-17.0	-0.1	-3.0	-5.1	-4.1	-1.9	-5.8	-5.7	-4.3	-1.2	
Combined deficit to be financed	-39.7	-53.2	-55.6	n.a.	-42.9	-57.4	-23.8	-23.5	16.3	-8.6	-27.0	-28.1	8.6	-9.1	-28.8	
Means of financing combined deficits: Net borrowing from public	33.7	42.0	42.3	n.a.	36.4	48.1	15.3	10.6	-4.6	12.4	18.0	17.2	1.3	5.8	23.8	
Decrease in cash operating balance	-1.8	9.2 ^{6/}	9.2	n.a.	0.4	3.9	6.1	8.6	-9.8	-6.7	8.3	7.9	-8.0	1.0	3.0	
Other ^{8/}	7.7	2.0 ^{6/}	4.2	n.a.	5.9	5.5	2.5	4.2	-1.9	2.9	0.7	3.0	-2.0	2.5	2.0	
Cash operating balance, end of period	24.2	15.0	15.0	n.a.	15.9	12.0	16.3	7.7	17.5	24.2	15.9	8.0	16.0	15.0	12.0	
Memo: Sponsored agency borrowing ^{9/}	22.1	n.a.	24.3	n.a.	24.5	21.0	4.9	6.4	6.0	4.8	7.3	5.0	6.0	6.0	4.0	
NIA Budget ^{10/}							Seasonally adjusted annual rates									
Receipts	479.0	525.3	533.3	594.2	497.7	539.8	463.5	475.0	485.8	504.8	525.1	527.2	532.0	543.1	556.9	
Expenditures	493.9	546.9	558.3	617.7	507.8	574.2	479.7	486.8	492.9	516.1	535.4	550.5	562.6	584.6	599.1	
Purchases (total)	161.8	178.7	183.3	203.7	166.3	188.3	159.0	163.6	161.7	162.9	177.1	181.4	185.4	189.5	197.0	
Defense	104.9	116.0	118.7	131.5	108.3	121.9	101.2	103.4	106.0	109.0	114.8	117.3	120.0	122.7	127.6	
Nondefense	56.9	62.7	64.6	72.1	58.0	66.4	57.8	60.2	55.7	53.9	62.3	64.1	65.4	66.8	69.4	
All other expenditures	332.1	368.2	375.0	414.0	341.5	385.9	320.7	323.2	331.2	353.2	358.3	369.1	377.2	395.1	402.1	
Surplus(+)/Deficit(-) ^{11/}	-14.9	-21.6	-25.1	-23.5	-10.1	-34.4	-16.3	-11.7	-7.0	-11.3	-10.3	-23.3	-30.6	-41.5	-42.2	
High Employment Surplus(+)/ Deficit(-) (NTA basis) ^{12/}	11.5	n.a.	36.8	84.6	18.4	43.3	-0.8	7.9	20.2	18.7	26.7	33.3	42.8	44.2	52.9	
		*--actual		e--estimated											n.a.--not available	

- Administration estimates as of October 11, 1979, except as noted.
- Administration NIA estimates are from OMB Mid-Session Review of the 1980 Budget, July 12, 1979.
- In the Second Concurrent Resolution on the Budget, Fiscal Year 1980, (November 28, 1979), Congress approved receipts of \$517.8 billion and outlays of \$547.6 billion.
- Excludes \$0.4 billion of outlays for the Exchange Stabilization Fund in order to be consistent with all historical data and Treasury reporting practices.
- Confidential administration estimate as of September 4, 1979.
- Estimate from OMB Mid-Session Review of the 1980 Budget, July 12, 1979.
- Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, Rural Telephone Bank, and Pension Benefit Guaranty Corporation.
- Checks issued less checks paid, accrued items and other transactions.
- Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives marketable debt on an offerings basis.
- All NIA data incorporate the Department of Commerce's July 1979 GNP revisions.
- The fiscal year totals are translations of the OMB Mid-Session Review of the 1980 Budget, July 1979; the translations are based on unadjusted data and do not conform to the average of four seasonally adjusted quarters. The FRB staff estimates, therefore, have been adjusted in order to make the BEA and staff estimates comparable.
- FRB staff estimates are consistent with the Council's new potential GNP series as reported in the Economic Report of the President, January 1979.

DOMESTIC FINANCIAL DEVELOPMENTS

Summary

Most market interest rates have fallen 20 to 60 basis points on balance since the November 20 FOMC meeting, continuing to retrace part of the sharp advance in early October associated with the System's tightening actions. Even so, the fourth quarter ended with short-term rates about 1/2 to 1-1/2 percentage points, and bond yields about 1/2 to 1 percentage point, above levels registered three months before. The higher market rates, reinforced by a tightening of lending standards and nonprice terms and by a slackening of nominal spending growth, exerted a depressing effect on credit flows over the quarter. Net funds raised by domestic nonfinancial sectors are estimated to have fallen nearly one-fifth below the third quarter pace.

A substantial weakening in credit demands by nonfinancial firms over the quarter was in part related to a slowdown in inventory accumulation that reduced the corporate financing gap. Business borrowing at commercial banks and in the commercial paper market, after slowing appreciably in October, turned negative in November before apparently recovering moderately in December. The higher cost of bank credit was indicated by the 2 percentage point rise in the prevailing prime rate over the quarter, despite a drop in December, and by bank reports in mid-November of a substantial decline in the proportion of short-term loan extensions at rates below prime. Banks also reported a reduced willingness to make business loans compared to responses to the August survey.

Issuance of longer-term corporate debt in November and December fell substantially below average monthly levels earlier in the year.

Publicly offered bonds by industrial concerns were particularly meager, likely reflecting reluctance to issue longer-term debt at rates that remain close to the record November highs. Rate spreads between Aaa and A issues of industrial bonds have widened in recent weeks to about twice their average over the first nine months of the year, but remain well below levels reached in mid-October.

Households are estimated to have reduced both mortgage and consumer installment borrowing during the fourth quarter, partly in response to significantly tighter supply conditions, including constraints posed by usury ceilings. Average rates on new mortgage commitments at S&Ls have edged up 10 basis points since the last FOMC meeting to a level more than 150 basis points above that of late September. Commitment policies at S&Ls also remain much more stringent than three months ago despite some reported liberalization since mid-November, a month when new commitments fell by more than 40 percent. Sharply higher consumer finance rates at commercial banks and finance companies and a reported upgrading of consumer lending standards contributed to a slowing of consumer installment credit growth to around 8 percent, at an annual rate, in October and November.

Borrowing by all levels of government remained large in the fourth quarter. The Treasury raised substantial amounts of new money to accommodate both a larger current budget deficit and higher anticipated financing needs for the first quarter. In addition, sponsored agencies' borrowing reached a record amount during the quarter. Bond offerings by state and local governments accelerated in the quarter, owing in part

to a rise in the issuance of housing revenue bonds, which averaged \$1 billion per month.

As with credit flows, growth in the monetary aggregates over the quarter was depressed by the tighter stance of monetary policy and the weakening economy. M-1 advanced at a 5-1/2 percent annual rate in December, and at about a 5 percent rate for the quarter. Quarterly M-2 growth also decelerated, reflecting in part a slowing of the interest-bearing component. Despite rapid growth of large time deposits in October and November, commercial banks significantly reduced the increase in their managed liabilities compared to the previous quarter, as the level of nondeposit funds declined on balance over the three months. By late December, member banks had reduced their managed liabilities subject to marginal reserve requirements to a little over 1 percent of their total managed liabilities and U.S. agencies and branches of foreign banks generally were considerably below their base levels.

Outlook

Some easing of money market conditions may well be associated with the projected decline in economic activity in the first quarter. If market participants conclude that the cyclical peak in short-term interest rates has passed, long-term debt markets also would be likely to strengthen, providing a more receptive environment for corporate debt issuance. Even with a somewhat larger financing gap, short- and intermediate-term credit demands probably will rise little above the reduced fourth quarter pace, as corporations attempt to rebuild their depleted balance sheet positions. Credit demands by the Treasury, sponsored

agencies and state and local governments are likely to remain relatively strong over coming months.

A relaxation of certain constraints on credit supplies by legislative and regulatory actions may facilitate a moderate pickup in mortgage credit flows. The suspension until March 31, 1980 of state usury ceilings--unless revoked by state action--on conventional first mortgages for purchase of residential property just signed into law can be expected to bolster housing credit flows. Similarly, the new 2-1/2 year floating rate time deposit is expected to result in some additional deposit growth at thrift institutions and contribute to enhanced availability of lendable mortgage funds.

In contrast, the expansion of consumer installment credit is likely to moderate further in the coming quarter, given anticipated declines in real income and consumption expenditures and a further moderate rise in debt repayment burdens relative to disposable personal income.

INTERNATIONAL DEVELOPMENTS

Summary. The dollar came under selling pressure again in mid-November, influenced primarily by developments associated with the Iran-U.S. confrontation, including the U.S. freeze of Iranian official assets, and a firming of monetary conditions in a number of foreign countries. During the past seven weeks, the trade-weighted value of the dollar has depreciated by about 4-1/4 percent, reversing the dollar's sharp rise in October. At the end of 1979, the value of the dollar on an average weighted basis was slightly below its year-earlier level, up substantially against the yen, but down against the pound and the German mark.

The weakness of the dollar over the past seven weeks was most pronounced against European currencies, with the British pound, German mark, French franc, Swiss franc and Dutch guilder appreciating between 5 to 6-1/2 percent. Pressure among EMS currencies intensified, and on November 30 the Danish krone was devalued by 5 percent against other EMS currencies. The yen/dollar exchange rate registered wide fluctuations over this period, reflecting market uncertainty about the impact on the Japanese economy of higher oil prices and a possible reduction of oil supplies. The yen was subject to continued downward pressure through the end of November; its subsequent appreciation by about 8 percent in early December has been partially reversed in recent weeks. By the beginning of the year the yen was 3-3/4 above its mid-November level. Oil price developments, the Iranian situation, and other political developments also were reflected in the gold price, with the price reaching above \$630 an ounce by January 3, an increase of over 60 percent over the past seven weeks.

. U.S.

intervention since mid-November has been relatively light.

The \$24 billion (annual rate) U.S. merchandise trade deficit in November was the smallest deficit since July. For October/November combined, the deficit rate was \$26 billion, slightly below the third-quarter rate. Both agricultural and non-agricultural exports in October/November were 8 percent above the third-quarter rate. This increase resulted from higher official contract and spot market prices; the volume of oil imports declined slightly from an average 8.6 mbd in the third quarter.

The U.S. current account for the third quarter was in surplus by \$3 billion (annual rate) following a \$4.2 billion deficit rate in the previous quarter. The shift to surplus reflected a small reduction in the trade deficit and a substantial increase in net investment income to a \$35 billion rate in the third quarter.

U.S. banks reported a net private capital inflow of \$3.9 billion in October, bringing the cumulative net inflow for the first 10 months last year to \$24 billion. Reflecting the increasing cost advantage of offshore banking markets as interest rates in the United States rose, non-banks' dollar-denominated deposits in foreign branches of member banks increased by \$1.5 billion in October.

Official foreign assets of G-10 countries and Switzerland declined by about \$3-1/2 billion in October. In November and December foreign official holdings of these countries at the FRBNY declined further by \$5 billion. For the year as a whole, foreign official assets of these countries are estimated to have declined by about \$22-1/2 billion,

. OPEC official assets in the United States increased by about \$2-1/4 billion in October. OPEC holdings at the FRBNY in the final two months of the year were virtually unchanged,

The steep rise in oil prices in 1979 does not appear to have had a visible adverse effect thus far on economic activity abroad. Most major foreign countries continued to record moderate output gains in the third quarter. Estimated growth over the four quarters of 1979 at about 3 percent is close to the growth that was projected at the start of last year. The inflation performance abroad for 1979, however, was substantially worse than foreseen a year ago, reflecting primarily the higher oil prices. In response to the persistent inflationary pressures, and exchange-market pressures in some instances, monetary authorities in most major industrial countries have tightened monetary conditions further. Since the beginning of November, discount rates were increased in all foreign G-10 countries except France, and monetary targets announced for 1980 by Canada, Germany, Switzerland and the United Kingdom indicate a determination to curb the growth of money supplies in these countries in the period ahead.

Outlook. Increases in oil prices have worsened the prospects for growth and inflation abroad and for the U.S. trade account. The impact of higher oil prices and tightened monetary conditions abroad is expected to result in a slowing of economic expansion abroad. From the fourth quarter of 1979 to the fourth quarter of 1980 the staff projects the rate of growth of the foreign G-10 countries and Switzerland to be about 1 percent, compared with almost 3 percent growth over the four quarters of 1979. Looking further ahead, the staff expects economic activity abroad to begin to rebound by the end of 1980, with the growth rate from the fourth quarter of 1980 to the fourth quarter of 1981 expected to be about 2-1/2 percent. The pace of inflation abroad in 1980 is projected to moderate slightly from the recent 10 percent rate and on average to remain slightly below the projected U.S. rate.

The revised projections for economic activity and inflation abroad and in the United States, and the assumption of higher oil prices (see below), are expected to reduce the gains foreseen earlier for the U.S. current and trade accounts for the period ahead. For 1980, the staff now projects the U.S. current account to move into surplus by about \$5 billion after estimated to be about in balance in 1979. The expected movement in the current account is attributable to a further strengthening of non-trade current-account transactions; no change in the estimated \$28 billion trade deficit for 1979 is foreseen this year. For 1981, despite expectations of a small increase in the U.S. trade deficit, further increases in net receipts from other current-account transactions, primarily net investment income, are expected to widen the current-account surplus to about \$8 billion.

The persistence of U.S. trade deficits on the order of some \$30 billion being projected by the staff for 1980 and 1981 results primarily from the sharp increases expected in the oil import bills, despite projections of a 13 percent decline in the volume of petroleum imports in 1980 and a further 4 percent decline in 1981. The U.S. import price for a barrel of oil is projected to average \$31 in the final quarter of 1980 (an increase of 32 percent over the estimated fourth quarter of 1979 and 133 percent over the fourth quarter of 1978) and to rise a further 13 percent by the fourth quarter of 1981. For 1980, the staff projects an oil import bill of about \$84 billion, compared with \$60 billion estimated for 1979. A further rise in the import bill to nearly \$90 billion is foreseen for 1981.

In the framework of the assumptions underlying the green book projection for the U.S. and foreign economies, the staff expects no significant change in the weighted-average value of the dollar over the forecast period from the average level recorded in the past few months. The outlook for a small surplus in the U.S. current account over the next two years, despite the burden of a gigantic oil import bill, is viewed by some as a factor that will contribute to a strengthening of the value of the dollar in the period ahead. In contrast to this favorable development, however, is the prospect for relatively higher U.S. inflation rates than those for its principal trading partners and the possibility of a continuation and perhaps an acceleration of the tendency on the part of dollar holders to diversify their holdings.

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OUTLOOK FOR U.S. NET EXPORTS AND RELATED ITEMS
(BILLIONS OF DOLLARS, SEASONALLY ADJUSTED ANNUAL RATES)

January 3, 1979

	1979 ANN.	1980 ANN.	1981 ANN.	1979 Q I	1979 Q II	1979 Q III	1979 Q IV	1980 Q I	1980 Q II	1980 Q III	1980 Q IV	1981 Q I	1981 Q II	1981 Q III	1981 Q IV
1. GNP NET EXPORTS															
CURRENT \$, NET	-2.0	0.9	1.9	4.0	-8.1	-2.3	-1.8	-5.5	-0.4	4.5	4.9	3.1	2.2	1.4	1.0
EXPORTS OF G&S	258.8	299.2	323.2	238.5	243.7	267.3	285.6	292.8	297.1	301.0	305.7	311.5	318.3	326.7	336.5
IMPORTS OF G&S	260.8	298.3	321.3	234.4	251.9	269.5	287.4	298.3	297.5	296.4	300.9	308.4	316.1	325.3	335.5
CONSTANT 72 \$, NET	18.4	27.8	27.1	17.0	13.1	20.1	23.4	25.6	28.2	28.9	28.4	27.6	27.2	26.7	26.8
EXPORTS OF G&S	120.1	122.9	121.8	117.0	116.0	122.2	125.3	124.2	123.3	122.3	121.8	121.4	121.4	121.8	122.7
IMPORTS OF G&S	101.7	95.1	94.7	100.0	102.9	102.1	101.9	98.6	95.1	93.4	93.4	93.8	94.2	95.0	95.9
TERMS OF TRADE (1972=100) 1/	84.0	77.6	78.2	87.0	85.8	82.8	80.8	77.9	77.0	77.5	77.9	78.0	78.2	78.4	78.4
2. U.S. MERCHANDISE TRADE BALANCE 2/	-28.1	-27.8	-30.9	-24.5	-30.9	-29.1	-28.0	-33.2	-28.3	-25.2	-24.7	-27.2	-29.3	-32.2	-35.0
EXPORTS (EXCL. MILITARY)	182.7	213.7	229.8	165.4	171.2	189.3	205.0	208.7	213.0	214.8	218.4	222.4	226.8	231.9	238.3
AGRICULTURAL	35.2	38.7	41.1	30.6	30.9	38.4	41.0	39.3	39.3	37.9	38.2	39.2	40.4	41.7	43.1
NONAGRICULTURAL	147.5	175.0	188.7	134.8	140.2	150.9	164.0	169.4	173.7	176.9	180.1	183.2	186.4	190.2	195.2
IMPORTS	210.8	241.6	260.7	189.9	202.0	218.5	232.9	241.9	241.3	240.0	243.0	249.6	256.1	264.1	273.3
PETROLEUM AND PRODUCTS	59.4	83.8	89.0	46.6	51.6	66.5	72.9	82.7	84.6	83.9	84.2	85.9	87.8	89.8	92.4
NONPETROLEUM	151.4	157.7	171.7	143.3	150.4	152.0	160.0	159.2	156.7	156.1	158.9	163.6	168.2	174.3	180.8
3. U.S. CURRENT ACCOUNT BALANCE	0.5	4.6	8.2	1.7	-4.2	3.0	1.6	-2.8	3.3	8.6	9.1	7.4	7.3	8.4	9.8
OF WHICH: NET INVESTMENT INCOME	30.9	32.4	38.2	27.5	29.9	35.2	31.0	31.4	31.8	33.2	33.1	33.8	35.8	39.7	43.7
4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/															
REAL GNP % CHANGE, ANNUAL RATES	3.3	1.7	2.0	1.9	3.8	2.4	3.5	0.8	0.5	1.3	1.7	2.1	2.5	2.7	2.8
CONSUMER PRICES, 4/, % CHANGE, ANNUAL RATES	7.9	9.7	7.8	8.7	10.1	11.8	10.2	9.7	9.1	8.4	8.0	7.8	7.6	7.0	7.2

1/ GNP EXPORT IMPLICIT DEFLATOR DIVIDED BY GNP IMPORT IMPLICIT DEFLATOR.

2/ INTERNATIONAL ACCOUNTS BASIS.

3/ GEOMETRIC WEIGHTS USED TO AGGREGATE FOREIGN REAL GNP AND CONSUMER PRICES -- PER CENT SHARE IN TEN-COUNTRY TOTAL MULTILATERAL TRADE. CANADA (9.1%), JAPAN (13.6%), UNITED KINGDOM (11.9%), GERMANY (20.8%), FRANCE (13.1%), ITALY (9.0%), BELGIUM (6.4%), THE NETHERLANDS (8.3%), SWITZERLAND (3.6%), SWEDEN (4.2%).

4/ WHOLESALE PRICES FOR JAPAN.

P/ PROJECTED.

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