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July 1, 1981

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee

By the staff of the Board of Governors of the Federal Reserve System

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary. The expansion of economic activity apparently halted in the second quarter. Housing activity contracted further, business fixed investment outlays apparently receded, and consumer spending weakened for both autos and other discretionary goods. Rates of increase in aggregate price measures also have slowed recently--mainly reflecting a leveling off in prices for food and energy. Wages generally have continued to rise rapidly, although recently there have been some signs of a moderation.

Industrial production continued to edge higher through May. As in most recent months, the gains were small, and current information suggests that output probably edged down in June. Despite continued weakness in sales, motor vehicles and parts accounted for about half of the May advance in output; in part, production has exceeded sales as automakers have built inventories in preparation for a longer-than-usual summer shutdown. Production of business equipment also rose in May, while output of construction supplies fell for the second month in a row.

Employment at manufacturing establishments declined somewhat in May, following several months of small increases. Employment fell further in construction, returning to the cyclical lows recorded last summer. Reflecting an easing in the demand for labor in goods-producing industries, the unemployment rate rose one-fourth percentage point to 7.6 percent.

Consumer spending in the second quarter retraced some of its gain of earlier months. In auto markets, sales of domestic models have been mired at about a 5-3/4 million unit rate since major price concessions

ended in late March. In addition, sales of imported autos slipped to a 2.2 million unit rate in May, nearly one-half million units below the first quarter average. Sales at general merchandise, apparel, furniture and appliance stores are reported to have edged lower in May; outlays for these items have increased by less than one-half percent over the last three months.

The strength evident in business investment spending earlier in the year appears to have dissipated. In May, a small increase in real shipments of nondefense capital goods offset only a little of the sharp April decline, and nominal spending on business structures has leveled off following a quickening of outlays around the turn of the year. Moreover, indicators of future investment spending have not been strong: constant dollar orders for nondefense capital goods declined in April and were flat in May; contracts for future construction also dropped in April; and the Commerce Department's May survey of capital spending plans indicated that firms have scaled back their planned outlays for 1981 and now anticipate real outlays to be little higher than in 1980.

The book value of manufacturing and trade inventories grew more rapidly in April than in March, as durable goods stocks accumulated at a relatively rapid pace. In particular, there was a sizable increment to auto stocks at dealers, and a buildup of lumber, machinery, and auto products at the wholesale level. In May, manufacturers increased stocks at about the same pace as in April. But overall, firms have maintained tight control over stocks, and current inventories are still at low levels relative to current sales.

The retrenchment of activity in the housing market continued through May. Housing starts, at a 1.15 million annual rate, were off 14 percent from an already low level, and permits remained near the 1-1/4 million unit rate that has prevailed over the last six months. Sales of new and existing houses together have been on a downtrend since last autumn, and edged down further in May. Nonetheless, at a 3 million unit annual rate, May sales still were higher than the cyclical trough reached in the spring of 1980--probably due to the more widespread use of creative financing techniques.

The increase in aggregate price measures slowed in the second quarter, mainly reflecting developments in the food and energy markets. Consumer prices excluding food and energy also showed some improvement over the first five months of the year as homeownership costs and prices for some consumer commodities moderated. Inflation pressure still persists, however; farm prices for livestock have rebounded from earlier declines, the index for homeownership began to rise rapidly again in May, and price increases for capital goods have slowed only a little from their high rates of 1980.

Outlook. It now appears that real GNP was about unchanged in the second quarter, following the 8-1/2 percent (annual rate) surge in the first quarter. Real final sales are estimated to have declined at about a 3 percent rate, while inventories--especially auto stocks--appear to have increased substantially. Aggregate activity is expected to remain sluggish through the summer. The near-term inflation outlook has improved, reflecting in large part recent reductions in the prices of petroleum and petroleum products. The GDBP fixed-weighted price index is

expected to rise at an 8-1/4 percent rate in the third quarter, the same as we now estimate for the second quarter; previously a 9 percent rate increase was projected for the spring and summer period. Increases in the implicit deflator are likely to be smaller than for the fixed-weighted price measure, in part reflecting shifts in the composition of GNP away from relatively high priced items such as petroleum and petroleum products.

During the third quarter, personal consumption expenditures are expected to pick up somewhat as the payback of auto sales "borrowed" from the future as a result of rebate programs comes to an end. A rise in business purchases of autos and trucks also is anticipated. At the same time, however, further declines are projected for residential construction outlays and a reduction in business construction spending. Additional cutbacks in state and local government purchases, due to the continued elimination of public employment jobs, will likely act as an additional drag on GNP growth in the third quarter.

The anticipated contour of economic activity through the end of 1982 has been altered somewhat to reflect revised fiscal policy assumptions. The staff now assumes that personal income taxes will be cut by 7 percent on October 1, 1981, rather than 10 percent as shown in the last Greenbook. In addition, it now is assumed that a further tax reduction of 10 percent will occur on July 1, 1982. A speed up in depreciation allowances (a modified "10-5-3" plan) is assumed to be retroactive to March 1, 1981. On the expenditures side, the staff assumes that nondefense program costs will be cut \$38 billion in FY1982, \$5 billion more than shown in the last Greenbook. As a result of these changes in fiscal policy

assumptions, the unified budget deficit is projected to be \$79 billion in FY1982, little changed from the last Greenbook; the FY1981 deficit is projected to be \$60 billion.

The financial assumptions underlying the staff's economic projections continue to show shift-adjusted M1-B increasing 4-3/4 percent over the four quarters of 1981, and 4-1/4 percent during 1982. Short-term interest rates most likely will continue to exhibit some volatility, but on average they are expected to be a bit higher than in recent months. Expectational factors, however, may permit some reduction in long rates over the next year or so.

Some boost to activity in response to the tax cut is anticipated in the fourth quarter of 1981 and again in the last half of 1982. Generally, however, the growth of GNP over the projection period is constrained by the assumed growth of the monetary aggregates, which results in little abatement of recent pressures in financial markets. On balance, real GNP is projected to rise at a 3/4 percent annual rate over the last half of 1981 and 1-1/4 percent during 1982. Reflecting this sluggish growth, the unemployment rate is projected to rise from 7-1/2 percent in 1981-Q2 to 8-1/4 percent by the end of 1982.

Financial market effects are most noticeable on outlays for investment goods. Housing activity is expected to remain at depressed levels through mid-1982 when underlying demand pressures and some easing of financial conditions permits a modest upturn. In the business area, real outlays are projected to be on a downtrend throughout the entire period, reflecting the relatively wide margin of unused capacity, the high real cost of capital, and growth of cash flow that barely exceeds

the rate of inflation. The high cost of borrowing also is likely to constrain consumer purchases of autos and other durable goods.

The current softening of energy prices is expected to continue for a few more months. Thereafter, energy prices are projected to outpace the overall inflation rate by about 1 to 2 percentage points, reflecting the reported longer-run OPEC strategy to slowly raise the relative price of crude oil. Food prices also are expected to put pressure on the overall inflation rate later this year, reflecting reduced supplies of red meat. Excluding food and energy, price increases are projected to show a moderate improvement. By 1982, continued slack in both labor and product markets, as well as a heightened perception of the credibility of monetary policy, should have further favorable effects on inflation expectations and damp the rate of increase in wages. As a result, the GDBP fixed-weighted price index is projected to slow from an 8-1/2 percent annual rate in the second half of this year to a 7-1/4 percent rate by the end of 1982.

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				
5/13/81	7/1/81	5/13/81	7/1/81	5/13/81	7/1/81	5/13/81	7/1/81	5/13/81	7/1/81	
Annual changes:										
1979 1/	12.0	12.0	3.2	3.2	9.7	9.7	8.4	8.4	5.8	5.8
1980 1/	8.8	8.8	-.2	-.2	9.8	9.8	8.7	8.7	7.1	7.1
1981	11.2	11.6	2.3	2.6	9.5	9.3	8.4	8.7	7.4	7.6
1982	8.6	8.3	.8	.8	8.2	8.0	7.7	7.7	7.9	8.2
Quarterly changes:										
1980-Q1 1/	12.6	12.6	3.1	3.1	10.1	10.1	7.4	7.4	6.2	6.2
1980-Q2 1/	-1.1	-1.1	-9.9	-9.9	9.8	9.8	9.5	9.5	7.3	7.3
1980-Q3 1/	11.8	11.8	2.4	2.4	9.6	9.6	9.3	9.3	7.5	7.5
1980-Q4 1/	14.9	14.9	3.8	3.8	9.3	9.3	8.2	8.2	7.5	7.5
1981-Q1 1/	14.9	19.2	6.5	8.6	10.2	10.5	7.5	8.1	7.4	7.3
1981-Q2	9.2	6.5	1.0	.2	9.3	8.4	9.2	10.0	7.3	7.5
1981-Q3	8.4	7.5	.3	.3	8.9	8.3	8.3	8.4	7.4	7.7
1981-Q4	10.0	10.3	1.5	1.1	8.6	8.5	7.7	7.8	7.5	7.8
1982-Q1	7.8	7.6	.2	.4	8.1	8.1	7.6	7.4	7.7	8.0
1982-Q2	7.7	7.3	.4	.2	7.8	7.8	7.2	7.3	7.9	8.2
1982-Q3	8.7	8.8	1.5	2.0	7.6	7.6	7.1	7.2	8.0	8.3
1982-Q4	9.4	9.8	1.5	2.3	7.3	7.3	7.0	7.1	8.1	8.3
Two-quarter changes: 2/										
1980-Q2 1/	5.6	5.6	-3.6	-3.6	9.9	9.9	8.4	8.4	1.4	1.4
1980-Q4 1/	13.3	13.3	3.1	3.1	9.5	9.5	8.8	8.8	.2	.2
1981-Q2	12.0	12.6	3.7	4.3	9.6	9.4	8.4	9.1	-.2	.0
1981-Q4	9.2	8.9	.9	.7	8.7	8.4	8.0	8.1	.2	.3
1982-Q2	7.7	7.4	.3	.3	7.9	7.9	7.4	7.3	.4	.4
1982-Q4	9.0	9.3	1.5	2.2	7.5	7.4	7.0	7.1	.2	.1
Four-quarter changes: 3/										
1979-Q4 1/	9.9	9.9	1.7	1.7	10.3	9.7	8.2	8.2	.1	.1
1980-Q4 1/	9.4	9.4	-.3	-.3	9.7	9.7	8.6	8.6	1.6	1.6
1981-Q4	10.6	10.8	2.3	2.5	9.2	8.9	8.2	8.6	.0	.3
1982-Q4	8.4	8.4	.9	1.2	7.7	7.7	7.2	7.2	.6	.5

1/ Actual.

2/ Percent change from two quarters earlier.

3/ Percent change from four quarters earlier.

July 1, 1981

CONFIDENTIAL - FR
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.)

	1979				1980			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	2340.6	2374.6	2444.1	2496.3	2571.7	2564.8	2637.3	2730.6
Final purchases	2316.2	2341.5	2430.8	2497.1	2569.1	2557.4	2653.4	2748.0
Private	1858.0	1876.4	1955.4	2000.7	2052.3	2027.4	2119.9	2189.4
Excluding net exports	1838.1	1868.2	1937.5	1993.1	2044.1	2010.3	2075.4	2166.1
Personal consumption expenditures	1454.1	1478.0	1529.1	1582.3	1631.0	1626.8	1682.2	1751.0
Goods	784.3	793.8	824.8	855.3	882.0	858.4	883.0	926.8
Services	669.9	684.2	704.3	727.0	749.0	768.4	799.2	824.2
Gross private domestic investment	408.3	423.2	421.7	410.0	415.6	390.9	377.1	397.7
Residential construction	116.7	117.2	119.8	120.6	115.2	93.6	99.2	113.0
Business fixed investment	267.3	272.9	288.5	290.2	297.8	289.8	294.0	302.1
Change in business inventories	24.3	33.1	13.3	-8	2.5	7.4	-16.0	-17.4
Nonfarm	20.8	29.2	7.8	-4.4	1.5	6.1	-12.3	-14.0
Net exports of goods and services ^{1/}	19.9	8.2	17.9	7.6	8.2	17.1	44.5	23.3
Exports	259.1	266.8	293.1	306.3	337.3	333.3	342.4	346.1
Imports	239.2	258.6	275.2	298.7	329.1	316.2	297.9	322.7
Gov't. purchases of goods and services	458.2	465.1	475.4	496.4	516.8	530.0	533.5	558.6
Federal ^{2/}	164.8	163.6	165.1	178.1	190.0	198.7	194.9	212.0
State and local	293.4	301.6	310.4	318.3	326.8	331.3	338.6	346.6
Gross national product in constant (1972) dollar	1479.9	1473.4	1488.2	1490.6	1501.9	1463.3	1471.9	1485.6
Personal income	1864.6	1906.3	1972.3	2032.0	2088.2	2114.5	2182.1	2256.2
Wage and salary disbursements	1194.8	1218.6	1248.6	1282.2	1314.7	1320.4	1341.8	1397.8
Disposable personal income	1580.2	1612.8	1663.8	1710.1	1765.1	1784.1	1840.6	1897.0
Saving rate (percent)	5.3	5.6	5.4	4.7	4.9	6.2	6.1	5.1
Corporate profits with I.V.A. and C.C. Adj	201.9	196.6	199.5	189.4	200.2	169.3	177.9	183.3
Corporate profits before tax	253.1	250.9	262.0	255.4	277.1	217.9	237.6	249.5
Federal government surplus or deficit (-) (N.I.A. basis)	-11.5	-8.1	-15.2	-24.5	-36.3	-66.5	-74.2	-67.9
High employment surplus or deficit (-)	-4.6	5.1	-2.3	-7.1	-17.1	-21.5	-21.2	-13.4
State and local government surplus or deficit (-) (N.I.A. basis)	29.5	21.9	26.5	28.9	26.6	23.9	28.6	37.1
Excluding social insurance funds	7.1	-1.7	2.1	4.0	1.3	-1.7	.9	8.1
Civilian labor force (millions)	102.3	102.4	103.2	103.7	104.2	104.7	105.0	105.2
Unemployment rate (percent)	5.8	5.7	5.8	5.9	6.2	7.3	7.5	7.5
Nonfarm payroll employment (millions)	89.1	89.7	90.2	90.6	91.1	90.5	90.1	90.9
Manufacturing	21.1	21.1	21.1	21.0	21.0	20.3	19.9	20.3
Industrial production (1967=100)	152.7	152.3	152.6	152.5	152.5	144.6	142.1	149.1
Capacity utilization: all mfg. (percent)	86.9	85.9	85.3	84.4	83.4	77.9	75.7	79.2
Materials (percent)	88.4	87.5	87.2	86.3	85.5	78.7	74.9	80.0
Housing starts, private (million units, A.R.)	1.64	1.84	1.79	1.59	1.23	1.06	1.39	1.54
New autos sales, (millions, A.R.)	11.56	10.65	10.79	9.80	10.65	7.68	8.80	9.04
Domestic models	9.30	8.16	8.63	7.43	7.87	5.53	6.51	6.57
Foreign models	2.25	2.49	2.16	2.37	2.77	2.14	2.29	2.47

^{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.

July 1, 1981

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

	1979				1980			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	
<u>Constant (1972) dollars</u>								
Gross national product	3.9	-1.7	4.1	.6	3.1	-9.9	2.4	3.8
Final purchases	2.5	-2.5	7.2	2.9	3.1	-10.4	4.1	4.4
Private	3.0	-3.0	8.7	2.2	2.2	-13.3	6.5	4.9
Excluding net exports	1.1	-1.6	5.5	1.9	-4	-14.4	4.6	8.5
Personal consumption expenditures	.9	-1.2	4.7	3.6	.8	-9.8	5.1	7.0
Goods	-2.7	-4.6	6.0	4.2	-.3	-17.7	4.0	10.2
Services	5.5	3.0	3.1	2.8	2.1	.0	6.4	3.7
Gross private domestic investment	10.6	1.7	-9.9	-17.8	-5.6	-28.9	-10.0	11.1
Residential structures	-6.5	-10.8	-3.6	-3.1	-24.2	-60.2	16.0	64.2
Business fixed investment	5.2	-.4	13.4	-5.4	2.2	-19.9	-1.5	4.0
Gov't. purchases of goods and services	.7	-.5	1.2	6.1	6.9	2.5	-5.0	2.2
Federal	8.0	-7.9	-3.6	13.1	18.9	11.9	-13.1	2.0
State and local	-3.3	4.0	3.9	2.4	.6	-2.8	.3	2.3
Disposable personal income	3.1	.5	3.5	.8	1.3	-4.9	4.1	2.9
<u>Current dollars</u>								
Gross national product	12.7	5.9	12.2	8.8	12.6	-1.1	11.8	14.9
Final purchases	11.5	4.4	16.1	11.4	12.0	-1.8	15.9	15.0
Private	12.8	4.0	17.9	9.6	10.7	-4.8	19.5	13.8
Excluding net exports	10.8	6.7	15.7	12.0	10.6	-6.5	13.6	18.7
Personal consumption expenditures	11.0	6.7	14.6	14.7	12.9	-1.0	14.3	17.4
Goods	8.5	4.9	16.6	15.6	13.1	-10.3	12.0	21.4
Services	14.2	8.8	12.2	13.5	12.7	10.8	17.0	13.1
Gross private domestic investment	17.0	15.4	-1.5	-10.6	5.6	-21.8	-13.3	23.7
Residential structures	1.8	1.8	9.1	2.8	-16.7	-56.4	25.7	68.5
Business fixed investment	13.9	8.6	25.0	2.3	11.0	-10.4	6.0	11.5
Gov't. purchases of goods and services	6.3	6.2	9.2	18.8	17.5	10.6	2.6	20.2
Federal	10.7	-2.9	3.7	35.4	29.5	19.8	-7.5	40.2
State and local	3.9	11.6	12.2	10.6	11.2	5.6	9.1	9.7
Disposable personal income	13.5	8.5	13.3	11.6	13.5	4.4	13.3	12.8
Personal income	12.8	9.3	14.6	12.7	11.5	5.1	13.4	14.3
Wage and salary disbursements	13.5	8.2	10.2	11.2	10.5	1.8	6.6	17.8
Corporate profits with IVA & C.C. Adj.	-1.6	-10.1	6.0	-18.8	24.8	-48.9	21.9	12.7
Corporate profits before tax	8.3	-3.4	18.9	-9.7	38.6	-61.8	41.4	21.6
Nonfarm payroll employment	4.3	2.4	2.3	1.7	2.5	-2.7	-1.6	3.6
Manufacturing	4.6	.6	-.6	-1.7	-.8	-11.7	-7.2	6.4
Nonfarm business sector								
Output per hour	-.9	-1.9	-1.4	-.3	.0	-3.0	3.8	-.4
Compensation per hour	10.9	10.0	8.1	9.6	9.9	11.2	9.3	9.6
Unit labor costs	11.9	12.1	9.7	9.9	9.9	14.6	5.3	10.1
GNP implicit deflator ^{1/}	8.4	7.8	7.8	8.1	9.3	9.8	9.2	10.7
Gross domestic business product								
fixed-weighted price index ^{2/}	9.7	9.7	9.5	10.0	10.1	9.8	9.6	9.3
Excluding food and energy	7.5	7.2	6.9	11.1	7.4	9.5	9.3	8.2
Consumer price index (all urban)	10.2	12.5	14.0	14.3	16.5	13.1	7.7	12.9
Industrial production	5.4	-1.0	.8	-.3	.0	-19.2	-6.7	21.2

^{1/} Excluding Federal pay increases, rates of change were: 1979-Q1, 8.3 percent; 1979-Q4, 7.5 percent; 1980-Q1, 9.2 percent; 1980-Q4, 9.7 percent.

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

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CONFIDENTIAL - FR
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.)

	1981				Projected	1982			
	Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4
Gross national product	2853.0	2898.1	2951.3	3024.6	3080.7	3135.2	3201.7	3277.5	
Final purchases	2848.5	2875.9	2930.0	3004.3	3060.9	3115.9	3187.2	3261.0	
Private	2272.0	2297.7	2340.2	2397.4	2442.2	2486.5	2546.9	2602.2	
Excluding net exports	2242.8	2272.6	2319.4	2377.1	2428.0	2478.7	2547.0	2607.1	
Personal consumption expenditures	1810.1	1839.2	1884.2	1936.3	1980.8	2024.1	2082.8	2132.5	
Goods	964.3	965.1	987.2	1015.4	1037.9	1059.2	1093.9	1122.2	
Services	845.8	874.1	897.0	920.9	942.9	964.9	988.9	1010.3	
Gross private domestic investment	437.1	455.6	456.5	461.1	467.0	473.9	478.7	491.1	
Residential construction	116.7	110.7	106.2	107.7	110.2	113.2	118.0	123.3	
Business fixed investment	315.9	322.7	329.0	333.1	337.0	341.4	346.2	351.3	
Change in business inventories	4.5	22.2	21.3	20.3	19.8	19.3	14.5	16.5	
Nonfarm	6.8	20.2	21.3	20.3	19.8	19.3	14.5	16.5	
Net exports of goods and services ^{1/}	29.2	25.1	20.8	20.3	14.2	7.8	-1.1	-4.9	
Exports	367.4	373.6	380.4	388.1	393.0	398.0	401.7	407.3	
Imports	338.2	348.6	359.7	367.7	378.8	390.2	401.8	412.2	
Gov't. purchases of goods and services	576.5	578.2	589.8	606.9	618.7	629.4	640.3	658.8	
Federal ^{2/}	221.6	218.3	223.8	234.9	240.8	245.7	250.8	263.5	
State and local	354.9	359.9	366.0	372.0	377.9	383.7	389.5	395.3	
Gross national product in constant (1972) dollars	1516.4	1517.1	1518.1	1522.3	1523.7	1524.6	1532.3	1541.0	
Personal income	2319.8	2366.4	2433.3	2493.4	2541.1	2590.8	2654.3	2714.2	
Wage and salary disbursements	1442.9	1467.0	1494.4	1527.4	1554.1	1580.1	1608.5	1647.1	
Disposable personal income	1947.8	1984.1	2037.7	2104.1	2144.3	2182.6	2266.2	2312.9	
Saving rate (percent)	4.6	4.8	5.0	5.5	5.1	4.8	5.6	5.3	
Corporate profits with I.V.A. and C.C. Adj.	203.0	196.1	189.1	197.8	191.5	187.5	192.2	197.6	
Corporate profits before tax	259.1	233.7	227.9	234.4	211.8	204.7	206.4	208.8	
Federal government surplus or deficit (-) (N.I.A. basis)	-43.3	-41.0	-54.7	-77.8	-80.3	-79.6	-119.8	-121.3	
High employment surplus or deficit (-) ^{3/}	3.6	9.6	3.4	-13.3	-6.7	1.9	-36.8	-34.3	
State and local government surplus or deficit (-) (N.I.A. basis)	37.0	32.1	31.3	30.5	29.0	29.0	30.9	32.4	
Excluding social insurance funds	6.7	1.1	-3	-1.7	-4.0	-4.7	-3.6	-2.9	
Civilian labor force (millions)	105.8	107.2	107.5	107.8	108.1	108.4	108.7	109.0	
Unemployment rate (percent)	7.3	7.5	7.7	7.8	8.0	8.2	8.3	8.3	
Nonfarm payroll employment (millions)	91.6	91.5	91.6	91.7	91.7	91.7	91.8	92.0	
Manufacturing	20.4	20.4	20.5	20.4	20.4	20.4	20.4	20.5	
Industrial production (1967=100)	151.8	152.7	153.0	153.5	153.7	153.7	155.1	157.0	
Capacity utilization: all mfg. (percent)	79.9	80.1	79.6	79.3	78.9	78.4	78.6	79.2	
Materials (percent)	81.7	81.1	80.7	80.6	79.9	79.4	79.5	80.0	
Housing starts, private (million units, A.R.)	1.39	1.21	1.15	1.15	1.20	1.25	1.30	1.35	
New autos sales, (millions, A.R.)	9.96	7.90	8.70	8.90	8.40	8.80	9.10	8.85	
Domestic models	7.31	5.70	6.40	6.50	6.30	6.50	6.70	6.45	
Foreign models	2.66	2.20	2.30	2.40	2.10	2.30	2.40	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.

^{3/} Estimates in table are evaluated at a 5.1 percent high employment unemployment rate. Evaluated at a 6.1 percent unemployment rate, the high employment budget would show a deficit of \$37.8 billion in 1980-Q4 and a deficit of \$40.8 billion in 1981-Q4, and a deficit of \$62.9 billion in 1982-Q4.

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

	1981				1982			
	Q1	Q2	Q3	Q4	Projected Q1	Q2	Q3	Q4
<u>Constant (1972) dollars</u>								
Gross national product	8.6	.2	.3	1.1	.4	.2	2.0	2.3
Final purchases	6.9	-3.1	.4	1.2	.4	.3	2.7	2.0
Private	7.3	-2.8	.2	1.7	.3	.4	3.3	2.3
Excluding net exports	6.7	-2.6	1.3	2.5	1.2	1.2	4.2	2.8
Personal consumption expenditures	5.8	-1.1	2.5	3.3	1.7	1.5	4.8	3.1
Goods	12.5	-.7	1.3	1.1	-.0	.1	2.7	3.0
Services	1.4	3.7	1.7	3.1	2.0	1.5	2.2	2.0
Gross private domestic investment	24.2	15.2	-5.0	-2.5	-1.7	-1.0	-3.4	3.5
Residential structures	3.6	-25.8	-21.6	-2.1	1.3	2.9	9.1	10.2
Business fixed investment	13.3	-3.0	1.1	-1.5	-2.1	-1.5	-1.1	-.8
Gov't. purchases of goods and services	5.4	-4.0	1.0	-.7	1.2	-.0	.3	.9
Federal	14.8	-6.4	4.9	.3	5.3	2.2	3.1	4.8
State and local	.2	-2.5	-1.3	-1.3	-1.2	-1.4	-1.4	-1.5
Disposable personal income	3.0	-.1	3.6	5.3	.2	-.1	8.7	1.8
<u>Current dollars</u>								
Gross national product	19.2	6.5	7.5	10.3	7.6	7.3	8.8	9.8
Final purchases	15.5	3.9	7.7	10.5	7.7	7.4	9.5	9.6
Private	16.0	4.6	7.6	10.2	7.7	7.5	10.1	9.0
Excluding net exports	14.9	5.4	8.5	10.3	8.8	8.6	11.5	9.8
Personal consumption expenditures	14.2	6.6	10.2	11.5	9.5	9.0	12.1	9.9
Goods	17.2	.3	9.5	11.9	9.2	8.5	13.8	10.8
Services	10.9	14.1	10.9	11.1	9.9	9.7	10.3	8.9
Gross private domestic investment	45.9	18.0	.8	4.1	5.2	6.0	4.1	10.8
Residential structures	14.0	-19.1	-15.3	5.8	9.6	11.3	18.1	19.2
Business fixed investment	19.6	8.8	8.0	5.1	4.8	5.3	5.7	6.0
Gov't. purchases of goods and services	13.5	1.2	8.3	12.1	8.0	7.1	7.1	12.1
Federal	19.3	-5.8	10.5	21.4	10.4	8.4	8.6	21.8
State and local	10.0	5.8	7.0	6.7	6.5	6.3	6.2	6.1
Disposable personal income	11.2	7.7	11.3	13.7	7.9	7.3	16.2	8.5
Personal income	11.8	8.3	11.8	10.2	7.9	8.1	10.2	9.3
Wage and salary disbursements	13.5	6.8	7.7	9.1	7.2	6.9	7.4	9.9
Corporate profits with IVA & C.C. Adj.	50.4	-12.9	-13.5	19.7	-12.1	-8.1	10.4	11.7
Corporate profits before tax	16.3	-33.9	-9.5	11.9	-33.3	-12.8	3.4	4.6
Nonfarm payroll employment	3.0	-.4	.3	.3	.3	.1	.4	.7
Manufacturing	2.4	3.1	.6	-.7	-1.0	-.8	1.7	2.9
Nonfarm business sector								
Output per hour	4.0	-.4	-.4	.7	-.1	.2	1.9	1.7
Compensation per hour	11.4	9.0	9.2	8.5	8.9	8.0	7.9	7.9
Unit labor costs	7.2	9.4	9.7	7.7	9.0	7.7	5.9	6.1
GNP implicit deflator ^{1/}	9.8	6.3	7.3	9.1	7.2	7.0	6.6	7.3
Gross domestic business product								
fixed-weighted price index ^{2/}								
Excluding food and energy	10.5	8.4	8.3	8.5	8.1	7.8	7.6	7.3
Consumer price index (all urban)	8.1	10.0	8.4	7.8	7.4	7.3	7.2	7.0
Consumer price index (all urban)	10.8	7.6	10.0	10.4	8.8	7.9	7.4	7.0
Industrial production	7.4	2.4	.8	1.3	.5	.0	3.7	5.0

^{1/} Excluding Federal pay increases, the rates of change are: 1981-Q1, 9.7 percent; 1981-Q4, 8.2 percent; 1982-Q1, 7.2 percent; 1982-Q4, 6.4 percent.

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

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

	1975	1976	1977	1978	1979	1980	Projected	
							1981	1982
Gross national product	1549.2	1718.0	1918.0	2156.1	2413.9	2626.1	2931.7	3173.8
Final purchases	1556.1	1706.2	1897.0	2133.9	2396.4	2632.0	2914.7	3156.3
Private	1216.2	1344.1	1502.5	1701.3	1922.6	2097.3	2326.8	2519.5
Excluding net exports	1189.4	1330.4	1506.7	1701.9	1909.2	2074.0	2303.0	2515.2
Personal consumption expenditures	976.4	1084.3	1205.5	1348.7	1510.9	1672.8	1867.5	2055.0
Goods	539.5	598.5	657.8	729.1	814.5	887.6	983.0	1078.3
Services	437.0	485.7	547.7	619.6	696.3	785.2	884.5	976.7
Gross private domestic investment	206.1	257.9	322.3	375.3	415.8	395.3	452.6	477.7
Residential construction	55.3	72.0	95.8	111.3	118.6	105.3	110.3	116.2
Business fixed investment	157.7	174.1	205.5	242.0	279.7	296.0	325.2	344.0
Change in business inventories	-6.9	11.8	21.0	22.2	17.5	-5.9	17.1	17.5
Nonfarm	-10.5	13.9	20.2	21.8	13.4	-4.7	17.2	17.5
Net exports of goods and services ^{1/}	26.8	13.7	-4.2	-6	13.4	23.3	23.8	4.3
Exports	154.9	170.9	183.3	219.8	281.3	339.8	377.4	400.0
Imports	128.1	157.1	187.5	220.4	267.9	316.5	353.5	395.7
Gov't. purchases of goods and services	339.9	552.1	394.5	432.6	473.8	534.7	587.8	636.8
Federal ^{2/}	122.7	129.2	143.9	153.4	167.9	198.9	224.6	250.2
State and local	217.2	232.9	250.6	279.2	305.9	335.8	363.2	386.6
Gross national product in constant (1972) dollars	1233.9	1300.4	1371.7	1436.9	1483.0	1480.7	1518.5	1530.4
Personal income	1265.0	1391.2	1538.0	1721.8	1943.8	2160.2	2403.2	2625.1
Wage and salary disbursements	806.4	889.9	983.8	1105.2	1236.1	1343.7	1482.9	1597.4
Disposable personal income	1096.1	1194.4	1311.5	1462.9	1641.7	1821.7	2018.4	2226.5
Saving rate (percent)	8.6	6.9	5.6	5.2	5.2	5.6	5.0	5.2
Corporate profits with I.V.A. and C.C. Adj.	110.5	138.1	164.7	185.5	196.0	182.7	196.5	192.2
Corporate profits before tax	132.1	166.3	192.6	223.3	255.4	245.5	238.8	207.9
Federal government surplus or deficit (N.I.A. basis)	-69.3	-53.1	-46.4	-29.2	-14.8	-61.2	-54.2	-100.2
High employment surplus or deficit (-)	-29.2	-20.1	-23.0	-15.7	-2.2	-18.3	.8	-19.0
State and local government surplus or deficit (-) (M.I.A. basis)	5.5	16.6	28.1	29.0	26.7	29.1	32.7	30.3
Excluding social insurance funds	-7.6	.9	10.1	9.0	2.9	2.1	1.4	-3.8
Civilian labor force (millions)	92.6	94.8	97.4	100.4	102.9	104.7	107.1	108.5
Unemployment rate (percent)	8.5	7.7	7.0	6.0	5.8	7.1	7.6	8.2
Nonfarm payroll employment (millions)	77.0	79.4	82.5	86.7	89.9	90.7	91.6	91.8
Manufacturing	18.3	19.0	19.7	20.5	21.1	20.4	20.4	20.4
Industrial production (1967=100)	117.8	130.5	138.1	146.1	152.5	147.1	152.7	154.9
Capacity utilization: all manufacturing (percent)	72.9	79.5	81.9	84.4	85.6	79.1	79.7	78.8
Materials (percent)	73.4	81.1	82.7	85.6	87.4	79.8	81.0	79.7
Housing starts, private (million units, A.R.)	1.16	1.54	1.99	2.02	1.75	1.29	1.22	1.27
New auto sales, (millions, A.R.)	8.66	10.12	11.13	11.28	10.70	9.04	8.87	8.79
Domestic models	7.08	8.63	9.07	9.29	8.38	6.62	6.48	6.49
Foreign models	1.58	1.50	2.06	1.99	2.32	2.42	2.39	2.30

^{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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AND RELATED ITEMS

	1975	1976	1977	1978	1979	1980	Projected	
							1981	1982
<u>Constant (1972) dollars</u>								
Gross national product	-1.1	5.4	5.5	4.8	3.2	-.2	2.6	.8
Final purchases	.3	4.2	5.2	4.7	3.5	.7	1.8	.7
Private	-.1	5.3	6.0	15.4	4.0	.2	2.1	.9
Excluding net exports	-.6	6.2	6.5	5.2	2.9	-1.0	2.6	1.7
Personal consumption expenditures	2.2	5.6	4.9	4.7	2.9	.5	3.0	2.4
Goods	1.3	6.7	5.2	4.2	1.9	-1.4	3.1	.9
Services	3.3	4.3	4.5	5.4	4.1	2.6	2.9	2.2
Gross private domestic investment	-20.8	19.2	15.7	7.6	1.3	-12.5	5.9	-1.1
Residential structures	-12.5	21.3	18.5	2.9	-5.2	-18.6	-2.8	-2.8
Business fixed investment	-12.1	5.3	11.9	9.1	6.5	-3.0	1.7	-1.3
Gov't. purchases of goods and services	2.1	.0	2.1	2.0	1.5	2.9	.6	.1
Federal	.8	-.7	4.1	-.9	1.9	6.3	2.1	2.6
State and local	2.9	.5	.9	3.7	1.2	1.0	-.4	-1.4
Disposable personal income	2.0	2.6	3.6	4.4	3.1	.7	2.2	2.6
<u>Current dollars</u>								
Gross national product	8.0	10.9	11.6	12.4	12.0	8.8	11.6	8.3
Final purchases	9.6	9.6	11.2	12.5	12.3	9.8	10.7	8.3
Private	9.0	10.5	11.8	13.2	13.0	9.1	10.9	8.3
Excluding net exports	7.9	11.8	13.3	12.9	12.2	8.6	11.0	9.2
Personal consumption expenditures	9.9	11.1	11.2	11.9	12.0	10.7	11.6	10.0
Goods	9.0	10.9	9.9	10.8	11.7	9.0	10.8	9.7
Services	11.1	11.2	12.7	13.1	12.4	12.8	12.6	10.4
Gross private domestic investment	-9.9	25.1	25.0	16.5	10.8	-4.9	14.5	5.5
Residential structures	-4.7	30.2	33.1	16.1	6.6	-11.3	4.8	5.3
Business fixed investment	.8	10.3	18.1	17.7	15.6	5.8	9.9	5.8
Gov't. purchases of goods and services	11.8	6.5	8.9	9.7	9.5	12.9	9.9	8.3
Federal	10.6	5.3	11.4	6.6	9.5	18.5	12.9	11.4
State and local	12.5	7.3	7.6	11.4	9.6	9.8	8.2	6.4
Disposable personal income	9.8	9.0	9.8	11.5	12.2	11.0	10.8	10.3
Personal income	8.2	10.0	10.6	12.0	12.9	11.1	11.2	9.2
Wage and salary disbursements	5.3	10.4	10.6	12.3	11.8	8.7	10.4	7.7
Corporate profits with IVA & C.C. Adj.	16.5	25.0	19.3	12.6	6.1	-7.2	7.6	-2.2
Corporate profits before tax	-3.3	25.9	15.8	15.9	14.4	-3.9	-2.7	-12.9
Nonfarm payroll employment	-1.7	3.2	3.9	5.1	3.7	.9	1.0	.3
Manufacturing	-8.8	3.7	3.6	4.2	2.8	-3.4	.3	.0
Nonfarm business sector								
Output per hour	2.1	3.2	2.0	-.2	-.8	-.4	1.1	.4
Compensation per hour	9.6	8.1	7.6	8.5	9.6	9.8	9.9	8.5
Unit labor costs	7.4	4.7	5.5	8.7	10.4	10.3	8.7	8.0
GNP implicit deflator	9.6	5.2	5.8	7.3	8.5	9.0	8.8	7.4
Gross domestic business product								
fixed-weighted price index ^{1/}	9.2	5.5	6.3	7.8	9.7	9.8	9.3	8.0
Excluding food and energy	9.2	6.0	6.5	7.5	8.4	8.7	8.7	7.7
Consumer price index (all urban)	9.1	5.8	6.5	7.7	11.3	13.5	10.1	8.7
Industrial production	-8.9	10.8	5.8	5.8	4.4	-3.5	3.9	1.4

^{1/} Uses expenditures in 1972 weights.

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FEDERAL SECTOR ACCOUNTS
(billions of dollars)

	Fiscal Year 1980*	FY 1981 e/		FY 1982 e/		CY 1980*	CY 1981 e/ F.R. Board	FRB Staff Estimates								
		Admin. 1/	F.R. Board	Admin. 1/	F.R. Board			Calendar quarters; unadjusted data								
								1980			1981			1982		
								IV*	I*	II	III	IV	I	II	III	
Unified budget receipts	520.0	600.3	602.8	650.3	646.1	533.0	620.4	127.0	135.2	182.7	157.9	144.9	146.8	195.5	158.9	
Unified budget outlays	579.6	655.2	663.1	695.3	724.8	601.1	687.1	160.6	167.3	165.9	169.3	184.6	165.5	185.5	189.2	
Surplus(+)/deficit(-), unified budget	-59.6	-54.9	-60.3	-45.0	-78.7	-68.1	-66.7	-33.6	-32.1	16.8	-11.4	-39.7	-18.7	10.0	-30.3	
Surplus(+)/deficit(-), off-budget agencies 2/	-14.2	-23.6	-22.8	-16.7	-17.5	-15.3	-22.0	-2.2	-6.4	-6.8	-7.5	-1.3	-4.7	-5.4	-6.2	
Combined deficit to be financed	-73.8	-78.5	-83.1	-61.7	-96.2	-83.4	-88.7	-35.8	-38.5	10.0	-18.9	-41.0	-23.4	4.6	-36.5	
Means of financing combined deficits:																
Net borrowing from public	70.5	71.0	74.8	60.0	93.9	79.3	79.0	27.7	35.8	-3.0	14.4	31.5	23.9	1.4	37.0	
Decrease in cash operating balance	3.2	6.0	6.0	0.0	0.0	3.6	0.3	8.7	1.6	-6.3	2.0	3.0	4.0	-4.0	-3.0	
Other 3/	0.1	1.5	2.3	1.7	2.3	0.5	9.4	-0.6	1.1	-0.7	2.5	6.5	-4.5	-2.0	2.5	
Cash operating balance, end of period	21.0	15.0	15.0	15.0	15.0	12.3	12.0	12.3	10.7	17.0	15.0	12.0	8.0	12.0	15.0	
Memo: Sponsored agency borrowing 4/	21.4	18.2	27.8	24.9	23.2	24.3	25.3	9.0	3.6	9.5	5.7	6.5	5.7	5.5	5.5	
NIA Budget								Seasonally adjusted annual rates								
Receipts	527.3	609.5	615.5	665.0	645.4	540.8	631.6	573.2	620.7	626.0	642.2	637.5	645.8	657.3	641.0	
Expenditures	578.2	663.1	667.7	707.1	735.4	602.0	686.5	641.1	664.0	668.2	697.7	716.0	726.8	737.4	761.3	
Purchases	190.2	216.6	218.9	244.7	243.0	198.9	224.7	212.0	221.6	218.3	223.8	234.9	240.8	245.7	250.8	
Defense	126.1	148.2	146.6	172.9	168.9	131.7	151.7	141.6	145.2	147.9	151.9	161.6	166.5	171.5	176.2	
Nondefense	64.1	68.4	72.3	71.8	74.1	67.2	73.0	70.4	76.4	70.4	71.9	73.3	74.3	74.2	74.6	
All other expenditures	388.0	446.5	448.8	426.4	492.4	403.1	461.8	429.1	442.4	449.9	473.9	481.1	486.0	491.7	510.5	
Surplus(+)/deficit(-)	-50.9	-53.6	-52.2	-42.1	-90.0	-61.2	-54.9	-67.9	-43.3	-42.2	-55.5	-78.5	-81.0	-80.1	-120.3	
High Employment (H.E.) surplus(+)/deficit(-) evaluated at H.E. unemployment rate of:																
5.1 percent	-16.7	n.a.	0.8	n.a.	-13.8	-18.3	0.8	-13.4	3.6	9.6	3.4	-13.3	-6.7	1.9	-36.8	
6.1 percent	-39.5	n.a.	-25.0	n.a.	-41.7	-41.7	-25.7	-37.8	-21.8	-16.6	-23.7	-40.8	-34.8	-26.6	-64.7	
		*-actual		e--estimated			n.a.--not available									

1. Fiscal Year 1982 Budget Revisions, March 1982. In its report on the First Concurrent Resolution for FY 1982, the Congress recommended receipts of \$657.8 billion and outlays of \$695.5 billion. The revised Budget Resolution for FY1981 recommended receipts of \$603.3 billion and outlays of \$661.4 billion.
2. Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, and Rural Telephone Bank.
3. Checks issued less checks paid, accrued items and other transactions.
4. FRB staff estimates include Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives marketable debt on an offerings basis.

DOMESTIC FINANCIAL DEVELOPMENTS

Summary. Interest rates have declined since the mid-May FOMC meeting, in response to incoming data indicating soft economic activity, reduced inflation and weak money growth. While the federal funds rate has been slow to respond, market participants have been anticipating a more marked decline, and other short-term market interest rates have come down between 1-1/2 and 2-1/2 percentage points since their early May highs. By contrast, the bank prime rate of 20 percent is now 1 percentage point above its early-May level. Treasury and corporate bond yields have declined 1 to 1-1/2 percentage points from all-time highs in early May. The primary rate on conventional fixed rate home mortgages, which tends to lag, has edged down only slightly in recent weeks from an unprecedented level.

M1-B, adjusted for shifts into NOW accounts, appears to have declined by more than 5 percent at an annual rate in May and June. The earlier rapid growth of other checkable deposits ceased on balance over the two months. However, an expanded survey by the Survey Research Center of the University of Michigan during June suggested that households continued to open new accounts, albeit at a reduced pace. The second-quarter growth of shift-adjusted M1-B of 5-3/4 percent again fell short of the increase implied by historical money demand relationships with income and interest rates, but the shortfall was considerably less than in the first quarter.

Expansion in M2 was markedly slower during May and June, owing mainly to the weakness in M1-B. In addition, inflows to money market mutual funds slackened in May as yields on these instruments exhibited a typical lagged response to the previous rise in market rates. A resumption of sizable outflows from savings accounts at commercial banks and thrift institutions

was more than offset by an acceleration in small time deposits bearing market-related interest rates. Rapid growth of M3 was sustained over the two months by heavy issuance of large CDs, principally by commercial banks.

Business borrowing in short-term markets apparently was boosted by inventory accumulation that, along with large tax payments, heightened needs for external financing. Nonfinancial businesses tapped large commercial banks and particularly the commercial paper market in large volume. Perhaps in anticipation of near-term improvements in market conditions, they cut back on longer-term offerings, despite their continuing desire for balance sheet restructuring. Besides the record ratio of short-term to total debt at nonfinancial corporations, other signs that businesses are experiencing financial stress have emerged, including higher bankruptcy filings this spring and mounting failures. Moreover, downgradings of corporate bond ratings continue to exceed upgradings. Negative ratings actions on commercial paper have been less pronounced, with savings and loan associations accounting for two-fifths of the adverse changes so far this year.

S&Ls generally have experienced earnings difficulties and are estimated on average to have sustained losses over the first half of the year, joining MSBs, whose average net income was negative during 1980 as well. Sluggish deposit flows and high costs of funds have made thrift institutions cautious in their mortgage lending, and high mortgage rates damped loan demand. At S&Ls, new mortgage commitments fell sharply in May, pulling the volume of commitments outstanding down further; net acquisitions of mortgages stayed at about a reduced \$2 billion. Similarly, federally related lending remained well below levels attained last fall. However, financings

through buydown arrangements and loan assumptions, as well as earlier issues of tax-exempt bonds, have provided some support to the market.

Consumer installment credit growth probably slowed in May and June, judging by evidence on consumer spending. This presumption is supported by a renewed decline in consumer credit outstanding at commercial banks in May and by little change apparent in preliminary data for large banks in June.

Government borrowing has fallen off on balance since mid-May, as the Treasury has raised essentially no new money. However, funds raised by state and local governments have remained fairly sizable, and borrowing by federally sponsored credit agencies has surged.

Outlook. Although short-term interest rates may soften further in the very near term, the staff expects credit market conditions to firm again as the summer progresses. The demand for narrow money is likely to begin expanding more in line with the growth of nominal GNP than in the first half, boosting demands for reserves. Fairly strong growth of the broader monetary aggregates also is anticipated. Commercial banks may need to rely significantly on managed liabilities to finance fairly buoyant bank credit expansion. Substantial business borrowing at banks as well as in the commercial paper market appears in prospect as a side-effect of the reluctance of corporations to issue longer-term debt in an environment of continued high bond rates.

The turnabout in Treasury financing needs will also work to firm interest rates over the summer. The Treasury is expected to raise about \$15-1/2 billion in new money over the next three months, mainly through coupon issues. On the other hand, federal agency and state and local government borrowing is projected to remain near the pace of recent months.

Despite the substantial current spread of the primary conventional mortgage rate over corporate bond rates, there appears to be little likelihood of any significant reduction in primary mortgage rates. Taut conditions in this market are likely to persist, particularly at thrift institutions, and any pickup in overall mortgage flows is likely to be small.

Summary. The weighted-average exchange value of the dollar has appreciated a further 4-1/2 percent since the May Greenbook, registering a cumulative rise of 25 percent over the past year. In the recent period sterling has shown the largest depreciation against the dollar, with most currencies depreciating more moderately. The sharp rise of the dollar through early June occurred despite a drop in the spread of U.S. short-term interest rates over foreign rates, and reflected various downward influences on other currencies. Sterling was affected especially by the declining world price of oil; among the EMS currencies, the German mark was weakened by internal political difficulties and continued apprehension about the situation of Poland; and selling pressure on the French franc was heavy after the French election on May 10, before being reversed after the new French government announced a package of support measures on May 22.

Gold prices have declined nearly 15 percent since the May Greenbook--to about \$425 per ounce--and the price of silver has dropped sharply to around \$8.50 per ounce.

Economic activity in the major foreign industrial economies remains relatively weak on balance, though recent data for some countries

suggest an improving trend. In both Germany and Japan the pace of activity was stepped up in the first quarter, though consumer demand in both countries was weak. In the U.K. industrial production data through April suggest some bottoming out from a prolonged slump in activity, and recent surveys in France seem to indicate that activity may have stabilized after a weak first quarter. In Italy and Canada real growth was positive in the first quarter but slower than strong fourth-quarter results.

Unemployment remains at high and rising levels in all these countries, and no significant change in inflation rates has emerged on average. Further progress in reducing the large current-account deficits of most industrial countries has been uneven. There have been few important policy changes; in France the new socialist government has begun to introduce its new program, and in Italy an import deposit scheme was introduced.

The sharp rise in interest rates on dollar-denominated assets in early May, together with market expectations of a strong dollar, created conditions for a sizable net flow of private capital to the U.S. As noted above, foreign authorities resisted the pressure on their currencies by large sales of dollars, of which a large part was financed by the liquidation of U.S. Treasury securities; the daily average of banks' net borrowings from affiliated foreign offices rose by about \$9 billion. As the interest rate differential declined from its May peak some reversals of these private inflows occurred and official intervention sales of dollar assets slackened. Official inflows from OPEC countries were again substantial in April, but appear to be minor in May and early June.

Foreign net purchases of U.S. stocks in April were maintained at about the high \$600 million monthly average of the preceding six months.

The U.S. current account surplus rose to a \$12.3 billion annual rate in the first quarter; the deficit on merchandise trade was less than in the fourth quarter of 1980, while the surplus on other current transactions rose slightly. Included in these "other" transactions was a rise in investment income offset by a substantial jump in net tourist expenditures. The trade deficit rose to a \$30 billion rate (international transactions basis) in April-May, although the value of oil imports was held down by a 10 percent drop in volume compared with the first quarter. Exports of most commodities were sluggish, and coal exports were down sharply as a result of the strike. Imports, apart from oil, rose moderately in April-May over the first quarter rate.

Outlook. Since the previous Greenbook several elements in the outlook have changed, tending, on balance, to raise the staff estimate of the trade deficit this year and in 1982. Some gain is expected from lower import prices for oil and other basic commodities and from some improvement in U.S. price performance compared with other countries. However, this is more than offset by the effects of a higher average value for the U.S. dollar, which has a sizable impact in 1982, somewhat stronger U.S. economic activity, and a moderate reduction in agricultural exports (primarily lower prices) compared with the earlier projection. With these changes, the trade deficit is expected to rise to about \$27 billion this year, and to \$52 billion in 1982. Net receipts from investment income and other service transactions are not expected to rise significantly over the projection period, so that the current-account

deficit is now projected to rise to about \$25 billion in 1982, after near balance in 1981.

The outlook for economic activity in other countries is for continued weakness this year, as monetary and fiscal policies feature restraint, with a slow recovery starting in the second half and continuing into 1982. Consumer price pressure should moderate by the second half of 1981, but is expected to remain at about the same level in 1982 as is projected for the United States. Some lessening of the current-account deficits of the major industrial countries should occur as the counterpart of a rising U.S. deficit and a declining OPEC surplus. Relatively high U.S. interest rates, together with specific factors depressing some foreign currencies, have contributed to sustained strength for the U.S. dollar. In the period immediately ahead these factors are expected to support the dollar near the recent average. However, as the higher dollar begins to have a noticeable negative impact on the trade and current-account balances in 1982, while some other countries show gains, the staff expects a substantial decline in the dollar's value.

	1980 ANN.	1981 ANN.	1982 ANN.	1981 Q I	1981 Q II	1981 Q III	1981 Q IV	1982 Q I	1982 Q II	1982 Q III	1982 Q IV
1. GNP NET EXPORTS											
CURRENT \$, NET	23.3	23.8	4.3	29.2	25.1	20.8	20.3	14.2	7.8	-.1	-4.9
EXPORTS OF G&S	339.8	377.4	400.0	367.4	373.6	380.4	388.1	393.0	398.0	401.7	407.3
IMPORTS OF G&S	316.5	353.5	395.7	338.2	348.6	359.7	367.7	378.8	390.2	401.8	412.2
CONSTANT 72 \$, NET	52.0	48.1	39.2	50.9	49.8	46.9	44.9	42.3	40.1	37.8	36.4
EXPORTS OF G&S	161.1	165.0	165.1	162.5	164.3	166.2	167.1	166.4	165.7	164.5	163.7
IMPORTS OF G&S	109.1	116.9	125.9	111.6	114.5	119.4	122.2	124.1	125.6	126.7	127.3
TERMS OF TRADE (1972=100) 1/	72.7	75.6	77.1	74.6	74.7	75.9	77.1	77.4	77.3	77.0	76.8
2. U.S. MERCHANDISE TRADE BALANCE 2/											
EXPORTS (EXCL. MILITARY)	224.0	243.8	244.7	244.5	244.0	243.0	243.8	243.2	243.8	244.7	247.3
AGRICULTURAL	42.2	47.5	51.0	50.9	46.0	46.0	47.1	49.1	50.4	51.5	52.9
NONAGRICULTURAL	181.7	196.3	193.8	193.5	198.0	197.0	196.6	194.2	193.4	193.3	194.4
IMPORTS	249.3	271.2	296.8	262.9	269.2	274.5	278.2	285.1	292.0	301.0	309.2
PETROLEUM AND PRODUCTS	78.9	83.0	81.8	83.3	84.2	83.5	81.0	80.3	81.2	82.7	83.2
NONPETROLEUM	170.4	188.2	215.0	179.6	185.0	191.0	197.2	204.8	210.8	218.2	226.0
3. U.S. CURRENT ACCOUNT BALANCE											
OF WHICH: NET INVESTMENT INCOME	3.7	1.8	-25.0	12.3	3.8	-2.9	-6.1	-13.5	-20.8	-29.8	-35.7
4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/											
REAL GNP, % CHANGE, ANNUAL RATES	.3	1.1	2.5	1.5	.4	1.0	1.7	2.2	2.4	2.7	2.8
CONSUMER PRICES, 4/, % CHANGE, ANNUAL RATES	10.3	9.1	7.5	10.7	10.4	7.9	7.6	7.9	7.9	7.1	7.2

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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 -- PERCENT 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.