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CONFIDENTIAL (FR)

April 12, 1978

SUMMARY AND OUTLOOK

By the Staff
Board of Governors
of the Federal Reserve System

SUMMARY AND OUTLOOK

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary. Economic activity continued to rebound in March as employment, industrial production and retail sales posted further sizable advances. Growth for the first quarter as a whole, however, now appears to have been smaller as a result not only of the sharp deterioration of the Nation's foreign trade position but also because of temporary losses arising from bad weather and the coal strike. At the same time, the inflation rate worsened as diminishing supplies brought on particularly sharp mark-ups in meat prices and as increases in payroll tax costs and in the minimum wage began to be reflected in prices generally.

Demands for labor have been unusually strong recently. For the first quarter as a whole, total employment rose nearly 1 million and the unemployment rate fell 0.4 percentage point to 6.2 per cent. In March, nonfarm payroll jobs rose by 450,000, with three-fourths of the industry groups reporting gains. Manufacturers added 75,000 jobs over the month and the factory workweek rebounded by half an hour, recovering to the average for the final quarter of 1977.

Industrial production also exhibited considerable strength in March. Auto production rose about 13 per cent and output of other consumer goods and business equipment is estimated to have advanced sharply. Production of most materials other than coal evidently rose markedly in March, while coal output continued to be depressed by the strike. Over-all industrial production is estimated to have risen about 1-1/2 per cent from February.

Total retail sales rose strongly in February (upward revised) and March. But because of the weakness in January, which was related in part to bad weather, such sales were about unchanged between the fourth quarter of 1977 and the first quarter of 1978. Auto sales were at a 12.0 million unit annual rate in March--up more than 1.5 million units from February. The selling pace apparently was boosted by major sales contests as well as by purchases that had been deferred during bad weather. Gains in retail sales excluding autos and nonconsumption items were widespread by type of store.

Inventory accumulation picked up early this year, following the very low rates of investment late in 1977. The book value of manufacturers' inventories rose at about a \$16 billion annual rate over the first two months, after a fourth quarter rate of about \$3 billion. Accumulation would have been even larger had it not been for substantial liquidation of coal stocks during the strike.

Outlays for business fixed capital early this year remained below levels in late 1977, as the severe weather interrupted activity. In February, nondefense capital goods shipments recovered most of the January decline, and the average value of nonresidential building put-in-place in the first two months of 1978 was slightly below the average level in the final quarter of 1977. Indicators of future capital outlays continued to trend upward. New orders for nondefense capital goods rose 7 per cent in February to a level well above the rate for late 1977, and the value of contracts for private nonresidential projects increased sharply further.

Activity in the housing sector weakened in the first quarter after a robust performance in the closing months of 1977. During January and February starts of both single-family and multifamily units were substantially below the fourth-quarter pace. According to newly revised data, sales of new homes in the first two months of 1978 were down 8-1/2 per cent from the advanced fourth-quarter pace. Bad weather was apparently a key factor in the softness in both starts and sales.

Growth in economic activity in the first quarter was also limited by small increases in government purchases. Growth of Federal NIA purchases during the first quarter of 1978 was below Administration expectations, mainly because of sharply reduced payments by the Commodity Credit Corporation and continued slow growth in outlays for the strategic petroleum reserve program. State and local construction activity continued to be curtailed by bad weather in February. However, employment picked up further in March, reflecting the final stages of the build-up in the public service employment program.

Prices have continued to rise at a rapid pace in recent months. Wholesale prices of finished goods rose at a 7-1/4 per cent annual rate in March, as nonfood finished goods increased at a 6 per cent rate while finished food products rose at a 9-1/2 per cent rate. Wholesale finished goods prices increased at a 9-1/2 per cent annual rate over the three months ending in March. Consumer prices, paced by large increases for food as well as a very sharp rise in natural gas and electricity rates, rose at a 7-1/4 per cent annual rate in February; these prices moved up at about an 8-1/2 per

cent rate over the first two months of 1978, almost twice as fast as over the last half of 1977.

Outlook. The staff has reduced its estimate of real GNP growth in the first quarter of 1978 to about an 1-1/2 per cent annual rate, mainly because recent data indicate that net exports have been substantially weaker than had been expected. In addition, there are indications that adverse weather curtailed private and public construction activity more than was previously thought.

The fiscal and monetary policy assumptions underlying the staff projections are essentially unchanged from last month. The staff continues to assume that a \$25 billion tax cut will take effect on October 1 of this year with about two-thirds of it accruing to individuals. Federal outlays in FY 1978 are still expected to be around \$455 billion, while projected outlays in FY 1979 have been raised slightly to just over \$500 billion. We continue to assume a 5-1/4 per cent annual growth rate of M-1 through 1979:QII. Short-term interest rates are assumed to rise substantially over the spring and summer months. In the international sector, the trade-weighted exchange rate for the dollar is now assumed to decline further from the March level.

Following a strong weather-related rebound now indicated in the second quarter, growth in real GNP over the ensuing four quarters is projected to average almost 4-1/2 per cent, fractionally less than expected last month. As is explained in the International Developments section, the deterioration of the trade balance has placed more of a drag on aggregate

activity. Because of the resulting loss of domestic income growth, consumption is projected to rise somewhat more slowly.

The business sector continues to be a source of strength, with real fixed investment growth projected to average 6-1/4 per cent (annual rate) from mid-1978 to mid-1979. Residential building activity, on the other hand, still is expected to decline significantly during this period, mainly reflecting less accommodative mortgage market conditions.

Employment gains are also expected to be somewhat smaller. Growth of nonfarm payroll employment is projected to be at a 2.9 per cent annual rate over the impending five quarters; over the last four quarters, employment rose by 3.9 per cent. With employment growth slowing, the improvement in unemployment appears likely to be moderate; the over-all jobless rate is now projected to decline less than half a percentage point to 5.8 per cent in the second quarter of 1979, in contrast to the decline of 1.2 percentage points over the last year. Our projections of wage increases have been raised--in part because of the run-up of consumer prices--and, as a result, the projected rise of unit labor costs is somewhat larger.

The staff also is now projecting a higher rate of inflation. Over the six quarters through mid-1979, the fixed-weighted price index for gross business product is projected to rise at a 7 per cent annual rate, about 1/2 percentage point faster than last month. The recent weakening of the dollar and the anticipated further depreciation are expected to put upward pressure on prices of imports and the domestic goods with which they compete. In addition, the projected rise in food prices has been raised further,

mainly because estimates of meat supplies have been reduced. (See Appendix A.)

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

STAFF GNP PROJECTIONS

	Per cent changes, annual rate							
	Nominal GNP		Real GNP		Gross business product fixed-weighted price index		Unemployment rate (per cent)	
	3/15/78	4/12/78	3/15/78	4/12/78	3/15/78	4/12/78	3/15/78	4/12/78
1974 ^{1/}	8.1	8.1	-1.4	-1.4	10.4	10.4	5.6	5.6
1975 ^{1/}	8.2	8.2	-1.3	-1.3	9.5	9.5	8.5	8.5
1976 ^{1/}	11.6	11.6	6.0	6.0	5.4	5.4	7.7	7.7
1977 ^{1/}	10.8	10.7	4.9	4.9	6.0	6.0	7.0	7.0
1978	11.1	11.1	4.4	4.2	6.4	6.6	6.0	6.0
1977-III ^{1/}	10.2	10.2	5.1	5.1	5.0	5.0	6.9	6.9
1977-IV ^{1/}	10.4	9.9	4.0	3.8	5.5	5.4	6.6	6.6
1978-I	11.1	8.7	3.4	1.4	7.3	7.4	6.2	6.2
1978-II	11.6	14.5	5.0	6.7	6.7	7.3	6.0	6.0
1978-III	10.6	11.4	4.5	4.4	6.2	6.8	6.0	6.0
1978-IV	11.8	12.0	4.8	4.6	6.2	6.8	5.9	5.9
1979-I	11.7	11.9	4.9	4.6	6.7	7.4	5.8	5.8
1979-II	10.8	10.8	4.4	4.1	6.4	7.0	5.7	5.8
Change:								
76-IV to 77-IV ^{1/}	11.9	11.8	5.7	5.7	6.2	6.1	-1.2	-1.2
77-II to 78-II	10.8	10.8	4.4	4.2	6.1	6.3	-1.1	-1.1
77-IV to 78-IV	11.3	11.6	4.4	4.2	6.6	7.1	-.7	-.7
78-II to 79-II	11.2	11.5	4.6	4.4	6.4	7.0	-.3	-.2

^{1/} Actual.

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

	1977		1978				1979	
	III	IV	I	II	Projected III	Projected IV	I	II
Gross National Product	1915.9	1961.8	2003.3	2072.5	2129.0	2190.1	2252.3	2310.8
Final purchases	1892.2	1948.2	1983.3	2048.0	2103.5	2163.1	2222.0	2279.3
Private	1491.3	1534.4	1563.8	1617.5	1661.5	1707.2	1755.6	1801.8
Excluding net exports	1498.8	1552.6	1583.3	1631.9	1672.7	1720.2	1767.9	1814.5
Personal consumption expenditures	1218.9	1259.5	1284.1	1319.8	1352.6	1392.3	1431.5	1468.9
Goods	659.4	685.9	691.4	710.6	728.7	751.1	771.3	789.6
Services	559.5	573.7	592.7	609.2	623.9	641.2	660.2	679.3
Gross private domestic investment	303.6	306.7	319.2	336.6	345.6	354.9	366.7	377.1
Residential construction	92.5	99.7	100.7	105.7	106.7	107.2	108.2	109.7
Business fixed investment	187.5	193.5	198.5	206.4	213.4	220.7	228.2	235.9
Change in business inventories	23.6	13.5	20.0	24.5	25.5	27.0	30.3	31.5
Nonfarm	23.1	9.0	18.0	23.5	25.5	27.0	30.3	31.5
Net exports of goods and services ^{1/}	-7.5	-18.2	-19.5	-14.4	-11.2	-13.0	-12.3	-12.7
Exports	179.9	170.6	180.4	190.9	200.3	207.5	218.0	223.9
Imports	187.4	188.8	199.9	205.3	211.5	220.5	230.3	236.6
Gov't. purchases of goods and services	400.9	413.8	419.5	430.5	442.0	455.9	466.4	477.5
Federal 2/	148.1	153.8	154.6	156.7	160.9	167.5	170.9	174.9
State and local	252.9	260.0	264.9	273.8	281.1	288.4	295.5	302.6
Gross national product in constant (1972) dollars	1347.4	1360.2	1365.0	1387.2	1402.1	1418.0	1434.0	1448.6
Personal income	1549.8	1603.0	1637.6	1684.5	1732.7	1779.8	1824.1	1868.4
Wage and salary disbursements	998.9	1029.1	1056.0	1084.7	1110.7	1140.1	1172.4	1200.9
Disposable income	1323.8	1368.3	1399.9	1437.4	1475.7	1529.5	1569.7	1605.6
Saving rate (per cent)	5.5	5.6	5.8	5.7	5.9	6.6	6.4	6.1
Corporate profits with I.V.A. and C.C. Adj.	149.0	144.5	138.9	154.1	158.0	168.4	167.8	171.1
Corporate profits before tax	172.8	178.0	180.3	192.6	195.6	206.2	206.1	209.9
Federal government surplus or deficit (-) (N.I.A. basis)	-58.9	-60.1	-55.3	-48.4	-45.5	-62.3	-54.8	-48.7
High employment surplus or deficit (-)	-20.4	-22.1	-13.5	-11.5	-8.1	-28.2	-19.7	-13.0
State and local government surplus or deficit (-) (N.I.A. basis)	32.9	31.1	29.8	29.6	27.4	27.4	26.0	24.1
Excluding social insurance funds	17.4	15.4	12.3	11.6	8.9	8.4	6.5	4.1
Civilian labor force (millions)	97.6	98.6	99.2	99.8	100.3	100.9	101.5	102.0
Unemployment rate (per cent)	6.9	6.6	6.2	6.0	6.0	5.9	5.8	5.8
Nonfarm payroll employment (millions)	82.5	83.2	84.1	84.9	85.4	86.0	86.6	87.2
Manufacturing	19.6	19.8	20.1	20.3	20.5	20.7	20.9	21.2
Industrial production (1967=100)	138.4	139.3	139.7	143.1	145.5	148.2	150.9	153.1
Capacity utilization: all manufacturing (per cent)	83.0	82.9	82.2	83.5	84.3	85.0	85.7	86.1
Materials (per cent)	82.3	82.2	81.6	83.3	84.2	85.1	86.1	86.7
Housing starts; private (millions, A.R.)	2.04	2.15	1.75	2.05	1.85	1.80	1.80	1.80
Sales new autos, (millions, A.R.)	10.92	10.75	10.80	10.85	10.90	11.05	11.10	10.95
Domestic models	8.88	8.77	8.80	8.75	8.90	9.10	9.15	9.10
Foreign models	2.04	1.98	2.00	2.10	2.00	1.95	1.95	1.85

1/ Balance of payments data and projection underlying these estimates are shown in the International Development 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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CLASS II FOMCCHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1977		1978				1979	
	III	IV	I	II	Projected		I	II
					III	IV		
----- Billions of dollars -----								
Gross National Product	46.0	45.9	41.5	69.2	56.5	61.1	62.2	58.5
Inventory change	1.9	-10.1	6.5	4.5	1.0	1.5	3.3	1.2
Final purchases	44.0	56.0	35.0	64.7	55.5	59.6	58.9	57.3
Private	33.7	43.1	29.3	53.7	44.0	45.7	48.4	46.2
Net exports	2.2	-10.7	-1.3	5.1	3.2	-1.8	.7	-.4
Excluding net exports	31.5	53.8	30.6	48.6	40.8	47.5	47.7	46.6
Personal consumption expenditures	24.9	40.6	24.6	35.7	32.8	39.7	39.2	37.4
Goods	6.4	26.5	5.5	19.2	18.1	22.4	20.2	18.3
Services	18.4	14.2	19.0	16.5	14.7	17.3	19.0	19.1
Residential fixed investment	1.7	7.2	1.0	5.0	1.0	.5	1.0	1.5
Business fixed investment	5.1	6.0	5.0	7.9	7.0	7.3	7.5	7.7
Government	10.3	12.9	5.7	11.0	11.5	13.9	10.5	11.1
Federal	4.5	5.7	.8	2.1	4.2	6.6	3.4	4.0
State and local	5.9	7.1	4.9	8.9	7.3	7.3	7.1	7.1
GNP in constant (1972) dollars	16.7	12.8	4.8	22.2	14.9	15.9	16.0	14.6
Final purchases	14.3	19.7	.6	19.3	14.1	15.1	14.1	13.3
Private	10.3	16.7	.9	16.2	10.8	12.4	11.9	10.6
----- In Per Cent Per Year ^{1/} -----								
Gross National Product	10.2	9.9	8.7	14.5	11.4	12.0	11.9	10.8
Final purchases	9.9	12.4	7.4	13.7	11.3	11.8	11.3	10.7
Private	9.6	12.1	7.9	14.5	11.3	11.5	11.8	10.9
Personal consumption expenditures	8.6	14.0	8.0	11.6	10.3	12.3	11.7	10.9
Goods	4.0	17.0	3.3	11.6	10.6	12.9	11.2	9.8
Services	14.3	10.5	14.0	11.6	10.0	11.6	12.4	12.1
Gross private domestic investment	12.4	4.1	17.3	23.7	11.1	11.2	14.0	11.8
Residential structures	7.7	35.0	4.1	21.4	3.8	1.9	3.8	5.7
Business fixed investment	11.6	13.4	10.7	16.9	14.3	14.4	14.3	14.2
Gov't. purchases of goods and services	11.0	13.5	5.6	10.9	11.1	13.2	9.5	9.9
Federal	12.9	16.3	2.1	5.5	11.2	17.4	8.4	9.7
State and local	9.9	11.8	7.8	14.1	11.1	10.8	10.2	10.0
GNP in constant (1972) dollars	5.1	3.8	1.4	6.7	4.4	4.6	4.6	4.1
Final purchases	4.4	6.1	.2	5.8	4.2	4.4	4.1	3.8
Private	4.0	6.5	.3	6.2	4.0	4.6	4.4	3.8
GNP implicit deflator ^{2/}	4.8	5.9	7.2	7.4	6.7	7.1	6.9	6.4
Gross business product fixed-weight price index ^{3/}	5.0	5.4	7.4	7.3	6.8	6.8	7.4	7.0
Personal income	8.9	14.5	8.9	12.0	12.0	11.3	10.3	10.1
Wage and salary disbursements	7.5	12.7	10.9	11.3	9.9	11.0	11.8	10.1
Disposable income	10.0	14.1	9.5	11.2	11.1	15.4	10.9	9.5
Corporate profits before tax	-2.7	12.6	5.1	30.3	6.5	23.3	-.1	7.6
Nonfarm payroll employment	3.3	3.2	4.4	4.0	2.2	2.9	2.8	2.9
Manufacturing	1.3	2.7	6.4	4.2	4.4	4.5	4.4	4.1
Nonfarm business sector								
Output per hour	3.8	.5	-.3	3.1	2.6	2.4	2.4	2.0
Compensation per hour	7.5	7.3	11.5	7.9	8.2	8.3	11.6	8.2
Unit labor costs	3.5	6.8	11.8	4.8	5.6	5.9	9.2	6.2
Industrial production	4.2	2.6	1.2	10.1	6.9	7.6	7.5	6.0
Housing starts, private	22.1	22.3	-55.8	88.3	-33.7	-10.4	.0	.0
Sales new autos	-24.1	-6.2	2.0	1.8	1.9	5.6	1.8	-5.3
domestic models	-18.4	-4.8	1.4	-2.4	7.0	9.3	2.2	-2.2
foreign models	-43.9	-12.3	4.7	21.6	-17.7	-9.6	.0	-19.0

^{1/} Percentage rates are annual rates compounded quarterly.^{2/} Excluding Federal pay increases rates of change are: 1977-IV, 5.1 per cent; 1978-I, 7.2 per cent; 1978-IV, 6.5 per cent; 1979-I, 6.9 per cent.^{3/} Using expenditures in 1972 as weights.

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CLASS II FOMC

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

April 12, 1978

	1971	1972	1973	1974	1975	1976	1977	Projected 1978
Gross National Product	1063.4	1171.1	1306.6	1412.9	1528.8	1706.5	1889.6	2098.7
Final purchases	1057.1	1161.7	1288.6	1404.0	1540.3	1693.1	1871.4	2074.5
Private	823.4	908.6	1019.1	1101.3	1201.4	1331.7	1476.4	1637.5
Excluding net exports	821.8	911.9	1012.0	1095.3	1181.0	1323.9	1487.3	1652.0
Personal consumption expenditures	668.2	733.0	809.9	889.6	980.4	1094.0	1211.2	1337.2
Goods	374.8	410.5	457.5	498.3	542.2	601.6	660.5	720.4
Services	293.4	322.4	352.3	391.3	438.2	492.3	550.7	616.7
Gross private domestic investment	160.0	188.3	220.0	214.6	189.1	243.3	294.2	339.1
Residential construction	49.6	62.0	66.1	55.1	51.5	68.0	91.0	105.1
Business fixed investment	104.1	116.8	136.0	150.6	149.1	161.9	185.1	209.7
Change in business inventories	6.4	9.4	17.9	8.9	-11.5	13.3	18.2	24.2
Nonfarm	5.1	8.8	14.7	10.8	-15.1	14.9	17.1	23.5
Net exports of goods and services	1.6	-3.3	7.1	6.0	20.4	7.8	-10.9	-14.5
Exports	65.6	72.7	101.6	137.9	147.3	162.9	174.7	194.8
Imports	64.0	75.9	94.4	131.9	126.9	155.1	185.6	209.3
Gov't. purchases of goods and services	233.7	253.1	269.5	302.7	338.9	361.4	395.0	437.0
Federal	96.2	102.1	102.2	111.1	123.3	130.1	145.4	159.9
State and local	137.5	151.0	167.3	191.5	215.6	231.2	249.6	277.0
Gross national product in constant (1972) dollars	1107.5	1171.1	1235.0	1217.8	1202.1	1274.7	1337.3	1393.1
Personal income	859.1	942.5	1052.4	1154.9	1253.4	1382.7	1536.7	1708.6
Wage and salary disbursements	579.4	633.8	701.3	764.6	805.7	891.8	990.0	1097.9
Disposable income	742.8	801.3	901.7	984.6	1084.4	1185.8	1309.2	1460.6
Saving rate (per cent)	7.7	6.2	7.8	7.3	7.4	5.6	5.1	6.0
Corporate profits with I.V.A. and C.C. Adj.	77.2	92.1	99.1	83.6	99.3	128.1	139.8	154.8
Corporate profits before tax	82.0	96.2	115.8	126.9	123.5	156.9	171.6	193.7
Federal government surplus or deficit (-) (N.I.A. basis)	-22.0	-17.3	-6.7	-10.7	-70.2	-54.0	-49.5	-52.9
High employment surplus or deficit (-)	-5.3	-5.9	-.7	17.1	-20.3	-10.4	-8.7	-15.3
State and local government surplus or deficit (-) (N.I.A. basis)	3.7	13.7	13.0	7.5	5.9	18.4	29.2	28.6
Excluding social insurance funds	-3.8	5.6	4.1	-2.9	-6.2	3.9	13.7	10.3
Civilian labor force (millions)	84.1	86.5	88.7	91.0	92.6	94.8	97.4	100.0
Unemployment rate (per cent)	5.9	5.6	4.9	5.6	8.5	7.7	7.0	6.0
Nonfarm payroll employment (millions)	71.2	73.7	76.9	78.4	77.1	79.4	82.1	85.1
Manufacturing	18.6	19.1	20.1	20.0	18.3	19.0	19.6	20.4
Industrial production (1967=100)	109.6	119.7	129.8	129.3	117.8	129.8	137.0	144.1
Capacity utilization: all manufacturing (per cent)	78.0	83.1	87.5	84.2	73.6	80.2	82.4	83.8
Materials (per cent)	83.1	88.0	92.4	87.7	73.6	80.4	81.9	83.5
Housing starts, private (millions, A.R.)	2.05	2.36	2.05	1.34	1.16	1.54	1.19	1.86
Sales new autos (millions, A.R.)	10.24	10.93	11.42	8.91	8.66	10.12	11.13	10.90
Domestic models	8.68	9.32	9.65	7.49	7.08	8.63	9.07	8.89
Foreign models	1.56	1.61	1.77	1.42	1.58	1.50	2.06	2.01

April 12, 1978

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

	1971	1972	1973	1974	1975	1976	1977	Projected 1978
-----Billions of Dollars-----								
Gross National Product	81.0	107.7	135.5	106.3	115.9	177.7	183.1	209.1
Inventory change	2.6	3.0	8.5	-9.0	-20.4	24.8	4.9	6.0
Final purchases	78.5	104.6	126.9	115.4	136.3	152.8	178.3	203.1
Private	63.7	85.2	110.5	82.2	100.1	130.3	144.7	161.1
Net exports	-2.3	-4.9	10.4	-1.1	14.4	-12.6	-18.7	-3.6
Excluding net exports	66.0	90.1	100.1	83.3	85.7	142.9	163.4	164.7
Personal consumption expenditures	49.4	64.8	76.9	79.7	90.8	133.6	117.2	126.0
Goods	25.2	35.7	47.0	40.8	43.9	59.4	58.9	59.9
Services	24.3	29.0	29.9	39.0	46.9	54.1	58.4	66.0
Residential fixed investment	13.0	12.4	4.1	-11.0	-3.6	16.5	23.0	14.1
Business fixed investment	3.6	12.7	19.2	14.6	-1.5	12.8	23.2	24.6
Government	14.8	19.4	16.4	33.2	36.2	22.5	33.6	42.0
Federal	.6	5.9	.1	8.9	12.2	6.8	15.3	14.5
State and local	14.3	13.5	16.3	24.2	24.1	15.6	18.4	27.4
GNP in constant (1972) dollars	32.2	63.6	63.9	-17.2	-15.7	72.6	62.6	55.8
Final purchases	29.9	60.8	56.8	-8.6	2.1	54.2	59.3	51.9
Private	30.7	57.1	57.4	-13.8	-3.2	52.8	52.6	41.7
-----In Per Cent Per Year-----								
Gross National Product	8.2	10.1	11.6	8.1	8.2	11.6	10.7	11.1
Final purchases	8.0	9.9	10.9	8.9	9.7	9.9	10.5	10.9
Private	8.4	10.3	12.2	8.1	9.1	10.8	10.9	10.9
Personal consumption expenditures	8.0	9.7	10.5	9.8	10.2	11.6	10.7	10.4
Goods	7.2	9.5	11.4	8.9	8.8	11.0	9.8	9.1
Services	9.0	9.9	9.3	11.1	12.0	12.4	11.9	12.0
Gross private domestic investment	13.6	17.7	16.8	-2.5	-11.9	28.7	20.9	15.3
Residential structures	35.5	25.1	6.6	-16.7	-6.5	32.2	33.7	15.5
Business fixed investment	3.6	12.3	16.4	10.8	-1.0	8.6	14.3	13.3
Gov't. purchases of goods and services	6.8	8.3	6.5	12.3	12.0	6.6	9.3	10.6
Federal	.6	6.1	.1	8.7	11.0	5.5	11.8	10.0
State and local	11.6	9.8	10.8	14.5	12.6	7.2	7.9	11.0
GNP in constant (1972) dollars	3.0	5.7	5.5	-1.4	-1.3	6.0	4.9	4.2
Final purchases	2.8	5.5	4.9	-.7	.2	4.5	4.7	3.9
Private	3.7	6.7	6.3	-1.4	-.3	5.6	5.3	3.9
GNP implicit deflator	5.1	4.1	5.8	9.7	9.6	5.3	5.5	6.6
Gross business product fixed-weighted index ^{1/}	4.4	3.3	5.7	10.4	9.5	5.4	6.0	6.6
Personal income	7.2	9.7	11.7	9.7	8.5	10.3	11.1	11.2
Wage and salary disbursements	6.0	9.4	10.7	9.0	5.4	10.7	11.0	10.9
Disposable income	8.3	7.9	12.5	9.2	10.1	9.4	10.4	11.6
Corporate profits before tax	14.7	17.3	20.4	9.6	-2.7	27.0	9.4	12.9
Nonfarm payroll employment	.4	3.5	4.3	2.0	-1.7	3.1	3.4	3.6
Manufacturing	-4.0	2.8	5.1	-1	-8.5	3.3	3.2	4.3
Nonfarm business sector								
Output per hour	2.9	3.0	1.7	-2.9	1.6	4.1	2.1	1.6
Compensation per hour	6.6	5.8	7.8	9.4	9.6	8.7	8.7	8.7
Unit labor costs	3.5	2.7	6.0	12.7	7.9	4.5	6.4	7.0
Industrial production	1.7	9.2	8.4	-.4	-8.9	10.2	5.5	5.2
Housing starts	43.1	14.9	-13.2	-34.6	-13.3	32.5	29.3	-6.4
Sales new autos	21.9	6.8	-4.7	-14.5	-2.8	16.9	9.9	-2.0
Domestic models	21.9	7.4	3.5	-22.4	-5.5	21.9	5.1	-2.0
Foreign models	21.8	3.1	9.7	-19.9	11.4	-5.1	37.2	-2.1

^{1/} Using expenditures in 1972 as weights.

FEDERAL SECTOR ACCOUNTS
(billions of dollars)

April 12, 1978

	FY 1977*	FY 1978 e/		FY 1979 e/		CY77* F.R.	CY78e/ F.R.	F.R. Staff Estimates									
		Admin. 1/ 2/	F.R. Board	Admin. 1/	F.R. Board			Calendar quarters; unadjusted data									
								1977			1978			1979			
								III*	IV*	I	II	III	IV	I	II	III	
Unified budget receipts	356.9	400.5	399.0	439.8	441.0	365.2	409.3	91.3	84.5	85.2	123.5	105.8	94.8	96.9	133.4	115.9	
Unified budget outlays	401.9	453.5	454.6	499.4	500.4	416.1	464.3	103.4	113.3	109.8	113.9	117.6	123.0	121.5	125.6	130.3	
Surplus (+)/Deficit(-), unified budget	-45.0	-53.0	-55.6	-59.6	-59.4	-50.9	-55.0	-12.2	-28.8	-24.6	9.6	-11.8	-28.2	-24.6	7.8	-14.4	
Surplus(+)/Deficit(-), off-budget agencies 3/	-8.7	-11.5	-9.9	-12.5	-11.5	-10.4	-10.4	-4.9	-1.3	-3.3	-1.4	-4.0	-1.7	-3.9	-1.3	-4.6	
Means of financing combined deficits:																	
Net borrowing from public	53.5	58.8	55.3	74.7	72.9	56.8	62.9	19.6 ^{8/}	20.7 ^{8/}	20.8	1.3	12.5	28.3	27.5	-4.6	21.7	
Decrease in cash operating balance	-1.7	n.a.	7.1	0.0	0.0	-0.6	0.3	-2.8 ^{8/}	6.8 ^{8/}	5.9	-9.6	4.0	0	0	0	0	
Other 4/	1.9	n.a.	3.1	-2.6	-2.0	5.3	2.1	0.4	2.6	1.2	0	-0.7	1.6	1.0	-1.9	-2.7	
Cash operating balance, end of period	19.1	12.0	12.0	12.0	12.0	12.3	12.0	19.1 ^{8/}	12.3	6.4	16.0	12.0	12.0	12.0	12.0	12.0	
Memo: Sponsored agency borrowing 5/	5.2	n.a.	17.9	n.a.	12.9	6.8	18.3	1.1	2.0	4.5	5.4	6.0	2.4	2.5	3.5	4.5	
NIA Budget																	
								Seasonally adjusted annual rates									
Receipts	361.8 ^{6/}	n.a.	404.4 ^{6/}	n.a.	n.e.	373.9	417.3	373.2	386.1	395.8	411.6	431.1	430.6	445.2	458.7	n.e.	
Outlays	411.9	n.a.	458.5	n.a.	504.8	423.4	470.2	432.1	446.3	451.1	460.0	476.6	492.9	500.0	507.4	518.9	
Purchases (total)	140.6	n.a.	156.5	n.a.	172.6	145.5	159.9	148.1	153.8	154.6	156.7	160.9	167.5	170.9	174.9	177.2	
Defense	91.8	n.a.	99.7	n.a.	107.8	94.3	101.1	95.6	98.5	99.4	100.0	100.9	104.2	106.4	109.0	111.7	
Non-defense	48.8	n.a.	56.8	n.a.	64.8	51.2	58.8	52.5	55.3	55.2	56.7	60.0	63.3	64.5	65.9	65.5	
All other outlays	271.4 ^{6/}	n.a.	302.0 ^{6/}	n.a.	332.2	278.0	310.3	284.0	292.5	296.5	303.3	315.7	325.4	329.1	332.5	341.7	
Surplus(+)/Deficit (-)	-50.0 ^{6/}	n.a.	-54.1 ^{6/}	n.a.	n.e.	-49.5	-52.9	-58.9	-60.2	-55.3	-48.4	-45.5	-62.3	-54.8	-48.7	n.e.	
High Employment Surplus(+)/Deficit(-) (NIA basis) 7/	-5.0	n.a.	-13.8	n.a.	-15.8	-8.7	-15.3	-20.4	-22.1	-13.5	-11.5	-8.1	-28.2	-19.7	-13.0	-2.1	
	*actual	e--estimated	r--revised	n.e.--not estimated				n.a.--not available				p--preliminary					

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- 1/ The Budget of the United States Government, Fiscal Year 1979, January 1978 and OMB Current Budget Estimates, March 1978.
- 2/ The Second Concurrent Resolution on the Budget (September 15, 1977) set the Congressional receipt and outlay targets at \$397 and \$458.3 billion, respectively.
- 3/ Includes Federal Financing Bank, Postal Service, U.S. Railway Association, Rural Electrification and Telephone Revolving fund, Housing for the Elderly or Handicapped Fund (until October 1977), and Pension Benefit Guaranty Corporation.
- 4/ Checks issued less checks paid, accrued items and other transactions.
- 5/ Includes Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.
- 6/ Quarterly average exceeds fiscal year total by \$1.7 billion for FY 1977 and by \$1.8 billion for FY 1978 due to spreading of wage base effect over calendar year.
- 7/ Estimated by F.R.B. staff.
- 8/ Includes \$2.5 billion of borrowing from the Federal Reserve on September 30 which was repaid October 4.

Comments on the Fiscal Policy Outlook

The fiscal policy assumptions underlying the April forecast continue to incorporate a \$25 billion tax cut that becomes effective October 1, 1978. Although our tax assumptions remain unchanged, the receipts forecast for fiscal year 1978 has been raised slightly to \$399 billion, because of higher projected income levels. Federal spending for farm aid and the strategic petroleum reserve did not increase as much as expected during February. Consequently, total outlays for the current fiscal year (1978) have been lowered slightly to just under \$455 billion.

These estimates suggest a unified deficit in fiscal year 1978 of \$56 billion and a total deficit to be financed (unified plus off-budget) of \$65-1/2 billion. About \$10 billion of this deficit is expected to be financed through a run down of the exceptionally high cash balance that the Treasury had built up at the start of the fiscal year, and through other miscellaneous sources of financing. The remaining \$55-1/2 billion must be raised through security sales; of this amount, \$41-1/2 billion has already been raised during the first six months of the current fiscal year (through March 1978). Since April 1, the Treasury has issued \$6 billion of cash management bills set to mature shortly after the April tax date, and \$2.5 billion of 5-year notes. During the remainder of the current quarter (1978:2), seasonally high tax receipts will enable the Treasury to pay down around \$10 billion

in marketable debt, mostly Treasury bill. The staff, therefore, expects net borrowing from the public to total \$12-1/2 billion in the final quarter of the fiscal year (1978:3).

For fiscal year 1979, a deficit of \$59-1/2 billion is now forecast by the staff, about equal to the President's March estimate, but down slightly (\$1 billion) from last month. The staff's outlay projection for the fiscal year beginning October 1, has been revised upward from \$499 billion to \$500-1/2 billion, reflecting the impact of higher projected rates of inflation and unemployment on the budget. Moreover, the current (fiscal year 1978) spending shortfall in the strategic petroleum reserve program is expected to be made up by additional spending in fiscal year 1979.^{1/} The receipts forecast--reflecting the staff's higher corporate profits projection--has been increased from \$438-1/2 billion to \$441 billion.

The current full employment budget forecast--with its October 1, 1978 tax reductions--continues to show a large \$20 billion increase in the deficit from 1978:3 to 1978:4. During the first nine months of 1979, however, the increased receipts resulting from higher social security taxes and from the progressive nature of the income tax, partially offset the proposed tax cut. As a consequence, the high

^{1/} The assumptions behind this month's outlay forecast also have been modified to include a 5-1/2 per cent rather than a 6 per cent Federal pay raise, and some small outlay increases associated with the President's farm and urban programs.

employment deficit drops \$26 billion by the end of 1979:3. Last month the shift in the full employment budget over the same time period was estimated at \$22 billion. The difference between the two forecasts results from the projected higher rate of inflation on full employment tax receipts.

DOMESTIC FINANCIAL DEVELOPMENTS

Summary. Most market interest rates have increased about 15 to 20 basis points since the last FOMC meeting. The increases were in response to a more rapid rate of inflation, the continuing weakness of the foreign exchange value of the dollar, and concerns over the possibility that monetary policy would tighten in the coming months. Yields on short-term government securities also were affected by a somewhat larger than anticipated sale of cash management bills by the Treasury, while acquisitions of short-term Treasury debt were curtailed by foreign central banks.

Expansion of the key monetary aggregates was moderate in March. M-1 grew at about a 4 per cent annual rate, after declining slightly in February; for the first quarter as a whole, M-1 expanded at about a 5 per cent annual rate. With market rates of interest at or above comparable deposit rate ceilings, March growth in the interest-bearing components of M-2 and M-3 remained sluggish. The broader aggregates increased at about a 5 to 6 per cent annual rate during the month--somewhat below the rate of expansion for the quarter.

Available evidence indicates that funds raised by nonfinancial sectors expanded further in March. Business borrowing at banks and in the commercial paper market rose sharply, along with the quickening in economic activity in recent weeks. Offerings in the public bond market also increased. Mortgage borrowing by households is estimated to have risen somewhat, and fragmentary data suggest that consumer credit continued

to grow rapidly. At the same time, public sector debt issues increased noticeably, reflecting a pick-up in Treasury financing and greater State and local government bond offerings, particularly advance refunding issues.

Outlook. Aggregate credit demands in the second quarter do not appear likely to strengthen relative to the first quarter. Between now and around the end of May, the Treasury is expected to pay down a substantial amount of debt--about \$14 billion--with most of the reduction occurring in outstanding cash management bills. Although the Treasury will probably be a net borrower throughout the remainder of the quarter, its demands on credit markets from around the end of May to midyear are likely to be relatively small.

In the State and local sector, aggregate surpluses are expected to remain quite high. But the large forward bond calendar suggests that issues of tax-exempt debt will be substantial well into the second quarter. Current concerns that the IRS may promulgate new regulations further limiting possible advantages from advance refundings also may buoy near-term tax-exempt offerings.

The gap between investment outlays and business cash flows is projected to narrow in the second quarter. External financing, however, may be maintained in order to limit the decline in liquidity positions which has been underway for some time. Judging by underwriter reports and the current forward calendar, a somewhat greater volume of corporate financing may develop in the public bond markets. Business credit demands in short-term markets are expected to remain generally strong, although such demands may taper off from the exceptional first quarter pace.

Second quarter demands for consumer credit may pick up in concert with an anticipated increase in consumer outlays. Mortgage demands also will probably remain strong, given the projected snapback in housing activity.

While demands for credit may not strengthen significantly in the months immediately ahead, it is likely that interest rates will begin rising as the quarter progresses. Depository institutions, which have been reducing liquidity to finance loan demands, may gradually become more reluctant to do so; thrifts will continue to curtail mortgage commitments, putting further upward pressure on mortgage rates. In addition, unless expectations of inflation are dampened by the Administration's new program, recent and prospective price rises will tend to increase the inflation premiums in interest rates. Finally, resumption of stronger growth in M-1 can be expected in response to the projected rebound in growth of nominal GNP in the second quarter, and efforts by the Federal Reserve to limit such growth would place additional upward pressure under interest rates.

INTERNATIONAL DEVELOPMENTS

Summary. In the past four weeks the dollar declined by over 1 per cent on a weighted average basis, largely influenced by the announcement of a greatly enlarged U.S. trade deficit for February.

The currency in strongest demand against the dollar during the period was the Japanese yen, which rose by over 6 per cent against the dollar.

The Swiss franc and French franc have risen by 4 per cent and the mark by 2 per cent over the past month. On the other hand, the pound and the Canadian dollar have each declined over the period.

The only large-scale System sales of marks over the past month were on the day of the announcement of the February U.S. trade deficit. The System made net sales of \$15 million equivalent of marks during the period, and purchased \$54 million equivalent of Swiss francs for use in repaying the pre-1971 swap debt.

Announcement of an unprecedented U.S. trade deficit for February heightened concern about the U.S. trade account. The value of

non-agricultural exports in January and February was no higher than a year earlier, and the volume of these exports was lower, as export prices rose considerably. Imports other than petroleum were up sharply in January-February compared to fourth-quarter 1977 rates, with steep increases for most commodity groups. Steel imports were high in February and may remain high for a while as deliveries are made on orders placed before February 21, when the trigger-price mechanism went into effect. Some of the increase in import values appeared to result from higher import prices, reflecting in part the depreciation of the dollar since last September.

Continued weakness in the U.S. trade balance is consistent with indications that recovery of economic growth abroad so far remains weak. In both Japan and Germany some hesitation in industrial production appeared in February after promising gains in previous months. The Canadian economy, a major market for U.S. goods, is also sluggish. However, there are some signs of economic revival in France, the United Kingdom, and Italy.

Interest rates have continued to decline in most foreign countries as economic recovery has lagged. Liquidity in Germany, Japan, and Switzerland has increased as a result of exchange market intervention, and interest rates declines have been reinforced by discount rate cuts in Switzerland and Japan.

Belgium was able to reduce rates sharply from year-end peaks as pressure on the Belgian franc subsided. In Canada, however, interest rates were pushed up to cushion mounting pressure in the exchange markets, with the discount rate now standing at 8-1/2 per cent. Mildly expansionary budgets were proposed in Canada and the United Kingdom this week, with the bulk of the stimulation coming from a cut in personal income taxes in Britain and from cuts in provincial sales taxes in Canada. British Chancellor of The Exchequer Healey also announced, in his budget address, that the target range for monetary growth in FY 1978/79 would be reduced slightly from last year's target range (and outcome).

Private capital flows reported by U.S. banks and securities dealers were generally inward in February - the latest month for which data are available. Banks' net claims on foreigners were reduced on balance, and transactions in U.S. and foreign securities showed a small net inflow. Sales of new foreign bond issues in the U.S. market were exceptionally small, but will rise somewhat as Canada reenters the market. Foreign private net purchases of U.S. corporate stocks were minimal in January and February, and OPEC official purchases were somewhat lower than last year's average rate.

Outlook. The extraordinary U.S. trade deficit reported for February, following the high January figure, suggests that there has been an upward shift in underlying import prices and volumes; moreover, exports as yet show no signs of a pickup in volume. Consequently, the

projected trade deficit (on the international transactions basis) for this year has been raised to \$37 billion (from \$33 billion last month).

The staff believes that the exchange market has not fully anticipated trade deficits as large as those projected by the staff at this time, and therefore a further depreciation of the dollar on the order of 5 per cent on a weighted average basis has been incorporated in the projection. This decline in the dollar's average exchange rate (which would not significantly affect our estimate of the trade balance over the next four quarters) would be expected to come about mainly through further appreciations against the dollar by the yen, German mark, and Swiss franc, the currencies of countries whose surpluses are expected to remain large.

	1976	1977	1978 ^P	1977				1978 ^P				1979 ^P	
				I	II	III	IV	I	II	III	IV	I	II
1. <u>GNP NET EXPORTS</u> - Intl Acct. data	7.8	-10.3	-13.9	-7.9	-8.8	-6.8	-17.6	-18.9	-13.8	-10.6	-12.4	-11.7	-12.1
2. (GNP net exports - GNP Acct. data) <u>1/</u>	(7.8)	(-10.9)	(-14.5)	(-8.2)	(-9.7)	(-7.5)	(-18.2)	(-19.5)	(-14.4)	(-11.2)	(-13.0)	(-12.3)	(-12.7)
3. a) Merchandise Trade Balance	-9.3	-31.2	-37.2	-28.6	-30.6	-30.2	-35.5	-41.3	-36.6	-34.3	-36.7	-37.1	-37.9
4. Exports (excl. military)	114.7	120.5	132.3	117.8	122.6	123.5	118.0	121.5	129.5	136.5	141.6	149.4	153.9
5. Agricultural	23.4	24.4	24.5	24.4	26.7	24.0	22.3	24.5	24.5	24.5	24.5	25.0	25.0
6. Nonagricultural	91.3	96.1	107.8	93.4	95.9	99.5	95.6	97.0	105.0	112.0	117.1	124.4	128.9
7. Imports	124.0	151.7	169.5	146.4	153.2	153.7	153.5	162.8	166.1	170.8	178.3	186.5	191.8
8. Petroleum and petrol. products	34.6	44.7	44.3	44.1	47.5	45.8	41.6	40.8	43.1	45.4	47.9	51.2	51.5
9. Nonpetroleum	89.4	107.0	125.2	102.3	105.7	107.9	111.9	122.0	123.0	125.4	130.4	135.3	140.3
10. b) Military transactions, net <u>2/</u>	--	1.0	2.0	1.7	.8	1.8	-.2	2.0	2.0	2.0	2.0	2.0	2.0
11. c) Investment income, net <u>3/</u>	14.3	17.4	18.7	17.6	18.9	18.2	15.2	17.9	18.3	19.1	19.7	20.6	21.0
12. d) Other services, net <u>4/</u>	2.7	2.5	2.6	1.4	2.2	3.3	2.9	2.5	2.5	2.6	2.7	2.8	2.8
13. <u>U.S. CURRENT ACCOUNT BALANCE</u>	-1.4	-20.2	-26.5	-17.1	-18.3	-17.3	-28.1	-30.9	-26.4	-23.3	-25.4	-25.6	-26.2
14. a) GNP net exports (line 1.)	7.8	-10.3	-13.9	-7.9	-8.8	-6.8	-17.6	-18.9	-13.8	-10.6	-12.4	-11.7	-12.1
15. b) U.S. Govt & private transfers <u>5/</u>	-9.2	-9.9	-12.6	-9.2	-9.5	-10.5	-10.5	-12.0	-12.6	-12.7	-13.0	-13.9	-14.1
<u>Constant (1972) dollars</u>													
16. Merchandise exports (excl. military)	66.7	66.9	68.4	66.1	67.8	68.7	65.1	64.8	67.7	70.0	71.2	73.7	74.9
17. (% change, annual rates)	(3.4)	(0.3)	(2.2)	(-7.4)	(10.8)	(5.3)	(-22.5)	(-1.6)	(18.8)	(14.3)	(7.4)	(14.3)	(6.6)
18. Merchandise imports	62.8	71.1	72.1	70.3	71.9	71.2	70.9	71.8	71.5	71.7	73.4	75.2	76.2
19. (% change, annual rates)	(22.5)	(13.2)	(1.4)	(28.2)	(9.1)	(-4.1)	(-1.6)	(5.3)	(-1.6)	(1.2)	(10.0)	(10.0)	(5.3)
<u>Foreign Outlook - Major Industrial Countries <u>6/</u></u>													
20. Real GNP, % change, annual rates	5.2	2.9	3.7	6.1	0	0.8	3.7	4.9	4.5	4.1	4.1	4.5	4.5
21. Wholesale Prices, % change, A.R. <u>7/</u>	9.4	8.7	4.7	10.4	7.4	3.7	2.8	4.5	5.7	5.7	5.7	5.7	6.1

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

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

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

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

5/ Includes U.S. Govt. grants, U.S. Govt. interest payments to foreigners, remittances and pensions, and exports to Israel financed by U.S. military assistance grants.

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

7/ Data are largely manufactured goods prices.

P/ Projected

E/ Estimated

* Published data.