

## **Prefatory Note**

The attached document represents the most complete and accurate version available based on original copies culled from the files of the FOMC Secretariat at the Board of Governors of the Federal Reserve System. This electronic document was created through a comprehensive digitization process which included identifying the best-preserved paper copies, scanning those copies,<sup>1</sup> and then making the scanned versions text-searchable.<sup>2</sup> Though a stringent quality assurance process was employed, some imperfections may remain.

Please note that this document may contain occasional gaps in the text. These gaps are the result of a redaction process that removed information obtained on a confidential basis. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

---

<sup>1</sup> In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

<sup>2</sup> A two-step process was used. An advanced optimal character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

CONFIDENTIAL (FR)

May 10, 1978

SUMMARY AND OUTLOOK

By the Staff  
Board of Governors  
of the Federal Reserve System

---

## **SUMMARY AND OUTLOOK**

---

---

DOMESTIC NONFINANCIAL DEVELOPMENTS

---

Summary. Economic activity has rebounded from the weather and strike depressed levels early this year, and the latest economic statistics suggest considerable near-term momentum. Employment, industrial production, and retail sales grew at brisk rates again in April. In addition, March data point to a rebound in construction activity and a further rise in inventories. However, price increases continued at a rapid rate, with especially large rises for farm products and foods.

Industrial production is tentatively estimated to have increased by about 1 per cent in April. Auto assemblies posted a further strong gain, and coal and steel mill output recovered from reduced, mainly strike-affected March levels. Output of business equipment appears to have continued to expand at a vigorous rate. Over-all industrial output has increased at about a 5 per cent annual rate over the last six months.

Total employment rose by more than half a million in April, exceeding a large rise in the labor force. The unemployment rate dropped to 6.0 per cent--its lowest level in 3-1/2 years. Nonfarm payroll employment increased by 465,000 (strike adjusted). Gains were widespread among the industries, with a particularly large rise in contract construction. Over the last six months, nonfarm payroll employment has increased by an impressive 2.3 million.

Large employment and wage increases thus far in 1978 have led to sizable advances in total wage and salary disbursements, and consumer spending recently has shown renewed strength. Retail sales, boosted by an increase in new car sales to a 12.1 million rate, appear to have

advanced significantly further in April following large advances in February and March.

Residential construction activity picked up in March; starts were at a 2.1 million unit annual rate, slightly below the fourth quarter pace. Sales of homes also rose in March but remained below the advanced rate of late 1977. Moreover, outstanding mortgage commitments declined in each month of the first quarter.

Business fixed investment spending was damped in the first quarter by bad weather but outlays strengthened at the end of the quarter. Orders for nondefense capital goods rose about 3-1/2 per cent in real terms in the first quarter--about the same as the average quarterly rise during 1977. The McGraw-Hill and Merrill Lynch spring surveys of capital spending plans for 1978 showed sizable upward revisions from spending increases anticipated last fall.

Manufacturers' inventories in book value terms grew at about a \$15 billion annual rate in March and during the first quarter. Despite this rapid growth, however, inventory-sales ratios in manufacturing edged still lower in February and March as shipments increased even more than inventories.

Federal government outlays, which fell short in the first quarter of anticipated amounts--and declined in real terms--are suggested by preliminary data to have fallen below agency expectations again during April. Fiscal caution continued to be exhibited in the State and local government sector as expenditures again were below receipts. Net budget surpluses in this sector (including both operational and retirement

accounts) have totaled about \$30 billion over the past four quarters.

Large food price increases have continued to boost the over-all inflation rate. Food prices rose at double-digit rates during the first quarter in part because of declining meat production and a temporary reduction in fruit and vegetable supplies. In addition, the earlier weakness of the exchange value of the dollar has led to somewhat higher car prices, and home financing costs have risen due to higher mortgage interest rates. Consumer prices increased at a 9 per cent annual rate during the first quarter of 1978, about the same rate as in the first half of 1977 but double the rate in the last half of 1977.

Government-mandated increases in the minimum wage as well as Social Security and unemployment insurance taxes contributed to a substantial increase in hourly compensation costs in the first quarter. This, in combination with a decline in productivity, resulted in an exceptionally large increase in unit labor costs.

Outlook. According to the Commerce Department's preliminary estimate of GNP for the first quarter, over-all activity was more severely curtailed by weather and strikes than had been anticipated in the previous Greenbook. However, the latest measures of employment, production, sales, and construction suggest a strong rebound in real GNP at a rate of about 9 per cent in the current quarter. Thus, activity in the second quarter is indicated to be at the same level as was projected last month.

The fiscal policy assumptions underlying the staff projections are unchanged from last month--basically they reflect the Administration's proposal for a \$25 billion dollar tax cut effective October 1. Our estimate of Federal outlays are assumed to be \$454 billion for FY 1978 and \$500 billion for FY 1979. With regard to monetary policy, we continue to assume a 5-1/4 per cent annual growth rate of M-1 through mid-1979, and interest rates are still projected to rise substantially over the spring and summer months, particularly in short-term markets. Given the recent sharp increase of M-1, however, our projection of interest rates consistent with a 5-1/4 per cent growth rate for the policy period has been raised from that of last month.<sup>1</sup>

Following the current quarter rebound, real GNP growth is projected to average about 4-1/4 per cent over the last four quarters of the projection period--about 1/4 per cent less than last month. The downward adjustment is concentrated in residential construction, which had been a major source of strength during this expansion. Residential construction activity now is projected to decline more steeply, especially in the first half of 1979, reflecting tighter conditions in financial markets than anticipated last month. Consequently, real GNP gains decelerate noticeably in the first half of next year. Despite the additional support provided by the assumed tax cut, we continue to project a less expansive

---

<sup>1</sup>/ Projected federal funds rate ranges are shown in Appendix Table 1 of the Bluebook. Our GNP projections assume interest rates toward the lower ends of those ranges.

consumption pattern than earlier in the recovery; this reflects slower growth of real disposable income, together with rising debt burdens and efforts to increase savings. Although business fixed investment is expected to provide continued support --with real outlays growing 6-1/4 per cent over the four quarters ending in QII:1979--the projected increase is smaller than the rise during 1977.

In the current projection, the unemployment rate declines only fractionally further to about 5-3/4 per cent in the first half of 1979. With compensation increases expected to be at a rapid rate and productivity gains likely to be moderate, cost pressures on prices are expected to continue to be intense. Inflation, as measured by the fixed-weighted price index for gross business product, is expected to be at about a 7 per cent annual rate over the projection period, about in line with the rate anticipated last month.

Details of the staff projection are shown on 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)	
	4/12/78	5/10/78	4/12/78	5/10/78	4/12/78	5/10/78	4/12/78	5/10/78
1974 <sup>1/</sup>	8.1	8.1	-1.4	-1.4	10.4	10.4	5.6	5.6
1975 <sup>1/</sup>	8.2	8.2	-1.3	-1.3	9.5	9.5	8.5	8.5
1976 <sup>1/</sup>	11.6	11.6	6.0	6.0	5.4	5.4	7.7	7.7
1977 <sup>1/</sup>	10.7	10.7	4.9	4.9	6.0	6.0	7.0	7.0
1978	11.1	11.1	4.2	4.1	6.6	6.4	6.0	5.9
1977-III <sup>1/</sup>	10.2	10.2	5.1	5.1	5.0	5.0	6.9	6.9
1977-IV <sup>1/</sup>	9.9	9.9	3.8	3.8	5.4	5.4	6.6	6.6
1978-I <sup>1/</sup>	8.7	6.5	1.4	-.6	7.4	6.6	6.2	6.2
1978-II	14.5	17.4	6.7	9.0	7.3	7.7	6.0	5.9
1978-III	11.4	11.6	4.4	4.4	6.8	6.9	6.0	5.9
1978-IV	12.0	12.2	4.6	4.6	6.8	6.9	5.9	5.8
1979-I	11.9	11.5	4.6	4.2	7.4	7.3	5.8	5.7
1979-II	10.8	10.5	4.1	3.8	7.0	6.9	5.8	5.7
Change:								
76-IV to 77IV <sup>1/</sup>	11.8	11.8	5.7	5.7	6.1	6.1	-1.2	-1.2
77-II to 78-II	10.8	10.9	4.2	4.3	6.3	6.1	-1.1	-1.2
77-IV to 78-IV	11.6	11.9	4.2	4.3	7.1	7.0	-.7	-.8
78-II to 79-II	11.5	11.4	4.4	4.3	7.0	7.0	-.2	-.2
Memo:								
Growth Over Annual Policy Period:								
78-I to 79-I	12.4	13.1	5.1	5.5	7.1	7.2	-.4	-.5

<sup>1/</sup> Actual.

May 10, 1978

CONFIDENTIAL - FR  
CLASS II FOMC

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

	1977		1978				1979	
	III	IV	I	II	Projected		I	II
Gross National Product	1915.9	1961.8	1992.9	2074.3	2132.2	2194.3	2254.6	2311.5
Final purchases	1892.2	1948.2	1976.4	2051.3	2108.2	2168.8	2227.3	2283.0
Private	1491.3	1534.4	1559.3	1622.6	1668.1	1714.9	1762.8	1807.7
Excluding net exports	1498.8	1552.6	1581.9	1639.5	1679.5	1725.4	1771.8	1816.9
Personal consumption expenditures	1218.9	1259.5	1284.0	1328.1	1361.0	1399.9	1439.0	1476.1
Goods	659.4	685.9	689.8	716.8	734.2	756.4	776.4	794.5
Services	559.5	573.7	594.3	611.3	626.8	643.5	662.6	681.6
Gross private domestic investment	303.6	306.7	314.4	334.4	342.5	351.0	360.1	369.3
Residential construction	92.5	99.7	100.2	104.7	105.2	105.2	105.2	105.7
Business fixed investment	187.5	193.5	197.7	206.7	213.3	220.3	227.6	235.1
Change in business inventories	23.6	13.5	16.5	23.0	24.0	25.5	27.3	28.5
Nonfarm	23.1	9.0	15.5	22.0	24.0	25.5	27.3	28.5
Net exports of goods and services <sup>1/</sup>	-7.5	-18.2	-22.6	-16.9	-11.4	-10.5	-9.0	-9.2
Exports	179.9	170.6	178.3	189.3	198.8	206.8	216.6	224.0
Imports	187.4	188.8	200.8	206.1	210.1	217.2	225.5	233.1
Gov't. purchases of goods and services	400.9	413.8	417.1	428.7	440.1	453.9	464.5	475.3
Federal <sup>2/</sup>	148.1	153.8	153.1	155.1	159.0	165.5	169.0	172.7
State and local	252.9	260.0	264.1	273.6	281.1	288.4	295.5	302.6
Gross national product in constant (1972) dollars	1347.4	1360.2	1358.3	1387.9	1402.9	1418.9	1433.6	1447.0
Personal income	1549.8	1603.0	1636.7	1687.4	1736.4	1784.8	1828.1	1872.2
Wage and salary disbursements	998.9	1029.1	1057.4	1091.2	1116.2	1146.1	1177.9	1205.4
Disposable income	1323.8	1368.3	1400.5	1440.7	1479.7	1534.7	1574.0	1609.9
Saving rate (per cent)	5.5	5.6	5.9	5.4	5.6	6.4	6.2	5.9
Corporate profits with I.V.A. and C.C. Adj.	149.0	144.8	125.3	147.1	151.3	160.7	158.8	162.1
Corporate profits before tax	172.8	178.3	170.5	189.4	192.7	202.3	200.9	204.7
Federal government surplus or deficit (-) (N.I.A. basis)	-58.9	-60.0	-60.5	-49.0	-44.7	-61.0	-54.1	-49.1
High employment surplus or deficit (-)	-20.4	-22.1	-12.3	-10.1	-4.9	-24.1	-15.9	-10.0
State and local government surplus or deficit (-) (N.I.A. basis)	32.9	31.1	34.1	33.7	30.5	30.1	28.6	26.5
Excluding social insurance funds	17.4	15.4	18.0	17.1	13.4	12.5	10.5	7.9
Civilian labor force (millions)	97.6	98.6	99.2	99.9	100.4	101.0	101.5	102.0
Unemployment rate (per cent)	6.9	6.6	6.2	5.9	5.9	5.8	5.7	5.7
Nonfarm payroll employment (millions)	82.5	83.2	84.1	85.3	85.7	86.3	86.8	87.3
Manufacturing	19.6	19.8	20.1	20.3	20.5	20.7	20.9	21.1
Industrial product (1967=100)	138.4	139.3	139.5	143.5	145.9	148.6	151.0	153.1
Capacity utilization: all manufacturing (per cent)	83.0	82.9	82.1	83.5	84.2	85.0	85.5	85.9
Materials (per cent)	82.3	82.2	81.4	83.3	84.1	85.0	85.8	86.4
Housing starts, private (millions, A.R.)	2.04	2.15	1.73	2.00	1.80	1.75	1.70	1.70
Sales new autos, (millions, A.R.)	10.92	10.75	10.80	10.95	10.90	11.05	11.10	10.95
Domestic models	8.88	8.77	8.80	8.85	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

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

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

May 10, 1978

CONFIDENTIAL - FR  
S II POMCCHANGES IN GROSS NATIONAL PRODUCT  
AND RELATED ITEMS

	1977		1978				1979	
	III	IV	I	Projected		I	II	
				II	III			IV
	-----Billions of dollars-----							
Gross National Product	46.0	45.9	31.1	81.5	57.9	62.1	60.3	56.9
Inventory change	1.9	-10.1	3.0	6.5	1.0	1.5	1.8	1.2
Final purchases	44.0	56.0	28.2	75.0	56.9	60.6	58.5	55.7
Private	33.7	43.1	24.9	63.4	45.5	46.8	47.9	44.9
Net exports	2.2	-10.7	-4.4	5.7	5.5	.9	1.5	-2
Excluding net exports	31.5	53.8	29.3	57.6	40.0	45.9	46.4	45.1
Personal consumption expenditures	24.9	40.6	24.5	44.1	32.9	38.9	39.1	37.1
Goods	6.4	26.5	3.9	27.0	17.4	22.2	20.0	18.1
Services	18.4	14.2	20.6	17.0	15.5	16.7	19.1	19.0
Residential fixed investment	1.7	7.2	.5	4.5	.5	.0	.0	.5
Business fixed investment	5.1	6.0	4.2	9.0	6.6	7.0	7.3	7.5
Government	10.3	12.9	3.3	11.6	11.4	13.8	10.6	10.8
Federal	4.5	5.7	-7	2.0	3.9	6.5	3.5	3.7
State and local	5.9	7.1	4.1	9.5	7.5	7.3	7.1	7.1
GNP in constant (1972) dollars	16.7	12.8	-1.9	29.6	15.0	16.0	14.7	13.3
Final purchases	14.3	19.7	-4.6	25.2	14.6	15.2	13.5	12.2
Private	10.3	16.7	-2.5	21.8	11.2	12.6	11.3	9.9
	-----In per cent per year <sup>1/</sup> -----							
Gross National Product	10.2	9.9	6.5	17.4	11.6	12.2	11.5	10.5
Final purchases	9.9	12.4	5.9	16.1	11.6	12.0	11.2	10.4
Private	9.6	12.1	6.7	17.3	11.7	11.7	11.6	10.6
Personal consumption expenditures	8.6	14.0	8.0	14.5	10.3	11.9	11.6	10.7
Goods	4.0	17.0	2.3	16.6	10.1	12.7	11.0	9.7
Services	14.3	10.5	15.2	12.0	10.5	11.1	12.4	11.9
Gross private domestic investment	12.4	4.1	10.4	28.0	10.0	10.3	10.8	10.6
Residential structures	7.7	35.0	2.1	19.2	1.9	.0	.0	1.9
Business fixed investment	11.6	13.4	9.0	19.5	13.4	13.8	13.9	13.8
Gov't. purchases of goods and services	11.0	13.5	3.3	11.6	11.1	13.1	9.7	9.6
Federal	12.9	16.3	-1.8	5.4	10.4	17.4	8.7	9.0
State and local	9.9	11.8	6.4	15.3	11.4	10.8	10.2	10.0
GNP in constant (1972) dollars	5.1	3.8	-6	9.0	4.4	4.6	4.2	3.8
Final purchases	4.4	6.1	-1.3	7.7	4.3	4.5	3.9	3.5
Private	4.0	6.5	-9	8.3	4.1	4.7	4.1	3.5
GNP implicit deflator <sup>2/</sup>	4.8	5.9	7.1	7.7	6.9	7.2	6.9	6.5
Gross business product fixed-weighted price index <sup>3/</sup>	5.0	5.4	6.6	7.7	6.9	6.9	7.3	6.9
Personal income	8.9	14.5	8.7	13.0	12.1	11.6	10.1	10.0
Wage and salary disbursements	7.5	12.7	11.5	13.4	9.5	11.2	11.6	9.7
Disposable income	10.0	14.1	9.8	12.0	11.3	15.7	10.6	9.4
Corporate profits before tax	-2.7	13.4	-16.4	52.2	7.3	21.4	-2.7	7.9
Nonfarm payroll employment	3.3	3.2	4.4	5.6	2.3	2.7	2.4	2.3
Manufacturing	1.3	2.7	6.6	4.0	4.5	4.4	4.2	4.0
Nonfarm business sector								
Output per hour	3.8	2.3	-3.3	3.9	3.3	2.8	2.1	1.9
Compensation per hour	7.5	8.2	13.2	7.7	7.9	8.0	11.6	8.2
Unit labor costs	3.5	5.8	17.0	3.8	4.6	5.2	9.5	6.3
Industrial production	4.2	2.6	.6	12.0	6.9	7.6	6.6	5.7
Housing starts, private	23.3	22.2	-57.6	77.8	-34.4	-10.7	-10.9	.0
Sales new autos	-24.1	-6.2	2.0	5.6	-1.8	5.6	1.8	-5.3
Domestic models	-18.4	-4.8	1.4	2.1	2.3	9.3	2.2	-2.2
Foreign models	-43.9	-12.3	4.7	21.6	-17.7	-9.6	.0	-19.0

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

Excluding Federal pay increases rates of change are: 1977-IV, 5.1 per cent; 1978-I, 7.0 per cent; 1978-IV, 6.6 per cent; 1979-I, 6.9 per cent.

Using expenditures in 1972 as weights.

CONFIDENTIAL - FR  
CLASS II FOMC

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

May 10, 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	2098.5
Final purchases	1057.1	1161.7	1288.6	1404.0	1540.3	1693.1	1871.4	2076.2
Private	823.4	908.6	1019.1	1101.3	1201.4	1331.7	1476.4	1641.2
Excluding net exports	821.8	911.9	1012.0	1095.3	1181.0	1323.9	1487.3	1656.6
Personal consumption expenditures	668.2	733.0	809.9	889.6	980.4	1094.0	1211.2	1343.3
Goods	374.8	410.5	457.5	498.3	542.2	601.6	660.5	724.3
Services	293.4	322.4	352.3	391.3	438.2	492.3	550.7	619.0
Gross private domestic investment	160.0	188.3	220.0	214.6	189.1	243.3	294.2	335.6
Residential construction	49.6	62.0	66.1	55.1	51.5	68.0	91.0	103.8
Business fixed investment	104.1	116.8	136.0	150.6	149.1	161.9	185.1	209.5
Change in business inventories	6.4	9.4	17.9	8.9	-11.5	13.3	18.2	22.2
Nonfarm	5.1	8.8	14.7	10.8	-15.1	14.9	17.1	21.7
Net exports of goods and services	1.6	-3.3	7.1	6.0	20.4	7.8	-10.9	-15.3
Exports	65.6	72.7	101.6	137.9	147.3	162.9	174.7	193.3
Imports	64.0	75.9	94.4	131.9	126.9	155.1	185.6	208.6
Gov't. purchases of goods and services	233.7	253.1	269.5	302.7	338.9	361.4	395.0	435.0
Federal	96.2	102.1	102.2	111.1	123.3	130.1	145.4	158.2
State and local	137.5	151.0	167.3	191.5	215.6	231.2	249.6	276.8
Gross national product in constant (1972) dollars	1107.5	1171.1	1235.0	1217.8	1202.1	1274.7	1337.3	1392.0
Personal income	859.1	942.5	1052.4	1154.9	1253.4	1382.7	1536.7	1711.3
Wage and salary disbursements	579.4	633.8	701.3	764.6	805.7	891.8	990.0	1102.7
Disposable income	742.8	801.3	901.7	984.6	1084.4	1185.8	1309.2	1463.9
Saving rate (per cent)	7.7	6.2	7.8	7.3	7.4	5.6	5.1	5.8
Corporate profits with I.V.A. and C.C. Adj.	77.2	92.1	99.1	83.6	99.3	128.1	139.9	146.1
Corporate profits before tax	82.0	96.2	115.8	126.9	123.5	156.9	171.7	188.7
Federal government surplus or deficit (-) (N.I.A. basis)	-22.0	-17.3	-6.7	-10.7	-70.2	-54.0	-49.5	-53.8
High employment surplus or deficit (-)	-5.3	-5.9	-.7	17.1	-20.3	-10.4	-8.7	-12.8
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	32.1
Excluding social insurance funds	-3.8	5.6	4.1	-2.9	-6.2	3.9	13.7	15.2
Civilian labor force (millions)	84.1	86.5	88.7	91.0	92.6	94.8	97.4	100.1
Unemployment rate (per cent)	5.9	5.6	4.9	5.6	8.5	7.7	7.0	5.9
Nonfarm payroll employment (millions)	71.2	73.7	76.9	78.4	77.1	79.4	82.1	85.4
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	144.4
Capacity utilization: all manufacturing (per cent)	78.0	83.1	87.5	84.2	73.6	80.2	82.4	83.7
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	1.99	1.82
Sales new autos (millions, A.R.)	10.24	10.93	11.42	8.91	8.66	10.12	11.13	10.93
Domestic models	8.68	9.32	9.65	7.49	7.08	8.63	9.07	8.91
Foreign models	1.56	1.61	1.77	1.42	1.58	1.50	2.06	2.01

May 10, 1978

DENTIAL - FR  
S II FOMC

CHANGES 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	208.9
Inventory change	2.6	3.0	8.5	-9.0	-20.4	24.8	4.9	4.0
Final purchases	78.5	104.6	126.9	115.4	136.3	152.8	178.3	204.8
Private	63.7	85.2	110.5	82.2	100.1	130.3	144.7	164.8
Net exports	-2.3	-4.9	10.4	-1.1	14.4	-12.6	-18.7	-4.4
Excluding net exports	66.0	90.1	100.1	83.3	85.7	142.9	163.4	169.3
Personal consumption expenditures	49.4	64.8	76.9	79.7	90.8	133.6	117.2	132.1
Goods	25.2	35.7	47.0	40.8	43.9	59.4	58.9	63.8
Services	24.3	29.0	29.9	39.0	46.9	54.1	58.4	68.3
Residential fixed investment	13.0	12.4	4.1	-11.0	-3.6	16.5	23.0	12.8
Business fixed investment	3.6	12.7	19.2	14.6	-1.5	12.8	23.2	24.4
Government	14.8	19.4	16.4	33.2	36.2	22.5	33.6	40.0
Federal	.6	5.9	.1	8.9	12.2	6.8	15.3	12.8
State and local	14.3	13.5	16.3	24.2	24.1	15.6	18.4	27.2
GNP in constant (1972) dollars	32.2	63.6	63.9	-17.2	-15.7	72.6	62.6	54.7
Final purchases	29.9	60.8	56.8	-8.6	2.1	54.2	59.3	51.4
Private	30.7	57.1	57.4	-13.8	-3.2	52.8	52.6	42.7
	-----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	11.2
Personal consumption expenditures	8.0	9.7	10.5	9.8	10.2	11.6	10.7	10.9
Goods	7.2	9.5	11.4	8.9	8.8	11.0	9.8	9.7
Services	9.0	9.9	9.3	11.1	12.0	12.4	11.9	12.4
Less private domestic investment	13.6	17.7	16.8	-2.5	-11.9	28.7	20.9	14.1
Residential structures	35.5	25.1	6.6	-16.7	-6.5	32.2	33.7	14.1
Business fixed investment	3.6	12.3	16.4	10.8	-1.0	8.6	14.3	13.2
Gov't. purchases of goods and services	6.8	8.3	6.5	12.3	12.0	6.6	9.3	10.1
Federal	.6	6.1	.1	8.7	11.0	5.5	11.8	8.8
State and local	11.6	9.8	10.8	14.5	12.6	7.2	7.9	10.9
GNP in constant (1972) dollars	3.0	5.7	5.5	-1.4	-1.3	6.0	4.9	4.1
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	4.0
GNP implicit deflator	5.1	4.1	5.8	9.7	9.6	5.3	5.5	6.7
Gross business product fixed-weighted index <sup>1/</sup>	4.4	3.3	5.7	10.4	9.5	5.4	6.0	6.4
Personal income	7.2	9.7	11.7	9.7	8.5	10.3	11.1	11.4
Wage and salary disbursements	6.0	9.4	10.7	9.0	5.4	10.7	11.0	11.4
Disposable income	8.3	7.9	12.5	9.2	10.1	9.4	10.4	11.8
Corporate profits before tax	14.7	17.3	20.4	9.6	-2.7	27.0	9.4	9.9
Nonfarm payroll employment	.4	3.5	4.3	2.0	-1.7	3.1	3.4	3.9
Manufacturing	-4.0	2.8	5.1	-.1	-8.5	3.3	3.2	4.2
Nonfarm business sector								
Output per hour	2.9	3.0	1.7	-2.9	1.6	4.1	2.2	1.5
Compensation per hour	6.6	5.8	7.8	9.4	9.6	8.7	8.8	9.1
Unit labor costs	3.5	2.7	6.0	12.7	7.9	4.5	6.4	7.6
Industrial production	1.7	9.2	8.4	-.4	-8.9	10.2	5.5	5.4
Housing starts	43.1	14.9	-13.2	-34.6	-13.3	32.5	29.2	-8.4
Sales new autos	21.9	6.8	-4.7	-14.5	-2.8	16.9	9.9	-1.8
Domestic models	21.9	7.4	3.5	-22.4	-5.5	21.9	5.1	-1.7
Foreign models	21.8	3.1	9.7	-19.9	11.4	-5.1	37.2	-2.1

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

FEDERAL SECTOR ACCOUNTS  
(billions of dollars)

May 10, 1978

	FY 1977*	F.R. Staff Estimates														
		FY 1978 e/		FY 1979 e/		CY77*	CY78e/	Calendar quarters; unadjusted data								
		Admin.	F.R.	Admin.	F.R.	F.R.	F.R.	1977			1978			1979		
	1/ 2/	Board	1/	Board	Board	Board	III*	IV*	I*	II	III	IV	I	II	III	
Unified budget receipts	356.9	400.5	400.0	439.8	440.0	365.2	409.3	91.3	84.5	84.9	124.7	105.9	93.8	96.6	133.3	116.4
Unified budget outlays	401.9	453.5	454.1	499.4	499.6	416.1	463.6	103.4	113.3	110.7	112.7	117.4	122.8	121.3	125.4	130.1
Surplus(+)/Deficit(-), unified budget	-45.0	-53.0	-54.1	-59.6	-59.6	-50.9	-54.3	-12.2	-28.8	-25.8	12.0	-11.5	-29.0	-24.7	7.9	-13.7
Surplus(+)/Deficit(-), off-budget agencies 3/	-8.7	-11.5	-11.6	-12.5	-11.5	-10.4	-11.9	-4.9	-1.3	-3.6	-2.0	-4.6	-1.7	-3.9	-1.3	-4.6
Means of financing combined deficits:																
Net borrowing from public	53.5	57.2	52.0	74.7	73.9	56.8	61.3	19.6 <sup>8/</sup>	20.7 <sup>8/</sup>	20.8	-1.4	11.9	30.0	27.6	-4.7	21.0
Decrease in cash operating balance	-1.7	n.a.	8.0	0	-0.9	-0.6	0.3	-2.8 <sup>8/</sup>	6.8 <sup>8/</sup>	5.9	-9.6	4.9	-0.9	0	0	0
Other 4/	1.9	n.a.	5.7	-2.6	-2.0	5.3	4.7	0.4	2.6	2.8	1.0	-0.7	1.6	1.0	-1.9	-2.7
Cash operating balance, end of period	19.1	12.0	11.1	12.0	12.0	12.3	12.0	19.1 <sup>8/</sup>	12.3	6.4	16.0	11.1	12.0	12.0	12.0	12.0
Memo: Sponsored agency borrowing 5/	5.2	n.a.	19.7	n.a.	13.5	6.8	20.7	1.1	2.0	4.5	6.4	6.8	3.0	2.5	3.5	4.5
<b>NIA Budget</b>								<b>Seasonally adjusted annual rates</b>								
Receipts	361.8 <sup>6/</sup>	410.9 <sup>9/</sup>	403.0 <sup>6/</sup>	451.6 <sup>9/</sup>	n.e.	373.9	415.6	373.2	386.3	391.1	411.1	430.5	429.8	443.8	457.0	n.e.
Outlays	411.9	457.0	458.3	503.4	503.7	423.4	469.4	432.1	446.3	451.6	460.1	475.2	490.8	497.9	506.1	520.0
Purchases (total)	140.6	156.0	155.3	171.4	170.9	145.5	158.2	148.1	153.8	153.1	155.1	159.0	165.5	169.0	172.7	176.5
Defense	91.8	99.3	99.8	107.6	107.8	94.3	101.4	95.6	98.5	99.2	100.3	101.4	104.5	106.4	109.0	111.4
Non-defense	48.8	56.7	55.4	63.8	63.1	51.2	56.8	52.5	55.3	53.9	54.8	57.6	61.0	62.6	63.7	65.1
All other outlays	271.4	301.0	303.0	332.0	332.8	278.0	311.2	284.0	292.5	298.5	305.0	316.2	325.3	328.9	333.4	343.5
Surplus(+)/Deficit(-)	-50.1 <sup>6/</sup>	-46.1	-55.3 <sup>6/</sup>	-51.8	n.e.	-49.5	-53.8	-58.9	-60.0	-60.5	-49.0	-44.7	-61.0	-54.1	-49.1	n.e.
High Employment Surplus(+)/																
Deficit(-) (NIA basis) 7/	-5.0	n.a.	-12.3	n.a.	-13.0	-8.7	-12.8	-20.4	-22.1	-12.3	-10.1	-4.9	-24.1	-15.9	-10.0	-1.9
	*actual	e--estimated	r--revised		n.e.--not estimated			n.a.--not available					p--preliminary			

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 issues 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.

9/ NIA estimates consistent with the March Update. The Survey of Current Business, March 1978.

---

DOMESTIC FINANCIAL DEVELOPMENTS

---

Summary. Since the last FOMC meeting most short-term market rates have increased by about 20 to 40 basis points, while yields on longer term securities have risen 5 to 35 basis points. Upward pressures were associated with an increase in the Federal funds rate by 50 basis points to around 7-1/4 per cent. In addition, market expectations were changed in the light of further rapid rises in the prices of goods and services, additional evidence of a strong pick-up in economic activity, and an acceleration in the growth of the monetary aggregates. However, interest rates did not increase as much as might have been expected, partly because of an anticipatory increase in rates prior to the April meeting and in part because of a continued scarcity of Treasury bills.

Despite interest rate increases and indications of a deterioration in the outlook regarding inflation, stock prices rallied strongly in late April. The surge in equity values was associated largely with the rebound in economic activity and a strengthening of the dollar in foreign exchange markets. Even after some net decline in stock prices in recent days most major price indexes are now about 2-1/2 per cent above their levels at the time of the last Committee meeting.

Growth in the key monetary aggregates increased markedly in April primarily due to a surge in M-1. This aggregate grew at an estimated 17 per cent annual rate in association with a rebound in economic activity and transitory tax factors--primarily due to delayed processing by the Treasury of checks for nonwithheld taxes. Inflows

into small time and savings deposits at banks and thrift institutions also picked up somewhat in April.

The exceptionally strong growth in demand deposits, along with some increase in flows of small time and savings deposits, enabled banks to finance vigorous growth in loans and investments while reducing their reliance on managed liabilities. By contrast, thrift institutions had to continue relying heavily on borrowed funds and liquid assets to support mortgage lending, given continued relatively modest deposit inflows.

Credit raised by most nonfinancial sectors apparently declined somewhat in April from the advanced March level. Funds raised by non-financial businesses fell modestly, as did borrowing by households. The Treasury, reflecting a seasonal build-up of tax receipts, paid down outstanding debt on balance. However, State and local government borrowing picked up markedly as a result of New York State's spring financing.

Outlook. Treasury borrowing over coming months is expected to follow usual patterns, remaining light over the remainder of this quarter and picking up noticeably over the third quarter.

Large surpluses are expected to continue for many State and local governments. Issues of tax-exempt debt are likely to remain around current levels, but volume--particularly for advance refundings--may be strongly affected by interest rate developments. Yields on New York-related and on some other lower-rated issues could be influenced by concerns about the financial status of New York City's.



Even with the June 30 expiration date for the Federal seasonal loan program rapidly approaching, no resolution of the city's financial plight seems in immediate prospect.

In the private sector, business and household demands for funds are projected to be little changed through the third quarter. However, further tightening of terms of lending--particularly for mortgage credit--could begin to slow increases in household debt as thrift institutions continue to react to sluggish deposit inflows, less ample margins of liquidity, and greater reliance on comparatively high cost nondeposit sources of funds. Adjustments in deposit ceiling rates, depending on their nature and magnitude, could provide some relief. But given the wide spreads prevailing between open market rates and rate ceilings on most deposit accounts, flows into many account categories would probably remain relatively slow.

Open market interest rates, moreover, are expected to rise further. Credit demands are likely to remain vigorous. Recent and prospective price increases, in addition, may raise inflation premiums in interest rates. Finally, the strong increases in nominal economic activity, now under way and in prospect, will augment transactions demands for money. Further upward pressures on interest rates then may result from System efforts to restrain growth in the monetary aggregates.

INTERNATIONAL DEVELOPMENTS

---

Summary. The weighted average exchange rate of the dollar rose by about 2-1/2 per cent during the past four weeks. This strong advance appears to have been associated with a judgment by market participants of a shift in the focus of U.S. economic policy toward greater emphasis on curbing inflation. This view was reinforced by the sharp rise in U.S. interest rates over the past month.

Over the month, the dollar appreciated against all major currencies, except the Canadian dollar, with the most pronounced advances recorded against the Swiss franc, the mark and the pound. The Canadian dollar firmed by about 2 per cent against the dollar, in response to the announcement of several large-scale foreign borrowings by the Canadian government to replenish declining reserves, as well as a continuing rise in Canadian interest rates.

. The Desk acquired \$461 million equivalent of marks during the period, which were used in part by the System and the Treasury to repay outstanding swap debt to the Bundesbank.

The U.S. trade deficit declined in March to an annual rate of \$41.5 billion, slightly above the rates of January and the fourth quarter of 1977. The record February imbalance raised the first-quarter deficit to an annual rate of \$45 billion.

In addition to the large first-quarter trade deficit, net private capital outflows in the quarter reached about \$7.5 billion. Bank-reported private capital transactions, adjusted for reporting bias, resulted in a net outflow of about \$5 billion in March, bringing the total net (adjusted) outflow for the first quarter to about \$8 billion. For 1977 as a whole, net private bank outflow was \$4.7 billion.

Foreign official assets in the United States (excluding OPEC holdings) increased by nearly \$8 billion in March,

. The net foreign inflow of \$13.5 billion for the first quarter was nearly as large as the inflow in the final quarter of last year. In April foreign official holdings at the New York Federal Reserve declined by more than \$3 billion,

. Assets of OPEC official accounts in the United States increased by \$1.3 billion in the first quarter. Preliminary data indicate that OPEC holdings showed little change in April.

Total new borrowing on international capital markets (Euro-credit, Euro-bond, and foreign bond markets) in the first quarter of 1978 expanded at a record rate -- about one-third larger at an annual rate than the 1977 total of \$67 billion. The sharp increase in medium-term Euro-credits reflected stronger demand for new funds by all major categories of borrowers. Loan spreads fell further, and the average maturity of credits lengthened considerably.

There are still no clear signs of a widespread and sustained economic expansion abroad; indeed, latest statistics are somewhat

disappointing. In Germany, industrial production declined in March for the second successive monthly decline. While industrial production in Japan advanced in March, there is little evidence of a recovery of private domestic demand. Large current-account imbalances persisted in the first quarter. Japan recorded a \$5.5 billion surplus (not annual rate), and preliminary data indicate no reduction in the German surplus. The U.K.'s external position worsened in the first quarter, with the current-account returning to deficit following two successive quarterly surpluses.

Outlook. The projected trade deficit for the year has been raised to \$39 billion, nearly \$2 billion higher than projected in last month's green book. The change in the projection is the result of a reassessment of recent published first-quarter trade data that showed non-oil imports even higher than were projected last month. Even though we expect non-oil imports to increase only marginally for the rest of the year (an increase more than accounted for by rising import prices), given the large increase in these imports in the first quarter, the value of imports for the full year is projected to be somewhat higher than was projected last month. This import increase is expected to be offset somewhat by slightly higher agricultural exports in 1978. We now expect a levelling off of the trade deficit at a rate of about \$36 billion starting in the third quarter of this year.

The staff's projection for the trade deficit for the next five quarters is substantially higher than what is generally anticipated currently by market participants. For this reason, the staff continues to expect a significant decline in the average value of the dollar in the year ahead from the higher level reached in recent weeks.

	1976	1977 <sup>F</sup>	1978 <sup>P</sup>	1977 <sup>F</sup>				1978 <sup>P</sup>				1979 <sup>P</sup>	
				I	II	III	IV	I	II	III	IV	I	II
1. <b>GNP NET EXPORTS</b> - Intl Acct. data	7.8	-10.6	-13.5	-9.3	-5.5	-5.7	-21.7	-20.8	-15.1	-9.5	-8.7	-7.2	-7.4
2. (GNP net exports - GNP Acct. data) <u>1/</u>	(7.8)	(-10.9)	(-15.3)	(-8.2)	(-9.7)	(-7.5)	(-18.2)	(-22.6*)	(-16.9)	(-11.4)	(-10.5)	(-9.0)	(-9.2)
3. a) Merchandise Trade Balance	-9.3	-31.5	-39.1	-30.0	-27.3	-29.1	-39.6	-44.8*	-40.3	-35.7	-35.6	-35.6	-36.2
4. Exports (excl. military)	114.7	120.5	133.6	117.9	122.4	123.9	117.7	122.3*	130.7	137.8	143.5	150.1	156.0
5. Agricultural	23.4	24.4	26.3	24.9	26.1	23.8	22.6	26.0*	26.4	26.4	26.4	27.0	27.0
6. Nonagricultural	91.3	96.1	107.3	93.0	96.3	100.1	95.1	96.4*	104.3	111.4	117.1	123.1	129.0
7. Imports	124.0	152.0	172.7	147.9	149.7	153.0	157.3	167.1*	171.0	173.5	179.1	185.7	192.2
8. Petroleum and petrol. products	34.6	45.0	44.4	46.3	46.1	45.2	42.2	39.9*	43.0	45.5	49.1	50.7	52.2
9. Nonpetroleum	89.4	107.0	128.3	101.6	103.6	107.8	115.1	127.3*	128.0	128.0	130.0	135.0	140.0
10. b) Military transactions, net <u>2/</u>	--	1.0	2.6	1.7	.8	1.8	-.2	2.1	2.4	2.8	3.1	3.5	3.6
11. c) Investment income, net <u>3/</u>	14.3	17.4	20.3	17.6	18.9	18.2	15.2	19.3	20.1	20.7	20.9	22.1	22.2
12. d) Other services, net <u>4/</u>	2.7	2.5	2.7	1.4	2.2	3.3	2.9	2.6	2.7	2.7	2.9	2.8	2.9
13. <b>U.S. CURRENT ACCOUNT BALANCE</b>	-1.4	-20.5	-28.5	-18.6	-15.0	-16.1	-32.2	-34.9	-29.7	-24.5	-24.9	-24.5	-25.3
14. a) GNP net exports (line 1.)	7.8	-10.6	-13.5	-9.3	-5.5	-5.7	-21.7	-20.8	-15.1	-9.5	-8.7	-7.2	-7.4
15. b) U.S. Govt & private transfers <u>5/</u>	-9.2	-9.9	-15.0	-9.2	-9.5	-10.5	-10.5	-14.1	-14.6	-15.0	-16.2	-17.3	-17.9
<b>Constant (1972) dollars</b>													
16. Merchandise exports (excl. military)	66.7	66.9	69.0	66.2	67.7	68.9	65.2	65.5	68.3	70.6	72.2	73.9	75.5
17. (% change, annual rates)	(3.4)	(0.3)	(3.4)	(-7.0)	(9.1)	(7.4)	(-24.8)	(2.8)	(18.3)	(13.9)	(9.5)	(9.5)	(9.1)
18. Merchandise imports	62.8	71.2	74.7	71.0	70.2	70.8	72.7	74.3	74.7	74.4	75.2	76.1	77.6
19. (% change, annual rates)	(22.5)	(13.4)	(4.8)	(33.5)	(-4.5)	(3.7)	(10.8)	(9.1)	(2.0)	(-1.6)	(4.5)	(4.9)	(8.2)
<b>Foreign Outlook - Major Industrial Countries <u>6/</u></b>													
20. Real GNP, % change, annual rates	5.2	2.9	3.7	5.3	.4	0.8	3.7	4.9	4.5	4.1	4.1	4.5	4.1
21. Wholesale Prices, % change, A.R. <u>7/</u>	9.4	8.7	4.8	10.4	7.4	3.7	2.8	4.5	6.1	5.7	5.7	5.7	5.7

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.