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June 23, 1982

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

Recent Developments. Broad measures of economic performance suggest that the cyclical decline in activity was ending in May. Payroll employment and industrial production were little changed, while auto demand, other retail sales, and housing starts advanced. However, fixed capital outlays, which declined moderately earlier in the recession, have dropped in recent months, and recent reductions in spending commitments point to further weakness in the months ahead. Consumer prices rose more rapidly in May than earlier this year as food prices accelerated and energy prices retraced some of their recent decline.

Industrial production edged down 0.2 percent in May, after declines of 0.8 percent in each of the two preceding months. The production of consumer goods rose again, primarily due to a 10 percent advance in auto assemblies. Auto manufacturers scheduled a further 9 percent increase in June, to a 6.1 million unit annual rate. In contrast, output of primary metals and business equipment continued to drop sharply in May.

Nonfarm payroll employment flattened in May after declining about 160,000 in each of the preceding four months. Employment in manufacturing was about unchanged in May, while job growth resumed at trade establishments. An earlier-than-usual influx of summer workers swelled the household survey's total employment count; but the unemployment rate also edged up 0.1 percentage point to 9.5 percent.

Retail sales increased 1.5 percent in May, following a smaller rise a month earlier. Unit sales of domestic cars rose from a 5.5 million annual rate in April to a 6.4 million unit pace in May, and sales remained

above 6 million units in the first ten days of June. Spending for consumer goods other than autos rose 1 percent in May, with large gains reported at apparel and general merchandise outlets. At the same time, surveys of consumer attitudes indicate a second month of slight recovery in household confidence.

Capital spending was weak in April and showed signs of widespread deterioration, reflecting the low level of capacity utilization (70.8 percent), reduced profits, and the high cost of capital. Shipments of nondefense capital goods rose nearly 5 percent in May largely offsetting the April decline; on balance, the April-May average was 2-3/4 percent below the first quarter level. Near-term commitments data for capital goods and nonresidential construction suggest further weakness in the second half of 1982. Moreover, the most recent Commerce Department survey of plant and equipment spending reported a significant downward revision to business investment plans for 1982 as a whole.

Housing starts climbed above a 1 million unit pace in May for the first time in nine months, with an especially large gain in the multi-family sector. A strong recovery in homebuilding still seems remote, however; home sales declined in April to the lowest level of the current downturn, and the downtrend in mortgage interest rates from their autumn peak has stalled recently at nearly 17 percent.

Inventories in constant dollars rose at a \$3.5 billion annual rate in April, following four months of sharp liquidation. While most manufacturing firms and retailers continued to draw from their stocks in April, merchant wholesalers reported a large stock buildup. The aggregate inventory liquidation since December has eliminated much of the

stock pile-up that occurred during the last half of 1981, returning the constant dollar value of inventories in April to their pre-recession level. However, with unit sales considerably lower than a year ago, inventory-to-sales ratios are still close to their recent highs.

Export demand remained weak in April. Exports have been declining since the middle of last year as a result of weak economic activity abroad and the impact of the strong dollar.

Slack demand and the wide margin of unutilized resources continued to generate downward pressure on both prices and wages, although food and energy prices accelerated sharply in May. Excluding the volatile food, energy, and homeownership components, consumer prices rose 0.4 percent in May; over the first five months of 1982 they increased at a 5-1/2 percent annual rate, down from 9-1/2 percent in 1981. At the producer level, inflation for finished goods has been close to zero for the last four months.

Measures of both wages and compensation have shown significant slowing so far in 1982. The wages of production workers have increased at a 6.6 percent rate in 1982, compared with 8.4 percent during 1981, and wages of white collar workers, which had continued to rise rapidly through the fourth quarter of 1981, have increased more slowly. Employers also are restraining the rate of increase in benefit costs.

Outlook. Real GNP in the second quarter is estimated to have edged up at about a one-half percent annual rate--the same as in the last Greenbook. The rise in real GNP reflects a sharp reduction in the rate of inventory liquidation; final sales are projected to have declined at a 1-1/4 percent annual rate. The major source of support for final

demand was an increase in consumer spending, while business investment, particularly for capital equipment, probably declined sharply. Price deceleration has been widespread this year, with declines in gasoline prices a dominant influence. Falling energy prices, along with lower-than-anticipated food prices, slowed the rise in the fixed-weighted price index for gross domestic business product during the second quarter to a 4 percent annual rate, compared with 5 percent projected in the May Greenbook.

The staff's monetary policy assumption has been altered somewhat for this projection. M1 still is assumed to grow about 5 percent over the four quarters of 1982, but it now is assumed to rise 4-1/2 percent during 1983, one percentage point faster than in the May Greenbook. Interest rates are expected to remain at very high levels in real terms, with nominal rates edging down slightly on balance from current levels over the next few quarters before firming again as private credit demands strengthen.

The thrust of fiscal policy is now assumed to be a bit less expansive than projected last month, reflecting the staff's assessment of Congress' first budget resolution for FY1983. It is assumed that \$40 billion of deficit-reducing measures will be implemented in FY1983, \$10 billion more than in the May projection. The staff assumption represents about three-fifths of the initiatives proposed in the budget resolution,¹ a proportion that seems reasonable considering the additional hurdles to

1. The budget resolution assumes savings in interest costs amounting to \$14-1/2 billion; these are not included in this comparison.

be cleared--both in the Congress and the executive branch--to fully implement the intentions expressed in the resolution. For FY1982 the budget deficit is estimated to be \$113 billion; based on the staff's economic projections as well as the assumptions just mentioned, the deficit is estimated to be \$166 billion in FY1983.

Economic activity is projected to recover at a relatively sluggish pace compared with previous business cycles, as real GNP advances at about a 3 percent rate over the next six quarters. The upturn in the second half of this year is expected to be led by the consumer sector, reflecting the effects of the July 1 tax cut, and by some improvement in housing activity. Consumption outlays will be boosted again in mid-1983 by the scheduled third round of personal income tax cuts. However, the staff continues to expect that business fixed investment will retard the pace of real GNP growth over the next year and a half owing to the wide margin of underutilized capacity and expected high levels of real interest rates. In addition, a strong dollar and sluggish economic recovery abroad are expected to weaken export demand through the end of 1982.

Because firms generally increase output during the initial stages of a recovery by utilizing their work force more intensively rather than by increasing employment, the unemployment outlook is not expected to improve over the last half of 1982 from the current 9-1/2 percent rate. Output growth during 1983 is projected barely to accommodate the influx of new job seekers, and the unemployment rate is expected to decline only gradually--to about 9 percent by the end of next year.

The overall rate of inflation is projected to move up to the 6 percent range during the second half of 1982 from a 4-1/4 pace in the first half of 1982, owing largely to increases in gasoline and meat prices that have already begun. Nonetheless, the staff continues to project a declining inflation trend as underlying business costs improve throughout the projection period. Prices measured by the fixed-weighted index for gross domestic business product are expected to rise about 5-1/4 percent over the four quarters of 1982 and 4-3/4 percent during 1983, compared with 9 percent last year. The unwinding of inflationary pressures coupled with slack demand already has begun to bring down wage and benefit increases, and hourly compensation is projected to slow from last year's 9-1/4 percent pace to 7 percent during 1982 and 6 percent over 1983. Moreover, the expected cyclical improvement in productivity should help hold unit labor cost increases to about 4-1/2 percent a year throughout the projection period.

STAFF GNP PROJECTION

Percent changes, annual rate										
Nominal GNP		Real GNP		Total		Excluding food and energy		Unemployment rate (percent)		
5/12/82	6/23/82	5/12/82	6/23/82	5/12/82	6/23/82	5/12/82	6/23/82	5/12/82	6/23/82	
Annual changes:										
1980 1/	8.8	8.8	-.2	-.2	9.8	9.8	8.2	8.2	7.1	7.1
1981 1/	11.4	11.4	2.0	2.0	9.4	9.4	9.2	9.2	7.6	7.6
1982	5.4	5.3	-1.0	-1.1	6.5	6.2	7.4	7.0	9.4	9.3
1983	8.0	7.5	2.9	2.5	5.2	5.2	4.9	4.9	9.2	9.4
Quarterly changes:										
1981-Q1 1/	19.2	19.2	8.6	8.6	10.5	10.5	8.4	8.4	7.4	7.4
1981-Q2 1/	4.7	4.7	-1.6	-1.6	8.2	8.2	9.6	9.6	7.4	7.4
1981-Q3 1/	11.4	11.4	1.4	1.4	9.9	9.9	11.5	11.5	7.4	7.4
1981-Q4 1/	4.6	4.6	-4.5	-4.5	7.5	7.5	8.2	8.2	8.3	8.3
1982-Q1 1/	-.4	-.9	-3.9	-4.3	5.4	4.7	6.2	5.2	8.8	8.8
1982-Q2	6.4	6.9	.4	.7	5.0	3.8	6.8	6.0	9.5	9.5
1982-Q3	9.6	8.3	3.9	2.5	6.0	6.6	5.9	5.8	9.6	9.6
1982-Q4	9.0	8.4	3.1	2.9	5.5	5.7	5.2	5.3	9.5	9.5
1983-Q1	7.1	6.6	2.3	1.9	5.2	5.1	4.7	5.0	9.4	9.5
1983-Q2	7.3	6.5	2.5	2.0	4.9	4.9	4.4	4.6	9.3	9.5
1983-Q3	8.7	8.1	4.6	4.1	4.4	4.5	4.2	4.0	9.1	9.3
1983-Q4	8.6	8.6	3.5	4.0	4.4	4.3	4.1	3.7	8.8	9.1
Two-quarter changes: <2>										
1981-Q2 1/	11.7	11.7	3.4	3.4	9.2	9.2	9.0	9.0	-.1	-.1
1981-Q4 1/	7.9	7.9	-1.6	-1.6	8.7	8.7	9.8	9.8	.9	.9
1982-Q2	2.9	3.4	-1.8	-1.5	5.3	4.2	6.5	5.6	1.2	1.2
1982-Q4	9.3	8.4	3.5	2.7	5.8	6.1	5.5	5.5	.0	.0
1983-Q2	7.2	6.6	2.4	1.9	5.1	5.0	4.6	4.8	-.2	.0
1983-Q4	8.7	8.4	4.1	4.1	4.4	4.4	4.1	3.8	-.5	-.4
Four-quarter changes: <3>										
1980-Q4 1/	9.4	9.4	-.3	-.3	9.7	9.7	8.6	8.6	1.5	1.5
1981-Q4 1/	9.8	9.8	.9	.9	9.0	9.0	9.4	9.4	.8	.8
1982-Q4	6.1	5.8	.8	.6	5.5	5.2	6.0	5.6	1.2	1.2
1983-Q4	7.9	7.5	3.2	3.0	4.8	4.7	4.4	4.3	-.7	-.4

<1> Actual.

<2> Percent change from two quarters earlier.

<3> Percent change from four quarters earlier.

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

	1980				1981			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	2571.7	2564.8	2637.3	2730.6	2853.0	2885.8	2965.0	2998.3
Final purchases	2569.1	2557.4	2653.4	2748.0	2848.5	2862.5	2937.6	2989.0
Private	2052.3	2027.4	2119.9	2189.4	2272.0	2285.1	2348.7	2367.0
Excluding net exports	2044.1	2010.3	2075.4	2166.1	2242.8	2264.3	2319.4	2342.3
Personal consumption expenditures	1631.0	1626.8	1682.2	1751.0	1810.1	1829.1	1883.9	1908.3
Goods	882.0	858.4	883.0	926.8	964.3	962.6	987.5	986.7
Services	749.0	768.4	799.2	824.2	845.8	866.5	896.4	921.5
Gross private domestic investment	415.6	390.9	377.1	397.7	437.1	458.6	463.0	443.3
Residential structures	115.2	93.6	99.2	113.0	116.7	110.7	100.5	94.2
Business fixed investment	297.8	289.8	294.0	302.1	315.9	324.6	335.1	339.8
Change in business inventories	2.5	7.4	-16.0	-17.4	4.5	23.3	27.5	9.4
Nonfarm	1.5	6.1	-12.3	-14.0	6.8	21.5	23.1	3.7
Net exports of goods and services <1>	8.2	17.1	44.5	23.3	29.2	20.8	29.3	24.7
Exports	337.3	333.3	342.4	346.1	367.4	368.2	368.0	365.6
Imports	329.1	316.2	297.9	322.7	338.2	347.5	338.7	341.0
Gov't purchases of goods and services	516.8	530.0	533.5	558.6	576.5	577.4	588.9	622.0
Federal <2>	190.0	198.7	194.9	212.0	221.6	219.5	226.4	253.3
State and local	326.8	331.3	338.6	346.6	354.9	357.9	362.5	368.7
Gross national product in constant (1972) dollars	1501.9	1463.3	1471.9	1485.6	1516.4	1510.4	1515.8	1498.4
Personal income	2088.2	2114.5	2182.1	2256.2	2319.8	2368.5	2441.7	2486.5
Wage and salary disbursements	1314.7	1320.4	1341.8	1397.8	1442.9	1467.0	1498.5	1522.5
Disposable personal income	1765.1	1784.1	1840.6	1897.0	1947.8	1985.6	2042.0	2088.5
Saving rate (percent)	4.9	6.2	6.1	5.1	4.6	5.4	5.2	6.1
Corporate profits with I.V.A. and C.C.Adj.	200.2	169.3	177.9	183.3	203.0	190.3	195.7	177.6
Corporate profits before tax	277.1	217.9	237.6	249.5	257.0	229.0	234.4	212.8
Federal government surplus or deficit (-) (N.I.A. basis)	-36.3	-66.5	-74.2	-67.9	-46.6	-47.2	-55.7	-100.0
High employment surplus or deficit(-) <3>	-18.3	-21.7	-24.2	-16.8	-1.3	10.6	4.3	-24.8
State and local government surplus or deficit(-) (N.I.A. basis)	26.6	23.9	28.6	37.1	36.9	36.1	37.8	35.9
Excluding social insurance funds	1.3	-1.7	.9	8.1	6.6	4.3	5.1	2.2
Civilian labor force (millions)	106.5	106.8	107.2	107.5	108.1	108.8	108.7	109.2
Unemployment rate (percent)	6.3	7.3	7.7	7.5	7.4	7.4	7.4	8.4
Nonfarm payroll employment (millions)	90.9	90.3	89.9	90.5	91.0	91.2	91.4	91.0
Manufacturing	20.9	20.3	19.9	20.1	20.2	20.3	20.3	19.9
Industrial production (1967=100)	152.7	144.5	142.3	148.8	151.8	152.5	153.0	146.3
Capacity utilization: all manufacturing (percent)	83.4	77.9	75.9	79.1	79.9	79.8	79.2	74.8
Materials (percent)	85.8	78.9	75.2	80.1	82.2	81.2	81.2	75.2
Housing starts, private (million units, A.R.)	1.25	1.06	1.39	1.50	1.40	1.17	.96	.87
New auto sales (millions, A.R.)	10.65	7.68	8.80	9.04	9.96	7.89	9.04	7.36
Domestic models	7.87	5.53	6.51	6.57	7.31	5.63	6.90	5.13
Foreign models	2.77	2.14	2.29	2.47	2.66	2.25	2.14	2.23

<1> Balance of payments data and details underlying these estimates are shown in the International Developments section in 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 \$36.9 billion in 1980-Q4, and a deficit of \$47.2 billion in 1981-Q4.

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PERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	1980				1981			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	3.1	-9.9	2.4	3.8	8.6	-1.6	1.4	-4.5
Final purchases	3.1	-10.4	4.1	4.4	6.9	-4.7	.3	-1.8
Private	2.2	-13.3	6.5	4.9	7.3	-4.5	.8	-4.5
Excluding net exports	-.4	-14.4	4.6	8.5	6.7	-3.2	1.9	-3.3
Personal consumption expenditures	.8	-9.8	5.1	7.0	5.8	-2.1	3.3	-2.2
Goods	-.3	-17.7	4.0	10.2	9.8	-5.3	3.8	-5.5
Services	2.1	.0	6.4	3.7	1.4	1.6	2.6	1.7
Gross private domestic investment	-5.6	-28.9	-10.0	11.1	24.2	16.1	3.3	-24.7
Residential structures	-24.2	-60.2	16.0	64.2	3.6	-23.4	-36.2	-27.1
Business fixed investment	2.2	-19.9	-1.5	4.0	13.3	-2.1	6.9	-2.9
Gov't purchases of goods and services	6.9	2.5	-5.0	2.2	5.4	-5.6	-1.5	10.2
Federal	18.9	11.9	-13.1	2.0	14.8	-8.4	3.1	28.2
National defense	9.8	6.2	-.1	5.9	1.1	2.6	7.9	16.3
State and local	.6	-2.8	.3	2.3	.2	-3.8	-4.2	.1
Disposable personal income	1.3	-4.9	4.1	2.9	3.0	1.4	2.6	1.6
<u>Current Dollars</u>								
Gross national product	12.6	-1.1	11.8	14.9	19.2	4.7	11.4	4.6
Final purchases	12.0	-1.8	15.9	15.0	15.5	2.0	10.9	7.2
Private	10.7	-4.8	19.5	13.8	16.0	2.3	11.6	3.2
Excluding net exports	10.6	-6.5	13.6	18.7	14.9	3.9	10.1	4.0
Personal consumption expenditures	12.9	-1.0	14.3	17.4	14.2	4.3	12.5	5.3
Goods	13.1	-10.3	12.0	21.4	17.2	-.7	10.8	-.3
Services	12.7	10.8	17.0	13.1	10.9	10.1	14.6	11.7
Gross private domestic investment	5.6	-21.8	-13.3	23.7	45.9	21.1	3.9	-16.0
Residential structures	-16.7	-56.4	25.7	68.5	14.0	-19.2	-32.1	-22.9
Business fixed investment	11.0	-10.4	6.0	11.5	19.6	11.4	13.6	5.8
Gov't purchases of goods and services	17.5	10.6	2.6	20.2	13.5	.6	8.2	24.5
Federal	29.5	19.8	-7.5	40.2	19.3	-3.7	13.1	56.7
National defense	23.2	12.4	8.4	35.0	10.4	8.7	16.9	47.0
State and local	11.2	5.6	9.1	9.7	10.0	3.3	5.3	7.1
Disposable personal income	13.5	4.4	13.3	12.8	11.2	8.0	11.8	9.4
Personal income	11.5	5.1	13.4	14.3	11.8	8.7	13.0	7.5
Wage and salary disbursements	10.5	1.8	6.6	17.8	13.5	6.9	8.9	6.6
Corporate profits with I.V.A. and C.C.Adj.	24.8	-48.9	21.9	12.7	50.4	-22.8	11.8	-32.2
Corporate profits before tax	38.6	-61.8	41.4	21.6	12.6	-37.0	9.8	-32.1
Nonfarm payroll employment	1.9	-2.3	-1.8	2.7	1.8	1.0	.8	-1.8
Manufacturing	-1.2	-10.4	-7.5	4.3	1.3	2.8	.1	-8.1
Nonfarm business sector								
Output per hour	.3	-2.9	3.6	-.2	4.4	1.4	-1.7	-6.9
Compensation per hour	10.3	11.3	9.0	9.8	11.7	9.6	9.5	6.3
Unit labor cost	9.9	14.6	5.3	10.1	7.0	8.1	11.5	14.1
GNP implicit deflator <1>	9.3	9.8	9.2	10.7	9.8	6.4	9.9	9.5
Gross domestic business product								
fixed-weighted price index <2>								
Excluding food and energy	7.4	9.5	9.3	8.2	8.4	9.6	11.5	8.2
Consumer price index (all urban)	16.5	13.5	7.7	12.8	11.0	7.8	11.8	7.7
Industrial production	.4	-19.8	-5.8	19.3	8.4	1.9	1.4	-16.6

<1> Excluding Federal pay increases, rates of change were: 1980-Q1, 9.2 percent; 1981-Q1, 9.7 percent; 1981-Q4, 7.4 percent.

<2> Uses expenditures in 1972 as weights.

June 23, 1982

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.)

	1982				Projected			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	2998.4	3048.7	3110.0	3173.4	3224.6	3276.0	3340.3	3410.3
Final purchases	3035.3	3068.2	3116.0	3170.9	3219.1	3269.5	3335.8	3405.3
Private	2408.9	2440.4	2481.1	2524.4	2563.7	2603.2	2658.2	2712.6
Excluding net exports	2377.4	2395.6	2444.5	2498.4	2545.4	2589.4	2649.1	2705.1
Personal consumption expenditures	1946.7	1971.1	2025.0	2071.6	2107.6	2143.6	2193.6	2237.4
Goods	999.8	1002.2	1029.6	1052.2	1066.2	1080.2	1105.2	1126.0
Services	946.9	968.9	995.4	1019.4	1041.4	1063.4	1088.4	1111.4
Gross private domestic investment	393.8	405.0	413.5	429.3	443.3	452.3	460.0	472.7
Residential structures	92.2	92.2	96.2	101.7	109.2	112.7	116.7	122.2
Business fixed investment	338.4	332.3	323.3	325.1	328.6	333.1	338.8	345.5
Change in business inventories	-36.8	-19.5	-6.0	2.5	5.5	6.5	4.5	5.0
Nonfarm	-35.7	-19.5	-6.0	2.5	5.5	6.5	4.5	5.0
Net exports of goods and services <1>	31.5	44.8	36.6	26.0	18.3	13.8	9.1	7.5
Exports	356.9	356.4	357.8	359.0	363.3	370.1	380.1	393.2
Imports	325.4	311.6	321.2	333.0	345.0	356.3	371.0	385.7
Gov't purchases of goods and services	626.4	627.7	634.8	646.5	655.4	666.3	677.6	692.7
Federal <2>	253.6	250.0	252.3	259.3	263.7	270.1	276.9	287.5
State and local	372.8	377.7	382.5	387.2	391.7	396.2	400.7	405.2
Gross national product in constant (1972) dollars	1484.5	1487.1	1496.2	1506.8	1513.9	1521.2	1536.7	1551.9
Personal income	2511.4	2548.1	2601.7	2650.4	2698.6	2743.6	2799.8	2853.2
Wage and salary disbursements	1538.6	1548.1	1570.6	1599.3	1623.1	1647.0	1675.7	1711.3
Disposable personal income	2113.3	2146.5	2217.8	2259.1	2298.4	2332.7	2405.8	2447.2
Saving rate (percent)	5.4	5.7	6.3	5.9	5.9	5.7	6.4	6.2
Corporate profits with I.V.A. and C.C.Adj.	152.2	168.9	178.9	188.5	189.7	195.6	206.3	215.3
Corporate profits before tax	171.8	185.2	195.5	196.9	192.1	190.9	193.7	193.3
Federal government surplus or deficit (-) (N.I.A. basis)	-123.5	-132.2	-165.4	-170.6	-165.7	-172.0	-211.4	-215.2
High employment surplus or deficit (-) <3>	-33.4	-29.4	-58.8	-58.9	-45.0	-46.7	-91.4	-96.4
State and local government surplus or deficit (-) (N.I.A. basis)	36.3	40.6	43.6	44.1	42.9	43.5	46.4	49.0
Excluding social insurance funds	1.5	4.4	5.9	4.9	2.2	1.3	2.7	3.8
Civilian labor force (millions)	109.1	110.0	110.2	110.5	110.8	111.1	111.4	111.6
Unemployment rate (percent)	8.8	9.5	9.6	9.5	9.5	9.5	9.3	9.1
Nonfarm payroll employment (millions)	90.4	90.0	89.9	90.1	90.3	90.5	90.8	91.4
Manufacturing	19.4	19.2	19.2	19.3	19.4	19.6	19.8	20.0
Industrial production (1967=100)	141.8	140.3	141.5	143.6	144.8	146.0	149.0	151.2
Capacity utilization: all manufacturing (percent)	71.7	70.8	71.1	71.7	71.8	71.9	73.0	73.7
Materials (percent)	72.0	70.0	70.6	71.9	72.4	72.8	74.5	75.6
Housing starts, private (million units, A.R.)	0.92	1.00	1.10	1.15	1.20	1.20	1.25	1.25
New auto sales (millions, A.R.)	8.12	7.90	8.70	8.80	8.90	8.90	9.30	9.30
Domestic models	5.90	5.90	6.40	6.50	6.60	6.60	6.90	6.90
Foreign models	2.22	2.00	2.30	2.30	2.30	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.

> 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 \$81.7 billion in 1982-Q4, and a deficit of \$120.6 billion in 1983-Q4.

CONFIDENTIAL - FR
CLASS II FOMC

PERCENT CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS
(Annual rates compounded quarterly)

	-----Projected-----							
	1982				1983			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	-3.7	.7	2.5	2.9	1.9	2.0	4.1	4.0
Final purchases	2.0	-1.3	.7	1.7	1.5	1.8	4.4	4.0
Private	2.5	.0	1.0	2.3	1.7	1.8	5.0	4.5
Excluding net exports	2.5	-1.0	2.0	3.6	2.6	2.2	5.1	4.5
Personal consumption expenditures	3.4	1.4	4.6	4.0	2.0	2.1	5.1	4.0
Goods	3.4	.5	5.2	4.4	1.4	1.4	5.9	4.2
Services	3.2	2.5	3.9	3.5	2.8	3.0	4.3	3.7
Gross private domestic investment	-36.2	2.1	3.3	11.4	8.6	3.7	2.4	7.4
Residential structures	-10.0	-3.9	12.9	18.8	26.6	8.1	10.1	15.4
Business fixed investment	.9	-13.8	-15.4	-2.3	.0	1.2	3.0	4.5
Gov't purchases of goods and services	.0	-6.4	-.6	-.7	.7	2.1	2.2	1.5
Federal	3.8	-13.5	.5	-.7	3.1	6.2	6.2	4.8
National defense	-2.9	9.9	5.7	1.3	6.3	11.1	12.2	9.2
State and local	-2.4	-1.5	-1.2	-.7	-.7	-.6	-.5	-.6
Disposable personal income	.0	2.7	7.0	2.2	2.0	1.3	8.5	2.8
<u>Current Dollars</u>								
Gross national product	.0	6.9	8.3	8.4	6.6	6.5	8.1	8.7
Final purchases	6.3	4.4	6.4	7.2	6.2	6.4	8.4	8.6
Private	7.3	5.3	6.8	7.2	6.4	6.3	8.7	8.4
Excluding net exports	6.1	3.1	8.4	9.1	7.7	7.1	9.6	8.7
Personal consumption expenditures	8.3	5.1	11.4	9.5	7.1	7.0	9.7	8.2
Goods	5.4	1.0	11.4	9.1	5.4	5.4	9.6	7.7
Services	11.5	9.6	11.4	10.0	8.9	8.7	9.7	8.7
Gross private domestic investment	-37.7	11.9	8.7	16.1	13.7	8.4	7.0	11.5
Residential structures	-8.2	.0	18.5	24.7	32.9	13.5	15.0	20.2
Business fixed investment	-1.6	-7.0	-10.4	2.3	4.4	5.6	7.0	8.2
Gov't purchases of goods and services	2.9	.8	4.6	7.6	5.6	6.8	7.0	9.2
Federal	.5	-5.5	3.7	11.6	7.0	10.1	10.5	16.2
National defense	-.1	14.3	10.7	15.2	11.2	15.7	17.1	21.5
State and local	4.5	5.4	5.2	5.0	4.7	4.7	4.6	4.6
Disposable personal income	4.8	6.4	14.0	7.7	7.1	6.1	13.2	7.1
Personal income	4.1	6.0	8.7	7.7	7.5	6.8	8.5	7.9
Wage and salary disbursements	4.3	2.5	5.9	7.5	6.1	6.0	7.2	8.8
Corporate profits with I.V.A. and C.C.Adj.	-46.1	51.8	25.8	23.2	2.7	13.1	23.7	18.6
Corporate profits before tax	-57.5	35.2	24.1	2.8	-9.3	-2.4	5.9	-.9
Nonfarm payroll employment	-2.4	-1.9	-.1	.6	1.0	.7	1.6	2.3
Manufacturing	-9.0	-5.5	.0	2.9	2.8	3.7	4.2	4.2
Nonfarm business sector								
Output per hour	.5	3.3	2.6	2.2	.9	.9	2.7	1.7
Compensation per hour	7.9	6.7	6.5	6.3	6.6	5.9	5.8	5.6
Unit labor cost	7.3	3.3	3.8	4.0	5.7	4.9	3.1	3.8
GNP implicit deflator	3.8	6.1	5.7	5.4	4.6	4.5	3.8	4.5
Gross domestic business product								
fixed-weighted price index <1>	4.7	3.8	6.6	5.7	5.1	4.9	4.5	4.3
Excluding food and energy	5.2	6.3	5.8	5.3	5.0	4.6	4.0	3.7
Consumer price index (all urban)	3.2	4.5	6.6	5.5	5.1	4.9	4.7	4.5
Industrial production	-11.7	-4.2	3.5	6.1	3.4	3.4	8.5	6.0

<1> Excluding Federal pay increases, the rates of change are: 1982-Q1, 3.7 percent; 1982-Q4, 4.8 percent; 1983-Q1, 4.6 percent; 1983-Q4, 3.8 percent.

June 23, 1982

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

	1976	1977	1978	1979	1980	1981	-----Projected-----	
							1982	1983
Gross national product	1718.0	1918.0	2156.1	2413.9	2626.1	2925.5	3082.6	3312.8
Final purchases	1706.2	1897.0	2133.9	2396.4	2632.0	2909.4	3097.6	3307.5
Private	1344.1	1502.5	1701.3	1922.6	2097.3	2318.2	2463.7	2634.4
Excluding net exports	1330.3	1506.8	1701.9	1909.2	2074.0	2292.2	2429.0	2622.3
Personal consumption expenditures	1084.3	1205.5	1348.7	1510.9	1672.8	1857.8	2003.6	2170.6
Goods	598.6	657.8	729.1	814.6	887.6	975.2	1021.0	1094.4
Services	485.7	547.7	619.6	696.3	785.2	882.6	982.6	1076.2
Gross private domestic investment	257.9	322.3	375.3	415.8	395.3	450.5	410.4	457.1
Residential construction	72.0	95.8	111.2	118.6	105.3	105.5	95.6	115.2
Business fixed investment	174.1	205.5	242.0	279.7	296.0	328.9	329.8	336.5
Change in business inventories	11.8	21.0	22.2	17.5	-5.9	16.2	-15.0	5.4
Nonfarm	13.9	20.2	21.8	13.4	-4.7	13.8	-14.7	5.4
Net exports of goods and services <1>	13.8	-4.2	-0.6	13.4	23.3	26.0	34.7	12.2
Exports	170.9	183.3	219.8	281.3	339.8	367.3	357.5	376.7
Imports	157.1	187.5	220.4	267.9	316.5	341.3	322.8	364.5
Gov't purchases of goods and services	362.1	394.5	432.6	473.8	534.7	591.2	633.9	673.0
Federal <2>	129.2	143.9	153.4	167.9	198.9	230.2	253.8	274.6
State and local	232.9	250.6	279.2	305.9	335.8	361.0	380.1	398.5
Gross national product in constant (1972) dollars	1300.4	1371.7	1436.9	1483.0	1480.7	1510.3	1493.7	1530.9
Personal income	1391.2	1538.0	1721.8	1943.8	2160.2	2404.1	2577.9	2773.8
Wage and salary disbursements	889.9	983.8	1105.2	1236.1	1343.7	1482.7	1564.2	1664.3
Disposable personal income	1194.4	1311.5	1462.9	1641.7	1821.7	2016.0	2184.2	2371.0
Saving rate (percent)	6.9	5.7	5.2	5.3	5.6	5.3	5.8	6.1
Corporate profits with I.V.A. and C.C.Adj.	138.1	164.7	185.5	196.8	182.7	191.7	172.1	201.7
Corporate profits before tax	166.3	192.6	223.3	255.4	245.5	233.3	187.4	192.5
Federal government surplus or deficit(-) (N.I.A. basis)	-53.1	-46.4	-29.2	-14.8	-61.2	-62.4	-147.9	-191.1
High employment surplus or deficit(-)	-17.4	-21.7	-15.1	-2.1	-20.3	-2.8	-45.1	-69.9
State and local government surplus or deficit (-) (N.I.A. basis)	16.6	28.1	29.0	26.7	29.1	36.7	41.2	45.5
Excluding social insurance funds	.9	10.1	9.0	2.9	2.1	4.6	4.2	2.5
Civilian labor force (millions)	96.2	99.0	102.2	105.0	107.0	108.7	110.0	111.2
Unemployment rate (percent)	7.7	7.1	6.1	5.9	7.2	7.6	9.3	9.4
Nonfarm payroll employment (millions)	79.4	82.5	86.7	89.8	90.4	91.1	90.1	90.7
Manufacturing	19.0	19.7	20.5	21.0	20.3	20.2	19.3	19.7
Industrial production (1967=100)	130.4	138.1	146.1	152.5	147.1	150.9	141.8	147.8
Capacity utilization: all manufacturing (percent)	79.5	81.9	84.4	85.6	79.1	78.4	71.3	72.6
Materials (percent)	81.1	82.7	85.6	87.4	80.0	79.9	71.1	73.8
Housing starts, private (million units, A.R.)	1.54	1.96	2.00	1.72	1.30	1.10	1.04	1.23
New auto sales (millions, A.R.)	10.12	11.13	11.29	10.68	9.04	8.56	8.42	9.10
Domestic models	8.63	9.07	9.29	8.36	6.62	6.24	6.19	6.75
Foreign models	1.49	2.06	2.00	2.32	2.42	2.32	2.22	2.35

<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.

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

	1976	1977	1978	1979	1980	1981	--Projected--	
							1982	1983
CONSTANT (1972) DOLLARS								
Gross national product	5.4	5.5	4.8	3.2	-.2	2.0	-1.1	2.5
Final purchases	4.2	5.2	4.7	3.5	.7	1.3	-.2	1.8
Private	5.3	6.0	5.4	4.0	.2	1.5	-.2	2.2
Excluding net exports	6.2	6.5	5.2	2.9	-1.0	2.2	.3	2.8
Personal consumption expenditures	5.6	4.9	4.7	2.9	.5	2.6	1.8	3.2
Goods	6.7	5.2	4.2	1.9	-1.4	2.5	.9	3.1
Services	4.3	4.5	5.4	4.1	2.6	2.6	2.7	3.3
Gross private domestic investment	19.2	15.7	7.6	1.3	-12.5	5.5	-12.9	6.2
Residential structures	21.3	18.4	3.0	-5.3	-18.6	-6.0	-13.4	15.0
Business fixed investment	5.3	11.9	9.1	6.5	-3.0	2.5	-4.5	-2.6
Gov't purchases of goods and services	.0	2.1	2.0	1.4	2.9	.6	-.1	-.3
Federal	-.6	4.0	-.9	1.9	6.3	3.2	2.8	2.0
National defense	-2.3	.7	.0	2.6	5.7	4.2	5.9	7.3
State and local	.4	.9	3.7	1.2	.4	-.4	-1.8	-.8
Disposable personal income	3.6	3.6	4.4	3.1	.7	2.2	2.2	3.4
CURRENT DOLLARS								
Gross national product	10.9	11.6	12.4	12.0	8.8	11.4	5.4	7.5
Final purchases	9.7	11.2	12.5	12.3	9.8	10.5	6.5	6.8
Private	10.5	11.8	13.2	13.0	9.1	10.5	6.3	6.9
Excluding net exports	11.9	13.3	13.0	12.2	8.6	10.5	6.0	8.0
Personal consumption expenditures	11.0	11.2	11.9	12.0	10.7	11.1	7.9	8.3
Goods	10.9	9.9	10.8	11.7	9.0	9.9	4.7	7.2
Services	11.2	12.8	13.1	12.4	12.8	12.4	11.3	9.5
Gross private domestic investment	25.1	25.0	16.5	10.8	-4.9	14.0	-8.9	11.4
Residential construction	30.2	33.1	16.1	6.6	-11.2	.2	-9.4	20.5
Business fixed investment	10.4	18.1	17.7	15.6	5.8	11.1	.3	2.0
Gov't purchases of goods and services	6.5	8.9	9.7	9.5	12.9	10.6	7.2	6.2
Federal	5.3	11.4	6.6	9.5	18.5	15.7	10.3	8.2
National defense	3.6	8.5	7.1	11.2	18.4	17.2	15.3	14.3
State and local	7.3	7.6	11.4	9.6	9.8	7.5	5.3	4.8
Disposable personal income	9.0	9.8	11.5	12.2	11.0	10.7	8.3	8.6
Personal income	10.0	10.6	12.0	12.9	11.1	11.3	7.2	7.6
Wage and salary disbursements	10.4	10.6	12.3	11.9	8.7	10.3	5.5	6.4
Corporate profits with I.V.A. and C.C.Adj.	25.0	19.3	12.6	6.1	-7.2	4.9	-10.2	17.2
Corporate profits before tax	25.9	15.8	16.0	14.4	-3.9	-5.0	-19.7	2.8
Nonfarm payroll employment	3.2	3.9	5.1	3.6	.7	.8	-1.1	.7
Manufacturing	3.7	3.6	4.2	2.6	-3.6	-.6	-4.5	2.4
Nonfarm business sector								
Output per hour	3.2	2.1	-.1	-.7	-.3	.9	-.3	1.8
Compensation per hour	8.1	7.6	8.6	9.7	10.0	10.0	7.4	6.2
Unit labor cost	4.7	5.5	8.7	10.5	10.3	9.0	7.6	4.4
GNP implicit deflator	5.2	5.8	7.3	8.5	9.0	9.2	6.5	4.9
Gross domestic business product								
fixed-weighted price index <1>	5.5	6.3	7.8	9.8	9.8	9.4	6.2	5.2
Excluding food and energy	6.0	6.5	7.5	8.4	8.2	9.2	7.0	4.9
Consumer price index (all urban)	5.7	6.5	7.7	11.3	13.5	10.3	6.2	5.2
Industrial production	10.7	5.9	5.8	4.4	-3.6	2.6	-6.0	4.2

<1> Uses expenditures in 1972 as weights.

June 23, 1982

FEDERAL SECTOR ACCOUNTS

	Fiscal Year 1981*	FY1982a/		FY1983a/2/		CY1982e/		FRB Staff Estimates Calendar quarters; unadjusted data									
		Admin. 1/	F.R. Board	Admin. 1/	F.R. Board	CY 1981*	F.R. Board	1981				1982			1983		
								IV*	I*	II	III	IV	I	II	III		
																1983	
Unified budget receipts	599.3	628.4	622.2	665.1	622.3	619.1	617.7	146.0	143.6	183.7	148.9	141.5	140.9	186.8	153.1		
Unified budget outlays	657.2	728.9	734.9	767.0	788.3	691.6	734.4	194.2	167.3	185.2	188.2	193.7	196.0	196.4	202.2		
Surplus/deficit(-), unified budget	-57.9	-100.5	-112.7	-101.9	-166.1	-72.5	-116.7	-48.2	-23.7	-1.5	-39.3	-52.2	-55.1	-9.7	-49.1		
Surplus/deficit(-), off-budget agencies ³	-21.0	-20.9	-18.7	-15.8	-18.2	-22.4	-19.3	-3.6	-2.0	-5.5	-7.6	-4.1	-5.5	-4.3	-4.3		
Combined deficit to be financed	-78.9	-121.4	-131.4	-117.7	-184.3	-94.9	-135.9	-51.8	-25.7	-7.0	-46.9	-56.3	-60.6	-14.0	-53.4		
Means of financing combined deficit:																	
Net borrowing from public	79.4	118.5	127.4	118.5	188.4	87.3	144.0	35.6	32.8	8.5	50.5	52.2	59.4	21.1	55.7		
Decrease in cash operating balance	2.3		0.5		-2.0	0.3	0.0	6.7	-1.0	-0.5	-4.7	6.2	0.4	-4.0	-4.6		
Other ⁴	-2.8	(2.9	3.5	(-0.8	-2.1	7.3	-8.1	9.5	-6.1	-1.0	1.1	-2.1	0.8	-3.1	2.3		
Cash operating balance, end of period	18.7	n.a.	18.2	n.a.	20.2	12.0	12.0	12.0	13.0	13.5	18.2	12.0	11.6	15.6	20.2		
Memo: Sponsored agency borrowing ⁵	35.7	46.6	21.6	50.1	28.5	30.0	25.1	4.0	1.6	8.7	7.3	7.5	7.0	7.0	7.0		
NIA Budget																	
								Seasonally adjusted annual rates									
Receipts	612.5	637.1	614.0	685.3	630.7	626.0	610.2	627.2	609.9	615.6	603.4	612.1	634.1	645.3	631.2		
Expenditures	667.4	744.0	744.3	794.1	810.6	688.4	760.0	727.2	733.4	747.7	768.8	782.7	799.8	817.3	842.6		
Purchases	217.8	252.4	252.3	278.4	267.5	230.2	256.4	253.3	253.6	250.0	252.3	259.3	263.7	270.1	276.9		
Defense	147.1	174.2	173.7	203.5	195.8	154.3	179.3	169.7	169.7	175.5	180.0	186.5	191.5	198.6	206.6		
Nondefense	70.7	78.2	78.5	74.9	71.7	75.9	77.1	83.5	83.9	74.5	72.3	72.8	72.2	71.5	70.3		
All other expenditures	449.6	491.6	492.0	515.7	543.1	458.2	503.6	473.9	479.8	497.7	516.5	523.4	536.1	547.2	565.7		
Surplus/deficit(-)	-54.9	-106.9	-130.3	-108.8	-179.9	-62.4	-147.9	-100.0	-123.5	-132.2	-165.4	-170.6	-165.7	-172.0	-211.4		
High Employment (H.E.) surplus/deficit(-)																	
evaluated at H.E. unemployment rate of:																	
5.1 percent	-0.8	n.a.	-36.6	n.a.	-60.5	-2.8	-45.1	-24.8	-33.4	-29.4	-58.8	-58.9	-45.0	-46.7	-91.4		
6.1 percent	-22.4	n.a.	-58.8	n.a.	-84.0	-25.0	-67.4	-47.2	-55.4	-51.6	-81.0	-81.7	-68.6	-70.7	-115.1		
	*--actual					e--estimated								n.a.--not available			

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1. OMB Current Budget Estimates, April 1982 and BEA NIA translations, April 1982.
 2. In the First Concurrent Resolution on the Budget -- Fiscal Year 1983, the Congress recommended revenues of \$665.9 billion and outlays of \$769.8 billion.
 3. Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, Rural Telephone Bank and (beginning in FY1982) the Strategic Petroleum Reserve.

4. Checks issued less checks paid, accrued items and other transactions.
 5. FRB staff estimates include Federal Home Loan Banks, FHLMC (excluding participation certificates), FNMA (excluding mortgage backed securities), Federal Land Banks, Federal Intermediate Credit Banks for Cooperatives, and Student Loan Marketing Association marketable debt on a payment basis. FRB and Administration estimates are not strictly comparable.

NOTE: Quarterly figures may not add to yearly totals due to rounding.

Recent Developments. While the federal funds rate remains below its level at the time of the last FOMC meeting, other market interest rates generally have risen 1/4 to 1-1/2 percentage points since then. One negative factor was a strengthening of M1 in early June, which heightened the anxiety of market participants who already were anticipating that it would bulge in July. In addition, a pickup in some economic indicators reinforced concerns that the prospective huge financing needs of the Treasury will collide with rising private credit demands.

Business credit demands have been strong. Business loans at commercial banks rose at almost a 20 percent annual rate in May, and data for large banks in early June suggest a further large increase. Issuance of commercial paper by nonfinancial firms also has been robust over this span. Public bond issuance in May was the largest since last November, as firms took advantage of a brief market rally, but it dropped off again in June. U.S. corporations through May also continued to raise a considerable amount of money in the Eurobond market.

It is estimated that, for nonfinancial corporations as a group, cash flows exceeded outlays by a small margin in the second quarter, after a slight shortfall in the first. The buoyancy of business borrowing suggests an accumulation of liquid assets as well as in an intensification of financial pressures on at least some firms. Signs of corporate stress continue to mount, including increasing numbers of dividend reductions or suspensions, a rising fraction of business loans at commercial banks with interest or principal past due, and relatively frequent rating downgradings. Even so, risk spreads in interest rates have held at levels that, while

sizable, are smaller than the previous highs reached last fall or in 1974-75.

Evidence that more households are experiencing financial difficulties was provided by the jump in mortgage delinquency and foreclosure rates in the first quarter and the continued high level of personal bankruptcies. On the brighter side, the ratio of debt repayments to disposable income is at close to a six-year low, and delinquency rates on installment loans have edged down to relatively low levels. High interest rates continue to depress household credit demands. Based on limited data at commercial banks and savings and loan associations, mortgage lending has receded somewhat after a marked pickup in the first quarter. The growth of consumer installment credit rose to around 4 percent in March and April, largely reflecting stronger auto sales. Partial data suggest a somewhat larger increase for May.

In the government sector, state and local security issuance remained relatively robust in May and June, supported in part by stepped-up offerings of mortgage revenue bonds. The Treasury financed a combined deficit of \$16 billion in the two months largely by running down its cash balance. The overall functioning of the government securities markets was not impaired by the widely-publicized problems of two small government securities dealers--Drysdale Government Securities and Comark. Nevertheless, a reassessment of credit relationships and practices appears to be in process and some smaller firms appear to be facing relatively high financing costs.

The key monetary aggregates have remained above the upper ends of their longer-run ranges. Although M1 contracted at a 2 percent annual rate in May, it increased appreciably in early June, suggesting the likelihood

of a small increase for the two months together. For the second quarter as a whole, growth at around a 3-3/4 percent annual rate represents a more normal pattern of money demand behavior after the extraordinary first-quarter strength. Other checkable deposits also have grown moderately since March--perhaps suggesting an easing, though not an unwinding, of what appeared in part to be a precautionary buildup earlier in the year.

The 10-1/4 percent growth of M2 in May was near the previous month's pace, as the decline in M1 was offset by a shift from term to overnight RPs following holiday-related reporting problems in April. A slowdown in the expansion of small time deposits at commercial banks in May countered a pickup at thrift institutions that was concentrated in accounts with a ceiling-rate differential. Partial data for early June indicate some slowing of M2 growth.

Outlook. The staff expects prospective supplies and demands for credit to be associated with interest rates averaging near present levels through the summer months. The federal government will have to finance a record deficit in the third quarter, but saving by the private sector is likely to be rising substantially as households lag in spending the added income from the July 1 tax cut and as business cash flows improve.

The Treasury is expected to borrow somewhat more than \$50 billion in the market in the third quarter; assuming passage of legislation raising the present \$70 billion limit on the volume of bonds outstanding, the government can be expected to tap all maturity sectors in volume. State and local government borrowing probably will continue sizable, reflecting not only the

basic budgetary trends in the sector, but also heavy issuance of housing revenue and industrial development bonds.

An anticipated pickup in consumer spending on durable goods should engender some further rise in net flows of consumer installment credit. The outlook for housing market activity suggests that residential mortgage credit flows will change little in the near term.

The staff expects no significant change in the financing gap of non-financial corporations during the third quarter as cash flows are projected to rise roughly in step with expenditures. Under the circumstances, overall business demands for external funds should drop off, with the easing occurring primarily in the short-term area. However, many corporations will still be suffering from strained cash flow and balance sheet positions, and any prominent corporate bankruptcies could heighten the current cautious attitude of investors in debt and equity markets.

Recent Developments. The weighted average value of the dollar rose by more than 7 percent since the May FOMC meeting, bringing the dollar to its highest level since early 1971.

. Much of the appreciation has been associated with an upward revision of expectations about dollar interest rates, partly in reaction to the course of negotiations over U.S. budget deficits and the apparent failure of the Versailles Summit to put substantial pressure on U.S. authorities to act to lower interest rates. Since the May FOMC meeting, the average interest differential favoring short-term dollar instruments over instruments denominated in other major currencies widened by over one percentage point, and long-term dollar interest rates have risen substantially as well. Another major factor contributing to the appreciation was the intensification of hostilities in the Middle East, which made the dollar more attractive as a safe-haven currency.

The dollar's exchange value was also affected by the realignment of exchange rates within the European Monetary System (EMS) on June 12. In terms of EMS central rates, the French franc and Italian lira were devalued by 5-3/4 percent and 2-3/4 percent, respectively, the German mark and the Dutch guilder were revalued upward by 4-1/4 percent, and the Belgian franc, the Danish krone and the Irish pound were left unchanged. The realignment followed several months of strong downward pressure on the French franc,

. The realignment brought to an end the downward pressure on the French franc,

The Canadian dollar has declined by 5 percent against the U.S. dollar since the last FOMC meeting, reflecting both the expectation that Canadian economic policies will ease substantially in the face of a weak economy and the persistent difference between U.S. and Canadian inflation rates.

On June 14, following the EMS realignment and a sharp rise in the dollar against all major currencies, exchange markets were judged to be disorderly. The Desk intervened on U.S. account for the first time since March 1981, selling \$21 million against marks and \$9 million against yen.

Economic activity abroad remains weak: while there are some tentative indications of an upturn in certain countries, there are offsetting tendencies in others. Thus far this year, in Germany, Italy and the United Kingdom industrial production has generally been rising, whereas in Canada, France and Japan it has declined to a level below that at the end of last year. Unemployment remains at very high levels in all countries, and is at post-war record levels in many.

Weakness in economic activity and employment has been associated with a reduction in inflation in most countries. For the six major foreign industrial countries the average annual rate of inflation (CPI) in the latest three months is about 8-1/2 percent, roughly 3

percentage points below the average rate of inflation in 1981. In France and Canada inflation has shown some tendency to increase.

The U.S. merchandise trade deficit in the first four months of the year was \$18 billion (SAAR), half the size of the deficit in the fourth quarter of 1981. In April there was, in fact, a small trade surplus as a decline in exports from the first-quarter rate was more than offset by a steep drop in imports. Weak U.S. economic activity, low capacity utilization and inventory reduction led to sharp declines in imports of a wide range of industrial supplies, capital goods and consumer goods. Oil imports in April also declined in both price and volume.

The reduction in exports in April (entirely in the non-agricultural component) represented a continuation of a year-long decline reflecting weak economic activity abroad and the appreciation of the dollar. The decrease in the volume of nonagricultural exports through April has amounted to about 15 percent since the second quarter of last year, when these exports peaked.

The U.S. current account showed a surplus in the first quarter of 1982 of \$4.7 billion (SAAR), after a deficit of \$3.7 billion in the preceding quarter. A decline in net investment income receipts from the fourth-quarter rate, reflecting weak economic conditions abroad, low oil company profits, and the appreciation of the dollar against major currencies and the Mexican peso, was more than offset by a reduction in the trade deficit.

On the financial side of U.S. international transactions, net borrowing by U.S. banking offices (including IBFs) from their own foreign offices increased by over \$5 billion between March and early June. Over this same period U.S. nonbank residents borrowed nearly \$1 billion from foreign branches of U.S. banks. Through March of this year (latest data available), Eurodollar holdings of U.S. nonbank residents increased by almost \$10 billion. Official holdings of marketable U.S. Treasury securities of the G-10 countries declined by about \$9 billion in the first four months of the year, largely to finance exchange market intervention sales of dollars. This decline in G-10 holdings was offset to a large extent by net purchases of almost \$7 billion by OPEC countries which occurred despite the projected elimination of the OPEC current account surplus this year.

Outlook. A gradual recovery in economic activity abroad is expected in the latter half of this year, and real growth is projected at about 2-3/4 percent during 1983. Inflation in the foreign G-10 countries is expected to subside only moderately over the projection period, declining from about 8 percent during this year to roughly 7 percent next year.

Recent data indicate that U.S. imports, both oil and nonoil, may be somewhat lower than previously anticipated. As a result, the trade deficit projected for this year has been reduced somewhat, and the current account surplus forecast for 1982 has been revised upward to about \$6 billion. In 1983, however, the current account is projected to shift to a large deficit between \$20 and \$25 billion as the continuing effects of the dollar's appreciation generate a considerable

widening of the trade deficit.

The staff now expects the weighted average exchange value of the dollar a year hence to be somewhat above the level previously projected because of its very recent high level and the slight upward revision in the current account surplus projected for this year. Although we would anticipate that the dollar will decline from its most recent peaks, we expect that the dollar will generally maintain the strength it has shown during the last several months into the first part of next year. As the U.S. current account moves into substantial deficit in 1983, however, we expect a significant decline in the dollar's value.

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

June 23, 1982

	1981 ANN.	1982 ^f ANN.	1983 ^f ANN.	1982 ^f Q I	1982 ^f Q II	1982 ^f Q III	1982 ^f Q IV	1983 ^f Q I	1983 ^f Q II	1983 ^f Q III	1983 ^f Q IV
1. GWP NET EXPORTS											
CURRENT \$, NET EXPORTS OF G&S	26.0	34.7	12.2	31.5	44.8	36.6	25.9	18.2	13.8	9.1	7.5
IMPORTS OF G&S	367.3	357.5	376.7	356.9	356.4	357.8	359.0	363.3	370.1	380.1	393.2
	341.4	322.8	364.5	325.4	311.6	321.2	333.0	345.0	356.3	371.0	385.7
CONSTANT 72 \$, NET EXPORTS OF G&S	44.9	39.3	32.9	39.3	42.4	39.6	35.9	33.5	32.4	32.5	33.1
IMPORTS OF G&S	160.4	151.9	153.0	152.1	152.5	152.2	150.9	150.6	151.4	153.6	156.5
	115.5	112.6	120.2	112.8	110.1	112.7	114.9	117.1	119.0	121.1	123.5
TERMS OF TRADE (1972=100) 1/	77.5	82.1	81.2	81.4	82.6	82.5	82.1	81.9	81.7	80.8	80.4
2. U.S. MERCHANDISE TRADE BALANCE 2/											
EXPORTS (EXCL. MILITARY)	236.3	215.1	216.9	222.4	216.2	212.1	209.8	210.7	213.1	218.0	225.7
AGRICULTURAL	44.3	42.4	47.9	42.0	42.0	41.9	43.6	45.3	46.7	48.5	50.9
NONAGRICULTURAL	192.0	172.8	169.0	180.4	174.2	170.2	166.3	165.4	166.3	169.4	174.8
IMPORTS	264.1	238.5	271.3	246.7	228.0	234.1	245.2	256.1	264.7	276.5	287.8
PETROLEUM AND PRODUCTS	77.6	56.4	64.2	62.6	52.3	54.1	56.8	60.2	62.5	65.9	68.3
NONPETROLEUM	186.6	182.1	207.0	184.1	175.7	180.0	188.4	195.9	202.2	210.6	219.5
3. U.S. CURRENT ACCOUNT BALANCE											
OF WHICH: NET INVESTMENT INCOME	4.5	6.3	-23.3	4.7	17.1	8.0	-4.7	-13.3	-20.2	-28.0	-31.6
	33.0	30.5	33.4	27.9	29.2	31.8	33.2	33.9	33.5	33.0	33.1
4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/											
REAL GNP, % CHANGE, ANNUAL RATES	.6	.7	2.4	.2	.6	1.5	2.1	2.8	2.6	2.8	3.1
CONSUMER PRICES, 4/, % CHANGE, ANNUAL RATES	9.7	8.5	7.5	7.9	9.1	7.7	7.6	7.8	7.1	6.9	6.9

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%).

f/ PROJECTED.