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July 6, 1983

# **SUMMARY AND OUTLOOK**

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Prepared for the Federal Open Market Committee

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

## DOMESTIC NONFINANCIAL DEVELOPMENTS

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Recent developments. The expansion in economic activity strengthened considerably in the second quarter. Production and employment rose rapidly in April and May as final demands accelerated and businesses completed their cyclical inventory liquidation. Much of the recent pickup in activity has been in the household sector--particularly outlays for autos and housing. In addition, business spending for new equipment rose further. Although a turnaround in energy prices boosted measured inflation in April and May, underlying trends in prices and wages remain favorable.

The index of industrial production rose 1.1 percent in May, following even larger gains in March and April. Since its cyclical trough in November, the index has increased 7 percent--about in line with the typical rise in previous recoveries. The advance in May reflected continued strength in the output of consumer durables and construction materials. In addition, production of business equipment rose strongly, the third consecutive monthly advance. Partial data for June point to further output increases, with auto and truck assemblies up sharply.

Much of the recent acceleration in output reflects inventory developments. Earlier in the year, aggregate production had been held down as businesses aggressively liquidated unwanted stocks. However, with inventories pared to more comfortable levels this spring, firms have begun meeting the needs of increasing sales out of current production and have started rebuilding stocks in some industries. The book value of manufacturers' inventories rose \$12 billion (annual rate) in May; non-automotive inventories held by wholesalers and retailers rose at a \$20 billion annual rate in April (the latest available data). In the

auto sector, however, production in the past few months has not kept pace with sales and the days' supply of dealer stocks has fallen to unusually low levels.

Nonfarm payroll employment increased 375,000 in May--the largest one-month advance of the current expansion--following a sharp rise in April. Increases in May were widespread, with particularly large gains in services, durable goods manufacturing, and construction. The civilian unemployment rate edged down again in May to 10.1 percent--0.7 percentage point below the December peak. The weekly volume of initial claims for unemployment insurance benefits and the number of benefit recipients have fallen appreciably in recent weeks, suggesting that labor market conditions have continued to improve since the May labor force survey.

The rapid growth of employment and a lengthening of the workweek have generated strong advances in wage and salary income. The gains in income, along with improved credit market conditions and the exceptional increase in the value of household equity and bond holdings over the past nine months, have helped sustain growth in consumer spending--especially outlays for big-ticket items. Sales of domestic autos have averaged about 7-1/4 million units (annual rate) since late May, up from a 6-1/2 million unit pace earlier in the spring. Outside of the auto sector, spending for consumer goods increased 1.3 percent in May--led by strong advances at general merchandise, furniture and appliance outlets--to a level nearly 2 percent above the first-quarter average.

Total private housing starts rose in May to a 1.8 million unit annual rate, following declines in the preceding two months. Starts have averaged 1.65 million units (annual rate) in April and May, 30 per-

cent higher than the pace in the fourth quarter of 1982; permits for new housing construction have shown a rise of about the same magnitude. The improvement in housing activity has occurred in both the single- and multifamily sectors, with most of the advance in multifamily construction apparently in private, non-subsidized rental units.

In the business sector, the recovery in spending for capital equipment appears to be taking hold. Shipments of nondefense capital goods have been trending up since early spring, and business purchases of cars and trucks have continued at a strong pace. In contrast, the average level of outlays for nonresidential construction in April and May was 4-1/4 percent below the first-quarter figure. Nonetheless, forward-looking indicators of total business fixed investment--such as new orders for nondefense capital goods and surveys of plant and equipment spending anticipations--point to a pickup in the second half of the year.

Wage increases have moderated somewhat further this year. The index of hourly earnings rose 4-1/2 percent at an annual rate over the first five months of 1983, compared with a 6 percent rise during the preceding year. Much of the slowing has been in manufacturing and construction, reflecting in part wage concessions by union workers at hard-pressed firms. However, wage increases also have moderated in the relatively less unionized trade and service sectors.

Consumer prices rose at about a 6-1/2 percent annual rate in April and May, after changing little during the opening months of the year. Much of the acceleration reflected a surge in gasoline prices, partly due to the imposition of a higher federal excise tax; however, survey data suggest that retail gasoline price increases have slowed in recent

weeks. Outside of the energy sector, inflation rates for consumer commodities and services generally continued to moderate. At the producer level, increases in capital equipment prices have slowed further, and spot prices of industrial commodities generally have shown little change since late March after rising sharply around the turn of the year. As indicated in the special reports on prices, wages and productivity compiled by the Federal Reserve Banks, businesses are taking a cautious approach to raising product prices in part because the cost of materials has been quite stable.

Outlook. The staff now estimates that real GNP rose at a 7-1/2 percent annual rate in the second quarter, compared with a 2.6 percent rate in the first quarter. A principal factor in the second-quarter advance was a sharp swing in inventory investment from liquidation to an estimated small accumulation. Consumption and housing led a strong advance in real private domestic final purchases (7 percent at an annual rate), while both the government and net export sectors declined.

The staff's assumptions about monetary policy are little changed from the May Greenbook. From its February-March base, M2 growth during 1983 is expected to be around the middle or perhaps in the upper half of the FOMC's 7 to 10 percent range; in 1984, M2 growth is assumed to average 8 percent. However, interest rates are projected to edge up during the second half of 1983, and then to move back down toward current levels during 1984. For fiscal policy, the staff projects a budget deficit for fiscal year 1984 of just under \$200 billion--slightly lower than in the last Greenbook. The effects of higher projected nominal income on receipts are partly offset by expected Congressional repeal of interest and dividend income withholding.

Economic activity is expected to remain vigorous in the third quarter, with real GNP rising at about a 7 percent annual rate, considerably more than anticipated earlier. In part, the strength is a result of further re-building of depleted inventories. But a healthy gain in final sales also is likely, reflecting the July 1 tax cut, lagged effects of the rapid first half gains in employment and income, and recent improvements in consumer attitudes.

Advances in economic activity are projected to moderate toward the end of this year and in early 1984 as the cyclical rebound in inventories is completed and the effects of last year's drop in interest rates fade. Real GNP is projected to increase at a 5 percent annual rate in the fourth quarter of 1983, and rise 4-1/4 percent over the four quarters of 1984. Business fixed investment should continue to expand at a relatively robust rate as the slack in unused capacity narrows; growing exports of goods and services also should provide a source of strength, in contrast to the experience through mid-1983 when exports were a source of weakness. But gains in consumer spending for autos and other durable goods as well as housing outlays are likely to slow from the rapid 1983 pace.

The civilian unemployment rate is projected to decline 1-1/2 percentage points over the next six quarters to about 8-1/2 percent. This still would represent considerable slack in the labor market, which is expected to remain a damping influence on wage increases. Nonetheless, additional deceleration of wages will be limited by increased profitability and tighter labor markets in some industries, and an increase in payroll taxes will boost labor costs. Over the four quarters of 1984, hourly compensation is projected to rise 5 percent, slightly faster than during 1983.

The rate of inflation is projected to slow a bit in the last half of 1983 from the second-quarter pace, as increases in food and energy prices moderate. However, the rate of price increase is expected to drift up slowly over the course of 1984, reflecting the firming of labor and product markets, a widening of profit margins, and the effects of the assumed depreciation of the dollar. Over the four quarters of 1984, the gross business product fixed-weighted price index is projected to rise 4-1/4 percent.

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



July 6, 1983

## STAFF GNP PROJECTIONS

Percent changes, annual rate										
	Nominal GNP		Real GNP		Gross domestic business product fixed-weighted price index				Unemployment rate (percent)	
					Total		Excluding food and energy			
	5/18/83	7/6/83	5/18/83	7/6/83	5/18/83	7/6/83	5/18/83	7/6/83	5/18/83	7/6/83
<b>Annual changes:</b>										
1981 <1>	11.6	11.6	1.9	1.9	9.6	9.6	9.4	9.4	7.6	7.6
1982 <1>	4.1	4.1	-1.7	-1.7	5.9	5.9	6.9	6.9	9.7	9.7
1983	7.1	7.7	2.7	3.2	4.1	4.3	4.8	4.9	10.0	9.8
1984	8.2	8.7	4.8	4.9	3.9	4.2	3.8	4.1	9.3	8.9
<b>Quarterly changes:</b>										
1982 Q1 <1>	-1.0	-1.0	-5.1	-5.1	4.4	4.4	5.3	5.3	8.8	8.8
Q2 <1>	6.8	6.8	2.1	2.1	3.8	3.8	5.9	5.9	9.4	9.4
Q3 <1>	5.8	5.8	.7	.7	5.9	5.9	5.2	5.2	10.0	10.0
Q4 <1>	2.6	2.6	-1.1	-1.1	4.3	4.3	4.7	4.7	10.7	10.7
1983 Q1 <1>	9.1	8.3	3.1	2.6	2.8	3.0	5.3	5.5	10.3	10.3
Q2	8.9	11.4	5.5	7.5	4.5	5.1	4.7	4.6	10.1	10.0
Q3	8.1	10.6	4.8	7.1	4.2	4.6	4.1	4.3	9.8	9.6
Q4	8.3	8.2	5.0	5.0	3.8	3.7	3.6	3.7	9.7	9.4
1984 Q1	7.9	7.9	4.7	4.3	3.7	4.0	3.6	3.9	9.6	9.2
Q2	8.1	8.3	4.6	4.2	3.8	4.2	3.7	4.2	9.4	9.0
Q3	8.4	8.6	4.8	4.1	3.8	4.4	3.7	4.4	9.1	8.8
Q4	9.0	8.6	4.9	4.1	3.8	4.4	3.7	4.4	8.9	8.6
<b>Two-quarter changes: &lt;2&gt;</b>										
1982 Q2 <1>	2.8	2.8	-1.6	-1.6	4.2	4.2	5.6	5.6	1.1	1.1
Q4 <1>	4.2	4.2	-.2	-.2	5.1	5.1	5.0	5.0	1.3	1.3
1983 Q2	9.0	9.8	4.3	5.0	3.7	4.0	5.0	5.0	-.6	-.7
Q4	8.2	9.4	4.9	6.0	4.0	4.1	3.8	4.0	-.4	-.6
1984 Q2	8.0	8.1	4.6	4.2	3.7	4.1	3.7	4.1	-.3	-.4
Q4	8.7	8.6	4.9	4.1	3.8	4.4	3.7	4.4	-.5	-.4
<b>Four-quarter changes: &lt;3&gt;</b>										
1981 Q4 <1>	9.6	9.6	.7	.7	8.9	8.9	9.3	9.3	.9	.9
1982 Q4 <1>	3.5	3.5	-.9	-.9	4.7	4.7	5.3	5.3	2.4	2.4
1983 Q4	8.6	9.6	4.6	5.5	3.8	4.1	4.4	4.5	-1.0	-1.3
1984 Q4	8.4	8.3	4.7	4.2	3.8	4.3	3.7	4.2	-.8	-.8

&lt;1&gt; Actual.

&lt;2&gt; Percent change from two quarters earlier.

&lt;3&gt; Percent change from four quarters earlier.

July 6, 1983

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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.)

	1981				1982			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	2864.9	2901.8	2980.9	3003.2	2995.5	3045.2	3088.2	3108.2
Final sales	2852.7	2877.2	2949.1	2989.9	3031.1	3061.4	3083.5	3156.5
Private	2274.6	2294.0	2348.9	2363.6	2401.0	2430.5	2431.8	2479.7
Domestic final purchases	2243.4	2270.3	2323.0	2340.1	2369.7	2395.6	2424.9	2470.6
Personal consumption expenditures	1799.9	1819.4	1868.8	1884.5	1919.4	1947.8	1986.3	2030.8
Goods	957.5	960.0	982.5	976.1	987.0	995.7	1008.7	1027.5
Services	842.4	859.4	886.3	908.3	932.4	952.1	977.6	1003.3
Gross private domestic investment	455.7	475.5	486.0	468.9	414.8	431.5	443.3	391.5
Residential structures	113.6	109.5	101.2	95.5	93.4	95.5	94.3	101.4
Business fixed investment	330.0	341.3	353.0	360.2	357.0	352.2	344.2	338.4
Change in business inventories	12.2	24.6	31.8	13.2	-35.6	-16.2	4.7	-48.3
Nonfarm	10.0	19.3	24.6	6.0	-36.0	-15.0	3.7	-50.0
Net exports of goods and services <1>	31.2	23.7	25.9	23.5	31.3	34.9	6.9	9.1
Exports	365.4	368.9	367.2	367.9	359.9	365.8	349.5	328.1
Imports	334.2	345.1	341.3	344.4	328.6	330.9	342.5	319.1
Gov't. purchases of goods and services	578.1	583.2	600.2	626.3	630.1	630.9	651.7	676.8
Federal <2>	217.0	218.2	230.0	250.5	249.7	244.3	259.0	278.7
State and local	361.1	365.0	370.1	375.7	380.4	386.6	392.7	398.0
Gross national product in constant (1972) dollars	1507.8	1502.2	1510.4	1490.1	1470.7	1478.4	1481.1	1477.2
Personal income	2330.0	2380.6	2458.2	2494.6	2510.5	2552.7	2592.5	2624.0
Wage and salary disbursements	1452.8	1479.4	1512.3	1531.2	1541.6	1556.6	1570.0	1574.5
Disposable personal income	1958.7	1996.5	2060.0	2101.4	2117.1	2151.5	2198.1	2224.3
Saving rate (percent)	5.4	6.1	6.5	7.5	6.6	6.7	6.9	6.0
Corporate profits with I.V.A. and C.C. Adj.	200.3	185.1	193.1	183.9	157.1	155.4	166.2	164.6
Corporate profits before tax	253.1	225.4	233.3	216.5	171.6	171.7	180.3	175.9
Federal government surplus or deficit (-) (N.I.A. basis)	-39.7	-40.5	-58.0	-101.7	-118.4	-119.6	-156.0	-204.2
High employment surplus or deficit (-) <3>	10.4	22.0	5.9	-20.3	-15.6	-6.2	-32.7	-64.3
State and local government surplus or deficit(-) (N.I.A. basis)	31.3	32.9	33.5	29.1	27.7	32.1	32.3	36.4
Excluding social insurance funds	1.1	1.7	1.2	-4.2	-6.8	-3.6	-4.5	-1.6
Civilian labor force (millions)	108.2	108.8	108.6	109.1	109.3	110.1	110.6	111.0
Unemployment rate (percent)	7.4	7.4	7.4	8.3	8.8	9.4	10.0	10.7
Nonfarm payroll employment (millions)	91.0	91.2	91.4	91.0	90.3	89.9	89.3	88.8
Manufacturing	20.2	20.3	20.3	19.9	19.4	19.1	18.7	18.3
Industrial production (1967=100)	151.8	152.5	153.0	146.3	141.7	139.4	138.2	135.2
Capacity utilization: all manufacturing (percent) <4>	80.6	80.8	80.3	75.9	72.9	71.6	71.0	69.0
Materials (percent) <4>	82.7	81.9	82.0	76.2	73.0	70.7	69.4	67.1
Housing starts, private (million units, A.R.)	1.39	1.18	.96	.87	.90	.95	1.12	1.26
New auto sales (millions, A.R.)	9.96	7.89	9.04	7.36	8.12	7.53	7.78	8.57
Domestic models	7.31	5.63	6.90	5.13	5.90	5.53	5.56	6.08
Foreign models	2.66	2.25	2.14	2.23	2.22	1.99	2.22	2.49

- <1> Balance of payments data and details underlying these estimates are shown in the International Developments section of this part of the Greenbook.
- <2> Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.
- <3> Estimates in table are evaluated at a 5.1 percent high employment unemployment rate. Evaluated at a 6.1 percent unemployment rate, the high employment budget would show a deficit of \$43.5 billion in 1981-Q4, and a deficit of \$89.5 billion in 1982-Q4.
- <4> Capacity measures have been revised back to 1967.

July 6, 1983

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

	1981				1982			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	7.9	-1.5	2.2	-5.3	-5.1	2.1	.7	-1.1
Final sales	5.4	-4.0	1.0	-2.3	.2	-9	-1.3	5.4
Private	5.5	-4.0	.4	-4.4	1.0	.2	-3.5	3.9
Domestic final purchases	4.7	-2.8	2.2	-3.6	.9	.6	-9	4.1
Personal consumption expenditures	4.4	-2.7	2.9	-3.3	2.5	2.5	.6	4.5
Goods	6.9	-5.1	4.0	-6.2	2.0	2.5	-4	6.6
Services	1.5	.1	1.7	.0	3.0	2.4	1.7	2.3
Gross private domestic investment	25.0	14.9	6.9	-22.6	-36.5	15.0	7.9	-37.3
Residential structures	1.0	-17.4	-31.9	-25.3	-10.2	12.9	-5.3	39.3
Business fixed investment	8.0	1.1	9.3	.6	-5.0	-11.8	-7.6	-6.0
Gov't. purchases of goods and services	5.2	-4.1	3.6	7.0	-2.9	-5.3	8.4	12.0
Federal	12.2	-3.2	14.8	20.4	-5.5	-13.5	23.1	32.8
National defense	8.0	11.5	7.6	10.1	-7.9	21.4	13.0	2.0
State and local	1.3	-4.6	-2.7	-8	-1.1	.4	-2	-4
Disposable personal income	3.7	.6	4.8	1.2	-1.9	3.1	1.3	.3
<u>Current Dollars</u>								
Gross national product	19.6	5.3	11.4	3.0	-1.0	6.8	5.8	2.6
Final sales	14.6	3.5	10.4	5.7	5.6	4.1	2.9	9.8
Private	14.8	3.5	9.9	2.5	6.5	5.0	.2	8.1
Domestic final purchases	13.4	4.9	9.6	3.0	5.2	4.4	5.0	7.8
Personal consumption expenditures	13.0	4.4	11.3	3.4	7.6	6.1	8.1	9.3
Goods	14.7	1.0	9.7	-2.6	4.5	3.6	5.3	7.7
Services	11.1	8.3	13.2	10.3	11.0	8.7	11.2	11.0
Gross private domestic investment	52.2	18.5	9.2	-13.3	-38.8	17.2	11.4	-39.1
Residential structures	11.5	-13.4	-27.0	-20.8	-8.4	9.4	-4.9	33.6
Business fixed investment	16.7	14.5	14.3	8.4	-3.5	-5.3	-8.7	-6.6
Gov't. purchases of goods and services	13.7	3.6	12.2	18.6	2.4	.6	13.8	16.3
Federal	20.9	2.2	23.5	40.7	-1.4	-8.3	26.3	34.2
National defense	15.4	22.1	10.8	36.7	-1.8	26.4	15.6	15.4
State and local	9.7	4.4	5.7	6.2	5.0	6.7	6.5	5.5
Disposable personal income	12.3	7.9	13.4	8.3	3.0	6.7	8.9	4.9
Personal income	13.0	9.0	13.7	6.1	2.6	6.9	6.4	4.9
Wage and salary disbursements	12.0	7.5	9.2	5.1	2.7	3.9	3.5	1.2
Corporate profits with I.V.A. and C.C. Adj.	49.3	-27.1	18.4	-17.7	-46.7	-4.3	30.8	-3.8
Corporate profits before tax	12.2	-37.1	14.8	-25.8	-60.5	.2	21.6	-9.4
Nonfarm payroll employment	1.7	.9	1.1	-1.8	-3.0	-1.8	-2.7	-2.3
Manufacturing	.8	2.4	.1	-7.2	-9.5	-7.5	-7.7	-8.6
Nonfarm business sector								
Output per hour	4.9	-1.3	-3	-3.5	.7	.9	3.4	.4
Compensation per hour	11.8	7.1	9.0	7.3	7.9	6.0	6.6	5.5
Unit labor costs	6.6	8.6	9.3	11.2	7.2	5.1	3.1	5.1
GNP implicit deflator <1>	10.9	6.8	9.0	8.8	4.3	4.6	5.0	3.7
Gross domestic business product								
fixed-weighted price index <2>	10.4	8.6	9.3	7.4	4.4	3.8	5.9	4.3
Excluding food and energy	8.4	9.4	11.0	8.6	5.3	5.9	5.2	4.7
Consumer price index (all urban)	10.5	8.5	12.1	7.1	3.0	5.3	7.7	1.9
Industrial production	8.4	1.9	1.4	-16.6	-11.8	-6.5	-3.4	-8.2

<1> Excluding Federal pay increases, rates of change were: 1981-Q1, 10.8 percent; 1981-Q4, 7.8 percent; 1982-Q1, 4.2 percent; 1982-Q4, 3.3 percent.

<2> Uses expenditures in 1972 as weights.

July 6, 1983

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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.)

	Projected							
	1983				1984			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	3170.6	3257.5	3340.3	3406.7	3472.4	3542.0	3615.7	3690.7
Final sales	3206.9	3252.1	3316.0	3352.7	3443.4	3515.0	3588.2	3661.7
Private	2530.6	2570.1	2616.9	2664.9	2714.3	2770.1	2828.3	2888.6
Domestic final purchases	2511.0	2581.5	2646.7	2707.0	2760.9	2817.7	2876.5	2936.5
Personal consumption expenditures	2052.9	2109.3	2165.0	2215.0	2256.3	2299.4	2344.4	2390.3
Goods	1034.4	1062.0	1090.0	1113.0	1131.8	1151.4	1171.4	1191.8
Services	1018.5	1047.3	1075.0	1102.0	1124.5	1148.0	1173.0	1198.5
Gross private domestic investment	421.7	477.6	506.0	546.0	533.6	545.3	559.6	575.2
Residential structures	121.0	134.0	140.0	144.0	148.0	152.0	155.5	159.0
Business fixed investment	337.1	338.2	341.7	348.0	356.6	366.3	376.6	387.2
Change in business inventories	-36.3	5.4	24.3	54.0	29.0	27.0	27.5	29.0
Nonfarm	-35.6	8.0	22.1	29.0	31.0	34.0	35.5	37.0
Net exports of goods and services <1>	19.6	-11.4	-29.8	-42.1	-46.6	-47.6	-48.2	-47.9
Exports	332.4	328.7	336.1	343.4	353.1	363.8	375.2	389.6
Imports	312.8	340.0	365.9	385.5	399.7	411.4	423.4	437.5
Gov't. purchases of goods and services	676.3	682.0	699.1	687.8	729.1	744.9	759.9	773.1
Federal <2>	274.1	275.3	284.0	264.8	299.2	307.9	315.7	321.3
State and local	402.2	406.7	415.1	423.0	429.9	437.0	444.2	451.8
Gross national product in constant (1972) dollars	1486.7	1513.9	1540.0	1558.7	1575.2	1591.3	1607.4	1623.6
Personal income	2648.2	2708.6	2774.8	2848.5	2877.5	2930.4	2987.9	3042.4
Wage and salary disbursements	1597.3	1638.1	1681.0	1709.8	1742.2	1774.7	1809.0	1843.1
Disposable personal income	2247.2	2295.8	2372.4	2432.9	2460.8	2505.6	2553.5	2599.2
Saving rate (percent)	5.9	5.4	6.1	6.3	5.6	5.5	5.5	5.4
Corporate profits with I.V.A. and C.C. Adj.	186.1	196.2	215.5	228.7	224.4	231.2	242.7	258.0
Corporate profits before tax	177.9	180.4	197.3	206.9	200.6	204.4	212.6	224.2
Federal government surplus or deficit (-) (N.I.A. basis)	-174.0	-163.3	-193.2	-193.0	-192.6	-191.6	-191.7	-190.7
High employment surplus or deficit (-) <3>	-31.9	-24.6	-64.0	-64.6	-64.2	-65.1	-66.3	-65.9
State and local government surplus or deficit (-) (N.I.A. basis)	42.3	51.9	56.3	58.8	56.2	56.2	56.0	56.6
Excluding social insurance funds	3.0	11.1	13.9	14.8	10.4	8.8	6.9	5.8
Civilian labor force (millions)	110.5	111.0	111.7	112.1	112.6	113.1	113.7	114.2
Unemployment rate (percent)	10.3	10.0	9.6	9.4	9.2	9.0	8.8	8.6
Nonfarm payroll employment (millions)	88.8	89.5	90.7	91.3	91.9	92.5	93.3	94.1
Manufacturing	18.3	18.5	18.9	19.2	19.5	19.8	20.1	20.5
Industrial production (1967=100)	138.5	144.4	148.5	151.4	154.3	156.9	159.8	162.9
Capacity utilization: all manufacturing (percent)<4>	70.7	73.8	75.6	76.9	77.9	78.9	79.9	81.1
Materials (percent)<4>	70.0	72.8	74.9	76.6	78.5	79.9	81.6	83.4
Housing starts, private (million units, A.R.)	1.69	1.65	1.65	1.65	1.65	1.70	1.75	1.85
New auto sales (millions, A.R.)	8.44	9.00	9.30	9.50	9.70	9.60	9.80	10.00
Domestic models	6.06	6.80	7.10	7.20	7.30	7.40	7.50	7.60
Foreign models	2.38	2.20	2.20	2.30	2.40	2.20	2.30	2.40

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

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

<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 \$94.1 billion in 1983-Q4, and a deficit of \$101.9 billion in 1984-Q4.

<4> Based on revised capacity measures.

July 6, 1983

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

	Projected							
	1983				1984			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	2.6	7.5	7.1	5.0	4.3	4.2	4.1	4.1
Final sales <1>	1.3	2.5	4.7	1.4	7.5	4.4	4.1	4.0
Private	4.0	3.3	4.7	4.9	4.3	4.3	4.1	4.3
Domestic final purchases	5.0	7.0	5.8	5.2	3.7	3.9	3.9	3.9
Personal consumption expenditures	2.5	5.9	6.0	5.1	3.1	3.2	3.2	3.2
Goods	3.7	6.6	6.4	5.2	3.1	3.2	3.1	3.0
Services	1.2	5.2	5.4	5.1	3.0	3.2	3.4	3.4
Gross private domestic investment	32.0	58.4	22.4	31.7	-11.7	5.4	7.1	7.8
Residential structures	80.5	44.7	14.7	7.3	6.7	6.3	4.3	3.9
Business fixed investment	3.9	2.9	2.3	5.0	6.9	7.8	8.0	8.0
Gov't. purchases of goods and services	-9.1	-.7	4.8	-12.5	22.1	4.8	3.8	2.7
Federal	-20.2	-.7	7.3	-31.7	61.9	9.5	7.0	3.8
National defense	6.4	11.7	13.6	7.9	7.0	6.3	4.8	5.3
State and local	-.4	-.7	3.1	2.8	1.6	1.7	1.7	1.9
Disposable personal income	2.3	3.6	8.8	6.1	.2	2.8	3.0	2.3
<u>Current Dollars</u>								
Gross national product	8.3	11.4	10.6	8.2	7.9	8.3	8.6	8.6
Final sales	6.5	5.8	8.1	4.5	11.3	8.6	8.6	8.4
Private	8.5	6.4	7.5	7.5	7.6	8.5	8.7	8.8
Domestic final purchases	6.7	11.7	10.5	9.4	8.2	8.5	8.6	8.6
Personal consumption expenditures	4.4	11.4	11.0	9.6	7.7	7.9	8.1	8.1
Goods	2.7	11.1	11.0	8.7	6.9	7.1	7.1	7.1
Services	6.2	11.8	11.0	10.4	8.4	8.6	9.0	9.0
Gross private domestic investment	34.6	64.5	26.0	35.6	-8.8	9.1	10.9	11.6
Residential structures	102.6	50.5	19.1	11.9	11.6	11.3	9.5	9.3
Business fixed investment	-1.6	1.3	4.2	7.6	10.3	11.3	11.7	11.7
Gov't. purchases of goods and services	-.3	3.4	10.4	-6.3	26.3	9.0	8.3	7.1
Federal	-6.4	1.8	13.3	-24.4	63.0	12.1	10.5	7.3
National defense	12.9	13.8	21.0	10.9	16.3	9.8	9.3	9.3
State and local	4.2	4.6	8.5	7.8	6.7	6.8	6.8	7.0
Disposable personal income	4.2	8.9	14.0	10.6	4.7	7.5	7.9	7.4
Personal income	3.7	9.4	10.1	11.1	4.1	7.6	8.1	7.5
Wage and salary disbursements	5.9	10.6	10.9	7.0	7.8	7.7	8.0	7.8
Corporate profits with I.V.A. and C.C. Adj.	63.4	23.5	45.4	27.0	-7.3	12.7	21.4	27.7
Corporate profits before tax	4.6	5.8	42.9	21.1	-11.6	7.8	17.0	23.7
Nonfarm payroll employment	.1	3.1	5.4	2.5	2.6	2.9	3.5	3.4
Manufacturing	-1	5.0	8.8	7.7	7.0	6.2	6.0	6.3
Nonfarm business sector								
Output per hour	4.7	3.1	2.7	3.1	1.9	1.6	.9	.8
Compensation per hour	6.0	4.0	4.9	4.5	6.3	4.5	4.6	4.6
Unit labor costs	1.2	.9	2.1	1.4	4.3	2.9	3.7	3.7
GNP implicit deflator	5.5	3.6	3.3	3.1	3.5	3.9	4.3	4.3
Gross domestic business product								
fixed-weighted price index <2>	3.0	5.1	4.6	3.7	4.0	4.2	4.4	4.4
Excluding food and energy	5.5	4.6	4.3	3.7	3.9	4.2	4.4	4.4
Consumer price index (all urban)	-.4	4.7	4.9	4.3	4.5	4.6	4.5	4.5
Industrial production	10.0	18.2	11.8	8.0	7.9	6.9	7.6	8.0

<1> Excluding Federal Commodity Credit Corporation net purchases, growth rates for final sales are: 1983-Q1, 3.6 percent; 1983-Q2, 3.3 percent; 1983-Q3, 5.0 percent; 1983-Q4, 4.7 percent; 1984-Q1, 3.9 percent.

<2> Uses expenditures in 1972 as weights.

July 6, 1983

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

	1977	1978	1979	1980	1981	1982	---Projected---	
							1983	1984
Gross national product	1918.3	2163.9	2417.8	2633.1	2937.7	3059.3	3293.8	3580.2
Final sales	1895.3	2137.4	2403.5	2643.1	2917.3	3083.1	3281.9	3552.1
Private	1501.5	1705.5	1929.1	2104.7	2320.4	2435.7	2595.6	2800.3
Domestic final purchases	1505.5	1706.6	1915.9	2079.5	2294.3	2415.2	2611.5	2847.9
Personal consumption expenditures	1204.4	1346.5	1507.2	1667.2	1843.2	1971.1	2135.5	2322.6
Goods	657.0	728.5	813.5	884.7	969.1	1004.8	1074.8	1161.6
Services	547.4	618.0	693.7	782.5	874.1	966.3	1060.7	1161.0
Gross private domestic investment	324.1	386.6	423.0	402.3	471.5	420.3	487.8	553.4
Residential construction	95.8	111.2	118.6	103.2	104.9	96.2	134.8	153.6
Business fixed investment	205.2	248.9	290.2	309.2	346.1	348.0	341.2	371.7
Change in business inventories	23.0	26.5	14.3	-10.0	20.5	-23.8	11.9	28.1
Nonfarm	21.9	25.4	8.6	-5.7	15.0	-24.3	5.9	34.4
Net exports of goods and services <1>	-4.0	-1.1	13.2	25.2	26.1	20.5	-15.9	-47.6
Exports	182.7	218.7	281.4	339.2	367.3	350.8	335.1	370.4
Imports	186.7	219.8	268.1	314.0	341.3	330.3	351.0	418.0
Gov't. purchases of goods and services	393.8	431.9	474.4	538.4	596.9	647.4	686.3	751.7
Federal <2>	143.4	153.6	168.3	197.2	228.9	257.9	274.5	311.0
State and local	250.4	278.3	306.0	341.2	368.0	389.4	411.7	440.7
Gross national product in constant (1972) dollars	1369.7	1438.6	1479.4	1474.0	1502.6	1476.9	1524.8	1599.4
Personal income	1540.4	1732.7	1951.2	2160.4	2415.8	2569.9	2745.1	2959.5
Wage and salary disbursements	983.2	1106.3	1237.6	1356.1	1493.9	1560.7	1656.5	1792.2
Disposable personal income	1314.0	1474.0	1650.2	1824.1	2029.1	2172.7	2337.1	2529.8
Saving rate (percent)	5.9	6.1	5.9	5.8	6.4	6.5	5.9	5.5
Corporate profits with I.V.A. and C.C.Adj.	167.3	192.4	194.8	181.6	190.6	160.8	206.6	239.1
Corporate profits before tax	194.7	229.1	252.7	242.4	232.1	174.9	190.6	210.5
Federal government surplus or deficit(-) (N.I.A. basis)	-45.9	-29.5	-16.1	-61.4	-60.0	-149.5	-180.9	-191.7
High employment surplus or deficit(-)	-20.5	-16.0	-2.0	-17.1	4.5	-29.8	-46.3	-65.4
State and local government surplus or deficit (-) (N.I.A. basis)	28.0	30.3	30.4	28.1	31.7	32.1	52.4	56.2
Excluding social insurance funds	10.1	10.0	6.6	.9	-1	-4.1	10.7	8.0
Civilian labor force (millions)	99.0	102.3	105.0	106.9	108.7	110.2	111.3	113.4
Unemployment rate (percent)	7.1	6.1	5.8	7.1	7.6	9.7	9.8	8.9
Nonfarm payroll employment (millions)	82.5	86.7	89.8	90.4	91.2	89.6	90.1	92.9
Manufacturing	19.7	20.5	21.0	20.3	20.2	18.9	18.7	20.0
Industrial production (1967=100)	138.1	146.1	152.5	147.0	150.9	138.6	145.7	158.5
Capacity utilization: all manufacturing (percent) <3>	82.2	84.7	86.0	79.6	79.4	71.1	73.9	79.4
Materials (percent) <3>	82.6	85.6	87.6	80.4	80.7	70.1	73.2	80.9
Housing starts, private (million units, A.R.)	1.96	2.00	1.72	1.30	1.10	1.06	1.66	1.74
New auto sales (millions, A.R.)	11.13	11.29	10.68	9.04	8.56	8.00	9.06	9.78
Domestic models	9.07	9.29	8.36	6.62	6.24	5.77	6.79	7.45
Foreign models	2.06	2.00	2.32	2.42	2.32	2.23	2.27	2.33

<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.

<3> Based on revised capacity measures.

July 6, 1983

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

	1977	1978	1979	1980	1981	1982	--Projected--	
							1983	1984
<u>Constant (1972) Dollars</u>								
Gross national product	5.5	5.0	2.8	-4	1.9	-1.7	3.2	4.9
Final sales	5.1	4.9	3.5	.5	1.0	-5	2.2	4.4
Private	6.0	5.6	4.0	.0	1.0	-1.0	2.8	4.4
Domestic final purchases	6.5	5.5	2.9	-1.1	1.8	-.1	4.3	4.5
Personal consumption expenditures	5.0	4.5	2.7	.3	1.8	1.0	3.9	4.0
Goods	5.1	4.2	1.9	-1.5	1.9	.3	4.6	4.1
Services	4.9	4.8	3.7	2.4	1.7	1.8	3.0	3.9
Gross private domestic investment	16.1	10.5	-.2	-11.8	8.3	-12.8	14.0	9.9
Residential structures	18.6	2.8	-5.3	-20.1	-4.9	-10.2	35.5	9.1
Business fixed investment	11.7	12.8	7.3	-2.2	3.6	-3.7	-.9	6.1
Gov't. purchases of goods and services	1.5	2.0	1.3	2.3	.9	1.5	.0	4.7
Federal	3.7	-.1	1.8	4.3	3.7	5.4	-.3	8.8
National defense	.8	.4	2.6	4.0	4.9	6.9	9.2	7.7
State and local	.2	3.3	1.1	1.1	-.8	-1.0	.2	1.9
Disposable personal income	4.0	4.9	2.7	.2	2.5	1.1	3.1	3.5
<u>Current Dollars</u>								
Gross national product	11.7	12.8	11.7	8.9	11.6	4.1	7.7	8.7
Final sales	11.1	12.8	12.4	10.0	10.4	5.7	6.4	8.2
Private	11.7	13.6	13.1	9.1	10.2	5.0	6.6	7.9
Domestic final purchases	13.2	13.4	12.3	8.5	10.3	5.3	8.1	9.1
Personal consumption expenditures	11.1	11.8	11.9	10.6	10.6	6.9	8.3	8.8
Goods	9.8	10.9	11.7	8.8	9.5	3.7	7.0	8.1
Services	12.7	12.9	12.2	12.8	11.7	10.5	9.8	9.5
Gross private domestic investment	25.7	19.3	9.4	-4.9	17.2	-10.9	16.1	13.4
Residential structures	33.1	16.1	6.6	-13.0	1.7	-8.3	40.1	14.0
Business fixed investment	17.9	21.3	16.6	6.5	12.0	.5	-1.9	8.9
Gov't. purchases of goods and services	8.8	9.7	9.8	13.5	10.9	8.5	6.0	9.5
Federal	11.0	7.1	9.6	17.1	16.1	12.6	6.5	13.3
National defense	8.0	8.0	11.5	17.5	17.0	16.2	15.5	13.0
State and local	7.5	11.2	9.9	11.5	7.9	5.8	5.7	7.0
Disposable personal income	10.0	12.2	12.0	10.5	11.2	7.1	7.6	8.2
Personal income	10.7	12.5	12.6	10.7	11.8	6.4	6.8	7.8
Wage and salary disbursements	10.5	12.5	11.9	9.6	10.2	4.5	6.1	8.2
Corporate profits with I.V.A. and C.C.Adj.	21.1	15.0	1.3	-6.8	5.0	-15.6	28.5	15.7
Corporate profits before tax	17.1	17.7	10.3	-4.0	-4.3	-24.6	9.0	10.4
Nonfarm payroll employment	3.9	5.1	3.6	.6	.8	-1.7	.5	3.2
Manufacturing	3.6	4.2	2.6	-3.6	-.6	-6.5	-.8	6.9
Nonfarm business sector								
Output per hour	2.2	.6	-1.3	-.9	1.4	.0	2.8	2.0
Compensation per hour	7.5	8.6	9.3	10.2	9.7	7.2	5.4	5.0
Unit labor costs	5.2	8.0	10.7	11.2	8.1	7.2	2.5	2.9
GNP implicit deflator	5.8	7.4	8.6	9.3	9.4	6.0	4.3	3.6
Gross domestic business product								
fixed-weighted price index <1>	6.1	8.0	9.9	10.1	9.6	5.9	4.3	4.2
Excluding food and energy	6.3	7.8	8.6	8.6	9.4	6.9	4.9	4.1
Consumer price index (all urban)	6.5	7.7	11.3	13.5	10.3	6.2	3.3	4.5
Industrial production	5.9	5.8	4.4	-3.6	2.6	-8.1	5.1	8.8

&lt;1&gt; Uses expenditures in 1972 as weights.

FEDERAL SECTOR ACCOUNTS

July 6, 1983

	Fiscal Year 1982*	FY1983e		FY1984e 2/		CY 1982*	CY1983e/ F.R. Board	FRB Staff Estimates								
		Admin. 1/	F.R. Board	Admin. 1/	F.R. Board			Calendar quarters; unadjusted data								
								1982			1983			1984		
								IV*	I*	II	III	IV	I	II	III	
Unified budget receipts	617.8	598.3	600.0	653.7	663.0	608.8	608.1	137.0	139.8	167.6	155.5	145.2	155.4	188.6	173.7	
Unified budget outlays	728.4	808.5	804.5	843.9	860.7	739.5	810.1	205.3	200.8	196.8	201.6	210.9	213.6	218.3	217.9	
Surplus/deficit(-), unified budget	-110.6	-210.2	-204.6	-190.2	-197.7	-130.7	-202.0	-68.3	-61.0	-29.2	-46.2	-65.7	-58.2	-29.7	-44.2	
Surplus/deficit(-), off-budget agencies <sup>3</sup>	-17.3	-16.8	-14.0	-14.4	-15.1	-14.9	-15.2	-1.1	-1.6	-4.2	-7.0	-2.4	-3.3	-4.3	-5.0	
Combined deficit to be financed	-127.9	-227.0	-218.5	-204.7	-212.8	-145.6	-217.2	-69.4	-62.6	-33.3	-53.2	-68.1	-61.5	-34.0	-49.2	
Means of financing combined deficit:																
Net borrowing from public	134.9	217.0	213.0	204.0	210.8	161.3	204.9	62.0	55.6	44.5	50.9	53.9	63.0	46.3	47.6	
Decrease in cash operating balance	-10.7	9.4	8.4	0.0	-1.8	-7.8	6.5	9.6	4.3	-12.5	7.0	7.7	1.6	-8.5	-2.6	
Other <sup>4</sup>	3.8	0.6	-2.9	-0.7	3.8	-7.9	5.8	-2.2	2.6	1.4	-4.8	6.5	-3.1	-3.8	4.2	
Cash operating balance, end of period	29.4	20.0	21.0	20.0	22.8	19.8	13.3	19.8	15.5	28.0	21.0	13.3	11.7	20.2	22.8	
Memo: Sponsored agency borrowing <sup>5</sup>	20.3	n.a.	0.3	n.a.	23.5	16.9	6.7	-0.4	-3.8	-0.2	4.7	6.0	4.5	6.5	6.5	
<b>NIA Budget</b>								<b>Seasonally adjusted annual rates</b>								
Receipts	619.0	631.2	634.6	682.3	693.7	613.9	646.9	615.0	629.5	648.7	646.3	663.2	688.4	703.0	720.3	
Expenditures	739.7	829.1	818.5	869.6	885.9	763.4	827.8	819.2	803.5	812.0	839.5	856.2	881.0	894.6	912.0	
Purchases	250.1	280.6	278.0	297.0	296.9	257.9	274.5	278.7	274.1	275.3	284.0	264.8	299.2	307.9	315.7	
Defense	173.0	199.3	199.4	229.2	227.2	178.6	206.3	189.3	195.2	201.6	211.4	217.0	225.3	230.6	235.8	
Nondefense	77.1	81.3	78.7	67.8	69.7	79.3	68.3	89.4	79.0	73.7	72.6	47.8	73.9	77.3	79.9	
All other expenditures	489.6	548.5	540.5	572.6	589.0	505.5	553.2	540.5	529.4	536.7	555.5	591.4	581.8	586.7	596.3	
Surplus/deficit(-)	-120.7	-197.9	-183.7	-187.6	-192.2	-149.5	-180.9	-204.2	-174.0	-163.3	-193.2	-193.0	-192.6	-191.6	-191.7	
High Employment (H.E.) surplus/deficit(-) evaluated at H.E. unemployment rate of:																
5.0 percent	-18.8	n.a.	-46.1	n.a.	-65.1	-29.8	-46.2	-64.3	-31.9	-24.6	-64.0	-64.6	-64.2	-65.1	-66.3	
6.0 percent	-43.0	n.a.	-71.2	n.a.	-96.9	-54.5	-72.4	-89.5	-55.0	-49.9	-90.5	-94.1	-95.3	-97.6	-100.5	
	*--actual			e--estimated				n.a.--not available								

1. OMB Current Budget Estimates, April 1983 and BEA NIA translations, April 1983.
2. In the First Concurrent Resolution on the Budget -- Fiscal Year 1984, the Congress recommended revenues of \$679.6 billion and outlays of \$849.5 billion; outlays would be \$8.5 billion higher if the "Reserve fund" for recession relief is fully utilized.
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 and actuals 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.

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



## DOMESTIC FINANCIAL DEVELOPMENTS

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Recent developments. Interest rates have moved up appreciably since early May. While reserve availability has tightened only a little, market expectations have been negatively affected by continuing rapid money stock growth in an environment of strengthening economic activity. Since the May FOMC meeting, short-term interest rates have risen about 55 to 75 basis points, bringing their rise since early May to about 1 to 1-1/4 percentage points. Long-term rates have backed up about as much as short rates.

M1 expanded in June at an estimated 12-1/2 percent annual rate, after the record May surge. All components of M1 advanced briskly in May and June, including demand deposits and currency. The recent strength in M1 may reflect in part the acceleration in spending which likely has bolstered transactions demands for money. From the fourth quarter of 1982 through June, M1 expanded at about a 14 percent annual rate, well above the Committee's longer-run range of 4 to 8 percent.

Growth in M2 and M3 also was strong in June with both aggregates estimated to have grown at around an 11 percent annual rate. Despite moderating inflows into the MMDA accounts, growth in the nontransaction component of M2 picked up in May and June from a depressed April rate, as flows to other household accounts strengthened. Savings deposits increased at a moderate rate in both months, small time deposits apparently expanded in June for the first time since September, and outflows from MMMFs have slowed appreciably from the first-quarter pace. M3 growth was buoyed in June by a resumption of large time deposit growth at commercial banks; over the preceding months banks had paid down more than \$80 billion in large CDs on balance, as MMDA flows raised core deposit growth. Reflecting the recent

strong growth, M2 in June is estimated to be near, and M3 slightly above, the upper ends of their respective long-run ranges.

External financing needs of nonfinancial corporations generally remained low in the second quarter, given improved profit flows and modest fixed investment spending. Firms concentrated on balance sheet restructuring, but in June the rise in bond rates discouraged corporations from issuing long-term debt. The volume of bond issuance dropped off substantially, and corporations increased moderately their short- and intermediate-term indebtedness for the first time since February. Business loans at commercial banks expanded at an estimated 10 percent annual rate in June, and outstanding commercial paper of nonfinancial corporations ceased its nine-month downtrend. During the second quarter, a good share of external financing was accomplished in equity markets, and stock issuance remained strong through June.

Credit flows to the household sector appear to have strengthened in the second quarter. Mortgage commitments outstanding at savings and loans climbed to a record high in May, and real estate loan growth at commercial banks increased in May and probably accelerated further in June. Consumer credit expanded at an annual rate of 8 percent in April, and likely grew still more rapidly later in the quarter in association with rising sales of autos and consumer durables and more attractive rates and terms available on installment loans.

The Treasury raised more than \$40 billion in credit markets in the April-June period, primarily in the intermediate- and long-term markets. About half of the quarter's financing occurred in June (despite a budget surplus in that month) as the Treasury sought to build its cash balances

in anticipation of huge third-quarter needs. By contrast, the exceptional pace of state and local long-term borrowing subsided somewhat in June, as interest rates firmed. The lighter volume of municipal issuance late in the month perhaps also reflected new registration requirements; tax-exempt issues brought to market in late June for delivery in July were required to be in registered form under the new law.

Outlook. Prospective developments in the economy suggest that total private credit demands will remain moderate in the next few months. In the household sector, consumer spending is likely to remain strong, but may not--in light of overall household financial positions--require an increased expansion in consumer installment credit from the recent accelerated pace. Mortgage credit flows also are likely to begin leveling off as the firming of interest rates discourages further growth in housing activity.

The financing gap of nonfinancial corporations is expected to stay quite low during the third quarter; internal cash flows should rise in step with increased inventory accumulation and fixed capital outlays. Overall business credit demands thus are expected to remain near or below recent levels. Firms are likely to continue stressing balance sheet improvement, but the relative emphasis on long-term financing through stock and bond issuance may be less marked than in the more attractive circumstances of earlier months. Some continued use of bank loan and commercial paper financing appears likely in the near term.

The Treasury is expected to borrow \$48 billion in markets in the third quarter to finance a projected deficit of \$53 billion. This would be a less-than-normal seasonal pickup in federal borrowing, as the government runs off some of its ample midyear cash balance. Long-term borrowing

by state and local governments should diminish from the heavy pace of recent months. In addition to some near-term drop associated with the new registration requirements, many municipal units apparently have reduced needs for funds owing to recent strong tax revenues.

The staff expects that, in an environment of somewhat greater restraint on monetary expansion, prospective credit demands will tend to exert further upward pressure on market interest rates in coming months. Short- and long-term interest rates are expected to rise gradually on average over the summer and into early fall, with markets likely remaining very sensitive to incoming monetary and economic data.

## INTERNATIONAL DEVELOPMENTS

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Recent developments. Since the last FOMC meeting, the weighted average value of the dollar has risen on balance by about 2-1/2 percent. It rose in the early part of the period to a new high, and subsequently has remained near that level. Increases in U.S. interest rates relative to those on foreign-currency assets helps to explain the rise. On a bilateral basis, the dollar has risen about 3 percent against EMS currencies, 2 percent against sterling, and over 1 percent against the yen; the dollar has declined slightly against the Canadian dollar.

The U.S. deficit on merchandise trade rose in April from its abnormally low first-quarter level and rose sharply further in May. For April and May combined, the deficit -- at an annual rate of more than \$60 billion -- was higher than in any previous quarter. Exports of manufactured goods declined significantly, and exports of agricultural commodities also were down, while imports, both oil and nonoil, rose. The increase in the deficit in April-May was generated both by the strong U.S. recovery and the continuing impact of the high value of the dollar, but it also reflected a reversal of some transitory factors that reduced the deficit in the first quarter.

Foreign offices of U.S. chartered banks, which had borrowed heavily from domestic offices in the first quarter of this year, reduced their net borrowings in the second quarter in the face of

continued strong growth in Eurodollar deposits by U.S. nonbank residents. In the Eurodollar and U.S. domestic interbank markets, gross claims and liabilities were scaled back in the first half of the year, perhaps reflecting efforts by banks to reduce the size of their balance sheets at a time of rising concern about capital adequacy.

U.S.-chartered bank claims on foreigners (nonbanks as well as banks) declined \$2.7 billion in the first quarter, following sizable increases in the first half and smaller increases in the second half of 1982. Within the total, net new lending to non-OPEC developing countries, to the smaller developed countries, and to offshore banking centers was weak relative to preceding quarters. Most of the changes in claims on individual non-OPEC developing countries were small. While Brazil and Mexico made initial drawings on large commercial bank loans, these drawdowns were largely offset by repayments of a bridge loan and a reduction (caused by a devaluation of the cruzeiro) in the dollar value of local currency loans, in the case of Brazil, and repayments of trade credits and, perhaps, of some private debt, in the case of Mexico.

Foreign net purchases of U.S. corporate stocks amounted to \$3.7 billion in the first four months of this year -- an amount approximately equal to net purchases in the full year 1982. U.S. net purchases of foreign stock amounted to \$1.5 billion in this period, also approximately equal to last year's purchases. Foreign official

reserve assets in the United States rose only \$0.6 billion in the first four months, with a decline in OPEC holdings more than offset by increases by other countries. Partial data for May-June suggest a sizable further drop in OPEC holdings.

Economic recovery in major foreign industrial countries seems to be under way. However, the pace is uneven and appears to be markedly slower than in the United States. The strongest recoveries, as measured by recent GNP growth, have been in Canada and the United Kingdom; growth in those two countries has been supported by changes in inventory behavior and by modest strength in private consumption. Unemployment rates everywhere remain high. Price inflation, on the other hand, continues to decline, except in France, and recent moderate wage settlements in several countries should help to sustain the improved performance. While in most countries trade and current account balances have not shown any swing toward surplus, the Japanese current account has been very strong, with the surplus in the first five months of 1983 -- at \$8 billion -- already exceeding the surplus for 1982 as a whole.

With respect to the debt problems of major developing countries, some news has been good, but the situation remains of considerable concern and new problems have arisen. The greatest progress has been achieved in Mexico (albeit at a tremendous cost in terms of domestic activity): full compliance with IMF performance criteria, a large trade surplus, declining inflation, and a more comfortable foreign exchange position. The financing situation has eased somewhat in Argentina, Chile, and Peru, as well. In contrast, Brazil's funding

problems have become more severe. Brazil -- by not meeting its performance criteria -- remains unable to draw on its IMF arrangement, despite recent monetary and fiscal measures that are said to have approached the bounds of political feasibility. A consolidated bank steering group has been formed to address Brazil's external financing problems after Brazil has come to terms with the IMF. Ecuador is also currently negotiating with banks, while the Philippine government has been acting to gain control of its deteriorating external situation.

Outlook. The staff continues to expect only a modest economic recovery in major foreign countries over the forecast period, with some further reduction in inflation rates. The virtual absence of any fiscal stimulus abroad is the major factor expected to cause this recovery to be slower than previous recoveries. In the developing countries, even where a large part of the necessary domestic adjustment already has taken place, the pace of activity is also likely to be only moderate, at best. Thus, with expected relatively weak demand abroad and an increasingly strong outlook for the U.S. economy, the staff has revised upward its projection of the U.S. trade and current account deficits. The projection is for the deficits to continue to increase sharply in the second half of this year and to level off in 1984; for the full years 1983 and 1984, the projection is for current account deficits of \$44 billion and \$74 billion, respectively. The persistently high value of the dollar is another important factor underlying the upward revision. The staff, however, continues to believe that the dollar will depreciate substantially during the forecast period as the widening trade and current account deficits become increasingly apparent.



JULY 5, 1983

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

	1982 ANN.	1983-P ANN.	1984-P ANN.	1982 Q3	1982 Q4	1983 Q1	1983-P Q2	1983-P Q3	1983-P Q4	1984-P Q1	1984-P Q2	1984-P Q3	1984-P Q4
<b>1. GNP NET EXPORTS</b>													
CURRENT \$, NET	20.5	-15.9	-47.5	7.0	9.0	19.6	-11.4	-29.8	-42.1	-46.6	-47.6	-48.1	-47.9
EXPORTS OF G+S	350.8	335.1	370.4	349.5	328.1	332.4	328.7	336.1	343.4	353.1	363.8	375.2	389.6
IMPORTS OF G+S	330.3	351.0	418.0	342.5	319.1	312.8	340.0	365.9	385.5	399.7	411.4	423.0	437.5
CONSTANT 72 \$, NET	31.8	15.1	13.9	27.5	27.2	24.7	14.3	11.1	10.4	12.2	13.5	14.3	15.7
EXPORTS OF G+S	148.1	138.5	147.5	147.5	138.8	138.9	135.9	138.5	140.8	143.6	146.0	148.4	151.9
IMPORTS OF G+S	116.2	123.4	133.5	120.0	111.6	114.2	121.7	127.4	130.4	131.4	132.5	134.1	136.2
TERMS OF TRADE (1972=100) 1/	83.4	85.2	80.3	83.0	82.7	87.4	86.5	84.5	82.5	80.8	80.2	80.1	79.9
<b>2. U.S. MERCHANDISE TRADE BALANCE 2/</b>													
EXPORTS (EXCL. MILITARY)	211.2	195.4	208.8	209.0	193.4	198.3	194.9	194.1	194.3	197.1	203.5	212.1	222.7
AGRICULTURAL	37.2	35.5	37.0	33.8	33.1	36.0	34.7	35.3	35.8	36.2	36.7	37.2	37.7
NONAGRICULTURAL	174.0	159.9	171.9	175.2	160.3	162.2	160.1	158.8	158.5	160.9	166.8	174.9	184.9
IMPORTS	247.6	263.8	315.3	261.3	238.8	233.2	254.4	276.1	291.4	301.6	309.8	319.4	330.7
PETROLEUM AND PRODUCTS	61.2	56.4	68.5	68.9	60.5	42.0	53.2	62.8	67.7	67.8	66.9	68.2	71.2
NONPETROLEUM	186.4	207.4	246.8	192.3	178.3	191.2	201.2	213.3	223.7	233.8	242.8	251.2	259.4
<b>3. U.S. CURRENT ACCOUNT BALANCE</b>													
OF WHICH: NET INVESTMENT INCOME	27.3	26.3	33.0	27.3	24.0	20.9	24.5	29.0	30.7	33.0	33.6	31.8	33.4
<b>4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/</b>													
REAL GNP, % CHANGE, ANNUAL RATES	0.0	1.2	2.6	-1.6	0.9	2.3	1.6	1.4	2.4	3.0	2.8	3.0	3.4
CONSUMER PRICES, % CHANGE, ANNUAL RATES	8.1	5.8	5.5	6.0	6.0	4.5	6.3	5.6	5.6	5.6	5.6	4.9	4.8

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.  
 GERMANY (20.8%), JAPAN (13.6%), FRANCE (13.1%), UNITED KINGDOM (11.8%) CANADA  
 (9.1%), ITALY (9.0%), THE NETHERLANDS (8.3%), BELGIUM (6.4%)  
 SWEDEN (4.2%), SWITZERLAND (3.6%)  
 P/ PROJECTED