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October 30, 1985

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. The economy still appears to be on a path of moderate growth, albeit with continuing sluggishness in the industrial sector. Inflation has remained relatively subdued.

The index of industrial production edged off 0.1 percent in September. Production of business equipment turned down after two months of increase, and output of consumer goods fell, owing to reduced assemblies of autos and light trucks and a decline in the production of home goods. However, output of defense and space equipment maintained its rapid ascent. On the whole, industrial production has followed an up-and-down pattern in recent months, with average growth this year running at about 1-1/2 percent at an annual rate.

Growth in payroll employment slowed appreciably in September. Nevertheless, for the third quarter as whole, job gains were almost as rapid as in the first half of the year. Employment in the private service sector continued to expand in September, and hiring in construction remained fairly vigorous. However, manufacturing employment fell further, to a level about 340,000 below its January peak. The civilian unemployment rate, after dropping 0.3 of a percentage point in August, edged up to 7.1 percent in September.

Consumer spending grew at a rapid pace again in the third quarter--in real terms, almost 5 percent at an annual rate--but it seems unlikely that this pace can be maintained. A large part of the third-quarter advance reflected consumers' response to the sales incentive programs

offered by automakers in August and September, and with the ending of these programs in early October, sales fell back substantially. Growth in real disposable income remained weak through late summer, and the saving rate fell to the lowest level in more than three decades.

Business fixed investment was quite weak in the third quarter, with preliminary GNP data showing declines in real outlays for both structures and equipment. So far this year, increases in real BFI have averaged about 2-1/2 percent at an annual rate. With respect to forward-looking indicators, equipment orders spurted in late summer, but because much of the increase was for aircraft, the recent advance may provide only a small impetus for near-term investment outlays. The outlook for capital spending in 1986 does not look strong either, as respondents to the McGraw-Hill fall survey (to be released November 8) plan to reduce nominal outlays to a bit less than the 1985 total.

Businesses seem fairly content with their current inventory positions. Except for a sharp drawdown of auto stocks in the third quarter, inventories generally have been rising about in line with sales. The constant-dollar inventory-sales ratio for manufacturing and trade edged down in August and was at the lower end of the narrow range in which it has been fluctuating so far this year.

Indicators of housing activity continue to be mixed. Total private housing starts sagged in September and were down 6 percent for the third third quarter as a whole. In contrast, other indicators have been more buoyant and seemingly more consistent with the reductions in interest rates since last spring. For example, sales of existing homes surged in the third quarter, and new home sales also advanced.

The rate of increase in labor compensation is holding fairly steady. As measured by the employment cost index, total hourly compensation in the private sector has risen about 4-3/4 percent over the past twelve months, roughly the same as in the previous year. Increases in the benefit component of compensation have slowed this year, but there has been an offsetting pickup in the ECI measure of wage inflation, centered mainly in the service-producing industries. The hourly earnings index, which is limited to production and nonsupervisory workers, slowed further in the third quarter, to an annual rate of 1 percent.

Incoming data suggest that price inflation has remained quite moderate in recent months. The consumer price index has been increasing 0.2 percent per month since the spring, and the producer price index, which was down sharply in September, has been essentially flat since the start of the year. Measures of industrial commodity prices have fluctuated in a narrow range recently. Farm crop prices have remained at low levels, but livestock prices have rebounded sharply from the depressed levels reached toward the end of summer.

Outlook. The staff expects that real GNP will grow at an annual rate of around 2-1/2 percent in the current quarter. Final sales are expected to register a small downturn, associated with depressed auto sales during the post-incentive "payback" period and a leveling off of federal spending after a surge in the third quarter. Excluding autos, private final sales are projected to register a moderate advance. In addition, business inventory accumulation is expected to pick up as auto dealers rebuild their stocks.

Inflation, as measured by the fixed-weighted price index for gross business product, is expected to increase at an annual rate of about 3-1/4 percent in the current quarter, more than in the third quarter but still less rapidly than in the first half of the year. Energy prices are not expected to fall as rapidly as in the third quarter, and, reflecting the rebound in livestock prices, consumer food prices appear likely to rise faster than in recent months.

The policy assumptions underlying the staff's economic forecast are similar to those in the last Greenbook. M1 is expected to grow moderately in the fourth quarter and then increase in 1986 at about the midpoint of the tentative target range. Interest rates are expected to ease somewhat over the period. For fiscal policy, the federal budget deficit, on a unified basis, is expected to be about \$193 billion, down only moderately from the \$203 billion of fiscal 1985. The structural deficit is expected to be little changed in 1986.

The staff's assumptions with respect to dollar exchange rates are virtually the same as those that were adopted last month in the wake of the G-5 announcement. Under the assumption of a continuing moderate decline, the dollar by the end of 1986 will have reversed about one-half of its cumulative increase from late 1980 to the quarterly peak in early 1985.

Growth of real GNP in 1986 is expected to average 2-1/2 percent. The forecast has been revised down slightly since the last Greenbook, primarily because of a more pessimistic assessment of the outlook for business fixed investment, which now is projected to rise less rapidly than total GNP. Overall, domestic demand is expected to increase just

under 2 percent next year, reflecting not only the weak investment picture, but also the constraining effect on the consumer sector of a sustained period of slow income growth. Homebuilding, however, is likely to provide some impetus to expansion in 1986, with the demand for owner-occupied dwellings boosted by favorable demographics and lower mortgage rates. And, with the dollar down considerably, the external sector is expected to exert an increasingly positive influence on the U.S. economy as the year progresses.

The depreciating dollar also is likely to lead to a faster rate of increase in import prices, but in the context of sluggish demand growth, the related inflation impulse should be damped. Consumer energy prices are expected to be little changed again in 1986, and food prices are projected to rise as much as general inflation, after only a small increase in 1985. Reflecting these influences, as well as a continuing margin of slack in the economy, the fixed-weighted price index for gross business product is expected to accelerate only moderately next year, to a rate of about 3-3/4 percent.

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						
9/25/85	10/30/85	9/25/85	10/30/85	9/25/85	10/30/85	9/25/85	10/30/85	9/25/85	10/30/85			
Annual changes:												
1983	<1>	7.7	7.7	3.7	3.7	3.7	3.7	4.6	4.6	9.6	9.6	
1984	<1>	10.8	10.8	6.8	6.8	4.0	4.0	4.3	4.3	7.5	7.5	
1985		6.1	6.2	2.4	2.4	3.6	3.6	4.2	4.2	7.3	7.2	
1986		6.3	6.0	2.7	2.4	3.6	3.5	4.2	3.9	7.1	7.2	
Quarterly changes:												
1984	Q1	<1>	14.9	14.9	10.1	10.1	4.2	4.2	3.4	3.4	7.9	7.9
	Q2	<1>	10.7	10.7	7.1	7.1	4.1	4.1	5.4	5.4	7.5	7.5
	Q3	<1>	5.6	5.6	1.6	1.6	4.0	4.0	4.9	4.9	7.4	7.4
	Q4	<1>	7.1	7.1	4.3	4.3	3.5	3.5	3.9	3.9	7.2	7.2
1985	Q1	<1>	5.6	5.6	.3	.3	3.6	3.6	4.6	4.6	7.3	7.3
	Q2	<1>	4.5	4.5	1.9	1.9	3.7	3.7	3.8	3.8	7.3	7.3
	Q3	<1>	6.2	6.7	3.0	3.3	2.8	2.6	3.7	3.5	7.2	7.2
	Q4		5.8	6.0	3.0	2.6	2.8	3.3	3.5	3.5	7.2	7.1
1986	Q1		5.6	5.7	2.5	2.1	3.5	3.7	4.0	3.8	7.2	7.1
	Q2		7.1	6.0	2.7	2.2	4.3	3.7	4.7	4.2	7.1	7.2
	Q3		7.3	6.2	2.8	2.4	4.3	3.9	4.7	4.3	7.0	7.2
	Q4		7.6	6.9	2.9	2.8	4.5	4.0	4.8	4.5	7.0	7.2
Two-quarter changes: <2>												
1984	Q2	<1>	12.8	12.8	8.6	8.6	4.2	4.2	4.4	4.4	-1.0	-1.0
	Q4	<1>	6.4	6.4	2.9	2.9	3.8	3.8	4.4	4.4	-.3	-.3
1985	Q2	<1>	5.1	5.1	1.1	1.1	3.7	3.7	4.2	4.2	.1	.1
	Q4		6.0	6.3	3.0	2.9	2.8	2.9	3.6	3.5	-.1	-.2
1986	Q2		6.3	5.8	2.6	2.1	3.9	3.7	4.4	4.0	-.1	.1
	Q4		7.4	6.5	2.9	2.6	4.4	4.0	4.8	4.4	-.1	.0
Four-quarter changes: <3>												
1983	Q4	<1>	10.4	10.4	6.3	6.3	3.7	3.7	4.4	4.4	-2.1	-2.1
1984	Q4	<1>	9.5	9.5	5.7	5.7	4.0	4.0	4.4	4.4	-1.3	-1.3
1985	Q4		5.5	5.7	2.0	2.0	3.2	3.3	3.9	3.9	.0	-.1
1986	Q4		6.9	6.2	2.7	2.4	4.2	3.8	4.6	4.2	-.2	.1

<1> Actual.

<2> Percent change from two quarters earlier.

<3> Percent change from four quarters earlier.

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

	1983				1984			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross National Product	3173.8	3267.0	3346.6	3431.7	3553.3	3644.7	3694.6	3758.7
Gross domestic purchases	3154.2	3273.4	3363.0	3461.5	3604.8	3703.4	3785.2	3814.8
Final sales	3216.8	3286.4	3350.9	3419.0	3479.5	3594.1	3622.8	3722.1
Private	2538.0	2604.2	2661.1	2727.6	2775.1	2850.4	2861.8	2941.6
Domestic final purchases	2518.4	2610.7	2677.5	2757.4	2826.6	2909.1	2952.4	2997.6
Personal consumption expenditures	2070.4	2141.6	2181.4	2230.2	2276.5	2332.7	2361.4	2396.5
Goods	1034.6	1073.0	1095.8	1122.8	1152.2	1179.0	1178.6	1192.8
-Services	1035.8	1068.6	1085.7	1107.5	1124.4	1153.7	1182.8	1203.8
Gross private domestic investment	405.0	449.6	491.9	540.0	623.8	627.0	662.8	637.8
Residential structures	113.3	129.8	142.3	143.4	151.2	155.6	155.3	153.5
Business fixed investment	334.6	339.3	353.9	383.9	398.8	420.8	435.7	447.7
Change in business inventories	-42.9	-19.4	-4.3	12.7	73.8	50.6	71.8	36.6
Nonfarm	-32.6	-5.4	11.6	14.1	60.6	47.0	63.7	27.2
Net exports of goods and services <1>	19.6	-6.5	-16.4	-29.8	-51.5	-58.7	-90.6	-56.0
Exports	328.5	328.1	342.0	346.1	358.9	362.4	368.6	367.2
Imports	308.9	334.5	358.4	375.9	410.4	421.1	459.3	423.2
Gov't. purchases of goods and services	678.8	682.2	689.8	691.4	704.4	743.7	761.0	780.5
Federal <2>	273.0	270.5	269.2	266.3	267.6	296.4	302.0	315.7
State and local	405.8	411.6	420.6	425.1	436.8	447.4	458.9	464.8
Gross national product in constant (1972) dollars	1491.0	1524.8	1550.2	1572.7	1610.9	1638.8	1645.2	1662.4
Personal income	2662.8	2714.4	2763.3	2836.5	2920.5	2984.6	3047.3	3096.2
Wage and salary disbursements	1608.1	1642.1	1671.3	1715.4	1755.7	1793.1	1819.5	1847.6
Disposable personal income	2261.4	2302.9	2367.4	2428.6	2502.2	2554.3	2606.4	2644.5
Saving rate (percent)	5.7	4.2	5.0	5.3	6.1	5.7	6.3	6.2
Corporate profits with I.V.A. and C.C. Adj.	179.1	216.7	245.0	260.0	277.4	291.1	282.8	291.6
Corporate profits before tax	161.7	198.2	227.4	225.5	243.3	246.0	224.8	228.7
Federal government surplus or deficit (-) (N.I.A. basis)	-185.7	-167.3	-180.9	-180.5	-161.3	-163.7	-180.6	-197.8
High employment surplus or deficit (-) <3>	-80.9	-74.2	-102.5	-113.1	-113.3	-129.6	-146.1	-169.3
State and local government surplus or deficit(-) (N.I.A. basis)	34.1	43.9	47.4	51.2	53.9	54.5	47.6	55.6
Excluding social insurance funds	-1.9	7.0	9.5	12.0	13.4	12.6	4.3	11.1
Civilian labor force (millions)	110.7	111.2	112.1	112.1	112.7	113.5	113.8	114.2
Unemployment rate (percent)	10.4	10.1	9.3	8.5	7.9	7.5	7.4	7.2
Nonfarm payroll employment	88.8	89.6	90.5	91.8	93.0	94.0	94.9	95.8
Manufacturing	18.1	18.3	18.5	18.9	19.2	19.4	19.5	19.6
Industrial production (1977=100)	103.3	106.8	111.7	114.9	119.3	121.5	123.4	123.1
Capacity utilization: all manufacturing (percent)	70.2	72.5	75.8	77.4	79.8	80.8	81.6	81.0
Materials (percent)	71.4	73.6	77.0	79.3	82.0	82.6	83.0	81.4
Housing starts, private (million units, A.R.)	1.64	1.67	1.79	1.72	1.95	1.86	1.66	1.60
New auto sales (millions, A.R.)	8.46	9.10	9.22	9.94	10.52	10.60	10.30	10.29
Domestic models	6.06	6.81	6.92	7.29	8.22	8.23	7.94	7.50
Foreign models	2.40	2.28	2.31	2.65	2.30	2.38	2.36	2.79

<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 expenditures are shown in the Federal Sector Account table which follows.

<3> Estimates in table are evaluated at a 6 percent high employment unemployment rate.

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

	1983				1984			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	3.3	9.4	6.8	5.9	10.1	7.1	1.6	4.3
Gross domestic purchases	3.7	12.3	7.4	8.7	12.9	7.9	5.4	.9
Final sales	1.1	6.4	4.9	4.2	3.6	10.3	-1.0	7.9
Private	3.5	8.6	6.2	6.3	4.2	8.5	-2.4	8.4
Domestic final purchases	4.0	12.1	6.9	9.7	7.6	9.5	2.3	4.0
Personal consumption expenditures	2.6	10.0	3.8	6.8	4.6	7.9	.7	3.6
Goods	3.5	12.6	5.4	9.5	7.8	10.7	-1.9	3.8
Services	1.5	7.3	2.1	3.8	1.2	4.6	3.8	3.3
Gross private domestic investment	34.1	52.5	38.4	37.0	71.6	-2.2	24.9	-13.1
Residential structures	64.5	78.1	31.6	4.0	21.3	1.2	-4.6	-5.5
Business fixed investment	.0	9.6	18.7	30.6	20.6	21.3	13.7	8.5
Gov't. purchases of goods and services	-8.2	-2.6	-.5	-4.3	1.0	18.6	5.4	5.9
Federal	-17.4	-5.9	-5.3	-8.7	-2.8	45.2	6.2	15.2
National defense	6.8	7.6	-1.9	9.2	3.4	12.2	-2.3	17.5
State and local	-1.2	-2	2.7	-1.4	3.5	3.7	4.8	-2
Disposable personal income	2.1	3.3	7.7	8.2	8.6	6.3	3.9	3.5
<u>Current Dollars</u>								
Gross national product	8.5	12.3	10.1	10.6	14.9	10.7	5.6	7.1
Gross domestic purchases	6.7	16.0	11.4	12.2	17.6	11.4	9.1	3.2
Final sales	5.9	8.9	8.1	8.4	7.3	13.8	3.2	11.4
Personal consumption expenditures	4.8	14.5	7.6	9.2	8.6	10.2	5.0	6.1
Goods	3.6	15.7	8.8	10.2	10.9	9.6	-.1	4.9
Services	6.1	13.3	6.6	8.3	6.2	10.9	10.5	7.3
Gross private domestic investment	34.3	52.0	43.2	45.3	78.0	2.0	24.9	-14.3
Residential structures	79.3	71.9	44.4	3.3	23.6	12.1	-.6	-4.7
Business fixed investment	-5.5	5.7	18.5	38.4	16.5	23.9	14.9	11.5
Gov't. purchases of goods and services	-1.3	2.0	4.5	.9	7.8	24.3	9.6	10.7
Federal	-8.9	-3.6	-2.0	-4.3	2.0	50.5	7.8	19.4
National defense	7.9	9.8	3.3	13.2	12.5	14.7	-.8	22.1
State and local	4.2	5.8	9.0	4.4	11.5	10.0	10.7	5.2
Disposable personal income	4.3	7.5	11.7	10.7	12.7	8.6	8.4	6.0
Personal income	3.6	8.0	7.3	11.0	12.4	9.1	8.6	6.7
Wage and salary disbursements	5.6	8.7	7.3	11.0	9.7	8.8	5.9	6.5
Corporate profits with I.V.A. and C.C.Adj.	94.8	114.3	63.4	26.8	29.6	21.3	-10.9	13.0
Corporate profits before tax	16.0	125.7	73.3	-3.3	35.5	4.5	-30.3	7.1
Nonfarm payroll employment	.5	3.4	4.2	5.8	5.5	4.3	3.9	4.0
Manufacturing	-1.2	4.4	6.2	7.8	6.4	4.5	2.4	1.1
Nonfarm business sector								
Output per hour	4.4	8.1	2.1	1.0	2.9	5.5	-1.1	2.2
Compensation per hour	5.7	3.5	2.2	4.1	6.1	3.7	3.6	3.7
Unit labor costs	1.3	-4.2	.1	3.0	3.1	-1.7	4.7	1.4
GNP implicit deflator <1>	5.0	2.6	3.1	4.4	4.4	3.3	3.9	2.8
Gross domestic business product								
fixed-weighted price index <2>	2.7	3.9	4.5	3.5	4.2	4.1	4.0	3.5
Excluding food and energy	4.9	3.5	5.4	3.8	3.4	5.4	4.9	3.9
Consumer price index (all urban)	.4	4.3	4.2	4.2	5.2	3.7	3.7	3.6
Industrial production	11.5	14.0	19.8	12.0	16.0	7.6	6.4	-.7

<1> Excluding the federal pay increase, the rate of change in 1983-Q4 was 4.4 percent.

<2> Uses expenditures in 1972 as weights.

October 30, 1985

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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.)

	1985				Projected 1986			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Gross National Product	3810.6	3853.1	3916.1	3973.4	4028.4	4087.6	4149.4
Gross domestic purchases	3885.2	3947.1	4005.3	4070.0	4127.0	4182.6	4244.4	4307.2
Final sales	3770.0	3835.2	3924.2	3948.7	4004.9	4065.6	4125.7	4195.3
Private	2978.1	3024.3	3078.3	3091.8	3142.9	3193.1	3240.6	3296.0
Domestic final purchases	3052.6	3118.3	3167.5	3188.4	3241.5	3288.1	3335.6	3383.8
Personal consumption expenditures	2446.5	2493.0	2536.5	2552.0	2597.0	2634.5	2672.7	2711.7
Goods	1212.1	1231.1	1251.2	1244.4	1265.8	1277.5	1289.6	1302.6
Services	1234.4	1261.9	1285.3	1307.6	1331.1	1357.0	1383.1	1409.1
Gross private domestic investment	646.8	643.2	622.8	661.0	668.0	675.6	686.6	696.3
Residential structures	155.2	158.0	163.4	166.9	170.4	174.4	178.4	182.4
Business fixed investment	450.9	467.3	467.5	469.5	474.1	479.2	484.5	489.8
Change in business inventories	40.7	17.9	-8.1	24.7	23.5	22.0	23.7	24.1
Nonfarm	34.1	11.4	-8.4	23.7	21.9	22.1	23.8	24.2
Net exports of goods and services <1>	-74.5	-94.0	-89.2	-96.6	-98.6	-95.0	-95.1	-87.9
Exports	360.7	347.7	347.6	355.1	361.4	372.3	382.8	398.4
Imports	435.2	441.6	436.7	451.8	460.0	467.3	477.8	486.3
Gov't. purchases of goods and services	791.9	810.9	845.9	857.0	862.0	872.5	885.1	899.3
Federal <2>	319.9	324.2	347.0	350.7	348.4	351.3	356.1	362.2
State and local	472.0	486.7	498.9	506.3	513.6	521.2	529.0	537.1
Gross national product in constant (1972) dollars	1663.5	1671.3	1684.8	1695.5	1704.4	1713.6	1723.8	1735.8
Personal income	3143.8	3174.7	3199.1	3263.0	3313.1	3361.3	3414.3	3471.5
Wage and salary disbursements	1882.7	1910.6	1935.2	1965.4	1994.2	2023.0	2052.1	2083.3
Disposable personal income	2654.8	2726.5	2712.6	2766.1	2818.5	2855.7	2897.7	2942.8
Saving rate (percent)	4.5	5.1	2.9	4.1	4.2	4.1	4.1	4.1
Corporate profits with I.V.A. and C.C. Adj.	292.3	298.5	324.1	313.9	304.9	306.4	306.6	307.9
Corporate profits before tax	222.3	221.0	235.8	225.6	217.8	221.1	220.3	220.6
Federal government surplus or deficit (-) (N.I.A. basis)	-165.1	-214.1	-196.3	-198.6	-196.9	-189.7	-186.6	-185.3
High employment surplus or deficit (-) <3>	-129.4	-178.3	-161.5	-163.5	-159.9	-150.5	-146.2	-144.8
State and local government surplus or deficit(-) (N.I.A. basis)	53.7	50.3	48.7	47.8	48.8	50.2	50.2	50.8
Excluding social insurance funds	8.3	4.2	2.2	.5	.7	1.3	.5	.1
Civilian labor force (millions)	115.2	115.2	115.5	116.0	116.6	117.1	117.6	118.1
Unemployment rate (percent)	7.3	7.3	7.2	7.1	7.1	7.2	7.2	7.2
Nonfarm payroll employment	96.6	97.3	97.9	98.4	99.0	99.4	99.9	100.4
Manufacturing	19.6	19.4	19.3	19.3	19.4	19.4	19.5	19.5
Industrial production (1977=100)	123.8	124.2	124.5	125.2	125.8	126.6	127.5	128.4
Capacity utilization: all manufacturing (percent)	80.5	80.3	80.1	79.9	79.8	79.8	79.8	79.8
Materials (percent)	81.5	80.4	79.6	79.4	79.3	79.3	79.2	79.3
Housing starts, private (million units, A.R.)	1.80	1.77	1.66	1.70	1.75	1.75	1.80	1.80
New auto sales (millions, A.R.)	10.87	10.92	12.31	9.90	10.70	10.70	10.70	10.70
Domestic models	8.46	8.27	9.40	6.90	7.70	7.70	7.60	7.60
Foreign models	2.42	2.65	2.90	3.00	3.00	3.00	3.10	3.10

<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 Account table which follows.

<3> Estimates in table are evaluated at a 6 percent high employment unemployment rate.

	1985				Projected 1986			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) Dollars</u>								
Gross national product	.3	1.9	3.3	2.6	2.1	2.2	2.4	2.8
Gross domestic purchases	3.9	3.2	3.2	2.5	1.9	1.7	1.9	1.9
Final sales	-.3	4.6	5.9	-1.0	2.4	2.3	2.2	2.8
Private	-.4	4.8	3.6	-1.5	3.3	2.6	2.2	2.8
Domestic final purchases	4.1	6.4	3.5	-1.5	3.1	2.0	1.6	1.6
Personal consumption expenditures	5.2	4.8	4.8	-2.2	3.3	1.8	1.5	1.5
Goods	5.4	5.4	6.8	-5.8	4.5	1.2	.8	1.0
Services	5.0	4.2	2.7	2.2	2.1	2.6	2.2	2.0
Gross private domestic investment	3.1	-3.5	-14.9	25.2	.7	2.0	3.2	2.1
Residential structures	5.3	6.4	10.9	6.1	5.1	6.1	5.6	5.2
Business fixed investment	-1.6	14.5	-4.7	.1	1.3	1.4	1.4	1.3
Gov't. purchases of goods and services	.3	3.7	16.1	1.0	-1.7	.8	2.4	3.1
Federal	.7	-.4	33.4	.1	-6.4	-.9	2.3	4.1
National defense	-.2	7.2	20.1	.8	1.6	2.8	1.2	1.6
State and local	.0	6.7	5.0	1.7	1.9	2.1	2.4	2.3
Disposable personal income	-1.6	8.2	-4.2	3.2	3.9	1.3	1.6	1.9
<u>Current Dollars</u>								
Gross national product	5.6	4.5	6.7	6.0	5.7	6.0	6.2	6.9
Gross domestic purchases	7.6	6.5	6.0	6.6	5.7	5.5	6.0	6.0
Final sales	5.2	7.1	9.6	2.5	5.8	6.2	6.0	6.9
Personal consumption expenditures	8.6	7.8	7.2	2.5	7.2	5.9	5.9	6.0
Goods	6.6	6.4	6.7	-2.1	7.1	3.7	3.8	4.1
Services	10.6	9.2	7.6	7.1	7.4	8.0	7.9	7.7
Gross private domestic investment	5.8	-2.2	-12.1	26.9	4.3	4.6	6.7	5.7
Residential structures	4.6	7.4	14.4	8.8	8.7	9.7	9.5	9.3
Business fixed investment	3.0	15.3	.1	1.7	4.0	4.3	4.6	4.4
Gov't. purchases of goods and services	5.9	10.0	18.4	5.3	2.4	4.9	5.9	6.6
Federal	5.4	5.6	31.2	4.3	-2.6	3.4	5.6	7.0
National defense	4.0	12.8	21.5	5.8	4.9	6.6	5.4	5.3
State and local	6.3	13.0	10.5	6.0	6.0	6.0	6.1	6.3
Disposable personal income	1.6	11.2	-2.0	8.1	7.8	5.4	6.0	6.4
Personal income	6.3	4.0	3.1	8.2	6.3	5.9	6.5	6.9
Wage and salary disbursements	7.8	6.1	5.3	6.4	6.0	5.9	5.9	6.2
Corporate profits with I.V.A. and C.C.Adj.	1.0	8.8	39.0	-12.0	-11.0	2.0	.3	1.7
Corporate profits before tax	-10.7	-2.3	29.6	-16.2	-13.1	6.2	-1.4	.5
Nonfarm payroll employment	3.3	2.9	2.5	2.1	2.1	1.9	1.9	2.1
Manufacturing	.0	-2.7	-2.0	.3	.8	.8	1.0	1.0
Nonfarm business sector								
Output per hour	-3.1	1.2	1.2	.7	.8	.8	1.1	1.1
Compensation per hour	5.0	3.4	3.9	4.0	4.6	4.1	4.3	4.5
Unit labor costs	8.4	2.1	2.7	3.3	3.8	3.3	3.2	3.4
GNP implicit deflator <1>	5.4	2.6	3.3	3.3	3.5	3.7	3.7	4.0
Gross domestic business product								
fixed-weighted price index <2>	3.6	3.7	2.6	3.3	3.7	3.7	3.9	4.0
Excluding food and energy	4.6	3.8	3.5	3.5	3.8	4.2	4.3	4.5
Consumer price index (all urban)	3.2	4.2	2.4	3.6	4.2	3.9	4.1	4.2
Industrial production	2.1	1.3	1.1	2.1	2.2	2.4	2.7	2.9

<1> Excluding Federal pay increase, the rate of change in 1985-Q1 was 5.0 percent.

<2> Uses expenditures in 1972 as weights.

	1979	1980	1981	1982	1983	1984	---Projected---	
							1985	1986
Gross national product	2417.8	2631.7	2957.7	3069.2	3304.8	3662.8	3888.3	4121.2
Gross domestic purchases	2404.5	2607.7	2929.8	3050.2	3313.1	3727.0	3976.8	4215.3
Final sales	2403.5	2641.4	2931.7	3095.4	3318.3	3604.6	3869.5	4097.9
Private	1929.2	2103.7	2335.2	2444.9	2632.7	2857.2	3043.1	3218.1
Domestic final purchases	1915.9	2079.7	2307.2	2425.9	2641.0	2921.4	3131.7	3312.3
Personal consumption expenditures	1507.1	1668.0	1849.1	1984.9	2155.9	2341.8	2507.0	2654.0
Goods	813.4	883.5	966.1	1002.6	1081.5	1175.7	1234.7	1283.9
Services	693.7	784.5	883.0	982.2	1074.4	1166.1	1272.3	1370.1
Gross private domestic investment	423.0	401.9	484.2	414.9	471.6	637.8	643.5	681.6
Residential construction	118.5	102.9	104.3	91.3	132.2	153.9	160.9	176.4
Business fixed investment	290.2	308.8	353.9	349.6	352.9	425.7	463.8	481.9
Change in business inventories	14.3	-9.8	26.0	-26.1	-13.5	58.2	18.8	23.3
Nonfarm	8.6	-4.5	18.2	-23.9	-3.1	49.6	15.2	23.0
Net exports of goods and services <1>	13.2	23.9	28.0	19.0	-8.3	-64.2	-88.6	-94.1
Exports	281.3	338.8	369.9	348.4	336.2	364.3	352.8	378.7
Imports	268.1	314.8	341.9	329.4	344.4	428.5	441.3	472.9
Gov't. purchases of goods and services	474.4	537.8	596.5	650.5	685.5	747.4	826.4	879.7
Federal <2>	168.3	197.0	228.9	258.9	269.7	295.4	335.4	354.5
State and local	306.0	340.8	367.6	391.5	415.8	452.0	491.0	525.2
Gross national product in constant (1972) dollars	1479.4	1475.0	1512.1	1480.0	1534.7	1639.3	1678.8	1719.4
Personal income	1951.1	2165.3	2429.4	2584.6	2744.2	3012.1	3195.1	3390.1
Wage and salary disbursements	1237.6	1356.7	1493.1	1568.7	1659.2	1804.0	1923.5	2038.1
Disposable personal income	1650.2	1828.9	2041.7	2180.5	2340.1	2576.8	2715.0	2878.7
Saving rate (percent)	5.9	6.0	6.7	6.2	5.0	6.1	4.1	4.1
Corporate profits with I.V.A. and C.C.Adj.	194.8	175.4	189.9	159.1	225.2	285.7	307.2	306.4
Corporate profits before tax	252.7	234.6	221.2	165.5	203.2	235.7	226.1	219.9
Federal government surplus or deficit (-) (N.I.A. basis)	-16.1	-61.2	-64.3	-148.2	-178.6	-175.8	-193.5	-189.6
High employment surplus or deficit (-)	-20.8	-36.4	-31.3	-61.6	-92.7	-139.6	-158.2	-150.4
State and local government surplus or deficit (-) (N.I.A. basis)	30.4	30.6	37.6	32.9	44.1	52.9	50.1	50.0
Excluding social insurance funds	6.6	3.5	7.8	-8	6.6	10.4	3.8	.7
Civilian labor force (millions)	105.0	106.9	108.7	110.2	111.6	113.5	115.5	117.3
Unemployment rate (percent)	5.8	7.1	7.6	9.7	9.6	7.5	7.2	7.2
Nonfarm payroll employment (millions)	89.8	90.4	91.2	89.6	90.2	94.5	97.6	99.7
Manufacturing	21.0	20.3	20.2	18.8	18.4	19.4	19.4	19.5
Industrial production (1977=100)	110.7	108.6	111.0	103.1	109.2	121.8	124.4	127.1
Capacity utilization: all manufacturing (percent)	84.6	79.3	78.3	70.3	74.0	80.8	80.2	79.8
Materials (percent)	87.1	81.1	81.1	71.7	75.3	82.3	80.2	79.3
Housing starts, private (million units, A.R.)	1.72	1.30	1.10	1.06	1.70	1.77	1.73	1.77
New auto sales (millions, A.R.)	10.68	9.04	8.56	8.00	9.18	10.43	11.00	10.70
Domestic models	8.36	6.62	6.24	5.77	6.77	7.97	8.26	7.65
Foreign models	2.32	2.42	2.32	2.23	2.41	2.46	2.74	3.05

<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.

	1979	1980	1981	1982	1983	1984	---Projected---	
							1985	1986
<u>Constant (1972) Dollars</u>								
Gross national product	2.8	-.3	2.5	-2.1	3.7	6.8	2.4	2.4
Gross domestic purchases	2.0	-1.2	3.1	-1.2	5.0	8.7	3.4	2.2
Final sales	3.5	.5	1.5	-.7	3.2	5.0	3.4	2.3
Private	4.0	.1	1.6	-1.3	4.1	5.3	2.9	2.2
Domestic final purchases	2.9	-1.0	2.2	-.2	5.6	7.6	4.2	2.0
Personal consumption expenditures	2.7	.5	2.0	1.4	4.8	5.3	3.9	1.9
Goods	1.9	-1.4	1.7	.4	6.0	7.1	3.9	1.5
Services	3.7	2.7	2.3	2.5	3.4	3.2	3.9	2.4
Gross private domestic investment	-.2	-11.8	10.7	-15.8	13.7	31.2	-.5	3.1
Residential structures	-5.3	-20.3	-5.5	-14.8	41.7	12.2	2.5	6.3
Business fixed investment	7.3	-2.4	5.6	-4.7	2.5	19.8	6.0	1.1
Gov't. purchases of goods and services	1.3	2.2	1.0	2.0	-.3	3.5	5.6	2.5
Federal	1.8	4.2	3.6	6.1	-.6	5.4	9.9	2.3
National defense	2.6	3.9	5.1	7.6	7.1	5.8	7.3	4.1
State and local	1.1	1.0	-.6	-.6	.0	2.2	2.7	2.7
Disposable personal income	2.7	.6	2.7	.9	3.5	6.7	2.3	2.1
<u>Current Dollars</u>								
Gross national product	11.7	8.8	12.4	3.8	7.7	10.8	6.2	6.0
Gross domestic purchases	11.1	8.4	12.3	4.1	8.6	12.5	6.7	6.0
Final sales	12.4	9.9	11.0	5.6	7.2	8.6	7.3	5.9
Personal consumption expenditures	11.9	10.7	10.9	7.3	8.6	8.6	7.1	5.9
Goods	11.7	8.6	9.3	3.8	7.9	8.7	5.0	4.0
Services	12.2	13.1	12.6	11.2	9.4	8.5	9.1	7.7
Gross private domestic investment	9.4	-5.0	20.5	-14.3	13.7	35.2	.9	5.9
Residential structures	6.6	-13.2	1.4	-12.4	44.7	16.4	4.5	9.7
Business fixed investment	16.6	6.4	14.6	-1.2	.9	20.6	9.0	3.9
Gov't. purchases of goods and services	9.8	13.4	10.9	9.0	5.4	9.0	10.6	6.4
Federal	9.6	17.1	16.2	13.1	4.2	9.5	13.5	5.7
National defense	11.5	17.3	17.2	16.8	11.7	10.5	11.1	7.9
State and local	9.9	11.4	7.9	6.5	6.2	8.7	8.6	7.0
Disposable personal income	12.0	10.8	11.6	6.8	7.3	10.1	5.4	6.0
Personal income	12.6	11.0	12.2	6.4	6.2	9.8	6.1	6.1
Wage and salary disbursements	11.9	9.6	10.1	5.1	5.8	8.7	6.6	6.0
Corporate profits with I.V.A. and C.C.Adj.	1.2	-9.9	8.3	-16.2	41.5	26.9	7.5	-.3
Corporate profits before tax	10.3	-7.1	-5.7	-25.2	22.8	16.0	-4.1	-2.7
Nonfarm payroll employment	3.6	.6	.8	-1.7	.7	4.7	3.3	2.1
Manufacturing	2.6	-3.6	-.6	-6.9	-1.8	5.3	.0	.2
Nonfarm business sector								
Output per hour	-1.5	-.7	1.5	.2	3.5	2.7	.3	.9
Compensation per hour	9.0	10.3	9.6	8.0	4.9	4.1	4.0	4.2
Unit labor costs	10.7	11.1	8.0	7.7	1.4	1.4	3.8	3.2
GNP implicit deflator	8.6	9.2	9.6	6.0	3.8	3.8	3.7	3.5
Gross domestic business product								
fixed-weighted price index <1>	9.9	9.9	9.7	5.9	3.7	4.0	3.6	3.5
Excluding food and energy	8.6	8.5	9.4	7.0	4.6	4.3	4.2	3.9
Consumer price index (all urban)	11.3	13.5	10.3	6.1	3.2	4.3	3.5	3.8
Industrial production	3.9	-1.9	2.2	-7.1	5.9	11.6	2.1	2.1

<1> Uses expenditures in 1972 as weights.

October 30, 1985

FEDERAL SECTOR ACCOUNTS
(Billions of dollars)

	Fiscal Year 1984*	Fiscal Year 1985*	FY1986 ^e 2/3/		CY 1984*	CY1985 ^e FRB Staff	FRB staff estimates								
			Admin. 1/	FRB Staff			Calendar quarters; not seasonally adjusted								
							1984			1985			1986		
							IV*	I*	II*	III*	IV	I	II	III	
Unified budget receipts	666	734	780	773	683	742	166	174	206	188	174	180	225	194	
Unified budget outlays	842	937	955	966	868	944	239	230	234	234	246	239	241	240	
Surplus/deficit(-), unified budget	-175	-203	-175	-193	-184	-202	-72	-56	-28	-47	-72	-60	-16	-46	
Surplus/deficit(-), off-budget agencies ⁴	-10	-9	-2	-5	-10	-11	1	-3	-5	-3	-1	-1	-2	-1	
Combined deficit to be financed	-185	-212	-178	-198	-195	-213	-71	-59	-32	-50	-72	-61	-18	-47	
Means of financing combined deficit:															
Net borrowing from public	171	197	180	201	199	206	64	42	45	46	73	52	31	45	
Decrease in cash operating balance	7	13	0	-8	-6	3	13	4	-10	7	2	0	-10	0	
Other ⁵	8	1	-2	5	2	4	-6	13	-3	-3	-3	9	-3	2	
Cash operating balance, end of period	30	17	20	25	18	15	18	14	24	17	15	15	25	25	
Memo: Sponsored agency borrowing ⁶	30	21	n.a.	20	30	22	4	4	8	5	5	5	5	5	
NIA Budget							Seasonally adjusted annual rates								
Receipts	688	750	809	799	705	766	722	771	734	774	784	789	804	818	
Expenditures	860	944	978	992	881	959	920	937	948	970	983	986	993	1004	
Purchases	283	327	343	352	295	335	316	320	324	347	351	348	351	356	
Defense	215	240	255	262	222	246	232	234	241	253	257	260	264	268	
Nondefense	68	87	88	90	74	89	84	86	83	94	94	89	87	89	
All other expenditures	577	617	635	640	586	624	604	617	624	623	632	638	642	648	
Surplus/deficit(-)	-172	-193	-169	-193	-176	-194	-198	-165	-214	-196	-199	-197	-190	-187	
High employment surplus/deficit(-) evaluated at 6 percent unemployment	-126	-160	n.a.	-155	-140	-158	-169	-129	-178	-162	-164	-160	-151	-146	
	*--actual			e--estimated			n.a.--not available								

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1. Mid-session Review, August 30, 1985.
2. The Congressional Budget Resolution, passed August 1, 1985, shows revenues of \$796 billion, combined unified and off-budget outlays of \$968 billion, and a total deficit of \$172 billion in fiscal year 1986.
3. The latest CBO budget estimates that incorporate the Budget Resolution policy assumptions and the August 1985 CBO economic forecast show revenues of \$790 billion, combined unified and off-budget outlays of \$965 billion, and a total deficit of \$175 billion in fiscal year 1986.

Note: Details may not add to totals due to rounding.

4. Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, Rural Telephone Bank, and Strategic Petroleum Reserve.
5. Checks issued less checks paid, accrued items and other transactions.
6. Sponsored agency borrowing includes net debt issuance by Federal Home Loan Banks, FHLMC (excluding participation certificates), FNMA (excluding mortgage-backed securities), Federal Land Banks, Federal Intermediate Credit Banks, Banks for Cooperatives, and Student Loan Marketing Association marketable debt on a payment basis. The Administration's definition of borrowing by these agencies is somewhat broader.

DOMESTIC FINANCIAL DEVELOPMENTS

Recent developments. Market rates of interest generally are unchanged or somewhat lower on net since the October FOMC meeting. Reserve market conditions have been fairly stable, with federal funds trading most recently a little below 8 percent. Some market participants had been anticipating a bit more accommodative stance on the part of the System, in light of the G-5 agreement, but sentiment has been buoyed by evidence of moderate economic expansion, subdued inflation, and slowing monetary growth.

Growth in the monetary aggregates slowed in September, with M1 rising at an 11-1/2 percent rate despite a surge late in the month associated with disruptions of financial flows caused by Hurricane Gloria. These effects seem to have been reversed in October, when M1 on average appears to have leveled off; this aggregate, however, still remains well above its target range. M2 decelerated to a 7 percent annual rate in September. There was an actual decline in M2 money market fund balances and a marked slowing in growth of savings deposits and MMDAs at both commercial banks and thrift institutions. Growth in small time deposits during September remained negative, but less so than in August. Current estimates suggest that M2 rose by about 2 percent in October, moving it into its 1985 target range. M3 accelerated slightly in September, to 9 3/4 percent, as managed liabilities at banks rose in response to the runoff of U.S. Government deposits. Issuance of large time deposits remained firm in October, but M3 remains well within its annual target range.

Growth of debt, in the aggregate, has remained rapid, but somewhat under the pace earlier in the year. Credit demands of nonfinancial business have weakened since midyear, especially in short-term components such as bank loans and commercial paper. A combination of rising cash flow and declining inventories has more than offset the effect of continued large net equity liquidations associated with mergers, buy-outs, and share repurchases. Business loans at banks and commercial paper declined a little on average for September, and gross issuance of corporate bonds slowed in both September and October.

Enthusiasm for debt lengthening may have been damped a bit by the backup in bond rates after early summer, but financial corporations nonetheless have not cut back their bond issuance as much as industrial firms. Financial subsidiaries of automobile firms have raised funds to support their low interest rate loan programs, while thrifts and subsidiaries of home builders have been strong issuers of collateralized mortgage obligations.

Gross issuance of tax-exempt securities has been quite high in the past few months. Activity has been spurred by heavy advance refunding and several kinds of private-purpose issues, all of which face threats from restrictive legislative proposals currently before Congress. Both commercial banks and mutual funds have been heavy purchasers of municipal debt lately. Overall demand for tax-exempts has been sufficient to result in some decline in rates on these securities despite the massive volume.

Consumer installment credit grew at a 15 percent annual rate in August, continuing the recent pattern of somewhat slower growth than

observed earlier in the year. Commercial bank data for September and October suggest further deceleration in consumer credit, but the overall recent total likely was boosted by heavy auto finance company lending under special rate programs.

Mortgage markets continue to show robust activity, with large increases in thrift holdings of mortgage assets recorded in August, as better income and capital positions permitted faster growth under the net worth requirements. Issuance of new mortgage pass-through securities was at a record \$11.6 billion in September, about half of which were swap issues under FNMA and FHLMC programs. A shift toward FHA-insured and VA-guaranteed mortgage financing also has occurred in recent months, as lending standards on conventional loans have tightened, especially with respect to high loan-to-value mortgages.

In the absence of legislative action to raise the debt ceiling, the pace of borrowing by the Treasury has been reduced. However, with the continued large federal deficit being reflected in a rundown in Treasury cash balances, and a surge of borrowing expected as soon as a new ceiling is established, the overall market impact of reduced Treasury issuance has been minimal. Sponsored agency borrowing during the third quarter was about in line with recent experience, and the Farm Credit Banks -- which reported a large loss for the quarter -- again paid down some debt. Yield spreads on Farm Credit securities relative to Treasuries have widened a bit.

Outlook. The staff is projecting that interest rates will come under some moderate downward pressure between now and next spring, as

households cut their spending on durables and increase their savings, and as business capital spending remains sluggish.

In the very near term the federal government is likely to be the major force in the credit markets. While the combined federal deficit is projected at around \$73 billion in the fourth quarter, the markets fully anticipate this development and any attendant rate pressures should be limited and transitory. Thereafter the pace of Treasury borrowing should subside to a degree, and the growth rate of federal debt will tend to moderate.

At the same time, there should be some deceleration of credit demands by other sectors, which likely will become even more evident in the first quarter of 1986. This is especially true in the tax-exempt markets, where current staff projections show a sharp drop in the pace of such borrowing--even in the absence of prompt legislative action on new rules for the issuance of municipal securities, owing to concerns about retroactivity.

While current staff projections for corporate profits and capital expenditures suggest the need for external financing will be minimal over the next six months, the amount of borrowing associated with gross equity retirements because of mergers and buyouts will still be high. Merger and stock buy-back announcements continue unabated, and the evidence points to heavy net share retirements at least into the opening months of 1986. The interest rate outlook suggests that corporate borrowing will be concentrated in long-term markets, although some pickup in short-term borrowing may occur as inventory accumulation resumes, and balance sheet structures will be only moderately affected.

Household debt growth likely will slow a little in coming months. In particular, consumer credit should stay on the decelerating path indicated by recent data, perhaps with some caution creeping into both borrower and lender behavior in light of the strains suggested by high debt-to-income ratios and rising installment loan delinquency rates. Net mortgage borrowing by households is projected to remain brisk, however, in line with the forecasted expansion of single-family housing starts. Thrift institutions probably will maintain a stronger lending pace than they did earlier this year, but purchases of mortgage pool securities by mutual funds, unit trusts, and diversified institutional investors will remain important.

INTERNATIONAL DEVELOPMENTS

Recent developments. The trade-weighted average foreign exchange value of the dollar has declined 2-3/4 percent further on balance since the last FOMC, bringing its net depreciation to 7-1/2 percent since the G-5 announcement of September 22. The dollar fell nearly 2-1/2 percent during the first week of October, as market participants remained concerned about the prospect for central bank sales of dollars and looked to the IMF/World Bank meetings in Seoul for further announcements by G-5 officials. The dollar firmed somewhat when reports from Seoul suggested that some G-5 authorities were satisfied with the dollar's level and then subsequently traded in a narrow range despite heavy intervention sales of dollars. Toward the end of the intermeeting period, the dollar began again to weaken, declining initially against the yen when the Bank of Japan indicated that in the context of efforts to support the yen, it would not accommodate seasonal demands for liquidity as it usually does. Interest rates on yen money-market instruments and bonds rose steeply in response. The decline of the dollar broadened to include the other major currencies in association with some increases in German and U.K. interest rates and declines in U.S. interest rates.

. Since the G-5 announcement, the New York Desk has sold a total of more than \$3 billion against yen and marks, divided evenly between the System and the Treasury; almost all of this activity occurred since the last FOMC meeting.

Available banking data for the first two months of the third quarter indicate substantial capital inflows into U.S. banking offices. In addition, private foreign purchases of U.S. corporate stocks and bonds continued very strong in July and August. However, net private foreign holdings of U.S. Treasury securities did not increase during these two months, in contrast to the substantial net acquisitions recorded in each of the previous five quarters. Net foreign official holdings of Treasury securities did increase in July and August, but at a rate sharply reduced from that in the second quarter.

In August, the merchandise trade deficit (s.a.a.r.) was somewhat smaller than that recorded in July as exports increased slightly and imports declined. For the two-month period on average the deficit was substantially smaller than in the second quarter, with most of the change coming in imports. These developments need to be assessed with caution, however, as monthly data are very volatile and preliminary calculations suggest that revisions will be substantial. Nonoil import prices for July and August averaged nearly 3 percent below their level a year ago, and the price of imported oil in August was unusually, and

probably temporarily, low. Trade data for September are to be released on October 31 and will be reported in the Greenbook supplement.

Economic growth continues moderate but uneven in the major foreign industrial countries. Inflation abroad on average remains low, with some major countries experiencing further gains against inflation in the most recent data. Through September the German current account had strengthened substantially when compared with 1984 as had the Japanese current account through August.

At the IMF/World Bank meetings in Seoul Treasury Secretary Baker presented an initiative calling for mutual action, by borrowers, by international institutions, and by the banking community, where additional financing from official institutions and the banks would support, and be dependent upon, the restructuring of the economies of debtor countries. For the individual countries, although it is out of compliance with its IMF program, Mexico is expected to receive up to \$800 million in emergency assistance from the IMF, the World Bank, and the Inter-American Development Bank. Argentina was found in compliance with the end-July IMF performance tests, but some difficulties may arise with the end-September tests. Real activity has continued to expand in Brazil, but negotiations between Brazil and the IMF remain stalled. The Peruvian government has refused a routine IMF mission and has suggested the possibility that Peru will withdraw from the IMF.

Outlook:

The staff forecast for the foreign exchange value of the dollar remains unchanged from the last Greenbook. It continues to project that

the dollar in the fourth quarter will be substantially below the average in the third quarter and that during 1986 there will be a further moderate decline. The outlook for economic activity in foreign industrial countries and in the developing countries is also essentially the same as in the last Greenbook. Real growth in the foreign industrial countries is expected to be about equal, on average, to that in the United States. The developing countries, while slowing somewhat from most recent rates of expansion, are expected to experience a growth rate slightly above that of the United States. Based on recent data for merchandise trade values and, in particular, prices, the staff has reduced somewhat its projection for the current account deficit for 1985 to \$125 billion, and for 1986 to about \$130 billion.

OCTOBER 29, 1985

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

	ANNUAL			1984		1985				1986			
	1984-	1985-P	1986-P	Q3-	Q4-	Q1-	Q2-	Q3-	Q4-P	Q1-P	Q2-P	Q3-P	Q4-P
1. GNP EXPORTS AND IMPORTS 1/													
CURRENT \$, NET	-64.2	-88.6	-94.2	-90.6	-56.0	-74.5	-94.0	-89.2	-96.7	-98.7	-95.1	-95.2	-88.0
EXPORTS OF G+S	364.3	352.8	378.7	368.6	367.2	360.7	347.7	347.6	355.1	361.4	372.3	382.8	398.4
IMPORTS OF G+S	428.5	441.3	472.9	459.3	423.2	435.2	441.6	436.7	451.8	460.0	467.3	477.8	486.3
CONSTANT 72 \$, NET													
EXPORTS OF G+S	146.0	140.1	145.5	147.4	147.1	143.7	137.9	138.1	140.5	141.7	143.9	146.1	150.3
IMPORTS OF G+S	161.1	172.6	175.7	174.4	160.5	172.1	171.8	172.1	174.6	175.3	175.5	175.9	176.2
2. U.S. MERCHANDISE TRADE BALANCE 2/	-108.3	-128.8	-134.8	-130.0	-98.2	-118.1	-132.0	-128.5 ^P	-136.6	-137.9	-135.7	-135.1	-130.6
EXPORTS	220.3	215.4	232.2	222.1	225.4	222.8	213.0	211.2 ^P	214.5	219.6	227.3	235.9	246.2
AGRICULTURAL	38.4	28.6	29.4	36.9	38.3	33.5	28.3	25.5 ^P	27.2	29.0	29.3	29.5	29.8
NONAGRICULTURAL	181.9	186.7	202.8	185.3	187.2	189.4	184.6	185.7 ^P	187.3	190.6	198.0	206.4	216.4
IMPORTS	328.6	344.2	367.1	352.1	323.6	341.0	345.0	339.7 ^P	351.1	357.5	362.9	371.0	376.8
PETROLEUM AND PRODUCTS	57.5	47.7	43.7	57.8	56.8	45.2	52.8	46.1 ^P	46.7	44.4	42.8	44.2	43.5
NONPETROLEUM	271.1	296.5	323.3	294.4	266.9	295.7	292.2	293.6 ^P	304.4	313.1	320.2	326.8	333.3
3. U.S. CURRENT ACCOUNT BALANCE	-101.5	-125.2	-129.4	-130.0	-101.9	-121.3	-127.2	-121.3 ^P	-130.9	-132.8	-129.4	-129.6	-125.7
OF WHICH: NET INVESTMENT INCOME	19.1	19.8	17.6	13.0	16.0	10.2	22.4	23.3 ^P	23.4	19.9	18.5	16.5	15.7
4. FOREIGN OUTLOOK 3/													
REAL GNP--TEN INDUSTRIAL 4/	3.2	2.7	2.8	4.8	3.3	0.4	4.3	3.3 ^P	2.8	2.7	2.6	2.5	2.6
REAL GNP--NONOPEC LDC 5/	4.1	3.7	3.8	4.3	3.7	3.3	3.4	3.6 ^P	3.8	4.0	3.9	3.8	3.6
CONSUMER PRICES--TEN IND. 4/	4.9	4.4	3.8	2.6	4.8	5.4	5.7	1.5 ^P	3.9	4.3	4.3	3.4	3.6

1-23

1/ ECONOMIC ACTIVITY AND PRODUCT ACCOUNT DATA.

2/ INTERNATIONAL ACCOUNTS BASIS.

3/ PERCENT CHANGE, ANNUAL RATES.

4/ WEIGHTED BY MULTILATERAL TRADE-WEIGHTS OF G-10 COUNTRIES PLUS SWITZERLAND; PRICES ARE NOT SEASONALLY ADJUSTED.

5/ WEIGHTED BY SHARE IN NONOPEC LDC GNP.

P/ PROJECTED