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Strictly Confidential (FR) Class II FOMC

June 26, 1991

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee

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

Overview of the Staff Forecast

Evidence has accumulated in recent weeks that the recession has ended and that the economy is entering the recovery phase of the business cycle. Real GNP probably has been little changed in the second quarter, and we expect that it will rise at about a 4-1/2 percent annual rate, on average, in the second half of the year. The growth of final sales is expected to remain relatively subdued, but, as typically occurs in the early stages of an expansion, a swing in inventory investment is projected to provide considerable impetus to output growth. The swing in inventory investment from substantial liquidation to modest accumulation accounts for half of the increase projected for real GNP in the second half of 1991.

Economic activity is projected to decelerate appreciably next year. The rate of increase in real final sales is expected to change little; but with sales and production having moved into closer balance, inventory accumulation will provide a lessening boost to output. On net, real GNP is expected to increase a little less than 3 percent over the course of 1992--only moderately above the staff's estimate of the economy's longer-run growth potential.

The reasons to expect a relatively modest recovery in economic activity are numerous and familiar. Consumers already have stretched to maintain their spending in the face of recent declines in real disposable income; thus their ability to provide impetus to expansion is doubtful. Construction activity will be held down by the overhang of vacant space and by the reluctance of lenders to finance new projects. Under the limitations set by the new federal budget procedures, fiscal policy will remain restrictive, and budgetary corrections at the state and local levels will impose an additional drag on aggregate demand. The stimulus from monetary policy probably has been less marked to date than in the periods preceding other upturns, and we have not built in any further easing, in contrast to what has occurred in the initial phases of some other recoveries. Moreover, the dollar has strengthened further, reducing the scope for a significant lift to domestic production from the external sector in the quarters ahead.

The moderate expansion in activity--and the resultant sustained slack in labor and product markets--should contribute to a significant diminution in the trend rate of inflation. Year-over-year changes in consumer prices have remained around 5 percent to date; but month-to-month increases have been much slower of late, and inflation expectations appear to have edged down. Increased unemployment evidently is damping wage gains, and the appreciation of the dollar is restraining increases in the prices of imported goods and their domestic substitutes. All told, the staff expects that the underlying trend of price increases will move significantly below 4 percent next year.

Key Assumptions

The policy assumptions underlying this forecast are essentially the same as in the May Greenbook. With regard to monetary policy, we continue to assume that the federal funds rate will remain near 5-3/4 percent through 1992. The recent rise in bond yields seems to have reflected in large measure an adjustment of market expectations of the recovery to something closer to our forecast than previously was the case, but there remains a risk that strong economic news will produce some further upward pressure in coming months. However, in light of the underlying degree of restraint on aggregate demand from the sources described above, any significant movement in that direction appears unlikely to be sustained for long. Indeed, we have projected that bond yields in 1992 will be significantly below current levels as the expansion moderates and disinflationary trends are fully recognized. Credit availability problems are assumed to ease gradually as the expansion progresses and asset quality improves.

As in the May Greenbook, growth in M2 over 1991 is projected to be about in line with the growth of nominal GNP, with the effects of declines in short-term interest rates since the fourth quarter of 1990 about offsetting the effect of the continuing constriction in depository intermediation; this would place the aggregate just in the upper half of its range of 2-1/2 to 6-1/2 percent. The growth of M3 in 1991 is projected at around the midpoint of its 1 to 5 percent range, as it continues to be held down by modest growth in bank credit and sizable RTC activity for the year as a whole. The staff foresees M2 growing slightly more rapidly in 1992 than in 1991; with short-term interest rates flat and no longer boosting money demands, the pace of M2 growth is still somewhat below the faster growth of nominal income. M3 will likely maintain its pace of 1991 as the restructuring of the thrift industry continues.

On the fiscal side, we continue to assume that the FY1992 budget will adhere closely to the budget act (OBRA) of 1990. As a result, federal fiscal policy is expected to impose a moderate amount of restraint on aggregate demand over the next year and a half--and beyond. The staff has reduced its estimate of the unified budget deficit in FY1991 to $255 billion, largely because Desert Storm contributions from other countries have come in somewhat faster than we had anticipated and outlays for deposit insurance have been a bit lower. The speedup of Desert Storm contributions implies an upward revision to the projected deficit for FY1992; but receipts also have been raised, and the staff's FY1992 deficit projection, at $304 billion, is little changed from the May Greenbook. Excluding Desert Storm and outlays for deposit insurance, the deficit is expected to be $213 billion in FY1991 and $182 billion in FY1992.

The dollar has risen, on net, in recent weeks; while some of the increase is expected to unwind in the near term, the projected path of the dollar through next year is now about 5 percent higher, on average, than in the May forecast. We have made only minor changes to the projections for economic activity in the other G-10 countries: Output is expected to strengthen, on average, in the second half of this year after its recent weakness and to expand at a fairly brisk pace in 1992. Crude oil prices have fallen slightly since the time of the May Greenbook, resulting in an average posted price in the second quarter for West Texas Intermediate (WTI) of about $19.50 per barrel; we expect the WTI price to hold near that level through next year.

The Current Quarter

The staff still estimates that real GNP has been essentially unchanged in the second quarter, even though the incoming data on domestic production and spending have been stronger than we anticipated in the May Greenbook. The effects of that positive surprise on GNP have been largely offset in this forecast by a sharp downward revision to the expected growth of the services component of net exports. This revision is the result of a bulge in the profits earned abroad by U.S oil companies in the fourth and first quarters and the anticipated return to more normal profit levels in the second quarter. Gross domestic product (GDP) excludes such transactions and is a measure of the pace of domestic activity; our forecast shows GDP rising about 1-1/2 percent in the current quarter--up from a forecast of no change in the May Greenbook.

PROJECTIONS OF NEAR-TERM OUTPUT
(Percent change from preceding quarter; annual rate)

	1990	1991		
	Q4	Q1*	Q2	Q3
Real GNP	-1.6	-2.8	.2	4.8
(May Greenbook)	-1.6	-2.8	-.2	4.1
Real GDP	-2.1	-3.0	1.6	4.7
(May Greenbook)	-2.1	-2.9	0	4.1

*The first-quarter figures on this and subsequent text tables incorporate the final NIPA estimates released today.

Recent labor market indicators point to a turnaround in the economy. In May, aggregate hours worked rebounded nearly 1 percent, reflecting both a small increase in private employment--the first in nearly a year--and a lengthening in the average workweek. Moreover, after smoothing through the gyrations in the latest monthly figures, the unemployment rate has been essentially flat since March. Data on unemployment insurance and other information suggest a continuation of the firmer labor market conditions in June.

As in the May Greenbook, the pickup in motor vehicle production from its first-quarter low is expected to have added about 1 percentage point to second-quarter real GNP growth. In the terms of GNP expenditure categories, some of the additional output is reflected in increased purchases of cars and trucks, but it shows up mainly as a smaller decumulation of dealer inventories. In contrast, stocks in other sectors appear to have run off more rapidly than in the first quarter, and the total nonfarm inventory liquidation likely was somewhat greater than in the first quarter.

Meanwhile, domestic final purchases appear to have expanded moderately. In particular, aggregate consumer spending has turned up and is expected to have risen about 3 percent in the second quarter. Apart from the increase in sales of motor vehicles, the reports on retail sales in April and May point to a firming in outlays for other goods. In addition, services have probably posted a large rise this quarter, given the sizable gains in these outlays in March and April and the likelihood that the hot weather in May pushed spending on electricity well above its seasonal norm. Domestic spending also is expected to have been buoyed by a small increase in expenditures on residential structures, after an extended period of steep declines; the effects of the uptrend in starts and sales of single-family homes are anticipated to have more than offset the continued weakness in the multifamily area.

Business fixed investment is likely to have fallen a bit further this quarter. For equipment spending, nominal shipments of office and computing equipment have declined, on net, in recent months; nonetheless, given the price cuts announced by the major manufacturers, outlays probably rose in real terms. Meanwhile, spending for industrial and other equipment has remained weak. In the nonresidential structures sector, construction put-in-place reportedly recorded a big gain in April; however, in light of the weak trends in contracts and permits, we have built in sizable declines over the balance of the quarter.

Real net exports of goods and services probably have declined appreciably in the second quarter, reflecting the aforementioned movement in the service accounts. Fragmentary data suggest that net exports of goods are likely to have been little changed.

As for inflation, price increases in recent months have been small, and for the second quarter as a whole, we expect that the CPI will have risen only about 2-1/4 percent at an annual rate. With prices advancing considerably less rapidly than wages, real disposable income is expected to have turned up--the first quarterly increase since the second quarter of last year.

The Outlook

Real GNP growth is projected to approach 5 percent at an annual rate in the third quarter. To be sure, there is only limited evidence at this stage that so sizable a step-up in production is in train. Perhaps most promising is the increase in durable goods orders over April and May; this development is consistent with our assessment that inventory positions are lean enough to encourage firms to begin bringing production into closer alignment with sales. Indeed, we anticipate that the pace of liquidation will slow markedly this summer and that firms will begin to rebuild stocks before year-end.

PROJECTIONS OF REAL GNP AND FINAL SALES
(Percent change from end of preceding comparable period; annual rate)

	1991				1992	
	Q1	Q2	Q3	Q4	H1	H2
Real GNP	-2.8	.2	4.8	4.1	3.0	2.5
Final sales	-2.9	.9	2.7	1.7	2.2	2.6

In the motor vehicles sector, where stocks of new cars have dropped to their lowest levels in many years, automakers have scheduled a hefty increase in assemblies in the third quarter. Although experience suggests that discounting these plans somewhat is prudent, we still expect output of motor vehicles to rise enough to add 1-1/2 percentage points to real GNP growth in the third quarter. We have also built in a marked slowing in the run-off of nonauto inventories, and this contributes another 1-1/2 percentage points to real growth in the third quarter.

Real GNP growth is expected remain at 4 percent in the fourth quarter but to taper off thereafter, averaging about 2-3/4 percent for 1992 as a whole. This upturn would be rather subdued by historical standards, but its dynamics would be similar in many respects to those of other postwar expansions. Inventory liquidation ceases and is followed by a resumption of stock building; this process generates jobs and income that should support growth in household spending. Lower interest rates and continued income gains stimulate housing demand and homebuilding. Business investment strengthens in response to improving sales trends.

The forecast continues to anticipate an appreciable slowing in wage and price inflation over the next year and a half. Rising productivity should account for a good part of the increased output in the near term, and the unemployment rate is likely to fall only to the vicinity of 6-1/2 percent by the end of 1991. With real output growing only somewhat faster than its longer-run potential in 1992, the jobless rate should remain above 6-1/4 percent. As a result of this slack and further reductions in inflation expectations, increases in hourly compensation are expected to slow steadily. Consumer price inflation is anticipated to hover around 4 percent in the second half of 1991 and to slow over the course of 1992, to about 3-1/2 percent in the second half.

PROJECTIONS OF INFLATION
(Percent change from end of preceding comparable period; annual rate)

	1991				1992	
	Q1	Q2	Q3	Q4	H1	H2
Consumer price index	3.6	2.2	4.0	3.8	3.9	3.5
CPI ex. food and energy	6.8	3.2	4.1	4.1	4.0	3.5
ECI hourly compensation	4.6	4.2	3.9	3.8	3.7	3.6
Civilian unemployment rate (percent)	6.5	6.8	6.8	6.6	6.4*	6.3*

*Final quarter of period.

Consumer spending and income. Real consumer expenditures are expected to rise less than 2-1/2 percent at an annual rate in the second half of 1991 and to pick up only a little next year. The projection of a mild increase in consumption largely reflects our assumption that growth in real disposable income will be quite moderate. The saving rate has fallen since mid-1990, and, even if it were to be revised upward at some point--as has happened frequently in the past--it probably would still be low by historical standards. Barring a sharp rise in household wealth--not anticipated in this forecast--a significant decline in the saving rate seems unlikely.

Among the components of PCE, purchases of cars and light trucks are expected to increase somewhat further over the next several quarters. In general, however, we do not expect the surge in outlays for durables that occurred in some of the previous cyclical upturns; this expectation seems reasonable in light of our income forecast and of the very high level of durables outlays during much of the 1980s, but it may constitute something of an upside risk to the forecast.

Business fixed investment. Real BFI is expected to rise moderately over the the second half of 1991. Spending on equipment is expected to be paced by relatively robust real outlays for computers and by increased business purchases of motor vehicles. Also, given the recent firming in orders for industrial and other equipment, actual outlays are expected to improve by late 1991. Construction activity, meanwhile, is anticipated to stay weak.

In 1992, we project real BFI to increase about 6 percent. Equipment outlays are expected to rise 8-1/2 percent, as the continued expansion of aggregate output and improved cash flow prompt a broad advance in spending. Meanwhile, the decline in structures investment is expected to slow somewhat over the course of the year. Although a number of major industries are facing serious excess capacity, rising activity and capacity utilization likely will stimulate additional plant construction in some sectors. Furthermore, contracts for nonoffice commercial space have already shown signs of firming, and absorption in some locales may be sufficient by next year to stem the decline in this sector. Construction of office buildings and hotels, however, is likely to remain depressed because of continued high vacancy rates, low rents, and reluctant lenders (many of whom have become reluctant owners recently).

Housing. The projection for housing remains relatively lackluster, with starts expected to increase only to about 1.2 million units by the end of 1992--the same as the figure for 1990 as a whole. Virtually all of the improvement is in the single-family sector. Demand for new homes is expected to respond gradually to rising employment and incomes and, in 1992, to declining mortgage interest rates. In addition, declines in house prices over the past couple of years have made homes much more affordable in some locales; the perception that prices are weak would, of course, make houses an unattractive investment, but the staff is expecting that the recent indications of a bottoming out in prices are presaging a period of moderate price increases. The outlook for multifamily construction remains poor: The surplus of unoccupied units should diminish somewhat over the projection period, but vacancy rates will remain high by historical standards, in part because of the relatively slow growth in the population of young adults. Also, lenders are expected to remain cautious in funding new projects.

Government sector. Federal spending on goods and services is expected to trend downward at an appreciable pace after the second quarter. The Gulf war temporarily boosted defense purchases, but the cutbacks in appropriations over the past few years and the planned force reductions point to a sizable decline in procurement and personnel outlays from here on. Nondefense purchases are expected to rise faster than GNP because of increases in spending on space exploration, law enforcement, and health research. Overall, however, real purchases are projected to fall at a 4 percent annual rate between mid-1991 and the end of 1992.

State and local governments also are taking actions to cope with budgetary problems stemming from structural imbalances as well as temporary difficulties brought on by the recession. In our forecast, real purchases of goods and services are held essentially flat over the next couple of quarters and post only a small increase next year, despite continued strong pressures for increases in public services and for infrastructure improvements; this trajectory for purchases would be unusually weak for a cyclical upturn. Also, many governments are raising taxes, and we have built in some further increases in income and sales taxes next year. These actions, in combination with the recovery in business activity, are expected to bring the sector's budget--as measured by the NIPA operating and capital accounts (excluding social insurance)--into balance by late 1992.

Net exports. The external sector now is expected to impart a small damping influence on the economic expansion over the next six quarters. Nonagricultural merchandise exports are expected to be fairly robust over this period, given the pickup in activity abroad. However, non-oil merchandise imports, which probably have fallen, on net, over the first half of 1991, are expected to more than retrace these declines during the second half of this year and to continue to rise briskly in 1992 as the U.S. business expansion takes hold and import price increases remain small. A more detailed discussion of these projections is presented in the International Developments section.

Labor costs and prices. Hourly compensation (as measured by the employment cost index) has decelerated noticeably to a 4-1/4 percent annual rate in recent quarters and is expected to edge below 4 percent in the second half of 1991. In 1992, with hiring more widespread and unemployment drifting down, the downward pressure on wages from labor market slack is expected to diminish a bit. With inflation expectations declining, the ECI is still anticipated to slow appreciably further--to just over 3-1/2 percent in the second half.

Consumer price inflation is expected to slow significantly over the forecast period. Food prices are projected to rise at about the overall rate of inflation, barring major demand or supply shocks, and retail energy prices are expected to rise only about 3 percent per year. Excluding food and energy, CPI inflation is forecast to run about 4 percent over the rest of 1991 and to move down to 3-1/2 percent in the second half of 1992. This improvement in underlying price performance reflects the lingering slack in the labor market and in industrial capacity utilization, as well as continued intense competition from foreign producers. Pressures on prices are also expected to be damped to some extent by above-trend growth in labor productivity. Output per hour is expected to rise at more than a 3 percent rate, on average, in the second half of 1991. And although productivity gains are expected to slow in 1992, the trend in unit labor costs should continue to improve, so that firms can raise their profit margins with only moderate increases in prices.

A Note on the Forecast in 1987 Prices

As discussed in Part II of the Greenbook, the Commerce Department will shift the GNP data to a 1987 basis when it releases the benchmark revisions to the National Income and Product Accounts next fall. Current BEA estimates indicate a slightly larger drop in real GNP, on net, over the fourth quarter of 1990 and the first quarter of 1991, measured in 1987 prices. The implications for the seven quarters of the forecast, however, appear to be small because growth is expected to be relatively well-balanced across sectors. Thus, although revisions could complicate the picture, the rebasing of the data should not itself significantly distort comparisons of the Committee's July Humphrey-Hawkins projections with the actual outcome to be discussed next February.

Details of the staff projection are shown on the green sheets, pages I-15 to I-21. The 1991:Q1 figures shown on these tables do not incorporate the revised NIPA data released today. To assist the Committee's Humphrey-Hawkins discussions, the table below shows four-quarter projections that incorporate today's NIPA data. For the most part, the effects of the revisions are microscopic and disappear in rounding.

GNP AND RELATED ITEMS
(Percent change; fourth quarter to fourth quarter)

	1991	1992
Nominal GNP	5.3	6.1
Real GNP (1982 dollars)	1.5	2.8
Real GNP (1987 dollars)	1.6	2.7
Implicit deflator (1982 dollars)	3.7	3.2
Fixed weight GNP price index (1982 dollars)	3.9	3.5

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STAFF GNP PROJECTIONS

Percent changes, annual rate

		Nominal GNP		Real GNP		GNP fixed-weight price index		Consumer Price Index <1>		Unemployment rate (percent)	
		5/8/91	6/26/91	5/8/91	6/26/91	5/8/91	6/26/91	5/8/91	6/26/91	5/8/91	6/26/91
Annual changes:											
1988	<2>	7.9	7.9	4.5	4.5	4.2	4.2	4.1	4.1	5.5	5.5
1989	<2>	6.7	6.7	2.5	2.5	4.5	4.5	4.8	4.8	5.3	5.3
1990	<2>	5.1	5.1	1.0	1.0	4.6	4.6	5.4	5.4	5.5	5.5
1991		3.7	3.9	-.1	.1	4.2	4.2	4.5	4.4	6.7	6.7
1992		6.4	6.6	3.2	3.2	3.4	3.6	3.5	3.7	6.3	6.4
Quarterly changes:											
1989	Q1 <2>	7.5	7.5	3.6	3.6	4.9	4.9	5.1	5.1	5.2	5.2
	Q2 <2>	5.8	5.8	1.6	1.6	4.6	4.6	6.0	6.0	5.3	5.3
	Q3 <2>	5.1	5.1	1.7	1.7	3.1	3.1	3.3	3.3	5.3	5.3
	Q4 <2>	3.9	3.9	.3	.3	3.8	3.8	3.9	3.9	5.3	5.3
90	Q1 <2>	6.7	6.7	1.7	1.7	6.6	6.6	7.5	7.5	5.3	5.3
	Q2 <2>	5.1	5.1	.4	.4	3.9	3.9	3.8	3.8	5.3	5.3
	Q3 <2>	5.3	5.3	1.4	1.4	4.2	4.2	7.0	7.0	5.6	5.6
	Q4 <2>	.9	.9	-1.6	-1.6	4.7	4.7	6.9	6.9	5.9	5.9
1991	Q1 <2>	2.6	2.5	-2.8	-2.6	5.1	5.1	3.6	3.6	6.5	6.5
	Q2	3.0	3.3	-.2	.2	3.1	3.1	2.7	2.2	6.8	6.8
	Q3	7.5	8.1	4.1	4.8	3.5	3.6	4.0	4.0	6.8	6.8
	Q4	7.4	7.6	4.0	4.1	3.5	3.5	3.6	3.8	6.6	6.6
1992	Q1	7.2	7.3	3.5	3.3	4.0	4.1	3.8	4.1	6.4	6.5
	Q2	6.0	6.0	3.1	2.7	3.3	3.5	3.5	3.6	6.3	6.4
	Q3	5.4	5.6	2.8	2.6	3.0	3.3	3.1	3.5	6.3	6.4
	Q4	5.1	5.5	2.6	2.5	2.9	3.3	3.1	3.5	6.2	6.3
Two-quarter changes: <3>											
1989	Q2 <2>	6.7	6.7	2.6	2.6	4.7	4.7	5.6	5.6	.0	.0
	Q4 <2>	4.5	4.5	1.0	1.0	3.4	3.4	3.6	3.6	.0	.0
1990	Q2 <2>	5.9	5.9	1.1	1.1	5.3	5.3	5.6	5.6	.0	.0
	Q4 <2>	3.1	3.1	-.1	-.1	4.4	4.4	6.9	6.9	.6	.6
1991	Q2	2.8	2.9	-1.5	-1.2	4.2	4.2	3.1	2.9	.9	.9
	Q4	7.4	7.8	4.0	4.4	3.5	3.5	3.8	3.9	-.2	-.2
1992	Q2	6.6	6.6	3.3	3.0	3.6	3.8	3.7	3.8	-.3	-.2
	Q4	5.3	5.6	2.7	2.5	3.0	3.3	3.1	3.5	-.1	-.1
Four-quarter changes: <4>											
1988	Q4 <2>	7.8	7.8	3.5	3.5	4.6	4.6	4.3	4.3	-.5	-.5
1989	Q4 <2>	5.6	5.6	1.8	1.8	4.0	4.0	4.6	4.6	.0	.0
1990	Q4 <2>	4.5	4.5	.5	.5	4.8	4.8	6.3	6.3	.6	.6
91	Q4	5.1	5.3	1.2	1.6	3.8	3.9	3.5	3.4	.7	.7
2	Q4	5.9	6.1	3.0	2.8	3.3	3.5	3.4	3.7	-.4	-.3

<1> For all urban consumers.
<2> Actual.
<3> Percent change from two quarters earlier.
<4> Percent change from four quarters earlier.

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GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Seasonally adjusted; annual rate)

	Units	1984	1985	1986	1987	1988	1989	1990	Projection 1991	Projection 1992
EXPENDITURES										
Nominal GNP	Billions of $	3772.2	4014.9	4231.6	4515.6	4873.7	5200.8	5465.1	5677.0	6052.4
Real GNP	Billions of 82$	3501.4	3618.7	3717.9	3845.3	4016.9	4117.7	4157.3	4163.1	4296.0
Real GNP	Percent change*	5.1	3.6	1.9	5.0	3.5	1.8	.5	1.6	2.8
Gross domestic purchases		6.4	4.3	2.1	4.2	2.6	1.1	-.5	1.5	3.0
Final sales		4.7	4.6	2.7	3.1	4.5	1.7	1.6	.6	2.4
Private dom. final purchases		5.6	4.6	2.9	2.5	4.0	1.2	-.1	.7	3.5
Personal consumption expend.		4.1	4.6	3.8	2.3	4.1	1.2	.1	1.7	2.8
Durables		10.8	7.0	11.5	-1.2	9.3	-1.4	-1.8	.9	4.1
Nondurables		2.3	3.3	2.9	1.3	2.4	.6	-2.4	.2	2.0
Services		3.5	5.0	2.1	4.1	3.7	2.4	2.5	2.9	2.8
Business fixed investment		13.8	3.7	-5.5	6.1	5.3	4.5	2.2	-3.7	5.9
Producers' durable equipment		14.9	4.6	.4	8.2	8.2	5.4	4.6	-2.7	8.6
Nonresidential structures		11.8	1.9	-17.7	.8	-2.7	1.7	-5.4	-7.2	-4.0
Residential structures		6.1	5.8	11.6	-2.2	-.1	-7.1	-10.2	-.8	8.8
Exports		5.9	-2.4	10.6	19.8	14.0	10.1	5.8	2.7	6.0
Imports		17.4	4.5	10.0	10.4	5.5	4.5	-.5	1.9	7.6
Government purchases		7.9	8.6	3.1	2.0	1.1	.3	3.8	-.5	-1.0
Federal		13.0	13.3	.5	1.5	-1.6	-2.8	5.2	-.7	-4.5
Defense		6.5	7.1	6.0	4.0	-1.8	-2.1	4.0	-2.8	-7.7
State and local		4.4	4.9	5.2	2.3	3.1	2.6	2.7	-.3	1.6
Change in business inventories	Billions of 82$	62.3	9.1	5.6	22.8	23.6	23.8	-3.6	-12.2	30.4
Nonfarm	Billions of 82$	57.8	13.4	8.0	28.7	26.5	18.7	-5.1	-14.3	28.1
Net exports	Billions of 82$	-84.0	-104.3	-129.7	-118.5	-75.9	-54.1	-33.8	-1.2	-10.7
Nominal GNP	Percent change*	8.6	6.6	4.6	8.2	7.8	5.6	4.5	5.3	6.1
EMPLOYMENT AND PRODUCTION										
Nonfarm payroll employment	Millions	94.5	97.5	99.5	102.2	105.5	108.4	110.3	109.2	110.9
Unemployment rate	Percent	7.5	7.2	7.0	6.2	5.5	5.3	5.5	6.7	6.4
Industrial production index	Percent change*	4.7	1.9	1.4	6.5	4.5	1.1	.3	.6	4.3
Capacity utilization rate-mfg.	Percent	80.4	79.5	79.0	81.4	83.9	83.9	82.3	78.1	79.3
Housing starts	Millions	1.77	1.74	1.81	1.62	1.49	1.38	1.19	1.01	1.15
Auto sales	Millions	10.35	11.03	11.44	10.23	10.65	9.89	9.53	8.69	9.43
Domestic	Millions	7.92	8.22	8.22	7.06	7.55	7.06	6.92	6.31	6.85
Foreign	Millions	2.43	2.82	3.22	3.18	3.10	2.83	2.61	2.38	2.58
INCOME AND SAVING										
Nominal personal income	Percent change*	8.4	6.6	5.8	8.1	7.6	6.8	5.6	4.6	6.8
Real disposable income	Percent change*	4.3	2.7	3.3	2.7	4.3	1.7	-.4	1.2	2.8
Personal saving rate	Percent	6.1	4.4	4.1	2.9	4.2	4.6	4.6	3.9	4.0
Corp. profits with IVA & CCAdj	Percent change*	7.4	9.2	-5.6	17.4	8.2	-16.8	-.7	16.4	4.1
Profit share of GNP	Percent	7.1	7.0	6.7	6.8	6.9	6.0	5.5	5.4	5.7
Federal govt. surplus/deficit	Billions of $	-169.6	-196.9	-206.9	-158.2	-141.7	-134.3	-166.0	-144.5	-149.7
State and local govt. surplus		64.6	65.1	62.8	51.0	46.5	46.4	35.4	41.0	70.0
Exc. social insurance funds		19.8	13.8	5.6	-8.3	-16.4	-19.9	-34.0	-31.5	-6.1
PRICES AND COSTS										
GNP implicit deflator	Percent change*	3.4	2.9	2.6	3.0	4.1	3.7	4.0	3.7	3.2
GNP fixed-weight price index		3.7	3.3	2.6	3.8	4.6	4.0	4.8	3.9	3.5
Cons. & fixed invest. prices		3.3	3.4	2.5	4.5	4.3	4.3	5.3	3.2	3.4
CPI		4.2	3.5	1.3	4.5	4.3	4.6	6.3	3.4	3.7
Exc. food and energy		5.0	4.3	3.9	4.3	4.5	4.3	5.3	4.6	3.7
ECI hourly compensation		4.9	3.9	3.2	3.3	4.8	4.8	4.6	4.1	3.7
Nonfarm business sector										
Output per hour		1.5	1.6	1.3	2.3	1.8	-1.6	-.3	2.6	1.6
Compensation per hour		4.1	4.6	4.9	3.7	4.2	2.2	4.4	4.2	3.8
Unit labor costs		2.6	3.0	3.6	1.4	2.3	3.9	4.7	1.5	2.2

* Percent changes are from fourth quarter to fourth quarter.

June 26, 1991

CONFIDENTIAL - FR
CLASS II FOMC

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Seasonally adjusted; annual rate)

	Units	1988				1989				1990	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
EXPENDITURES											
Nominal GNP	Billions of $	4735.8	4831.4	4917.9	5009.8	5101.3	5174.0	5238.6	5289.3	5375.4	5443.3
Real GNP	Billions of 82$	3970.2	4005.8	4032.1	4059.3	4095.7	4112.2	4129.7	4133.2	4150.6	4155.1
Real GNP	Percent Change	5.1	3.6	2.7	2.7	3.6	1.6	1.7	.3	1.7	.4
Gross domestic purchases		1.6	3.0	3.2	2.4	1.2	1.8	2.8	-1.2	.5	1.3
Final sales		7.1	5.1	1.1	4.6	2.4	1.7	1.8	.9	3.8	-.7
Private dom. final purchases		6.7	4.8	3.0	1.7	.8	1.4	4.1	-1.5	2.4	-1.2
Personal consumption expend.		6.9	2.7	3.5	3.5	-.3	1.3	4.6	-.8	1.1	.2
Durables		21.8	3.7	-1.1	14.1	-6.0	5.6	9.6	-13.0	14.4	-9.5
Nondurables		2.6	2.0	4.1	1.2	.6	-1.7	3.9	-.2	-3.2	-1.9
Services		5.6	2.9	4.5	1.9	.9	2.1	3.5	3.1	.1	5.1
Business fixed investment		11.4	15.7	1.6	-6.3	8.9	6.9	6.3	-3.8	5.0	-4.7
Producers' durable equipment		20.3	17.9	2.2	-5.5	9.5	12.2	6.1	-5.2	5.7	-3.3
Nonresidential structures		-10.5	9.9	-.3	-8.7	7.5	-8.2	7.1	1.3	2.3	-9.0
Residential structures		-6.8	6.8	.4	-.4	-3.6	-11.3	-7.6	-5.5	15.1	-11.2
Exports		31.7	4.4	5.4	16.7	15.8	12.4	-.5	13.5	11.2	-5.0
Imports		.5	.3	9.2	12.4	-2.3	12.8	6.4	1.7	2.5	.7
Government purchases		-9.2	3.3	-3.8	15.7	-3.3	4.0	-2.4	3.0	2.9	6.2
Federal		-24.1	3.5	-10.4	33.6	-9.1	7.0	-7.9	-.4	.4	16.4
Defense		-5.6	-1.4	-5.0	4.9	-10.9	3.2	7.2	-7.0	-1.7	3.3
State and local		3.9	3.2	1.2	4.3	1.3	1.8	1.8	5.6	4.8	-.6
Change in business inventories	Billions of 82$	31.0	16.9	32.6	14.0	26.1	25.5	24.6	18.9	-2.2	9.5
Nonfarm	Billions of 82$	28.8	19.2	31.0	27.2	16.4	21.5	21.7	15.3	-8.2	11.6
Net exports	Billions of 82$	-77.3	-72.2	-78.5	-75.7	-51.1	-53.3	-64.1	-47.9	-35.4	-44.6
Nominal GNP	Percent change	7.8	8.3	7.4	7.7	7.5	5.8	5.1	3.9	6.7	5.1
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	104.3	105.1	105.9	106.8	107.6	108.1	108.5	109.0	109.7	110.2
Unemployment rate	Percent*	5.7	5.5	5.5	5.3	5.2	5.3	5.3	5.3	5.3	5.3
Industrial production index	Percent change	5.0	4.2	5.9	2.8	2.7	2.8	-1.2	.2	.6	4.2
Capacity utilization rate-mfg.	Percent*	83.1	83.6	84.3	84.6	84.7	84.5	83.7	82.9	82.7	82.8
Housing starts	Millions	1.43	1.49	1.48	1.55	1.46	1.36	1.35	1.35	1.43	1.20
Auto sales	Millions	10.91	10.67	10.15	10.88	10.03	10.26	10.20	9.09	10.01	9.53
Domestic	Millions	7.60	7.50	7.20	7.89	7.08	7.26	7.36	6.56	7.11	6.78
Foreign	Millions	3.30	3.17	2.95	2.99	2.95	3.00	2.84	2.53	2.90	2.75
INCOME AND SAVING											
Nominal personal income	Percent change	6.4	8.6	8.1	7.4	11.6	5.8	3.7	6.2	8.6	5.3
Real disposable income	Percent change	7.3	2.7	4.9	2.3	4.2	-1.2	2.7	1.2	2.5	.3
Personal saving rate	Percent*	4.0	4.1	4.5	4.1	5.2	4.6	4.1	4.6	4.9	5.0
Corp. profits with IVA & CCAdj	Percent change	9.5	6.6	-1.7	19.5	-23.2	-7.0	-17.1	-19.1	8.4	13.9
Profit share of GNP	Percent*	7.0	7.0	6.8	7.0	6.4	6.2	5.9	5.5	5.5	5.6
Federal govt. surplus/deficit	Billions of $	-153.7	-136.9	-120.1	-156.3	-132.6	-122.7	-131.7	-150.1	-168.3	-166.0
State and local govt. surplus		45.5	48.3	46.8	45.2	48.9	50.3	48.1	38.5	38.1	38.6
Exc. social insurance funds		-15.6	-14.1	-17.0	-19.0	-16.2	-15.6	-18.7	-29.1	-30.2	-30.4
PRICES AND COSTS											
GNP implicit deflator	Percent change	2.7	4.4	4.7	4.7	3.9	3.9	3.2	3.8	4.8	4.7
GNP fixed-weight price index		3.9	4.7	5.5	4.4	4.9	4.6	3.1	3.8	6.6	3.9
Cons. & fixed invest. prices		2.9	4.9	4.5	5.0	5.0	5.3	2.3	4.6	6.8	2.6
CPI		3.2	4.5	5.2	4.4	5.1	6.0	3.3	3.9	7.5	3.8
Exc. food and energy		4.1	4.7	4.6	4.6	4.9	4.2	3.8	4.7	5.9	4.9
ECI hourly compensation**		5.2	5.2	3.8	5.1	4.2	4.9	5.3	4.4	5.6	5.1
Nonfarm business sector											
Output per hour		4.7	-.5	2.8	.2	-2.7	-.3	-1.0	-2.5	-1.3	.3
Compensation per hour		2.4	5.1	5.3	3.8	3.3	1.7	1.6	2.3	3.9	5.0
Unit labor costs		-2.2	5.7	2.5	3.6	6.1	2.0	2.6	5.0	5.3	4.7

* Not at an annual rate.
** Private industry workers

June 26, 1991

CONFIDENTIAL - FR
CLASS II FOMC

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Seasonally adjusted; annual rate)

					Projection						
		1990		1991				1992			
	Units	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
EXPENDITURES											
Nominal GNP	Billions of $	5514.6	5527.3	5561.7	5606.6	5717.2	5822.3	5925.1	6011.9	6095.1	6177.6
Real GNP	Billions of 82$	4170.0	4153.4	4126.5	4128.9	4177.3	4219.7	4254.0	4282.9	4310.4	4336.9
Real GNP	Percent Change	1.4	-1.6	-2.6	.2	4.8	4.1	3.3	2.7	2.6	2.5
Gross domestic purchases		1.6	-5.1	-4.0	1.6	4.1	4.4	3.6	3.1	2.6	2.8
Final sales		1.9	1.4	-2.8	.9	2.7	1.7	2.1	2.3	2.7	2.4
Private dom. final purchases		2.3	-3.8	-4.9	2.4	2.6	2.9	3.4	3.5	3.6	3.5
Personal consumption expend.		2.7	-3.4	-1.3	3.3	2.2	2.5	3.0	2.8	2.7	2.7
Durables		2.6	-12.3	-13.1	7.8	5.2	5.1	6.6	3.5	3.4	3.1
Nondurables		2.3	-6.5	-1.9	.3	1.2	1.2	1.8	2.2	2.1	2.1
Services		3.0	1.8	3.0	4.1	2.0	2.5	2.7	2.9	2.9	2.9
Business fixed investment		8.9	.1	-15.9	-2.8	1.5	3.5	4.4	5.9	6.5	6.8
Producers' durable equipment		10.2	6.3	-18.2	-1.8	4.6	6.5	7.6	8.8	9.0	9.0
Nonresidential structures		5.1	-18.2	-8.0	-6.1	-8.3	-6.5	-6.6	-4.7	-3.0	-1.9
Residential structures		-19.8	-20.6	-24.1	3.9	12.1	9.5	8.2	9.1	9.5	8.3
Exports		6.9	11.0	-2.6	-.9	6.4	8.3	6.4	6.1	5.8	5.9
Imports		7.6	-11.8	-11.3	8.0	1.9	10.5	8.6	8.2	5.9	7.6
Government purchases		1.2	4.7	-1.5	1.5	-.4	-1.4	-1.4	-1.1	-.9	-.7
Federal		.1	4.6	-1.3	4.1	-.8	-4.6	-4.7	-4.6	-4.4	-4.5
Defense		2.7	12.1	1.7	-1.3	-3.7	-7.5	-7.8	-7.7	-7.5	-7.7
State and local		2.0	4.9	-1.7	-.4	-.1	.9	1.1	1.5	1.7	2.0
Change in business inventories	Billions of 82$	4.7	-26.4	-23.7	-30.5	-9.5	14.8	26.9	31.8	31.0	31.7
Nonfarm	Billions of 82$	4.7	-28.5	-26.8	-32.6	-10.6	12.9	24.6	29.5	28.7	29.4
exports	Billions of 82$	-46.5	-8.8	6.4	-7.3	-.3	-3.6	-7.1	-10.6	-10.9	-14.1
inal GNP	Percent change	5.3	.9	2.5	3.3	8.1	7.6	7.3	6.0	5.6	5.5
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	110.2	109.8	109.2	108.8	109.1	109.7	110.2	110.7	111.1	111.5
Unemployment rate	Percent*	5.6	5.9	6.5	6.8	6.8	6.6	6.5	6.4	6.4	6.3
Industrial production index	Percent change	3.9	-7.0	-9.6	.0	7.2	5.7	5.1	4.8	3.8	3.7
Capacity utilization rate-mfg.	Percent*	82.9	80.8	78.0	77.4	78.2	78.7	79.0	79.3	79.4	79.5
Housing starts	Millions	1.13	1.04	.92	.99	1.05	1.07	1.11	1.13	1.16	1.19
Auto sales	Millions	9.68	8.93	8.25	8.43	8.96	9.15	9.35	9.40	9.45	9.50
Domestic	Millions	7.21	6.59	6.00	6.06	6.55	6.65	6.80	6.83	6.86	6.90
Foreign	Millions	2.47	2.34	2.25	2.37	2.41	2.50	2.55	2.57	2.59	2.60
INCOME AND SAVING											
Nominal personal income	Percent change	5.0	3.5	1.6	4.2	5.4	7.3	8.4	6.3	6.2	6.5
Real disposable income	Percent change	-.7	-3.5	-1.8	2.2	1.3	3.2	3.9	2.4	2.4	2.6
Personal saving rate	Percent*	4.2	4.2	4.1	3.9	3.7	3.9	4.1	4.0	4.0	4.0
Corp. profits with IVA & CCAdj	Percent change	-7.5	-14.8	-1.2	-5.2	58.7	23.6	12.3	.2	-1.3	5.8
Profit share of GNP	Percent*	5.5	5.2	5.2	5.1	5.6	5.8	5.8	5.8	5.7	5.7
Federal govt. surplus/deficit	Billions of $	-145.7	-184.3	-118.0	-150.1	-143.3	-166.4	-164.0	-152.6	-141.1	-140.9
State and local govt. surplus		39.3	25.7	30.4	34.3	44.9	54.3	62.0	67.6	72.8	77.6
Exc. social insurance funds		-30.5	-44.8	-40.7	-37.7	-28.0	-19.5	-12.7	-8.0	-3.7	.2
PRICES AND COSTS											
GNP implicit deflator	Percent change	3.7	2.8	5.2	3.0	3.2	3.3	3.8	3.2	3.0	3.0
GNP fixed-weight price index		4.2	4.7	5.1	3.1	3.6	3.5	4.1	3.5	3.3	3.3
Cons. & fixed invest. prices		5.4	6.4	3.1	2.6	3.8	3.5	3.5	3.4	3.3	3.3
CPI		7.0	6.9	3.6	2.2	4.0	3.8	4.1	3.6	3.5	3.5
Exc. food and energy		6.1	4.2	6.8	3.2	4.1	4.1	4.3	3.7	3.5	3.5
ECI hourly compensation**		4.3	3.8	4.6	4.2	3.9	3.8	3.8	3.7	3.7	3.6
n business sector											
ut per hour		.6	-.7	.3	3.5	4.4	2.3	1.8	1.6	1.5	1.4
ompensation per hour		4.7	3.9	4.0	4.5	4.2	3.9	4.3	3.7	3.6	3.6
Unit labor costs		4.1	4.7	3.7	1.0	-.2	1.6	2.5	2.1	2.1	2.2

* Not at an annual rate.
** Private industry workers

CONFIDENTIAL - FR
CLASS II FOMC

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Net changes, billions of 1982 dollars)

	1988				1989				1990		1987	1988	1989	1990
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	(fourth quarter to fourth quarter, net change)			
Real GNP	49.5	35.6	26.3	27.2	36.4	16.5	17.5	3.5	17.4	4.5	187.1	138.6	73.9	20.2
Gross domestic purchases	15.5	30.5	32.6	24.4	11.8	18.7	28.3	-12.7	4.9	13.7	163.0	103.0	46.1	-18.9
Final sales	66.9	49.7	10.6	45.7	24.4	17.0	18.5	9.3	38.4	-7.2	117.9	172.9	69.2	65.4
Private dom. final purchases	51.8	38.3	24.4	14.2	6.5	11.4	34.1	-12.9	20.2	-10.3	78.5	128.7	39.1	-3.8
Personal consumption expend.	42.6	17.3	22.3	22.4	-2.1	8.6	30.0	-5.4	7.4	1.5	56.4	104.6	31.1	3.7
Durables	19.8	3.8	-1.1	13.9	-6.6	5.8	9.9	-15.0	14.5	-10.8	-4.9	36.4	-5.9	-7.5
Nondurables	5.7	4.4	9.1	2.7	1.4	-3.9	8.8	-.4	-7.4	-4.4	11.7	21.9	5.9	-21.8
Services	17.1	9.1	14.2	6.0	3.0	6.7	11.3	10.0	.4	16.6	49.6	46.4	31.0	32.9
Business fixed investment	12.7	17.6	2.0	-8.0	10.5	8.4	7.8	-4.9	6.2	-6.2	26.6	24.3	21.8	11.0
Producers' durable equipment	16.0	14.9	2.0	-5.2	8.4	10.9	5.7	-5.2	5.4	-3.3	25.6	27.7	19.8	17.7
Nonresidential structures	-3.4	2.9	-.1	-2.8	2.2	-2.6	2.1	.4	.7	-2.9	1.0	-3.4	2.1	-6.7
Residential structures	-3.4	3.2	.2	-.2	-1.8	-5.7	-3.7	-2.6	6.5	-5.5	-4.5	-.2	-13.8	-18.5
Change in business inventories	-17.4	-14.1	15.7	-18.6	12.1	-.6	-.9	-5.7	-21.1	11.7	69.2	-34.4	4.9	-45.3
Nonfarm	-26.6	-9.6	11.8	-3.8	-10.8	5.1	.2	-6.4	-23.5	19.8	66.3	-28.2	-11.9	-43.8
Farm	9.1	-4.5	3.9	-14.8	22.9	-5.7	-1.1	.7	2.4	-8.1	3.0	-6.3	16.8	-1.5
Net exports	34.0	5.1	-6.3	2.8	24.6	-2.2	-10.8	16.2	12.5	-9.2	24.1	35.6	27.8	39.1
Exports	34.7	5.6	7.0	21.0	20.8	17.1	-.7	19.1	16.5	-8.0	80.5	68.3	56.3	35.6
Imports	.7	.5	13.3	18.2	-3.7	19.2	10.1	2.8	4.1	1.2	56.4	32.7	28.4	-3.4
Government purchases	-18.9	6.3	-7.5	28.7	-6.7	7.8	-4.8	6.0	5.7	12.3	15.3	8.6	2.3	30.1
Federal	-23.2	2.8	-8.9	23.9	-8.1	5.7	-6.9	-.3	.3	12.9	5.3	-5.4	-9.6	17.2
Defense	-3.8	-.9	-3.3	3.1	-7.4	2.0	4.5	-4.7	-1.1	2.1	10.2	-4.9	-5.6	10.2
Nondefense	-19.4	3.7	-5.6	20.8	-.8	3.8	-11.4	4.4	1.4	10.8	-4.9	-.5	-4.0	7.0
State and local	4.3	3.5	1.3	4.8	1.5	2.1	2.1	6.3	5.5	-.7	10.0	13.9	12.0	12.9

June 26, 1991

CONFIDENTIAL - FR
CLASS II FOMC

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Net changes, billions of 1982 dollars)

	1990		1991				1992				1989	1990	1991	1992
				Projection							(fourth quarter to fourth quarter, net change)		Projection	
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
Real GNP	14.9	-16.6	-26.9	2.4	48.4	42.4	34.3	28.9	27.5	26.5	73.9	20.2	66.3	117.2
Gross domestic purchases	16.8	-54.3	-42.1	16.1	41.3	45.7	37.9	32.3	27.9	29.6	46.1	-18.9	61.0	127.7
Final sales	19.7	14.5	-29.6	9.2	27.4	18.1	22.2	24.0	28.3	25.8	69.2	65.4	25.1	100.3
Private dom. final purchases	19.1	-32.8	-41.6	19.9	21.1	24.4	28.7	29.6	30.5	30.3	39.1	-3.8	23.8	119.1
Personal consumption expend.	18.0	-23.2	-8.7	21.9	14.8	16.4	20.1	18.7	18.5	18.3	31.1	3.7	44.4	75.6
Durables	2.7	-13.9	-14.3	7.6	5.3	5.1	6.7	3.7	3.6	3.3	-5.9	-7.5	3.7	17.3
Nondurables	5.2	-15.2	-4.4	.7	2.7	2.7	4.0	4.9	4.7	4.8	5.9	-21.8	1.6	18.5
Services	10.0	5.9	10.0	13.8	6.9	8.6	9.3	10.1	10.2	10.2	31.0	32.9	39.2	39.8
Business fixed investment	10.9	.1	-22.0	-3.5	1.9	4.3	5.4	7.3	8.1	8.6	21.8	11.0	-19.3	29.4
Producers' durable equipment	9.5	6.1	-19.7	-1.7	4.3	6.1	7.2	8.5	8.9	9.1	19.8	17.7	-11.0	33.7
Nonresidential structures	1.5	-6.0	-2.4	-1.8	-2.4	-1.8	-1.8	-1.3	-.8	-.5	2.1	-6.7	-8.4	-4.4
Residential structures	-9.8	-9.7	-10.9	1.5	4.5	3.7	3.2	3.6	3.9	3.5	-13.8	-18.5	-1.3	14.2
Change in business inventories	-4.8	-31.1	2.7	-6.8	21.0	24.3	12.1	4.9	-.8	.7	4.9	-45.3	41.2	16.9
Nonfarm	-6.9	-33.2	1.7	-5.8	22.0	23.5	11.7	4.9	-.8	.7	-11.9	-43.8	41.4	16.5
Farm	2.1	2.1	1.0	-1.0	-1.0	.8	.4	.0	.0	.0	16.8	-1.5	-.2	.4
Net exports	-1.9	37.7	15.2	-13.7	7.0	-3.3	-3.6	-3.4	-.3	-3.2	27.8	39.1	5.2	-10.5
Exports	10.4	16.7	-4.2	-1.4	10.1	13.1	10.3	10.1	9.7	9.9	56.3	35.6	17.6	40.1
Imports	12.3	-21.0	-19.4	12.3	3.1	16.4	13.9	13.5	10.0	13.1	28.4	-3.4	12.4	50.6
Government purchases	2.5	9.6	-3.2	3.0	-.8	-3.0	-2.9	-2.2	-1.8	-1.4	2.3	30.1	-4.0	-8.3
Federal	.1	3.9	-1.1	3.5	-.7	-4.1	-4.2	-4.0	-3.8	-3.8	-9.6	17.2	-2.4	-15.8
Defense	1.7	7.5	1.1	-.9	-2.5	-5.1	-5.2	-5.0	-4.8	-4.8	-5.6	10.2	-7.4	-19.8
Nondefense	-1.6	-3.6	-2.1	4.3	1.8	1.0	1.0	1.0	1.0	1.0	-4.0	7.0	5.0	4.0
State and local	2.4	5.7	-2.1	-.5	-.1	1.1	1.3	1.8	2.0	2.4	12.0	12.9	-1.6	7.5

FEDERAL SECTOR ACCOUNTS[1]
(Billions of dollars)

	Fiscal years				1990				1991				1992			
	1989a	1990a	1991	1992	Ia	IIa	IIIa	IVa	Ia	II	III	IV	I	II	III	IV
BUDGET									Not seasonally adjusted							
Budget receipts[2]	991	1031	1076	1169	229	319	254	249	233	319	274	261	261	355	292	283
Budget outlays[2]	1144	1252	1331	1473	310	331	312	336	299	336	361	379	364	369	362	378
Surplus/deficit(-)[2]	-153	-220	-255	-304	-80	-12	-58	-86	-66	-17	-86	-117	-104	-13	-70	-95
(On-budget)	-206	-277	-314	-372	-94	-41	-65	-96	-80	-42	-95	-130	-117	-46	-79	-108
(Off-budget)	53	57	59	67	14	29	7	10	15	26	9	12	13	33	9	13
Surplus excluding deposit insurance[3]	-131	-162	-187	-197	-74	17	-41	-72	-63	-2	-50	-89	-76	15	-47	-77
Means of financing:																
Borrowing	140	263	297	291	90	41	69	99	56	42	99	98	91	30	71	87
Cash decrease	3	1	-11	12	8	-16	-6	8	0	-13	-6	22	10	-15	-5	10
Other[4]	10	-44	-30	2	-18	-13	-6	-21	9	-12	-6	-2	3	-2	4	-2
Cash operating balance, end of period	41	40	52	40	18	35	40	32	32	45	52	30	20	35	40	30
NIPA FEDERAL SECTOR									Seasonally adjusted annual rates							
Receipts	1038	1092	1154	1258	1081	1106	1126	1127	1139	1159	1190	1218	1252	1271	1289	1311
Expenditures	1174	1249	1302	1414	1249	1272	1272	1311	1257	1309	1333	1385	1416	1424	1430	1452
Purchases	400	415	444	445	411	422	426	438	444	448	448	444	447	445	442	439
Defense	301	307	329	319	307	310	313	325	331	331	328	323	322	317	312	307
Nondefense	99	107	115	126	103	112	113	113	113	117	119	121	125	128	130	132
Other expend.	774	835	858	969	838	850	846	873	813	862	885	940	969	979	988	1013
Surplus/deficit	-136	-158	-149	-156	-168	-166	-146	-184	-118	-150	-143	-166	-164	-153	-141	-141
FISCAL INDICATORS[5]																
High-employment (HEB) surplus/deficit(-)	-149	-150	-87	-98	-166	-154	-127	-147	-55	-73	-74	-104	-105	-96	-86	-87
Change in HEB, percent of potential GNP	0	0	-1.2	.2	.3	-.2	-.5	.4	-1.6	.3	0	.5	0	-.2	-.2	0
Fiscal impetus measure (FI), percent	-3.5 *	-3.3 *	-2.8 *	-5.1 *	-2.3	1.2	-.8	1.8	-4	.6	-.5	-1.3	-2.6	-1	-1	-.9

a--actual *--calendar year

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

1. Staff projections. CBO's March deficit estimates are $309 billion in FY1991 and $294 billion in FY1992. OMB's February deficit estimates are $318 billion in FY1991 and $281 billion in FY1992.
2. Budget receipts, outlays, and surplus/deficit include social security (OASDI) receipts, outlays and surplus, respectively. The OASDI surplus is excluded from the "on-budget" deficit and shown separately as "off-budget", as classified under current law. The Postal Service deficit is included in off-budget outlays beginning in FY1990.
3. CBO's March deficit estimates, excluding deposit insurance spending, are $205 billion in FY1991 and $196 billion in FY1992. OMB's February deficit estimates, excluding deposit insurance spending, are $207 billion in FY1991 and $193 billion in FY1992.
4. Other means of financing are checks issued less checks paid, accrued items; and changes in other financial assets and liabilities.
5. HEB is the NIPA measure in current dollars with cyclically-sensitive receipts and outlays adjusted to a 6 percent unemployment rate and 2.3% potential output growth in the forecast period. Quarterly figures for change in HEB and FI are not at annual rates. Change in HEB, as a percent of nominal potential GNP, is reversed in sign. FI is the weighted difference of discretionary federal spending and tax changes (in 1982 dollars), scaled by real federal purchases. For change in HEB and FI, (-) indicates restraint.

Recent Developments

Mounting evidence of an end to the recession and the disappearance of expectations of further System easing have caused market interest rates to firm during the intermeeting period. While the federal funds rate has remained around 5-3/4 percent, Treasury and most private market rates have risen 5 to 25 basis points. At the same time, quality spreads have narrowed, as yields on investment-grade corporate bonds and asset-backed securities have risen less than those on Treasuries. Demand for such securities has been strong, with investors reaching for higher returns and apparently becoming more confident that corporate financial health will improve in a growing economy. Share prices rose to record highs in May, responding positively to signs of a business upturn, but retraced these gains in June when bond rates jumped; on balance since the May FOMC meeting, major stock indexes are little changed.

M2 growth picked up moderately in May, but appears to have waned in June. Although inflows to liquid retail deposits have been brisk, in part because their rates have lagged the decline in market yields, other components of M2, including small time deposits and shares of money market mutual funds, have been notably weak. Rather than rolling over maturing time deposits at greatly reduced rates, many households evidently have sought higher returns on assets outside M2. Continued strong inflows to bond and equity mutual funds indicate these funds have been the frequent choice. Apparently, the inflows to retail accounts have more than satisfied depositories' needs for funds to support credit expansion, and domestic institutions have continued to run off large time deposits and other managed liabilities in recent weeks. As a result, M3 was little changed in May and June.

Bank credit was unchanged in April and contracted in May owing to a drop in loans. While all loan categories were weak, the contraction in business loans was especially sharp in April and May. The decline in business loans in part may reflect tight standards by banks, but it is difficult to disentangle this effect from generally weak demands associated with declining outlays for inventories and fixed capital and with efforts by firms to strengthen balance sheets.

Total debt of nonfinancial businesses is estimated to have increased at only a 2 percent annual rate in the first quarter, and growth appears to have remained subdued in the second. The bulk of the borrowing this year has been by investment-grade firms in the bond markets; many of these companies reportedly have used proceeds to pay down commercial paper. Bond issuance was particularly heavy in April and May, and it dropped only a bit in June when bond rates backed up. Outstanding commercial paper of nonfinancial companies dropped sharply in May and, on net this year, is down about 5 percent at an annual rate. A small but growing number of lower-rated companies also have been able to issue bonds, suggesting some improvement in investor sentiment. In addition, equity markets have been receptive to new offerings, including those of new and smaller corporations. The volume of initial public offerings in May was the largest since before the market break in 1987, and the backlog of potential offerings reportedly is substantial.

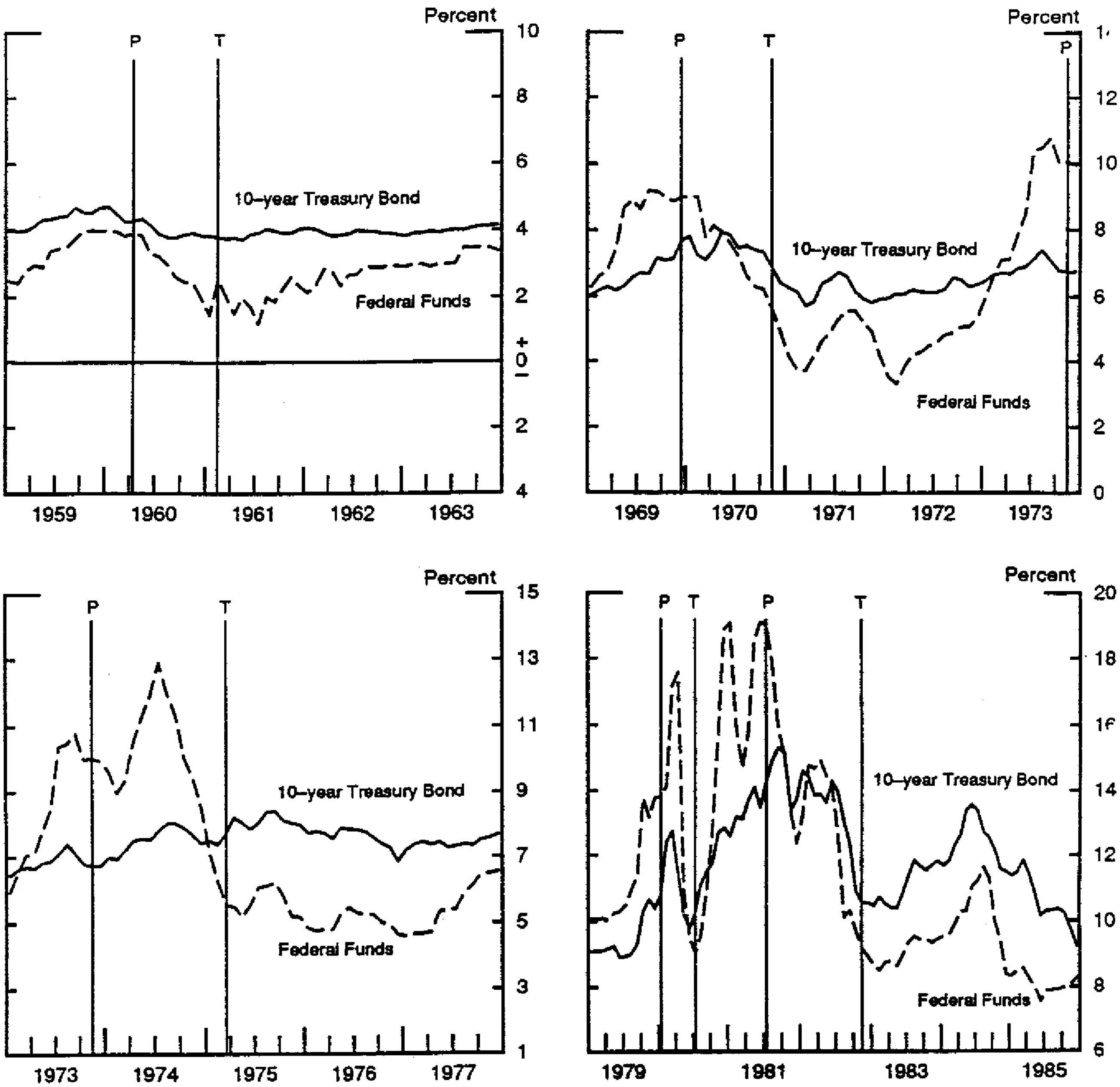
Household debt growth has shown some pickup, judging from the partial data available for the second quarter. Home mortgage borrowing appears to have increased somewhat as a result of a step-up in home sales and increased borrowing against home equity lines. Consumer installment credit increased in April after four months of decline, with the drag from falling auto loans much less than in earlier months; however, consumer loans at banks remained weak in May, even when account is taken of securitization. As in past recessions, interest rates on consumer loans have remained high in the face of falling market rates. This has helped to sustain the profitability of lending despite rising delinquency rates and loan losses. However, the competitive pressures in the credit card market have been reflected in a proliferation of nonrate enticements offered customers.

The Treasury has continued to borrow heavily in the second quarter despite a seasonally small federal deficit. Some proceeds from the debt issuance are being used to build cash balances in anticipation of large deficits in coming quarters. In tax-exempt markets, state and local governments have issued large volumes of long-term debt in recent weeks. Short-term volume also surged in June owing to note placements by New York State and Los Angeles, which needed to fund outlays in advance of tax payments. Quality spreads on municipal debt widened, but only slightly, in the wake of the bankruptcy filing by Bridgeport, Connecticut.

Outlook

The interest rate forecast associated with the staff's economic and financial projections is little changed from the May Greenbook. As before, the federal funds rate and other short-term interest rates are assumed to remain near their current levels through 1992. Although intermediate- and

INTEREST RATES IN POSTWAR CYCLES
(Monthly levels)



CHANGE IN INTEREST RATES
(Basis points)

	Trough date							
	February 1961		November 1970		March 1975		November 1982	
Period	Federal funds	10-year bond	Federal funds	10-year bond	Federal funds	10-year bond	Federal funds	10-year bond
Peak to trough	-138	-50	-337	-81	-449	100	-984	-373
Trough + 6 months	-54	26	-97	-45	70	70	-57	-17
Trough + 12 months	-17	26	-69	-103	-70	0	14	114
Trough + 18 months	39	20	-133	-71	-29	-14	112	286

long-term rates (especially on Treasuries) currently are a shade higher than projected in May, as noted earlier, we continue to anticipate that they will fall back over the next year or so.

The steepness of the term structure today indicates that the market perceives a clear risk that short-term rates will come under appreciable pressure at some point in the next couple of years--a development that certainly has its precedents in prior business upswings, including the most recent in 1983-84. But, as may be seen in the chart, there has been a good deal of variation in cyclical experience--and in some instances short and/or long rates have been lower a year or 18 months into the expansion than at the trough.

In the case of the present projection, stable short rates have been taken as the fundamental conditioning assumption, and long rates have been predicted along with other facets of the economic forecast. Several considerations have led us to project lower nominal bond yields in 1992, prominent among them being: (1) The decline in short rates during the recession was not especially large by past standards and the behavior of other policy indicators does not suggest that the economy has received the kind of monetary impulse recently that it has in some other cycles. (2) Real long-term interest rates appear still to be fairly high, especially viewed in the context of the restrictive forces stemming from the real estate and government sectors. (3) The staff forecast of wages and prices points to a likelihood that market expectations of inflation will be declining over the projection period.

Private sector borrowing is expected to increase gradually over the forecast period. On the demand side, increased spending by households and businesses will expand their credit needs. On the supply side, lenders will become more willing to extend credit as higher income flows lessen credit quality concerns; moreover, the lenders themselves will be in a better position to provide financing as they build capital and otherwise strengthen their own balance sheets. Nonetheless, debt growth of private domestic nonfinancial sectors is expected to trail that of nominal GNP by more than a percentage point this year and by three quarters of a point in 1992.

Total debt, however, is projected to rise more rapidly than GNP both this year and next, given the large borrowing requirements of the federal sector. An accelerated pace of RTC resolution activity, coupled with reduced payments by foreign governments to the Defense Cooperation Account, will add to Treasury borrowing in the second half of this year; federal debt growth should begin to moderate in 1992 as rising incomes generate higher tax receipts and RTC spending begins to decline.

In contrast to the federal government, debt growth of state and local governments is expected to remain moderate. These units continue to grapple with serious budget problems, as well as a rash of debt downgradings, and these are likely to inhibit bond-financed capital spending programs.

Borrowing by nonfinancial businesses is expected to pick up in coming months, largely because of a swing from inventory liquidation to inventory accumulation. In 1992, capital outlays, including spending on plant and equipment as well as on inventories, are expected to rise somewhat more rapidly than corporate cash flows, further adding to financing needs. The staff also anticipates a modest resumption in debt-financed merger activity in a more favorable financing environment. Overall, however, the projected acceleration in business borrowing is quite modest by historical standards, reflecting both the moderate rebound in real activity and the lingering effects of financial strains on borrower and lender behavior.

An obvious uncertainty in the outlook is the willingness and ability of banks and other intermediaries to accommodate rising credit demands. Smaller risk spreads on corporate bonds and increased IPO and junk bond issuance are signs of more positive lender attitudes in capital markets. Although we expect this trend to continue, insurance companies and other financial institutions will remain cautious in extending credit to weaker firms. Bank credit growth, in particular, is likely to be more restrained than usual in this recovery, although we anticipate some loosening of lending standards as the economy and borrower balance sheets improve; credit for real estate acquisition and development is likely to remain hard to come by, especially for speculative commercial projects, but banks are likely to become more aggressive in seeking sound business and consumer loans.

In the household sector, growth in consumer credit is expected to show a gradual rise through 1992. This sluggish pattern reflects the exceptionally subdued pace of consumer durable spending anticipated in this recovery. In addition, the distinctly lower after-tax borrowing cost associated with home equity loans for many borrowers will continue to damp the growth of consumer credit somewhat. The acceleration in home mortgage debt also is expected to be relatively restrained, in line with the unusually small rebound in single-family home building in the staff forecast. Home mortgage credit is likely to remain readily available to households, and, with continuing strong investor demand for high-quality mortgage-backed securities, spreads of mortgage rates over Treasuries should stay narrow. Mortgage pools are likely to supply a substantial share of home mortgage financing.

GROWTH RATES OF [illegible] T BY SECTOR[1]
(Period-end to period-end)

	Domestic Nonfinancial Sectors								Memo	
				Households						
	Total[2]	U.S. govt.[2]	Non-federal	Total	Home mtgs.	Cons. credit	Business	State & local govts.	Private financial assets[3]	Nominal GNP[4]
				Annual (percent)						
1982	9.3	19.4	6.9	5.4	4.5	4.4	7.8	9.1	10.3	3.1
1983	11.5	18.8	9.6	11.4	11.0	12.6	8.3	7.1	11.8	10.4
1984	14.4	16.9	13.7	12.9	11.7	18.7	15.6	7.9	13.4	8.6
1985	14.2	16.2	13.6	14.1	11.9	15.9	11.4	23.7	12.0	6.6
1986	12.3	13.4	12.0	12.8	14.9	9.6	12.0	7.6	9.1	4.6
1987	9.0	8.0	9.3	11.6	14.0	5.1	7.0	9.6	7.8	8.2
1988	9.1	8.0	9.5	10.9	12.2	7.2	8.2	8.2	8.7	7.8
1989	7.5	7.2	7.5	8.9	10.5	5.3	6.7	4.9	7.4	5.6
1990	6.5	12.0	4.9	7.3	9.1	1.8	2.9	2.3	4.4	4.5
1991	6.0	11.5	4.2	5.8	7.5	0.1	2.6	3.0	5.5	5.3
1992	6.5	9.8	5.4	6.6	7.9	2.9	4.4	3.1	4.7	6.1
				Quarterly (percent-SAAR)						
1989 -- Q1	8.2	7.0	8.6	9.2	10.6	5.1	8.4	6.6	7.5	7.5
Q2	7.2	4.6	7.9	8.0	9.7	4.9	8.3	5.4	8.0	5.8
Q3	7.2	8.0	6.9	8.7	10.2	4.8	5.6	4.6	8.4	5.1
Q4	6.4	8.3	5.9	8.5	9.6	5.7	3.8	2.6	4.6	3.9
1990 -- Q1	8.2	10.9	7.5	10.4	12.1	3.8	5.5	1.4	7.4	6.7
Q2	6.1	9.7	5.0	7.4	9.4	0.4	2.9	2.8	5.1	5.1
Q3	6.4	11.8	4.7	5.9	7.1	2.6	3.4	4.5	3.7	5.3
Q4	4.6	13.2	1.9	4.2	5.8	0.3	-0.2	0.5	1.0	0.9
1991 -- Q1	4.5	8.0	3.4	5.0	7.1	-2.9	2.0	1.1	5.8	2.5
Q2	5.2	9.2	3.9	5.7	7.3	0.4	1.8	4.2	4.4	3.3
Q3	7.1	15.2	4.4	5.9	7.4	1.1	2.9	3.3	6.0	8.1
Q4	6.5	11.8	4.8	6.0	7.5	1.7	3.7	3.2	5.3	7.6
1992 -- Q1	6.8	11.9	5.1	6.2	7.4	2.6	4.1	3.1	5.9	7.3
Q2	5.5	6.6	5.1	6.3	7.6	2.8	4.2	3.1	3.6	6.0
Q3	6.5	9.9	5.3	6.5	7.7	3.1	4.4	3.0	4.7	5.6
Q4	6.5	9.3	5.4	6.6	7.9	3.1	4.5	3.0	4.3	5.5

1. Published data through 1991:1; projections for other periods.
2. RTC activity adds roughly .6 and .7 percentage points to total debt growth in 1991 and 1992, respectively; it adds about 2.2 and 2.6 percentage points to federal debt growth in 1991 and 1992, respectively.
3. Sometimes referred to as the "Kaufman debt proxy"; includes liquid assets and credit market instruments.
4. Annual figures are Q4 to Q4.

2.6.3 FOF

FLOW OF FUNDS PROJECTION HIGHLIGHTS[1]
(Billions of dollars, seasonally adjusted annual rates)

		Calendar year				----1990----		-----------1991-----------				----1992----	
		1989	1990	1991	1992	Q3	Q4	Q1	Q2	Q3	Q4	H1	H2
	Net funds raised by domestic												
1	nonfinancial sectors	554.0	578.2	616.2	690.3	581.7	421.6	457.7	555.9	766.0	685.1	659.7	720.8
2	Net equity issuance	-124.2	-63.0	-12.5	-35.0	-74.0	-61.0	-17.0	2.0	0.0	-35.0	-35.0	-35.0
3	Net debt issuance	678.2	641.2	628.7	725.3	655.7	482.6	474.7	553.9	766.0	720.1	694.7	755.8
	Borrowing sectors												
	Nonfinancial business												
4	Financing gap[2]	33.9	37.1	13.3	71.6	50.9	33.1	-17.5	8.7	19.8	42.3	63.1	80.1
5	Net equity issuance	-124.2	-63.0	-12.5	-35.0	-74.0	-61.0	-17.0	2.0	0.0	-35.0	-35.0	-35.0
6	Credit market borrowing	211.9	99.8	92.4	157.3	119.4	-8.3	70.3	64.3	101.9	133.1	149.8	164.7
	Households												
7	Net borrowing, of which:	285.0	254.3	222.0	267.6	221.7	159.4	192.6	222.5	234.2	238.7	256.6	278.6
8	Home mortgages	221.6	214.1	200.1	226.0	183.7	150.9	189.3	197.5	204.4	209.2	217.0	235.0
9	Consumer credit	39.1	14.3	0.5	23.8	21.3	2.5	-23.6	3.0	8.7	13.8	21.8	25.8
10	Debt/DPI (percent)[3]	89.8	93.1	96.6	96.4	95.9	96.1	96.9	97.2	97.3	97.1	96.2	96.5
	State and local governments												
11	Net borrowing	29.6	14.6	19.3	20.7	28.5	3.1	7.1	27.2	22.0	20.9	20.7	20.7
12	Current surplus[4]	-25.7	-30.9	-23.3	6.8	-35.7	-36.8	-37.9	-28.4	-19.1	-7.8	2.1	11.5
	U.S. government												
13	Net borrowing from public	151.6	272.5	295.0	279.7	286.1	328.4	204.7	239.9	408.0	327.4	267.6	291.8
14	Net borrowing from public[5]	151.6	272.5	295.0	279.7	68.4	98.7	55.8	42.5	98.7	98.0	121.5	158.3
15	Unified budget deficit[5]	155.0	236.1	285.9	281.9	57.9	86.2	65.6	16.7	86.5	117.2	117.2	164.7
	Funds supplied by												
16	depository institutions	92.8	-22.1	-42.8	-19.5	-60.6	-92.8	-10.0	-81.7	-38.2	-41.3	-32.7	-6.3
	Memoranda: As percent of GNP:												
17	Dom. nonfinancial debt[3]	181.7	186.3	191.6	190.9	189.3	191.1	192.0	192.9	192.6	192.2	190.4	191.1
18	Dom. nonfinancial borrowing	13.0	11.7	11.1	12.0	11.9	8.7	8.5	9.9	13.4	12.4	11.6	12.3
19	U.S. government[6]	2.9	5.0	5.2	4.6	5.2	5.9	3.7	4.3	7.1	5.6	4.5	4.8
20	Private	10.1	6.7	5.9	7.4	6.7	2.8	4.9	5.6	6.3	6.7	7.2	7.6

1. Published data through 1991:1; projections for other periods.
2. For corporations: excess of capital expenditures over U.S. internal funds.
3. Annuals are average debt levels in the year (computed as the average of year-end debt positions) divided by annual GNP.
4. NIPA surplus, net of retirement funds.
5. Quarterly data at quarterly rates, nsa.
6. Excludes gov't-insured mortgage pool securities.

2.6.4 FOF

Recent Developments

The foreign exchange value of the dollar, in terms of the other G-10 currencies, has risen 4-1/2 per cent since the May FOMC meeting. The dollar strengthened during the period with the release of a range of statistical reports indicating an upturn in U.S. economic activity. Around the time of the G-7 meeting on June 23, the dollar declined slightly on perceptions that authorities might act to limit the rise in the dollar. The dollar has risen strongly against the mark and other European currencies over the intermeeting period, but has remained little changed against the yen on balance. This differential performance can be explained in part by perceived differences in the actual and prospective stances of monetary policy in Germany and Japan. In the face of strong first-quarter growth in both countries, Japanese authorities are perceived to have postponed anticipated monetary easing, while the Bundesbank is perceived to have postponed anticipated tightening. In addition, the mark has been affected negatively by market reactions to recent and prospective domestic political developments in Germany as well as to uncertainties in the Soviet Union.

; the Bank of Japan sold $300 million, and the Desk did not intervene.

Recent indicators of economic activity in the major foreign industrial countries have been mixed. In Germany and Japan, unusually favorable weather and other transitory factors helped to push GNP to unexpectedly high levels in the first-quarter. Economic activity in both countries appears to have declined a bit in the second quarter. In Canada and the United Kingdom, first-quarter GNP data confirmed the continuation of recessions, while in France, economic activity was flat in the first quarter. Signs of improvement have emerged recently, however, at least in Canada and possibly in France. Recent Canadian data on new orders, shipments, auto sales, and housing suggest a pick-up, and the Canadian unemployment rate, though still above 10 percent, has started to edge down.

Inflation has been steady to somewhat lower in most industrial countries in recent months. Twelve-month inflation in the United Kingdom has dropped sharply, partly because of special factors; even absent special tax and interest rate effects the underlying rate of U.K. inflation has declined to about 6-1/2 percent. Germany is an exception to the general trend toward easing inflationary pressures.

The U.S. merchandise trade deficit narrowed further in April, from a substantially improved rate in the first quarter. While lower imports had accounted for most of the narrowing of the deficit in the first quarter, a rebound in exports led the improvement in April. Exports in April were about 5 percent higher than in the first quarter, and imports were about 2 percent higher. Import prices declined further in April; all of the decline was in non-oil import prices (reflecting the effects of the stronger dollar), whereas the decline in the first quarter had been concentrated in oil prices. The current account showed a surplus of $41 billion at an annual rate in the first quarter, primarily because of an inflow of $91 billion (annual rate) in transfers associated with Operation Desert Storm.

Outlook

Relative to the May Greenbook, the current forecast incorporates a higher path for the dollar, stronger near-term growth in the United States, and slightly weaker near-term growth abroad. As a result, the outlook for real net exports of goods and services has worsened somewhat. The projected nominal trade and current account deficits for 1991 remain little changed from the May forecast, because the initial favorable effects of a stronger dollar on import prices offset most of the near-term weakening in real net exports. Next year the current account deficit is projected to widen to nearly $50 billion, about $5 billion more than in the previous forecast.

The Dollar. In the staff forecast, the foreign exchange value of the dollar against the other G-10 currencies is projected to decline somewhat from its recent highs in the near term and then to remain unchanged. However, over the forecast period on average, the projected value of the dollar has been revised up by about 5 percent compared with the May Greenbook, largely in response to the persistent strength of the dollar. Against the currencies of eight developing countries, the dollar is expected to show a small depreciation in real terms over this year and next.

Foreign Industrial Countries. Average real GNP growth among the foreign G-7 countries (weighted by their shares in U.S. nonagricultural exports), which is expected to have been essentially zero during the first half of the year, is projected to pick up to 2 percent in the second half and to strengthen to 3 percent next year. Differences in growth rates among countries are expected to narrow significantly over the next year as Canada and the United Kingdom recover from recessions and growth in France picks up.

The outlook for inflation in the G-6 countries has been lowered slightly from that in May, to an average rate of about 4 percent for 1991.

The revision reflects recent improvements in inflation performance in the United Kingdom and, to a lesser extent, Japan and Canada. In 1992, average inflation is expected to slow by an additional 1/2 percentage point to a rate of 3-1/2 percent.

The outlook for interest rates in the major foreign industrial countries remains consistent with a cautious easing of monetary policy in a context of slowing inflation and weak, but recovering, real demand. Short-term interest rates are expected to move down gradually by another 1/2 percentage point from current levels on average by the end of 1992. German short-term interest rates are expected to rise slightly in coming months in response to mounting inflationary pressures, and then to return to about present levels by the second half of next year. Japanese authorities are expected to allow short-term interest rates to decline somewhat during the second half of this year as growth of aggregate demand eases; Japanese rates are expected to level off thereafter. Foreign long-term interest rates are expected to decline slightly on average over the forecast period.

Developing Countries. Growth in developing countries that are major U.S. trading partners is projected to increase moderately in 1991 to about 5-1/4 percent, on average, and to rise slightly further in 1992. All countries in this group are expected to be affected negatively by the decline in growth in industrial countries this year. However, government policies are sufficiently expansionary in several key developing countries to offset expected slower growth in external demand. Lower average oil prices expected for this year also will be a net positive factor.

U.S. Real Net Exports of Goods and Services. After having improved dramatically through the first quarter of this year, real net exports of goods and services are expected to decline fairly steadily through the end of next year. The decline reflects primarily the effects of a faster pickup in growth at home than abroad. The trajectory of net exports is more negative in the current forecast than in the previous one, primarily because of the higher projected value of the dollar.

TRADE QUANTITIES*
(Percent change from end of preceding comparable period, annual rate)

	1990	Projection 1991 Q1	Q2	H2	1992
Nonagricultural exports	8.6	6.5	11.4	9.4	8.7
Agricultural exports	-6.1	13.1	2.1	1.5	0.6
Non-oil imports	1.4	-10.2	5.4	9.4	9.2
Oil imports	-12.3	21.2	45.0	4.9	9.9

* GNP basis, 1982 dollars.

The growth of real exports of goods is projected to increase to more than 9 percent at an annual rate during the second half of this year as growth abroad recovers. Export growth is then projected to decline to about a 7 percent rate in the second half of 1992 as the negative effects of the recent rise in the dollar begin to outweigh the positive effects of the earlier decline in the dollar. Because of the stronger dollar, the export growth rate over the next year and a half is more than 1 percentage point below the previous forecast. The quantity of computer exports is expected to continue to expand rapidly, adding nearly 2 percentage points to the growth rate for total export volume over the projection period. Agricultural exports are expected to pick up somewhat in the near term, largely because of the recent provision of credit guarantees to the Soviet Union, but to remain sluggish over the rest of the forecast period.

The quantity of non-oil imports of goods is projected to rise at about a 5 percent rate in the second quarter and then to expand at an average annual rate of 9-1/4 percent over the next six quarters. The U.S. economic recovery and recent declines in the relative price of imports associated with the rise in the dollar are expected to stimulate demand for imports. Constant-dollar imports of computers are expected to grow especially rapidly, as in the case of exports, and will add several percentage points to the growth rate for total non-oil imports. Oil imports are expected to jump in the current quarter as stocks are rebuilt and to expand steadily thereafter, in line with growing domestic consumption and gradually receding domestic production.

Oil Prices. The outlook for oil prices in the near term has been lowered somewhat since the May forecast, reflecting the market's response to OPEC's agreement in early June not to cut its production quotas, and to continued strong increases in petroleum stocks. We now assume that oil import prices will remain under $18 per barrel through the summer, before returning to a flat $18 per barrel path by the end of the year (a level consistent with a posted price of $19.25 per barrel for West Texas Intermediate crude).

SELECTED PRICE INDICATORS
(Percent change from the end of preceding comparable period, annual rate)

		------ Projection -----			
	1990	1991			1992
		Q1	Q2	H2	
PPI (export-share wts.)	4.8	-2.0	-2.5	1.8	2.3
Nonagric exports (Fx-Wt)	4.0	-1.0	-1.6	0.5	2.0
Non-oil imports (Fx-Wt)	2.9	4.0	0.3	1.5	2.0
Oil imports ($/barrel)	20.57	20.33	17.68	17.92	18.00

Prices of Exports and Non-oil Imports. The fixed-weight price index for U.S. nonagricultural exports is projected to decline further in the second quarter, owing primarily to recent declines in domestic producer prices (particularly among industrial supplies and materials). The rise in the dollar may restrain U.S. exporters from raising their prices as well.

Moderate growth in export prices should resume by the end of this year with the projected turnaround in domestic materials prices. Non-oil import prices are projected to remain about unchanged in the current quarter, and to rise only slowly through the end of the forecast period; the recent rise in the dollar is expected to depress import prices for much of this year.

Nominal Trade and Current Account Balances. The merchandise trade deficit is projected to narrow further in the second quarter, to less than $70 billion (annual rate), as a result of sluggish imports and expanding exports. Thereafter, the deficit is projected to widen gradually, returning to a level of close to $80 billion next year. Excluding the effects of transfer payments associated with the Gulf War, the current account deficit this year is projected to be roughly $45 billion, or about $25 billion less than the trade deficit. Next year, the widening of the trade deficit is expected to be only slightly offset by net improvements in the non-trade portions of the current account (other than transfers), resulting in a current account deficit approaching $50 billion.

NOMINAL EXTERNAL BALANCES
(Billions of dollars, SAAR)

	1990	------ Projection -----			
		1991			1992
		Q1	Q2	H2	
Trade Balance	-108.1	-73.5	-67.0	-69.5	-80.3
Current Account excl. Gulf War Cash Grants	-87.8	-49.9	-48.7	-42.8	-47.7
Gulf War Cash Grants	4.3	90.8	48.0	16.0	0.0
Current Account	-92.1	40.9	-0.7	-26.8	-47.7

Within the non-trade portions of the current account, net service receipts are expected to expand steadily in the near term; this growth will be depressed somewhat over time by the effects of the higher dollar. Net investment income receipts are expected to decline from a level in the first quarter that had been pushed to abnormal heights by a transitory surge in the earnings of U.S. oil companies abroad. Through the forecast period, net investment income receipts are projected to make a small positive contribution to the current account, as they did in 1990; that contribution is expected to increase slightly over the next few quarters as recent declines in dollar interest rates show through to lower net payments on U.S. debt to foreigners.

With respect to transfer payments, total cash grants from foreign governments to support Operation Desert Storm are expected to amount to $43 billion this year. Payments received in the first quarter this year totaled $23 billion (not at an annual rate). An additional $12 billion is expected in the second quarter, and a remaining $8 billion in the third quarter. As a result, a current account surplus of $41 billion was recorded in the first quarter and a near zero balance is expected in the second quarter. The current account is then projected to move significantly into deficit in the second half of the year.

June 26, 1991

STRICTLY CONFIDENTIAL - FR
CLASS II FOMC

REAL GNP AND CONSUMER PRICES, SELECTED COUNTRIES, 1988-92
(Percent change from fourth quarter to fourth quarter)

Measure and country	1988	1989	1990	Projection 1991	Projection 1992
REAL GNP					
Canada	3.1	2.9	-1.6	-0.2	2.7
France	4.0	3.9	2.1	1.2	2.4
Western Germany	3.5	3.2	5.3	2.8	2.9
Italy	3.7	2.9	1.1	1.9	2.8
Japan	5.6	4.8	4.8	3.6	3.6
United Kingdom	3.3	1.5	-1.3	0.3	2.0
Average, weighted by 1987-89 GNP	4.2	3.5	2.5	2.1	2.9
Average, weighted by share of U.S. nonagricultural exports					
Total foreign	4.1	3.7	1.8	2.2	3.4
G-6	3.8	3.2	0.7	1.1	2.8
Developing countries	5.3	5.0	4.7	5.6	5.6
CONSUMER PRICES					
Canada	4.1	5.2	4.9	5.3	3.4
France	3.0	3.6	3.6	2.6	2.9
Western Germany	1.6	3.1	3.0	3.8	2.8
Italy	5.2	6.6	6.3	6.2	5.2
Japan	1.5	2.9	3.5	3.1	3.0
United Kingdom	6.5	7.6	10.0	4.7	4.6
Average, weighted by 1987-89 GNP	3.2	4.4	4.9	4.0	3.5
Average, weighted by share of U.S. non-oil imports	3.0	4.2	4.5	4.1	3.3

Strictly Confidential (FR) Class II-FOMC June 26, 1991

OUTLOOK FOR U.S. CURRENT ACCOUNT AND REAL NET EXPORTS

(Billions of dollars, seasonally adjusted annual rates)

	ANNUAL			1990				1991				1992
	1990	1991-P	1992-P	Q1	Q2	Q3	Q4	Q1	Q2-P	Q3-P	Q4-P	Q4-P
1. GNP Real Net Exports (82$)	-33.8	-1.2	-10.7	-35.4	-44.6	-46.5	-8.8	6.4	-7.3	-0.3	-3.6	-14.1
a. Exports of G+S	631.5	650.3	690.1	628.1	620.1	630.5	647.2	643.0	641.6	651.7	664.8	704.9
Merchandise	423.9	457.0	496.1	422.4	418.4	421.0	433.8	441.3	452.5	462.5	471.8	509.7
Services	207.6	193.3	194.0	205.7	201.7	209.5	213.4	201.7	189.1	189.2	193.1	195.2
b. Imports of G+S	665.3	651.5	700.7	663.5	664.7	677.0	656.0	636.6	648.9	652.0	668.4	719.0
Merchandise	517.0	518.8	569.2	517.8	515.2	526.5	508.4	501.2	515.2	522.0	536.7	586.7
Oil	95.5	94.2	104.3	100.8	96.9	100.9	83.3	87.4	95.9	95.5	98.2	107.9
Non-oil	421.5	424.5	464.9	417.1	418.3	425.5	425.1	413.8	419.3	426.5	438.6	478.8
Services	148.3	132.7	131.6	145.6	149.4	150.5	147.6	135.4	133.7	130.0	131.7	132.3
Memo:												
Percent Changes (AR) 1/												
Exports G+S	5.8	2.7	6.0	11.2	-5.0	6.9	11.0	-2.6	-0.9	6.4	8.3	5.9
of which: Merchandise	7.1	8.8	8.0	18.1	-3.7	2.5	12.7	7.1	10.6	9.2	8.2	7.0
Imports G+S	-0.5	1.9	7.6	2.5	0.7	7.6	-11.8	-11.3	8.0	1.9	10.5	7.6
of which: Non-oil Merch.	1.4	3.2	9.2	-2.1	1.2	7.1	-0.4	-10.2	5.4	7.1	11.8	7.9
2. U.S. Current Account Balance	-92.1	-3.3	-47.7	-90.7	-88.7	-95.5	-93.6	40.9	-0.7	-8.2	-45.3	-52.4
a. Merchandise Trade, net	-108.1	-69.8	-80.3	-110.1	-96.4	-115.0	-110.9	-73.5	-67.0	-66.1	-72.9	-83.6
Exports	389.5	416.9	453.4	381.0	388.4	386.6	402.3	403.4	412.9	421.5	429.9	466.3
Agricultural	40.2	40.3	41.8	43.0	40.8	39.3	37.8	39.7	40.4	40.9	40.1	42.8
Nonagricultural	349.3	376.7	411.6	338.0	347.5	347.3	364.5	363.7	372.5	380.7	389.8	423.5
Imports	497.7	486.8	533.7	491.1	484.7	501.6	513.2	476.9	479.8	487.7	502.7	549.9
Oil	62.1	52.6	57.6	63.2	51.3	61.8	72.1	52.6	51.7	52.0	54.0	59.7
Non-oil	435.6	434.2	476.1	427.9	433.4	439.8	441.1	424.3	428.1	435.7	448.7	490.2
b. Other Current Account	16.0	66.5	32.7	19.5	7.6	19.5	17.3	114.3	66.3	57.9	27.6	31.2
Investment Income, net	11.9	8.7	5.6	12.0	0.0	11.2	24.5	18.6	3.3	6.5	6.5	4.1
Direct, net	52.7	48.7	43.0	51.9	43.6	53.5	61.7	60.6	45.8	43.9	44.6	42.7
Portfolio, net	-40.7	-40.0	-37.4	-39.8	-43.6	-42.3	-37.2	-42.0	-42.5	-37.4	-38.1	-38.6
of which: Gov't Payments	37.9	36.5	35.9	36.8	37.4	38.1	39.1	38.5	36.5	35.7	35.2	36.5
Military Transactions, net	-7.2	-5.6	-2.1	-6.9	-6.2	-6.7	-9.0	-8.7	-6.8	-4.8	-2.0	-1.2
Other Services, net	33.6	40.0	46.9	30.5	32.6	32.3	38.9	36.7	38.8	41.2	43.1	48.4
Unilateral Transfers, net	-22.3	23.4	-17.8	-16.1	-18.8	-17.3	-37.1	67.8	31.0	15.0	-20.0	-20.0

1/ Percent change from previous period; percent changes for annual data are calculated Q4/Q4.