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Part 1

August 6, 1980

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

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**

DOMESTIC NONFINANCIAL DEVELOPMENTS

Summary. Recent data suggest that the decline in economic activity has moderated, following the precipitous contraction in the second quarter. In particular, demand and activity appear to have firmed somewhat in autos and housing. Increases in major price indexes have slowed considerably since their rapid rise in the first quarter, but supply conditions are adding to inflationary pressures in the food sector.

Industrial production continued to decline in July, but apparently by less than during the three preceding months. While auto assemblies increased in July for the second consecutive month, there were further cuts in production of machinery and some nondurables. The capacity utilization rate in manufacturing dropped further in July, to a level more than 10 percentage points below its 1979 peak.

Employment in manufacturing establishments was reduced another quarter-million in July, with job losses widespread among major industries. Since the beginning of the year, factory employment has dropped by 1.2 million. Nonfarm payroll employment in the private sector as a whole, however, was about unchanged in July after allowance for increased strike activity. In contrast, the household employment series rose by nearly half a million and the unemployment rate remained at 7-3/4 percent, the level of May and June.

Consumer spending turned up in June following a record decline of 10 percent in real retail sales over the four preceding months. The turnaround was led by an advance in automotive sales; however, spending on many other items also increased, and total sales less autos and

nonconsumption items in nominal terms retraced the losses of the two previous months. Furthermore, in July unit sales of domestic autos rose to a 6.4 million unit rate--an improvement from the two preceding months but still well below the first quarter average.

Measures of consumer confidence, which had plummeted through most of the first half of 1980, perked up a bit in June and July. However, the income gains necessary to sustain increases in consumer outlays still are not evident; nominal personal income was up at only a 4-1/2 percent annual rate in June, and wages and salaries were virtually unchanged. In July, income was boosted by a cost of living adjustment in social security benefits, but wage and salary income probably was again little changed.

Continuing the general pattern of recent months, business investment spending declined sharply in June, and incoming commitments data suggest further near-term declines. Shipments of nondefense capital goods fell 1.2 percent in June, and new orders for these goods remained depressed, particularly for machinery. Moreover, contracts for non-residential construction have been trending down since the beginning of the year, although there was an increase in June.

Production adjustments have significantly reduced the rate of business inventory accumulation in recent months. In May, total manufacturing and trade inventories declined in real terms. The latest data--which are only available in nominal terms--indicate that in June the book value of manufacturers' inventories increased at only a \$4 billion annual rate, although wholesale trade stocks rose at a \$14 billion rate, following a \$5 billion increase in May. Despite the

generally prompt attempts to correct inventory imbalances, at currently reduced levels of sales, the constant dollar stock-sales ratio for manufacturing and trade remains close to its 1974-75 recession peak.

With mortgage interest rates down sharply from their spring peaks, there has been some revival of activity in the housing sector. Sales of new homes appear to have increased again in June following a strong May advance. In addition, sales of existing homes were up 8 percent in June following declines over the previous eight months. Housing starts and permits also rose strongly in June, and early reports suggest a further rise in residential building permits in July.

Price increases have eased considerably in recent months, largely as a result of the dramatic slowdown in the rise of overall energy prices. Nonetheless, the inflation rate remains extremely high by past standards. Increases in mortgage interest costs continued to put upward pressure on the consumer price index through June, but these effects should be reversed in coming months as the index of homeownership costs begins to pick up this spring's reduction in commitment rates.

Food prices continued to exert a moderating influence on overall consumer prices through June, but an acceleration in these prices that was already evident in producer markets late in the second quarter may have been exacerbated by drought conditions in July. In addition, labor cost pressures intensified in the second quarter as hourly compensation in the nonfarm business sector rose at an estimated 10-3/4 percent rate and productivity declined considerably further.

Outlook. The staff is now projecting a smaller decline in economic activity for the third quarter: real GNP is expected to fall about 4

percent at an annual rate compared with the 6 percent drop that was shown in the last Greenbook. This revision stems in part from incoming data on housing activity and consumer spending, which suggest that the downturn is moderating faster than previously anticipated. Also, production adjustments during the second quarter limited the extent of inventory accumulation; as a result, the shift to stock liquidation in the third quarter is likely to be less severe than was projected last month.

The monetary policy assumptions underlying the projection are slightly more restrictive than in the last Greenbook, following the decisions of the FOMC in July. It is now assumed that M-1A will fall in the lower part of the Committee's range for 1980 and that it will grow 4-1/4 percent over 1981 (abstracting from the impact of nationwide NOW accounts). Consequently, short-term interest rates are expected to rise somewhat more than previously anticipated. The fiscal policy assumptions are little changed. It is still assumed that corporate and personal income taxes will be cut by \$28 billion beginning January 1. The fiscal year 1980 and fiscal year 1981 budget deficits are both projected by the staff to be in the area of \$60 billion, some \$6 to \$7 billion more than in the last Greenbook; this results primarily from increased expenditures estimated for payrolls, unemployment compensation, and defense.

Economic activity is not expected to show a significant upturn before the end of 1980. The demand for housing and autos appears to be improving, but on the whole households are expected to restrain their spending over the next several months and to attempt to rebuild

saving positions in the face of uncertain income prospects. Despite the recent liquidation of stocks, inventories still are high relative to sales and likely will continue to be worked down through year-end. Moreover, real capital outlays are expected to be curtailed as a result of continued weakness in final demand.

The recovery in 1981 is still projected to be moderate compared with previous expansions as a result of the restrictive stance assumed for monetary and--even with a tax cut--for fiscal policy. Real GNP is projected to rise about 2-1/4 percent over the four quarters of 1981, somewhat less than indicated last month. The relatively slow growth of output in part reflects the effects of tightening credit market conditions and weak growth in real disposable income, which are expected to retard the recovery of housing and consumption. The relatively high cost of capital also is likely to be an influence holding down real business capital outlays, as is the projected slack in capacity utilization. Reflecting the continued caution observed in recent years, businesses are expected to keep their inventories about in line with the slow growth of sales. Nevertheless, the projected advance in output during 1981 should be sufficient to permit gains in employment that exceeds the moderate growth in the labor force, and the jobless rate is expected to edge down to 8.5 percent by the end of the year after peaking at 8.8 percent in the first quarter of 1981.

The staff outlook for inflation over the next year and a half is little changed. During the last half of this year, gross business product prices are projected to rise at about a 9-3/4 percent rate, and then slow to an 8-1/2 percent rate by the end of next year. The

projected rate of inflation for 1981, still quite high on an historical basis, reflects further increases in the price of imported oil, the effects of domestic crude oil price decontrol, a reacceleration of food prices, and continued large increases in unit labor costs.

Detailed data for these projections are shown in the following tables.

STAFF GNP PROJECTIONS

Percent changes, annual rate										
Nominal GNP		Real GNP		Gross domestic business product fixed-weighted price index				Unemployment rate (percent)		
7/2/80	8/6/80	7/2/80	8/6/80	Total		Excluding food and energy		7/2/80	8/6/80	
7/2/80	8/6/80	7/2/80	8/6/80	7/2/80	8/6/80	7/2/80	8/6/80	7/2/80	8/6/80	
Annual changes:										
1978 1/	12.0	12.0	4.4	4.4	7.6	7.6	7.2	7.2	6.0	6.0
1979 1/	11.3	11.3	2.3	2.3	9.5	9.5	8.1	8.1	5.8	5.8
1980	7.1	7.6	-1.7	-1.4	9.9	9.9	7.9	7.9	7.8	7.5
1981	9.1	9.4	-2.2	.1	9.4	9.4	7.8	7.8	8.8	8.6
Quarterly changes:										
1979-Q1 1/	10.6	10.6	1.1	1.1	10.0	10.0	7.7	7.7	5.7	5.7
1979-Q2 1/	6.7	6.7	-2.3	-2.3	10.1	10.1	7.9	7.9	5.8	5.8
1979-Q3 1/	11.9	11.9	3.1	3.1	10.4	10.4	7.6	7.6	5.8	5.8
1979-Q4 1/	10.5	10.5	2.0	2.0	8.4	8.4	6.6	6.6	5.9	5.9
1980-Q1 1/	10.8	10.8	1.2	1.2	11.2	11.2	8.8	8.8	6.1	6.1
1980-Q2 1/	-4	.4	-8.8	-9.1	9.5	9.4	8.6	8.7	7.6	7.5
1980-Q3	2.1	3.1	-6.1	-4.1	9.5	9.6	7.8	8.0	8.6	8.1
1980-Q4	8.2	9.9	-2.1	-1.0	9.8	9.8	7.7	7.7	8.9	8.5
1981-Q1	12.0	12.0	1.9	1.9	9.7	9.9	8.0	8.1	9.0	8.8
1981-Q2	12.6	11.8	3.6	3.0	9.3	9.4	7.7	7.7	8.9	8.7
1981-Q3	10.3	10.2	2.2	2.1	8.4	8.4	7.2	7.3	8.8	8.6
1981-Q4	10.9	10.8	2.2	2.0	8.4	8.5	7.2	7.2	8.7	8.5
Two-quarter changes: ^{2/}										
1979-Q4 1/	11.2	11.2	2.5	2.5	9.3	9.3	7.1	7.1	.1	.1
1980-Q2 1/	5.1	5.5	-3.9	-4.1	10.4	10.4	8.6	8.6	1.7	1.6
1980-Q4	5.1	6.4	-4.1	-2.6	9.6	9.7	7.7	7.9	1.3	1.0
1981-Q2	12.3	11.9	2.8	2.5	9.5	9.6	7.9	7.9	.0	.2
1981-Q4	10.6	10.5	2.2	2.0	8.4	8.5	7.3	7.2	-.2	-.2
Four-quarter changes: ^{3/}										
1978-Q4 1/	13.4	13.4	4.8	4.8	8.6	8.6	8.1	8.1	-.7	-.7
1979-Q4 1/	9.9	9.9	1.0	1.0	9.7	9.7	7.5	7.5	.1	.1
1980-Q4	5.1	6.0	-4.0	-3.3	10.0	10.0	8.1	8.2	3.0	2.6
1981-Q4	11.4	11.2	2.5	2.2	8.9	9.0	7.6	7.6	-.2	.0

1/ Actual.

2/ Percent change from two quarters earlier.

3/ Percent change from four quarters earlier.

August 6, 1980

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

	1980				1981			
	Q1	Q2	Q3	Q4	Projection		Q3	Q4
Gross national product	2520.8	2523.4	2542.9	2603.4	2678.2	2753.8	2821.2	2894.5
Final purchases	2516.1	2511.7	2551.9	2618.7	2687.5	2747.6	2809.2	2879.3
Private	1998.9	1984.7	2016.6	2068.1	2126.2	2175.7	2225.1	2277.6
Excluding net exports	2012.5	1983.4	2015.6	2059.2	2113.9	2168.5	2221.0	2276.8
Personal consumption expenditures	1629.5	1628.2	1658.5	1693.9	1740.7	1786.9	1829.7	1872.9
Goods	872.2	851.4	860.8	876.4	899.4	922.6	943.6	965.7
Services	757.3	776.8	797.7	817.5	841.3	864.3	886.1	907.2
Gross private domestic investment	387.7	366.9	348.1	350.0	363.9	387.8	403.3	419.1
Residential construction	110.4	89.3	89.3	96.8	102.8	108.3	114.8	122.3
Business fixed investment	272.6	265.9	267.8	268.5	270.4	273.3	276.5	281.6
Change in business inventories	4.7	11.7	-9.0	-15.3	-9.3	6.2	12.0	15.2
Nonfarm	4.4	12.4	-9.0	-15.3	-9.3	6.2	12.0	15.2
Net exports of goods and services ^{1/}	-13.6	1.3	1.0	8.9	12.3	7.2	4.1	.8
Exports	308.1	307.3	310.1	316.3	326.2	336.0	346.0	355.6
Imports	321.7	306.0	309.1	307.3	313.9	328.9	341.8	354.7
Gov't. purchases of goods and services	517.2	527.0	535.3	550.6	561.3	571.9	584.1	601.7
Federal ^{2/}	186.2	192.5	195.0	204.1	208.5	212.6	216.8	226.4
State and local	331.0	334.5	340.3	346.5	352.8	359.3	367.3	375.3
Gross national product in constant (1972) dollars	1444.7	1410.8	1396.0	1392.5	1398.9	1409.5	1416.7	1423.7
Personal income	2057.4	2078.3	2129.9	2175.6	2214.5	2268.6	2328.2	2386.7
Wage and salary disbursements	1303.7	1309.3	1319.0	1344.1	1370.1	1401.0	1428.8	1464.4
Disposable personal income	1737.4	1754.0	1800.1	1837.5	1886.9	1929.3	1980.4	2025.9
Saving rate (percent)	3.7	4.7	5.4	5.3	5.2	4.8	5.0	5.0
Corporate profits with I.V.A. and C.C. Adj.	175.0	151.5	133.7	138.2	146.9	154.4	162.1	165.3
Corporate profits before tax	260.4	203.9	197.0	203.8	212.0	219.0	226.2	232.9
Federal government surplus or deficit (-) (N.I.A. basis)	-22.9	-47.6	-74.7	-72.9	-77.2	-67.4	-74.8	-71.8
High employment surplus or deficit (-)	4.2	10.4	9.3	23.8	24.8	34.7	30.0	36.7
State and local government surplus or deficit (-) (N.I.A. basis)	24.6	21.1	21.7	21.9	23.7	25.3	25.1	24.9
Excluding social insurance funds	-4.2	-9.0	-8.9	-9.3	-8.1	-7.1	-7.9	-8.7
Civilian labor force (millions)	104.2	104.7	105.3	105.5	105.8	106.2	106.5	106.8
Unemployment rate (percent)	6.1	7.5	8.1	8.5	8.8	8.7	8.6	8.5
Nonfarm payroll employment (millions)	91.1	90.5	89.7	89.6	89.6	90.0	90.3	90.7
Manufacturing	21.0	20.3	19.7	19.4	19.4	19.6	19.7	19.8
Industrial production (1967=100)	152.2	144.7	140.4	138.7	138.9	140.3	140.8	141.4
Capacity utilization: all mfg. (percent)	83.8	78.4	75.2	73.7	73.4	73.6	73.3	73.2
Materials (percent)	85.4	79.5	74.4	72.7	72.2	72.5	72.4	72.4
Housing starts, private (million units, A.R.)	1.26	1.05	1.20	1.25	1.30	1.35	1.35	1.40
New autos sales, (millions, A.R.)	10.65	7.67	8.45	8.95	9.10	9.30	9.45	9.80
Domestic models	7.87	5.53	6.10	6.60	6.70	6.85	6.95	7.30
Foreign models	2.77	2.14	2.35	2.35	2.40	2.45	2.50	2.50

^{1/} Balance of payments data and details underlying these estimates are shown in the International Developments section of this part of the Greenbook.

^{2/} Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

August 6, 1980

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

	1980				1981			
	Q1	Q2	Q3	Q4	Projection		Q3	Q4
<u>Constant (1972) dollars</u>								
Gross national product	1.2	-9.1	-4.1	-1.0	1.9	3.0	2.1	2.0
Final purchases	1.5	-9.6	-2.2	-1	1.0	.8	1.2	1.5
Private	.9	-12.0	-2.4	-1	1.2	.9	1.2	1.5
Excluding net exports	-.8	-13.6	-2.9	-1.1	1.1	1.3	1.4	1.8
Personal consumption expenditures	.5	-9.4	-2.1	-1.3	1.4	1.4	1.4	1.3
Goods	-1.8	-16.6	-4.7	-3.3	.3	.8	.7	1.1
Services	3.2	-.6	.7	.8	2.5	2.1	2.1	1.5
Gross private domestic investment	-8.3	-27.9	-19.6	-7.0	6.9	19.2	8.1	7.7
Residential structures	-26.2	-60.3	-8.4	27.3	17.2	13.5	15.8	18.2
Business fixed investment	1.7	-17.8	-6.1	-6.9	-5.1	-3.5	-2.9	-.3
Gov't. purchases of goods and services	4.2	.9	-1.6	-.2	-.0	.3	1.3	1.6
Federal	13.1	8.9	-2.4	.8	1.0	1.5	1.4	2.0
State and local	-.7	-3.6	-1.1	-.7	-.7	-.5	1.2	1.3
Disposable personal income	.9	-5.6	.9	-1.5	1.1	-.2	2.4	1.0
<u>Current dollars</u>								
Gross national product	10.8	.4	3.1	9.9	12.0	11.8	10.2	10.8
Final purchases	11.0	-.7	6.6	10.9	10.9	9.2	9.3	10.4
Private	10.4	-2.8	6.6	10.6	11.7	9.6	9.4	9.8
Excluding net exports	10.7	-5.7	6.7	8.9	11.1	10.7	10.0	10.4
Personal consumption expenditures	13.0	-.3	7.7	8.8	11.5	11.0	9.9	9.8
Goods	12.5	-9.2	4.5	7.4	10.9	10.7	9.4	9.7
Services	13.6	10.7	11.2	10.3	12.2	11.4	10.5	9.9
Gross private domestic investment	.5	-19.8	-19.0	2.2	16.9	28.9	17.0	16.6
Residential structures	-19.3	-57.0	-.2	38.1	27.2	23.2	26.3	28.8
Business fixed investment	11.6	-9.5	2.9	1.0	2.9	4.4	4.8	7.6
Gov't. purchases of goods and services	13.4	7.8	6.4	11.9	8.0	7.8	8.8	12.6
Federal	18.7	14.3	5.2	20.0	8.9	8.1	8.1	18.9
State and local	10.5	4.2	7.1	7.5	7.5	7.6	9.2	9.0
Disposable personal income	13.5	3.9	10.9	8.6	11.2	9.3	11.0	9.5
Personal income	10.9	4.1	10.3	8.9	7.4	10.1	10.9	10.4
Wage and salary disbursements	10.9	1.7	3.0	7.8	8.0	9.3	8.2	10.3
Corporate profits with IVA & C.C. Adj.	-3.1	-43.8	-39.3	14.2	27.7	22.0	21.5	8.1
Corporate profits before tax	31.9	-62.5	-12.8	14.6	17.0	13.8	13.7	12.4
Nonfarm payroll employment	2.5	-2.8	-3.5	-.3	.2	1.8	1.5	1.7
Manufacturing	-.8	-11.8	-11.5	-6.1	.2	4.6	2.3	2.0
Nonfarm business sector								
Output per hour	-1.1	-4.1	-.8	-.8	1.9	1.6	.9	.5
Compensation per hour	10.7	10.8	9.4	9.0	11.6	8.2	8.1	8.3
Unit labor costs	12.0	15.6	10.3	9.9	9.5	6.5	7.1	7.8
GNP implicit deflator ^{1/}	9.5	10.4	7.5	11.0	10.0	8.5	7.9	8.7
Gross domestic business product								
fixed-weighted price index ^{2/}	11.2	9.4	9.6	9.8	9.9	9.4	8.4	8.5
Excluding food and energy	8.8	8.7	8.1	7.7	8.0	7.7	7.2	7.2
Consumer price index (all urban)	17.2	13.8	8.2	9.8	10.8	10.4	9.5	9.0
Industrial production	.0	-18.3	-11.4	-4.7	.6	4.0	1.5	1.7

^{1/} Excluding Federal pay increases, the rates of change are: 1980-Q1, 9.4 percent; 1980-Q4, 10.3 percent; 1981-Q1, 9.9 percent; 1981-Q4, 8.1 percent.

^{2/} Uses expenditures in 1972 as weights.

August 6, 1980

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

	1978				1979			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Gross national product	2011.3	2104.2	2159.6	2235.2	2292.1	2329.8	2396.5	2456.9
Final purchases	1988.5	2078.4	2139.5	2214.5	2272.9	2296.4	2381.9	2451.4
Private	1569.1	1630.1	1698.6	1760.7	1812.8	1829.8	1904.1	1950.2
Excluding net exports	1591.3	1657.7	1705.4	1765.2	1808.8	1837.9	1906.4	1962.1
Personal consumption expenditures	1287.2	1331.2	1369.3	1415.4	1454.2	1475.9	1528.6	1580.4
Goods	691.2	722.1	740.2	770.2	784.9	789.9	818.1	846.9
Services	596.0	609.1	629.1	645.1	669.3	686.0	710.6	733.5
Gross private domestic investment	327.0	352.3	356.2	370.5	373.8	395.4	392.3	387.2
Residential construction	100.5	107.7	110.2	113.7	111.2	112.9	116.0	116.4
Business fixed investment	203.7	218.8	225.9	236.1	243.4	249.1	261.8	265.2
Change in business inventories	22.8	25.8	20.0	20.6	19.1	33.4	14.5	5.6
Nonfarm	22.0	25.3	18.5	19.3	18.8	32.6	12.6	2.1
Net exports of goods and services ^{1/}	-22.2	-7.6	-6.8	-4.5	4.0	-8.1	-2.3	-11.9
Exports	184.4	205.7	213.8	224.9	238.5	243.7	267.3	280.4
Imports	206.6	213.3	220.6	229.4	234.4	251.9	269.5	292.4
Gov't. purchases of goods and services	419.4	428.3	440.9	453.8	460.1	466.6	477.8	501.2
Federal ^{2/}	150.9	148.2	152.3	159.0	163.6	161.7	162.9	178.4
State and local	268.5	280.1	288.6	294.8	296.5	304.9	314.9	322.8
Gross national product in constant (1972) dollar	1367.8	1395.2	1407.3	1426.6	1430.6	1422.3	1433.3	1440.3
Personal income	1634.8	1689.3	1742.5	1803.1	1852.6	1892.5	1946.6	2005.0
Wage and salary disbursements	1052.0	1090.0	1116.8	1154.3	1189.3	1212.4	1238.1	1270.5
Disposable personal income	1395.0	1437.3	1476.5	1524.8	1572.2	1601.7	1640.0	1683.1
Saving rate (percent)	5.3	5.0	4.8	4.7	5.0	5.4	4.3	3.5
Corporate profits with I.V.A. and C.C. Adj.	141.2	169.4	175.2	184.8	178.9	176.6	180.8	176.4
Corporate profits before tax	177.5	207.2	212.0	227.4	233.3	227.9	242.3	243.0
Federal government surplus or deficit (-) (N.I.A. basis)	-49.4	-24.6	-20.4	-16.3	-11.7	-7.0	-11.3	-15.7
High employment surplus or deficit (-)	-26.3	-9.8	-6.8	-7.8	-1.1	13.7	9.6	7.7
State and local government surplus or deficit (-) (N.I.A. basis)	30.2	29.6	22.7	27.1	27.6	19.7	25.3	25.8
Excluding social insurance funds	7.9	6.5	-9	3.3	2.6	-6.3	-1.8	-2.2
Civilian labor force (millions)	99.1	100.2	100.8	101.5	102.3	102.4	103.2	103.7
Unemployment rate (percent)	6.2	6.0	6.0	5.8	5.7	5.8	5.8	5.9
Nonfarm payroll employment (millions)	85.0	86.4	87.2	88.2	89.1	89.7	90.2	90.6
Manufacturing	20.2	20.4	20.5	20.9	21.1	21.1	21.1	21.0
Industrial production (1967=100)	140.8	145.1	147.9	150.7	152.2	151.9	152.3	152.2
Capacity utilization: all mfg. (percent)	82.0	83.9	85.2	86.4	86.7	85.9	85.4	84.6
Materials (percent)	82.6	85.0	86.4	88.2	88.0	87.3	87.2	86.3
Housing starts, private (million units, A.R.)	1.86	2.10	2.03	2.06	1.67	1.82	1.81	1.59
New autos sales, (millions, A.R.)	10.80	12.09	11.16	11.06	11.56	10.65	10.79	9.80
Domestic models	8.80	10.01	9.21	9.14	9.30	8.16	8.63	7.43
Foreign models	2.00	2.09	1.96	1.92	2.25	2.49	2.16	2.37

^{1/} Balance of payments data and details underlying these estimates are shown in the International Developments section of this part of the Greenbook.

^{2/} Components of purchases and total receipts and total expenditures are shown in the Federal Sector Accounts table which follows.

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

	1978				1979			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<u>Constant (1972) dollars</u>								
Gross national product	1.9	8.3	3.5	5.6	1.1	-2.3	3.1	2.0
Final purchases	.4	8.7	4.6	5.7	1.1	-3.9	6.4	3.6
Private	.8	10.7	4.4	6.7	1.8	-4.1	7.8	3.1
Excluding net exports	1.0	7.9	4.1	6.9	.4	-2.9	5.3	3.1
Personal consumption expenditures	.8	5.6	4.8	6.8	.6	-2.9	4.9	4.1
Goods	-4.7	9.2	4.2	9.9	-4.4	-7.3	6.0	4.7
Services	7.9	1.4	5.5	3.2	7.1	2.5	3.6	3.5
Gross private domestic investment	12.3	15.7	-5.0	6.6	-5	8.5	-12.8	-11.6
Residential structures	-4.7	11.0	-4.9	-1.1	-14.3	-7.2	-1.5	-4.5
Business fixed investment	4.6	23.2	3.9	11.3	4.8	-.8	10.7	-.3
Gov't. purchases of goods and services	-1.2	.9	5.0	1.8	-1.8	-3.3	1.0	6.0
Federal	-7.4	-12.3	8.2	3.2	7.2	-11.3	-2.6	16.0
State and local	2.7	9.3	3.3	1.0	-6.6	1.6	3.1	.8
Disposable personal income	2.0	4.0	4.2	6.4	2.1	-1.4	.2	1.1
<u>Current dollars</u>								
Gross national product	8.4	19.8	10.9	14.8	10.6	6.7	11.9	10.5
Final purchases	7.5	19.3	12.3	14.8	11.0	4.2	15.8	12.2
Private	7.7	22.3	12.3	15.4	12.4	3.8	17.3	10.0
Excluding net exports	8.8	17.8	12.0	14.8	10.3	6.6	15.8	12.2
Personal consumption expenditures	9.0	14.4	11.9	14.2	11.4	6.1	15.0	14.3
Goods	3.3	19.1	10.4	17.2	7.9	2.6	15.1	14.8
Services	16.1	9.1	13.8	10.6	15.8	10.4	15.1	13.5
Gross private domestic investment	13.3	34.8	4.5	17.1	3.6	25.2	-3.0	-5.1
Residential structures	2.4	32.0	9.5	13.5	-8.5	6.1	11.7	1.4
Business fixed investment	10.6	33.3	13.7	19.3	12.9	9.6	22.0	5.4
Gov't. purchases of goods and services	6.5	8.8	12.3	12.2	5.6	5.8	10.0	21.1
Federal	-.9	-7.0	11.7	18.7	12.1	-4.6	3.1	43.8
State and local	11.1	18.5	12.6	8.9	2.3	11.9	13.8	10.4
Disposable personal income	10.3	12.7	11.4	13.8	13.0	7.7	9.9	10.9
Personal income	10.0	14.0	13.2	14.7	11.4	8.9	11.9	12.6
Wage and salary disbursements	11.7	15.3	10.2	14.1	12.7	8.0	8.8	10.9
Corporate profits with IVA & C.C. Adj.	-27.5	107.2	14.4	23.8	-12.2	-5.0	9.9	-9.4
Corporate profits before tax	-11.5	85.7	9.6	32.4	10.8	-8.9	27.8	1.2
Nonfarm payroll employment	4.7	7.0	3.7	4.7	4.3	2.4	2.3	1.7
Manufacturing	5.4	3.5	2.6	6.3	4.6	.6	-.6	-1.7
Nonfarm business sector								
Output per hour	-.9	1.8	2.4	.7	-3.3	-3.9	-1.5	.8
Compensation per hour	11.4	7.3	8.5	8.7	10.2	8.1	8.5	9.5
Unit labor costs	12.4	5.4	5.9	7.9	14.0	12.5	10.1	8.6
GNP implicit deflator 1/	6.3	10.6	7.2	8.7	9.3	9.3	8.5	8.4
Gross domestic business product								
fixed-weighted price index 2/	6.6	10.5	8.8	8.7	10.0	10.1	10.4	8.4
Excluding food and energy	5.5	9.4	8.9	8.7	7.7	7.9	7.6	7.7
Consumer price index (all urban)	7.8	10.2	8.8	9.1	11.1	13.6	12.9	13.2
Industrial production	1.4	12.8	7.9	7.8	4.0	-.8	1.1	-.3

1/ Excluding Federal pay increases, rates of change were: 1978-Q1, 6.3 percent; 1978-Q4, 8.1 percent; 1979-Q1, 9.3 percent; 1979-Q4, 8.0 percent.

2/ Uses expenditures in 1972 as weights.

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

	1974	1975	1976	1977	1978	1979	Projected	
							1980	1981
Gross national product	1412.9	1528.8	1702.2	1899.5	2127.6	2368.8	2547.7	2786.9
Final purchases	1404.0	1539.6	1692.1	1877.6	2105.2	2350.6	2549.6	2780.9
Private	1101.3	1201.2	1330.8	1481.4	1669.6	1874.2	2017.1	2201.2
Excluding net exports	1095.3	1180.8	1322.8	1491.3	1679.9	1878.8	2017.7	2195.0
Personal consumption expenditures	889.6	979.1	1089.9	1210.0	1350.8	1509.8	1652.5	1807.5
Goods	498.3	541.5	601.3	660.1	730.9	809.9	865.2	932.8
Services	391.3	437.5	488.5	549.8	619.8	699.8	787.3	874.7
Gross private domestic investment	214.6	190.9	243.0	303.3	351.5	387.2	363.2	393.5
Residential construction	55.1	51.5	68.1	91.9	108.0	114.1	96.5	112.0
Business fixed investment	150.6	150.2	164.9	189.4	221.1	254.9	268.7	275.4
Change in business inventories	8.9	-10.7	10.0	21.9	22.3	18.2	-2.0	6.0
Nonfarm	10.8	-14.3	12.1	20.7	21.3	16.5	-1.9	6.0
Net exports of goods and services ^{1/}	6.0	20.4	8.0	-9.9	-10.3	-4.6	-.6	6.1
Exports	137.9	147.3	163.3	175.9	207.2	257.5	310.4	340.9
Imports	131.9	126.9	155.4	185.8	217.5	262.1	311.0	334.8
Gov't. purchases of goods and services	302.7	338.4	361.3	396.2	435.6	476.4	532.5	579.7
Federal ^{2/}	111.1	123.1	129.7	144.4	152.6	166.6	194.5	216.1
State and local	191.5	215.4	231.6	251.8	283.0	309.8	338.1	363.7
Gross national product in constant (1972) dollars	1217.8	1202.3	1273.0	1340.5	1399.2	1431.6	1411.0	1412.2
Personal income	1154.9	1255.5	1381.6	1531.6	1717.4	1924.2	2110.3	2299.5
Wage and salary disbursements	764.6	805.9	890.0	984.0	1103.3	1227.6	1319.0	1416.1
Disposable personal income	984.6	1086.7	1184.5	1305.1	1458.4	1624.3	1782.3	1955.6
Saving rate (percent)	7.3	7.7	5.8	5.0	4.9	4.5	4.8	5.0
Corporate profits with I.V.A. and C.C. Adj.	83.6	95.9	126.8	150.0	167.7	178.2	149.6	157.2
Corporate profits before tax	126.9	120.4	156.0	177.1	206.0	236.6	216.3	222.5
Federal government surplus or deficit (N.I.A. basis)	-10.7	-70.6	-53.6	-46.3	-27.7	-11.4	-54.5	-72.8
High employment surplus or deficit (-)	9.1	-20.5	-16.2	-20.7	-12.7	7.5	11.9	31.5
State and local government surplus or deficit (-) (N.I.A. basis)	7.6	6.2	17.9	26.8	27.4	24.6	22.3	24.7
Excluding social insurance funds	-2.9	-6.2	2.3	7.3	4.2	-1.9	-7.8	-8.0
Civilian labor force (millions)	91.0	92.6	94.8	97.4	100.4	102.9	104.9	106.3
Unemployment rate (percent)	5.6	8.5	7.7	7.0	6.0	5.8	7.5	8.6
Nonfarm payroll employment (millions)	78.3	77.0	79.4	82.5	86.7	89.9	90.2	90.2
Manufacturing	20.1	18.3	19.0	19.7	20.5	21.1	20.1	19.6
Industrial production (1967=100)	129.3	117.8	130.5	138.2	146.1	152.2	144.0	140.4
Capacity utilization: all manufacturing (percent)	83.8	72.9	79.5	81.9	84.4	85.7	77.8	73.4
Materials (percent)	87.1	73.4	81.1	82.7	85.6	87.2	78.0	72.4
Housing starts, private (million units, A.R.)	1.34	1.16	1.54	1.99	2.02	1.75	1.19	1.35
New auto sales, (millions, A.R.)	8.91	8.66	10.12	11.13	11.28	10.70	8.93	9.41
Domestic models	7.49	7.08	8.63	9.07	9.29	8.38	6.53	6.95
Foreign models	1.42	1.58	1.50	2.06	1.99	2.32	2.40	2.46

^{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.

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

	1974	1975	1976	1977	1978	1979	Projected	
							1980	1981
<u>Constant (1972) dollars</u>								
Gross national product	-1.4	-1.3	5.9	5.3	4.4	2.3	-1.4	.1
Final purchases	-.7	.2	4.5	4.8	4.4	2.7	-.6	-.3
Private	-1.4	-.3	5.6	5.6	5.0	3.2	-1.2	-.4
Excluding net exports	-2.3	-1.0	6.5	6.2	5.0	2.6	-2.3	-.7
Personal consumption expenditures	-.9	1.8	5.9	5.0	4.5	2.6	-.9	-.3
Goods	-3.4	.7	6.9	5.1	4.1	1.3	-3.4	-2.0
Services	2.3	3.2	4.8	4.9	5.1	4.3	2.1	1.6
Gross private domestic investment	-11.4	-22.3	21.6	15.4	7.1	.4	-13.8	.1
Residential structures	-24.6	-13.9	23.3	20.7	4.2	-5.7	-22.6	6.7
Business fixed investment	-.3	-13.0	4.8	8.6	8.4	6.2	-3.2	-5.6
Gov't. purchases of goods and services	2.1	1.9	.2	2.0	1.8	.4	2.0	.1
Federal	-.8	.7	-.2	4.4	-2.0	.9	6.3	1.2
State and local	3.8	2.6	.5	.6	4.0	.2	-.5	-.5
Disposable personal income	-1.5	2.1	3.7	4.2	4.6	2.3	-.7	.1
<u>Current dollars</u>								
Gross national product	8.1	8.2	11.3	11.6	12.0	11.3	7.6	9.4
Final purchases	8.9	9.7	9.9	11.0	12.1	11.7	8.5	9.1
Private	8.1	9.1	10.8	11.3	12.7	12.3	7.6	9.1
Excluding net exports	8.2	7.8	12.0	12.7	12.6	11.8	7.4	8.8
Personal consumption expenditures	9.8	10.1	11.3	11.0	11.6	11.8	9.5	9.4
Goods	8.9	8.7	11.0	9.8	10.7	10.8	6.8	7.8
Services	11.1	11.8	11.7	12.5	12.7	12.9	12.5	11.1
Gross private domestic investment	-2.5	-11.0	27.3	24.8	15.9	10.2	-6.2	8.4
Residential structures	-16.7	-6.5	32.3	35.0	17.5	5.7	-15.4	16.2
Business fixed investment	10.8	-.3	9.8	14.9	16.7	15.2	5.4	2.5
Gov't. purchases of goods and services	12.3	11.8	6.8	9.7	9.9	9.4	11.8	8.9
Federal	8.7	10.7	5.4	11.3	5.7	9.2	16.7	11.1
State and local	14.5	12.5	7.5	8.7	12.4	9.5	9.1	7.6
Disposable personal income	9.2	10.4	9.0	10.2	11.7	11.4	9.7	9.7
Personal income	9.7	8.7	10.0	10.9	12.1	12.0	9.7	9.0
Wage and salary disbursements	9.0	5.4	10.4	10.6	12.1	11.3	7.4	7.4
Corporate profits with IVA & C.C. Adj.	-15.6	14.7	32.2	18.3	11.8	6.3	-16.0	5.1
Corporate profits before tax	9.6	-5.1	29.6	13.5	16.3	14.9	-8.6	2.9
Nonfarm payroll employment	2.0	-1.7	3.1	3.9	5.1	3.7	.3	.0
Manufacturing	-.4	-8.7	3.7	3.6	4.2	2.8	-4.7	-2.2
Nonfarm business sector								
Output per hour	-3.1	1.9	3.5	1.5	.5	-1.1	-1.5	.4
Compensation per hour	9.1	9.9	8.3	7.9	8.6	9.0	9.8	9.5
Unit labor costs	12.7	7.9	4.7	6.3	8.0	10.2	11.5	9.0
GNP implicit deflator	9.7	9.6	5.2	6.0	7.3	8.8	9.2	9.2
Gross domestic business product								
fixed-weighted price index ^{1/}	10.4	9.4	5.3	6.2	7.6	9.5	9.9	9.4
Excluding food and energy	8.1	9.5	5.8	6.3	7.2	8.1	7.9	7.8
Consumer price index (all urban)	11.0	9.1	5.8	6.5	7.7	11.3	13.4	10.1
Industrial production	-.4	-8.9	10.8	5.9	5.7	4.2	-5.4	-2.5

^{1/} Uses expenditures in 1972 weights.

FEDERAL SECTOR ACCOUNTS
(Billions of dollars)

August 6, 1980

	Fiscal Year 1979*	FY 1980 e/		FY 1981 e/2/		CY 1979*	CY80e/ F.R. Board	Calendar quarters; unadjusted data									FRB Staff Estimates		
		Admin. 1/	F.R. Board	Admin. 1/	F.R. Board			1979				1980					1981		
								IV*	I*	II*	III	IV	I	II	III				
																	1981		
Unified budget receipts	465.9	517.9	519.8	604.0	572.2	480.5	529.8	114.0	114.6	156.2	134.9	124.0	126.7	172.2	149.2				
Unified budget outlays	493.7	578.8	578.0	633.8	633.1	508.7	595.2	138.6	141.8	148.1	149.5	155.8	156.5	157.8	163.0				
Surplus(+)/deficit(-), unified budget	-27.7	-60.9	-58.2	-29.8	-60.9	-28.2	-65.4	-24.6	-27.2	8.2	-14.6	-31.8	-29.8	14.4	-13.8				
Surplus(+)/deficit(-), off-budget agencies 3/	-12.4	-16.1	-15.8	-21.7	-20.0	-13.2	-16.2	-1.0	-3.8	-4.4	-6.7	-1.3	-6.9	-6.6	-5.2				
Combined deficit to be financed	-40.2	-77.0	-73.9	-51.5	-80.9	-41.4	-81.6	-25.6	-31.0	3.8	-21.3	-33.1	-36.7	7.8	-19.0				
Means of financing combined deficits:																			
Net borrowing from public	33.7	69.7	67.2	45.8	74.5	37.3	79.4	18.9	19.1	5.4	23.8	31.1	25.7	-1.8	19.5				
Decrease in cash operating balance	-1.8	4.2	4.2	5.0	5.0	0.4	-0.1	8.3	7.7	-5.9	-5.9	4.0	8.0	-4.0	-3.0				
Other 4/	8.3	3.1	2.7	0.7	1.5	3.5	2.4	-1.7	4.1	-3.1	3.4	-2.0	3.0	-2.0	2.5				
Cash operating balance, end of period	24.2	20.0	20.0	15.0	15.0	15.9	16.0	15.9	8.2	14.1	20.0	16.0	8.0	12.0	15.0				
Memo: Sponsored agency borrowing 5/	19.1	16.2	22.4	16.7	14.2	25.5	18.2	7.5	7.7	5.3	1.9	3.3	2.9	4.0	4.0				
NIA Budget								Seasonally adjusted annual rates											
Receipts 6/	483.7	532.1	528.6	612.3	567.4	497.6	538.8	524.7	538.4	531.4	535.2	550.0	557.1	575.7	590.8				
Expenditures 6/	493.6	572.9	572.7	642.0	641.6	509.0	593.3	540.4	561.3	579.0	609.9	622.9	634.3	643.1	665.6				
Purchases (total)	162.4	188.4	188.0	211.3	210.5	166.6	194.5	178.4	186.2	192.5	195.0	204.1	208.5	212.6	216.8				
Defense	105.9	121.6	121.4	143.1	141.5	108.3	126.8	114.6	119.6	123.6	127.9	135.9	139.7	143.5	147.1				
Nondefense	56.5	66.8	66.6	68.2	68.9	58.4	67.7	63.8	66.6	68.9	67.1	68.2	68.8	69.1	69.7				
All other expenditures	331.2	384.5	384.7	430.7	431.1	342.4	398.8	362.0	375.1	386.5	414.9	418.8	425.8	430.5	448.8				
Surplus(+)/deficit(-) 6/	-9.9	-40.8	-44.1	-29.7	-74.2	-11.4	-54.5	-15.7	-22.9	-47.7	-74.7	-72.9	-77.3	-67.4	-74.8				
High employment surplus(+)/deficit(-) (NIA basis)	3.6	n.a.	7.9	n.a.	28.3	7.5	11.9	7.7	4.2	10.4	9.3	23.8	24.8	34.7	30.0				

*--actual e--estimated n.a.--not available

1. OMB Mid-Session Review of the 1981 Budget, July 1980 and BEA NIA translations, July 1980.
2. In the First Concurrent Resolution on the Budget, Fiscal Year 1981, June 1980, the Congress called for receipts of \$613.8 billion and outlays of \$613.6 billion.
3. Includes Federal Financing Bank, Postal Service Fund, Rural Electrification and Telephone Revolving Fund, Rural Telephone Bank, and Pension Benefit Guaranty Corporation.
4. Checks issued less checks paid, accrued items and other transactions.
5. FRB staff estimates include Federal Home Loan Banks, FNMA, Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives marketable debt on an offerings basis.
6. BEA NIA translations, July 1980. The fiscal year totals are based on unadjusted data and do not conform to the average of four seasonally adjusted quarters. The FRB staff estimates, therefore, have been adjusted in order to make the BEA and the staff estimates comparable.

DOMESTIC FINANCIAL DEVELOPMENTS

Summary. Market interest rates have increased since the July FOMC meeting, extending the rise that began in mid-June. The intermeeting increase in rates occurred toward the end of July when a tightening of bank reserve positions put upward pressure on the federal funds rate. With market expectations influenced by evidence of a strengthening of activity in some sectors of the economy and by rapid monetary expansion, market yields have generally increased $1/2$ to $3/4$ of a percentage point. Average rates on new mortgage commitments at S&Ls are up only slightly, however, and the prime rate has fallen $1/2$ percentage point since early July in lagged adjustment to earlier declines in market rates.

The monetary aggregates grew less during July than in the previous month, but the increases still were sizable. M-1A grew at a $7-3/4$ percent annual rate, lifting it closer to the lower bound of the FOMC target range for 1980. Another large increase in ATS accounts produced an 11 percent growth rate for M-1B and pushed it up to the lower limit of the FOMC's long-run range for this aggregate. With growth of the non-transactions component of M-2 registering only a slight deceleration from its June pace, M-2 expanded at a $16-1/4$ percent annual rate; this broader aggregate stands near the upper end of its longer-run range.

Among the components of M-2, overnight RPs, money market mutual funds, and savings deposits all registered strong growth during July, while small time deposits appear to have declined slightly, following only a small advance in June. Large time deposits continued to contract during July, and Eurodollar borrowing of member banks declined further. The drop in total managed liabilities at commercial banks,

however, was moderated by a pickup in other borrowings, particularly RPs.

Bank credit apparently increased somewhat in July. Partial data indicate additional acquisitions of securities, but a leveling out of total loans at commercial banks, after three months of substantial declines, also contributed to the strengthening of bank credit. Business loans at large banks increased during July, possibly by enough to more than offset what appears to be a continuing contraction at small banks. If so, business loans at all commercial banks in July would have increased for the first time since March. Meanwhile, perhaps reflecting the narrowing of the spread between the prime rate and open market rates, growth in commercial paper of nonfinancial firms apparently slowed. Overall short-term borrowing was limited, however, as firms continued to tap the bond and stock markets in volume.

Developments in mortgage markets have mirrored the recent pickup in housing activity. Although the loan portfolios of S&Ls contracted for the second consecutive month in June, mortgage commitments outstanding turned up for the first time since last September. Following a small decline in mortgage loans outstanding at commercial banks in June, partial bank data for July suggest the strongest expansion since March.

The paydown of consumer installment debt appears to be moderating. Although outstanding installment credit is estimated to have declined sharply again in June, loans to individuals at large commercial banks in July appear to have declined half as fast as in the month before. Some

easing of lending policies has been reported at large banks, but consumer credit conditions generally have remained relatively taut.

The Federal government borrowed heavily in July and early August. With the \$3.2 billion of net new funds raised in this week's three-part quarterly refunding operation, the Treasury's borrowing for the quarter to date has amounted to somewhat more than \$17 billion. Borrowing by federally sponsored credit agencies picked up in July to an estimated \$1-1/4 billion, seasonally adjusted, after virtually no change in June. Gross debt offerings by states and municipalities also rose on a seasonally adjusted basis, owing to enlarged bond sales to finance the construction and improvement projects of public utilities and to greater short-term security offerings.

Outlook. Credit demands are expected to strengthen further as nominal spending picks up over the months ahead, subjecting market interest rates to upward pressure. The Treasury, facing an enlarged deficit, will continue to borrow heavily in both the bill and coupon sectors of the market. Borrowing by state and municipal units is likely to remain high, given the existence of sizable operating deficits and the likely continued heavy issuance of housing revenue bonds.

Nonfinancial corporations should experience a continued narrowing of the financing gap as inventories are liquidated. Nevertheless, business borrowing is expected to increase as firms seek to bolster their liquidity positions. The pickup in borrowing may be concentrated at commercial banks, given the relatively more attractive prime rate now prevailing.

Mortgage lending by depository institutions is expected to grow as housing activity recovers. Even though federally-related lenders may reduce somewhat their role in the residential mortgage market, total mortgage credit flows are expected to rise in the months ahead. Mortgage interest rates may edge upward, reflecting the reaction of lending institutions to higher costs of funds and the now very narrow spread between primary and secondary mortgage yields.

Consumer installment debt is projected to continue to run off on net through the third quarter, although at a much more moderate pace. Consumers may well remain cautious in their spending and in their use of credit in light of economic uncertainties. At the same time, with delinquency rates and personal bankruptcies evidently on an uptrend, lenders are expected to maintain relatively taut loan policies, despite the ending of the credit restraint program.

Summary. During most of July the dollar fluctuated within a narrow range, but in the last week of the month the dollar came under some upward pressure. Over the five-week period since the last Greenbook, the weighted-average exchange rate of the dollar rose about 1 percent to almost the level at the beginning of the year. Recent movements in the dollar rate have reflected mainly relative interest rate shifts and expectations about the future course of monetary policy here and abroad. While U.S. short-term interest rates have tended to firm, rates in other major countries have continued on a downward path.

Net U.S. intervention over the period was negligible, with U.S. sales of dollars in the last week of July (primarily against German marks) offsetting purchases earlier in the month.

Recent data on industrial production abroad and other indicators show a general weakening of economic activity in the second quarter. At the same time, the rate of inflation has moderated further in most of the major foreign countries. With the exception of the United Kingdom and Canada, major countries abroad continued to register large current-account deficits.

Gross borrowing in international capital markets picked up sharply in the second quarter as dollar interest rates receded from their peaks; total borrowing in the first half was down about 10 percent from the high level of the comparable period in 1979. Within that total,

however, borrowing by industrial countries was up substantially while borrowing by the Communist countries and the non-oil developing countries was greatly reduced. In the LDC group, new credits to some of the largest borrowers (Brazil in particular) were cut back sharply as borrowing costs rose and lenders shifted toward countries with lower debt exposures.

The U.S. merchandise trade deficit in the second quarter was \$31 billion at an annual rate (international accounts basis), down about one-third from the first-quarter rate. Exports were about the same in the two quarters, but imports declined about 5 percent. Non-oil imports decreased 6 percent, with a sizable drop in imports of gold and silver; automotive imports from Canada were lower but such imports from Europe and Japan were about unchanged. Oil imports declined 3 percent from the first-quarter rate; a 12 percent drop in volume was nearly offset by rising prices, though import prices through June did not yet fully reflect the earlier OPEC price increases.

The main feature of U.S. international financial transactions beginning in March has been an outflow of funds through banks. In April and again in May the net outflow exceeded \$6 billion per month, as banking offices in the United States reduced their net Eurodollar borrowings, and the outflow appears to have accelerated somewhat in June. Partial data for July indicate further outflows. Placements of funds abroad by U.S. nonbanks have not been significant in recent months as the interest rate differential favoring dollar deposits abroad has declined. While foreign banking offices have loaned the bulk of their available funds to foreign customers, there has also

been a substantial increase in loans by foreign branches of member banks to U.S. nonbanks in recent months.

In international securities transactions, the heavy foreign purchases of U.S. corporate equities evident in the early months of the year faded out in the second quarter, while new issues of foreign bonds placed in the U.S. market have been on the rise.

Outlook. Projections of the U.S. trade and current accounts through 1981 have been modified only slightly in the past month -- the trade deficit is expected to decline into early 1981 and then to rise above the present level as the U.S. economy expands. On this projection, the U.S. trade deficit would be close to \$30 billion in each year of the 1977-81 period. Over this period, the other elements in the current account show sizable increases in net receipts, bringing the overall current account near to balance this year and to a small surplus next year. The main element underlying developments in the trade accounts is a sharper slowdown this year in the U.S. economy than is projected for other industrial countries and a somewhat stronger U.S. recovery during 1981.

The dollar has strengthened somewhat recently and the principal elements supporting that increase -- relative firmness of U.S. interest rates and a relatively satisfactory U.S. current account compared to that of other major countries -- are expected to contribute to some further gains over the year ahead.

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

	1979 ANN.	1980 ANN.	1981 ANN.	1980 Q I	1980 Q II ^p	1980 Q III ^p	1980 Q IV ^p	1981 Q I ^p	1981 Q II ^p	1981 Q III ^p	1981 Q IV ^p
1. GNP NET EXPORTS											
CURRENT \$, NET	-4.6	-0.6	6.1	-13.6	1.3	1.0	8.9	12.3	7.2	4.1	0.9
EXPORTS OF G&S	257.5	310.4	341.0	308.1	307.3	310.1	316.3	326.2	336.0	346.0	355.6
IMPORTS OF G&S	262.1	311.0	334.8	321.7	306.0	309.1	307.3	313.9	328.9	341.9	354.7
CONSTANT 72 \$, NET	17.6	29.5	32.7	25.0	29.3	30.5	33.3	33.7	32.9	32.5	31.9
EXPORTS OF G&S	119.9	128.0	128.0	131.7	128.7	126.0	125.5	126.0	127.2	128.8	129.9
IMPORTS OF G&S	102.3	98.5	95.3	106.7	99.4	95.6	92.2	92.3	94.4	96.3	98.0
TERMS OF TRADE (1972=100) 1/	83.8	76.8	75.8	77.6	77.6	76.1	75.6	76.1	75.8	75.7	75.7
2. U.S. MERCHANDISE TRADE BALANCE 2/											
EXPORTS (EXCL. MILITARY)	182.1	221.9	242.7	218.8	218.7	222.0	228.2	234.4	239.8	245.3	251.3
AGRICULTURAL	35.4	40.6	45.4	41.5	38.8	39.9	42.2	44.1	45.0	45.7	46.7
NONAGRICULTURAL	146.6	181.3	197.3	177.3	179.9	182.1	186.0	190.3	194.8	199.6	204.7
IMPORTS	211.5	254.9	273.0	262.3	249.8	254.8	252.7	256.5	268.4	278.4	288.6
PETROLEUM AND PRODUCTS	60.0	89.0	104.3	86.4	84.0	91.8	93.6	86.7	102.8	106.5	111.3
NONPETROLEUM	151.5	165.9	168.7	175.9	165.8	163.1	158.9	159.7	165.5	172.0	177.4
3. U.S. CURRENT ACCOUNT BALANCE											
OF WHICH: NET INVESTMENT INCOME	-0.8	0.0	4.3	-10.3	0.2	0.9	9.3	12.0	6.0	1.6	-2.3
	32.5	38.5	38.9	40.5	36.7	38.5	38.2	38.2	38.8	39.1	39.3
4. FOREIGN OUTLOOK - TEN INDUSTRIAL COUNTRIES 3/											
REAL GNP, % CHANGE, ANNUAL RATES	3.7	2.0	1.0	3.1	-0.9	0.4	0.3	1.0	1.5	2.2	2.4
CONSUMER PRICES, 4/, % CHANGE, ANNUAL RATES	7.8	11.7	8.7	14.5	12.5	9.8	9.2	8.6	7.9	7.2	6.8

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1/ GNP EXPORT IMPLICIT DEFLATOR DIVIDED BY GNP IMPORT IMPLICIT DEFLATOR.

2/ INTERNATIONAL ACCOUNTS BASIS.

3/ GEOMETRIC WEIGHTS USED TO AGGREGATE FOREIGN REAL GNP AND CONSUMER PRICES -- PER CENT SHARE IN TEN-COUNTRY TOTAL MULTILATERAL TRADE. CANADA (9.1%), JAPAN (13.6%), UNITED KINGDOM (11.9%), GERMANY (20.8%), FRANCE (13.1%), ITALY (9.0%), BELGIUM (6.4%), THE NETHERLANDS (8.3%), SWITZERLAND (3.6%), SWEDEN (4.2%).

4/ WHOLESALE PRICES FOR JAPAN.

P/ PROJECTED.