

Prefatory Note

The attached document represents the most complete and accurate version available based on original copies culled from the files of the FOMC Secretariat at the Board of Governors of the Federal Reserve System. This electronic document was created through a comprehensive digitization process which included identifying the best-preserved paper copies, scanning those copies,¹ and then making the scanned versions text-searchable.² Though a stringent quality assurance process was employed, some imperfections may remain.

Please note that this document may contain occasional gaps in the text. These gaps are the result of a redaction process that removed information obtained on a confidential basis. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

¹ In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

² A two-step process was used. An advanced optimal character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

CONFIDENTIAL (FR)
CLASS III - FOMC

March 24, 1989

SUPPLEMENT
CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Prepared for the
Federal Open Market Committee

By the Staff
Board of Governors
of the Federal Reserve System

TABLE OF CONTENTS

	Page
THE DOMESTIC NONFINANCIAL ECONOMY	
Revised GNP data for the fourth quarter of 1988.	1
Personal income and consumption.	1
Sales of existing homes	4
<u>Tables</u>	
Real gross national product and related items	2
Personal income	3
Real personal consumption expenditures	3
Private housing activity	5
THE FINANCIAL ECONOMY	
<u>Tables</u>	
Monetary aggregates	6
Commercial bank credit and short- and intermediate-term business credit	7
Selected financial market quotations	8
ADDENDUM:	
Summary of President Bush's Budget Plan for 1990 and Recent Budget Developments	A-1

SUPPLEMENTAL NOTES

DOMESTIC NONFINANCIAL ECONOMY

Revised GNP data for the fourth quarter of 1988

Real GNP grew 2.4 percent at an annual rate in the fourth quarter of 1988 according to BEA's final (third) report, an upward revision of 0.4 percentage point from the preliminary estimate; excluding drought effects, real GNP advanced 3.5 percent last quarter. Among the components of GNP, there were upward revisions to government purchases and to outlays for producers' durable equipment, which more than offset a sharper decline in net exports than had been reported previously. In contrast, only slight adjustments were made to consumer spending, residential investment, and inventory accumulation. On the price side, the estimated increase in the GNP fixed-weight price index--4.2 percent at an annual rate--was the same as in the preliminary GNP report. The rate of increase in the implicit price deflator for GNP, at 5.3 percent, also was the same as was reported previously. Fourth-quarter corporate profits--reported for the first time in the latest GNP release--posted a sizable gain, and the profit share edged up to 6.8 percent.

Personal income and consumption

The growth of personal income remained strong in February. In nominal terms, personal income increased \$42.4 billion last month, following a \$72.1 billion rise in January. Part of the February advance reflected a large increase in subsidy payments to farm proprietors. Excluding these payments, personal income increased \$30.1 billion. Private wages and salaries rose \$11.8 billion in February, about in line with increases over

REAL GROSS NATIONAL PRODUCT AND RELATED ITEMS

(Percent change from previous period at compound annual rates;
based on seasonally adjusted data)

	1987-Q4 to 1988-Q4	1988-Q3	1988-Q4	
		Final	Prelim.	Final
1. Gross national product	2.8	2.5	2.0	2.4
1a. Excluding drought effects	3.5	3.0	3.1	3.5
2. Final sales	3.9	2.0	3.1	3.5
2a. Excluding CCC purchases	4.1	2.0	2.5	2.8
3. Consumer spending	3.7	3.9	3.5	3.5
3a. Excluding motor vehicles	3.5	4.2	3.5	3.6
4. Business fixed investment	5.7	4.0	-4.6	-2.9
4a. Producers' durable equipment	10.0	4.6	-5.9	-3.5
4b. Structures	-5.0	2.6	-3	-1.0
5. Residential structures	2.0	4.3	10.9	10.9
6. Federal purchases	-3.5	-13.2	16.8	20.7
6a. Defense	-2.1	-10.5	7.5	9.9
7. State and local purchases	3.4	1.1	5.1	6.0
8. Exports of goods and services	13.7	14.5	7.7	6.5
9. Imports of goods and services	7.2	13.1	13.0	13.5

ADDENDA:				
10. Inventory change ¹	42.5 ²	39.5	29.3	29.1
10a. Nonfarm ¹	40.0 ²	40.4	37.7	37.6
10b. Farm ¹	2.5 ²	-8	-8.3	-8.5
11. Net exports ¹	-100.2 ²	-93.9	-103.3	-105.4
12. Nominal GNP	7.2	7.3	7.2	7.6
13. GNP implicit price deflator	4.3	4.7	5.3	5.3
14. GNP fixed-weight price index	4.5	5.3	4.2	4.2
15. Real disposable personal income	3.6	5.6	4.8	4.1
16. Saving rate (percent)	4.2 ²	4.2	4.5	4.3
17. Profit share (percent)	6.7 ²	6.7	n.a.	6.8

1. Level, billions of constant dollars.
2. Annual average.

PERSONAL INCOME

	1988		1988	1989	
	Q3	Q4	Dec.r	Jan.r	Feb.p
<i>--- Average monthly change, billions of dollars ---</i>					
1. Personal income	23.3	28.7	35.6	72.1	42.4
2. Wage and salary disbursements	15.8	18.2	15.4	28.9	14.2
3. Proprietors' income	-2.6	1.0	11.7	26.7	16.1
3a. Farm proprietors' income	-4.4	-1.4	9.6	23.9	15.0
4. Personal interest income	6.8	7.3	7.4	8.6	8.8
5. Transfer payments	2.0	2.7	1.4	15.2	2.0
6. Other income	1.2	-2	-5	-7.3	1.3
7. Personal tax and nontax payments	3.2	4.0	4.0	11.7	2.7
8. Disposable personal income	20.1	24.7	31.6	60.4	39.8

r = revised p = preliminary

REAL PERSONAL CONSUMPTION EXPENDITURES

	1988		1988	1989	
	Q3	Q4	Dec.r	Jan.r	Feb.p
<i>--- Percent change from preceding period ¹ ---</i>					
1. Personal consumption expenditures	3.9	3.5	.3	-.3	.4
2. Durable goods	-.2	6.1	3.9	-3.8	-.2
3. Nondurable goods	5.0	1.3	-1.2	1.0	-.1
4. Services	4.5	4.2	.2	.0	.9

1. Quarterly changes are at annual rate.

r = revised p = preliminary

the past year. Among the nonwage components of income, the rise in farm subsidies accounted for most of a \$15 billion rise in farm income. Personal interest income rose \$8.8 billion, while other components of nonwage income showed only modest increases. The big gains in nominal income in January and February were only partly offset by price increases, and in real terms, the average level of disposable income for the two months was about 1.7 percent above the fourth-quarter average (not at an annual rate).

Real personal consumption expenditures increased 0.4 percent in February, following a decline of 0.3 percent in January. Spending for goods edged down in February, as real purchases of gasoline and oil fell more than \$4 billion at an annual rate. In the durable goods category, spending on new cars and trucks was about flat in real terms, but net purchases of used cars declined roughly \$1 billion. Outlays for services rose sharply, largely reflecting a rebound in purchases of electricity and natural gas from January's weather-depressed figure.

Sales of existing homes

Sales of existing homes fell 3 percent in February from a downward-revised January pace to 3.44 million units at an annual rate. The February decline in home sales was concentrated mainly in the Northeast. In other regions, sales of existing homes were little changed in February, but were down from their strong pace in the fourth quarter of 1988. The median price of resold homes was \$93,100 in February--up 4.7 percent from a year earlier. The average sales price was \$119,400, up 7.7 percent over the year. (These price data are not adjusted for changes in quality or regional mix.)

PRIVATE HOUSING ACTIVITY
(Seasonally adjusted annual rates; millions of units)

	1988	1988			1988	1989	
	Annual	Q2	Q3	Q4 ^r	Dec. ^r	Jan. ^r	Feb. ^p
All units							
Permits	1.45	1.46	1.43	1.53	1.57	1.51	1.40
Starts	1.49	1.48	1.47	1.56	1.58	1.69	1.50
Single-family units							
Permits	1.00	.98	.99	1.05	1.08	1.06	.99
Starts	1.08	1.06	1.06	1.14	1.14	1.20	1.05
Sales							
New homes	.68	.69	.70	.68	.67	.70	n.a.
Existing homes	3.59	3.64	3.66	3.77	3.92	3.55	3.44
Multifamily units							
Permits	.45	.48	.43	.48	.48	.44	.42
Starts	.41	.42	.41	.42	.44	.49	.45

p--preliminary estimates. r--revised. n.a.--not available.

MONETARY AGGREGATES
(based on seasonally adjusted data unless otherwise noted)

	1988 ¹	1988 Q3	1988 Q4	1988 Dec	1989 Jan	1989 Feb p	Growth Q4 88- Feb 89p
-----Percent change at annual rates-----							
1. M1	4.3	5.2	2.3	5.5	-6.1	1.8	0.0
2. M2	5.2	3.8	3.6	4.0	-1.3	1.7	1.8
3. M3	6.3	5.7	5.0	5.4	1.6	3.2	3.5

	-----Percent change at annual rates-----						Levels bil. \$ Feb 89p
<u>Selected components</u>							
4. M1-A	2.5	3.3	1.7	5.2	-6.9	3.8	506.6
5. Currency	8.1	7.5	6.6	7.4	9.1	5.1	214.3
6. Demand deposits	-1.2	0.4	-1.8	3.8	-19.1	3.4	284.8
7. Other checkable deposits	7.7	8.7	3.3	5.6	-4.7	-1.7	280.8
8. M2 minus M1 ²	5.5	3.3	4.1	3.5	0.3	1.7	2282.9
9. Overnight RPs and Eurodollars, NSA	-5.9	-3.0	-9.2	44.6	52.2	-36.8	79.1
10. General purpose and broker/dealer money market mutual fund shares, NSA	7.5	-2.9	9.7	11.1	12.0	29.3	247.9
11. Commercial banks	6.9	5.5	6.8	5.7	2.8	4.5	993.9
12. Savings deposits, SA, plus MMDAs, NSA ³	1.4	1.0	-1.8	-4.2	-12.8	-14.2	532.7
13. Small time deposits	14.7	11.6	18.0	18.1	21.9	26.9	461.2
14. Thrift institutions	4.6	2.3	0.3	-2.1	-3.3	-5.2	964.4
15. Savings deposits, SA, plus MMDAs, NSA ³	-4.3	-2.0	-8.6	-7.7	-16.3	-21.3	377.0
16. Small time deposits	11.7	5.4	6.6	1.7	5.4	5.1	587.3
17. M3 minus M2 ⁴	10.6	13.1	10.2	10.3	12.4	8.3	863.2
18. Large time deposits	11.0	13.4	11.3	7.4	14.7	15.7	551.4
19. At commercial banks, net ⁵	12.2	18.1	13.0	12.3	18.7	24.3	378.1
20. At thrift institutions	8.8	4.1	8.0	-2.1	5.6	-2.1	173.4
21. Institution-only money market mutual fund shares, NSA	-0.8	-23.3	10.9	2.7	23.3	4.0	89.6
22. Term RPs, NSA	15.0	13.0	8.4	-33.5	14.4	28.4	129.8
23. Term Eurodollars, NSA	13.3	45.6	11.0	40.5	-57.0	-9.4	101.4

-----Average monthly change in billions of dollars-----

MEMORANDA:⁶

24. Managed liabilities at commercial banks (25+26)	4.9	4.5	4.5	0.7	0.3	10.3	653.2
25. Large time deposits, gross	3.3	5.5	3.1	4.6	5.8	5.5	440.4
26. Nondeposit funds	1.7	-1.0	1.4	-3.9	-5.5	4.8	212.8
27. Net due to related foreign institutions, SA	-0.4	0.0	-0.5	-2.6	1.3	2.7	10.6
28. Other ⁷	2.1	-1.0	1.9	-1.3	-6.8	2.1	202.2
29. U.S. government deposits at commercial banks ⁸	0.0	0.5	0.5	1.9	-4.6	0.0	20.3

1. Amounts shown are from fourth quarter to fourth quarter.
 2. Nontransactions M2 is seasonally adjusted as a whole.
 3. Commercial bank savings deposits excluding MMDAs grew during January and February at rates of -10.6 percent and -2.5 percent, respectively. At thrift institutions, savings deposits excluding MMDAs grew during January and February at rates of -9 percent and -13.7 percent, respectively.
 4. The non-M2 component of M3 is seasonally adjusted as a whole.
 5. Net of large denomination time deposits held by money market mutual funds and thrift institutions.
 6. Dollar amounts shown under memoranda are calculated on an end-month-of-quarter basis.
 7. Consists of borrowing from other than commercial banks in the form of federal funds purchased, securities sold under agreements to repurchase, and other liabilities for borrowed money (including borrowing from the Federal Reserve and unaffiliated foreign banks, loan RPs and other minor items). Data are partially estimated.
 8. Consists of Treasury demand deposits and note balances at commercial banks.
- p - preliminary

COMMERCIAL BANK CREDIT AND SHORT- AND INTERMEDIATE-TERM BUSINESS CREDIT*
(Percentage changes at annual rates, based on seasonally adjusted data)¹

	1987:Q4	1988			1989		Levels
	to 1988:Q4	Q3	Q4	Dec.	Jan.	Feb.	bil.\$ Feb.
----- Commercial Bank Credit -----							
1. Total loans and securities at banks	7.3	5.1	6.1	3.7	2.4	14.4	2441.8
2. Securities	4.7	2.2	5.0	3.3	-11.9	4.6	551.9
3. U.S. government securities	7.4	5.0	10.4	13.1	-2.0	5.3	363.4
4. Other securities	.2	-2.6	-5.1	-14.7	-30.5	3.2	188.5
5. Total loans	8.1	6.0	6.4	3.8	6.7	17.3	1889.9
6. Business loans	6.3	3.5	4.0	1.6	9.6	24.0	616.6
Security loans	-6.2	-28.4	13.1	.0	-28.5	227.0	44.0
8. Real estate loans	13.4	12.8	11.0	10.0	11.6	12.7	678.3
9. Consumer loans	8.6	6.4	8.3	9.5	5.7	3.0	357.9
10. Other loans	.2	-1.8	-5.9	-20.6	-16.0	-1.2	193.1
----- Short- and Intermediate-Term Business Credit -----							
11. Business loans net of bankers acceptances	6.4	3.6	4.1	2.0	9.7	24.5	613.7
12. Loans at foreign branches ²	30.3	20.1	13.4	11.2	-38.9	28.7	21.4
13. Sum of lines 11 & 12	7.1	4.2	4.4	2.3	8.0	24.7	635.1
14. Commercial paper issued by nonfinancial firms	15.6	-.9	50.1	82.7	57.4	22.4	109.3
15. Sum of lines 13 & 14	8.2	3.5	10.3	13.1	15.0	24.3	744.4
16. Bankers acceptances: U.S. trade related ^{3,4}	-6.8	-6.0	11.0	36.9	17.9	28.2	34.8
17. Line 15 plus bankers acceptances: U.S. trade related	7.4	3.0	10.3	14.0	15.4	24.4	779.2
18. Finance company loans to business ³	12.4	10.9	12.7	7.7	4.6	n.a.	235.3 ⁵
19. Total short- and intermediate-term business credit (sum of lines 17 & 18)	8.5	4.9	10.9	12.6	12.6	n.a.	998.8 ⁵

1. Average of Wednesdays.

2. Loans at foreign branches are loans made to U.S. firms by foreign branches of domestically chartered banks.

3. Based on average of data for current and preceding ends of month.

4. Consists of acceptances that finance U.S. imports, U.S. exports, and domestic shipment and storage of goods.

5. January data.

p--preliminary.

n.a. not available.

*Data reflect benchmarking to the June 1988 call report and new seasonal adjustments.

SELECTED FINANCIAL MARKET QUOTATIONS 1/
(percent)

	1987		1988	1989	1989	Change from:
	Jan-Feb lows	2/ Oct 16	Feb lows	FOMC Feb 8	Mar 23	FOMC Feb 8
Short-term rates						
Federal funds 3/	5.95	7.59	6.38	9.13	9.85	0.72
Treasury bills 4/						
3-month	5.30	6.93	5.59	8.53	9.04	0.51
6-month	5.31	7.58	5.77	8.47	9.02	0.55
1-year	5.35	7.74	6.10	8.44	8.93	0.49
Commercial paper						
1-month	5.81	7.94	6.41	9.11	9.98	0.87
3-month	5.73	8.65	6.45	9.17	10.06	0.89
Large negotiable CD's 4/						
1-month	5.85	7.92	6.44	9.15	9.98	0.83
3-month	5.80	8.90	6.49	9.29	10.18	0.89
6-month	5.78	9.12	6.55	9.44	10.56	1.12
Eurodollar deposits 5/						
1-month	6.00	8.00	6.44	9.25	10.00	0.75
3-month	6.00	9.06	6.50	9.38	10.25	0.87
Bank prime rate	7.50	9.25	8.50	10.50	11.50	1.00
Intermediate- and long-term rates						
U.S. Treasury (constant maturity)						
3-year	6.34	9.52	7.28	9.19	9.76	0.57
10-year	7.01	10.23	8.11	8.95	9.43	0.48
30-year	7.29	10.24	8.32	8.82	9.23	0.41
Municipal revenue 6/ (Bond Buyer index)	6.92	9.59	7.76	7.58	7.95	0.37
Corporate—A utility Recently offered	8.78	11.50	9.63	10.05	10.46	0.41
Home mortgage rates 7/						
Fixed-rate	9.10	11.58	9.84	10.55	10.98	0.43
ARM, 1-year	7.52	8.45	7.59	8.56	9.02	0.46
	1986	1987		1989	1989	Percent change from:
	Year end	Record highs	Lows	FOMC Feb 8	Mar 23	FOMC Feb 8
Stock prices						
Dow-Jones Industrial	1895.95	2722.42	1738.74	2343.21	2243.04	-4.27
NYSE Composite	138.58	187.99	125.91	167.69	162.64	-3.01
AMEX Composite	263.27	365.01	231.90	327.23	324.87	-0.72
NASDAQ (OTC)	348.83	455.26	291.88	407.97	400.94	-1.72

1/ One-day quotes except as noted.

2/ Last business day prior to stock market decline on Monday Oct. 19, 1987.

3/ Average for two-week reserve maintenance period closest to date shown except lows shown which are one-week averages ending Feb. 25 and Feb. 10, respectively. Last observation is average for maintenance period ending March 22, 1989.

4/ Secondary market.

5/ Bid rates for Eurodollar deposits at 11 a.m. London time.

6/ Based on one-day Thursday quotes and futures-market index changes.

7/ Quotes for week ending Friday closest to date shown.

e—estimate

SUMMARY OF PRESIDENT BUSH'S BUDGET PLAN FOR 1990
AND RECENT BUDGET DEVELOPMENTS

President Bush presented his proposed budget priorities in a document, Building A Better America, that accompanied his February 9 message to Congress. The aggregate budget goals and underlying economic assumptions are presented in table 1.¹ CBO's analysis of President Bush's budget proposals was presented early in March. The biggest issue raised by CBO about the administration's budget estimates related to the accounting for the President's proposed resolution of the thrift crisis. In Congress, hearings are proceeding on the thrift proposal, and congressional leadership and administration representatives are just finishing a round of negotiations before the Budget Committees begin to formulate the Congressional Budget Resolution.

The President's budget document emphasizes limiting the year-to-year growth in spending to no more than the available growth in receipts, less the amount necessary to reduce the deficit from almost \$165 billion for FY1989 (\$171 on a GRH accounting basis) to the \$100 billion level mandated by the Gramm-Rudman law for FY1990. Consequently, the plan for FY1990 calls for an increase in spending (excluding the effects of asset sales) of only \$11 billion. After allowing for some reduction in asset sales between FY1989 and FY1990, total net outlays rise by \$14 billion, about matching the restrained advance in FY1987 and less than one-quarter the average year-to-year rise for the period 1980 through 1988. With such substantial

1. The economic assumptions that had been used in the Reagan Administration budget submitted in January were slightly modified, in light of incoming data, and the FY1989 budget estimate was revised, mainly to reflect the greater-than-anticipated surge in FSLIC activity in December.

restraints on spending and an anticipated increase of \$81 billion in receipts under existing tax laws, the deficit could be reduced to \$100 billion, even without the estimated \$5.6 billion revenue gain from proposed legislation. After allowing for this gain and for asset sales, the President proposes a FY1990 deficit of \$91 billion.

The largest boost to revenues from proposed changes in tax law (\$4.8 billion) is estimated to result from a reduction in the capital gains tax rate for selected assets. In addition, proposals are made (as in President Reagan's January Budget) for extension of the Medicare payroll tax to state and local employees not now covered and for retention of aviation-related taxes that would expire under current law. President Bush also proposes some revenue reductions, mainly larger tax breaks for research and experimentation costs. (His child-care tax credit results almost entirely in a small addition to outlays, rather than a loss of receipts, because it is refundable and leads to cash payments to low-income beneficiaries.)

On the spending side, the President's document does not specify all policy changes necessary to arrive at the outlay total that he endorses. Rather, it lays out a series of principles for determining subtotals for major blocks of the budget and identifies key priorities. Military outlays are estimated on the basis of holding appropriations constant in real terms for FY1990; in addition, an increase of \$0.7 billion for the "clean-up" of atomic weapons production is recommended. This results in a year-to-year increase in total defense spending of \$2.1 billion from FY1989 to FY1990, as shown in table 2. Income security programs, such as Social security and unemployment compensation, and key "means-tested" entitlements (the safety

net programs for the poor) are to be "fully funded"--that is, spending is estimated to grow as required to meet the increase in the recipient population and the cost-of-living adjustments specified in the current law.

Other existing, and some new, programs are identified as "areas of priority initiative spending. The Bush figures indicate proposed nominal increases in these categories relative to the FY1989 levels of \$11.7 billion. The Board staff estimates this increase to be about \$3.5 billion relative to current services levels for FY1990. The major priority areas were identified as: (a) investment projects in NASA and National Institute of Health; (b) education programs, principally involving small amounts of spending for initiatives to encourage excellence in teaching and student performance; (c) programs for ending drug abuse and increasing law enforcement; (d) environmental programs to curb acid rain and promote land and water conservation; (e) welfare programs, primarily related to homelessness and increased effectiveness of Medicaid; (f) spending for the Federal Aviation Administration; and (g) international affairs.

The Bush budget identifies specific program cuts from current services amounting to almost \$15 billion. Within this total, \$11.8 billion of cuts are concentrated in Medicare, federal employee health benefits, federal lump-sum retirement benefits, and farm price supports; a one-year freeze on COLAs in federal retirement benefits would save \$1.4 billion. Proposals to shift from direct loans to guaranteed loans or vouchers in a number of agricultural credit and rural housing programs are estimated to save an additional \$1.7 billion.

The President's plan explicitly incorporates the proposed reform of deposit insurance and off-budget financing for rapid resolution of insolvent

thrift institutions; it also reflects the growth of interest outlays and proposes to raise offsetting receipts by sale of some public activities to the private sector. Remaining programs are not considered specifically; the Board staff estimates that outlays for these programs would be required to decline by about \$5 billion between FY1989 and FY1990 to meet the President's aggregate spending objective. Such a decline would reduce them about \$11 billion below the level that would result if current laws were retained and spending levels for discretionary programs were raised enough to compensate for projected inflation.² Overall, outlays (excluding loan asset sales) proposed for FY1990 are shown in table 2 to be about \$27 billion below the current services total reported in the January budget document (adjusted for the revisions to economic assumptions).³

The Congressional Budget Office has prepared an analysis of President Bush's budget plan that was presented early in March in testimony by CBO Director Robert Reischauer. In his testimony, he noted that the economic and technical assumptions that CBO used in preparing its own baseline (essentially current services) budget projections would add a total of \$17 billion to the FY1990 budget deficit projected by OMB. CBO's baseline budget estimates and economic projections are shown on table 3. CBO's

2. A significant part of the year-to-year decline and the reduction from current services in the residual program category could be accomplished by the President's proposals for increases in offsetting collections from service fees and charges, and leasing. In total, these increases are estimated to amount to \$5.2 billion in FY1990.

3. It is difficult to estimate the magnitude of the Bush budget proposals in NIPA terms without more detail--including determination of the unspecified components of the proposal that have been left for negotiation with Congress. It appears likely, however, that as much as \$25 billion of the outlay reduction from current services could be reflected in NIPA terms. On the receipts side, proposed changes are very small except for the highly controversial effects of the proposed change in the capital gains tax. These changes in tax law would be reflected in the NIPA accounts.

projection of higher interest rates than anticipated by the administration accounts for essentially all of the \$9 billion net contribution of economic assumptions to their higher FY1990 deficit; CBO's higher inflation projection raises receipts and costs of indexed benefit programs by roughly offsetting amounts. CBO's estimates of spending for defense and by FDIC account for most of the \$8 billion technical difference with the administration.⁴

Allowing for these economic and technical differences would raise the President's estimated deficit (excluding asset sales) from \$95 billion to \$112 billion. Apart from the effects of the thrift proposal, CBO's reestimates imply \$26 billion of deficit reduction in the President's proposed budget for FY1990, or roughly \$7 billion less than implied in the administration's projections. This difference is almost entirely accounted for by CBO's expectation of smaller increases in receipts from the President's proposed changes in capital gains taxes and their conclusion that anticipated new leasing income could not be realized in 1990.

The President's proposal for resolving the savings and loan industry problems would provide for substantially more spending than in the CBO baseline but would also bring in modest amounts of additional income, both from higher deposit insurance premiums and from sources such as FHLB earnings. CBO estimates that this proposal would result, on net, in FY1990 outlays of \$22 billion, before allowing for the proposed offsetting receipts of \$25 billion from the Resolution Financing Corporation (REFCORP). CBO questions the off-budget status of this new financing agency in the

4. Estimates of FSLIC outlays are considered separately by CBO and are discussed below.

President's plan. If the President's plan were fully implemented and incorporated in the budget as he proposed, however, the FY1990 deficit would be reduced to \$109 billion, according to CBO.

The issue of the off-budget status of REFCORP has been raised in hearings on the thrift proposal. Several alternatives to the administration's plan also have been suggested. These include: (a) shifting the timing of budget outlays for thrift resolutions so as to avoid adding to difficulties in meeting the Gramm-Rudman targets for FY1990 and (b) providing some form of exemption from Gramm-Rudman accounting for extraordinary thrift resolution outlays. Like the administration's proposal, these alternatives are designed to avoid a sequester.

General budget negotiations also have been underway between senior representatives of the administration and the Budget Committees. Before leaving for the Easter recess, these negotiators reported to the President in a March 23 letter that a number of budget options had been considered and progress had been made on technical issues. It was noted, however, that policy differences remain and that it would be "essential to resume negotiations after the Easter break."

Table 1

BUSH ADMINISTRATION FEDERAL BUDGET PROPOSALS
(Billions of dollars)

	Fiscal years					
	1989	1990	1991	1992	1993	1994
Outlays	1150	1160	1212	1249	1284	n.a.
Receipts	979	1066	1148	1219	1287	n.a.
Deficit, excluding asset sales	171	95	64	31	-3	n.a.

Source: Building a Better America, February 9, 1989.

* In testimony before the House Budget Committee on February 22, OMB Director Darman revised the FY1989 administration outlay total upward by \$0.4 billion. The FY1989 deficit, excluding asset sales, now rounds to \$171 billion.

BUSH ADMINISTRATION ECONOMIC ASSUMPTIONS

	Calendar years					
	1989	1990	1991	1992	1993	1994
	-----Percent change, Q4 to Q4-----					
Nominal GNP	7.3	7.0	6.4	5.8	5.3	4.7
Real GNP	3.5	3.4	3.3	3.2	3.2	3.2
GNP deflator	3.7	3.5	3.0	2.5	2.0	1.5
	-----Percent, annual average-----					
Civilian unemployment rate	5.3	5.2	5.0	5.0	5.0	5.0
Interest rate						
(3-month Treasury bills)	7.4	5.5	4.5	4.0	3.5	3.0
(10-year Treasury Notes)	8.6	7.2	6.0	5.0	4.5	4.0

Source: OMB, Revised Economic Assumptions for the Bush Budget, February 9, 1989.

Table 2

SUMMARY OF BUSH BUDGET PLAN FOR FY1990
(Billions of dollars)

	FY1989	FY1990	1990	
			Year-to-year	Change From current services ¹
Receipts	979.3	1065.6	+86.3	5.6
Outlays				
<u>Defense</u>	298.2	300.3	+2.1	-.6 ²
<u>Income security--</u> Social security, unemployment comp., veterans pensions, and means-tested programs.	314.4	330.9	+16.5	.0
<u>Priority spending--</u> Science, conservation, education, drugs, crime prevention, Medicaid, and interna- tional affairs.	104.4	116.1	+11.7	+3.5e
<u>Specified programs with</u> <u>cuts from current</u> <u>services--farm price</u> support and credit, Medicare, federal employee health and retirement.	167.3	165.5	-1.8	-14.8
<u>Deposit insurance</u> ³	14.7	.4	-14.3	-.3
<u>Interest</u>	168.8	173.3	+4.5	-1.1
<u>Offsetting receipts</u>	-36.9	-39.6	-2.7	-2.7
<u>All other spending</u>	<u>118.6</u>	<u>113.5</u>	<u>- 5.1</u>	<u>-11.3</u>
Total ⁴	1149.5	1160.4	+10.9	27.3
Deficit	-170.2	-94.8	+75.4	-32.9
Deficit, with asset sales	-163.3	-91.1	+72.2	n.a.

e--estimated by the staff.

1. Current services as estimated in the January budget documents, adjusted for changes in economic assumptions.

2. Reduction in outlays from current services is in parts of the defense function other than the military functions of the Department of Defense and the nuclear waste clean-up activities in the Department of Energy.

3. Deposit insurance estimates include all aspects of the President's thrift resolution proposal as estimated February 9; current services estimate was preliminary.

4. Outlays before asset sales, which are estimated to amount to \$6.9 billion in FY1989 and \$3.7 billion in FY1990.

Table 3

CBO BASELINE BUDGET ESTIMATES¹
(Billions of dollars)

	Fiscal years					
	1989	1990	1991	1992	1993	1994
Outlays	1142	1215	1287	1348	1416	1489
Receipts	983	1069	1140	1209	1280	1359
Deficit	159	146	146	140	135	130

CBO ECONOMIC ASSUMPTIONS

	Calendar years					
	1989	1990	1991	1992	1993	1994
	-----Percent change, year-to-year-----					
Nominal GNP	7.2	6.4	6.5	6.4	6.4	6.5
Real GNP	2.9	2.1	2.2	2.2	2.3	2.3
GNP deflator	4.2	4.2	4.2	4.1	4.1	4.1
	-----Percent, annual average-----					
Civilian unemployment rate	5.5	5.5	5.5	5.6	5.6	5.6
Interest rate (Treasury bills)	7.9	7.1	6.7	6.4	6.1	5.9
(Treasury notes)	9.3	9.0	8.6	8.1	7.7	7.4

Source: CBO, An Analysis of President Reagan's Budgetary Proposals for Fiscal Year 1990, (February 1989).

1. CBO projections assume that revenues and outlays evolve according to laws now on the statute books, and that defense and nondefense discretionary appropriations are held constant in real terms.