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Strictly Confidential (FR) Class II FOMC

Part 1

December 16, 1998

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

Strictly Confidential (FR) Class II FOMC

December 16, 1998

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee
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Domestic Developments

Overview

The information that we have received in the brief interval since the last Greenbook suggests that the economic expansion has remained robust through the autumn months. We have raised our forecast of real GDP growth in the fourth quarter a full percentage point, to more than 3 percent, and the indications of ongoing support for robust final demand have led us to add several tenths to our prediction of the output gain in 1999. However, despite the higher levels of resource utilization that accompany this stronger outlook, our projection for inflation is only marginally higher; in part, this reflects still another favorable surprise from the commodity markets, where the prices of oil and other materials have plunged further because of excess world capacity and the weakness in the Asian and Latin American economies.

We still think it likely that the expansion will slow over the coming months, most probably to a pace that is below the trend rate of growth in potential output. Underlying that projection is the notion that "accelerator" effects have been important in pushing investment in consumer durables, homes, and business equipment to very high levels; going forward, the abatement of these effects should be an important moderating force on the economy.

But, clearly, our tune has changed materially from that of a few months ago when, in the midst of the financial market turmoil, we thought that growth might come almost to a halt in the first half of 1999. The biggest difference: Monetary policy has eased more rapidly than we assumed in the earlier forecasts, and the effects have been magnified by the wildly enthusiastic response of the equity markets. The upside risks that we noted in recent Greenbooks--and gauged in some of our model simulations--have, in effect, been realized. Even maintaining the view that poor corporate earnings will dent share prices in coming months, we have a considerably more accommodative financial environment than was built into our baseline projections in the last couple of Greenbooks.

We are now predicting that, with no further changes in the federal funds rate, real GDP will rise 2 percent or so in 1999 and about 2-1/4 percent in 2000. Given this path for production, the demand for labor should be sufficient to hold the overall unemployment rate below 5 percent. We continue to think that wage increases have topped out--a notion at least not contradicted by the latest monthly readings on average hourly earnings. However, the stronger economy and tighter labor market in this forecast have left us no room to pass the recent declines in commodity prices into the outlook for core and overall inflation: We continue to expect about a 3/4 percentage point step-up in inflation in 1999 and then little further change in 2000.

Key Background Factors in the Staff's Economic Forecast

Interest rates on intermediate- and long-term Treasuries have fallen roughly 1/4 percentage point, on net, since the November FOMC meeting. Although the bulk of the incoming news on economic activity has suggested that growth is holding up better than expected, the markets seem to have been more heavily influenced by the softness in the prices of oil and other commodities and by further indications of weakness in manufacturing; these developments have raised expectations of additional easing by the FOMC sometime in the first half of 1999. Renewed concern about foreign economies, especially Brazil, also appears to have affected Treasury rates in the past couple of weeks, with skittish investors turning once again to the greater safety of government securities.

As noted above, we are assuming no further easing steps in this forecast. The failure of the Fed to be as generous as the market is hoping and an ebbing of the risk aversion and liquidity preference still apparent today will tend to push Treasury yields somewhat higher in coming months. However, in private securities markets, a return to more realistic quality spreads should permit rates to hold steady or even decline--especially as year-end tensions pass. Most borrowers appear to have found a way to obtain credit in the aftermath of the recent turmoil, and we are assuming that the vast majority of businesses and households will continue to have good access to credit moving forward.

In equity markets, the rally that began in October carried most of the indexes to new highs in late November and early December. Astonishing run-ups in Internet-related stocks (including some IPOs), merely spectacular gains in some high-tech standbys, and the effervescence of M&A activity created a market atmosphere that made questions about valuations seem almost irrelevant. In the past couple of weeks, renewed worries about earnings have caused share prices to slip modestly, and we think that this trend will persist in the first half of 1999. But partly because we have elevated our output and profit paths from those in the last Greenbook, share prices have been notched up again in this forecast.

We have revised up slightly our predictions of foreign economic growth, but the outlook is still quite sluggish. In total, foreign GDP is expected to increase a bit less than 1/2 percent in 1998, about 1-1/2 percent in 1999, and 2-1/4 percent in 2000. Recovery in Asia is expected to begin in early 1999 but to proceed very slowly for several quarters. Meanwhile, activity in Europe seems to be decelerating, and Latin America is in the midst of a contraction that we think will extend through most of 1999. Although these growth prospects do not provide much encouragement for U.S. producers, we think that a little lift for our exports may be coming from exchange rate movements: The value of the dollar, having changed little in recent weeks, remains well below its third-quarter peak, and we continue to assume that it will record further small declines over the next couple of years.

In response to the recent plunge of oil prices, our assumptions about the price of crude going forward have been revised downward this month, especially in the near term. The average spot price of West Texas intermediate (WTI) this quarter is now expected to be more than a dollar lower than we previously were projecting--and although we still expect prices to be moving back up after this quarter, the rebound leaves prices lower than before. The WTI price averages slightly less than $14-3/4 per barrel in 1999, down more than a dollar from the previous forecast. The price averages $16 per barrel in 2000, down fifty cents from the last Greenbook.

Our projection of the surplus in the federal budget has been raised further this month. We now expect the unified surplus to amount to $81 billion in fiscal 1999, up from $55 billion in the last Greenbook. The surplus in fiscal 2000 is projected to be $101 billion, up from $73 billion. The bulk of the revision reflects the stronger economic forecast. Our assumptions regarding fiscal policy have not changed; the thrust of policy is projected to be roughly neutral over the next two years.

The Current Quarter

With the data now in hand, growth of real GDP in the third quarter appears to have been only slightly greater than we previously were predicting. But our forecast for the current quarter has been revised up appreciably--to 3.1 percent, versus 2.1 percent last month.

The labor market report for November and the recent weekly figures on initial claims suggest that the pace of hiring has not slowed as much as we had thought. Although payrolls in manufacturing have continued to shrink, overall manufacturing output should rise at an annual rate of more than 3 percent this quarter because of a sizable increase in auto production, a reflection mainly of the rebound from the GM strike.

On the spending side, the available data are tracing out another quarter of strong gains in household demand. Sales of light vehicles fell back in November, but that came as no surprise because sales in October had been astronomical; the average

Summary of the Near-Term Outlook

(Percent change at annual rate except as noted)

Measure	1998:Q3		1998:Q4	
	Nov. GB	Dec. GB	Nov. GB	Dec. GB
Real GDP	3.6	3.8	2.1	3.1
Private domestic final purchases	3.6	3.8	4.3	5.5
Personal consumption	3.9	4.1	3.8	4.1
Residential investment	7.7	9.4	5.1	10.5
Business fixed investment	-.5	-.3	7.3	12.2
Government outlays for consumption and investment	1.6	1.8	4.2	2.8
	Change, billions of chained (1992) dollars			
Inventory investment	27.2	17.7	-25.2	-24.2
Net exports	-20.8	-12.8	-21.0	-16.8

this quarter almost certainly will be up substantially from that of the third quarter. The strong retail sales figures for October and November suggest that spending on other goods also has posted a sizable gain this quarter. We are guessing that spending on services has decelerated, partly because the abnormally mild weather has held down outlays on energy services. All told, real personal consumption expenditures look to be on a track to repeat the 4 percent-plus gain of the third quarter.

Housing continues to be another area of strength. All the indicators of demand for single-family homes have remained at elevated levels, and starts have been spectacular in the past couple of months, bolstered by large backlogs of orders and good weather. In response to these developments, we have raised our current-quarter forecast of real residential investment spending to about 10-1/2 percent at an annual rate, more than double what we estimated last month.

Many cross-currents have been evident over the past few months in the indicators of business fixed investment, but for this quarter at least, they seem to be pointing to a hefty gain overall. We are projecting that total BFI will rise at an annual rate of more than 12 percent after having declined slightly in the third quarter; in the last Greenbook, we posited a fourth-quarter gain of just over 7 percent. Based on orders and shipments data through October, outlays for computers and other high-tech equipment seem to be headed for substantial increases. Investment in transportation equipment looks very strong as well: Shipments of heavy trucks are still rising rapidly; purchases of light vehicles appear to be rebounding from the strike-depressed level of the third quarter; and aircraft deliveries seem to be retracing a little of last quarter's drop. Outlays for other types of equipment are still projected to rise moderately this quarter. In contrast, real outlays on nonresidential structures probably will decline.

Federal purchases, which had dropped back a little in the third quarter, are projected to rise at an annual rate of about 3-3/4 percent this period; a downward revision from the November projection largely reflects some changes in the timing of defense purchases within the current fiscal year. The forecast of current-quarter growth in state and local purchases has been lowered because incoming data on construction did not support the above-trend growth of purchases we predicted earlier; the current forecast has real state and local outlays rising at an annual rate of 2-1/2 percent, about in line with the trend of recent quarters.

We have maintained a forecast that has net exports falling somewhat faster than they did in the third quarter. Imports seem likely to pick up this quarter, not only because domestic demand remains strong but also because shipments of vehicles from Canada are rebounding after having been held down by strike activity in the third quarter. Real exports of goods and services are expected to post a small gain.

Inventory investment in the nonfarm business sector proceeded at an annual rate of more than 4 percent in the third quarter, but we are projecting that businesses will be cutting the rate of accumulation to less than half that pace in the fourth quarter. This slowdown trims more than a full percentage point from the projected rate of GDP growth. Insofar as stocks of motor vehicles are expected to rise a bit this quarter after having declined sharply in the third quarter, the brunt of the slowdown in stockbuilding occurs in other sectors. In October, nonvehicle inventories in manufacturing and trade rose much less rapidly in current-cost terms than they did in the third quarter.

The one important piece of news that we have received on wages since the last Greenbook is the November report on average hourly earnings, which rose only 0.2 percent for the third consecutive month. The year-to-year rate of rise in average hourly earnings--3.7 percent in November--has come down more than 1/2 percentage point from its peak of a few months ago, and we take that to be a signal that the earlier acceleration of the wage trend probably has abated. We are predicting that the twelve-month change in the employment cost index also will begin to tilt downward before long. That said, our forecast of the fourth-quarter rate of rise in the ECI has been nudged up this month because of the greater-than-expected firmness in the recent earnings data for the finance, insurance, and real estate category; those gains probably reflect, in part, the rise in commissions being generated by the strength of the stock market and robust mortgage activity.

Our forecast of the fourth-quarter rate of rise in the CPI is 2.0 percent at an annual rate, up a couple of tenths from the November Greenbook. The forecast of the quarterly rise in the core CPI has been raised three tenths, to 2.5 percent, in the expectation that much of the recently announced hike in tobacco product prices will be passed on to the retail level in December; we had not thought that the producers would move quite so quickly to recoup the costs of the recent tobacco settlement. We have also raised the current-quarter forecast for food prices in reaction to the CPI reports for October and November. By contrast, this quarter's drop in energy prices will likely be larger than we had been expecting.

The Outlook for the Economy in 1999 and 2000

The upward revision to our estimate of activity in the second half of 1998 has boosted the forecast of real GDP growth for the year as a whole to a little above 3-1/2 percent, only a touch shy of the strong gains of 1996 and 1997. This added strength, underpinned by a higher level of stock market wealth, generates some momentum for faster growth going forward. Thus, our forecast of real GDP growth in 1999 has been raised 1/2 percentage point, to 2.1 percent. We expect a further small pickup in growth in 2000, to about 2-1/4 percent. By the end of 2000, the level of real GDP is 3/4 percent higher than it was in our previous forecast, an increment that we attribute largely to the recent financial market developments and the related upward revision to our forecast of stock prices.

Consumer spending. Although we have raised our forecast of real PCE growth somewhat for both 1999 and 2000, we continue to anticipate much smaller gains than in 1998. A 2.7 percent rise is predicted for 1999, and we are projecting the growth in 2000 to be 2.5 percent--these rates are about half the rate of increase this year.

This prediction of a slowdown rests in good part on the conviction that the wherewithal to support spending will not be increasing so fast as it has been. Indeed, our forecast for the stock market implies a considerable decline in the ratio of household net worth to income--which, ceteris paribus, should cause the "wealth effect" (with the usual lags) to swing gradually from strongly positive this year to mildly negative in 2000. As this factor begins to weigh on aggregate demand,

Summary of Staff Projections
(Percent change, compound annual rate)

Measure	1998:H2	1999:H1	1999:H2	2000
Real GDP	**3.5**	**2.1**	**2.0**	**2.3**
Previous	2.9	1.4	1.7	2.3
Final sales	3.6	2.1	1.8	2.2
Previous	2.8	1.7	1.7	2.1
PCE	4.1	3.0	2.4	2.5
Previous	3.8	2.7	2.2	2.4
Residential investment	10.0	.1	-2.5	-.6
Previous	6.4	-1.6	-1.8	.4
BFI	5.7	4.5	3.7	5.1
Previous	3.3	4.6	2.8	5.4
Government purchases	2.3	1.3	1.2	1.5
Previous	2.8	1.0	1.5	1.4
Exports	-.2	1.6	3.4	4.8
Previous	-1.9	1.5	3.2	4.7
Imports	4.8	6.6	5.3	6.2
Previous	5.4	6.9	5.4	6.5
	Change, billions of chained (1992) dollars			
Inventory change	-6.5	-.5	8.3	3.4
Previous	2.0	-13.5	2.9	10.7
Net exports	-29.5	-32.7	-16.6	-34.4
Previous	-41.7	-35.1	-19.0	-39.8

consumer demand will be damped further by diminishing job and income gains. Household debt burdens are high, but we do not foresee debt-service strains becoming widespread; and although lenders may become a bit more cautious with respect to consumer credit, borrowing should remain pretty easy for all but the most marginal of households.

Spending on consumer durables might be expected to be restrained by another factor as well: Large gains in spending over the past few years have added substantially to the stocks of both vehicles and household equipment, and the urgency to add further to these stocks probably is not great. This past year's jump in consumer purchases of light vehicles was prompted, in part, by the attractive pricing offered by manufacturers fighting aggressively for market share; sustaining sales at so high a level probably would require much sweeter deals still, which we do not foresee. The major automakers seem to be planning on a mild drop-off in sales.

Housing. The housing market looks very solid, with households viewing buying conditions as extraordinarily favorable, bolstered by the low level of interest rates. The appreciable backlog of building projects may sustain starts at a high level in the near term if weather permits.

The conditions in mortgage markets are not expected to change much over the projection period. Although interest rates on Treasuries are anticipated to rise, the spreads between mortgage rates and Treasury rates should narrow. Meanwhile, the availability of loans should continue to be excellent except in the riskiest portions of the market. The multifamily segment of the market, unlike the commercial real estate area, has not suffered any serious tightening in credit availability, in part because of the support of Freddie Mac and Fannie Mae.

Nonetheless, we do expect that housing activity will weaken over the projection period. The story here is much the same as with consumer spending: a sizable stock of housing units reflecting the large additions made recently, coupled with less favorable movements in employment, income, and wealth. But, given the extraordinarily good "affordability" conditions expected to continue to prevail in the single-family sector, we do not expect a major retrenchment. Total housing starts, which appear to be running at about 1.62 million units this year, are projected to drop off to around 1.55 million by the second half of next year and then to edge down a bit more in 2000. Factoring in as well an expected softening in other components of housing expenditure (such as commissions on sales), real residential investment declines only moderately over 1999 and by just a small amount in 2000--but this is a marked departure from the 12 percent gain projected for 1998.

Business fixed investment. After rising about 11-1/2 percent in 1998, total BFI is projected to decelerate sharply to growth of about 4 percent in 1999 and 5 percent in 2000. In view of widespread expectations of slower sales growth and increased pressures on profits, we do not think that businesses will want to keep adding to capacity as rapidly as they have been in recent years. Although the markets for business credit should continue to mend, some lingering damage to commercial mortgage channels--and the persistence of a bit more caution in lending generally--probably will squeeze out a few of the riskier projects that might have found ready support before the recent financial turmoil.

Real outlays for equipment, which we now estimate to have risen more than 17 percent in 1998, are expected to rise at less than half that pace in each of the next two years. Categories that are likely to be notably soft include: industrial machinery, orders for which have been showing some faint hints of falling off in conjunction with the weakness in manufacturing; farm machinery, demand for which already has weakened considerably; and aircraft, deliveries of which seem poised to decline in value terms if not in numbers.

Computers and related equipment are a bit of a wild card. Declining prices and technological innovations will continue to spur expansion and replacement, but we expect that purchases of these machines will rise less rapidly, at least in real terms, than they have on average this year. A recent canvass of firms by Reserve Bank staff does suggest--unsurprisingly--that many companies advanced their replacement of computers (particularly PCs) this year as part of their Y2K preparation and that some will avoid making big changes to their systems in the latter part of 1999 and at the beginning of 2000. Our guess is that, after growing more than 60 percent this year, real computer outlays will increase at less than half that pace over the next two years. To a degree, we have front-loaded 1999 expenditures in light of the Y2K consideration, and this front-loading explains a good bit of the intrayear variation of overall PDE next year.

The forecast for nonresidential investment has not changed much. After declining 3 percent in 1998, real outlays on these structures are projected to fall somewhat further next year and to be little changed in 2000. The construction of office buildings still seems to be on a course of expansion that should persist for a few more quarters. But weakness is apparent in the outlook for many other categories. Construction of industrial buildings seems likely to continue falling sharply in view of the sluggish conditions and excess capacity in many parts of manufacturing, and we are projecting further cutbacks in the construction of commercial buildings, a category that recorded strong gains earlier in the expansion but more recently has been in decline. The weakness of oil prices continues to take a toll on drilling.

Business inventories. Inventory overhangs currently appear to be present in only a few parts of the nonfarm economy, and if accumulation proceeds this quarter at the slower pace that we are projecting, then businesses should not need to gear down their stockbuilding further in the new year. We expect changes in the rate of accumulation to contribute just a touch to the growth of real GDP over the next two years. As noted in the last Greenbook, a moderate zig-zag pattern that shows up in the inventory forecast in late 1999 and early 2000 represents our effort, however crude, to capture the stockpiling behavior that could be precipitated by worries about Y2K glitches; if the aforementioned Reserve Bank survey captured anything of what is going on, most firms either have not focused on this issue yet or simply do not believe that there will be a reason to do much extra precautionary stocking. In the farm sector, stockpiling is projected to gradually slow as producers respond to the present overhangs and low prices.

Government spending. We continue to think that real federal purchases of goods and services will trend gradually lower over the forecast period. We are assuming that the statutory restrictions on overall federal spending will hold, albeit with some end-runs in the form of still more emergency authorizations that are not subject to the spending limits. But the temptation to spend the surpluses is considerable; if the discussion of social security reform were to break down, a major impediment to more spending (and tax cuts) would be removed.

State and local government finances have been improving for some time, and we do not see any serious setbacks ahead. Nonetheless, we expect that these governments will continue to pursue relatively cautious spending programs. Their real outlays for consumption and investment are projected to rise between 2-1/2 percent and 2-3/4 percent in both 1999 and 2000--within the narrow range of annual outcomes recorded in previous years of the current expansion. We expect construction to pick up after a year of no gain in 1998, lifted in part by the new federal transportation law. However, the growth of real consumption outlays--a far bigger element in the total--is expected to be moderate, only about 2-1/4 percent on average over the next two years. Many states and localities probably will continue to view tax cuts as the preferred way of dealing with their buildup of surpluses.

Net exports. After dropping about 2-3/4 percent this year, exports should post positive but slow growth in the first half of next year. Thereafter, growth gradually picks up in response to firming demand in foreign economies and exchange rate movements that should be more positive to U.S. producers than those of the past few years. Although the rise in exports next year adds up to only 2-1/2 percent, the predicted increase for 2000 is close to 5 percent. Increases in real imports should be damped by the slower pace of U.S. expansion but are still expected to be around 6 percent in each of the next two years. Taken together, these numbers mean that net exports will continue to fall rapidly but not quite so fast as they have this past year. The negative contribution of net exports to real GDP growth moves from 1-1/2 percentage points in 1998 to about 1/2 percentage point in 1999 and 1/4 percentage point in 2000. (A fuller discussion of the forecast for net exports is contained in the International Developments section.)

The Outlook for the Labor Market
(Percent change, Q4 to Q4, except as noted)

Measure	1997	1998	1999	2000
Output per hour, nonfarm business	1.7	1.8	1.3	1.9
Previous	1.7	1.7	1.0	2.0
Nonfarm payroll employment	2.7	2.3	1.3	.8
Previous	2.7	2.2	.8	.9
Employment, household survey	2.1	1.2	.8	.5
Previous	2.1	1.0	.5	.6
Labor force participation rate[1]	67.1	67.1	67.0	66.9
Previous	67.1	67.0	66.9	66.8
Civilian unemployment rate[1]	4.7	4.5	4.7	4.9
Previous	4.7	4.6	5.0	5.3

1. Percent, average for the fourth quarter.

Labor markets. The changes to our labor market forecast are relatively straightforward: Part of the added output growth in the current forecast translates into higher productivity. The remainder shows up mainly in added employment growth that causes the unemployment rate to remain lower than we previously were forecasting; it ends up slightly under 5 percent in the fourth quarter of 2000 instead of rising to 5-1/4 percent.

Employment growth in our forecast remains a good bit slower than it has been in recent years. The tightness of the labor market may cause firms to hesitate before letting a good worker go at the first hint of a slackening in sales, but as profit margins continue to erode, the need to trim costs will be reflected in reduced hirings and in increased layoffs and firings; the recent downsizing announcements by some large corporations underscore the point. We are predicting that a deceleration of job growth will become clearly evident in the first half of 1999 and that the net rise in jobs next year will amount to 1-1/2 million, just a bit more than half of this year's increase. A still smaller rise is projected for 2000--slightly over 1 million. Some "cyclical" variations in productivity growth accompany this employment forecast: In 1999, when output is slowing, growth of output per hour falls below its estimated trend of 1.8 percent; in 2000, productivity growth picks up again as output rises a little more rapidly and Y2K work is completed.

Wages and prices. In view of the lower unemployment rate, we have added a couple of tenths to the forecasted increases in the employment cost index in both 1999 and 2000. The index now rises 3.3 percent in each of those years after having increased 3.6 percent in 1998.[1]

Although the labor market is expected to loosen a little in the future, it is projected to remain sufficiently tight that many workers should be able to command further sizable increases in real compensation. However, we think that the low rate of inflation that has prevailed for a while now will tend to moderate nominal wage increments in the coming year.[2] Moreover, the slackening of economic expansion--and the absolute drop-off in activities such as home sales and mortgage originations--should put a damper on commission and bonus payments; the disproportionate contributions of the FIRE industry and certain sales occupations to the acceleration of compensation over the past year suggests that this could be quite important. Our forecast of benefits still shows some pickup over the next two years; we continue to expect a substantial acceleration in health insurance costs--though not so much as the scarier numbers being cited would imply because we think that employers will find ways to deflect some of the potential hit.

All of the broader price indexes are expected to accelerate in 1999 from the low rates of this year, mainly because retail energy prices rise after dropping very sharply in 1998. The total CPI picks up from a 1.6 percent increase in 1998 to a 2.3 percent increase in 1999. Pickups of similar magnitude are evident in our forecasts of the various GDP price measures, but the rates of increase in those are expected to remain appreciably below the rate of rise in the CPI. Little further change in the rate of inflation is anticipated in 2000, partly because energy prices do not keep accelerating but more importantly because core inflation remains in check: The CPI excluding food and energy is projected to rise 2.3 percent in both 1999 and 2000--virtually the same pace as in 1998, once adjustment is made for the effects of

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1. A step-up in compensation growth toward the end of 2000 is a reflection of our assumption, introduced in November, that a fifty-cent increase in the federal minimum wage would take effect in the fourth quarter of that year.

2. As noted earlier, average hourly earnings already have shown a marked moderation in the past three months. However, while those data are a key source for the estimates of compensation in the quarterly productivity and costs figures, they are not a particularly reliable guide to the short-run movements in the ECI.

Staff Inflation Projections

(Percent change, Q4 to Q4, except as noted)

Measure	1997	1998	1999	2000
Consumer price index	1.9	1.6	2.3	2.2
Previous	1.9	1.5	2.2	2.1
Food	1.7	2.3	1.3	1.8
Previous	1.7	2.0	1.4	1.7
Energy	-1.0	-9.0	3.7	1.1
Previous	-1.0	-8.6	3.7	1.4
Excluding food and energy	2.2	2.4	2.3	2.3
Previous	2.2	2.4	2.2	2.2
PCE chain-weighted price index	1.5	.8	1.7	1.7
Previous	1.5	.8	1.6	1.6
Excluding food and energy	1.6	1.2	1.7	1.7
Previous	1.6	1.2	1.6	1.6
GDP chain-weighted price index	1.7	.9	1.5	1.7
Previous	1.7	.9	1.5	1.6
ECI for compensation of private industry workers[1]	3.4	3.6	3.3	3.3
Previous	3.4	3.5	3.1	3.1
Prices of core non-oil merchandise imports	-.7	-2.0	1.5	1.4
Previous	-.7	-2.2	1.1	1.2
	Percentage points			
MEMO: *Adjustments for technical changes to the CPI*[2]				
Core CPI	.2	.4	.6	.6

1. December to December.

2. Adjustments are calculated relative to the methodological structure of the CPI in 1994.

technical changes slated for the start of next year.[3] In the near term, prices will be damped by the falling costs of raw materials and intermediate supplies (including the wide range of petroleum-related inputs). These downward pressures actually look a bit

3. Some gyrations in the monthly indexes will be caused in the near term by the announced big increases in tobacco prices, although those may be muted to a degree by rebates. We had anticipated relatively large increases in these prices previously, so the effects in the current forecast are mainly matters of timing.

more intense than we had anticipated in our previous projection. But any benefits in terms of lower inflation should be offset by the higher resource utilization rates in this forecast (in the case of the capacity utilization figures, the upward revision reflects in part the recent upward benchmark revisions). Food prices are projected to rise less than core inflation both in 1999 and 2000 after having about matched the rate of rise in the core this past year.

Money and Credit Flows

The turmoil in financial markets in late summer and early fall does not seem to have slowed the growth of domestic nonfinancial debt. Reflecting the continued strong borrowing of households and businesses, this aggregate appears on track to expand at a 6-1/4 percent rate in the current quarter--about equal to the increases posted in the first three quarters of the year. In the business sector, attractive interest rates have spurred heavy bond issuance by investment-grade corporations, and speculative-grade corporate issuance has continued to recover, though activity in this market remains well below the extraordinary pace earlier this year. Year-end pressures are evident in hefty risk spreads on lower-rated commercial paper, but riskier borrowers appear to be securing adequate funding to get through year-end, with many drawing on banks. Business lending at banks, which ballooned early in the quarter, has downshifted lately with the resumption of bond issuance. In the household sector, growth of home mortgage and consumer debt appears to have remained quite brisk in the current quarter, reflecting the absence of any pullback in consumer outlays or housing activity.

For 1998 as a whole, domestic nonfinancial debt is estimated to have grown about 6-1/4 percent, almost 2 percentage points faster than nominal GDP. We expect it to outpace GDP again next year, but in 2000 the gradual slowing in nonfederal debt growth and a steady contraction of federal debt is projected to pull total growth into rough alignment with the 4 percent rise in nominal spending.

Absent some shock unforeseen in this forecast, we would expect a lessening of stress in U.S. capital markets next year. Dealers are expected to become more active in making markets, and investors are likely to become more receptive to riskier corporate debt issues, allowing premiums on bonds and longer-maturity commercial paper to narrow further. Liquidity should improve as well. Still, yield spreads for a variety of debt instruments will probably not return to the levels of earlier this year. The firmer terms and standards of bank lending to businesses of late should remain in place, especially given the slower growth of the economy and the softer outlook for corporate earnings.

The corporate financing gap is forecast to widen over the next two years, as profits slip and as investment outlays continue to rise, though more moderately than in 1998. Increased demand for external funding associated with the wider gap should be more than offset, however, by some slackening in share buybacks and by reduced reliance on credit for the financing of large mergers. Merger activity is still expected to be robust; but, in keeping with the pattern of recently announced deals, a large share of mergers will be financed with stock swaps.

The expansion of household debt, which has been brisk this year, is expected to moderate over the course of 1999, as home sales gradually weaken and demand for autos and other durables slackens. Banks and other consumer lenders are expected to snug their terms and standards for consumer loans as income growth slows and unemployment edges higher--but not by enough to impede significantly the use of credit by households.

Expansion of the debt of state and local governments is expected to remain moderate over the next two years. Opportunities for further advance refundings are limited. Nonetheless, the issuance of municipal bonds to fund new capital should remain strong, consistent with the heavy slate of projects authorized in the recent election and our outlook for substantial state and local expenditures on infrastructure.

The growth rates of the broad monetary aggregates will exceed their ranges by several percentage points this year. However, we expect that the extraordinary boost to the aggregates from the recent heightened demand for safe and liquid assets will unwind over time. With the slowing of nominal spending next year and the waning effects from recent monetary policy easings, we expect a sharp deceleration of M2, although the aggregate is likely to continue growing faster than nominal GDP. M3 should continue to outstrip M2, but growth is likely to moderate substantially in 1999, in part because of a slowing expansion of bank credit. The velocities of the broad monetary aggregates are expected to continue to trend down through 2000, but at a diminishing pace.

Alternative Simulations

We have included in this Greenbook the results of three alternative simulations generated with our quarterly econometric model. Two of the simulations are based on alternative assumptions about the stock market, and the other is designed to indicate the effect of a different monetary policy path.

The first stock market scenario has equity prices falling more sharply over the first half of 1999 than we are anticipating in our baseline and then holding at a level roughly 10 percent below the baseline over the ensuing year and a half. This drop in share prices trims GDP growth by somewhere between 1/4 to 1/2 percentage point in both 1999 and 2000. Unemployment rises slightly more than in the baseline, and inflation is a touch lower. In the second, more bullish stock price scenario, the market rises at a pace about in line with the growth of nominal disposable income. Under this scenario, growth is a few tenths stronger, the unemployment rate is a couple of tenths lower by the end of 2000, and inflation is a bit higher.

The final alternative hypothesizes a reversal of the recent Fed easing, with the funds rate moving back up to 5-1/2 percent by next spring--and holding there through the end of 2000. This scenario trims GDP growth about 1/4 percentage point in 1999 and about 3/4 percentage point in 2000. The unemployment rate ends up in the fourth quarter of 2000 about 1/2 percentage point above the forecast in the baseline. Inflation in 1999 differs little from the baseline, but it is 1/2 percentage point lower in 2000. The incremental economic consequences of an additional 75 basis points of easing, to a 4 percent funds rate by the spring, would be essentially symmetrical to those shown for the tightening.

Alternative Federal Funds Rate and Stock Market Assumptions

(Percent change, Q4 to Q4, except as noted)

Measure	1999	2000
Real GDP		
Baseline	2.1	2.3
Lower stock prices	1.8	1.9
Higher stock prices	2.3	2.7
Higher funds rate	1.8	1.5
Civilian unemployment rate[1]		
Baseline	4.7	4.9
Lower stock prices	4.8	5.1
Higher stock prices	4.6	4.7
Higher funds rate	4.8	5.4
CPI excluding food and energy		
Baseline	2.3	2.3
Lower stock prices	2.3	2.2
Higher stock prices	2.3	2.4
Higher funds rate	2.2	1.8

1. Average for the fourth quarter.

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December 16, 1998

STAFF PROJECTIONS OF CHANGES IN GDP, PRICES, AND UNEMPLOYMENT
(Percent, annual rate)

Interval		Nominal GDP		Real GDP		GDP chain-weighted price index		Consumer price index[1]		Unemployment rate[2]	
		11/12/98	12/16/98	11/12/98	12/16/98	11/12/98	12/16/98	11/12/98	12/16/98	11/12/98	12/16/98
ANNUAL											
1996		5.4	5.4	3.4	3.4	1.9	1.9	3.0	3.0	5.4	5.4
1997		5.9	5.9	3.9	3.9	1.9	1.9	2.3	2.3	4.9	4.9
1998		4.7	4.8	3.6	3.7	1.0	1.0	1.6	1.6	4.5	4.5
1999		3.2	3.8	1.9	2.5	1.3	1.3	2.1	2.2	4.8	4.5
2000		3.5	3.6	1.9	2.0	1.6	1.6	2.1	2.2	5.2	4.8
QUARTERLY											
1997	Q1	7.2	7.2	4.2	4.2	2.8	2.8	2.0	2.0	5.3	5.3
	Q2	5.6	5.6	4.0	4.0	1.7	1.7	1.5	1.5	4.9	4.9
	Q3	5.4	5.4	4.2	4.2	1.2	1.2	1.8	1.8	4.9	4.9
	Q4	4.2	4.2	3.0	3.0	1.1	1.1	2.3	2.3	4.7	4.7
1998	Q1	6.4	6.4	5.5	5.5	0.9	0.9	0.5	0.5	4.7	4.7
	Q2	2.7	2.7	1.8	1.8	0.9	0.9	2.0	2.0	4.4	4.4
	Q3	4.5	4.7	3.6	3.8	0.8	0.8	1.7	1.7	4.6	4.6
	Q4	3.2	4.2	2.1	3.1	1.1	1.0	1.8	2.0	4.6	4.5
1999	Q1	3.1	4.5	1.4	2.5	1.7	1.9	2.2	2.3	4.6	4.4
	Q2	2.8	3.0	1.4	1.7	1.3	1.3	2.3	2.4	4.7	4.5
	Q3	3.0	3.2	1.5	1.8	1.5	1.4	2.1	2.2	4.8	4.6
	Q4	3.4	3.6	1.9	2.2	1.4	1.4	2.1	2.2	5.0	4.7
2000	Q1	2.9	2.9	0.9	0.9	1.9	2.0	2.1	2.2	5.1	4.8
	Q2	4.4	4.5	2.9	2.8	1.5	1.6	2.1	2.2	5.2	4.8
	Q3	4.2	4.3	2.6	2.6	1.5	1.6	2.1	2.2	5.2	4.9
	Q4	4.3	4.3	2.7	2.7	1.5	1.6	2.1	2.2	5.3	4.9
TWO-QUARTER[3]											
1997	Q2	6.4	6.4	4.1	4.1	2.2	2.2	1.8	1.8	-0.4	-0.4
	Q4	4.8	4.8	3.6	3.6	1.2	1.2	2.0	2.0	-0.2	-0.2
1998	Q2	4.6	4.6	3.7	3.7	0.9	0.9	1.2	1.2	-0.3	-0.3
	Q4	3.9	4.4	2.9	3.5	1.0	0.9	1.8	1.9	0.2	0.1
1999	Q2	2.9	3.7	1.4	2.1	1.5	1.6	2.2	2.3	0.1	-0.0
	Q4	3.2	3.4	1.7	2.0	1.4	1.4	2.1	2.2	0.3	0.2
2000	Q2	3.6	3.7	1.9	1.9	1.7	1.8	2.1	2.2	0.2	0.1
	Q4	4.2	4.3	2.6	2.6	1.5	1.6	2.1	2.2	0.1	0.1
FOUR-QUARTER[4]											
1996	Q4	5.8	5.8	3.9	3.9	1.8	1.8	3.2	3.2	-0.3	-0.3
1997	Q4	5.6	5.6	3.8	3.8	1.7	1.7	1.9	1.9	-0.6	-0.6
1998	Q4	4.2	4.5	3.3	3.6	0.9	0.9	1.5	1.6	-0.1	-0.2
1999	Q4	3.1	3.6	1.6	2.1	1.5	1.5	2.2	2.3	0.4	0.2
2000	Q4	3.9	4.0	2.3	2.3	1.6	1.7	2.1	2.2	0.3	0.2

1. For all urban consumers.
2. Level, except as noted.
3. Percent change from two quarters earlier; for unemployment rate, change in percentage points.
4. Percent change from four quarters earlier; for unemployment rate, change in percentage points.

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REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, ANNUAL VALUES
(Seasonally adjusted annual rate)

December 16, 1998

Item	Units[1]	1992	1993	1994	1995	1996	1997	1998	1999	2000
								- - - Projected	- - -	- - -
EXPENDITURES										
Nominal GDP	Bill. $	6244.4	6558.1	6947.0	7269.6	7661.6	8110.9	8496.6	8821.6	9143.2
Real GDP	Bill. Ch. $	6244.4	6389.6	6610.7	6761.7	6994.8	7269.8	7539.9	7726.6	7881.8
Real GDP	% change	3.6	2.4	3.3	2.1	3.9	3.8	3.6	2.1	2.3
Gross domestic purchases		4.0	3.0	3.6	1.6	4.2	4.4	4.9	2.5	2.5
Final sales		3.9	2.1	2.7	2.7	3.7	3.4	4.1	2.0	2.2
Priv. dom. final purchases		4.9	3.7	3.7	2.9	4.4	4.5	6.3	2.7	2.7
Personal cons. expenditures		4.2	2.7	3.1	2.6	3.3	3.7	5.1	2.7	2.5
Durables		9.4	7.4	6.3	4.5	5.8	7.4	10.9	2.2	4.3
Nondurables		3.4	1.6	3.0	1.7	2.8	2.0	4.5	2.3	1.9
Services		3.6	2.3	2.5	2.6	3.0	3.8	4.2	3.0	2.5
Business fixed investment		5.5	9.9	7.6	7.3	11.7	9.8	11.4	4.1	5.1
Producers' dur. equipment		9.6	12.2	10.2	9.1	11.8	12.7	17.2	6.5	6.7
Nonres. structures		-3.4	4.5	1.1	2.7	11.6	2.5	-3.1	-2.8	0.4
Residential structures		16.9	7.8	4.2	-1.4	5.4	4.2	12.6	-1.2	-0.6
Exports		4.1	4.6	10.0	10.5	10.3	9.6	-2.8	2.5	4.8
Imports		7.4	10.2	12.3	5.6	11.8	14.0	8.5	5.9	6.2
Gov't. cons. & investment		1.7	-1.4	0.1	-0.9	2.1	1.4	1.6	1.3	1.5
Federal		1.3	-6.1	-3.9	-5.6	1.1	-0.6	0.0	-1.5	-0.8
Defense		-1.3	-6.9	-6.0	-5.0	-0.1	-1.4	-2.5	-2.0	-0.9
State & local		2.0	2.0	2.7	2.1	2.8	2.6	2.4	2.7	2.6
Change in bus. inventories	Bill. Ch. $	7.0	22.1	60.6	27.7	30.0	63.2	54.3	33.2	37.1
Nonfarm		2.0	29.5	49.0	37.7	23.2	58.8	46.8	28.7	34.9
Net exports		-29.5	-70.2	-104.6	-96.5	-111.2	-136.1	-244.1	-309.9	-346.8
Nominal GDP	% change	6.3	5.0	5.8	4.2	5.8	5.6	4.5	3.6	4.0
EMPLOYMENT AND PRODUCTION										
Nonfarm payroll employment	Millions	108.6	110.7	114.1	117.2	119.6	122.7	125.8	127.9	129.1
Unemployment rate	%	7.5	6.9	6.1	5.6	5.4	4.9	4.5	4.5	4.8
Industrial prod. index	% change	3.6	3.3	6.5	3.5	5.3	6.6	1.7	2.0	2.5
Capacity util. rate - mfg.	%	79.5	80.5	82.5	82.7	81.4	82.0	80.8	79.3	79.3
Housing starts	Millions	1.20	1.29	1.46	1.35	1.48	1.47	1.62	1.56	1.52
Light motor vehicle sales		12.85	13.86	15.01	14.72	15.05	15.03	15.33	15.04	14.56
North Amer. produced		10.51	11.71	12.88	12.82	13.35	13.11	13.33	13.04	12.64
Other		2.34	2.15	2.13	1.90	1.70	1.92	2.00	2.00	1.92
INCOME AND SAVING										
Nominal GNP	Bill. $	6255.5	6576.8	6955.2	7287.1	7674.0	8102.9	8475.2	8787.6	9097.3
Nominal GNP	% change	6.2	5.1	5.7	4.4	5.6	5.2	4.4	3.4	3.9
Nominal personal income		7.2	4.0	5.2	4.6	5.9	5.4	4.9	3.8	4.0
Real disposable income		4.0	1.2	2.5	2.1	2.7	2.9	3.3	2.6	2.3
Personal saving rate	%	5.7	4.4	3.5	3.4	2.9	2.1	0.5	0.2	0.2
Corp. profits, IVA & CCAdj.	% change	11.3	19.0	14.1	14.6	7.7	7.7	0.3	-3.4	1.9
Profit share of GNP	%	6.8	7.5	8.2	9.2	9.8	10.1	9.7	9.2	8.7
Excluding FR Banks		6.6	7.2	7.9	8.9	9.5	9.8	9.4	8.9	8.4
Federal surpl./deficit	Bill. $	-280.9	-250.7	-186.7	-174.4	-110.3	-21.1	76.3	76.2	86.4
State & local surpl./def.		86.3	87.4	96.8	111.7	122.6	134.1	149.0	156.2	162.2
Ex. social ins. funds		18.3	19.7	27.9	37.0	52.2	66.0	81.5	88.7	94.7
Gross natl. saving rate	%	14.5	14.4	15.5	16.3	16.6	17.4	17.3	16.7	16.3
Net natl. saving rate		3.7	3.7	4.7	5.8	6.3	7.3	7.4	6.7	6.4
PRICES AND COSTS										
GDP chn.-wt. price index	% change	2.6	2.6	2.5	2.1	1.8	1.7	0.9	1.5	1.7
Gross Domestic Purchases chn.-wt. price index		2.7	2.3	2.5	2.0	1.8	1.3	0.4	1.5	1.6
CPI		3.1	2.7	2.7	2.6	3.2	1.9	1.6	2.3	2.2
Ex. food and energy		3.5	3.1	2.8	3.1	2.6	2.2	2.4	2.3	2.3
ECI, hourly compensation[2]		3.5	3.6	3.1	2.6	3.1	3.4	3.6	3.3	3.3
Nonfarm business sector										
Output per hour		3.5	-0.4	0.1	1.2	2.1	1.7	1.8	1.3	1.9
Compensation per Hour		4.5	1.6	2.1	2.8	3.7	3.9	4.1	3.5	3.4
Unit labor cost		1.0	2.0	2.0	1.6	1.6	2.1	2.2	2.2	1.5

1. Changes are from fourth quarter to fourth quarter.
2. Private-industry workers.

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Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES
(Seasonally adjusted, annual rate except as noted)

December 16, 1998

Item	Units	1996 Q1	1996 Q2	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2
EXPENDITURES											
Nominal GDP	Bill. $	7495.3	7629.2	7703.4	7818.4	7955.0	8063.4	8170.8	8254.5	8384.2	8440.6
Real GDP	Bill. Ch. $	6882.0	6983.9	7020.0	7093.1	7166.7	7236.5	7311.2	7364.6	7464.7	7498.6
Real GDP	% change	3.3	6.1	2.1	4.2	4.2	4.0	4.2	3.0	5.5	1.8
Gross domestic purchases		4.5	7.0	3.4	1.8	5.5	4.4	4.6	3.2	7.8	3.9
Final sales		3.6	5.4	0.9	5.1	2.9	2.7	5.8	2.1	4.3	4.6
Priv. dom. final purchases		5.1	6.2	3.1	3.3	4.6	3.3	7.2	2.9	8.5	7.4
Personal cons. expenditures		3.7	4.7	1.8	2.9	4.3	1.6	6.2	2.8	6.1	6.1
Durables		5.8	12.7	-1.9	7.2	12.3	-1.5	16.8	3.1	15.8	11.2
Nondurables		2.2	4.8	1.2	2.9	3.6	-0.2	5.1	-0.4	7.4	5.3
Services		4.0	3.0	3.0	2.0	3.1	3.2	4.7	4.3	3.5	5.4
Business fixed investment		13.1	11.0	14.2	8.8	7.0	14.0	17.0	1.8	22.2	12.8
Producers' dur. equipment		15.7	12.3	16.2	3.2	8.3	22.8	18.8	2.2	34.3	18.8
Nonres. structures		6.4	7.4	8.9	24.5	3.9	-6.2	12.4	0.9	-4.9	-2.3
Residential structures		9.3	19.5	-1.7	-3.9	3.1	6.1	-0.4	8.2	15.6	15.0
Exports		3.7	5.8	2.1	32.0	8.3	15.5	10.6	4.4	-2.8	-7.7
Imports		13.1	13.5	13.6	7.0	18.6	17.9	13.5	6.3	15.7	9.3
Gov't. cons. & investment		3.2	7.1	-1.6	0.0	2.1	2.1	1.4	0.1	-1.9	3.7
Federal		8.0	8.1	-4.7	-6.3	-2.7	3.6	-1.2	-2.1	-8.8	7.3
Defense		7.2	8.1	-6.3	-8.3	-9.9	9.1	-1.8	-2.0	-18.5	9.9
State & local		0.5	6.5	0.3	3.8	4.9	1.3	2.9	1.3	2.1	1.8
Change in bus. inventories	Bill. Ch. $	14.4	26.1	47.5	32.1	56.3	79.0	51.0	66.5	91.4	38.2
Nonfarm		10.4	15.2	38.6	28.7	56.2	72.1	44.0	62.7	85.9	29.9
Net exports		-95.5	-113.5	-140.1	-95.9	-121.5	-131.6	-142.4	-149.0	-198.5	-245.2
Nominal GDP	% change	5.7	7.3	3.9	6.1	7.2	5.6	5.4	4.2	6.4	2.7
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	118.5	119.3	120.0	120.7	121.5	122.3	123.0	123.9	124.8	125.5
Unemployment rate	%	5.6	5.4	5.3	5.3	5.3	4.9	4.9	4.7	4.7	4.4
Industrial prod. index	% change	2.8	9.6	5.5	3.5	6.6	6.0	7.2	6.6	1.6	2.8
Capacity util. rate - mfg.	%	80.9	81.6	81.8	81.3	81.6	81.7	82.1	82.5	81.8	81.2
Housing starts	Millions	1.47	1.49	1.49	1.42	1.47	1.46	1.45	1.53	1.58	1.57
Light motor vehicle sales		15.10	15.18	15.00	14.91	15.32	14.54	15.19	15.07	15.02	16.08
North Amer. produced		13.44	13.46	13.33	13.16	13.41	12.68	13.20	13.13	13.07	14.09
Other		1.66	1.72	1.68	1.76	1.92	1.86	1.99	1.94	1.95	1.99
INCOME AND SAVING											
Nominal GNP	Bill. $	7515.0	7643.3	7708.6	7829.0	7952.4	8062.3	8162.0	8234.9	8369.4	8421.8
Nominal GNP	% change	5.6	7.0	3.5	6.4	6.5	5.6	5.0	3.6	6.7	2.5
Nominal personal income		6.6	6.9	5.5	4.6	7.3	4.7	4.7	5.0	5.9	4.5
Real disposable income		2.9	2.1	4.4	1.3	3.3	2.9	2.4	2.9	4.0	2.6
Personal saving rate	%	3.2	2.6	3.1	2.6	2.4	2.6	1.7	1.7	1.2	0.4
Corp. profits, IVA & CCAdj.	% change	16.9	6.9	3.8	3.5	18.1	11.1	13.1	-9.2	4.2	-4.1
Profit share of GNP	%	9.8	9.8	9.8	9.7	10.0	10.1	10.3	10.0	9.9	9.7
Excluding FR Banks		9.5	9.5	9.5	9.5	9.7	9.8	10.0	9.7	9.6	9.5
Federal surpl./deficit	Bill. $	-150.1	-112.6	-100.1	-78.3	-51.2	-34.8	-0.3	2.2	58.8	74.4
State & local surpl./def.		117.3	129.1	122.3	121.7	128.4	130.1	136.6	141.4	140.2	141.3
Ex. social ins. funds		45.3	58.2	52.5	52.9	59.8	61.6	68.7	73.8	72.7	73.6
Gross natl. saving rate	%	16.4	16.4	16.8	16.7	17.0	17.6	17.5	17.3	17.7	17.2
Net natl. saving rate		6.0	6.2	6.6	6.5	7.0	7.6	7.5	7.3	7.8	7.2
PRICES AND COSTS											
GDP chn.-wt. price index	% change	2.2	1.4	1.8	1.6	2.8	1.7	1.2	1.1	0.9	0.9
Gross Domestic Purchases chn.-wt. price index		2.1	1.4	1.5	2.1	2.2	0.9	1.1	1.0	-0.2	0.4
CPI		3.2	3.7	2.6	3.3	2.0	1.5	1.8	2.3	0.5	2.0
Ex. food and energy		2.5	2.5	2.7	2.7	2.2	2.6	1.9	2.1	2.4	2.6
ECI, hourly compensation[1]		2.5	3.5	2.8	2.8	2.5	3.7	3.4	4.3	2.7	3.6
Nonfarm business sector											
Output per hour		4.1	3.0	0.0	1.2	0.5	1.8	3.6	0.9	3.5	0.3
Compensation per hour		2.6	5.2	3.7	3.3	4.0	2.6	3.9	4.9	4.6	4.0
Unit labor cost		-1.5	2.2	3.7	2.1	3.6	0.7	0.3	4.0	1.1	3.7

1. Private-industry workers.

Strictly Confidential <FR>
Class II FOMC

REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS, QUARTERLY VALUES
(Seasonally adjusted, annual rate except as noted)

December 16, 1998

		Projected									
Item	Units	1998 Q3	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2	2000 Q3	2000 Q4
EXPENDITURES											
Nominal GDP	Bill. $	8537.1	8624.6	8719.1	8783.0	8852.6	8931.8	8996.6	9095.8	9191.6	9288.6
Real GDP	Bill. Ch. $	7568.7	7627.6	7674.3	7706.5	7741.2	7784.1	7802.1	7857.0	7908.1	7960.0
Real GDP	% change	3.8	3.1	2.5	1.7	1.8	2.2	0.9	2.8	2.6	2.7
Gross domestic purchases		4.3	3.8	3.0	2.4	2.2	2.4	1.2	3.2	2.9	2.7
Final sales		2.9	4.4	2.5	1.7	1.8	1.8	1.6	2.4	2.3	2.7
Priv. dom. final purchases		3.8	5.5	3.4	2.7	2.4	2.2	1.8	2.9	3.0	3.1
Personal cons. expenditures		4.1	4.1	3.1	2.9	2.5	2.3	1.9	2.9	2.6	2.7
Durables		2.3	14.7	0.6	4.1	2.0	2.1	2.2	4.5	5.1	5.5
Nondurables		2.1	3.4	2.9	2.3	2.2	1.9	1.9	1.9	1.9	1.9
Services		5.4	2.4	3.7	2.9	2.7	2.5	1.8	3.1	2.5	2.5
Business fixed investment		-0.3	12.2	4.6	4.3	4.6	2.9	2.7	4.2	6.5	6.8
Producers' dur. equipment		-0.7	19.2	8.1	6.8	6.8	4.5	4.0	5.6	8.5	8.6
Nonres. structures		0.7	-5.7	-4.9	-2.8	-1.8	-1.7	-1.0	0.2	0.8	1.6
Residential structures		9.4	10.5	4.7	-4.3	-3.3	-1.7	-1.7	-1.3	-0.4	0.9
Exports		-3.0	2.7	1.1	2.2	3.1	3.8	3.2	4.5	5.6	5.9
Imports		1.8	7.8	5.7	7.5	5.9	4.6	4.6	7.3	7.3	5.7
Gov't. cons. & investment		1.8	2.8	1.6	1.1	1.3	1.1	1.7	2.4	1.1	0.7
Federal		-1.3	3.7	-0.6	-1.9	-1.4	-2.0	-0.1	1.9	-2.0	-3.0
Defense		4.3	-3.5	-1.4	-2.6	-2.0	-1.9	-2.0	-1.6	-0.9	1.0
State & local		3.4	2.5	2.8	2.7	2.7	2.7	2.6	2.6	2.7	2.6
Change in bus. inventories	Bill. Ch. $	55.9	31.7	31.5	31.2	30.7	39.5	26.6	36.5	42.6	42.9
Nonfarm		47.6	23.8	24.9	26.2	26.9	36.9	24.4	34.2	40.3	40.8
Net exports		-257.9	-274.7	-289.6	-307.4	-318.4	-324.0	-331.3	-343.7	-354.0	-358.4
Nominal GDP	% change	4.7	4.2	4.5	3.0	3.2	3.6	2.9	4.5	4.3	4.3
EMPLOYMENT AND PRODUCTION											
Nonfarm payroll employment	Millions	126.1	126.8	127.3	127.8	128.1	128.4	128.7	129.1	129.2	129.4
Unemployment rate	%	4.6	4.5	4.4	4.5	4.6	4.7	4.8	4.8	4.9	4.9
Industrial prod. index	% change	0.9	1.4	1.5	1.7	1.7	2.9	0.2	2.9	3.4	3.6
Capacity util. rate - mfg.	%	80.3	79.8	79.5	79.3	79.2	79.3	78.9	79.1	79.4	79.7
Housing starts	Millions	1.63	1.69	1.60	1.56	1.55	1.54	1.53	1.52	1.52	1.52
Light motor vehicle sales		14.55	15.69	15.28	15.19	14.96	14.73	14.48	14.50	14.57	14.69
North Amer. produced		12.55	13.62	13.27	13.15	12.97	12.77	12.57	12.59	12.65	12.76
Other		2.01	2.07	2.01	2.04	1.99	1.96	1.91	1.91	1.92	1.93
INCOME AND SAVING											
Nominal GNP	Bill. $	8510.2	8599.4	8689.0	8751.2	8817.7	8892.6	8953.0	9052.7	9145.0	9238.5
Nominal GNP	% change	4.3	4.3	4.2	2.9	3.1	3.4	2.7	4.5	4.1	4.2
Nominal personal income		4.3	4.9	4.5	3.4	3.8	3.5	4.5	4.2	3.6	3.6
Real disposable income		3.1	3.5	5.4	1.4	1.9	1.6	3.8	2.2	1.6	1.6
Personal saving rate	%	0.2	0.0	0.6	0.3	0.1	-0.0	0.5	0.3	0.1	-0.2
Corp. profits, IVA & CCAdj.	% change	3.1	-1.6	-1.7	-5.7	-3.8	-2.5	-14.7	9.5	8.5	6.5
Profit share of GNP	%	9.7	9.6	9.4	9.2	9.1	8.9	8.5	8.6	8.7	8.8
Excluding FR Banks		9.4	9.3	9.2	9.0	8.8	8.7	8.3	8.4	8.5	8.5
Federal surpl./deficit	Bill. $	91.0	80.9	64.4	74.2	80.5	85.7	70.5	79.9	93.9	101.3
State & local surpl./def.		149.9	164.6	157.2	157.3	155.6	154.9	161.0	161.8	162.5	163.3
Ex. social ins. funds		82.5	97.1	89.7	89.8	88.1	87.4	93.5	94.3	95.0	95.8
Gross natl. saving rate	%	17.3	17.1	17.0	16.8	16.6	16.4	16.4	16.4	16.4	16.3
Net natl. saving rate		7.3	7.1	7.1	6.8	6.6	6.4	6.3	6.4	6.4	6.4
PRICES AND COSTS											
GDP chn.-wt. price index	% change	0.8	1.0	1.9	1.3	1.4	1.4	2.0	1.6	1.6	1.6
Gross Domestic Purchases chn.-wt. price index		0.5	1.0	1.7	1.4	1.4	1.4	1.9	1.5	1.5	1.5
CPI		1.7	2.0	2.3	2.4	2.2	2.2	2.2	2.2	2.2	2.2
Ex. food and energy		2.3	2.5	3.0	2.1	2.1	2.1	2.3	2.3	2.3	2.3
ECI, hourly compensation[1]		4.4	3.6	3.3	3.3	3.2	3.2	3.2	3.2	3.2	3.6
Nonfarm business sector											
Output per hour		2.7	0.8	1.5	1.0	1.2	1.5	-0.0	2.6	2.5	2.5
Compensation per hour		4.0	3.6	3.8	3.4	3.4	3.4	3.5	3.2	3.2	3.6
Unit labor cost		1.3	2.8	2.3	2.4	2.2	1.9	3.5	0.6	0.7	1.1

1. Private-industry workers.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3	96Q4/ 95Q4	97Q4/ 96Q4	98Q4/ 97Q4
Real GDP	2.1	4.2	4.2	4.0	4.2	3.0	5.5	1.8	3.8	3.9	3.8	3.6
Gross dom. purchases	3.5	1.9	5.5	4.4	4.7	3.2	7.9	4.0	4.4	4.2	4.4	5.0
Final sales	0.9	5.1	2.9	2.7	5.7	2.1	4.3	4.6	2.9	3.7	3.3	4.0
Priv. dom. final purchases	2.5	2.7	3.8	2.7	5.9	2.4	7.0	6.1	3.2	3.6	3.7	5.2
Personal cons. expenditures	1.3	2.0	2.9	1.1	4.2	1.9	4.1	4.1	2.8	2.2	2.5	3.4
Durables	-0.2	0.6	1.0	-0.1	1.3	0.3	1.2	0.9	0.2	0.5	0.6	0.9
Nondurables	0.2	0.6	0.7	-0.0	1.0	-0.1	1.4	1.0	0.4	0.6	0.4	0.9
Services	1.2	0.8	1.2	1.3	1.9	1.7	1.4	2.1	2.2	1.2	1.5	1.7
Business fixed investment	1.4	0.9	0.7	1.4	1.7	0.2	2.2	1.4	-0.0	1.2	1.0	1.2
Producers' dur. equip.	1.1	0.2	0.6	1.6	1.3	0.1	2.4	1.4	-0.1	0.8	0.9	1.3
Nonres. structures	0.2	0.6	0.1	-0.2	0.4	0.0	-0.2	-0.1	0.0	0.3	0.1	-0.1
Residential structures	-0.1	-0.2	0.1	0.2	-0.0	0.3	0.6	0.6	0.4	0.2	0.2	0.5
Net exports	-1.3	2.4	-1.2	-0.5	-0.5	-0.3	-2.2	-2.1	-0.6	-0.3	-0.6	-1.4
Exports	0.2	3.2	1.0	1.8	1.2	0.5	-0.3	-0.9	-0.3	1.2	1.1	-0.3
Imports	-1.6	-0.9	-2.2	-2.2	-1.7	-0.8	-1.9	-1.2	-0.2	-1.4	-1.7	-1.1
Government cons. & invest.	-0.3	0.0	0.4	0.4	0.3	0.0	-0.3	0.6	0.3	0.4	0.3	0.3
Federal	-0.3	-0.4	-0.2	0.2	-0.1	-0.1	-0.6	0.4	-0.1	0.1	-0.0	0.0
Defense	-0.3	-0.4	-0.5	0.4	-0.1	-0.1	-0.8	0.4	0.2	-0.0	-0.1	-0.1
Nondefense	0.0	0.0	0.3	-0.2	0.0	-0.1	0.3	0.1	-0.3	0.1	0.0	0.1
State and local	0.0	0.4	0.6	0.2	0.3	0.2	0.2	0.2	0.4	0.3	0.3	0.3
Change in bus. inventories	1.2	-0.8	1.3	1.3	-1.4	0.9	1.2	-2.7	0.9	0.2	0.5	-0.5
Nonfarm	1.3	-0.5	1.5	0.9	-1.5	1.0	1.2	-2.8	0.9	0.1	0.5	-0.5
Farm	-0.1	-0.3	-0.2	0.4	0.1	-0.1	0.0	0.1	0.0	0.0	0.0	0.1

Note. Components may not sum to totals because of rounding.

CONTRIBUTIONS TO GROWTH IN REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

Item	1998 Q4	1999 Q1	1999 Q2	1999 Q3	1999 Q4	2000 Q1	2000 Q2	2000 Q3	2000 Q4	98Q4/ 97Q4	99Q4/ 98Q4	00Q4/ 99Q4
Real GDP	3.1	2.5	1.7	1.8	2.2	0.9	2.8	2.6	2.7	3.6	2.1	2.3
Gross dom. purchases	3.9	3.1	2.4	2.2	2.4	1.2	3.3	3.0	2.8	5.0	2.5	2.6
Final sales	4.4	2.5	1.7	1.8	1.8	1.5	2.4	2.3	2.6	4.0	2.0	2.2
Priv. dom. final purchases	4.6	2.8	2.2	2.1	1.8	1.5	2.4	2.5	2.6	5.2	2.2	2.3
Personal cons. expenditures	2.8	2.1	2.0	1.7	1.6	1.3	2.0	1.8	1.9	3.4	1.8	1.8
Durables	1.2	0.1	0.3	0.2	0.2	0.2	0.4	0.4	0.4	0.9	0.2	0.4
Nondurables	0.7	0.6	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.9	0.5	0.4
Services	1.0	1.5	1.2	1.1	1.0	0.7	1.3	1.0	1.0	1.7	1.2	1.0
Business fixed investment	1.3	0.5	0.5	0.5	0.3	0.3	0.5	0.7	0.7	1.2	0.4	0.5
Producers' dur. equip.	1.4	0.6	0.5	0.5	0.4	0.3	0.4	0.7	0.7	1.3	0.5	0.5
Nonres. structures	-0.2	-0.1	-0.1	-0.1	-0.0	-0.0	0.0	0.0	0.0	-0.1	-0.1	0.0
Residential structures	0.4	0.2	-0.2	-0.2	-0.1	-0.1	-0.1	-0.0	0.0	0.5	-0.1	-0.0
Net exports	-0.7	-0.6	-0.7	-0.4	-0.2	-0.3	-0.5	-0.4	-0.1	-1.4	-0.5	-0.3
Exports	0.3	0.1	0.2	0.3	0.4	0.3	0.5	0.6	0.6	-0.3	0.3	0.5
Imports	-1.0	-0.7	-1.0	-0.8	-0.6	-0.6	-0.9	-1.0	-0.8	-1.1	-0.8	-0.8
Government cons. & invest.	0.5	0.3	0.2	0.2	0.2	0.3	0.4	0.2	0.1	0.3	0.2	0.3
Federal	0.2	-0.0	-0.1	-0.1	-0.1	-0.0	0.1	-0.1	-0.2	0.0	-0.1	-0.0
Defense	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.0	0.0	-0.1	-0.1	-0.0
Nondefense	0.4	0.0	-0.0	-0.0	-0.0	0.1	0.2	-0.1	-0.2	0.1	-0.0	-0.0
State and local	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Change in bus. inventories	-1.2	-0.0	-0.0	-0.0	0.4	-0.6	0.5	0.3	0.0	-0.5	0.1	0.0
Nonfarm	-1.2	0.1	0.1	0.0	0.5	-0.6	0.5	0.3	0.0	-0.5	0.2	0.0
Farm	0.0	-0.1	-0.1	-0.1	-0.1	-0.0	-0.0	-0.0	-0.0	0.1	-0.1	-0.0

Note. Components may not sum to totals because of rounding.

Strictly Confidential (FR)
Class II FOMC

STAFF PROJECTIONS OF FEDERAL SECTOR ACCOUNTS AND RELATED ITEMS
(Billions of dollars except as noted)

December 16, 1998

Item	Fiscal year[5]				1998				1999				2000			
	1997[a]	*1998[a]*	*1999*	*2000*	Q1[a]	Q2[a]	Q3[a]	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
UNIFIED BUDGET					Not seasonally adjusted											
Receipts[1]	1579	1721	1787	1848	378	544	412	408	404	541	433	425	417	559	446	433
Outlays[1]	1601	1651	1706	1747	409	407	409	463	396	421	425	441	448	432	427	445
Surplus/deficit[1]	-22	70	81	101	-30	137	3	-55	8	120	8	-16	-30	127	19	-12
On-budget	-103	-29	-43	-34	-51	87	1	-57	-47	67	-5	-55	-54	70	6	-54
Off-budget	81	99	124	134	21	50	2	2	55	53	13	39	24	58	14	42
Surplus excluding deposit insurance[2]	-36	66	77	97	-31	136	2	-56	7	119	7	-16	-31	127	18	-13
Means of financing																
Borrowing	38	-51	-71	-105	26	-82	-29	30	0	-101	0	5	20	-100	-30	-3
Cash decrease	1	5	-1	0	4	-45	33	18	0	-15	-5	10	10	-25	5	20
Other[3]	-17	-24	-9	4	0	-10	-8	6	-8	-5	-3	1	1	-3	6	-5
Cash operating balance, *end of period*	44	39	40	40	28	72	39	21	20	35	40	30	20	45	40	20
NIPA FEDERAL SECTOR					Seasonally adjusted annual rate											
Receipts	1687	1818	1885	1931	1809	1838	1858	1879	1875	1886	1899	1913	1916	1937	1958	1978
Expenditures	1728	1761	1809	1848	1750	1764	1765	1797	1810	1811	1818	1827	1846	1857	1863	1876
Consumption expend.	458	458	470	479	451	464	458	464	473	471	471	470	481	485	483	480
Defense	306	301	304	306	293	303	303	301	306	304	304	303	308	307	307	308
Nondefense	152	157	166	173	158	161	155	163	167	167	167	167	173	177	176	171
Other expenditures	1270	1302	1340	1369	1299	1300	1307	1333	1338	1340	1347	1357	1365	1372	1380	1397
Current account surplus	-41	57	75	83	59	74	93	81	65	74	81	86	71	80	94	102
Gross investment	61	60	59	58	61	57	61	60	59	59	58	58	58	58	57	58
Current and capital account surplus	-102	-2	16	25	-2	18	33	21	5	16	22	28	13	23	37	44
FISCAL INDICATORS[4]																
High-employment (HEB) surplus/deficit	-163	-101	-91	-59	-102	-85	-75	-92	-106	-90	-77	-67	-69	-59	-42	-33
Change in HEB, percent of potential GDP	-.8	-.8	-.1	-.4	-.5	-.2	-.1	.2	.2	-.2	-.2	-.1	0	-.1	-.2	-.1
Fiscal impetus (FI), percent, cal. year	-2.1	-2	1.5	-1.2	-2.1	1.1	.3	-.1	2.3	-.6	-.6	-1.3	.3	.5	-.5	-.7

1. OMB's May 1998 surplus estimates (assuming the enactment of the President's proposals) are $39 billion in FY98, $54 billion in FY99 and $61 billion in FY00. CBO's August 1998 baseline surplus estimates are $63 billion in FY98, $80 billion in FY99 and $79 billion in FY00. Budget receipts, outlays, and surplus/deficit include corresponding social security (OASDI) categories. 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 FY90.

2. OMB's May 1998 surplus estimates (assuming the enactment of the President's proposals), excluding deposit insurance spending, are $35 billion in FY98, $51 billion in FY99 and $58 billion in FY00, and CBO's August baseline estimates are $59 billion in FY98, $76 billion in FY99 and $76 billion in FY00.

3. Other means of financing are checks issued less checks paid, accrued items, and changes in other financial assets and liabilities.

4. HEB is the NIPA current and capital account surplus in current dollars, with cyclically sensitive receipts and outlays adjusted to the level of potential output associated with an unemployment rate of 6 percent. Real potential GDP growth is assumed to be 2.8 percent beginning 1995:Q3. Quarterly figures for change in HEB and FI are not at annual rates. Change in HEB, as a percent of nominal potential GDP, is reversed in sign. FI is the weighted difference of discretionary changes in federal spending and taxes in chained (1992) dollars, scaled by real federal consumption plus investment. For change in HEB and FI, negative values indicate restraint.

5. Fiscal year data for the unified budget come from OMB; quarterly data come from the Monthly Treasury Statement and may not sum to OMB fiscal year totals.

a--Actual.

Strictly Confidential Class II FOMC
December 16, 1998

Change in Debt of the Domestic Nonfinancial Sectors
(Percent)

			Nonfederal						Memo:
				Households					
Period [1]	Total [2]	Federal government [3]	Total [4]	Total	Home mortgages	Consumer credit	Business	State and local governments	Nominal GDP
Year									
1990	6.4	11.0	5.2	7.5	9.6	1.5	3.1	5.0	4.4
1991	4.3	11.1	2.3	4.7	6.4	-1.3	-1.7	8.6	3.8
1992	4.6	10.9	2.6	4.3	5.2	0.5	0.8	2.2	6.3
1993	5.0	8.3	3.8	5.3	4.3	7.6	1.6	6.0	5.0
1994	4.6	4.7	4.6	7.5	5.8	14.5	4.0	-4.0	5.8
1995	5.4	4.1	5.8	7.7	5.5	14.1	6.7	-4.6	4.2
1996	5.3	4.0	5.8	7.7	8.0	7.9	5.2	-0.6	5.8
1997	5.3	0.6	7.0	6.9	7.5	4.3	7.5	5.3	5.6
1998	6.2	-1.4	8.8	8.6	9.2	6.0	9.5	6.6	4.5
1999	4.8	-2.6	7.1	7.7	8.3	4.8	6.7	5.5	3.6
2000	3.9	-3.1	5.8	5.7	6.3	2.6	6.1	4.9	4.0
Quarter									
1997:3	5.6	0.8	7.3	6.8	9.1	4.1	7.9	6.7	5.4
4	6.4	1.1	8.2	7.3	8.2	3.0	9.1	8.4	4.2
1998:1	6.1	-0.8	8.3	7.9	8.4	4.5	8.8	8.4	6.4
2	6.1	-1.9	8.7	8.4	9.1	5.1	9.4	6.9	2.7
3	5.9	-3.6	9.0	8.3	9.1	6.8	10.4	6.3	4.7
4	6.3	0.5	8.0	8.7	8.9	7.2	8.2	4.1	4.2
1999:1	4.9	-4.0	7.6	8.4	9.0	5.7	7.1	6.0	4.5
2	4.7	-2.5	6.8	7.5	8.0	5.5	6.4	5.1	3.0
3	4.8	-1.5	6.6	7.1	7.9	4.1	6.4	5.2	3.2
4	4.5	-2.5	6.4	6.7	7.5	3.4	6.3	5.6	3.6

Note. Quarterly data are at seasonally adjusted annual rates.

1. Data after 1998:Q3 are staff projections. Changes are measured from end of the preceding period to end of period indicated except for annual nominal GDP growth, which is calculated from Q4 to Q4.
2. On a monthly average basis, total debt is projected to grow 6.3 percent in 1998 and 5.0 percent in 1999.
3. On a monthly average basis, federal debt is projected to grow -1.2 percent in 1998 and -2.2 percent in 1999.
4. On a monthly average basis, nonfederal debt is projected to grow 8.8 percent in 1998 and 7.2 percent in 1999.

2.6.3 FOF

Flow of Funds Projections: Highlights
(Billions of dollars except as noted)

					Seasonally adjusted annual rates									
	Calendar year				1997		1998				1999			
Category	1997	1998	1999	2000	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net funds raised by domestic nonfinancial sectors														
1 Total	655.1	692.1	679.8	592.8	705.6	811.8	782.9	809.3	708.8	467.5	690.4	678.1	679.3	671.3
2 Net equity issuance	-114.4	-254.9	-98.5	-63.4	-124.0	-143.3	-139.2	-128.7	-221.8	-530.0	-105.6	-94.6	-116.8	-76.8
3 Net debt issuance	769.6	947.0	778.2	656.2	829.6	955.1	922.1	938.0	930.6	997.5	796.0	772.7	796.1	748.1
Borrowing sectors														
Nonfinancial business														
4 Financing gap [1]	74.3	104.5	121.3	152.1	51.3	83.3	119.1	97.2	106.3	95.7	103.8	115.4	124.9	141.1
5 Net equity issuance	-114.4	-254.9	-98.5	-63.4	-124.0	-143.3	-139.2	-128.7	-221.8	-530.0	-105.6	-94.6	-116.8	-76.8
6 Credit market borrowing	334.8	455.5	350.9	341.1	363.8	427.1	420.6	460.2	521.6	419.5	370.8	342.7	345.7	344.7
Households														
7 Net borrowing [2]	355.6	472.5	457.8	366.2	362.9	394.9	437.2	469.8	472.7	510.3	504.2	460.4	442.4	424.4
8 Home mortgages	261.9	345.7	342.5	278.9	327.5	302.0	316.1	351.7	356.2	358.7	369.7	334.7	338.8	326.6
9 Consumer credit	52.5	76.3	63.8	36.9	50.3	37.8	57.3	65.1	88.2	94.8	76.4	74.8	56.5	47.3
10 Debt/DPI (percent) [3]	91.8	95.2	98.3	100.8	92.0	92.7	93.6	94.7	95.7	96.6	96.9	98.1	99.0	99.9
State and local governments														
11 Net borrowing	56.1	73.5	66.2	61.9	72.6	92.3	94.3	78.9	72.7	48.0	71.2	61.2	63.2	69.2
12 Current surplus [4]	135.6	185.6	191.8	202.7	117.6	171.5	179.1	169.4	192.6	201.2	194.4	185.1	194.0	194.0
Federal government														
13 Net borrowing	23.1	-54.4	-96.7	-113.0	30.3	40.8	-30.0	-70.9	-136.5	19.7	-150.1	-91.5	-55.1	-90.1
14 Net borrowing (quarterly, n.s.a.)	23.1	-54.4	-96.7	-113.0	10.6	33.7	25.9	-81.8	-28.8	30.3	-0.2	-100.9	-0.4	4.9
15 Unified deficit (quarterly, n.s.a.)	2.4	-54.9	-120.5	-104.3	10.9	39.7	30.2	-136.9	-3.0	54.9	-7.9	-120.0	-8.3	15.6
Depository institutions														
16 Funds supplied	336.3	291.7	293.5	267.4	204.4	470.7	319.5	147.0	301.1	399.3	322.5	298.1	278.7	274.4
Memo (percentage of GDP)														
17 Domestic nonfinancial debt [5]	182.8	184.6	187.6	188.8	182.0	182.8	182.8	184.3	185.0	185.9	186.4	187.3	188.1	188.5
18 Domestic nonfinancial borrowing	9.5	11.1	8.8	7.2	10.2	11.6	11.0	11.1	10.9	11.6	9.1	8.8	9.0	8.4
19 Federal government [6]	0.3	-0.6	-1.1	-1.2	0.4	0.5	-0.4	-0.8	-1.6	0.2	-1.7	-1.0	-0.6	-1.0
20 Nonfederal	9.2	11.8	9.9	8.4	9.8	11.1	11.4	12.0	12.5	11.3	10.9	9.8	9.6	9.4

Note. Data after 1998:Q3 are staff projections.
1. For corporations: Excess of capital expenditures over U.S. internal funds.
2. Includes change in liabilities not shown in lines 8 and 9.
3. Average debt levels in the period (computed as the average of period-end debt positions) divided by disposable personal income.
4. NIPA surplus less changes in retirement fund assets plus consumption of fixed capital.
5. Average debt levels in the period (computed as the average of period-end debt positions) divided by nominal GDP.
6. Excludes government-insured mortgage pool securities.

International Developments

The negative balance in net exports is expected to deteriorate over the forecast period, but at a diminishing rate as the effects of past dollar appreciation wane and foreign growth begins to recover. Our forecast for the external sector of the U.S. economy is little changed from that presented in the November Greenbook. Recent data indicate some slowing of economic activity in Europe but further signs of stabilization, and in some cases a pickup, in output in the developing economies of Asia. Monetary policy has eased in many countries, most notably in Europe, since the last FOMC meeting. While the change in monetary policy in Europe came sooner than we expected, these trends were largely anticipated in the last Greenbook.

The situation in Brazil remains a major downside risk to the foreign outlook. The IMF and a large group of bilateral creditors have put in place a substantial support package for Brazil. But the failure of Brazil's congress to approve one part of the government's fiscal reform package has undermined investor confidence, and capital continues to flow out. President Cardoso's government remains committed to fiscal reform, and our forecast continues to be built on the assumption that Brazil's economic program will succeed. If this assumption proves incorrect, however, the implications for global financial markets and for economic activity in Latin America over the forecast period could be quite negative.

Recent Developments

International financial markets. Since the November FOMC meeting, the dollar has depreciated about 1 percent against a weighted average of 35 currencies. The impeachment proceedings against President Clinton as well as renewed concerns about Brazil weighed on the dollar over the intermeeting period. The dollar depreciated 3 percent against the yen and 1/4 percent against the mark. The yen appreciated as long-term interest rates in Japan increased almost 50 basis points over the period. Yields on Japanese long-term government bonds increased in anticipation of further fiscal stimulus and following the nationalization of Nippon Credit Bank on December 14. A coordinated interest rate cut by euro-area central banks on December 3, which took market participants by surprise, contributed to the stability of the dollar relative to the currencies of those countries. All euro-area central banks except the Bank of Italy lowered their key official rates to 3 percent, largely completing the process of short-term interest rate convergence before the introduction of the euro in January. Declines in official short-term interest rates, as well as weaker-than-expected economic data, contributed to declines of 30 to 50 basis points in yields on long-term government bonds in euro-area countries.

After the easing of U.S. monetary policy at the last FOMC meeting, financial conditions affecting emerging market countries continued to improve. But the improvement was reversed late in the period after the lower house of Brazil's congress rejected the proposed public sector pension reform just hours after the IMF had approved Brazil's Fund program. The congress passed the other pieces of the fiscal package, and the government plans to resubmit the measure that failed in January. Brazil is in the process of drawing $9.3 billion on its IMF and bilateral credit lines. Capital outflows from Brazil continued, and totaled $3.4 billion over the intermeeting period. Spreads on Brazilian Brady bonds widened by about 240 basis points, on net, over the intermeeting period.

Credit spreads on Brady bonds for other emerging market countries also widened in recent weeks, but they were generally little changed for the intermeeting period as a whole. The Mexican peso has moved little since the November meeting, although short-term domestic interest rates edged up late in the period. In most emerging market economies in Asia share prices increased in recent weeks. The announcement of plans to restructure five major industrial groups gave Korean financial markets a lift, contributing to a nearly 30 percent increase in equity prices and an 8 percent appreciation of the won over the intermeeting period.

Economic activity abroad. Recent data suggest that the pace of growth in most major industrial countries has slowed over the past several months. Japan remains mired in a deep recession. Real GDP fell 2.6 percent (s.a.a.r.) in the third quarter, with a double-digit decline in investment. Retail sales and auto registrations fell again in October, and the ratio of job offers-to-applicants fell to a new low. The December Tankan survey showed declines in business confidence, but the results were not out of line with expectations. In Germany, orders for manufactured goods in October were more than 3-1/2 percent below their level in July, and business confidence has deteriorated substantially over the same period. German industrial production rebounded somewhat in October, but it remains below the third-quarter average after sharp declines in the previous two months. In France, both business confidence and consumption of manufactured goods have weakened since the end of the third quarter. Recent indicators for the British economy are also quite weak: Retail sales fell in October, business and consumer confidence remained depressed, and surveys indicate that inventories were seen as excessive. The one exception to this pattern of weakness in recent months may be Canada. Substantial increases in orders for manufactured goods in October and employment in November suggest a healthy pickup in growth in the fourth quarter, but recent production trends have been difficult to gauge because of strikes in manufacturing and construction.

Consumer price inflation in major industrial countries is very subdued, reflecting low or negative inflation in import prices, especially for commodities, and output that is below potential in most of the major foreign industrial countries. On a twelve-month basis, inflation is close to zero in Japan, is at or below 1 percent in Germany, France, and Canada, and is 1-1/2 percent in Italy. In the United Kingdom, retail price inflation appears to have stabilized at a rate of 2-1/2 percent.

There is more evidence of a bottoming out of activity in developing Asia. In the third quarter, economic activity appears to have accelerated in China and Taiwan. The staff estimates that real GDP growth in Korea turned positive on a seasonally adjusted basis in the third quarter for the first time this year. The pace of real GDP declines in Indonesia and Malaysia diminished significantly in the third quarter, and industrial production appears to have stabilized in Thailand in recent months.

After growing strongly in the first of the year, real GDP in Brazil and Argentina fell sharply in the third quarter. In both cases, higher interest rates needed to maintain currency pegs contributed to the declines. Although low oil prices have reduced Mexico's exports, economic growth appears to have been maintained in the third quarter.

Inflation remains at or near single-digit levels in most major emerging market countries. The only significant exception to this pattern in Asia is Indonesia, where consumer price inflation on a year-over-year basis has leveled out at about 70 percent. In Latin America, consumer price inflation remains elevated in Mexico (17 percent) and in Venezuela (31 percent). Inflation in Russia has picked up significantly since the sharp ruble devaluation starting in mid-August. The twelve-month change in Russian consumer prices in November was 67 percent, compared with just 7 percent in the second quarter.

U.S. net exports and prices. In September, the U.S. trade deficit in goods and services was $14.0 billion, significantly smaller than in August. The value of exports increased 2-1/4 percent in September, owing largely to increased shipments of aircraft and automotive products following the settlement of the GM strike. Exports to a number of developing countries in Asia appear to have stopped falling. Nominal imports decreased slightly in September, as increases in automotive products from Canada were largely offset by the decline in the value of oil imports. For the third quarter as a whole the trade deficit was up only modestly from the previous quarter. The increased deficit in real net exports in the third quarter reduced the growth of real GDP by 0.6 percentage point (s.a.a.r.).

Prices of non-oil imports edged up in October and November, marking the first time since 1995 that these prices increased two months in a row. For all major trade categories except computers and non-oil industrial supplies, import prices swung from declines in previous quarters to increases in October-November. Prices of exports declined in October and then rose slightly in November. Increases in prices of agricultural exports–particularly for grain and oilseed–more than offset small price declines for other export products. The spot price of West Texas Intermediate reached $14.39 in October–because of weather-driven delays in delivery, civil unrest in Nigeria and Colombia, and decreased production due to maintenance in the North Sea–but has since fallen to around $12 per barrel owing to weak demand and the inability of major producers to implement agreed production cuts in full.

The U.S. current account deficit widened $18 billion (s.a.a.r.) in the third quarter to $245 billion. The increase resulted primarily from a widening in the deficit on investment income (importantly from a reduction in direct investment receipts from abroad). The deficit in goods trade in the third quarter was virtually unchanged from the second quarter.

Outlook

The staff expects foreign real GDP growth (weighted by U.S. nonagricultural export shares) to pick up from an annual rate of about 3/4 percent in the second half of this year to about 1-1/2 percent next year, and 2-1/4 percent in 2000. This is still well below the average rate during 1992-96. Relative to the November forecast, we have added about two tenths of a percentage point to foreign growth in the first half of 1999 and about one tenth thereafter. These revisions reflect small changes in a number of countries. We project that U.S. real net exports will decline enough to subtract about 1/2 percentage point from U.S. GDP growth in 1999 and about 1/4 percentage point from growth in 2000.

Our forecast continues to assume that the international support package for Brazil, combined with Brazil's own internal efforts, will succeed in stabilizing financial markets in Latin America and other emerging markets. For this to happen the prospects for continued reform must be sufficient to engender a recovery of investor confidence and a return to some net private capital inflows, permitting lower interest rates. In light of current uncertainties, we see a significant chance that the Brazilian reform program will fail, which implies substantial downside risk to the foreign outlook. While our assessment is that the consequences of such failure are essentially unchanged from the last FOMC meeting, the possibility of failure may be somewhat higher.

Summary of Staff Projections
(Percentage change from end of previous period)

Measure	Projection					
	1998			1999		2000
	H1	Q3	Q4	H1	H2	
Foreign output	.0	1.1	.3	1.2	2.0	2.3
November	*.0*	*.2*	*-.0*	*.9*	*1.9*	2.2
Real exports	-5.3	-3.0	2.7	1.6	3.4	4.8
November	*-5.3*	*-3.7*	*-.1*	*1.5*	*3.2*	*4.7*
Real imports	12.5	1.8	7.8	6.6	5.3	6.2
November	*12.5*	*3.8*	*6.9*	*6.9*	*5.4*	*6.5*

The dollar. We project that the trade-weighted exchange value of the dollar against the major foreign currencies will decline from current levels, as growing current account surpluses in Japan and the euro area and a growing current account deficit in the United States begin to generate pressures for exchange rate adjustments. External imbalances are projected to affect the dollar's rate against the yen only with a lag, however. Further deterioration in economic activity in Japan and limited progress in resolving banking sector problems are expected to weigh on the yen for some time. Because of the offsetting nature of these effects in the near term, we project the dollar to average about current levels against the yen before declining late in the forecast period. We continue to forecast that the dollar will decline against the Canadian dollar as global recovery and firmer commodity prices help the Canadian dollar regain some of the ground it has lost during 1998.

Our forecast calls for the real exchange value of the dollar against a broad group of 35 currencies to edge down over the forecast period; real dollar depreciation against the major currencies, most Asian emerging-market currencies, and the Mexican peso is nearly offset by appreciation against South American currencies and the Chinese renminbi. The renminbi, which has remained essentially unchanged against the dollar in nominal terms over the past year and a half, is projected to undergo some adjustment later in the forecast period, as Chinese authorities begin to allow some modest depreciation. The dollar is projected to rise against the Brazilian *real* in nominal and price-adjusted terms as macroeconomic policy adjustments and external financial assistance allow Brazil to maintain its crawling currency peg with no resurgence of inflation. In this context, we continue to assume that the Argentine and Hong Kong currency pegs will hold.

Activity in foreign industrial countries. The staff projects that real GDP growth in foreign industrial countries will rise from an annual rate of 1-1/2 percent in the first half of 1999 to about 2 percent in the second half and into 2000. These rates of growth are marginally higher than in the November forecast, reflecting increases in a number of other industrial countries that are partially offset by downward revisions to the outlook for the United Kingdom.

Incoming data have not changed our basic outlook for Japan. We expect that Japanese GDP will decline at an annual rate of about 1 percent in the first half of 1999 and continue to fall, although at somewhat slower rates, well into 2000. Annual real output growth in the euro area is expected to remain near 2-1/4 percent through the forecast period, sustained by domestic demand. Real GDP growth in the United Kingdom is projected to slow sharply in the near term but to pick up moderately later next year and in 2000 in response to recent and projected interest rate cuts. Growth in Canada has been revised up in the near term owing to recent indicators and the stronger outlook for U.S. growth.

Inflation. Consumer price inflation in foreign industrial countries (on a four-quarter basis and weighted by U.S. non-oil import shares) is projected to be 3/4 percent in 1999 before picking up to about 1 percent in 2000. The projected pickup largely reflects a swing in inflation in Japan. Japanese consumer prices are projected to fall 1 percent, on a Q4/Q4 basis, next year and level out in 2000.

Interest rates. The coordinated reduction in interest rates by euro-area central banks in December came sooner than we anticipated in the last Greenbook. But the interest rate cuts did not have a significant impact on our forecast because they merely brought forward by a few months interest rate cuts we had already assumed. Statements by euro-area monetary policy officials are consistent with the view that euro-area policy rates are likely to hold at current levels for some time. We expect short-term interest rates in the euro area to remain at current levels for the rest of the forecast period. The recent signs of weakness in the U.K. economy have led us to lower our projection for sterling short-term interest rates. We now assume that the Bank of England will lower short-term rates another 75 basis points by the middle of next year. Consistent with a somewhat stronger outlook for the Canadian economy, we now expect short-term interest rates to decline only slightly from current levels over the forecast horizon.

Other countries. Led by a turnaround in Asian developing economies, the real GDP of major developing-country trading partners of the United States is projected to increase about 3/4 percent at an annual rate during the first half of 1999, somewhat faster than we projected in November. We project that real GDP in Asian developing countries will expand 1-1/2 percent for 1999 as a whole, and more than 3 percent in 2000. This is about 1/2 percent stronger in 1999 than we anticipated in the last Greenbook.

We now expect real GDP in Latin America, after falling in the fourth quarter, to increase at an annual rate of about 1/2 percent in the first half of 1999 and rise 2-1/2 percent in 2000. This forecast is marginally weaker than our last, owing to a weaker outlook for Brazil. In light of the problems in implementing the Brazilian reform package, we now anticipate that interest rates will decline more slowly than we had previously assumed. Accordingly, our forecast for Brazilian growth in the first half of 1999 has been marked down about 1-1/2 percentage points to an annual rate of decline of 4.5 percent. Success of the Brazilian program should relieve financial market pressures and support growth in other Latin American countries, particularly Argentina. Inflation in major developing economies (weighted by U.S. non-oil import shares) is expected to decline from about 8 percent in the first half of 1999 to 7 percent in 2000.

Real exports and imports of goods and services. Recent monthly trade data have led us to raise the projected growth of real exports of goods and services in the fourth quarter. We now project that the decline in real net exports will subtract 0.7 percentage point from GDP growth for the quarter at an annual rate.

Looking beyond the fourth quarter, we have revised up the growth of exports in light of a modestly weaker dollar and somewhat stronger foreign growth. Total exports are expected to increase at an annual rate of 1-3/4 percent in the first half of 1999 and pick up to a growth rate of 4-3/4 percent in 2000. This acceleration in export growth reflects, primarily, a pickup in the growth of core goods exports (goods exports excluding agricultural products, computers and semiconductors) following declines in 1998.

After increasing at a brisk pace of about 8 percent in the fourth quarter, we expect the growth of imports of goods and services to ease as the U.S. economy decelerates and the dollar depreciates. We are now projecting total imports to increase at an annual rate of about 6 percent over both 1999 and 2000, a modest downward revision from our previous forecast that reflects primarily the impact of a weaker outlook for the dollar. The quantity of oil imports should decline this quarter and next as inventories are drawn down from unusually high levels. Thereafter we project that oil imports will rise a bit faster than consumption as U.S. oil production is adversely affected by low oil prices.

Oil prices. The staff has lowered its projected path for the price of imported oil in the near term to reflect recent decreases in spot oil prices caused by OPEC production above agreed levels and weaker-than-expected consumption, particularly in Asia. We project that the oil import price will be about $11.55 per barrel in the fourth quarter of 1998, slightly less than in the third quarter. We assume that OPEC production will hold at current levels through 1999. Combined with increased consumption as world activity expands, this supply outcome should support somewhat higher oil prices. We expect oil import prices to increase steadily in 1999 from around $10.50 per barrel in the first quarter to about $13.30 per barrel in the fourth quarter. For 2000, we predict an oil import price of $13.50 per barrel.

Selected Trade Prices
(Percentage change from end of previous period except as noted; seasonally adjusted)

Trade category	Projection					
	1998			1999		2000
	H1	Q3	Q4	H1	H2	
Exports						
Nonagricultural (core)	-2.1	-2.4	-1.5	1.7	1.9	1.4
Agricultural	-11.0	-8.2	-1.8	0.0	2.0	2.1
Imports						
Non-oil (core)	-2.6	-3.3	.5	1.6	1.4	1.4
Oil (level, dollars per barrel)	12.51	11.60	11.54	11.86	13.28	13.50

NOTE. Prices for exports and non-oil imports of goods, excluding computers and semiconductors, are on a NIPA chain-weighted basis.

The price of imported oil for multiquarter periods is the price for the final quarter of the period.

Prices of non-oil imports and exports. The slowdown in global growth continues to put downward pressure on the prices of traded goods. However recent and projected depreciation of the dollar is expected to push up commodity prices (expressed in dollars) and U.S. import and export prices. After falling almost 14 percent in the first three quarters of this year, commodity prices are expected to be about flat in the fourth quarter and to increase 3-1/4 percent in 1999 and somewhat less in 2000. We expect core import prices to follow a similar pattern. After falling for the last two years core import price inflation is expect to increase to 1-1/2 percent (s.a.a.r.) in the first half of 1999 before slowing to 1-1/4 percent by the second half of 2000 as the effects of the dollar's recent sharp depreciation wane. Nonagricultural export prices for core goods are expected to fall at a 1-1/2 percent annual rate in the fourth quarter. Prices of core export goods are expected to rise in 1999 and 2000 owing to the increases in comparable domestic prices and the end of the effects of past dollar appreciation.

Nominal trade and current account balances. The nominal trade deficit for goods and services is projected to widen significantly further over the forecast period, from about $198 billion in the fourth quarter of this year to about $270 billion in the fourth quarter of 2000. The deficit for net investment income also is projected to widen. As a result, the current account deficit is expected to grow from $270 billion in the current quarter (just over 3 percent of GDP) to an average of more than $340 billion for the year 2000 (almost 3.7 percent of GDP, just above the previous peak for this ratio which was reached in 1987).

Risks to the Foreign Outlook.

Pessimistic Brazil. The situation in Brazil remains precarious. The government has taken a number of significant steps to reduce Brazil's long-term fiscal problems. Nonetheless, investor confidence about the ability of the government to meet its ambitious, but necessary, targets for economic policy reform remains fragile. While we continue to believe that the single most likely outcome among a range of alternatives is that the Brazilian program will succeed and the government will be able to maintain its current exchange rate regime, the chances that this will not happen appear to have increased somewhat since the last FOMC meeting, and, consequently, the downside risks to the foreign outlook have also increased.

In this context, we believe that the alternative scenario presented in the last Greenbook, one involving a failure of Brazil's IMF program possibly combined with wider financial disruptions (proxied by a 10 percent drop in the U.S. stock market), remains the most relevant alternative scenario. In that projection we assumed that a failure of the Brazilian program would cause the *real* to depreciate 30 percent in real terms against the dollar over the next several months relative to the Greenbook baseline and Brazil's GDP growth would fall 8 percentage points relative to baseline during 1999 and 2 percentage points during 2000. Contagion to other countries in Latin America was assumed to force the Argentine peso off its peg and other currencies to depreciate significantly. The impact of these alternative assumptions on our forecast for the U.S. economy is presented in the table below. As we did in the last Greenbook, we want to note that this is by no means a "worst case" concerning the potential effects of a meltdown in Brazil on both global and U.S. GDP.

Dollar depreciation. The projected widening of global current account imbalances poses risks to our assumed path for the dollar. If market participants become concerned about the sustainability of the U.S. net external asset position the dollar could depreciate sharply. To illustrate the implications of such an outcome we have simulated the effect of additional across the board depreciation of the dollar relative to its baseline path that reaches 10 percent at the end of 1999 and is held at that level through 2000. Note that this simulation assumes that the direct impact of the shift in the demand for U.S. dollar assets falls only on the exchange rate and not U.S. interest rates or stock prices. The results of this simulation are shown in the table below. Under the assumption that U.S. monetary policy does not respond to this sharp depreciation of the dollar U.S. GDP and inflation rise noticeably, particularly in 2000.

Impact of Alternative Assumptions*
(Percent change, Q4 to Q4)

Measure	1999	2000
U.S. Real GDP		
Baseline	2.0	2.3
Pessimistic Brazil**	1.4	1.5
Dollar depreciation	2.2	3.2
U.S. CPI ex. food and energy		
Baseline	2.3	2.3
Pessimistic Brazil**	2.2	1.9
Dollar depreciation	2.5	2.8

*All simulations assume fixed Federal Funds rate.

** Assumes U.S. stock market falls an additional 10 percent.

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Class II FOMC

December 16, 1998

OUTLOOK FOR FOREIGN REAL GDP AND CONSUMER PRICES: SELECTED COUNTRIES
(Percent, Q4 to Q4)

Measure and country	1992	1993	1994	1995	1996	1997	1998 (Projected)	1999 (Projected)	2000 (Projected)
REAL GDP (1)									
Total foreign	2.2	3.3	5.1	2.0	4.1	4.1	0.4	1.6	2.3
Industrial Countries	0.6	1.8	4.0	1.7	2.6	3.3	1.6	1.7	1.9
of which:									
Canada	0.9	2.9	5.5	1.1	1.7	4.4	2.3	2.3	2.4
Japan	0.1	0.5	0.9	2.5	5.1	-0.8	-2.7	-0.7	-0.2
United Kingdom	0.7	3.2	4.6	1.9	2.6	4.0	1.5	1.0	2.1
Euro-11	0.1	-0.1	3.4	1.3	1.9	3.1	2.5	2.3	2.2
Germany	0.9	-0.2	3.4	0.0	2.1	2.3	2.6	2.2	2.2
Developing Countries	4.6	5.5	6.7	2.6	6.3	5.1	-1.2	1.3	2.7
Asia	6.7	8.3	8.3	6.8	7.0	5.0	-3.9	1.5	3.2
Korea	2.4	8.1	9.5	7.3	7.1	3.9	-7.9	0.6	3.1
China	14.6	13.1	12.1	10.0	9.4	7.9	7.1	6.3	6.8
Latin America	3.1	2.6	5.7	-4.1	6.2	5.9	1.5	1.1	2.4
Mexico	2.8	1.9	5.2	-7.0	7.1	6.7	3.3	2.6	2.7
Brazil	0.1	4.4	9.6	-1.5	5.0	1.6	-1.0	-3.3	-0.3
CONSUMER PRICES (2)									
Industrial Countries	2.0	2.1	1.1	1.3	1.5	1.6	1.0	0.7	1.1
of which:									
Canada	1.8	1.8	-0.0	2.1	2.0	1.0	1.1	1.3	1.5
Japan	0.9	1.2	0.8	-0.8	0.1	2.1	0.3	-1.0	0.0
United Kingdom (3)	3.7	2.7	2.2	2.9	3.2	2.8	2.5	2.4	2.5
Euro-11 (4)	NA	NA	NA	2.7	2.0	1.4	1.2	1.4	1.4
Germany	3.4	4.2	2.6	1.7	1.4	1.8	0.7	1.0	1.1
Developing Countries	21.7	24.8	23.0	17.0	11.2	6.9	8.8	7.6	7.0
Asia	5.5	7.7	10.7	6.4	4.8	2.8	4.8	3.0	3.9
Korea	4.7	5.5	5.8	4.4	5.1	5.0	6.2	5.9	4.9
China	8.2	17.1	26.9	11.1	7.0	1.0	-0.8	0.2	3.6
Latin America	72.4	74.5	54.6	42.2	26.0	15.6	15.4	15.0	12.1
Mexico	13.2	8.6	6.9	48.8	28.1	17.2	17.2	16.5	13.2
Brazil	1150.1	2321.7	1237.1	22.5	10.5	4.2	2.9	2.4	2.4

1. Foreign GDP aggregates calculated using shares of U.S. non-agricultural exports.
2. Foreign CPI aggregates calculated using shares of U.S. non-oil imports.
3. CPI excluding mortgage interest payments, which is the targeted inflation rate.
4. Harmonized CPI's, weighted by shares in final consumption of households converted to a common currency using estimated PPP exchange rates.

Strictly Confidential (FR)
Class II FOMC

December 16, 1998

OUTLOOK FOR FOREIGN REAL GDP AND CONSUMER PRICES: SELECTED COUNTRIES
(Percent, quarterly change at an annual rate)

	1998				Projected 1999				Projected 2000			
Measure and country	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
REAL GDP (1)												
Total foreign	-0.8	0.7	1.3	0.3	1.0	1.3	1.7	2.2	1.6	2.3	2.5	2.7
Industrial Countries	2.0	1.1	1.4	1.8	1.5	1.6	1.8	2.1	1.3	2.0	2.2	2.3
of which:												
Canada	3.1	1.4	1.8	3.0	2.2	2.2	2.2	2.7	1.8	2.4	2.6	2.8
Japan	-4.8	-2.9	-2.6	-0.5	-1.5	-0.7	-0.2	-0.2	-1.4	-0.2	0.3	0.6
United Kingdom	3.1	1.9	1.5	-0.6	0.5	0.8	1.1	1.5	1.5	2.0	2.4	2.4
Euro-11	3.3	2.1	2.8	1.8	2.0	2.2	2.3	2.5	1.7	2.4	2.4	2.4
Germany	5.9	0.2	3.5	0.9	1.5	2.3	2.3	2.6	1.7	2.3	2.4	2.4
Developing Countries	-4.6	0.2	1.3	-1.8	0.4	0.9	1.7	2.4	2.1	2.7	3.0	3.1
Asia	-10.2	-3.8	0.7	-2.0	0.3	1.1	1.9	2.8	2.3	3.1	3.6	3.9
Korea	-22.8	-5.1	2.3	-4.1	-1.0	0.5	1.0	2.1	1.8	2.6	3.5	4.5
China	7.3	6.2	10.7	4.5	5.2	6.5	6.5	7.0	6.3	7.0	7.0	7.0
Latin America	1.1	4.9	2.4	-2.2	0.4	0.6	1.5	2.0	1.9	2.5	2.5	2.5
Mexico	1.0	6.1	7.7	-1.6	2.4	2.4	2.8	2.8	2.4	2.8	2.8	2.8
Brazil	2.1	5.4	-5.9	-5.0	-5.0	-4.0	-3.0	-1.0	-1.0	0.0	0.0	0.0
CONSUMER PRICES (2)												
Industrial Countries	1.4	1.1	0.8	1.0	0.7	0.6	0.6	0.7	0.9	0.9	1.1	1.1
of which:												
Canada	1.0	1.0	0.9	1.1	1.2	1.2	1.3	1.3	1.4	1.4	1.5	1.5
Japan	2.1	0.6	-0.1	0.3	-0.7	-1.3	-1.5	-1.0	-0.7	-0.5	0.0	0.0
United Kingdom (3)	2.5	3.0	2.6	2.5	2.5	2.4	2.4	2.4	2.5	2.4	2.5	2.5
Euro-11 (4)	1.2	1.5	1.2	1.2	1.2	1.2	1.3	1.4	1.4	1.4	1.4	1.4
Germany	1.2	1.3	0.8	0.7	0.8	0.9	0.9	1.0	1.0	1.1	1.1	1.1
Developing Countries	7.3	7.6	8.0	8.8	8.0	8.2	8.2	7.6	7.3	7.0	6.9	7.0
Asia	4.2	4.6	4.6	4.8	3.6	3.4	3.1	3.0	3.1	3.3	3.5	3.9
Korea	8.9	8.2	7.0	6.2	2.5	3.8	5.3	5.9	5.5	5.1	4.9	4.9
China	0.4	-0.9	-1.4	-0.8	-0.1	1.3	1.3	0.2	0.6	1.4	2.4	3.6
Latin America	14.1	14.2	14.3	15.4	14.7	15.3	16.0	15.0	13.8	13.0	12.3	12.1
Mexico	15.3	15.1	15.6	17.2	16.4	17.4	18.0	16.5	15.2	14.2	13.5	13.2
Brazil	4.4	4.5	3.6	2.9	1.7	0.8	1.7	2.4	2.4	2.4	2.4	2.4

1. Foreign GDP aggregates calculated using shares of U.S. non-agricultural exports.
2. Foreign CPI aggregates calculated using shares of U.S. non-oil imports.
3. CPI excluding mortgage interest payments, which is the targeted inflation rate.
4. Harmonized CPI's, weighted by shares in final consumption of households converted to a common currency using estimated PPP exchange rates.

Strictly Confidential (FR)
Class II FOMC

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1992	1993	1994	1995	1996	1997	------ Projected ------ 1998	1999	2000
NIPA REAL EXPORTS and IMPORTS									
	Percentage point contribution to GDP growth, Q4/Q4								
Net Goods & Services	-0.4	-0.6	-0.4	0.5	-0.3	-0.6	-1.4	-0.5	-0.3
Exports of G&S	0.4	0.5	1.0	1.1	1.2	1.1	-0.3	0.3	0.5
Imports of G&S	-0.8	-1.1	-1.4	-0.7	-1.4	-1.7	-1.1	-0.8	-0.8
	Percentage change, Q4/Q4								
Exports of G&S	4.1	4.6	10.0	10.5	10.3	9.6	-2.8	2.5	4.8
Services	-0.9	4.1	6.0	9.8	7.5	1.5	-2.8	2.5	2.0
Agricultural Goods	10.4	-5.5	16.6	-4.3	4.8	2.8	-10.8	-1.7	0.2
Computers	25.2	23.7	32.0	55.5	35.9	40.7	8.7	26.6	28.3
Semiconductors	64.8	32.9	66.9	79.6	46.2	21.0	6.5	20.7	23.6
Other Goods 1/	2.3	3.6	7.0	5.8	8.0	11.6	-3.4	-0.1	3.6
Imports of G&S	7.4	10.2	12.3	5.6	11.8	14.0	8.5	5.9	6.2
Services	1.4	3.2	1.4	6.1	5.5	12.4	1.7	1.9	3.0
Oil	12.1	10.1	-0.2	2.4	7.9	4.0	4.4	3.2	5.3
Computers	45.1	39.3	44.8	48.1	24.4	30.3	24.6	28.2	28.0
Semiconductors	42.0	34.2	54.5	92.4	57.6	32.7	-4.0	26.2	26.2
Other Goods 2/	5.4	9.5	12.2	-1.2	10.4	13.0	9.7	4.5	4.5
	Billions of chained 1992 dollars								
Net Goods & Services	-29.5	-70.2	-104.6	-96.5	-111.2	-136.1	-244.1	-309.9	-346.8
Exports of G&S	639.4	658.2	712.4	792.6	860.0	970.0	975.0	983.8	1022.7
Imports of G&S	669.0	728.4	817.0	889.0	971.2	1106.1	1219.1	1293.7	1369.5
	Billions of dollars								
US CURRENT ACCOUNT BALANCE	-51.4	-86.1	-123.8	-115.3	-134.9	-155.2	-231.8	-299.4	-341.7
Net Goods & Services (BOP)	-38.7	-71.9	-100.9	-99.9	-108.6	-110.2	-174.2	-228.7	-259.0
Exports of G&S (BOP)	617.3	643.2	703.8	795.6	850.8	937.6	922.0	921.6	959.9
Imports of G&S (BOP)	656.0	715.2	804.7	895.5	959.3	1047.8	1096.2	1150.2	1219.0
Net Investment Income	22.5	23.9	16.5	19.3	14.2	-5.3	-16.1	-29.0	-40.9
Direct, Net	51.6	55.7	51.8	63.0	66.2	63.7	58.0	51.3	56.4
Portfolio, Net	-29.1	-31.7	-35.3	-43.7	-51.9	-69.1	-74.2	-80.4	-97.3
Net Transfers	-35.2	-38.1	-39.4	-34.6	-40.6	-39.7	-41.5	-41.8	-41.8

1. Merchandise exports excluding agricultural products, computers, and semiconductors.
2. Merchandise imports excluding oil, computers, and semiconductors.

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1995 Q1	1995 Q2	1995 Q3	1995 Q4	1996 Q1	1996 Q2	1996 Q3	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1997 Q4
NIPA REAL EXPORTS and IMPORTS												
Percentage point contribution to GDP growth												
Net Goods & Services	-0.2	-0.3	1.6	0.7	-1.1	-1.0	-1.4	2.4	-1.3	-0.4	-0.5	-0.3
Exports of G&S	1.0	0.6	1.9	1.1	0.4	0.6	0.2	3.2	0.9	1.7	1.2	0.5
Imports of G&S	-1.2	-0.9	-0.3	-0.4	-1.5	-1.6	-1.6	-0.9	-2.2	-2.2	-1.7	-0.8
Percentage change from previous period, SAAR												
Exports of G&S	9.2	5.4	17.8	10.2	3.7	5.8	2.1	32.0	8.3	15.5	10.6	4.4
Services	9.1	2.9	21.7	6.4	-4.0	10.3	-9.9	39.8	-6.7	11.8	5.9	-4.0
Agricultural Goo	1.8	-13.4	5.0	-9.4	22.6	-32.8	-1.6	48.7	-16.1	-7.8	8.7	32.8
Computers	36.4	33.8	86.6	71.6	57.6	24.7	27.7	35.9	70.2	78.7	41.9	-9.2
Semiconductors	72.0	100.8	96.2	53.6	23.8	29.7	30.2	118.6	41.3	17.3	32.3	-2.2
Other Goods 1/	4.3	1.4	9.4	8.1	0.1	6.0	5.7	21.3	13.8	15.6	9.2	8.0
Imports of G&S	9.8	7.2	2.0	3.5	13.1	13.5	13.6	7.0	18.6	17.9	13.5	6.3
Services	20.5	-3.3	3.1	5.5	9.2	4.3	9.9	-1.1	17.8	10.6	15.8	5.8
Oil	-11.4	15.4	31.4	-18.2	-9.8	68.9	3.5	-14.0	-8.2	37.0	6.0	-12.2
Computers	15.4	51.6	62.7	69.3	22.5	22.9	18.8	33.8	54.5	39.0	30.6	2.9
Semiconductors	37.1	105.5	128.2	113.3	38.7	8.9	50.1	172.1	89.0	16.0	20.3	17.6
Other Goods 2/	7.2	1.5	-8.8	-3.8	13.9	10.5	13.5	4.2	16.2	16.1	11.8	8.1
Billions of chained 1992 dollars, SAAR												
Net Goods & Services	-109.5	-114.7	-86.8	-74.8	-95.5	-113.5	-140.1	-95.9	-121.5	-131.6	-142.4	-149.0
Exports of G&S	763.9	774.0	806.3	826.1	833.6	845.5	849.9	911.1	929.4	963.6	988.1	998.8
Imports of G&S	873.4	888.7	893.1	900.9	929.1	958.9	990.0	1007.0	1050.9	1095.2	1130.5	1147.8
Billions of dollars, SAAR												
US CURRENT ACCOUNT BALANCE	-123.7	-134.2	-115.5	-87.7	-112.9	-132.0	-161.6	-133.2	-148.0	-140.4	-152.4	-180.2
Net Goods & Services (BOP)	-109.3	-125.8	-90.0	-74.5	-92.4	-112.8	-132.3	-96.8	-112.5	-106.1	-108.4	-113.8
Exports of G&S (BOP)	765.4	782.0	809.7	825.6	833.6	845.3	837.5	886.7	904.7	936.1	951.7	957.8
Imports of G&S (BOP)	874.7	907.7	899.7	900.1	926.0	958.2	969.8	983.5	1017.3	1042.1	1060.1	1071.7
Net Investment Income	20.1	24.0	10.2	22.7	21.4	15.9	6.9	12.7	0.1	1.8	-6.2	-17.0
Direct, Net	59.9	67.2	56.5	68.3	64.8	64.4	61.9	73.6	64.2	69.6	65.5	55.6
Portfolio, Net	-39.8	-43.2	-46.2	-45.5	-43.3	-48.5	-55.0	-60.9	-64.2	-67.8	-71.7	-72.6
Net Transfers	-34.5	-32.4	-35.8	-35.9	-41.9	-35.1	-36.2	-49.1	-35.5	-36.1	-37.8	-49.3

1. Merchandise exports excluding agricultural products, computers, and semiconductors.
2. Merchandise imports excluding oil, computers, and semiconductors.

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Class II FOMC

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OUTLOOK FOR U.S. INTERNATIONAL TRANSACTIONS

	1998				Projected 1999				Projected 2000			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
NIPA REAL EXPORTS and IMPORTS												
	Percentage point contribution to GDP growth											
Net Goods & Services	-2.3	-2.1	-0.6	-0.7	-0.6	-0.7	-0.4	-0.2	-0.3	-0.5	-0.4	-0.1
Exports of G&S	-0.3	-0.9	-0.3	0.3	0.1	0.2	0.3	0.4	0.3	0.5	0.6	0.6
Imports of G&S	-1.9	-1.2	-0.2	-1.0	-0.7	-1.0	-0.8	-0.6	-0.6	-0.9	-1.0	-0.8
	Percentage change from previous period, SAAR											
Exports of G&S	-2.8	-7.7	-3.0	2.7	1.1	2.2	3.1	3.8	3.2	4.5	5.6	5.9
Services	-1.2	1.7	-10.4	-1.0	3.2	3.0	1.8	2.0	1.0	2.0	2.3	2.8
Agricultural Goods	-9.9	-23.4	-14.1	7.1	3.5	-12.1	0.9	1.8	-6.8	-2.7	8.2	2.6
Computers	-15.5	8.7	20.5	26.2	26.2	26.2	26.7	27.2	27.7	28.2	28.6	28.6
Semiconductors	-2.0	-18.7	30.6	23.9	19.3	20.4	21.6	21.6	22.7	23.9	23.9	23.9
Other Goods 1/	-1.6	-11.0	-1.6	1.1	-3.3	0.2	0.9	1.9	2.0	3.4	4.1	4.7
Imports of G&S	15.7	9.3	1.8	7.8	5.7	7.5	5.9	4.6	4.6	7.3	7.3	5.7
Services	9.3	-0.6	-0.6	-1.1	0.6	1.3	2.5	3.0	1.7	3.8	3.4	3.3
Oil	8.8	41.4	-10.2	-14.1	-12.1	41.6	10.4	-17.6	0.2	29.7	13.4	-16.7
Computers	38.8	22.4	10.3	28.6	29.6	29.6	27.4	26.2	26.2	28.6	28.6	28.6
Semiconductors	9.9	-28.0	-8.3	17.0	26.2	26.2	26.2	26.2	26.2	26.2	26.2	26.2
Other Goods 2/	16.1	10.7	2.9	9.4	5.3	4.8	3.9	4.1	3.1	4.2	5.4	5.3
	Billions of chained 1992 dollars, SAAR											
Net Goods & Services	-198.5	-245.2	-257.9	-274.7	-289.6	-307.4	-318.4	-324.0	-331.3	-343.7	-354.0	-358.4
Exports of G&S	991.9	972.1	964.8	971.2	973.7	979.1	986.6	995.8	1003.6	1014.8	1028.8	1043.6
Imports of G&S	1190.4	1217.3	1222.7	1245.9	1263.3	1286.4	1305.0	1319.8	1334.9	1358.5	1382.8	1401.9
	Billions of dollars, SAAR											
US CURRENT ACCOUNT BALANCE	-186.9	-226.8	-245.2	-268.3	-271.9	-292.9	-305.9	-327.0	-325.9	-334.6	-344.9	-361.2
Net Goods & Services (BOP)	-140.0	-175.5	-183.0	-198.2	-207.8	-227.0	-236.9	-242.8	-248.3	-257.5	-264.3	-266.1
Exports of G&S (BOP)	946.2	922.3	909.3	910.2	910.2	916.8	925.0	934.1	941.8	952.4	965.7	979.8
Imports of G&S (BOP)	1086.2	1097.8	1092.3	1108.4	1118.1	1143.9	1162.0	1177.0	1190.0	1209.9	1230.0	1245.9
Net Investment Income	-9.0	-13.5	-21.8	-20.1	-25.1	-26.9	-29.9	-34.2	-38.6	-38.1	-41.6	-45.1
Direct, Net	62.4	60.7	54.7	54.3	49.7	50.9	52.1	52.7	52.6	56.9	57.7	58.3
Portfolio, Net	-71.3	-74.2	-76.6	-74.5	-74.8	-77.7	-82.0	-86.9	-91.2	-95.0	-99.4	-103.4
Net Transfers	-37.9	-37.8	-40.3	-50.0	-39.0	-39.0	-39.0	-50.0	-39.0	-39.0	-39.0	-50.0

1. Merchandise exports excluding agricultural products, computers, and semiconductors.
2. Merchandise imports excluding oil, computers, and semiconductors.