

August 10, 1988

SUMMARY AND OUTLOOK

Prepared for the Federal Open Market Committee

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

staff's projected growth in real GNP has been revised up in the second half.

Based on USDA crop estimates as of mid-July, the BEA has indicated to the staff that they are projecting that the drought will reduce real farm output about \$11 billion in 1988 on an annual average basis. The staff has incorporated losses of a similar magnitude in the current projection--considerably more than the \$4 billion that was assumed in the June Greenbook. In the GNP projection, these output losses show up primarily as a run-off of private and government farm inventories, and, to a lesser extent, as a drop in agricultural exports. All told, these effects are projected to reduce current-quarter growth about 3/4 percentage point at an annual rate and fourth-quarter growth 1 percentage point--trimming about 1/2 percentage point from the fourth-quarter growth in real GNP in 1988. In 1989, agricultural production is projected to reverse this year's decline, boosting the growth in real GNP by 1-1/2 percentage points and 3/4 percentage point in the first and second quarters respectively.²

| | Real GNP and the Drought (Percent change, annual rate) | | | |
|--|---|-----|------|-----|
| | 1988 | | 1989 | |
| | Q3 | Q4 | Q1 | Q2 |
| Real GNP | 3.1 | 1.8 | 3.6 | 2.5 |
| Real GNP excluding effects of drought | 3.8 | 2.8 | 2.2 | 1.8 |

2. There remains considerable uncertainty surrounding the manner in which the BEA will adjust components of farm output and income in response to emerging information about the drought. Thus, current staff estimates should be viewed as a rough attempt to lay out the dimensions of the effect of the drought on real GNP.

August 10, 1988

CONFIDENTIAL - FR
CLASS II FOMC

STAFF GNP PROJECTIONS

Percent changes, annual rate

| | | Nominal GNP | | Real GNP | | GNP fixed-weighted price index | | GNP deflator | | Unemployment rate (percent) | |
|---------------------------|--------|-------------|---------|----------|---------|-----------------------------------|---------|-----------------|---------|-----------------------------------|---------|
| | | 6/22/88 | 8/10/88 | 6/22/88 | 8/10/88 | 6/22/88 | 8/10/88 | 6/22/88 | 8/10/88 | 6/22/88 | 8/10/88 |
| Annual changes: | | | | | | | | | | | |
| 1986 | <1> | 5.6 | 5.6 | 2.9 | 2.8 | 2.7 | 2.8 | 2.6 | 2.7 | 7.0 | 7.0 |
| 1987 | <1> | 6.0 | 6.8 | 2.9 | 3.4 | 3.4 | 3.6 | 3.0 | 3.3 | 6.2 | 6.2 |
| 1988 | | 6.8 | 7.1 | 3.6 | 3.9 | 4.0 | 4.0 | 3.1 | 3.0 | 5.6 | 5.5 |
| 1989 | | 6.3 | 6.7 | 2.2 | 2.7 | 4.4 | 4.7 | 4.1 | 3.9 | 5.8 | 5.6 |
| Quarterly changes: | | | | | | | | | | | |
| 1987 | Q1 <1> | 8.6 | 8.4 | 4.4 | 4.6 | 4.5 | 4.2 | 4.2 | 3.5 | 6.6 | 6.6 |
| | Q2 <1> | 6.3 | 8.7 | 2.5 | 5.0 | 4.1 | 4.2 | 3.5 | 3.5 | 6.3 | 6.3 |
| | Q3 <1> | 7.3 | 7.7 | 4.3 | 4.5 | 3.4 | 3.7 | 2.8 | 3.1 | 6.0 | 6.0 |
| | Q4 <1> | 7.6 | 8.6 | 4.8 | 6.1 | 3.6 | 3.8 | 2.7 | 2.4 | 5.9 | 5.9 |
| 1988 | Q1 <1> | 5.4 | 5.4 | 3.9 | 3.4 | 3.6 | 3.5 | 1.7 | 1.7 | 5.7 | 5.7 |
| | Q2 <1> | 8.2 | 7.2 | 3.3 | 3.1 | 4.7 | 4.7 | 4.7 | 4.1 | 5.6 | 5.5 |
| | Q3 | 6.3 | 7.3 | 2.1 | 3.1 | 4.4 | 4.6 | 4.2 | 4.0 | 5.7 | 5.4 |
| | Q4 | 6.7 | 6.1 | 2.3 | 1.8 | 4.5 | 4.6 | 4.3 | 4.2 | 5.7 | 5.4 |
| | Q1 | 6.5 | 7.7 | 2.0 | 3.6 | 4.9 | 5.1 | 4.4 | 4.0 | 5.7 | 5.4 |
| | Q2 | 5.5 | 6.4 | 1.7 | 2.5 | 4.1 | 4.6 | 3.7 | 3.8 | 5.8 | 5.5 |
| | Q3 | 6.1 | 5.8 | 2.4 | 2.0 | 4.0 | 4.4 | 3.5 | 3.7 | 5.8 | 5.6 |
| | Q4 | 6.1 | 5.8 | 2.4 | 2.0 | 4.0 | 4.3 | 3.6 | 3.6 | 5.9 | 5.7 |
| Two-quarter changes: <2> | | | | | | | | | | | |
| 1987 | Q2 <1> | 7.5 | 8.5 | 3.4 | 4.8 | 4.4 | 4.2 | 3.9 | 3.5 | - .5 | - .5 |
| | Q4 <1> | 7.4 | 8.1 | 4.6 | 5.3 | 3.6 | 3.7 | 2.8 | 2.7 | - .4 | - .4 |
| 1988 | Q2 <1> | 6.8 | 6.3 | 3.6 | 3.3 | 4.2 | 4.0 | 3.2 | 2.9 | - .3 | - .4 |
| | Q4 | 6.5 | 6.7 | 2.2 | 2.4 | 4.5 | 4.6 | 4.2 | 4.1 | .1 | - .1 |
| 1989 | Q2 | 6.0 | 7.1 | 1.9 | 3.0 | 4.5 | 4.9 | 4.0 | 3.9 | .1 | .1 |
| | Q4 | 6.1 | 5.8 | 2.4 | 2.0 | 4.0 | 4.4 | 3.6 | 3.7 | .1 | .2 |
| Four-quarter changes: <3> | | | | | | | | | | | |
| 1986 | Q4 <1> | 4.5 | 4.8 | 2.2 | 2.0 | 2.3 | 2.7 | 2.2 | 2.8 | - .3 | - .3 |
| 1987 | Q4 <1> | 7.4 | 8.3 | 4.0 | 5.0 | 4.0 | 4.0 | 3.3 | 3.1 | - .9 | - .9 |
| 1988 | Q4 | 6.7 | 6.5 | 2.9 | 2.8 | 4.3 | 4.3 | 3.7 | 3.5 | - .2 | - .5 |
| 1989 | Q4 | 6.0 | 6.4 | 2.1 | 2.5 | 4.2 | 4.6 | 3.8 | 3.8 | .2 | .3 |

<1> Actual.

<2> Percent change from two quarters earlier.

<3> Percent change from four quarters earlier.

August 10, 1988

CONFIDENTIAL - FR
ISS II FOMCGROSS NATIONAL PRODUCT AND RELATED ITEMS
(Seasonally adjusted; annual rate)

| | Units | Projection | | | | | | | | | |
|--------------------------------|------------------|------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| | | 1987 | | 1988 | | 1989 | | | | | |
| | | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| EXPENDITURES | | | | | | | | | | | |
| Nominal GNP | Billions of \$ | 4568.0 | 4662.8 | 4724.5 | 4806.9 | 4892.3 | 4964.7 | 5058.1 | 5136.8 | 5209.9 | 5283.4 |
| Real GNP | Billions of 82\$ | 3865.3 | 3923.0 | 3956.1 | 3986.3 | 4016.9 | 4034.6 | 4070.1 | 4095.3 | 4116.0 | 4136.9 |
| Nominal GNP | Percent change | 7.7 | 8.6 | 5.4 | 7.2 | 7.3 | 6.1 | 7.7 | 6.4 | 5.8 | 5.8 |
| Real GNP | | 4.5 | 6.1 | 3.4 | 3.1 | 3.1 | 1.8 | 3.6 | 2.5 | 2.0 | 2.0 |
| Gross domestic product | | 4.7 | 5.8 | 4.2 | 3.2 | 3.3 | 1.8 | 3.5 | 2.5 | 2.1 | 2.0 |
| Gross domestic purchases | | 4.8 | 5.4 | 1.6 | 1.1 | 2.3 | 1.4 | 2.7 | 1.7 | 1.2 | 1.2 |
| Final sales | | 6.1 | .4 | 3.6 | 5.4 | 3.5 | 3.0 | 2.8 | 2.3 | 2.4 | 2.6 |
| Private dom. final purchases | | 6.6 | -1.3 | 4.3 | 4.0 | 3.4 | 2.4 | 1.6 | 1.5 | 1.5 | 1.4 |
| Personal consumption expend. | | 4.6 | -2.1 | 4.5 | 2.3 | 2.6 | 2.3 | 1.3 | 1.3 | 1.3 | 1.3 |
| Durables | | 16.5 | -17.3 | 14.7 | 7.2 | 1.6 | 1.2 | -1.8 | .1 | .6 | .6 |
| Nondurables | | .9 | -.6 | 1.0 | -2.0 | 1.3 | 1.9 | 1.4 | .2 | .2 | .2 |
| Services | | 3.7 | 2.2 | 4.0 | 3.9 | 3.9 | 2.9 | 2.3 | 2.3 | 2.3 | 2.3 |
| Business fixed investment | | 28.4 | 1.7 | 7.6 | 14.0 | 8.6 | 5.1 | 6.2 | 5.1 | 3.7 | 2.5 |
| Producers' durable equipment | | 29.4 | -2.4 | 21.6 | 14.8 | 12.0 | 7.7 | 7.0 | 6.5 | 5.5 | 4.5 |
| Nonresidential structures | | 25.6 | 13.4 | -22.4 | 11.8 | -.4 | -2.1 | 3.9 | 1.1 | -1.5 | -3.5 |
| Residential structures | | -10.7 | 1.3 | -6.5 | 2.8 | -.2 | -2.3 | -6.4 | -5.7 | -2.5 | -.8 |
| Exports | | 25.7 | 17.7 | 25.7 | 8.0 | 16.8 | 14.6 | 15.5 | 13.8 | 12.0 | 11.4 |
| Imports | | 23.4 | 9.9 | 6.9 | -6.2 | 8.6 | 10.1 | 7.6 | 7.0 | 5.5 | 4.6 |
| Government purchases | | 5.7 | 5.0 | -7.9 | .4 | -.2 | 3.2 | 3.3 | 1.9 | 2.2 | 3.1 |
| Federal | | 12.6 | 6.7 | -21.0 | -3.0 | -3.1 | 4.8 | 5.0 | 1.6 | 2.2 | 4.2 |
| Defense | | 7.3 | -1.9 | -5.3 | -5.5 | -10.6 | -.2 | 2.2 | -1.1 | -1.6 | -.9 |
| State and local | | .6 | 3.8 | 3.5 | 2.9 | 1.9 | 2.0 | 2.0 | 2.0 | 2.2 | 2.3 |
| in business inventories | Billions of 82\$ | 13.0 | 67.1 | -66.0 | 45.0 | 41.7 | 30.2 | 38.1 | 40.2 | 36.6 | 31.1 |
| arm | Billions of 82\$ | 18.3 | 68.2 | 51.9 | 33.9 | 39.1 | 42.1 | 39.0 | 36.2 | 33.0 | 32.3 |
| orts | Billions of 82\$ | -130.7 | -126.0 | -109.0 | -90.1 | -82.7 | -79.5 | -71.3 | -63.9 | -56.0 | -47.2 |
| EMPLOYMENT AND PRODUCTION | | | | | | | | | | | |
| Nonfarm payroll employment | Millions | 102.7 | 103.7 | 104.7 | 105.6 | 106.5 | 107.0 | 107.4 | 107.8 | 108.1 | 108.4 |
| Unemployment rate | Percent* | 6.0 | 5.9 | 5.7 | 5.5 | 5.4 | 5.4 | 5.4 | 5.5 | 5.6 | 5.7 |
| Industrial production index | Percent change | 8.8 | 7.0 | 3.9 | 4.7 | 6.4 | 4.1 | 2.6 | 2.4 | 2.5 | 2.5 |
| Capacity utilization rate-mfg. | Percent* | 81.4 | 82.3 | 82.7 | 83.1 | 83.6 | 83.7 | 83.6 | 83.4 | 83.3 | 83.1 |
| Housing Starts | Millions | 1.62 | 1.53 | 1.48 | 1.47 | 1.47 | 1.41 | 1.37 | 1.35 | 1.34 | 1.34 |
| Auto sales | Millions | 11.42 | 10.02 | 10.79 | 10.76 | 10.44 | 10.52 | 10.05 | 10.02 | 10.05 | 10.03 |
| Domestic | Millions | 7.84 | 6.63 | 7.64 | 7.57 | 7.36 | 7.39 | 7.05 | 7.05 | 7.10 | 7.10 |
| Foreign | Millions | 3.58 | 3.38 | 3.15 | 3.19 | 3.08 | 3.13 | 3.00 | 2.97 | 2.95 | 2.93 |
| INCOME AND SAVING | | | | | | | | | | | |
| Nominal personal income | Percent change | 7.1 | 11.6 | 4.6 | 6.8 | 7.4 | 7.8 | 8.6 | 6.2 | 5.6 | 6.5 |
| Real disposable income | Percent change | 4.8 | 6.9 | 5.0 | -.4 | 4.2 | 2.1 | 3.3 | .5 | .6 | 1.3 |
| Personal saving rate | Percent* | 2.3 | 4.3 | 4.4 | 3.8 | 4.2 | 4.1 | 4.6 | 4.4 | 4.2 | 4.2 |
| Corp. profits with IVA & CCAdj | Percent change | 23.9 | -7.1 | .1 | 12.4 | -2.9 | -7.1 | 8.4 | 6.9 | -2.9 | .7 |
| Profit share of GNP | Percent* | 7.0 | 6.8 | 6.7 | 6.8 | 6.6 | 6.4 | 6.4 | 6.4 | 6.3 | 6.2 |
| Federal govt. surplus/deficit | Billions of \$ | -138.3 | -160.4 | -155.1 | -119.8 | -125.7 | -133.1 | -139.5 | -132.6 | -126.8 | -130.2 |
| State and local govt. surplus | | 52.9 | 49.7 | 55.8 | 51.9 | 58.9 | 62.7 | 67.8 | 70.4 | 71.8 | 72.8 |
| Exc. social insurance funds | | -10.1 | -14.8 | -10.3 | -15.8 | -10.0 | -7.4 | -3.5 | -2.1 | -1.9 | -2.1 |
| PRICES AND COSTS | | | | | | | | | | | |
| GNP implicit deflator | Percent change | 3.1 | 2.4 | 1.7 | 4.1 | 4.0 | 4.2 | 4.0 | 3.8 | 3.7 | 3.6 |
| GNP fixed-weight price index | | 3.7 | 3.8 | 3.5 | 4.7 | 4.6 | 4.6 | 5.1 | 4.6 | 4.4 | 4.3 |
| Cons. & fixed invest. prices | | 3.9 | 4.3 | 2.5 | 4.9 | 4.3 | 4.9 | 4.9 | 4.9 | 4.7 | 4.6 |
| CPI | | 3.6 | 3.9 | 3.2 | 4.9 | 4.3 | 5.1 | 5.3 | 4.9 | 4.8 | 4.8 |
| Exc. food and energy | | 3.6 | 4.2 | 4.4 | 5.0 | 4.5 | 5.3 | 5.2 | 5.2 | 5.2 | 5.2 |
| business sector | | | | | | | | | | | |
| ut per hour | | 3.7 | .9 | 3.4 | -1.7 | .0 | .9 | .5 | .8 | .7 | .8 |
| ensation per hour | | 4.5 | 6.4 | 3.5 | 4.1 | 4.5 | 4.7 | 5.1 | 4.9 | 5.1 | 5.2 |
| labor costs | | .7 | 5.4 | .1 | 5.9 | 4.5 | 3.8 | 4.6 | 4.1 | 4.4 | 4.4 |

* Not at an annual rate.

August 10, 1988

CONFIDENTIAL - FR
CLASS II FOMCGROSS NATIONAL PRODUCT AND RELATED ITEMS
(Seasonally adjusted; annual rate)

| | Units | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | Projection | |
|--------------------------------|------------------|--------|--------|--------|--------|--------|--------|--------|------------|--------|
| | | | | | | | | | 1988 | 1989 |
| EXPENDITURES | | | | | | | | | | |
| Nominal GNP | Billions of \$ | 3052.6 | 3166.0 | 3405.7 | 3772.2 | 4014.9 | 4240.3 | 4526.7 | 4847.1 | 5172.0 |
| Real GNP | Billions of 82\$ | 3248.8 | 3166.0 | 3279.1 | 3501.4 | 3618.7 | 3721.7 | 3847.0 | 3998.5 | 4104.6 |
| Real GNP | Percent change* | .6 | -1.9 | 6.5 | 5.1 | 3.6 | 2.0 | 5.0 | 2.8 | 2.5 |
| Gross domestic product | | .3 | -1.6 | 6.6 | 5.3 | 3.8 | 2.3 | 5.1 | 3.1 | 2.5 |
| Gross domestic purchases | | .8 | -.8 | 8.4 | 6.4 | 4.3 | 2.4 | 4.4 | 1.6 | 1.7 |
| Final sales | | .1 | .3 | 3.7 | 4.7 | 4.6 | 2.5 | 3.0 | 3.9 | 2.5 |
| Private dom. final purchases | | -.3 | .8 | 7.7 | 5.6 | 4.6 | 2.8 | 2.4 | 3.5 | 1.5 |
| Personal consumption expend. | | .2 | 2.9 | 5.4 | 4.1 | 4.6 | 4.2 | 1.8 | 2.9 | 1.3 |
| Durables | | -3.3 | 9.0 | 14.7 | 10.8 | 7.0 | 11.5 | -2.4 | 6.0 | -.1 |
| Nondurables | | .5 | 1.8 | 4.4 | 2.3 | 3.3 | 3.1 | .6 | .5 | .5 |
| Services | | .9 | 2.3 | 3.9 | 3.5 | 5.0 | 2.7 | 4.2 | 3.7 | 2.3 |
| Business fixed investment | | 5.6 | -11.3 | 10.8 | 13.8 | 3.7 | -7.3 | 8.8 | 8.8 | 4.4 |
| Producers' durable equipment | | 2.2 | -12.5 | 20.9 | 14.9 | 4.6 | -2.4 | 9.6 | 13.9 | 5.9 |
| Nonresidential structures | | 11.7 | -9.1 | -4.8 | 11.8 | 1.9 | -17.4 | 6.7 | -4.1 | -.1 |
| Residential structures | | -22.4 | 4.9 | 38.1 | 6.1 | 5.8 | 11.3 | -3.5 | -1.6 | -3.9 |
| Exports | | 2.4 | -13.8 | 5.8 | 5.9 | -2.4 | 5.6 | 18.4 | 16.1 | 13.2 |
| Imports | | 4.9 | -5.9 | 23.8 | 17.4 | 4.5 | 7.6 | 10.4 | 4.7 | 6.2 |
| Government purchases | | 2.9 | 3.8 | -2.7 | 7.9 | 8.6 | 2.9 | 2.3 | -1.2 | 2.6 |
| Federal | | 9.5 | 8.2 | -8.1 | 13.0 | 13.3 | .0 | 2.1 | -6.1 | 3.2 |
| Defense | | 7.6 | 8.8 | 5.1 | 6.5 | 7.1 | 4.8 | 6.0 | -5.4 | -.4 |
| State and local | | -1.3 | .6 | 1.5 | 4.4 | 4.9 | 5.3 | 2.5 | 2.6 | 2.1 |
| Change in business inventories | Billions of 82\$ | 23.9 | -24.5 | -6.4 | 62.3 | 9.1 | 15.4 | 34.4 | 45.7 | 36.5 |
| Nonfarm | Billions of 82\$ | 19.0 | -23.1 | -.1 | 57.8 | 13.4 | 17.9 | 36.9 | 41.8 | 35.1 |
| Exports | Billions of 82\$ | 49.4 | 26.3 | -19.9 | -84.0 | -104.3 | -137.5 | -128.9 | -90.3 | -59.6 |
| Nominal GNP | Percent change* | 9.3 | 3.1 | 10.4 | 8.6 | 6.6 | 4.8 | 8.3 | 6.5 | 6.4 |
| EMPLOYMENT AND PRODUCTION | | | | | | | | | | |
| Nonfarm payroll employment | Millions | 91.2 | 89.6 | 90.2 | 94.5 | 97.5 | 99.5 | 102.3 | 105.9 | 107.9 |
| Unemployment rate | Percent | 7.6 | 9.7 | 9.6 | 7.5 | 7.2 | 7.0 | 6.2 | 5.5 | 5.6 |
| Industrial production index | Percent change* | -1.0 | -7.7 | 14.3 | 6.6 | 1.7 | 1.0 | 5.8 | 4.8 | 2.5 |
| Capacity utilization rate-mfg. | Percent | 78.2 | 70.3 | 73.9 | 80.5 | 80.1 | 79.7 | 81.0 | 83.3 | 83.3 |
| Housing Starts | Millions | 1.10 | 1.06 | 1.71 | 1.77 | 1.74 | 1.81 | 1.63 | 1.46 | 1.35 |
| Auto sales | Millions | 8.56 | 8.00 | 9.18 | 10.43 | 11.09 | 11.52 | 10.34 | 10.63 | 10.04 |
| Domestic | Millions | 6.24 | 5.77 | 6.77 | 7.97 | 8.24 | 8.28 | 7.14 | 7.49 | 7.08 |
| Foreign | Millions | 2.32 | 2.23 | 2.41 | 2.46 | 2.84 | 3.25 | 3.21 | 3.14 | 2.96 |
| INCOME AND SAVING | | | | | | | | | | |
| Nominal personal income | Percent change* | 9.2 | 5.3 | 7.8 | 8.4 | 6.6 | 5.9 | 8.5 | 6.7 | 6.7 |
| Real disposable income | Percent change* | .7 | 1.0 | 5.1 | 4.3 | 2.7 | 3.4 | 3.0 | 2.7 | 1.4 |
| Personal saving rate | Percent | 7.5 | 6.8 | 5.4 | 6.1 | 4.4 | 4.0 | 3.2 | 4.1 | 4.3 |
| Corp. profits with IVA & CCAdj | Percent change* | 2.3 | -19.1 | 70.1 | 7.4 | 9.2 | .9 | 7.6 | .4 | 3.2 |
| Profit share of GNP | Percent | 6.2 | 4.7 | 6.3 | 7.1 | 7.0 | 7.0 | 6.9 | 6.6 | 6.3 |
| Federal govt. surplus/deficit | Billions of \$ | -63.8 | -145.9 | -176.0 | -169.6 | -196.9 | -205.6 | -157.8 | -133.4 | -132.3 |
| State and local govt. surplus | | 34.1 | 35.1 | 47.5 | 64.6 | 65.1 | 61.2 | 52.9 | 57.3 | 70.7 |
| Exc. social insurance funds | | 4.1 | -1.7 | 4.4 | 19.8 | 13.8 | 5.0 | -9.2 | -10.9 | -2.4 |
| PRICES AND COSTS | | | | | | | | | | |
| GNP implicit deflator | Percent change* | 8.7 | 5.2 | 3.6 | 3.4 | 2.9 | 2.8 | 3.1 | 3.5 | 3.8 |
| GNP fixed-weight price index | | 8.5 | 5.0 | 3.9 | 3.7 | 3.3 | 2.7 | 4.0 | 4.3 | 4.6 |
| Cons. & fixed invest. prices | | 8.2 | 4.4 | 3.3 | 3.3 | 3.4 | 2.5 | 4.7 | 4.2 | 4.8 |
| CPI | | 9.6 | 4.4 | 3.2 | 4.1 | 3.5 | 1.3 | 4.4 | 4.4 | 5.0 |
| Exc. food and energy | | 10.2 | 5.2 | 4.2 | 4.8 | 4.3 | 3.9 | 4.3 | 4.8 | 5.2 |
| Nonfarm business sector | | | | | | | | | | |
| Output per hour | | -.6 | 1.0 | 3.6 | 1.5 | 1.5 | 1.2 | 1.9 | .7 | .7 |
| Compensation per hour | | 8.3 | 7.3 | 3.3 | 4.2 | 4.5 | 4.2 | 4.1 | 4.2 | 5.1 |
| Unit labor costs | | 9.0 | 6.2 | -.3 | 2.6 | 2.9 | 3.0 | 2.1 | 3.6 | 4.3 |

* Percent changes are from fourth quarter to fourth quarter.

CONFIDENTIAL - FR
CLASS II FOMC

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

August 10, 1988

| | Projection | | | | | | | | | | Projection | | | |
|--------------------------------|------------|-------|-------|-------|------|-------|------|------|------|------|--|-------|-------|-------|
| | 1987 | | 1988 | | | | 1989 | | | | 1986 | 1987 | 1988 | 1989 |
| | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | (fourth quarter to fourth quarter, net change) | | | |
| Real GNP | 42.3 | 57.7 | 33.1 | 30.2 | 30.6 | 17.7 | 35.6 | 25.2 | 20.7 | 20.9 | 72.3 | 188.3 | 111.6 | 102.3 |
| Gross domestic product | 43.6 | 54.3 | 40.3 | 31.1 | 32.6 | 18.1 | 35.2 | 25.4 | 20.9 | 20.0 | 83.3 | 188.3 | 122.1 | 101.5 |
| Gross domestic purchases | 47.0 | 53.0 | 16.1 | 11.3 | 23.3 | 14.4 | 27.4 | 17.7 | 12.9 | 12.1 | 89.4 | 171.9 | 65.1 | 70.0 |
| Final sales | 57.0 | 3.7 | 34.2 | 51.2 | 33.9 | 29.2 | 27.7 | 23.1 | 24.3 | 26.4 | 90.5 | 110.7 | 148.5 | 101.4 |
| Private dom. final purchases | 51.0 | -10.7 | 33.4 | 31.5 | 27.0 | 19.8 | 13.2 | 12.0 | 12.2 | 11.5 | 85.8 | 76.2 | 111.8 | 48.9 |
| Personal consumption expend. | 28.6 | -13.5 | 28.1 | 14.4 | 16.9 | 14.6 | 8.6 | 8.2 | 8.6 | 8.6 | 99.3 | 45.5 | 74.0 | 34.1 |
| Durables | 15.2 | -18.9 | 13.5 | 7.0 | 1.6 | 1.2 | -1.9 | .1 | .6 | .6 | 40.9 | -9.7 | 23.3 | -.5 |
| Nondurables | 2.1 | -1.4 | 2.2 | -4.5 | 2.9 | 4.2 | 3.1 | .5 | .4 | .4 | 27.0 | 5.2 | 4.8 | 4.6 |
| Services | 11.3 | 6.8 | 12.3 | 12.1 | 12.3 | 9.3 | 7.4 | 7.6 | 7.5 | 7.5 | 31.4 | 50.0 | 45.9 | 30.0 |
| Business fixed investment | 28.0 | 2.0 | 8.6 | 15.8 | 10.3 | 6.3 | 7.7 | 6.5 | 4.8 | 3.3 | -33.6 | 37.5 | 41.0 | 22.2 |
| Producers' durable equipment | 20.9 | -2.0 | 16.7 | 12.3 | 10.4 | 7.0 | 6.5 | 6.1 | 5.3 | 4.4 | -7.6 | 29.2 | 46.4 | 22.3 |
| Nonresidential structures | 7.1 | 4.1 | -8.1 | 3.5 | -.1 | -.7 | 1.2 | .3 | -.5 | -1.1 | -26.1 | 8.3 | -5.4 | -.1 |
| Residential structures | -5.5 | .6 | -3.2 | 1.3 | -.1 | -1.1 | -3.1 | -2.7 | -1.2 | -.4 | 20.3 | -7.0 | -3.1 | -7.4 |
| Change in business inventories | -14.8 | 54.1 | -1.1 | -21.0 | -3.3 | -11.5 | 7.9 | 2.1 | -3.6 | -5.5 | -18.2 | 77.6 | -36.9 | .9 |
| Nonfarm | -6.7 | 49.9 | -16.3 | -18.0 | 5.2 | 3.0 | -3.1 | -2.8 | -3.2 | -.7 | -22.0 | 67.0 | -26.1 | -9.8 |
| Farm | -8.0 | 4.2 | 15.2 | -3.0 | -8.5 | -14.5 | 11.0 | 4.9 | -.4 | -4.8 | 3.8 | 10.6 | -10.8 | 10.7 |
| Net exports | -4.7 | 4.7 | 17.0 | 18.9 | 7.4 | 3.3 | 8.2 | 7.5 | 7.8 | 8.8 | -17.1 | 16.4 | 46.5 | 32.3 |
| Exports | 24.5 | 18.3 | 27.0 | 9.4 | 19.6 | 17.8 | 19.6 | 18.2 | 16.3 | 16.1 | 20.4 | 71.4 | 73.8 | 70.1 |
| Imports | 29.3 | 13.6 | 9.9 | -9.4 | 12.3 | 14.6 | 11.4 | 10.7 | 8.5 | 7.2 | 37.6 | 55.0 | 27.3 | 37.8 |
| Government purchases | 10.7 | 9.7 | -16.2 | .8 | -.5 | 6.1 | 6.3 | 3.6 | 4.3 | 6.0 | 21.8 | 18.1 | -9.8 | 20.3 |
| Federal | 10.0 | 5.6 | -19.9 | -2.5 | -2.6 | 3.8 | 4.0 | 1.3 | 1.8 | 3.4 | -.1 | 7.2 | -21.2 | 10.6 |
| Defense | 4.7 | -1.3 | -3.6 | -3.7 | -7.2 | -.1 | 1.4 | -.7 | -1.0 | -.6 | 11.7 | 15.1 | -14.6 | -.9 |
| Nondefense | 5.3 | 6.9 | -16.3 | 1.2 | 4.6 | 3.9 | 2.6 | 2.0 | 2.8 | 4.0 | -11.8 | -7.9 | -6.6 | 11.5 |
| State and local | .7 | 4.1 | 3.8 | 3.2 | 2.1 | 2.3 | 2.3 | 2.3 | 2.5 | 2.6 | 21.9 | 10.9 | 11.4 | 9.7 |

[illegible]

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

1. Mid-Session Review of the Fiscal 1989 Budget (July 28, 1988). The Congressional Budget Office baseline estimates released March 1988 indicated receipts of \$898 and \$954 billion, outlays of \$1059 and \$1131 billion, and deficits of \$161 and \$177 billion in FY1988 and FY1989, respectively. Their summer update is scheduled to be published August 19.
2. Includes social security receipts and outlays, which are classified as off-budget under current law.
3. Checks issued less checks paid, accrued items, and other transactions.
4. Sponsored agency borrowing includes net debt issuance by Federal Home Loan Banks, the Federal Home Loan Mortgage Corporation (excluding participation certificates), the Federal National Mortgage Association (excluding mortgage-backed securities), Farm Credit Banks, the Student Loan Marketing Association, and the Financing Corporation. The Administration's definition of borrowing by these agencies is somewhat broader.

Outlook for U.S. Net Exports and Related Items
(Billions of Dollars, Seasonally Adjusted Annual Rates)

| | ANNUAL | | | 1987 | | 1988 | | | | 1989 | | | |
|---|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| | 1987- | 1988-P | 1989-P | Q3- | Q4- | Q1- | Q2-P | Q3-P | Q4-P | Q1-P | Q2-P | Q3-P | Q4-P |
| 1. <u>GNP Exports and Imports</u> 1/ | | | | | | | | | | | | | |
| Current \$, Net | -123.0 | -92.4 | -69.4 | -125.2 | -125.7 | -112.1 | -90.6 | -84.4 | -82.5 | -77.4 | -72.7 | -66.8 | -60.6 |
| Exports of G+S | 428.1 | 515.5 | 605.5 | 440.4 | 459.7 | 487.8 | 501.1 | 524.7 | 548.4 | 573.7 | 595.9 | 616.3 | 636.2 |
| Imports of G+S | 551.1 | 607.9 | 674.9 | 565.6 | 585.4 | 599.9 | 591.7 | 609.0 | 630.9 | 651.1 | 668.6 | 683.1 | 696.8 |
| Constant 82 \$, Net | -128.9 | -90.3 | -59.6 | -130.7 | -126.0 | -109.0 | -90.1 | -82.7 | -79.5 | -71.3 | -63.9 | -56.0 | -47.2 |
| Exports of G+S | 427.8 | 507.5 | 578.4 | 440.9 | 459.2 | 486.2 | 495.6 | 515.2 | 533.0 | 552.6 | 570.8 | 587.1 | 603.2 |
| Imports of G+S | 556.7 | 597.8 | 638.0 | 571.6 | 585.2 | 595.1 | 585.7 | 598.0 | 612.5 | 623.9 | 634.6 | 643.1 | 650.3 |
| 2. <u>U.S. Merchandise Trade Balance</u> 2/ | -160.3 | -126.2 | -107.3 | -158.7 | -164.8 | -143.8 | -125.4 | -118.4 | -117.0 | -113.8 | -109.9 | -104.7 | -100.7 |
| Exports | 249.6 | 320.7 | 376.2 | 259.6 | 272.1 | 298.7 | 312.7 | 328.2 | 343.3 | 357.7 | 370.1 | 382.4 | 394.5 |
| Agricultural | 29.5 | 38.5 | 44.9 | 33.1 | 30.5 | 36.1 | 37.7 | 38.9 | 41.4 | 43.8 | 44.6 | 45.3 | 46.0 |
| Non-Agricultural | 220.1 | 282.2 | 331.2 | 226.5 | 241.6 | 262.6 | 275.0 | 289.3 | 301.9 | 313.9 | 325.5 | 337.0 | 348.4 |
| Imports | 409.9 | 446.9 | 483.4 | 418.3 | 436.8 | 442.5 | 438.1 | 446.6 | 460.4 | 471.5 | 480.0 | 487.1 | 495.1 |
| Petroleum and Products | 42.9 | 40.7 | 47.1 | 51.0 | 45.2 | 39.9 | 41.3 | 38.3 | 43.1 | 46.0 | 46.8 | 47.2 | 48.5 |
| Non-Petroleum | 367.0 | 406.2 | 436.3 | 367.2 | 391.7 | 402.5 | 396.8 | 408.3 | 417.3 | 425.6 | 433.2 | 439.9 | 446.6 |
| 3. <u>U.S. Current Account Balance</u> | -154.0 | -149.5 | -127.8 | -167.9 | -134.1 | -159.0 | -149.4 | -150.1 | -139.5 | -132.7 | -130.0 | -126.2 | -122.2 |
| Of Which: Net Investment Income | 20.4 | -10.2 | -9.9 | 4.3 | 50.2 | -2.4 | -10.1 | -19.4 | -9.1 | -6.9 | -9.1 | -11.4 | -12.2 |
| 4. <u>Foreign Outlook</u> 3/ | | | | | | | | | | | | | |
| Real GNP--Ten Industrial 4/ | 2.9 | 3.3 | 2.0 | 5.2 | 3.5 | 4.7 | 1.1 | 2.0 | 2.1 | 1.9 | 2.1 | 2.1 | 2.0 |
| Real GNP--NonOPEC LDC 5/ | 4.2 | 3.2 | 3.6 | 3.5 | 3.1 | 2.9 | 3.1 | 3.3 | 3.6 | 3.8 | 3.7 | 3.6 | 3.4 |
| Consumer Prices--Ten Ind. 4/ | 2.1 | 2.5 | 2.8 | 1.7 | 2.4 | 1.5 | 4.0 | 2.3 | 2.9 | 2.3 | 3.3 | 2.5 | 3.4 |

1/ National Income and Product Account data.

2/ International accounts basis.

3/ Percent change, annual rates.

4/ Weighted by multilateral trade-weights of G-10 countries plus Switzerland; prices are not seasonally adjusted.

5/ Weighted by share in NonOPEC LDC GNP.

P/ Projected

August 10, 1988

RECENT DEVELOPMENTS

Prepared for the Federal Open Market Committee
By the staff of the Board of Governors of the Federal Reserve System

MID-SESSION REVIEW OF THE BUDGET.

Budget Totals
(Billions of dollars)

| | Fiscal years | | | | | |
|----------|--------------|------|------|------|------|------|
| | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 |
| Outlays | 1066 | 1097 | 1157 | 1218 | 1259 | 1299 |
| Receipts | 913 | 974 | 1054 | 1132 | 1194 | 1265 |
| Deficit | 152 | 123 | 102 | 85 | 65 | 34 |

Note: Totals, as reported in the Mid-Session Review, include on-budget accounts plus the Social Security trust fund that is legally categorized as off-budget.

Economic Assumptions

| | Calendar years | | | | | |
|------------------------------------|----------------|------|------|------|------|------|
| | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 |
| -----Percent change, Q4 to Q4----- | | | | | | |
| Nominal GNP | 6.6 | 7.1 | 6.9 | 6.3 | 5.8 | 5.3 |
| Real GNP | 3.0 | 3.3 | 3.3 | 3.2 | 3.2 | 3.2 |
| GNP deflator | 3.5 | 3.7 | 3.5 | 3.0 | 2.5 | 2.0 |
| -----Percent, annual average----- | | | | | | |
| Civilian unemployment rate | 5.6 | 5.3 | 5.2 | 5.1 | 5.1 | 5.1 |
| Interest rate | | | | | | |
| (3-month Treasury bills) | 6.0 | 5.5 | 5.0 | 4.5 | 4.0 | 3.5 |
| (10-year Treasury notes) | 8.5 | 8.1 | 7.0 | 6.0 | 5.0 | 4.5 |

Gramm-Rudman-Hollings Targets
(Billions of dollars)

| | Fiscal years | | | | |
|-------------------------|--------------|------|------|------|------|
| | 1989 | 1990 | 1991 | 1992 | 1993 |
| Target | 136 | 100 | 64 | 28 | 0 |
| Trigger | 146 | 110 | 74 | 38 | 0 |
| Memo: | | | | | |
| G-R-H baseline estimate | | | | | |
| February Budget | 143 | | | | |
| Mid-Session Review | 140 | | | | |

Source: Office of Management and Budget, Mid-Session Review of the Budget, July 1988.

TREASURY AND AGENCY FINANCING¹
(Total for period; billions of dollars)

| | 1988 | | | 1988 | | |
|--|-------|-------------------|-----------------|-------------------|-------------------|-------------------|
| | Q1 | Q2 | Q3 ^e | Jul. ^P | Aug. ^e | Sep. ^e |
| <u>Treasury financing</u> | | | | | | |
| Total surplus/deficit (-) | -37.0 | .9 | -40.1 | -25.8 | -22.4 | 8.1 |
| Means of financing deficit: | | | | | | |
| Net cash borrowing from the public | 42.8 | 18.7 | 29.6 | 4.1 | 16.3 | 9.2 |
| Marketable borrowings/repayments (-) | 34.1 | 11.2 | 27.6 | 3.6 | 15.8 | 8.2 |
| Bills | 3.2 | -10.4 | 11.1 | .4 | 9.5 | 1.2 |
| Coupons | 30.9 | 21.5 | 16.5 | 3.2 | 6.3 | 7.0 |
| Nonmarketable | 8.7 | 7.5 | 2.0 | .5 | .5 | 1.0 |
| Decrease in the cash balance | -.4 | -16.6 | 0.5 | 15.6 | 8.1 | -23.2 |
| Memo: Cash balance at end of period | 23.0 | 39.6 | 39.2 | 24.1 | 16.0 | 39.2 |
| Other ² | -5.4 | -3.0 | 10.0 | 6.2 | -2.1 | 5.9 |
| <u>Federally sponsored credit agencies, net cash borrowing³</u> | | | | | | |
| | 11.1 | 4.2 | -- | 5.0 | -- | -- |
| FHLBs | 2.5 | -.5 | -- | 1.5 | -- | -- |
| FNMA | 2.8 | 4.9 | -- | 1.0 | -- | -- |
| Farm Credit Banks ⁴ | .9 | -.7 | -- | -.9 | -- | -- |
| FAC | -- | -- | -- | .5 | -- | -- |
| FHLMC | 2.5 | -1.5 ^P | -- | .4 | -- | -- |
| FICO | .7 | 1.1 | -- | .6 | -- | -- |
| SLMA | 1.8 | 1.0 | -- | 2.0 | -- | -- |

1. Data reported on a not seasonally adjusted, payment basis.

2. Includes checks issued less checks paid, accrued items and other transactions.

3. Excludes mortgage pass-through securities issued by FNMA and FHLMC.

4. Financial Assistance Corporation, an institution within Farm Credit System, was created in January 1988 by Congress to provide financial assistance to Farm Credit Banks. It first issued bonds in July 1988.

e--staff estimate.

p--preliminary.

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