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CONFIDENTIAL (FR)

CURRENT ECONOMIC and FINANCIAL CONDITIONS

Prepared for the Federal Open Market Committee

By the Staff

BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM

November 4, 1964

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IN BROAD REVIEW

From this point forward, consideration of the course of economic events in the near future can proceed without quite the same attention to some of the earlier uncertainties associated with the elections in the United Kingdom and the United States. Another set of uncertainties--associated with labor contract negotiations in the auto industry--is still in process of final resolution and any current analysis of the significance of recent developments in the economy must take account of the effect of the strike in many areas. Industrial production, for example, will show a sharp decline in October even though output in industries not affected has probably continued to expand. Retail sales have been affected to a lesser extent, with a slight decline in the total despite strength in markets for many products. The household employment data, which do not reflect the strike, show little change in October.

Private demands for cash balances and bank credit slackened in October, no doubt reflecting in part the temporary slowing down in the pace of economic expansion. Thus, the money supply after increasing $800 million in the first half of the month, due largely to a shift from government to private balances, decreased about half a billion dollars in the last half. Total loans and investments at all commercial banks probably declined a little over the month as a whole. Public offerings of corporate bonds have also continued light, though municipal offerings in the public market and corporate private placements remain high.

While reducing their rate of accumulation of demand deposits and currency, individuals and businesses stepped up their accumulation of savings in financial intermediaries. Thus time and savings deposit growth at commercial banks was very high in October, as was growth in savings and loan shareholdings in September, the latest month for which data are available. This combination of somewhat reduced demands for outside financing and availability for investment of an increased volume of savings, together with more confident expectations as to interest rate developments, has resulted in somewhat easier money market conditions and stronger bond markets.

A large deficit in the balance of payments is indicated by early and tentative data for October. The deficit for the month was swollen by increased purchases of new foreign bond issues.

The British Government imposed late last month a 15 per cent surcharge on imports as part of an effort to reduce Britain's large balance of payments deficit. Since then, pressure on the pound in foreign exchange markets has eased considerably.

SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally Adjusted)

	Latest period	Amount			Per cent change: 3/	
		Latest period	Preceding period	Year ago	Year ago	2 years ago
Civilian labor force (mil.)	Sept.'64	74.2	74.3	73.1	1.5	2.7
Unemployment (mil.)	"	3.8	3.8	4.0	-5.5	-6.1
Unemployment (per cent)	"	5.2	5.1	5.5	-	-
Nonfarm employment, payroll (mil.)	"	59.0	58.9	57.5	2.8	5.2
Manufacturing	"	17.5	17.4	17.1	2.2	3.1
Other industrial	"	7.8	7.8	7.7	1.5	3.7
Nonindustrial	"	33.8	33.7	32.7	3.3	6.6
Industrial production (57-59=100)	"	133.9	133.7	125.7	6.5	11.9
Final products	"	132.2	132.9	126.3	4.7	8.9
Materials	"	135.8	134.8	125.0	8.6	15.0
Wholesale prices (57-59=100)1/	"	100.7	100.3	100.3	0.4	-0.5
Industrial commodities	"	100.7	100.8	100.4	0.3	0.2
Sensitive materials	"	99.5	99.4	97.0	2.6	2.6
Farm products and foods	"	99.3	97.7	98.5	0.8	-2.7
Consumer prices (57-59=100)1/	"	108.4	108.2	107.1	1.2	2.2
Commodities except food	"	104.3	104.2	103.7	0.6	1.0
Food	"	107.2	106.9	105.4	1.7	2.3
Services	"	115.5	115.4	113.5	1.8	3.9
Hourly earnings, mfg. ($)	"	2.58	2.55	2.48	4.0	7.5
Weekly earnings, mfg. ($)	"	104.25	103.59	100.83	3.4	6.9
Personal income ($ bil.)2/	"	497.1	494.9	468.9	6.0	11.4
Retail sales, total ($ bil.)	"	22.2	22.3	20.4	8.6	12.2
Autos (million units)2/	"	8.505	8.012	7.180	18.5	30.5
GAF ($ bil.)	"	4.9	5.2	4.6	6.8	10.6
Selected leading indicators						
Housing starts, pvt. (thous.)2/	"	1,484	1,424	1,747	-15.1	9.4
Factory workweek (hours)	"	40.6	40.7	40.7	-0.2	-0.2
New orders, dur. goods ($ bil.)	"	19.9	19.3	18.2	9.1	20.3
New orders, nonel. mach. ($ bil.)	"	2.9	3.0	2.6	12.3	28.9
Common stock prices (1941-43=10)	Oct.'64	84.85	83.41	73.03	16.2	51.1
Inventories, book val. ($ bil.)	Aug.'64	106.7	106.6	102.7	3.9	7.9
Gross national product ($ bil.)2/	QIII'64	627.5	618.6	587.2	6.9	12.3
Real GNP ($ bil., 1963 prices)2/	"	613.8	608.5	586.6	4.6	8.3

1/ Not seasonally adjusted. 2/ Annual rate. 3/ Based on unrounded data.

SELECTED DOMESTIC FINANCIAL SERIES

	Week ended Oct. 30	Four-Week Average	Last six months High	Last six months Low
Money Market 1/ (N.S.A.)				
Federal funds (per cent)	3.45	3.24	3.50	1.50
Treasury bills 3 mo., yield (per cent)	3.57	3.58	3.58	3.43
Net free reserves 2/ (mil. $)	66	84	192	21
Member bank borrowings 2/ (mil. $)	230	305	478	159
Security Markets (N.S.A.)				
Market yields 1/				
5-year Government securities (per cent)	4.07	4.08	4.12	4.00
20-year Government securities	4.20	4.20	4.24	4.15
Corporate new issues, Aaa (per cent)	--	4.45	4.53	4.37
Corporate seasoned, Aaa (per cent)	4.43	4.43	4.43	4.40
Minicipal seasoned, Aaa (per cent)	3.11	3.11	3.12	3.07
FHA home mortgages-30-year (per cent 3/)	5.46	5.46	5.46	5.45
Common stocks - S&P composite index 4/				
Prices, closing (1941-43=10)	84.86	85.01	85.22	79.02
Dividend yield (per cent)	2.95	2.95	3.10	2.93

	Change in Sept.	Average change-- last 3 mos.	Annual rate of change (%) 3 mos.	Annual rate of change (%) 1 year
Banking (S.A., mil. $)				
Total reserves 5/	-97	84	4.7	5.0
Bank loans and investments:				
Total	3,000	1,800	8.4	8.4
Business loans	600	500	11.0	12.0
Other loans	900	500	5.7	12.2
U.S. Government securities	1,000	400	8.0	-1.6
Other securities	500	400	13.2	10.6
Money and liquid assets:				
Demand dep. & currency 5/	500	600	4.6	4.1
Time and savings dep. 5/	1,300	1,200	12.1	12.5
Nonbank liquid assets	2,700	1,000	5.1	6.9

N.S.A.--not seasonally adjusted. S. A.--seasonally adjusted. n.a.--not available.
1/ Average of daily figures. 2/ Averages for statement week ending October 28.
3/ Latest figure indicated is for month of September. 4/ Data are for weekly closing prices. 5/ Preliminary data for month of October.

U.S. BALANCE OF PAYMENTS

	1964 Sept.	1964 Aug.	1964 July	1964 Q-II	1964 Q-I	1963 Year	1962 Year
Seasonally adjusted annual rates, in billions of dollars							
Balance on regular trans.				- 2.7	- .9	- 3.3	- 3.6
Exports 1/	26.9	24.6	24.9	24.2	24.4	21.9	20.6
Imports 1/	-18.5	-18.9	-18.9	-18.3	-17.4	-16.9	-16.1
Trade balance 1/	8.4	5.7	6.0	5.9	7.0	5.0	4.4
Unadjusted monthly averages, in millions of dollars							
Balance on regular trans.	- 66	- 283	- 687	- 192	23	- 272	- 298
Trade balance 1/		388	411	567	587	416	361
Securities transactions		22	- 62	- 64	- 9	- 69	- 80
Bank-reported claims 2/	- 137	- 104	123	- 200	- 211	- 117	- 39
Other		- 589	-1159	- 494	- 344	- 502	- 540
Financing, total	66	283	687	192	- 23	272	298
Special receipts 3/	0	0	0	- 14	68	55	95
Liabilities increase							
To nonofficial 4/	- 126	146	551	37	77	49	16
To official	23	200	172	68	- 151	136	59
Monetary reserves decrease	169	- 63	- 36	101	- 17	32	128
of which: Gold sales	(14)	(-28)	(-6)	(-24)	(15)	(38)	(74)

1/ Balance of payments basis; differs a little from Census basis.
2/ Adjusted for changes in coverage and for long-term claims taken over from nonfinancial concerns.
3/ Other than nonmarketable bonds, which are included in liabilities to official. Advances on military exports are assumed as zero for individual months in absence of information.
4/ Including international institutions (except IMF), commercial banks and private nonbank.

General Motors, which consumes about 50 per cent of the steel mill products shipped to the automotive industry, apparently has not cancelled orders for steel originally scheduled for shipment in October, but has extended shipping dates. Trade reports indicate that supplying steel mills have continued to produce and inventory these orders for General Motors. Steel ingot production has not been adversely affected by the strike and has increased seasonally.

The chances for a full rebound of production in November are clouded. General Motors' output will still be relatively low in the first week of November as settlements at the plant-level are not yet complete. Also, there is the possibility of a strike at Ford if local settlements are not completed by the end of this week.

<u>Prices</u>. The daily index of raw industrial commodities has risen further in recent weeks, reflecting chiefly additional increases among nonferrous metals. However, the broader measures of prices--for industrial commodities and for all commodities--have remained relatively stable and the consumer price index has continued to rise at the slow pace of recent years.

According to the latest monthly figures for mid-September, the total wholesale price index and the major groupings for foodstuffs and industrial commodities were stable from mid-August to mid-September. The mid-September monthly indexes showed that of the 70 subgroups of industrial commodities, 32 were unchanged from the month before, while 22 were up and 16 were down. Compared with last December, only 3 subgroups were unchanged, while 44 were up and 23 were down, but the weighted average of all subgroups of industrial commodities was unchanged.

Since mid-September, according to the weekly estimates, the total index has continued to change little but stability in the total has resulted from a moderate decrease in foodstuffs and a small increase in industrial commodities. The rise shown for industrial commodities--weekly estimates for which are based on a very small sample of prices--reflects mainly recent further increases for lead, zinc, and scrap metals and some seasonal recovery for petroleum products.

Some of the price increases announced during the summer had not been reflected in the BLS indexes by mid-September and presumably did not actually go into effect. Specifically, the increases announced by producers in July and August for paper bags, passenger car tires, upholstered furniture, and some aluminum and stainless steel products do not show up in the indexes. Since mid-September, there have been announcements of price increases for other commodities, including woodpulp, printing papers, and a few steel products, but there is little evidence available yet to indicate the extent to which recent announced increases are holding.

The monthly figures through mid-September show that prices of machinery and equipment, on the average, have been stable since July following a rise of about 1 per cent over the preceding year. Compared with early 1963, prices are up about 4 per cent for metal-working and construction equipment and 2 per cent for agricultural equipment; transportation equipment is unchanged and the heavily weighted electrical machinery group is down 1 per cent.

Much attention has been focussed in recent months on the BLS daily index of raw industrial commodities, which is examined closely for its predictive value with respect to the over-all stability of the price level. This daily index is now up about 10 per cent from mid-year and 20 per cent from the summer of last year. In this index, which is an unweighted average of 13 commodities, the 5 metals have risen an average of about a fourth since mid-year and nearly a half since the summer of last year.

The rise in the daily index since last summer nearly equals the rise that occurred in the two years after early 1954, and the current level is almost as high as in early 1956. In the 1954-56 period, the broader Federal Reserve index of sensitive industrial materials rose 15 per cent, compared with somewhat more than 20 per cent for the daily index. Since early last year, however, the Federal Reserve index has increased only 3 per cent as against a 20 per cent rise in the daily index, reflecting the selectivity of price increases in this period. While tin has soared and all other nonferrous metals have increased substantially, prices of lumber and plywood have been declining since spring, after only a modest rise from a year earlier. Hides and rubber recently have recovered moderately, but from very low levels. And in textile markets, although demands are very strong and prices have increased somewhat lately, average prices are no higher than in the spring and summer of last year, in large part because of the decrease in the cost of raw cotton through Federal payments to domestic users and a reduction in the Federal support level.

On November 3, when the United States tin market was closed for Election Day, tin prices on the London Metal Exchange dropped sharply, following some earlier decline from the high reached October 30. In the United States also, tin prices had reached a record high in late October--over $2.10 a pound compared with $1.16 in the summer of 1963--despite the recent announcement by GSA that it will increase the quantity of the metal available from the stockpile. During the past 7 months, GSA has sold about 14,000 tons from an original allocation of 20,000 for the year ending in March 1965. To the 6,000 tons remaining to be sold over the next 5 months, GSA has now added 18,000 tons. Thus, over the 12 months ending in March 1965, GSA will have sold or made available a total of 38,000 tons, which may be appraised against estimated domestic consumption in the first three quarters of 1964 at an annual rate of 75,600 tons. Of this amount, 53,300 was new tin and the remainder was from scrap.

The consumer price index increased .2 per cent in September to 108.4 per cent of the 1957-59 average and was 1.2 per cent above a year earlier. Rent was unchanged in September and was less than 1 per cent above a year earlier. Average prices of other services continued to rise at about a 2 per cent annual rate, while price changes for commodities for the most part were associated with seasonal developments. Thus, prices of apparel increased as wool items returned to the market at higher levels than last winter's end-of-season prices and new car prices declined as dealers offered larger concessions in the closing month of the 1964 model year. Among foods, seasonal forces were outweighed by the effect of the organized movement in late August and early September to withhold livestock from markets. Retail prices of meats rose nearly 3 per cent. Since early September wholesale prices of livestock and meats have declined appreciably.

Labor market. The latest household survey--to be released by the Department of Labor on Thursday, November 5--shows that the labor force, employment and unemployment all showed little change from September to October. These employment and unemployment figures are not affected by the General Motors' strike.

Beginning in May the over-all unemployment rate has fluctuated narrowly around a level of 5.1 per cent, following some decline from the 5.7 level prevailing in 1963 and 1962.

In September and October, the unemployment rate for married men, which had declined to a low of 2.6 per cent this summer, increased to about 3.0 per cent--the same rate as a year earlier. Unemployment rates for married men, while still relatively low in comparison with rates for either group, have been consistently higher than the average rate of 2.3 per cent in 1956. The increase of about one-fourth for this group is almost the same as the increase in the total unemployment rate. Among teenage youths unemployment continued at about 14 per cent in September and October, about two-fifths above the 1956 rate.

Labor force and total employment have been relatively stable since mid-year. While monthly changes may often be suspect, for sampling and other statistical reasons, the relatively long period with little change in employment lends support to other evidence suggestive of a possible slow-down in employment gains in industries other than the volatile metal manufacturing industries.

Industrial relations. Although General Motors reached a national agreement with the auto workers union more than a week ago, production and employment have been limited because 8 of the 130 local unions, including some at important assembly and body plants, have not settled local issues and remain on strike. The company has expressed hopes that settlements will be reached soon and that output--now at 75 per cent of normal--will be resumed in full next week.

Meanwhile, 20 of Ford's 90 units have not signed local contracts but continue to work. The union has set this Friday as a deadline, and those units that have not concluded agreements by then will be free to go on strike.

While both sides in the steel industry have stressed a desire for an early settlement, there is little evidence that steps have been taken to begin negotiations. Union demands remain rather vague. Earlier it was thought that the union would stress money wage increases this time because wage rates have not changed since 1961. More recently, however, there have been reports that union members seem more interested in an early retirement program similar to the one in the auto industry than in large increases in pay scales.

Retail sales. Although the strike at General Motors sharply limited production and sales of new model cars, weekly data through October 24 indicate only a slight decline in total retail sales for the month. Revised data for September show a decline of 0.4 per cent from the August peak rather than the original 1.1 per cent.

Furniture and appliance sales, following a decline in September, returned to the level prevailing since last spring. At nondurable goods outlets, sales may have exceeded their August high, with gains widespread among most types of business.

Auto sales. In September, before the effects of the General Motors' strike were evident, auto sales exceeded their level a year earlier by about one-fifth, taking into account the earlier model introductions this year. In the first 20 days of October, reflecting strike effects, sales were down about one-fifth from last year.

The combined sales by Ford and Chrysler in the first 20 days of October were 9 per cent above their level last year. The significance of this for interpreting the underlying strength of demand, however, is limited. Aside from the effects of the strike on households' current and expected incomes, some buyers may have shifted their intended purchases to non-General Motors' cars while others may have been holding off new car purchases until they could compare all makes.

The 1964 model year, which closed just prior to the strike, realized record sales of 8.1 million new autos--7.7 million domestically produced, .4 million imported. This was the third model year in a row of marked increases in sales.

Accompanying rising sales there has been an increase in estimated annual scrappage. The accompanying table shows total sales, estimated acrappage, sales less scrappage, registered car stocks at the beginning of the year, and the per cent increase during the model year in cars on the road.

SALES OF NEW CARS, SCRAPPAGE, AND CARS ON ROAD
(millions of autos)

Model year	Sales	Estimated scrappage	Sales less scrappage	Beginning of year cars on road	Per cent change in cars on road
1955	7.4	4.3	3.1	43.2	7.2
1960	6.3	4.3	2.0	53.0	3.8
1961	5.9	4.4	1.5	55.0	2.7
1962	6.7	4.7	2.0	56.4	3.5
1963	7.6	4.9	2.7	58.4	4.6
1964	8.1	5.1	3.0	61.1	4.9

Estimates through 1962 by R. L. Polk and Company for scrappages and--with adjustments to model year basis--for cars on road. Extrapolations through 1963 and 1964 by actuarial analysis of survivor curves for all postwar models.

These figures indicate that the number of autos on the road has been increasing over the expansion period since 1961 at a rising rate. The rate for the 1964 model year, however, was still well below the exceptional rate of 1955. In the recent expansion period the number of licensed drivers has grown at about 3.5 per cent a year, a higher rate than in the mid-1950's.

Continued strength in auto sales is forecast by the Sindlinger Survey sampling of six-month new car buying plans by telephone owning households. Since mid-year buying plans have jumped to unprecedented levels. Beginning in July, plans jumped from 8.0 to 8.5 per cent of responding households, where they were in the first half of the year, to 10 per cent in late September and early October. In early autumn of 1963 the proportion was a little less than 9 per cent, which was about the record up to that time.

Consumer credit. Demands for consumer credit were strong in September according to a preliminary tabulation of commercial bank data and scattered reports for other holder groups. At commercial banks, instalment debt outstanding increased by about $235 million, compared with a rise of just under $200 million in August.

The seasonally adjusted increase in instalment debt for all holder groups probably amounted to about $500 million, up from $435 million in August. Such a pace for September would result in a third quarter rate of rise about in line with the first half of the year: higher than the second quarter but still below the record first quarter.

Delinquencies at commercial banks continue to be less than 1-1/2 per cent of all consumer loans made. The rate rose a little in the third quarter, but was below the third quarter rate the year before.

COMMERCIAL BANK DELINQUENCY RATES
Seasonally Adjusted

		Average for all consumer loans (per cent)
1963	Q1	1.34
	Q2	1.34
	Q3	1.40
	Q4	1.44
1964	Q1	1.36
	Q2	1.33
	Q3	1.37

The trend in delinquencies reported by GMAC has more or less paralleled that shown by the commercial bank data, despite some tendency toward slow pay-off on used car contracts. At CIT, on the other hand, the delinquency rate has shown a slight but persistent increase throughout most of this year.

Orders for durable goods. As is usual in a period of expanding activity, new orders for durable goods have continued to exceed shipments and order backlogs for durable goods increased appreciably further, to a level at the end of September 12 per cent higher than at the end of 1963. The September increase in unfilled orders reflected mainly gains in the steel and machinery industries.

Beginning with April, new orders for durable goods have been fluctuating around an average monthly level of about $20 billion, 10 per cent above the corresponding period in 1963. In September, at $19.9 billion new orders were close to this average and up 3 per cent from August.

As usual, defense orders have accounted for an important part of recent fluctuations in new orders; thus they were up sharply in July, taking total new orders to a peak of $21.3 billion, and in August and September they were down sharply, to a level well below last spring.

New orders for primary metals have also fluctuated considerably over this period but around a rising trend; a large increase in September--presumably reflecting in part steel stocking by consumers fearful of a strike--brought them to a new high for the year which equaled the peak monthly level reached in the early 1963 steel inventory build-up.

New orders for machinery and equipment have been showing little change in recent months at a level moderately below the highs reached in May and June. These recent new order levels have been high enough, however, so that despite a fairly steady advance in shipments, unfilled orders have continued to increase--by 3.5 per cent from June to September as compared with 8 per cent in the second quarter and 2.3 per cent in the first quarter.

Business inventories. For business as a whole, inventory changes probably continued small in September and October, and total inventory holdings continued at a low level in comparison with sales.

The pace of inventory accumulation has been stepped up at manufacturers since midyear, owing in part to the beginning of a build-up of steel stocks, but there has been a decline in distributors' stocks, which in July and August about equaled the rise at manufacturers. A large part of the distributor stock reduction reported for July and August came from a decline in auto stocks as sales rose sharply; since then auto stocks have been reduced further as a result of the General Motors' strike. On October 20 dealer stocks of new cars totaled 690,000 as compared with 785,000 a year earlier.

The current reduced level of dealer auto stocks is clearly involuntary. How far relatively low current levels of stocks in the hands of other distributors reflect sales greater than anticipated and how far they reflect other influences--cautious inventory policies and inventory economies--is uncertain.

Manufacturers' inventories. Manufacturers' inventory investment in September continued at about the stepped-up pace of July and August, and the book value increase for the entire third quarter totaled $550 million. This was moderately above manufacturers' anticipations reported in the Commerce Department August survey and about equal to the average quarterly rate for the year 1963.

The marked step-up in manufacturers' total inventory accumulation from only $70 million in the second quarter to $550 million in the third reflected mainly a shift from moderate decline to small rise in book value in the nondurable goods sector. Except for foods, which showed another appreciable decline, most nondurable industries were showing moderate inventory gains in the third quarter following little change or small declines in the second. Perhaps in part explaining these quarter-to-quarter differences in inventory behavior, actual nondurable goods shipments in the third quarter turned out about as anticipated (shipments were up 1 per cent from the second quarter) while second quarter shipments--up 3 per cent from the first--were well in excess of anticipation.

Durable goods inventories in September continued the steady--though relatively moderate--gain that began last April after a few months of little change at the beginning of the year. The book value increase totaled $465 million in the third quarter and $415 million in the second. (The average quarterly gain in 1963 was $425 million.) Third quarter inventory investment was moderately above anticipations, partly because third quarter shipments were moderately below those expected. While inventories have increased in most durable industries over recent months, the most pronounced gain in September--and the third quarter--was in the machinery industries. Part of the recent inventory increase reported for the machinery industry and other durable industries as well has reflected some pick-up in stocks of steel and other materials which had shown little change through the first half of the year despite expanding production.

Construction activity. Construction expenditures edged down in October to a seasonally adjusted rate of $65.5 billion. This was slightly above the advanced rate a year ago and within 2 per cent of the high reached earlier this year. Industrial and commercial building continued to rise in October, but residential activity dropped further and public construction also declined.

Residential building continues to be the one major area where demand is clearly down from earlier highs of this expansion period. Seasonally adjusted private housing starts did turn up in September, but the rise was moderate and followed two months of decline. As a result, the average annual rate in the third quarter--1.47 million, including farm--was down 6 per cent from the reduced second quarter rate and 12 per cent from the high in the first quarter. In the first nine months as a whole, starts were at an annual rate of 1.57 million, just below the average for all of 1963, and a fifth above averages for the (housing) recession year of 1960.

In contrast to starts, seasonally adjusted building permits in permit-issuing areas declined in September but like starts they were appreciably below a year earlier when both permits and starts were near their recent peaks. Permits for multifamily units, which had changed little in recent months, accounted for most of the decline in September.

PRIVATE HOUSING STARTS AND PERMITS

	September (thousands of units) 1/	Per cent change from: Month ago	Per cent change from: Year ago
Starts (total)	1,484	+4	-15
Permits (total)	1,231	-4	-11
1 - family	693	-1	-10
2-4 - family	93	-2	-17
5 or more	445	-8	-7

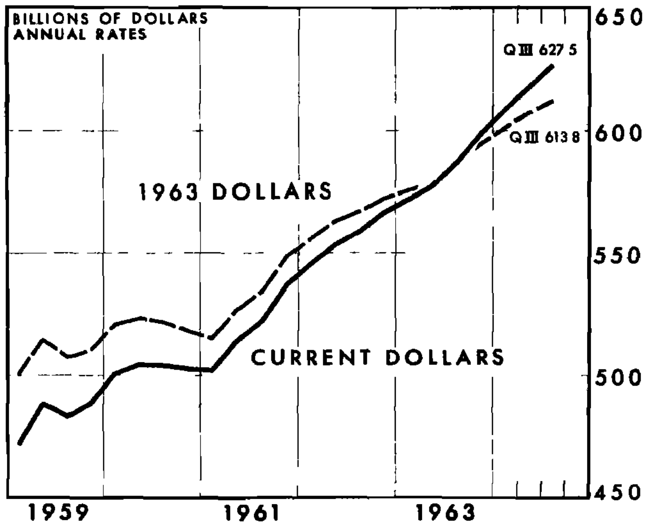
1/ Seasonally adjusted annual rate; preliminary.

Rental vacancy rates rose somewhat in the third quarter to an average of 7.7 per cent of units available and fit for use. As in the second quarter, however, the average was little changed from a year earlier and still moderately under the postwar peak (8.1 per cent) in the first half of 1961. Within metropolitan areas, rates moved higher from the second to the third quarter, but this appeared to be partly seasonal, and outside such areas, the average--which had tended downward for more than two years--changed very little. All regions except the South showed some rise; the increase in the North Central States, however, was from a particularly low level.

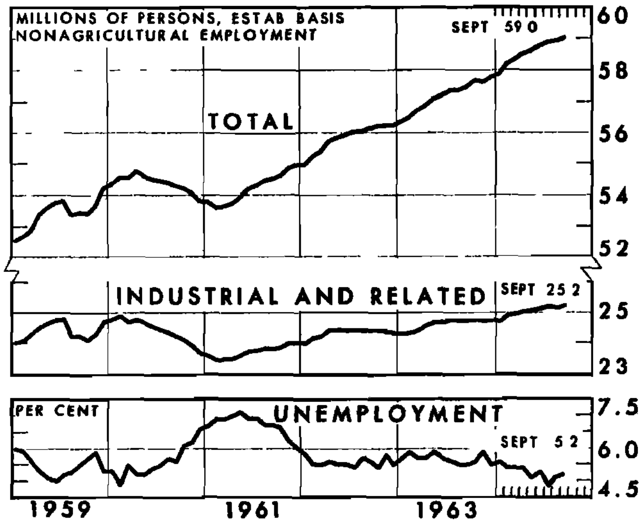
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

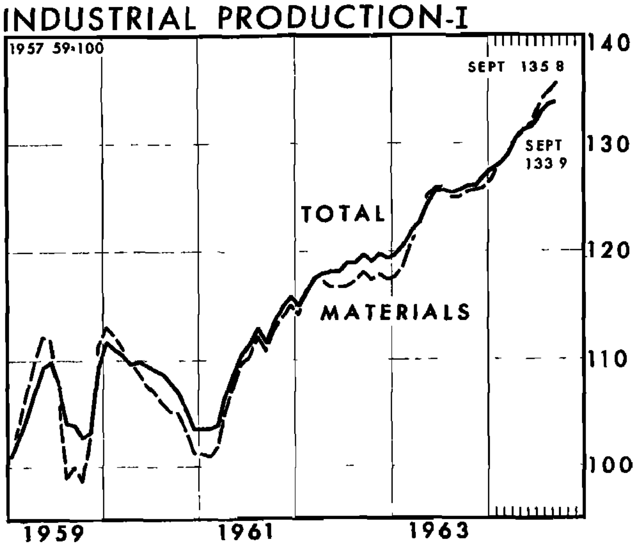
GROSS NATIONAL PRODUCT



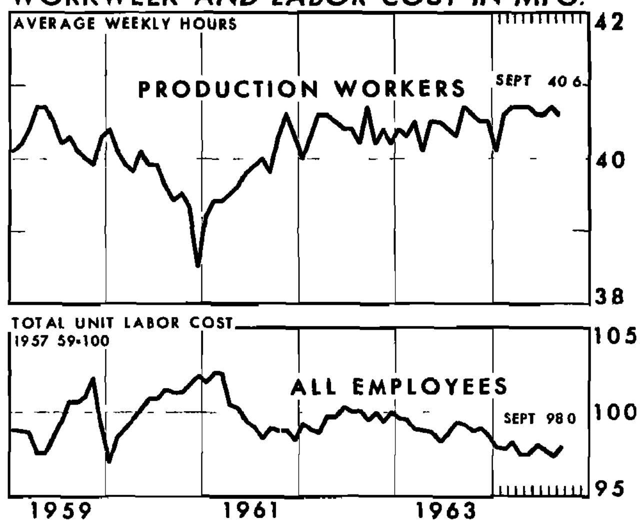
EMPLOYMENT AND UNEMPLOYMENT



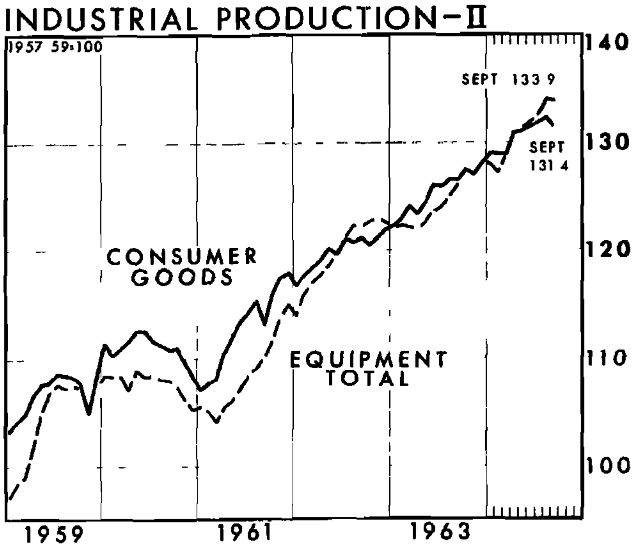
INDUSTRIAL PRODUCTION-I



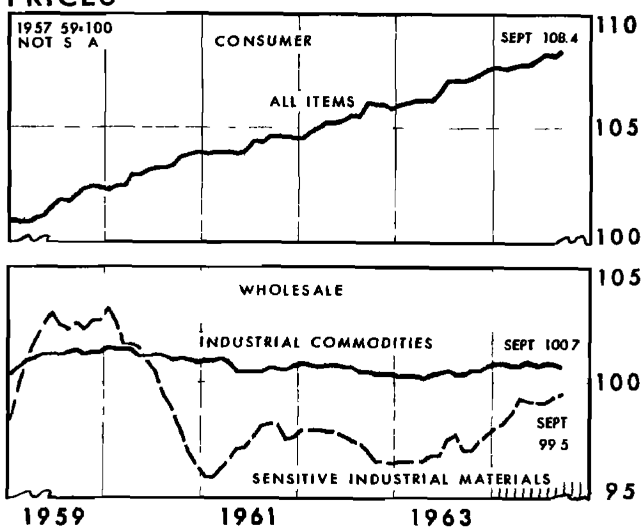
WORKWEEK AND LABOR COST IN MFG.



INDUSTRIAL PRODUCTION-II



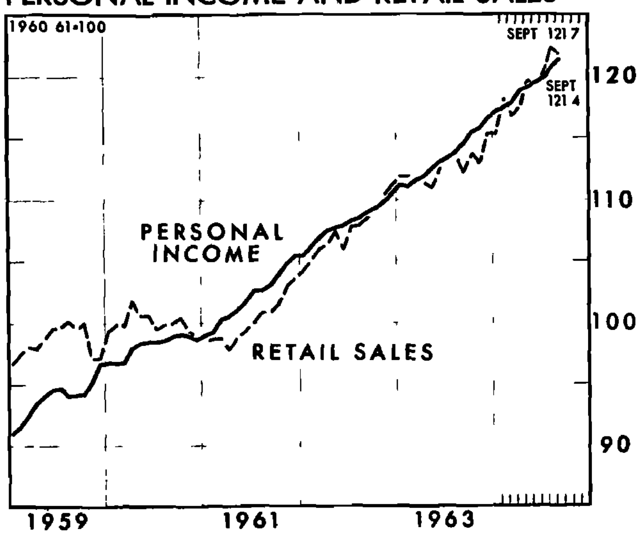
PRICES



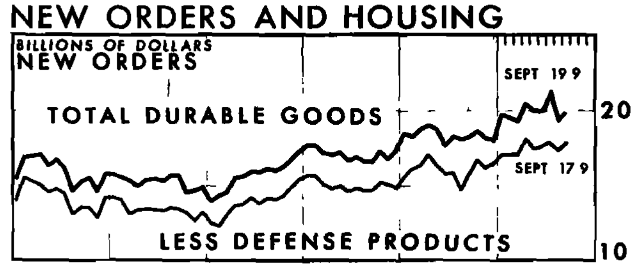
ECONOMIC DEVELOPMENTS - UNITED STATES

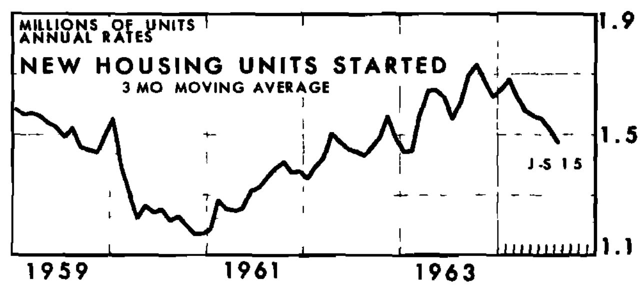
SEASONALLY ADJUSTED

PERSONAL INCOME AND RETAIL SALES

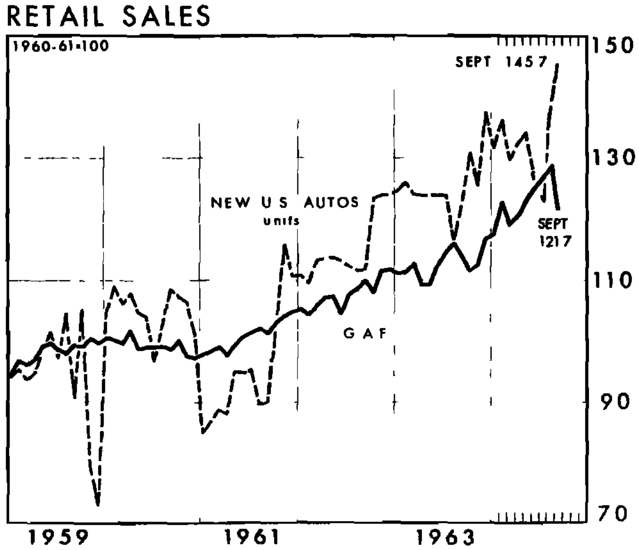


NEW ORDERS AND HOUSING

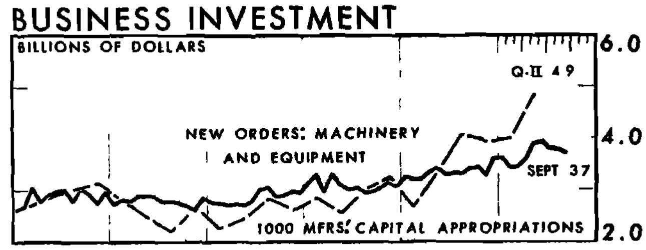


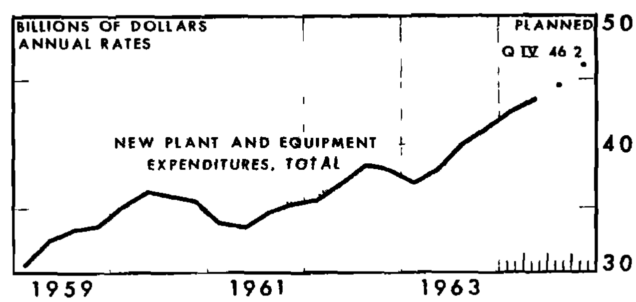


RETAIL SALES

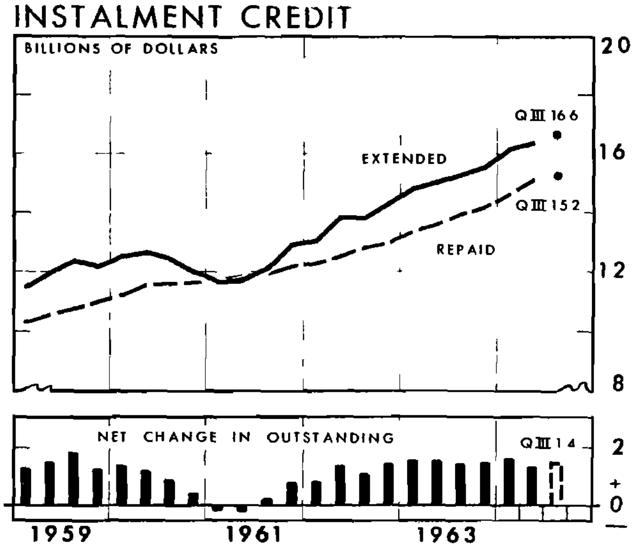


BUSINESS INVESTMENT

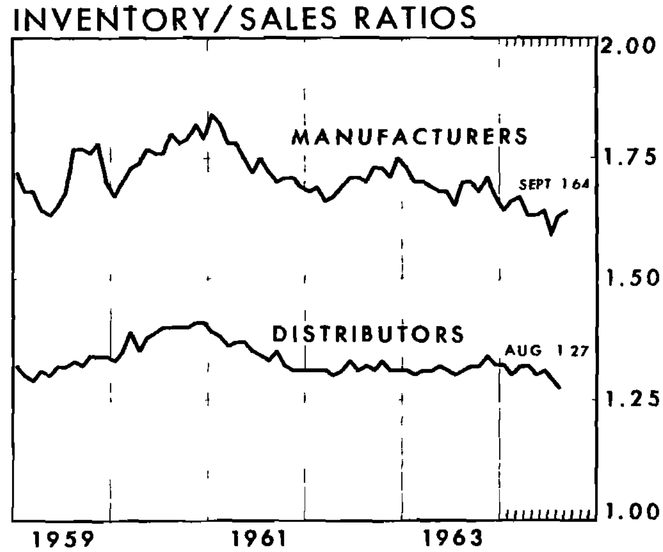




INSTALMENT CREDIT



INVENTORY/SALES RATIOS



DOMESTIC FINANCIAL SITUATION

U. S. Government finance. The market for Treasury notes and bonds strengthened during the last two weeks of October, and at month's end average yields on long-term U. S. bonds were at their lowest levels since early August. There were indications of some improvement in investment demand for Treasury coupon issues, notably for the longest maturities, and dealer positions in longer bonds declined about $15 million to a level of $112 million between October 16 and October 30. However, the market rally also reflected an expansion in the dealers own buying of short- and intermediate-term issues, and their net holdings of notes and bonds due in less than 10 years rose by $236 million in the last half of October to a level of $664 million. In this period market participants apparently came to feel that a change in System policy was not imminent, particularly in view of the decision by the new U. K. Labor Government to alleviate Britain's balance of payments problem through measures other than an increase in interest rates and in view of continued evidences of the moderate nature of developments in the domestic economy.

YIELDS ON U. S. GOVERNMENT SECURITIES
(Constant maturity series)

Date (closing bids)	3-month bills	6-month bills	3 years	5 years	10 years	20 years
1962						
December 31	2.92	2.96	3.40	3.56	3.85	3.92
1963						
December 31	3.51	3.64	4.05	4.06	4.14	4.19
1964						
June 30	3.47	3.52	3.95	4.01	4.15	4.15
September 30	3.55	3.72	4.01	4.05	4.18	4.19
October 19	3.59	3.73	4.04	4.09	4.21	4.22
October 30	3.55	3.71	4.02	4.06	4.17	4.16

Treasury bill rates also edged lower in the latter part of October. Market demand for bills was strong throughout most of October, but tended to taper off late in the month. This late slackness was made up by System purchases of nearly $540 million from dealers. In addition, the new supply of bills from the October 20 auction of $1.5 billion March tax bills was largely absorbed by the commercial banks because of the 50 per cent tax and loan credit allowed by the Treasury. And in the last part of October dealers were able to finance their holdings of bills and other securities at more attractive rates than earlier in the month.

The Treasury announced a cash financing on October 28 involving about $9-1/4 billion of new 4 per cent notes due in 18 months. This cash offering will refund about $8.7 billion of securities maturing November 15 ($2.3 billion publicly held). As a result of the financing, the Treasury cash position is likely to rise by almost $1 billion after taking into account the saving on attrition and possible over-allotments of the issue. The market reacted favorably to the 4 per cent rate, and sizable interest on the part of banks has been reported. The Treasury is expected to raise additional cash later in November through an offering of perhaps $1.5 billion in June tax bills. With these new funds, and with continued strong tax receipts, the Treasury may have the flexibility to go through the balance of this year without further cash borrowing, but the January cash drain will require additional funds.

Projections of cash receipts for all fiscal 1965 contained in the Administration's recent budget review were substantially unchanged from earlier estimates, after allowance for delay in enactment of the tax cut. But the new projections lower expenditures by about $500 million and leave the cash deficit for fiscal 1965, at $3.5 billion, some $1.2 billion below the fiscal 1964 deficit.

BUDGET OUTLOOK
(Fiscal years. In billions)

Description	1964 actual	1965	
		January estimate 1/	Current estimate
Administrative budget:			
Receipts	$ 89.4	$ 92.1	$ 91.5
Expenditures	97.7	97.9	97.2
Budget deficit	8.3	5.8	5.7
Consolidated cash budget:			
Receipts	115.4	118.8	118.8
Payments	120.1	122.7	122.2
Budget deficit	4.7	3.9	3.5

1/ Adjusted to allow for delay in tax cut.

Within fiscal 1965, the staff still anticipates a larger than usual swing from a deficit of almost $11 billion in July-December to a surplus of about $7.5 billion in January-June. About two-thirds of the swing is estimated as seasonal, so that the nonseasonal shift from deficit to surplus would be around $5 billion this year, compared with $1.2 billion last fiscal year. Thus, the new figures, while they contain no great surprises, would if anything make it less likely that Federal financing requirements will be exerting upward pressure on interest rates over the next few quarters.

Corporate and municipal bond markets. Like the market for U. S. Treasury securities, markets for corporate and municipal bonds have developed a stronger tone recently, as investors have begun to view the chance of a near-term rise in interest rates as less probable. Although yields on high-quality seasoned issues in both markets have remained stable, those on recently offered (unseasoned) issues have turned down in secondary market trading. Yields on seasoned municipal bonds of mixed quality have also declined several basis points. No current reading of the series on new corporate bonds is available due to an absence of offerings.

BOND YIELDS

	Corporate Aaa		State and local govt.	
	New	Seasoned	Moody's Aaa	Bond Buyer (mixed qualities)
1964 - High	4.54(5/8)	4.43(10/30)	3.16(3/26)	3.32(4/21)
Low	4.30(2/21)	4.35(2/28)	3.07(7/16)	3.13(1/20)
Summer low	4.37	4.40	3.07	3.16
September high	4.52	4.42	3.10	3.26
October low	4.44	4.42	3.11	3.26
Latest available week 1/	4.46	4.43	3.11	3.23

1/ Latest week in which relevant issue of new corporate bonds were offered was October 23; yields in other series are for the week ending October 30.

In the corporate bond market, the immediate technical position of underwriters' changed quickly in the week following the British election. At the time of the election five new issues were still in syndicate, with unsold balances aggregating about $100 million. After the Labor victory, four of these issues were released from syndicate, apparently as a precautionary step against the possibility of a rise in U.K. and U.S. interest rates stemming from expected action by the new British government to defend the pound. Initially, yields on these issues rose 2 to 7 basis points in secondary trading, but when the specifics of the British program became evident, the bulk of the yield advance was erased. The extremely light volume of corporate bonds scheduled for public offering in November and December was undoubtedly a factor also in this decline.

In the municipal market, new issue volume is expected to decline over the remainder of the year, although the drop should be no more than seasonal. Investor demand for current offerings of municipal bonds has been good, and interest in older issues has picked up. In consequence, dealers' advertised inventories have declined over $100 million to about $575 million, the lowest level since late July.

BOND OFFERINGS 1/
(Millions of dollars)

	Corporate				State & local govt.	
	Public offerings		Private placements			
	1964	1963	1964	1963	1964	1963
Jan.-July avg.	362	396	471	508	940	969
August	183	336	500	319	750e/	764
September	375e/	283	579e/	501	900e/	480
October	175e/	511	550e/	481	900e/	1,265
November	60e/	183	600e/	549	700e/	754

1/ Includes refundings--data are gross proceeds for corporate offerings and principal amounts for State and local government issues.

Stock prices. Common stock prices have fluctuated recently at levels slightly under the record highs reached in mid-October. Standard and Poor's composite index of 500 stocks closed November 2 at 85.18, only nominally below the peak. The generally favorable reports of third quarter corporate earnings now becoming available appear to have been largely discounted in the previous price rise.

Savings and loan associations. Preliminary data for September indicate an expansion in savings capital at savings and loan associations of more than $1 billion, almost one-sixth larger than in September a year ago. This recent experience continues the general pick-up in net savings flows that has been evident at all of the major depositary-type institutions in recent months.

During the May-September period this year, savings capital at savings and loan associations expanded $4.6 billion, $430 million more than in the like period of 1963. This year-over-year expansion offset about half of the short-fall that developed in the January-April period, when net inflows of savings to savings and loan associations were $861 million below the record growth of early 1963. Allowing roughly for seasonal influences, the September and third quarter net inflows seem to have regained the record proportions of early 1963.

NET CHANGE IN SAVINGS SHARE CAPITAL AT SAVINGS
AND LOAN ASSOCIATIONS
(Seasonally adjusted) 1/
(Monthly averages in millions of dollars)

Quarter	1964	1963	1962
I	777	1,030	680
II	888	912	741
III	1,030	854	808
IV		865	873

1/ Seasonally adjusted share figures should be treated as rough approximations, partly because major changes in dividend payment practices in recent years have influenced the pattern of monthly flows.

<u>Mortgage market developments</u>. While competition for mortgages has remained quite intense this autumn, the FHA-yield series, at 5.46 per cent in September, was virtually unchanged for the eighteenth consecutive month. Contract interest rates for conventional first mortgages also continued at earlier reduced levels--5.80 per cent for loans on new homes and 5.85 per cent for loans on existing houses, according to the Federal Housing Administration.

Reliance by private lenders on the secondary market facilities of the Federal National Mortgage Association has continued at low ebb this year, in sharp contrast with developments in the spring of 1963 when, in response to private demands, sales by FNMA reached a monthly rate of more than $165 million. The low level of activity since then has reflected, in part, the ability of private investors to meet portfolio requirements directly from the private market and, in part, the higher prices to purchasers which FNMA established early in 1963. A public offering of $300 million FNMA participation certificates--backed by a pool of mortgages held by FNMA and the Veterans' Administration--was successfully marketed by underwriters in October under authority of the recently passed Housing Act of 1964. However, these certificates are designed to attract funds not usually directly involved in FNMA's regular secondary market operations.

Bank credit. Loans and investments at city banks declined over $2 billion in the three weeks ending October 21, somewhat more than in the corresponding weeks last year, and much more than in 1962. A substantial rise is expected for the week of October 28, however, reflecting initial allotments to banks of nearly all the $1.5 billion of March tax bills, for which 50 per cent of the payment was permitted through credit to tax and loan accounts.

For the month as a whole, seasonally adjusted total credit at all commercial banks may show a small decline. This includes an estimated large rise at nonweekly reporting banks, data on which are available for only the first half of the month. A reduction in holdings of U. S. Government securities, following large increases in the previous two months, may more than offset moderate increases in loans and holdings of municipal and agency issues. From midyear through October, total commercial bank credit is estimated to have increased at an annual rate of about 6 per cent compared with 8 per cent over the first half of the year.

NET CHANGE IN CITY BANK CREDIT
FIRST THREE REPORTING WEEKS OF OCTOBER
(In millions of dollars)

	1964	1963	1962	1961
Total loans & investments	-2,144	-1,801	-697	674
Loans	-1,057	-1,178	-285	477
U. S. Govt. securities	-1,098	-573	-551	194
Other securities	11	- 50	139	3
Type of loan:				
Business	- 40	165	- 72	215
Real estate	147	162	215	85
Security	-727	-1,008	- 94	276
Nonbank financial	-494	-593	-262	-133

About half the city bank credit decline over the first three weeks of October was in holdings of U. S. Government securities. Banks made large reductions in holdings of bills following heavy acquisitions in September, and they continued to reduce their holdings of notes and bonds maturing in over 5 years. Purchases of municipal and agency issues, which had picked up in August and September, moderated in October.

Business loans at city banks declined somewhat over the first three weeks of October compared with increases in the corresponding period of most other recent years. This followed record expansion at these banks in September, however. At all commercial banks, based on recently revised seasonal factors, business loans increased $600 million in September, somewhat more than the substantial increases of the late spring and summer months. In October, however, growth probably was considerably smaller.

Since the September tax period, continuing strong loan demand has been confined mainly to the petroleum and checmicals group. In addition, loans to metals companies have not shown the usual post-tax period decline, presumably reflecting in part accumulation of steel inventory. But in several other major categories, particularly public utilities, trade, and miscellaneous manufacturing, where loans earlier had been expanding, loan demand appears to have moderated recently, after allowance is made for usual seasonal movements. In public utilities, a substantial volume of bank debt has been refinanced in the capital markets and in trade, some liquidation of auto-floor plan loans probably resulted from the General Motors' strike. Outstanding loans to the textiles-apparel group have been declining more than seasonally, possibly reflecting to some extent improved cash flow from the 6-1/2 cents per pound reduction in the cost of raw cotton which was authorized earlier this year.

In October, real estate and consumer loans appear to have increased at about the same relatively rapid rate as in other recent months. Security loans, both to U. S. Government security dealers and to others, declined substantially.

Money supply and time deposits. The seasonally adjusted money supply increased $500 million further in October (preliminary) with substantial growth early in the month offset in part by a subsequent decline. Since May, when money growth began to accelerate, the money supply has increased at an annual rate of 6.2 per cent compared with 2.0 per cent earlier in the year. During the last 3 months, however, the rise has fallen to 4.6 per cent, and for the year to date it has been 4.2 per cent. U. S. Government deposits at commercial banks showed a sizable seasonally adjusted decline in October.

Seasonally adjusted time and savings deposits at all commercial banks increased $1.3 billion in October (preliminary) or at a little faster pace than in other recent months. The annual rate of expansion in these deposits since June--11.4 per cent--has been slightly higher than that in the first six months of the year, 11 per cent.

The rate of growth in savings deposits at banks in leading cities has accelerated in the last couple of months relative to last year's expansion. Since July, growth in these deposits has been somewhat larger than that in the corresponding weeks of 1963 whereas in earlier months of 1964, it had been only three-fifths as much. Time deposits, which had declined somewhat in both September 1964 and 1963, associated principally with maturing CD's over the tax period, increased substantially in early October of both years. By October 21, CD's at banks in New York and Chicago were above their pre-tax period levels but at other city banks they were still somewhat below.

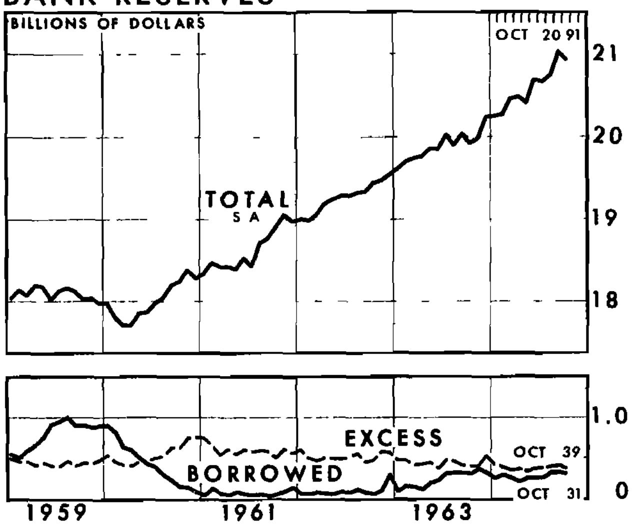
Bank reserves. Free reserves at all member banks averaged $84 million in October, about the same as in September, but below the $120 million level prevailing earlier in the year.[1/] Excess reserves at $389 million were below the September average but about the same as in previous months, while member bank borrowings at $305 million were higher than the average of other recent months. During October (through the 28th) the effective rate on Federal funds fell below 3-1/2 per cent on five days, with some transactions at lower rates on 10 days and some at higher rates on 7 days.

Seasonally adjusted required reserves against private demand deposits increased moderately further during October as a sharp rise early in the month was offset only in part by a subsequent decline. Required reserves against U. S. Government deposits declined considerably more than usual.

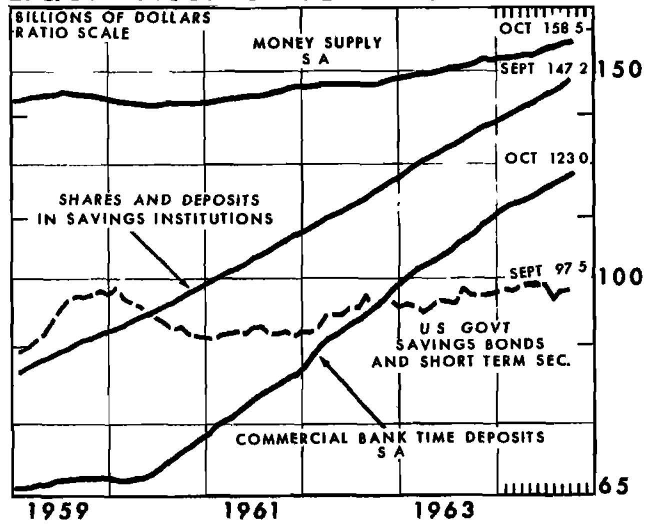
1/ Based on the average of daily figures for all of the reserve weeks ending in the month as used in the reserve memorandum to the FOMC, rather than an average of all days in the calendar month.

FINANCIAL DEVELOPMENTS - UNITED STATES

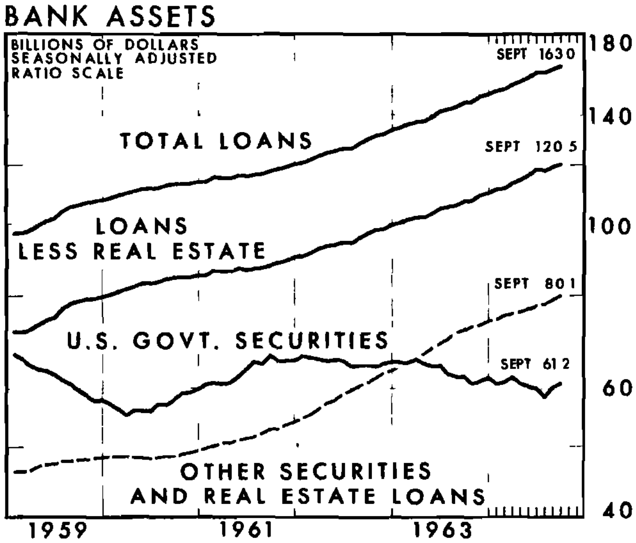
BANK RESERVES



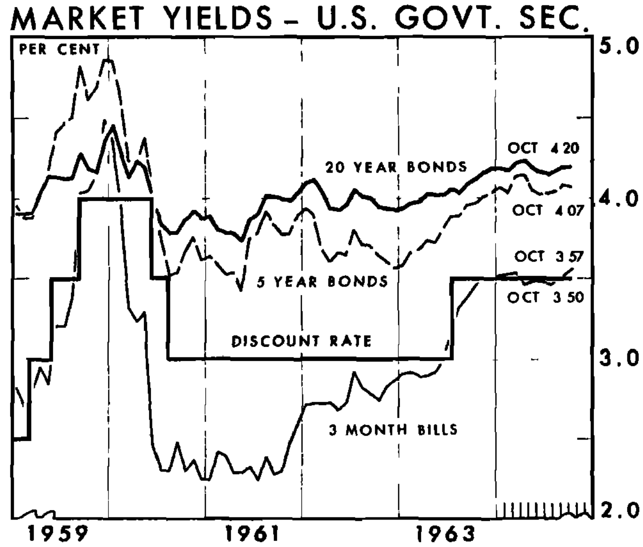
LIQUID ASSETS HELD BY PUBLIC



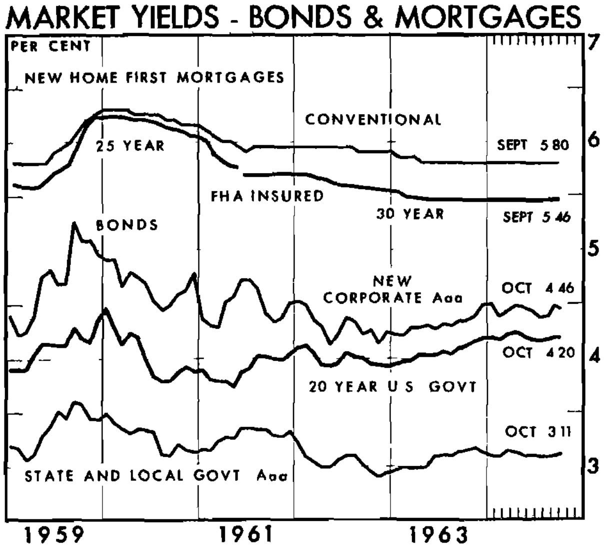
BANK ASSETS



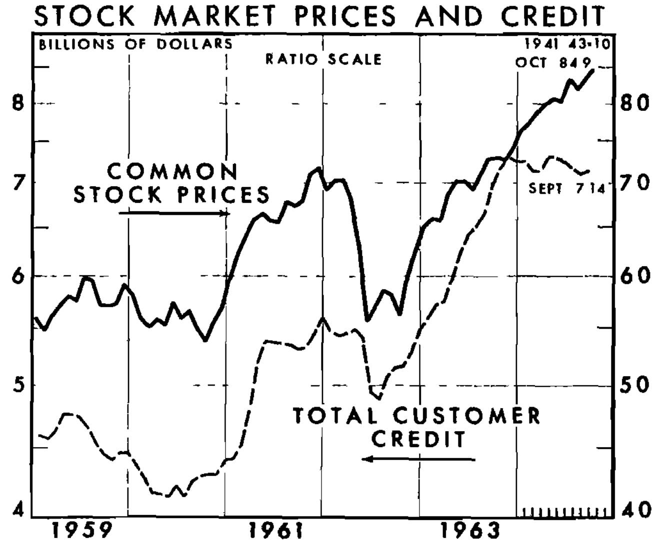
MARKET YIELDS – U.S. GOVT. SEC.



MARKET YIELDS - BONDS & MORTGAGES



STOCK MARKET PRICES AND CREDIT



INTERNATIONAL DEVELOPMENTS

U.S. Balance of Payments. The tentative data presently available show an over-all payments deficit for October of about $600 million. This figure, if confirmed by later data, is about as large as the deficit figure for October 1963. As then, one element in the increased deficit for the month as compared with September, appears to have been outflows of short-term capital into U.S. dollar deposits with Canadian banks seeking to build up published balance sheet totals.

The other major element in the larger deficit in October this year is that the outflow of long-term capital on new foreign bond issues has picked up in the fourth quarter, after having been small in the third. For the period July through November, this outflow now appears likely to exceed $500 million, compared with about $400 million in the first half of the year. Most of the borrowing since midyear has been for Canadian account, but one-fifth of the outflow reflects an issue by the Inter-American Development Bank. The IDB will place most of the proceeds in long-term bank deposits; such deposit holdings are regarded as long-term capital inflows in the U.S. balance of payments accounts, and the IDB issue will thus add little to the over-all payments deficit for the time being.

Long-term bank loans to foreigners rose substantially in September, bringing the third quarter outflow to almost $250 million, as compared to an exceptionally low $80 million in the second quarter. For the second and third quarters together, the outflow of these loans this year was up 10 per cent from 1963. There was a small net inflow of U.S. short-term capital reported by banks in September.

U.S. exports in September increased by more than $2 billion at a seasonally adjusted annual rate. However, much of this sharp increase was probably due to an acceleration of export shipments in anticipation of a port strike in October. There were reports in the last week of September indicating unusually high levels of port activity. In 1962, when a similar development occurred, it appeared in retrospect that about 10 per cent of total shipments were shifted from October to September. If the same proportion of total exports were affected this year, the adjusted rate of exports in September would not be greatly different from that of preceding months -- that is, around 24-1/2 billion at an annual rate.

Imports in September were slightly lower than in August, but remained above the advanced second quarter levels. Anticipations of a port strike presumably did not affect September imports, as in 1962.

Shifts in the timing of physical movement of exports and imports as a result of the threatened port strike are unlikely to have had any appreciable effect on the flows of payments associated with the movement of these goods. Statistics on the over-all payments balance in September and October would not have been significantly affected.

The new British surcharges on imports can be expected to have a noticeable effect on U.S. exports. Since early this year, U.S. exports to the United Kingdom have averaged $1.5 billion at a seasonally adjusted annual rate. Almost half of the total -- about $700 million annually -- will be subject to the surcharge; these exports -- mainly capital equipment and other manufactures -- have increased by about 50 per cent in the last four years, as shown in the accompanying chart, in contrast to the declines in foodstuffs, tobacco, and other raw materials.

Business and financial developments abroad. The new Labor Government's short-run proposals for dealing with Britain's payments problems have, at least temporarily, lessened the pressure on the pound. Before the announcement of the British measures, uncertainty about intermediate-run business prospects was increasing in France; whereas in Germany, growth of domestic demand and capacity was continuing.

In Britain, the new Labor Government announced on October 26 its program for dealing with the continuing large deficits in the British balance of payments. Just prior to the announcement, and after a widely anticipated increase in the Bank Rate failed to materialize, the pound came under heavy selling pressure in London. Following the announcement of the Government program, speculation against sterling came to a halt, and sterling has risen over the past week. On November 4, the spot pound was quoted at $2.7847, up 22 points from its low of $2.7825 on October 23.

The Government's short-run measures for lessening the trade deficit included (1) a 15 per cent surcharge on all imports except food, unmanufactured tobacco and raw materials, and (2) partial rebates of indirect taxes paid by exporters, averaging about 1-1/2 per cent of the value of the exports. The import surcharge would affect imports which in 1963 were valued at about $4 billion out of total imports of $13-1/2 billion. Most heavily affected by the import surtax will be exporters of manufactures in Europe and North America; only a small proportion of exports to the U.K. from Commonwealth and other nonindustrial countries are involved.

The immediate impact of the import surcharge may be quite large inasmuch as considerable uncertainty exists as to the duration of its application. Pressure from other European governments for the early removal of the surcharge has already begun to mount, but no retaliatory measures appear so far to be in prospect. A crude estimate would be that declines in imports as a result of the surcharge would not reduce the annual rate of the payments deficit -- currently £700-800 million -- by more than 25-35 per cent at the maximum.

Most recent figures on the British economy indicate continued sluggishness of output gains and poor export performance. The index of industrial production for August, seasonally adjusted, was again unchanged at 127 per cent of the 1958 average. New orders in engineering industries in July and August declined from record second quarter levels and were about the same as in the second half of 1963. The labor market remains tight, with unemployment continuing through October to fluctuate around 1-1/2 per cent of the labor force.

The third quarter seasonally adjusted trade deficit on a balance of payments basis was £150 million, compared with a deficit for the second quarter of £113 million. Imports increased further, while there was virtually no change in exports.

There are increasing signs of a slowing or cessation of the expansion of French economic activity. Slowdowns in production in the auto and allied industries have continued. Although analysts believe that industrial output will at least be maintained at present levels through the end of this year, increasing concern has been reported about the possibility of a downturn in 1965. Increases in new orders have apparently continued to slacken and the squeeze on profits is continuing.

The seasonally adjusted index of industrial production for July-August combined was down about 6 per cent from June, reportedly because the seasonal adjustment does not yet take into account the longer paid vacations granted by more and more industries over the last two years. Output in September is thought to have returned to the June level, but in that month it was no higher than in early spring.

Seasonally adjusted trade data for Germany show both imports and exports in September returning to about their July levels. For the third quarter as a whole, the trade surplus fell to $188 million from $525 million in the second quarter, mainly because of a higher level of imports.

In Canada, the index of industrial production rose nearly 2 per cent in August, returning to the record level reached last April. Although total retail sales in August, seasonally adjusted, were unchanged from the July level, new automobile sales rose about 3 per cent. Seasonally adjusted unemployment continue to decline through mid-September, and at 4.5 per cent of the labor force was 0.7 percentage points below the mid-June rate.

While construction activity continued to fall in August, new construction may be expected to pick up soon: new building permits rose 15 per cent from May to August, and the winter building bonus of $500 per house again came into effect on November 4, providing added building incentives for the next several months.

There has been a good deal of demand for the Canadian dollar in the foreign exchange market, primarily as the result of the conversion of the proceeds of Canadian security issues in the New York market. Official reserves have increased over the last month as a result of intervention by the Bank of Canada to moderate the rise in the Canadian exchange rate.

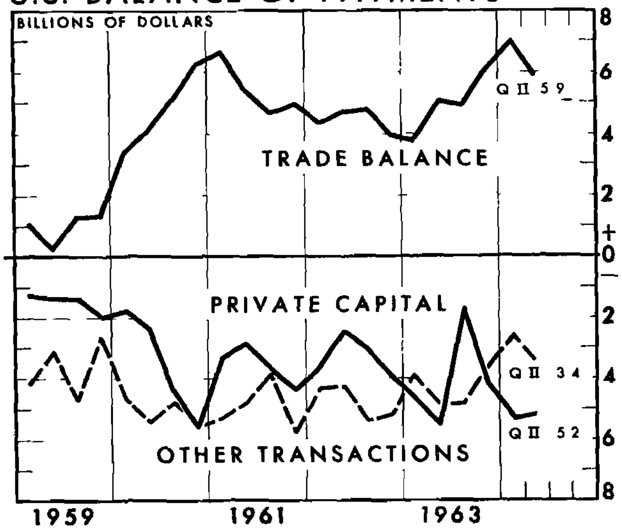
The seasonally adjusted Japanese trade deficit widened to $94 million in September as compared to an average monthly deficit of $50 million in July-August. Imports rose by 8 per cent while exports remained at approximately the same level as in the previous three months.

Wholesale prices continued to move upward for the third consecutive month in September, rising 0.4 per cent. Previously, the index had fallen 1.4 per cent, from a peak in November of 1963 to a low in June of this year.

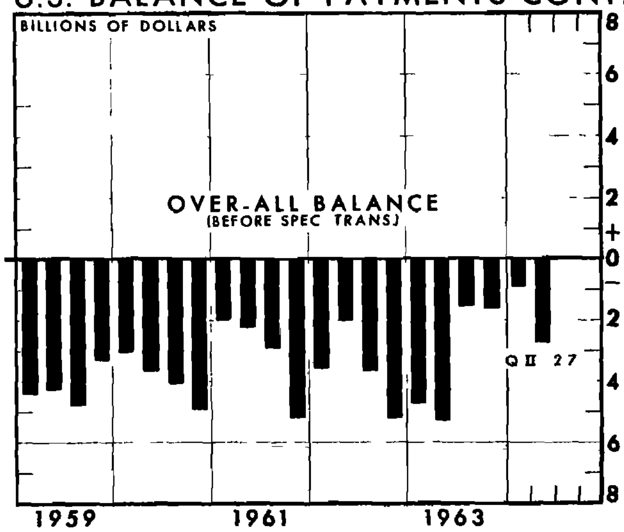
U.S. AND INTERNATIONAL - ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED, ANNUAL RATES

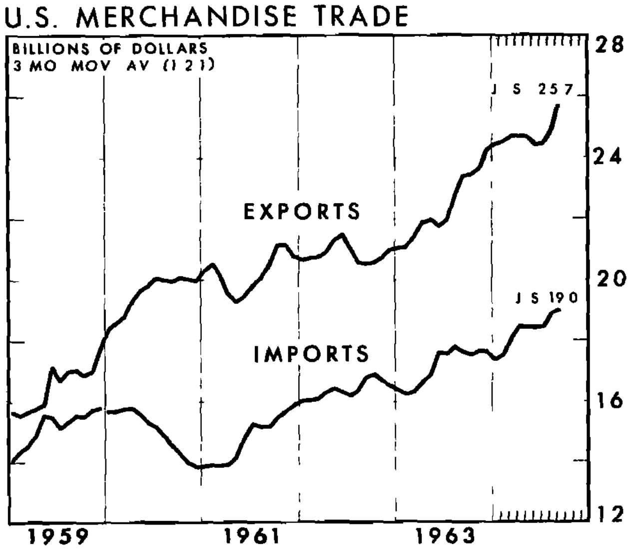
U.S. BALANCE OF PAYMENTS



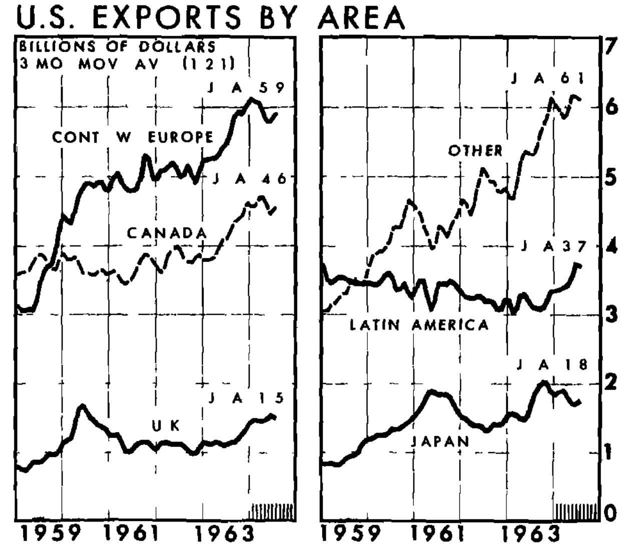
U.S. BALANCE OF PAYMENTS-CONT.



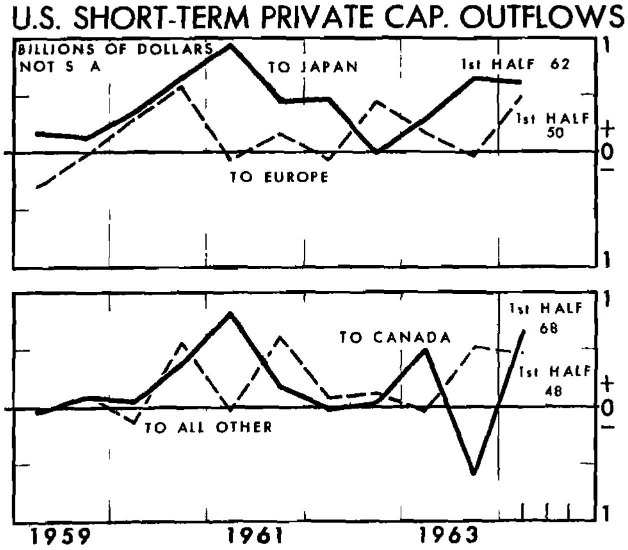
U.S. MERCHANDISE TRADE



U.S. EXPORTS BY AREA



U.S. SHORT-TERM PRIVATE CAP. OUTFLOWS



U.S. EXPORTS TO U.K.