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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

March 17, 1965

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IN BROAD REVIEW

The domestic economy has now entered the fifth year of sustained expansion and there is as yet little indication that the expansion is coming to an end. Despite continuing concern about labor negotiations and inventory imbalance in steel and related industries, economic activity has continued to rise and commodity prices have remained stable.

While activity has been spurred by demands for steel and autos, both at unsustainably high levels, gains have not been limited to these industries. The industrial production index rose from 137.5 in December to 138.8 in February without any further increase in combined output of autos and steel from the advanced December level. Although the rate of unemployment rose slightly in February, signs of strength in the labor market predominated, including a substantial increase in the number employed on nonfarm jobs.

Commodity prices have shown little response to the sustained expansion in demands. The broad industrial average has been stable this year at a level only 1.2 per cent higher than two years ago. The rise has been confined mainly to metals and machinery where demands have been exceptionally strong. An index of all other industrial prices now is no higher than two years ago and below the high level reached in the spring of 1959. At retail, prices of goods continued generally stable in January while prices of services rose further.

New information of notable importance since the last meeting of the Committee is the announcement of the results of two official surveys conducted in February. A Commerce-SEC survey reported business plans to spend 12 per cent more on plant and equipment this year than last. A year ago a rise of 10 per cent had been signaled for 1964, but, aided, in part, by the large tax cut stimulus, the actual rise was 14.5 per cent.

The second survey, on manufacturers' inventory and sales expectations, indicated a sharp decline in the rate of inventory accumulation in the first and second quarters from the very high rate in late 1964. A sizable increase was indicated for sales in the first quarter and a small decline in the second quarter.

In financial markets, yields on Treasury bills have inched downward recently despite the tauter reserve position of banks and the continuing firmness of general money market conditions. For the last four weeks, banks have shown net borrowed reserves averaging $25 million. In bond markets, there has also been a recent improvement in tone, with Treasury yields declining slightly and yields on corporate and municipal issues stabilizing following substantial increases in February and early March. In general, bond yields currently are at about the highs reached late last fall. Stock prices have continued to fluctuate in a narrow range below earlier highs. Trading has been quite active.

Seasonally adjusted bank credit expanded sharply again in February, with business loan demand continuing to show exceptional strength. Only a part of the rise can be attributed to special factors such as the surge in foreign lending and increased borrowing associated with the dock strike and steel inventory accumulation. In New York City, term lending has risen sharply so far this year, compared with a decline in early 1964.

Time and savings deposits at commercial banks rose by a near-record amount in February, but the money supply declined to the level of last November. In early March, the money supply apparently was rising again and time and savings deposits expansion was tapering off.

The initial reactions to the President's balance of payments program have been favorable. Data on the payments position show a surplus for the last three weeks in contrast to earlier large deficits; the Euro dollar market has tightened more than seasonally; the dollar has strengthened in foreign exchange markets; and the price of gold in London has fallen sharply.

Abroad, demand pressures on the British economy do not appear to have slackened since the beginning of the year, despite a sharp drop in bank advances. However, effects of the 7 per cent bank rate and of other restraints are undoubtedly working through the economy. Financial markets are waiting to see what further reinforcement of restraint policies the April 6 budget will bring.

In France, business activity has slowed. But because wage rates are continuing to rise, the Finance Minister's opposition to reflationary measures seems likely to prevail.

SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally adjusted)

	Latest period	Amount			Per cent change	
		Latest Period	Precedg Period	Year Ago	Year Ago*	2 Yrs. Ago*
Civilian labor force (mil.)	Feb.'65	75.1	74.9	73.8	1.7	3.6
Unemployment (mil.)	"	3.7	3.6	4.0	-5.8	-12.8
Unemployment (per cent)	"	5.0	4.8	5.4	--	--
Nonfarm employment, payroll (mil.)	"	59.6	59.3	57.7	3.3	6.3
Manufacturing	"	17.8	17.7	17.2	3.4	5.1
Other industrial	"	7.9	7.8	7.7	2.1	5.9
Nonindustrial	"	33.9	33.8	32.8	3.4	7.0
Industrial production (57-59=100)	"	138.1	138.0	128.2	7.7	14.5
Final products	"	138.5	137.3	128.1	8.1	13.0
Materials	"	139.5	138.6	128.1	8.9	17.5
Wholesale prices (57-59=100) 1/	Jan.'65	101.0	100.7	101.0	0.0	0.5
Industrial commodities	"	101.6	101.4	100.9	0.7	1.3
Sensitive materials	"	101.3	101.2	98.0	3.4	5.0
Farm products and foods	"	98.1	97.2	99.7	-1.6	-1.7
Consumer prices (57-59=100) 1/	"	108.9	108.8	107.7	1.1	2.7
Commodities except food	"	104.9	104.9	104.3	0.6	2.2
Food	"	106.6	106.9	105.8	0.8	1.8
Services	"	116.6	116.2	114.2	2.1	4.1
Hourly earnings, mfg. ($)	Feb.'65	2.59	2.57	2.51	3.2	6.6
Weekly earnings, mfg. ($)	"	107.05	106.78	101.97	5.0	9.3
Personal income ($ bil.) 2/	Jan.'65	509.6	505.9	479.4	6.3	12.0
Retail sales, total ($ bil.)	Feb.'65	23.0	22.9	21.5	6.9	13.0
Autos (million units) 2/	"	9.6	9.7	7.9	20.3	29.8
GAF ($ bil.)	"	5.2	5.2	5.0	4.7	15.6
Selected leading indicators						
Housing starts, pvt. (thous.) 2/	Jan.'65	1,487	1,596	1,718	-13.4	13.2
Factory workweek (hours)	Feb.'65	41.4	41.4	40.7	1.7	2.7
New orders, dur. goods ($ bil.)	Jan.'65	21.3	20.7	19.7	7.7	15.2
New orders, nonel. mach. ($ bil.)	"	3.1	3.1	2.8	11.4	25.7
Common stock prices (1941-43=10) 1/	Feb.'65	86.75	86.12	77.39	12.1	31.6
Inventories, book val. ($ bil.)	Jan.'65	109.7	109.0	105.4	4.1	9.1
Gross national product ($ bil.) 2/	Q4 - '64	634.6	628.4	599.0	5.9	12.0
Real GNP ($ bil., 1964 prices) 2/	"	630.6	626.6	606.2	4.0	8.1

*Based on unrounded data. 1/ Not seasonally adjusted. 2/ Annual rates.

SELECTED DOMESTIC FINANCIAL SERIES

	Week ended March 12	Four-Week Average	Last six months High	Last six months Low
Money Market 1/ (N.S.A.)				
Federal funds rate (per cent)	4.02	3.98	4.12	1.00
U.S. Treas. bills, 3-mo., yield (per cent)	3.94	3.96	4.00	3.50
Net free reserves 2/ (mil. $)	-23	-26	256	-53
Member bank borrowings 2/ (mil. $)	385	382	590	122
Security Markets (N.S.A.)				
Market yields1/ (per cent)				
5-year U.S. Treas. bonds	e/4.16	e/4.16	4.16	4.04
20-year U.S. Treas. bonds	e/4.21	e/4.21	4.22	4.15
Corporate new bond issues, Aaa	4.48	4.46	4.53	4.33
Corporate seasoned bonds, Aaa	4.41	4.41	4.45	4.41
Municipal seasoned bonds, Aaa	3.09	3.05	3.12	2.94
FHA home mortgages, 30-year3/	5.45	5.45	5.46	5.45
Common stocks S&P composite index4/				
Prices, closing (1941-43=10)	87.21	86.91	87.56	83.48
Dividend yield (per cent)	2.98	2.99	3.05	2.94

	Change in Feb.	Average change last 3 mos.	Annual rate of change (%) 3 mos.	Annual rate of change (%) 1 year
Banking (S.A., mil. $)				
Total reserves	180	107	6.0	5.3
Bank loans and investments:				
Total	2,400	2,100	9.4	9.1
Business loans	1,100	1,200	25.4	14.2
Other loans	600	900	10.3	12.4
U.S. Government securities	100	-600	-11.1	-2.6
Other securities	600	500	15.6	12.7
Money and liquid assets:				
Demand dep. & currency	-700	0	0.0	3.4
Time and savings dep.	2,300	2,000	19.2	13.9
Nonbank liquid assets	1,600	1,200	6.0	5.9

N.S.A.--not seasonally adjusted. S.A.--seasonally adjusted. 1/ Average of daily figures. 2/ Averages for statement week ending March 10. 3/ Latest figure indicated is for month of January. 4/ Data are for weekly closing prices. e/ Estimate.

U.S. BALANCE OF PAYMENTS

	1965		1964					1963
	Feb.	Jan.	Dec.	QIVp	QIII	QII	QI	Year
	Seasonally adjusted annual rates, in billions of dollar							
Balance on regular transactions				- 5.8	- 2.7	- 2.5	- 1.0	- 3.3
Current account balance					7.0	6.5	8.0	4.9
Trade balance 1/		- 0.1	9.3	6.9	6.5	5.8	6.8	5.0
Exports 1/		14.2	28.8	26.5	25.4	24.2	24.4	22.0
Imports 1/		-14.3	-19.5	-19.6	-18.9	-18.4	-17.6	-17.0
Services, etc., net					0.5	0.7	1.2	- 0.1
Capital account balance					- 9.1	- 8.9	- 8.2	- 7.8
Govt. grants & capital 2/					- 3.6	- 3.9	- 3.1	- 3.8
U.S. private direct inv.					- 2.1	- 2.3	- 2.1	- 1.9
U.S. priv. long-term protfolio					- 2.3	- 1.1	- 0.8	- 1.7
U.S. priv. short-term					- 1.7	- 2.2	- 2.3	- 0.7
Foreign nonliquid					0.6	0.5	0.1	0.3
Errors and omissions					- 0.7	- 0.2	- 0.7	- 0.3
	Monthly averages, in millions of dollars							
Deficit on regular transactions (seas. adjusted)				483	226	211	82	272
Additional seasonal element				- 8	- 112	15	105	---
Financing (unadjusted)	370	199	261	491	338	196	- 23	272
Special receipts 3/	0	0	0	33	2	- 10	68	55
Liabilities increase								
Nonofficial 4/	22 (	520	- 594	207	184	36	77	49
Official 5/	(	- 650	512	300	129	69	- 151	136
Monetary reserves decrease	348	329	343	- 50	23	101	- 17	32
of which: Gold sales	(215)	(263)	(95)	(57)	(- 7)	(- 24)	(15)	(38)
[Memo: Official financing] 6/		(- 321)	(855)	(284)	(154)	(160)	(- 100)	(223)

1/ Balance of payments basis which differs a little from Census basis.
2/ Net of associated liabilities and of scheduled loan repayments.
3/ Advance repayments on U.S. Govt. loans and advance payments for military exports: assumed zero in absence of information.
4/ Includes international institutions (except IMF), commercial banks and private nonbank.
5/ Includes nonmarketable bonds.
6/ Decrease in monetary reserves, increase in liabilities to foreign official institutions, and special receipts.

THE DOMESTIC ECONOMY

Industrial production. Industrial production in February rose to 138.8 per cent of the 1957-59 average from 138.1 per cent in January and remained 8 per cent above a year earlier. Output of consumer goods increased, despite a small decline in auto assemblies, and production of business equipment also rose. Materials production continued to expand although operations in the primary metals industries changed little at near-capacity rates.

Auto assemblies declined 2 per cent in February from the record December-January level as severe storms briefly closed many plants. March production schedules indicate a rise to a new high. Output of furniture, television sets, and many other consumer goods rose further in February and over-all output of home goods and apparel was 8-1/2 per cent above a year earlier.

Production of industrial and commercial equipment increased in February but output of trucks declined substantially from an extraordinary high in January. Total business equipment production in January and February was 12 per cent above the year ago level.

Output of iron and steel changed little and was 2 per cent below the record rate reached just before the 1959 steel strike. In early March, steel ingot production edged up slightly. Output of parts for business equipment and consumer durable goods and of chemicals and textiles rose further in February while output of coal and crude oil declined. Over-all production of materials was 9 per cent above a year earlier; output of iron and steel was up 20 per cent and all other materials were up 8 per cent or about as much as final products.

Retail sales. Retail sales in February rose 0.6 per cent from their record January level, according to the Commerce advance report. January total sales figures have been revised substantially upward to a rate slightly above the December level. Nondurable goods sales in February were up 1.5 per cent from their slightly reduced January level, reflecting widespread gains among most categories. Sales at durable goods stores, mirroring declines at lumber and hardware and "other durable goods" outlets, were down 1.2 per cent. Sales at automotive and furniture and appliance outlets, however, were up slightly.

For January and February combined, total sales were up almost 5 per cent from their reduced fourth quarter monthly average. Durable goods were up 12 per cent from the fourth quarter and nondurables 1 per cent.

SEASONALLY ADJUSTED RETAIL SALES
(Per cent change)

	December to February	Fourth quarter to January-February average
Total	+1.0	+ 4.6
Durable goods	+1.3	+12.2
Automotive	+2.5	+19.6
Furniture and appliances	-0.5	+ 0.2
Nondurable goods	+0.9	+ 1.1
Apparel	+1.5	+ 1.4
Drugs	+3.6	+ 2.6
Eat and drink	+3.8	+ 4.5
Food	-1.8	- 0.8
Gas	+1.3	+ 1.7
General mdse.	+0.2	+ 2.3
GAF	+0.4	+ 1.6

In units, deliveries of new domestic automobiles in February were at a seasonally adjusted annual rate of 9.6 million vehicles, down 1 per cent from January but a fifth higher than a year earlier. Storms in the last week of February had no immediate effect on deliveries, although they may have reduced orders for later delivery. In early March dealer deliveries declined 1 per cent from a month earlier in contrast with expectations of a sizable seasonal rise. Deliveries may have been limited by storms in late February, but a rise of seasonal proportions this month might not be possible in view of capacity limitations on production.

Dealers' new car inventories rose seasonally in February and early March. With sales at exceptionally high rates, stocks continued below a year earlier and in terms of days' supply, below the average of other recent years.

Consumer credit. Demands for instalment credit have been strong this year, with much of the strength stemming from the fast pace of auto sales; activity and credit demands in other consumer areas also have continued to expand. Final figures for January showed instalment credit rising at an annual rate of close to $8 billion, compared with $6.7 billion in December. Early reports for February suggest a slower pace, more like that in December.

Automobile terms continue on the easy side. The bulk of all new car contracts continue to be written for a 36-month maximum, while almost one-third of used car contracts fall in the over 24 months category. And the latest data show that one-fifth of all new car contracts are being written at a figure above 100 per cent of dealer cost. Three years ago, this proportion was one-sixth.

Delinquency rates on auto contracts, as reported by a sample of commercial banks to the ABA, have been edging up but only toward the levels of a year ago. The increase is most apparent in purchased auto paper. For direct auto loans, delinquency experience has shown gradual improvement since early 1961.

Construction activity. Seasonally adjusted new construction expenditures, which had dipped in January, increased in February to a new high annual rate of nearly $68 billion. Residential construction rose further and--including upward revisions in each of the previous two months--was 6 per cent above its recent low in November and only 4 per cent below the record rate reported in March of last year. Led by industrial construction, private nonresidential and public activity also rose in February and were at or near their recent highs.

NEW CONSTRUCTION PUT IN PLACE

	February (billions) 1/	Per cent change from	
		Month ago	Year ago
Total	$67.7	+ 2	+ 3
Private	47.2	+ 2	+ 2
Residential	27.1	+ 2	- 2
Nonresidential	20.2	+ 1	+ 8
Business	14.5	+ 1	+11
Public	20.5	+ 1	+ 6

1/ Seasonally adjusted annual rate; preliminary.

Business inventories. Business inventory accumulation in January was not far below the very high rate in the two preceding months, as a pronounced step-down in accumulation reported for manufacturers was in part offset by a step-up in distributors' stocks. According to preliminary figures, which in recent months have been subject to large subsequent upward revisions, the January book value increase totaled $679 million. This compares with a November-December average of $830 million and with a fourth quarter average of $568 million. In the first three quarters of 1964, inventory accumulation was at the rate of only $245 million per month.

Manufacturers' inventory accumulation totaled only $225 million in January as contrasted to around $600 million in November and in December and $750 million in October. This January slackening stemmed primarily from a near leveling off in durable goods inventories after a series of sharp increases.

In view of a continuing high rate of accumulation of steel inventories the recently reported slow-down is difficult to explain. The book value of stocks of materials did continue to rise at durable goods manufacturers, but the rise was only half as large as the preceding 3-month average. On the other hand, according to a separate Census report on steel inventories in tonnage terms (and without seasonal adjustment), accumulation by steel consumers was proceeding at least as rapidly in January as in the fourth quarter.

Inventories held by nondurable goods manufacturers increased $167 million in January, about the rate of increase in the preceding three months. Increases from October to January followed nine months of little change, and the rise over the entire twelve-month period was quite moderate.

Distributors' inventories increased $452 million in January, and at the end of the month were slightly above the September level. Auto dealers accounted for half the January rise. Retail stocks of other durable goods also rose further in January, while nondurable goods inventories were about unchanged at a level that was low in relation to sales. Wholesale stocks continued the moderate but steady rise of other recent months.

CHANGE IN BOOK VALUE OF BUSINESS INVENTORIES
(millions, seasonally adjusted)

	January	Monthly average	
		Nov.-Dec.	Q IV
Total	$679	$830	$568
Manufacturers	227	584	642
Durable goods	60	448	458
Nondurable goods	167	136	184
Distributors	452	246	-74
Wholesale	60	93	80
Retail	392	153	-154
Addendum:			
Total, seasonally adjusted annual rate in billions	$8.1	$10.0	$6.8

Plant and equipment expenditure plans. Business spending for new plant and equipment is expected to increase throughout 1965 and to total $50.2 billion, exceeding capital outlays in 1964 by $5.3 billion or 12 per cent, according to the latest Commerce-SEC quarterly survey taken in February. The anticipated increase this year compares with an actual increase of 14.5 per cent in 1964.

EXPENDITURES FOR NEW PLANT AND EQUIPMENT
(Per cent change)

	Planned 1965		Actual 1964	
	1964 to 1965	'64-IV to '65-IV*	1963 to 1964	'63-IV to '64-IV
All industries	11.7	7.5	14.5	15.9
Manufacturing	15.9	8.3	18.4	22.5
Durable	13.6	5.6	20.1	22.3
Nondurable	18.2	11.1	16.8	22.7
Mining	10.1	5.4	14.4	23.8
Railroad	14.9	9.7	28.2	14.8
Transportation other than rail	8.0	-7.7	24.0	23.8
Public utilities	5.5	5.8	10.1	9.5
Communications, commercial, and other	9.6	8.0	9.5	9.0

*--Estimated from the February survey totals for the last half of th year and the indicated trend for the first two quarters of the year.

Most major industries expect a higher rate of outlays in the second half of the year than in the first half, but spending plans suggest outlays in the final quarter of 1965 may be only 7.5 per cent higher than in the fourth quarter of 1964, as compared with a rise of 16 per cent from late 1963 to late 1964.

A year ago, the Commerce-SEC survey taken in February indicated a gain in fixed capital spending for 1964 of 10 per cent whereas actual spending increased 14.5 per cent. Upward revisions in plans occurred throughout last year, with the largest revision in the fourth quarter. Last year's upward adjustment was exceptionally large and can be explained by special factors, including the reduction in Federal income taxes.

Manufacturers' expenditures for new plant and equipment this year are expected to increase 16 per cent, with advances widespread among industries. The gain from recent levels to the end of this year, however, may be no more than half the rise indicated for the year as a whole. Outlays now planned for the second half of this year by electrical machinery, motor vehicles, and food and beverage industries are less than indicated for the first half.

The survey also indicates that manufacturers expect an increase in sales of 6 per cent in 1965. A year ago manufacturers had expected a 6 per cent increase in sales for 1964; the actual increase turned out to be 7 per cent.

A recent survey by the National Industrial Conference Board of the 1,000 largest companies indicates that new capital appropriations of manufacturers in the final quarter of 1964 were down 20 per cent from the third quarter. This decline followed substantial increases in the two preceding quarters. Significantly, the backlog of unspent appropriations at the end of the year was as large as at the end of the third quarter. This survey, according to the Conference Board interpretation, suggests that the expansion in manufacturers' capital spending "may tend to slow down a bit toward the end of this year."

Manufacturers' inventory and sales expectations. Manufacturers now expect their inventories to increase much more slowly in the first and second quarters of 1965 than in late 1964. According to the Commerce quarterly survey, conducted in February, manufacturers anticipate book value increases of only $700 million in the first quarter and of $900 million in the second quarter, as compared with actual accumulation totaling $1.9 billion in the fourth quarter. The shift in pace is expected to come primarily in durable goods industries; nondurable goods producers look for accumulation to continue near their moderate fourth quarter rate. The February survey represents the second reading on first quarter prospects and the change now anticipated is almost identical with the first "anticipation" obtained in last November's survey.

Assuming the fourth quarter data are correct, manufacturers had seriously underestimated their accumulation in the two successive anticipatory surveys of last August and November. There is thus a possibility that the first quarter rate is also being underestimated. An important factor in the high rate of inventory investment in the fourth quarter was the stepped-up rate of steel stock building at mills and by steel users; in the first quarter, inventory accumulation at the steel mills may have tapered off but accumulation by steel consumers must have continued substantial.

The survey indicated a large rise in manufacturers' sales expectations from the fourth to the first quarter, but most of this rise had occurred by December after the auto strikes. Manufacturers' expectations for the first quarter as a whole can be achieved by only a small further gain from the advanced December level. Actual manufacturers' sales in January were reported slightly below the record December level.

More interesting is an expected small sales decline in the second quarter as a result of a 3 per cent decline anticipated by durable goods producers as a group. Nondurable goods sales are expected to continue upward. Cutbacks in auto and steel shipments from the very high first quarter levels are expected in the second quarter, according to the survey.

Labor market. Employment in nonfarm establishments continued to rise in February and the length of the workweek in manufacturing was maintained at a high level. Employment increased 230,000 last month; about one-fourth of the rise was due to the return of longshoremen to work at most ports. At 59.6 million in February, nonfarm employment was 1.8 million higher than a year earlier.

The gain in manufacturing employment was somewhat smaller than in January as transportation equipment and machinery industries reported smaller increases and primary metals showed little change. In nondurable goods industries, employment was unchanged; declines in foods and apparel offset small advances in most other industries. Durable goods have accounted for 460,000 of the nearly 600,000 rise in total manufacturing employment over the past year.

The employment gain in nonfarm industries as a whole so far this year has been about the same as in the comparable period of 1964, if allowance is made for the dock strike. Construction employment has increased less but durable goods manufacturing has increased much more than last year. Other industries have experienced about the same changes as in early 1964.

CHANGES IN NONFARM EMPLOYMENT
(Seasonally adjusted, in thousands)

Industry	December 1964 to February 1965	December 1963 to February 1964
Total	354	393
Manufacturing	135	56
Durable goods	112	23
Nondurable goods	23	33
Nonmanufacturing	219	337
Construction	6	80
Other industrial 1/	-35	9
Trade	155	133
Finance and service	72	84
Government	21	31
Federal	-15	-9
State and local	36	40

1/ Decline in 1965 due to the dock strike.

Unemployment in February was 5 per cent of the civilian labor force and the rate has shown relatively little change since July 1964. During this period, employment has increased significantly, but job gains have been largely matched by growth in the labor force. A year ago, the unemployment rate was 5.4 per cent.

The teenage unemployment rate declined slightly in February but it was still not much below the 15 per cent level which has persisted for more than 2 years. The gain of about 200,000 in teenage employment over the past year is about as large as the net addition to the teenage work force. In recent months, fewer young people have been entering the labor force than expected and their participation rate has been declining. However, the situation may change in the spring and summer when youths are expected to enter the labor force in exceptionally large numbers. It probably will not be possible until then to judge the impact on the labor market of the sharply increased numbers of young people graduating from high school this year.

The jobless rates for adult men and for married men changed little last month and, at 3.6 and 2.6 respectively, were close to the low levels of early 1957 when the total unemployment rate was 4 per cent. Long-term unemployment (15 weeks or longer) rose in February but was 100,000 below a year ago.

Hours and earnings. The average workweek in manufacturing continued in February at the postwar high level of 41.4 hours. In durable goods industries as a whole, hours declined somewhat although they continued to edge up in transportation equipment (to 43.8) and in primary metals (to 42.5). In nondurable industries, the workweek reached an average of 40.0 hours at the end of 1964 and has since increased slightly to 40.2 in February. A level this high has not been sustained so long since the winter of 1955-56.

Average hourly earnings in manufacturing, seasonally adjusted, rose 2 cents in February to $2.59 and were 1 cent above the September 1964 high. Hourly earnings were 3.2 per cent higher than in February a year ago--about in line with the increase in the preceding year. Average weekly pay has increased 5 per cent reflecting, in addition to the higher hourly earnings, the rise in overtime hours at premium pay, principally in the high wage metals industries.

Labor negotiations. Since March 1, over 30,000 members of the steelworkers union have been on strike against the two major can companies. Negotiations are continuing. The general outline of a settlement which is now developing appears to be for a 3-1/2 year contract retroactive to last October 1, with a 12 cent an hour, or nearly 4 per cent money wage increase the first year and a concentration on fringe benefit improvements in the second year. For the third year there would be a small wage boost and further fringe improvements. Major disagreements seem to be over the extent of supplementary unemployment benefits and pension increases.

A settlement with the can companies is expected to have considerable influence on steel negotiations. An expanded union bargaining team, including members of McDonald's opposition, is being established and it is expected that there is sufficient unity on the union side to carry on serious talks with the steel companies.

Prices. The industrial commodity price index, according to weekly estimates, has been stable since mid-January at a level less than 1 per cent above that prevailing during the first nine months of 1964. Wholesale prices of foodstuffs have increased slightly from mid-January, mainly as a consequence of reduced supplies of livestock and fruits and vegetables. Reflecting the rise in foodstuffs, the combined wholesale index has edged up further in recent weeks, and at 101.3 per cent of the 1957-59 average, is about 1 per cent higher than in the first quarter of last year.

In early March, list prices of certain types of tool steels were increased for the first time sinee 1958. Producers cited rising costs, particularly for alloying materials. While tool steels are of great importance to the machine tool industry, they account for less than one per cent of the total value of finished steel. Major producers also posted increases for some grades of electrical sheet and a reduction in one other grade. Mainly because of the strike possibility, demand currently is strong enough to support these increases. More generally, prospects for steel prices still appear to depend on the outcome of labor contract negotiations--whether or not supplies are reduced by a strike as well as by the terms of the contract eventually agreed on.

Meanwhile, steel scrap prices have weakened in recent weeks. Supplies, from automobile stamping plants, have increased at the same time that mills have curtailed their buying because of adequate inventories and the prospects of a decrease in steel production. Export demands for scrap also are reported to have declined.

Nonferrous metals are still generally in short supply. However, both the Senate and the House have now passed bills to authorize sales of copper, lead, and zinc from the stockpile, and such sales should help to lessen shortages until supplies from commercial sources increase sufficiently. The GSA is prepared to act promptly upon final passage of the authorizations. Tin continues to be released by the GSA in quantities such that all reasonable domestic demands are being met at prices around $1.60 per pound.

Apart from the metal markets, the past several weeks have been a relatively quiet period for prices. Increases have once again been announced for a variety of paper and packaging products, and perhaps some of the increases will stick this time. Among chemicals, there have been decreases as well as increases. Fuel oils apparently have turned down again. A price index of all industrial commodities other than metals and machinery has been nearly stable over the past 2 years at a level a little more than 1 per cent below the high reached in the spring of 1959. The combined index for metals and machinery has risen nearly 3 per cent over the past 2 years; it is 1.3 per cent above the high reached in 1960, but it is likely that at least some portion of that rise reflects inadequate allowance in the indexes for improvement in the quality of machinery.

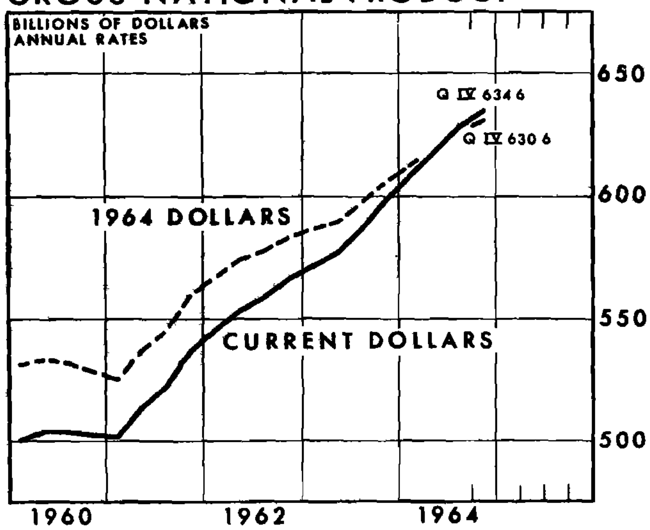
The consumer price index rose 0.1 per cent in January and remained 1.1 per cent above a year earlier. While prices of services continued to rise, prices of foods declined. The average for nonfood commodities was stable.

Fuels rose further, to about the year-ago level, but apparel declined by about the usual seasonal amount. New car prices declined, but by less than the usual seasonal amount because of strong demand and the lingering effects of the strike last autumn; nevertheless, retail prices of new cars were slightly lower than a year earlier. Household durables continued their slow but steady downward trend, and textile housefurnishings declined.

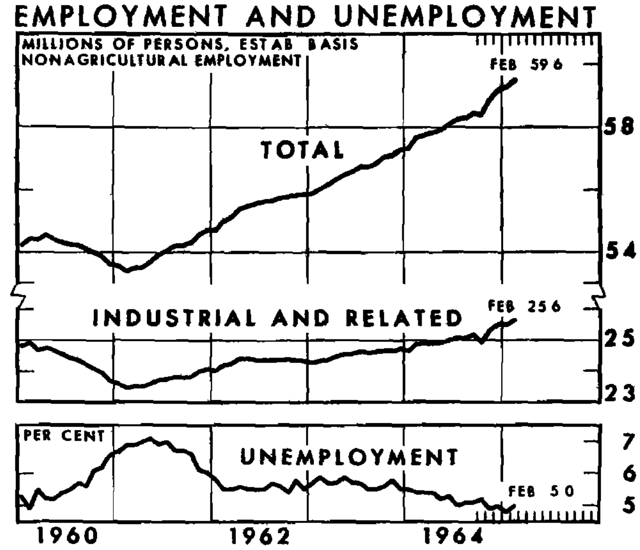
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

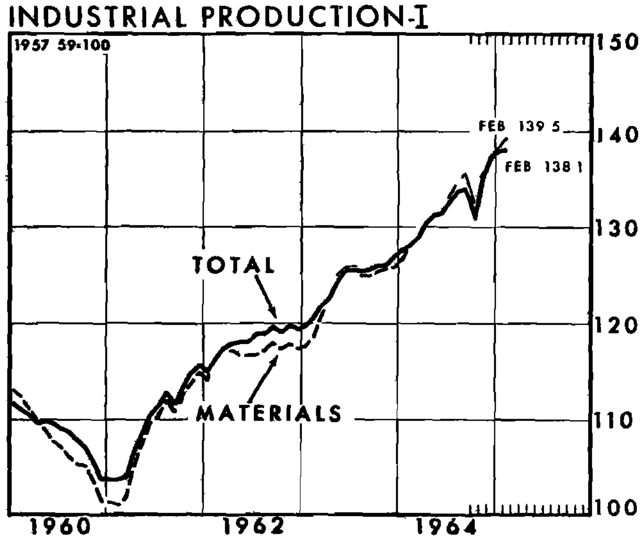
GROSS NATIONAL PRODUCT



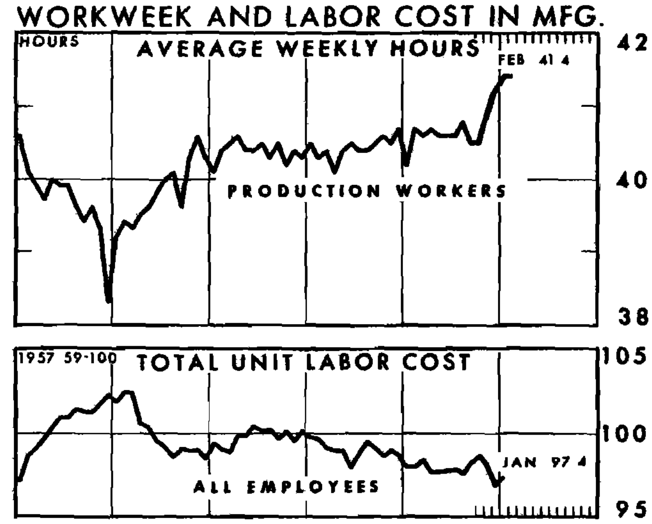
EMPLOYMENT AND UNEMPLOYMENT



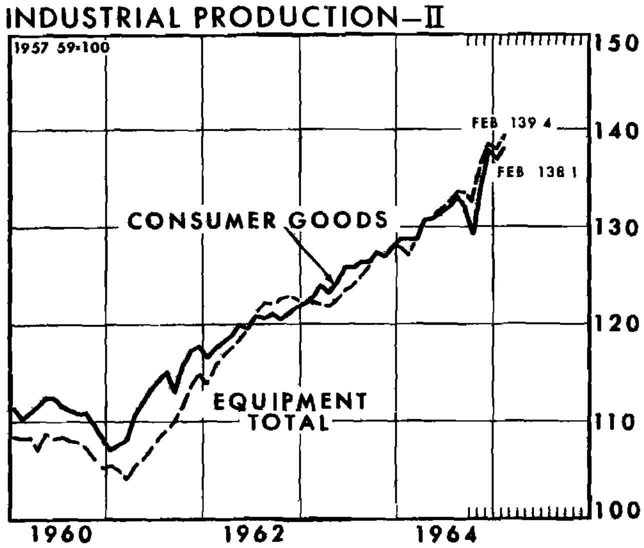
INDUSTRIAL PRODUCTION-I



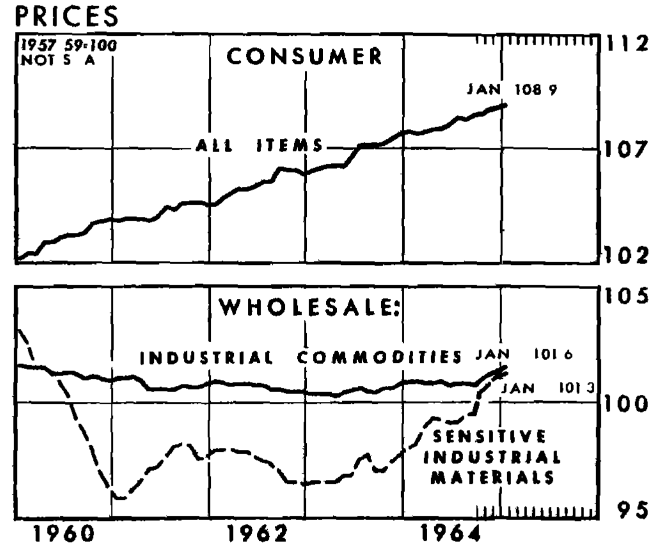
WORKWEEK AND LABOR COST IN MFG.



INDUSTRIAL PRODUCTION—II



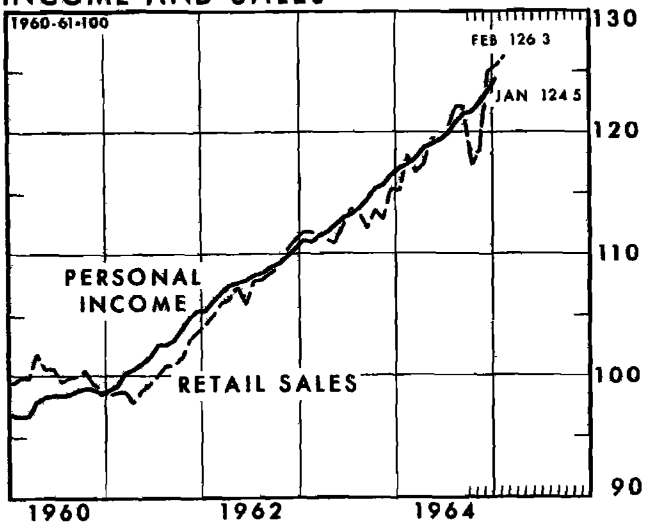
PRICES



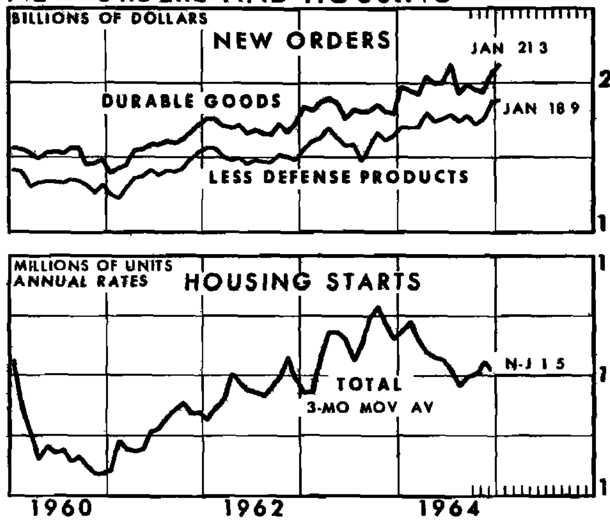
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

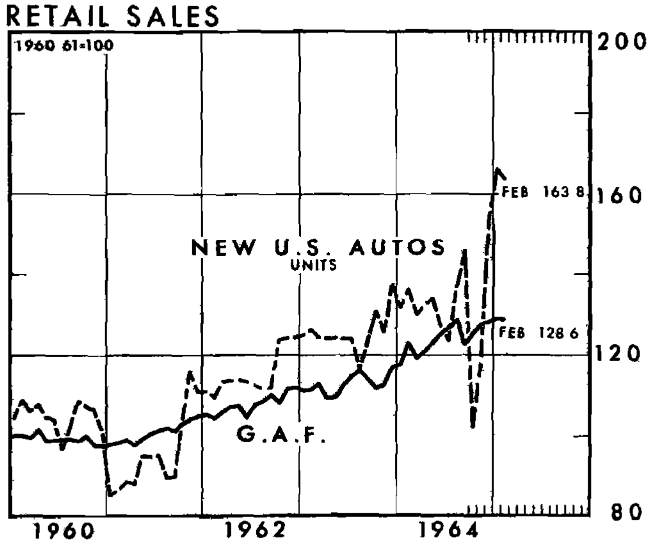
INCOME AND SALES



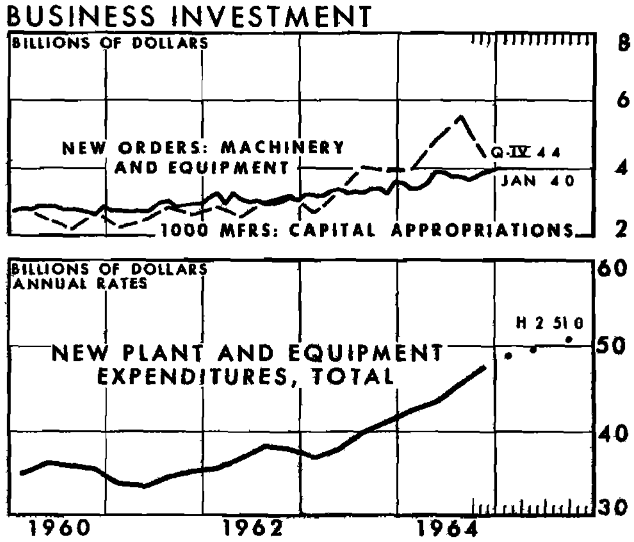
NEW ORDERS AND HOUSING



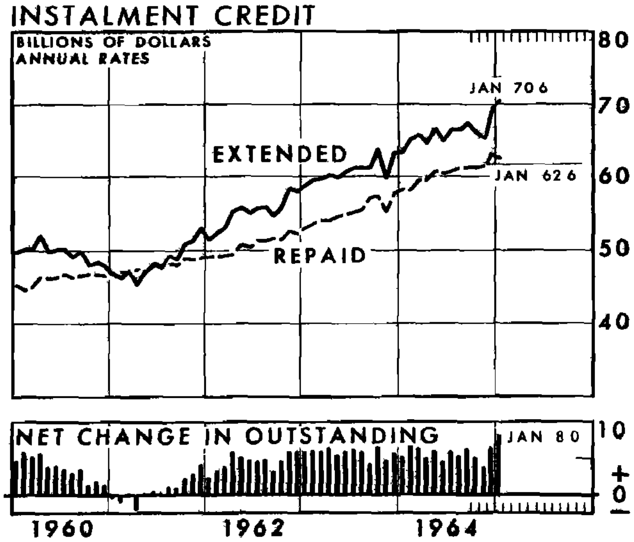
RETAIL SALES



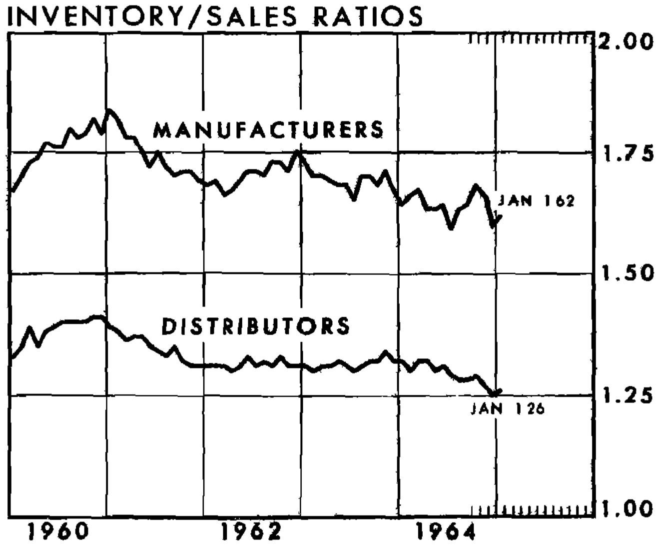
BUSINESS INVESTMENT



INSTALMENT CREDIT



INVENTORY/SALES RATIOS



DOMESTIC FINANCIAL SITUATION

U. S. Government securities market. Yields on U. S. Government securities have declined from recent peaks reached in late February or early March. The Treasury bond market has been strengthened by a growing conviction that the Administration's current program to improve the balance of payments will prove effective, thereby lessening the need for a more restrictive monetary policy. Meanwhile, the technical position of the long-term market has improved, as dealers have continued to make progress in reducing their holdings of Treasury bonds. Small but steady investment demand for notes and bonds has been reported over the past three weeks, a period when purchases of coupon issues by the System and the Treasury trust accounts have been minor in amount. Toward the end of this period, bond prices were run up further on the appearance of some demand from dealers and other temporary holders.

YIELDS ON U. S. GOVERNMENT SECURITIES

Date (closing bids)	3-month bills	6-month bills	3 years	5 years	10 years	20 years
1964-65						
Highs	4.00	4.05	4.22	4.21	4.26	4.26
Lows	3.42	3.50	3.92	3.99	4.12	4.14
1964-65						
December 31	3.82	3.92	4.06	4.12	4.21	4.21
February 2	3.88	3.95	4.04	4.12	4.20	4.19
March 2	3.98	4.03	4.15	4.18	4.24	4.22
March 16	3.92	3.98	4.14	4.14	4.20	4.20

A more surprising feature of the government securities market has been the recent declines in Treasury bill yields. Selling associated with the March dividend and tax dates has been relatively light, while sizable market demand has been evident from a wide range of investors, notably public funds but also including banks and nonfinancial corporations. Market participants have reported that the demand for bills may have been augmented recently by a return flow of funds from the Euro dollar and other money markets abroad, but direct evidence is lacking.

With demand strong, dealer bill positions have tended to decline, and dealers have had to bid rather aggressively at weekly auctions to restock inventories. In auctions held March 8 and March 15, the average issuing rate for the 3-month bill declined to 3.95 per cent and 3.92 per cent respectively.

The downdrift in bill rates has occurred despite continued pressure on bank reserve positions and a generally taut atmosphere in the Federal funds market. Reflecting this tautness, dealer financing costs have remained relatively high at money market banks, but dealer financing needs have declined along with their lower positions in bills and bonds. With a lower need, dealers have not had to rely heavily on high cost New York City bank financing. At the same time, a large amount of financing (through repurchase agreements) has been available from corporations and banks outside New York at relatively attractive rates, reflecting in part the temporary build-up of corporate cash prior to the March tax date. Thus, in the recent period, pressures on central money market banks have not been transmitted to the bill market.

Corporate and municipal bond markets. Yields on corporate and municipal bonds, after advancing by as much as 15 basis points from late January to early March, have recently stabilized at about the levels prevailing last fall. An enlarged volume of new issues is currently meeting favorable reception at these levels. The improved tone of the market probably reflects both the more realistic pricing of new issues and some lessening of investor concern that the balance of payments situation might require further near-term yield adjustments.

Earlier this year, a light calendar had led underwriters to bid aggressively for publicly offered issues but retail distribution proved slow, and when syndicates were broken, yields rose sharply. In contrast the latest offerings have sold out quickly, and some of the increased investor interest has spilled over to issues remaining in syndicate. At the same time, the market in early March readily absorbed the $343 million secondary offering of U.S. Government holdings of General Aniline and Film Corporation common stock.

In the municipal market, yields on Aaa-rated issues also have stabilized after rising sharply from mid-February to early March. At these higher levels, the distribution of new offerings quickened considerably. While the average yield on seasoned, Aaa-rated State and local government bonds is the highest since early last November, it is still 7 basis points below the 1964 high reached in May. The record $831 million inventory of unsold securities, advertised by dealers early this month, has declined to about $740 million as investor reception of new issues has improved and price cutting on older tax-exempts has resulted in sales from inventory.

BOND YIELDS
(Weekly averages - per cent per annum)

	Corporate Aaa		State and local government	
	New	Seasoned	Moody's Aaa	Bond Buyer (mixed qualities)
1964				
Sterling crisis high	4.47 1/	4.45	3.09	3.21
Year-end	n.a.	4.43	2.99	3.12
1965				
Jan.-Feb. - High	4.42	4.44	3.03	3.20
Low	4.33	4.41	2.94	3.04
Week ending				
1965 - Feb. 26	4.41	4.41	3.03	3.17
Mar. 5	4.48	4.41	3.09	3.20
12	4.48	4.41	3.09	3.18

1/ Week ending December 4.

While the total volume of new corporate bonds scheduled to be publicly offered this month is the largest since December 1963, this should not be overemphasized as a measure of either present or future corporate financing needs. Public offerings in January and February were small and, even with the exceptionally large March total, public offerings for the first quarter will still be below a year ago. The volume of private placements is expected to continue heavy in the current month, and during the first quarter directly placed bonds will exceed those publicly offered by two-thirds. As a result, total corporate bond offerings in the first quarter of 1965 are likely to exceed a year earlier by about 10 per cent.

Gross new issues of corporate stock in the first quarter also appear to have been somewhat larger than a year earlier, but this comparison is misleading as a measure of the change in net new equity funds flowing to corporations. First, the statistics on gross offerings for the first quarter of 1964 include none of the $1.2 billion AT&T issue, though over half of the proceeds were delivered to the company in March. Second, data on gross offerings are before allowance for retirements of outstanding stock. Retirements have been unusually large this year and, as a result, corporations have obtained almost no net new funds from equity financing.

In the case of State and local government financing, while the estimated volume of bond issues for this month is 10 per cent above that of March 1964, total offerings for the first three months of 1965 are estimated to be slightly below the first quarter last year. For the second quarter, the projected volume should be about the same as the first quarter, after rough allowance for the usual seasonal change. The timing of new issues over the period is apt to have considerable influence on market developments.

BOND OFFERINGS 1/
(Millions of dollars)

	Corporate				State & local govt.	
	Public offerings		Private placements			
	1965	1964	1965	1964	1965	1964
Jan.-Mar. avg.	305e/	326	517e/	407	892e/	912
January	165e/	338	550e/	526	825e/	1,009
February	190e/	279	500e/	342	900e/	858
March	560e/	361	500e/	343	950e/	860

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

Stock market. Common stock prices, as measured by Standard and Poor's index of 500 stocks, have fluctuated within a narrow range during the past several weeks. Trading has been very active averaging 6.1 million shares daily. At the close Tuesday, the index registered 87.13, not significantly below the all-time high of 87.58 reached on February 1. The total amount of customer credit in the stock market declined slightly further in February to a little less than $6.9 billion, but customers' net debit balances carried with member firms of the New York Stock Exchange rose by $19 million to slightly more than $5 billion, reversing an extended downtrend.

Mortgage markets. Mortgage funds have generally remained ample this year. In February, secondary market yields on FHA-insured, 30-year mortgages again held at 5.45 per cent, as in most of the past two years. Contract interest rates for conventional first mortgages on homes also remained at the reduced rates reached in early 1963--5.80 per cent for new loans and 5.85 per cent for loans on previously occupied homes according to the Federal Housing Administration. Indications are, however, that downward pressure on origination fees and associated charges have persisted this year.

Nonrate terms on conventional first mortgages on existing property loans generally remained slightly more liberal than a year earlier. For new home loans, larger average loan amounts were being allowed on higher priced homes, but loan-to-price ratios and maturities were the same or somewhat lower than a year earlier.

AVERAGE TERMS ON CONVENTIONAL FIRST MORTGAGES FOR HOME PURCHASE

	December 1964	January 1965	Per cent increase to January 1965 from a year earlier
New home loans			
Purchase price ($1,000)	24.3	23.9	+ 6
Loan amount ($1,000)	17.8	17.5	+ 4
Loan/price (per cent)	73.9	74.0	- 1
Maturity (years)	25.2	24.7	--
Existing home loans			
Purchase price ($1,000)	19.2	19.1	+ 2
Loan amount ($1,000)	13.7	13.6	+ 2
Loan/price (per cent)	71.7	71.6	+ 2
Maturity (years)	20.1	19.9	+ 2

Foreclosures on nonfarm real estate--mainly homes--dipped slightly from the third to the fourth quarter of last year. While the total for the year exceeded 100,000 for the first time in the postwar period, the increase from 1963--one tenth--was the smallest since 1959. In 1963, the number of foreclosures increased a seventh, and in 1961, two-fifths.

NONFARM MORTGAGE FORECLOSURES

Year	Number (thousands)	Rate per thousand mortgaged homes
1964	108.6	4.6
1963	98.2	4.4
1962	86.4	4.1
1961	73.1	3.6
1960	51.4	2.7
1959	44.1	2.3

Bank credit. Seasonally adjusted total credit at all commercial banks increased substantially further in February. The annual rate of growth for January and February averaged 11-1/2 per cent, considerably above the 8 per cent rise in 1964. At city banks, credit growth continued at a more-than-seasonal pace in the week of March 3, but this was followed by a contraseasonal decline at New York City banks in the week of March 10.

The credit rise in February, as in January, reflected a continued strong loan demand and large inflow of time and savings deposits, but both have moderated recently. While business loans have accounted for most of the surge in loan demand, growth in real estate and consumer loans also has accelerated this year. After showing little net change since last summer, the loan-deposit ratio rose to a new postwar high at the end of February.

NET CHANGES IN COMMERCIAL BANK CREDIT
(Seasonally adjusted)

Item	Dollar amount (billions of dollars)			Annual rate (per cent)		
	Feb. 1965	Average Jan.-Feb.1965	Average Year 1964	Jan.-Feb. 1965	Year 1964	Jan.-Feb. 1964
Total loans & investments	2.4	2.6	1.6	11.5	7.9	4.6
U.S. Govt. securities	0.1	-0.7	-0.1	-12.8	-1.9	-8.7
Other securities	0.6	0.8	0.3	23.4	9.7	6.9
Total loans	1.7	2.5	1.4	17.6	11.6	9.6
Business	1.1	1.4	0.5	29.2	10.8	10.4
Security	-0.6	0.1	1/	8.7	3.0	17.9
Nonbank financial	0.2	0.1	0.1	11.9	11.0	-6.6
Real estate	0.5	0.4	0.4	11.0	11.3	13.8
Consumer	0.4	0.4	0.2	14.3	10.1	9.0
Loans (excl. security)	2.3	2.4	1.4	18.0	12.0	9.2

1/ Less than $0.05 billion.

Holdings of U.S. Government securities declined less than usual in the second half of February after rapid liquidation earlier in the year. A large part of the decline has been in Treasury bills which, together with heavy participation in the January advance refunding, has resulted in a substantial decline in bank liquidity. Nevertheless, the ratio of short-term Governments to total deposits at all commercial banks remains well within the range of fluctuation over the past year. In late February and early March, some city banks added to their bill holdings, particularly in New York City, where holdings of short Governments previously had fallen to unusually low levels.

Seasonally adjusted business loans at all commercial banks increased $1.1 billion in February, more than in any previous month except for the unusually sharp $1.7 billion rise in January. The average rate of growth over the two months was almost three times the monthly average in 1964. Loan demand at city banks continued strong in the week of March 3, but this was followed by a contraseasonal decline in outstanding loans at New York City banks in the week of March 10.

The less rapid expansion since January presumably reflected in part some tapering off in the pace of lending to foreign businesses following the President's balance-of-payments message and the launching of the voluntary credit restraint program. Also, borrowing stemming from the dock strike has terminated. For example, outstanding loans to commodity dealers, after rising contraseasonally at a rapid rate in January and at a reduced rate in February, turned down in March.

On the other hand, inventory borrowing in anticipation of a possible steel strike has continued at a moderate pace. Moreover, a strong undercurrent of loan demand, presumably related to the rapid pace of domestic economic expansion, has persisted in the trade, public utilities, petroleum and chemicals and miscellaneous manufacturing groups.

Term lending at New York City banks has increased sharply this year, also presumably reflecting the accelerated pace of foreign lending and increased domestic plant and equipment expenditures. Through March 10, these loans had increased over $600 million compared with a $220 million decline in the comparable period last year. As a result, the ratio of term to total business loans outstanding at these banks rose substantially after showing only a small net increase over the preceding two years.

Money supply and time deposits. The seasonally adjusted money supply declined $700 million in February to a level of $159.1 billion, the same as in November. This decline was associated with a larger-than-usual build-up in U.S. Government deposits at commercial banks and with a continued large growth in time and savings deposits. In the first half of March, however, preliminary data indicate a substantial money supply increase.

Seasonally adjusted time and savings deposits at all commercial banks increased $2.2 billion in February following the record rise of $2.4 billion in January. Over the two months growth was at an annual rate of almost 22 per cent, close to the highs of early 1962.

Preliminary data suggest, however, that the rate of growth tapered off somewhat in the first half of March.

At city banks, the dollar amount of savings deposit growth so far this year has been about the same as in early 1962, although the percentage rise has been about one-fourth less. Other time deposits (IPC) have increased more so far this year than in the comparable period of any other recent year. A major contributor to this year's more rapid rise is the large growth in nennegotiable savings and investment certificates.

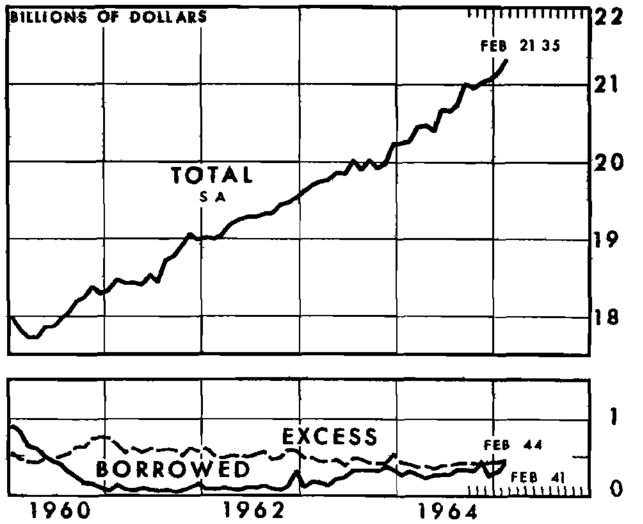
Negotiable CD's also are up more this year than in prior years. But after rising rapidly in January, they rose only moderately in February and early March. Most of the January growth was at banks outside New York City, but since then, outstandings at these banks have shown little net change. In the week of March 10, New York City banks increased their outstandings by $227 million, presumably in anticipation of large maturities on the March 15 tax date, which exceeded $450 million or nearly twice as much as a year earlier. Negotiable CD's maturing in March, according to the February 17 survey, amounted to nearly 24 per cent of total outstandings on that date, the highest ratio reported for any tax month thus far.

To obtain new CD funds, some New York City banks raised their rates on maturities of 6 months or more to 4-3/8 per cent. At these rates, it is possible that some nonprime banks may again be encountering difficulties in rolling over their outstandings under the existing ceiling rates. On March 3, unsecured notes outstanding reached a new high of $183 million, an increase of more than $100 million since the beginning of the year.

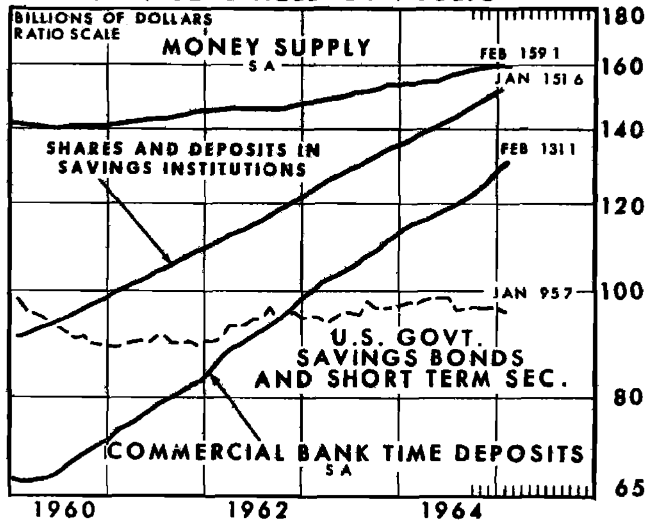
<u>Bank reserves</u>. Net borrowed reserves averaged $25 million over the four weeks ending March 10, with borrowings exceeding excess reserves in three of the four weeks. Borrowings rose to an average of $380 million between mid-February and mid-March compared with about $300 million over the previous four weeks. In addition, excess reserves declined to $360 million from the previous $400 million average. The effective rate on Federal funds was consistently at the discount rate between February 10 and March 15 except for four days. Some transactions took place at higher than 4 per cent on 16 days and at lower rates on 6 days.

FINANCIAL DEVELOPMENTS - UNITED STATES

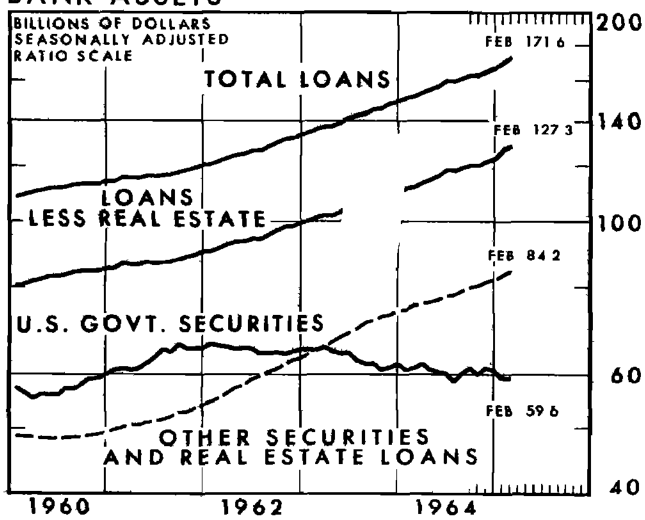
BANK RESERVES



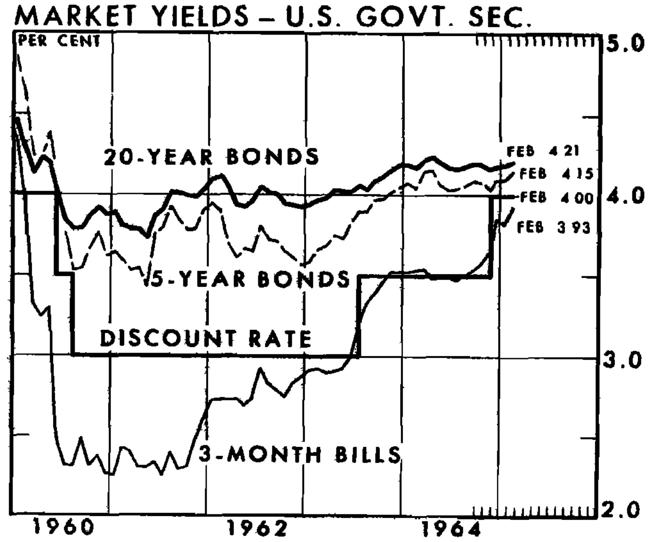
LIQUID ASSETS HELD BY PUBLIC



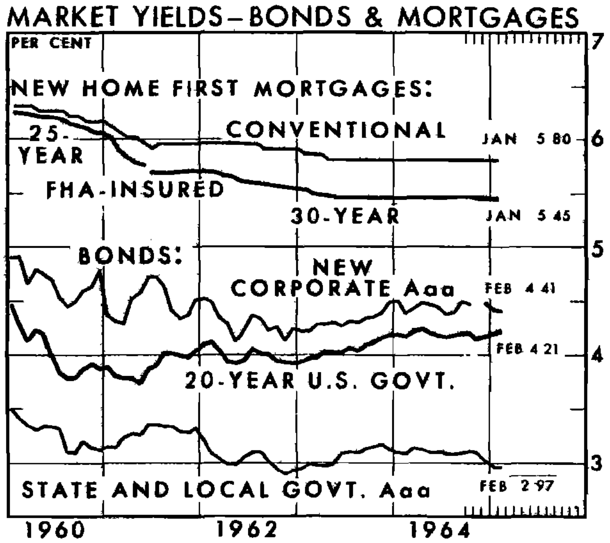
BANK ASSETS



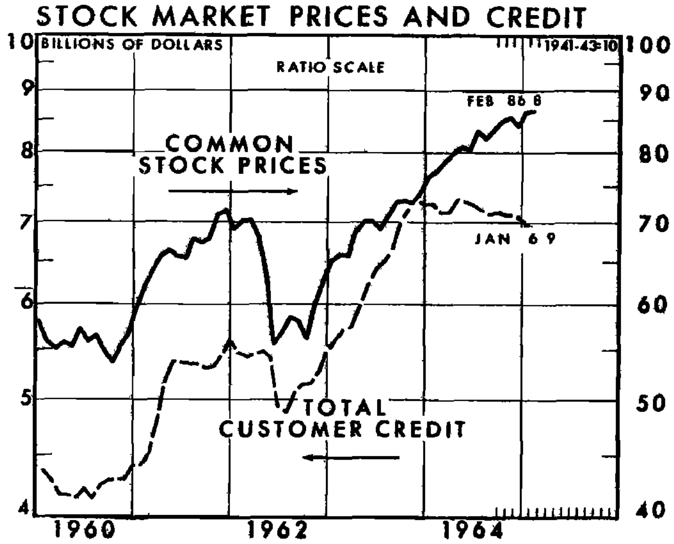
MARKET YIELDS – U.S. GOVT. SEC.



MARKET YIELDS–BONDS & MORTGAGES



STOCK MARKET PRICES AND CREDIT



INTERNATIONAL DEVELOPMENTS

U.S. balance of payments. The over-all payments position has shown a marked improvement since the middle of February, according to the fragmentary information presently available. The large deficit of the first month and a half of the year has seemingly been replaced, at least temporarily, by a modest surplus. Despite the recent improvement, the over-all deficit in January and February totalled over $600 million (as measured by changes in U.S. monetary reserves, increases in liquid liabilities to foreigners and estimated advance payments on military sales).

In part, the improvement of the last few weeks reflected the intra-quarterly pattern of movements of U.S. corporate funds into foreign liquid investments early in the quarter and a return flow late in the quarter to meet the tax date. The behavior of the over-all deficit indicators taken together with developments in the Euro-dollar market may mean, however, that this year the shift in these flows was greater than in the corresponding periods of 1963 and 1964. Another element in the improvement was a probable cut back, from the reportedly very heavy rates early in the month, in outflows of long-term bank loans to developed countries following the imposition of the Interest Equalization Tax on these loans beginning February 11. No information is available for this most recent period on short-term bank credit and other capital outflows, and the possible impact of the balance of payments program on these flows.

Details on bank-reported capital movements in January show that of net long-term bank loans to foreigners totaling $261 million, the major portion went to countries outside Europe, and especially to Latin America. This contrasts with the fourth quarter when about two-thirds of the net outflow of these loans went to European countries.

The decline in short-term bank-reported claims of $134 million in January consisted principally of a fall in acceptance credits and some reflow out of dollar deposits and other liquid investments abroad. The latter reflow followed the large December outflows into these investments in response to year-end liquidity demands abroad.

Merchandise exports and imports were cut sharply in January, as a result of the port strikes beginning in the middle of the month. As in comparable circumstances two years earlier, exports were reduced by one-half and by a much larger absolute amount than imports. Imports declined by about one-fourth. The trade figures for February, when they appear, are not likely to show a big rebound, since most ports did not reopen until mid-February. Strenuous efforts have reportedly been made since the end of the strike to clear backlogs of goods at ports but trade estimates of the time needed to accomplish this have ranged from 6 to 8 weeks.

Euro-dollar and foreign exchange markets. Posted rates for U.S. dollar deposits in London increased sharply in the first two weeks of March. Tightness in the Euro-dollar market was particularly acute around March 8-10, when increases of from 1/4 to nearly 1/2 per cent occurred for most maturities and when no sellers appeared on one or two days and only bid quotations were available.

As Euro-dollar rates in London moved up, rates for prime 3-month British hire-purchase paper and local authority deposits also increased sharply from 7-1/2 and 7-1/4 per cent, respectively, on March 1 to 8 and 8-1/8 per cent in the week ending March 12. Movements in Euro-dollar and other rates are shown in the following table:

SELECTED MONEY MARKET RATES IN LONDON
(in per cent)

	Euro-dollar deposits					Hire-purchase paper	Local authority deposits
	Call	7-day	30-day	90-day	180-day	3 mos.	3 mos.
Dec. 23,'64	3-7/8	4-5/8	4-7/8	4-7/8	4-7/8	7-3/4	7-3/4
Jan. 6,'65	3-13/16	4-1/16	4-3/8	4-9/16	4-5/8	7-1/4	7-1/8
Feb. 10	4-1/16	4-3/16	4-3/8	4-1/2	4-9/16	7-3/8	7-1/4
Mar. 3	4-1/8	4-5/16	4-9/16	4-11/16	4-13/16	7-5/8	7-3/4
Mar. 10	4-3/16	4-5/8	5	5-1/8	5-1/4	8	8-1/8
Mar. 16	4-1/8	4-5/16	4-3/4	5	5-1/8	8	8

The rise in Euro-dollar rates in the first two weeks of March was partly seasonal. Usually, these rates fall in January after the period of year-end tightness has passed; in March some recovery in rates occurs partly because U.S. corporate funds are withdrawn to meet the mid-March tax date. The rise this year, however, was much sharper than usual, bringing rates back up to the peak seasonal level of last December. This may have reflected larger than usual withdrawals of U.S. corporate funds, possibly in response to the balance of payments program. In addition, the initial seasonal rise in rates may have helped to trigger some speculative demands for Euro-dollars in anticipation of large withdrawals of U.S. funds from the market. The absence of sellers and the availability on one or two days of bid quotations only,may have been indicative of such a development.

At the end of the second week of March, rates began to ease off as lenders reappeared in the market.

The rise in Euro-dollar rates has had some repercussions in foreign exchange markets. Many borrowers in the Euro-dollar market have apparently been seeking funds elsewhere rather than renew existing credits at the higher rates. In Britain, Switzerland and the Netherlands demands for dollars to repay maturing contracts have added to existing pressures on the exchange rates. In Switzerland, for example, where a very liquid money market had already produced some decline in the Swiss franc rate, these added pressures pushed the rate vis-à-vis the dollar to its lowest point in several years.

Demands for gold in the London gold market reached exceptionally heavy proportions in the first week of March. The continuing debate in Europe about the future of gold and continuing uncertainties about Viet Nam were among the factors behind a further marked rise in the gold price. A peak price of $35.178 was reached on Friday, March 5. Since then, demands have eased off, and the price has fallen sharply to $35.134 on March 17.

Western Europe. The near-term business outlook in several European countries will be vitally affected by important policy decisions that governments must now make. In the United Kingdom, the Budget to be presented on April 6 will indicate how much restraint the Labor Government is prepared to impose to strengthen the external position of the pound. In France, the authorities must make a judgment of whether or not the current decline in economic activity will develop into a full-fledged recession if they take no reflationary measures. In Switzerland, where a surprisingly large popular vote has extended for two years the Government's powers to continue its anti-inflationary program, the Swiss authorities now have to decide what part of their restrictive measures to keep in force. Their problems have been aggravated by the decision--made for domestic political reasons--to reduce the supply of foreign labor in Switzerland, despite the prevailing labor scarcity.

United Kingdom. In the United Kingdom, a judgment about how restrictive the budget for the year beginning April 1 should be depends chiefly on an assessment of how effective the measures already taken in the past six months have been, and are going to be, in restraining aggregate domestic demand this year. In the "little budget" of November 11, announcement was made of increases in the basic income tax rate and in social insurance contributions, and unspecified changes in the corporation and capital gains taxes, all to take effect with the regular April budget. Since the turn of the year bank credit has been in short supply primarily because of the heavy first quarter flow of tax funds to the Treasury and in some measure because of the selective squeeze on bank loans requested by the Bank of England last December. Bank advances, seasonally adjusted, fell sharply in January, and continued to fall in February.

Thus far there is little evidence of any slackening of demand pressures in the economy. Consumer demand appears to be growing steadily; from late 1963 to late 1964 the real volume of consumption expenditures rose by 3.3 per cent, slightly more than real disposable income. And since October retail sales have increased somewhat faster than earlier in 1964. This year consumer expenditures are expected to continue rising, in part because the increase in social insurance payments to take effect in April will tend to increase the spending power of lower income groups.

Data on private investment as yet show no signs of being affected by recent restrictive measures. Between October 1964 and January 1965 there was little change in investment plans as shown by surveys of investment intentions undertaken by the Board of Trade. Both surveys suggested a rise of 10 per cent in capital expenditures by manufacturing industries for 1965 as compared with 1964. However, because of the steep rise of these expenditures during 1964--a 15 per cent rise was recorded between the end of 1963 and the end of 1964--the change from the rate in the fourth quarter 1964 to fourth quarter 1965 would be substantially less than 10 per cent.

There have been some indications of slackening of inventory investment, but this may have affected mainly imported materials. The industrial production index is not available beyond December.

Exports appear to be trending up: the fourth quarter (1964) showed a good increase from previous months, and February exports (after a decline in January) were again on the uptrend. Imports, on the other hand, have been declining since December 1964, in part probably because of the import surcharge but in February also because of the U.S. dock strike.

Thus, the composite picture in Britain appears to be one of further expansion of aggregate demand. This has been accompanied by a rising rate of capacity utilization and a continuing tightening of the labor market. Accordingly, some observers have been urging the Government to put forward a budget restrictive enough to hold down final demand and to help bring the U.K. balance of payments into equilibrium by 1966. For example, the National Institute of Economic and Social Research has estimated that an improvement of about £300 million in the United Kingdom balance of payments will be required from 1965 to 1966: £100 million might be obtained by measures to cut overseas Government expenditure and private investment flows, but £200 million would have to be found through an adjustment in home demand.

A second school suggests that the tax increases announced in November 1964, the 7 per cent Bank rate, and the credit squeeze are likely to have an appreciable effect on output later in the year. These observers fear that a budget with additional tax increases or heavy cuts in Government expenditure, coming on top of these earlier measures, would generate the "stop" phase of another "stop-go" cycle.

Within the Government, opinions are divided. The Minister of Economic Affairs, George Brown, has gone on record that the restrictive actions taken or announced so far will provide sufficient domestic resources for the needed growth in exports (or displacement of imports); on the other hand, Chancellor of the Exchequer Callaghan is known to lean more in the direction of some additional restraint on home consumption.

France. The de Gaulle Government is being pressed to reverse its anti-inflationary program. There is definitely a slowdown in business activity. Private demand slackened during 1964, and industrial output (seasonally adjusted) in December 1964 was at the same level as in December 1963, and 2 per cent below September 1964. Private industrial investment in plant and equipment may have been 5 per cent smaller in real terms in 1964 than in 1963; it is expected to decline further in 1965, by 2 to 7 per cent.

The latest industry surveys conducted by the Institut National de la Statistique et des Etudes Economiques in December and January showed a widespread deterioration in business confidence: increasingly larger numbers of respondents judged their inventory levels too high, their order books unsatisfactory, and the expected trend for production in the next three months as downwards.

Unemployment (after seasonal adjustment) has risen steadily since mid-1964, and in January was 30 per cent above the preceding year's level. Job vacancies also declined fairly steadily, and in January were nearly 50 per cent below their year-earlier level. Despite the slowdown in business activity, however, hourly wage rates have continued to rise rapidly, and in the latter part of 1964 were increasing at an annual rate of about 6 per cent.

Partly because of the continued increase in wage rates, France's Finance Minister Giscard d'Estaing is strongly opposing any relaxation of the restrictive policies at this time.

Some measures to stimulate investment are in the offing, however, according to a speech last week by Prime Minister Pompidou.

It is not clear whether these will be long-term measures aimed at stimulating investment and encouraging business concentration (sought by the Finance Minister) or whether they will be designed for short-term expansion. Most observers think that a cut in the corporate tax will be the most likely measure to be taken. So far, the Government has continued to hold to its basic goal of price stability, and it has made only small moves towards relaxing the price freeze instituted in September 1963: manufacturers may raise the selling prices of some of their products provided they reduce prices for others.

France's external position has continued to improve in recent months. In January-February official reserves increased by $155 million, as compared with a rise of $46 million in the corresponding period of 1964. Exports rose during the latter part of 1964 and this uptrend may have carried into early 1965. Imports, on the other hand, are no longer growing as rapidly as in October-November, 1964, if at all. Consequently, the trade deficit with the non-franc area in January-February was some 30 per cent less than a year earlier.

Switzerland. In last month's referendum, the Swiss Federal Government received the votes it required to continue in effect for two years the anti-inflationary measures taken last year under emergency authorization, which had been due to expire in March.

An unexpectedly large number of voters--60 per cent of the registered voting population--approved by comfortable majorities the Government's anti-inflation program. The authorities now have the option to keep in force the measures designed to keep out foreign funds, to limit credit expansion, and to control the expansion of private and public construction.

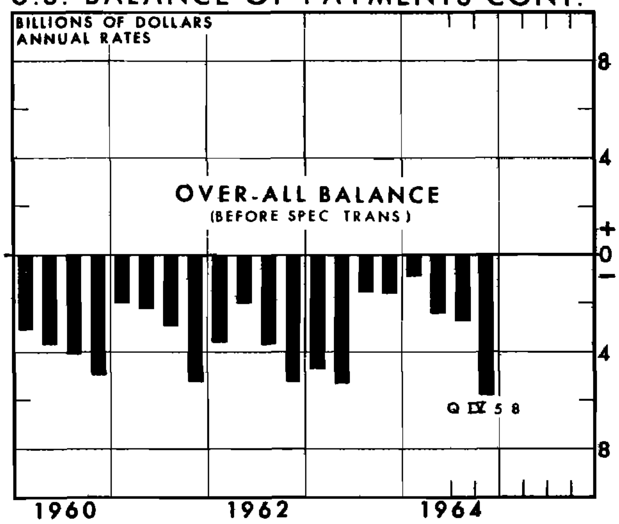
Even after ten months of efforts to restrain inflationary pressures, however, the pressures remain relatively strong. Investment in plant and equipment continues at a high rate, partly stimulated by the increasingly tight labor situation. While direct controls have cut into building demand since May 1964, pressures on construction capacity are continuing.

But the authorities' restrictive efforts are beginning to show some effect: consumer demand is no longer expanding as fast as in previous months and a downturn in exports has become apparent recently. In this situation, the authorities have decided to reduce the number of foreign workers in Switzerland, despite current pressures on resources. The 770,000 foreign workers constitute approximately 25 per cent of the Swiss labor force. In two executive orders, the authorities have closed the border to foreign labor entering without a signed labor contract, and are requiring all Swiss companies to reduce their foreign work force by 5 per cent by June 30, 1965, and by another 5 per cent in the following twelve months.

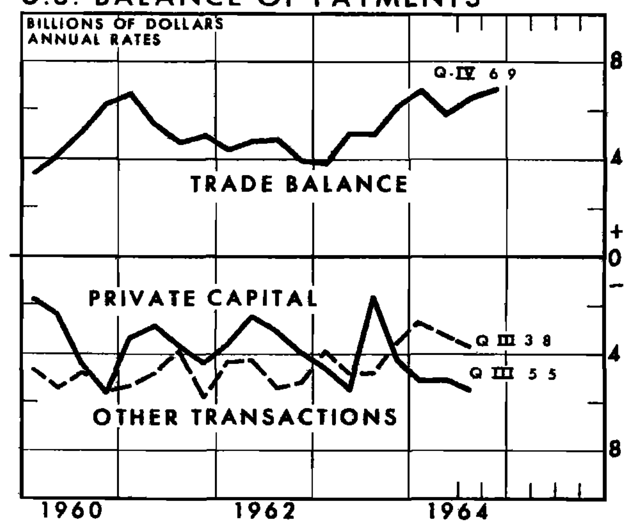
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED

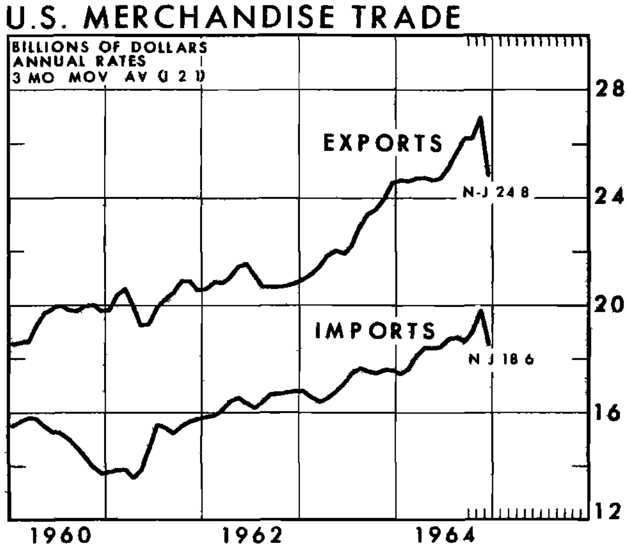
U.S. BALANCE OF PAYMENTS-CONT.



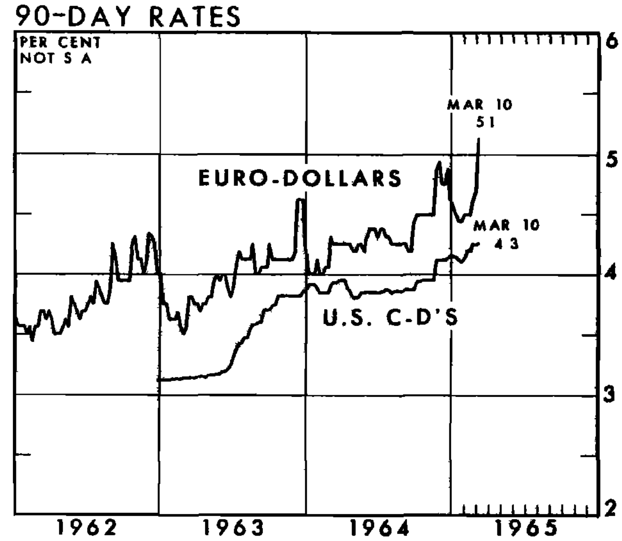
U.S. BALANCE OF PAYMENTS



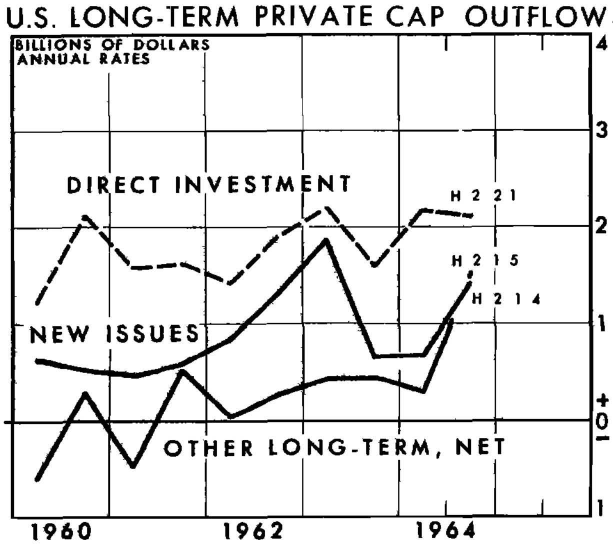
U.S. MERCHANDISE TRADE



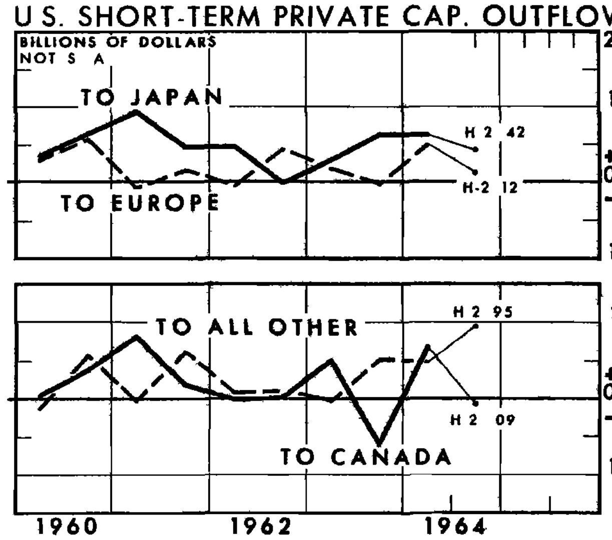
90-DAY RATES



U.S. LONG-TERM PRIVATE CAP OUTFLOWS



U S. SHORT-TERM PRIVATE CAP. OUTFLOWS



APPENDIX A: PROPOSED MAJOR HOUSING LEGISLATION

The proposed "Housing and Urban Development Act of 1965" was presented to the Congress on March 4 and will soon be followed by a bill for a cabinet-level Department of Housing and Urban Development, mentioned March 2 in the President's message on cities.

The President's message outlined some of the problems associated with the anticipated growth of urban areas and many of the provisions in the housing bill intended to alleviate these problems. As in the Housing Act of 1964, numerous features of the present proposal, if enacted, would have an impact, albeit often delayed, on new construction, capital markets, and existing real estate facilities, through the extension, liberalization, or initiation of a variety of urban and rural programs. Unlike last year's legislation, there are no provisions this time for further broad liberalization in the investment powers of either national banks or savings and loan associations.

For major existing programs, the bill includes authorizations over a 4-year period totaling: (a) $2.9 billion additional for urban renewal; (b) $188 million additional in annual grants for the construction of some 140,000 new units of low-rent public housing and for the purchase or leasing of 100,000 existing dwellings; (c) over $2.3 billion additional for special-assistance purchase by the Federal National Mortgage Association with Treasury-borrowed funds of certain FHA and VA mortgages, including proposed FHA-insured land development loans; and (d) $955 million additional for low-cost college housing loans.

Some major new programs would include: (a) $200 million yearly by fiscal 1969 for annual grants payable by the Federal Housing Administration to certain private landlords to subsidize the rents of qualified lower-income tenants in up to 500,000 new dwellings; (b) FHA insurance of first mortgages of up to $25 million each to help finance larger-scale private land development primarily for residential sites, related uses, or public facilities; and (c) matching grants to certain public agencies for designated public works, neighborhood facilities, advance land acquisition, and urban beautification and improvement.

The precise cost of this year's bill is more difficult to estimate than usual, in part because existing statutory ceilings on some programs would be eliminated. Through the fiscal year 1969 only, the bill would provide new obligational authority for major programs of nearly $3.3 billion in grants and $3.3 billion in loans. Most new authorizations as well as disbursements would come one or more years after enactment. Through the fiscal year 1966, for example, the bill would provide grant authorizations of $772 million and loan authorizations of $260 million. Full payments, of course, could be delayed for some time beyond this date, pending the writing of new regulations, development of local plans, or Federal approval of local grant or loan applications.

APPENDIX B: LABOR FORCE PROJECTIONS TO 1960

The Bureau of Labor Statistics recently has issued a new set of labor force projections which supersede the projections published in 1962. For 1970, the new projection is 300,000 higher than previously estimated, mainly because of upward revisions in participation rates of females. Lower revised population projections, however, partly offset the upward revisions in participation rates. The new estimates call for an 83.3 million civilian labor force in 1970, or 9 million more than in 1964. The average annual growth in the labor force between 1964 and 1970 is projected at 1.5 million, or 1.8 per cent, per year, which compares with actual annual increases averaging less than 1 million since 1960. The faster growth anticipated in the labor force in part reflects the first influx of postwar babies who are now reaching working ages.

Employment will thus need to expand by 9 million in the six-year period just to keep pace with labor force growth and to prevent unemployment from rising above the 1964 level. To bring the unemployment rate down to 4 per cent by 1970, employment would have to grow by 1.6 million per year. By comparison, employment increases since 1960 have averaged about 1 million per year, although in 1964 employment expanded by 1.5 million.

The output requirements to attain relative full-employment are quite large. Assuming a continuation of the postwar rate of increase in productivity, and further assuming that the workweek will remain relatively stable, BLS estimates that real GNP will have to expand by 4-3/4 per cent annually in order to employ 96 per cent of the projected civilian labor force by 1970. A 4-3/4 per cent rate of increase in real GNP was achieved in 1964 but the postwar average was 3-1/2 per cent.

The projected composition of the labor force in 1970 suggests that demands for labor will also have to depart from past trends in order to minimize unemployment. Nearly half of the anticipated growth in the labor force will be among young persons age 14 to 24. Provided enough jobs become available, there may be 1.5 million more teenagers and 2.75 million more 20-24 year-olds in 1970 than in 1964. The number of workers under 25 years of age would total over 20 million in 1970 and would amount to 23.6 per cent of the labor force compared to 20.7 per cent in 1964. To absorb the rising tide of young males in the labor force, a continued strong expansion in the goods sector and in blue-collar occupations, which normally employ a substantial share of these young workers, would presumably be needed. Official projections of job opportunities, however, indicate that employment growth in these areas may continue to expand at a slower than average rate in the years ahead.

AVERAGE ANNUAL CHANGE IN LABOR FORCE
1960-1970

Sex and age	Actual change 1960-64		Projected change 1964-70	
	Number	Per cent	Number	Per cent
Males	390	0.8	787	1.5
14-19 years	129	3.4	142	3.3
20-24 years	186	3.8	297	5.2
25-54 years	73	0.2	244	0.8
55 years and over	2	0.0	103	1.2
Females	593	2.5	711	2.7
14-19 years	76	3.2	116	4.3
20-24 years	167	6.5	174	5.4
25-54 years	222	1.5	267	1.7
55 years and over	129	3.3	154	3.5

Growth in the labor force of women workers 25 and over is also expected to be slightly faster than in recent years. This would presume continued job gains in the service, sales, and clerical occupations where women are traditionally employed. With more women and youths coming into the labor force, competition for jobs may be more intense both among youths and older women. Many of these workers will be seeking part-time employment.

The labor force of men 25 years and over will also rise more rapidly between 1964 and 1970 than in recent years. Their labor force is expected to grow by 2 million by 1970, accounting for nearly one-fourth of the increase in the total labor force. The labor force of older workers, age 65 and over is expected to grow little as their participation rate continues its long-term down-trend. The participation rate of 60-64 year-old men is also expected to decline further as the result of a sharp increase in early retirement plans and the lowering of the retirement age in the social security law.