

Prefatory Note

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

Please note that some material may have been redacted from this document if that material was received on a confidential basis. Redacted material is indicated by occasional gaps in the text or by gray boxes around non-text content. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

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

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

CONFIDENTIAL (FR)

CURRENT ECONOMIC and FINANCIAL CONDITIONS

**Prepared for the
Federal Open Market Committee**

By the Staff

**BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM**

March 26, 1969

CONFIDENTIAL (FR)

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

March 26, 1969

SUMMARY AND OUTLOOK

Outlook for economic activity

Increases in GNP in the first and successive quarters are likely to be larger than we had earlier anticipated, but the rate of real GNP growth is still expected to be somewhat slower than in the fourth quarter of 1968. Growth of real GNP should dip from the 3.4 per cent rate of the fourth quarter of 1968 to about 2.5 per cent by midyear. The prospect, however, is for little easing of price pressures.

Views on the economic outlook have been strengthened by the survey results indicating business plans to accelerate expenditures for plant and equipment. These heightened expectations are being confirmed, at least for the short run, by the rise in new orders for durable goods and increased output of business equipment. In addition, a somewhat stronger pattern of consumer expenditures this quarter has emerged after the recent revision in the seasonal adjustment factors for the retail sales figures. The trend of retail sales, excluding autos, appears to be stronger while auto sales are weaker this quarter.

Much of the impact of the 14 per cent pick-up in capital expenditures now projected by businessmen for this year is concentrated in the current quarter, to be followed by a dip in the second quarter and moderate increases for the remainder of the year. We are doubtful that all of this increase will be realized, either in the first quarter--when physical limitations are a factor--or later in the year, when

financial constraints may force stretch-outs in spending plans. For the year as a whole, the staff projection shows a rise in business fixed investment of 12 per cent. Also the increasing pressure from monetary restraint should begin to cut significantly into building activity before long, with housing starts probably easing by the next quarter.

The growth of disposable income is being reduced this quarter by higher social security taxes, and the rise in consumption is apparently being supported in significant part by a sharp cut in the savings rate. Since unusually large income tax payments will continue to dampen growth of disposable income through midyear, and with the saving rate apparently at a relatively low level and not expected to fall further, a slower rate of growth of consumption still seems likely in the upcoming quarter.

Outlook for prices and resource use

Industrial prices at wholesale rose an estimated 0.4 per cent from mid-February to mid-March; the January-to-February increase was revised up to 0.5 per cent; and the January rise holds at 0.6 per cent. Thus, for the first three months of this year industrial prices were rising at an exceptionally rapid 6 per cent annual rate. Lumber and plywood continued to bulk large in the overall rise-- accounting, for the three months, for almost a third of the total increase. Prices of metals, petroleum and products, and machinery and equipment have also increased sharply.

Lumber and plywood prices, now up 40 per cent from a year ago and nearly 60 per cent from early 1967, are vulnerable to any significant shifts in the supply-demand balance and perhaps also to the belated outcry over the extraordinary price run-up of the past 2 years. Excluding lumber and plywood, industrial prices have been increasing this year at the high annual rate of nearly 4-1/2 per cent and the diffusion of increases has been unusually widespread. Continued strong demands from the construction and producers' equipment sectors are likely to exert a continuing upward pull on prices, and upward pressure from the labor cost side appears likely to continue quite strong in the coming quarter.

The consumer price index continued to rise in February at about the 4-1/2 per cent annual rate of the past year. Food prices leveled off, in line with longer-run expectations, but the price increase for non-food commodities showed a step-up from recent moderate rates. The increase in service prices in February was at a 6 per cent annual rate--little changed from increases prevailing over the past year--with boosts in housing costs and medical care again prominent and, within the housing sector, higher conventional mortgage interest rates augmenting the rise. Excluding mortgage interest rates--with their heavy weight in the CPI--the consumer price rise may slow somewhat if food prices continue to show little change.

The expansion in industrial production thus far in 1969 has been considerably slower than in the late months of 1968, in part because of a slower rise in total output of consumer goods. The rate of manufacturing capacity utilization has drifted off slightly to about 84 per cent.

Employment increased sharply in January and February, with the emphasis on non-manufacturing activities. Employment demands might ease in the second quarter, especially if industrial production continues to rise only slowly, and the unemployment rate is expected to rise slightly.

Outlook for credit demands

Demand for business loans from banks is expected to continue strong over the next several weeks, influenced in part by large corporate tax payments to be made in April. The further rise in the prime rate in mid-March is likely to be a marginal factor, however, in dampening demands on banks, and may induce businesses to divert some additional short-term borrowing to the commercial paper market, where borrowing costs are somewhat less expensive.

There is also likely to be some increase in corporate bond offerings during the spring, reflecting rising outlays for plant and equipment, a widening gap of corporate financing needs over internal sources of funds, recent erosion in corporate liquidity, and continued constraints on bank credit availability. Many bond offerings may continue to contain equity features to increase the attractiveness of the security and to reduce interest costs.

In the municipal market, offerings of new issues are likely to remain modest, though rising from the exceptionally low March volume. Some prospective issues are likely to be postponed at current interest costs, but, on the other hand, adjustment of State interest rate ceilings will permit some borrowers to enter the market who would otherwise be blocked out.

Around the end of April, the U.S. Treasury will announce terms for refunding almost \$4 billion of publicly-held coupon securities maturing in mid-May. The Treasury could also include the over \$2 billion of publicly-held bonds maturing in mid-June in the package. It is too early to have a clear notion as to the nature of the Treasury exchange offering and whether they will make use of the large second quarter budget surplus to redeem some coupon debt as well as bill issues.

With the Treasury's net cash needs now behind and debt repayment in prospect, the principal sources of upward interest rate pressure from the demand side are likely to be from corporations and in the mortgage area. These demands may be strong enough to lead to some further upward interest rate movement in long-term markets as a whole, or at least would tend to forestall a sustained downward movement. A factor that could ease long-term rate pressures as the spring progresses would be a continued downward drift in Treasury bill yields, since that might permit banks to maintain security portfolios as CD's became more competitive.

Outlook for supply of funds

The outlook for the supply of funds through banks and other financial institutions to the business loan, State and local Government, and mortgage markets will depend very much on the extent to which prospective Treasury debt repayment leads to lower market interest rates, particularly in the short-term area. Assuming that short-term rates at least do not rise much from current levels, the run-off of large CD's at banks may slow somewhat in spring (after adjustment for April tax period seasonal declines). Not only are amounts maturing declining, but also banks may be able to take advantage of the reduced availability of Treasury bills to market relatively more CD's than has been the case in recent months. With respect to demand deposits, private deposits will be affected by continued pressure on businesses to economize on cash balances to help finance current outlays, given bank loan policies and high market interest rates. April tax payments and the recent bill financing will also tend to drain private demand deposits.

Consumer-type time and savings deposits are likely to be withdrawn in some volume from banks in early April (after the March interest-crediting), to be invested in high yielding market securities. But if recent experience is any guide, these deposits are likely to resume a moderate growth trend in subsequent weeks. However, banks will face somewhat more competition from savings and loan associations for such deposits, since associations (effective April 1) can now issue 90-day notice accounts at the same ceiling rate as has applied to commercial banks.

While this new account will provide S&L's with a little more ammunition, net inflows of funds to them are still expected to be further constricted in the coming March-April reinvestment period and possibly in subsequent weeks. Current market interest rates are relatively attractive, although it is not clear to what extent savings deposits would substitute for long-term bonds, which have shown the greatest yield increase in recent months. In addition, thrift institutions, as well as banks, may be affected by withdrawals by individuals to finance large April tax payments.

In view of these inflow prospects, new mortgage commitments by thrift institutions may be cut back, and mortgage yields should continue upwards. To meet outstanding commitments, thrift institutions will probably have to reduce liquid assets further and S&L's will have to increase their borrowing from the Home Loan Banks. FNMA is expected to continue its support of Government-underwritten mortgages at its current pace, but this will tend only to modify mortgage market pressure somewhat and will over time require sizable marketing of new FNMA debt issues.

Balance of payments outlook

It seems improbable that the deficit on the liquidity basis will continue during the second quarter at the extremely high rate experienced in the first 2-1/2 months of the year. However, in the absence of an adequate explanation of recent large monthly deficits,

prediction is hazardous. Possibly the net balance on goods and services will prove to have been negative in the first quarter, as a result of more rapid catching up in the flow of imports than in exports after the ending of the longshoremen's strike last month at most ports. If so, before long we should be seeing a swing toward a smaller rate of over-all deficit as exports catch up.

Guesses that have been made as to the magnitude of the port strike impact on the first-quarter deficit are not large enough to explain even half of the liquidity deficit in this period, which is currently estimated in the \$1-1/2 to 2 billion (per quarter) range. As foreign purchases of U.S. corporate stocks appear to have continued on a large scale in January and February, and as U.S. bank credit reflows have been at least as large as at this time a year ago, it seems possible that U.S. corporations have been taking advantage of the large leeways many have under the direct investment controls to place funds abroad with their subsidiaries. Conceivably this in turn may help to some extent to explain the success U.S. banks have been having during March in bidding for fresh Euro-dollar money.

SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally adjusted)

	Latest Period	Amount			Per Cent Change	
		Latest Period	Preced'g Period	Year Ago	Year Ago*	2 Yrs. Ago*
Civilian labor force (mil.)	Feb '69	80.4	79.9	78.6	2.3	4.5
Unemployment (mil.)	"	2.6	2.6	2.9	-10.3	-7.9
Unemployment (per cent)	"	3.3	3.3	3.7	--	--
Nonfarm employment, payroll (mil.)	"	70.0	69.6	67.6	3.5	6.6
Manufacturing	"	20.1	20.0	19.6	2.3	2.5
Other industrial	"	8.5	8.4	8.3	2.5	4.4
Nonindustrial	"	41.4	41.2	39.7	4.4	9.2
Industrial production (57-59=100)	"	169.5	169.1	162.0	4.6	8.2
Final products	"	169.4	168.1	162.0	4.6	7.9
Materials	"	169.1	169.4	161.8	4.5	8.3
Wholesale prices (57-59=100) ^{1/}	"	111.1	110.7	108.0	2.9	4.8
Industrial commodities (FR)	"	110.4	109.9	107.6	2.6	5.0
Sensitive materials (FR)	"	114.4	112.4	107.1	6.8	12.3
Farm products, foods & feeds	"	110.0	109.8	106.8	3.0	4.1
Consumer prices (57-59=100) ^{1/}	"	124.6	124.1	119.0	4.7	8.5
Commodities except food	"	115.7	115.0	111.5	3.8	7.5
Food	"	121.9	122.0	117.4	3.8	6.7
Services	"	139.7	139.0	131.3	6.4	11.0
Hourly earnings, mfg. (\$)	"	3.11	3.11	2.93	6.1	11.9
Weekly earnings, mfg. (\$)	"	126.24	126.43	119.84	5.3	12.4
Personal income (\$ bil.) ^{2/}	"	721.4	716.1	663.0	8.8	17.4
Corporate profits before tax (\$ bil.) ^{2/}	QIV '68	95.8	92.7	85.4	12.2	12.7
Retail sales, total (\$ bil.)	Feb '69	29.0	29.0	27.4	5.7	13.9
Autos (million units) ^{2/}	"	8.7	8.2	7.9	10.6	29.9
GAF (\$ bil.)	"	7.8	7.6	7.3	7.1	17.3
Selected leading indicators:						
Housing starts, pvt. (thous.) ^{2/}	"	1,700	1,842	1,537	10.6	48.0
Factory workweek (hours)	"	40.5	40.6	40.8	-0.7	0.5
New orders, dur. goods (\$ bil.)	"	30.7	29.7	26.8	14.3	27.0
New orders, nonel. mach. (\$ bil.)	"	5.4	5.4	4.5	18.6	30.3
Common stock prices (1941-43=10)	"	101.46	102.04	90.75	11.8	16.1
Inventories, book val. (\$ bil.)	Jan '69	154.1	153.9	144.1	7.0	11.5
Gross national product (\$ bil.) ^{2/}	QIV '68	887.4	871.0	811.0	9.4	15.5
Real GNP (\$ bil., 1958 prices) ^{2/}	"	718.4	712.3	681.8	5.4	7.7

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

SELECTED DOMESTIC FINANCIAL DATA

	Week ended	4-week	Last 6 months	
	March 22	average	High	Low
Money Market <u>1/</u> (N.S.A.)				
Federal funds rate (per cent) <u>9/</u>	6.85	6.68	6.85	5.08
U.S. Treas. bills, 3-mo., yield (per cent)	6.00	6.06	6.22	5.12
U.S. Treas. bills, 1-yr., yield (per cent)	6.17	6.25	6.38	5.15
Net free reserves <u>2/</u> (\$ millions)	-719	-637	- 52	-719
Member bank borrowings <u>2/</u> (\$ millions)	775	785	1,320	337
Capital Market (N.S.A.)				
Market yields (per cent)				
5-year U.S. Treas. bonds <u>1/</u>	6.42	6.42	6.44	5.45
20-year U.S. Treas. bonds <u>1/</u>	6.27	6.21	6.27	5.25
Corporate new bond issues, Aaa adj. <u>8/</u>	7.57	7.25	7.57	6.24
Corporate seasoned bonds, Aaa <u>1/</u>	6.94	6.77	6.94	6.00
Municipal seasoned bonds, Aaa <u>1/</u>	5.02	4.91	5.02	4.20
FHA home mortgages, 30-year <u>3/</u>	--	7.99	7.99	7.28
Common stocks, S&P composite series <u>4/</u>				
Prices, closing (1941-43=10)	99.63	98.60	108.37	98.00
Dividend yield (per cent)	3.17	3.19	3.21	2.87

	Latest month	Amount	3-month average	Change from	
				year earlier	Latest 3-month month average
New Security Issues (N.S.A., \$ millions)					
Corporate public offerings <u>5/</u>	Apr. <u>e/</u>	1,400	1,361	408	288
State & local govt. offerings	Apr. <u>e/</u>	750	767	-568	-526
Comm. & fin. co. paper (net change in outstandings) <u>6/</u>	Feb. '69	+1,052	+215	+1,609	+399

	Latest month	Out-standings Latest month	Change Latest month	3-month average	Annual rate of change from		
					Pre-ceding month	3 months ago	12 months ago
Banking (S.A.)							
(\$ billions)							
Total reserves <u>1/</u>	Feb. '69	27.18	-0.01	0.15	-0.6	6.7	5.5
Credit proxy <u>1/</u> <u>10/</u>	"	294.8	-0.3	0.5	-1.2	2.2	6.6
Bank credit, total <u>6/</u>	"	386.7	1.4	1.7	4.4	5.3	9.3
Business loans	"	97.7	1.2	1.1	14.9	14.4	12.2
Other loans	"	160.2	2.9	1.4	22.1	10.5	12.7
U.S. Govt. sec.	"	57.8	-2.6	-1.1	-51.7	-21.0	-6.8
Other securities	"	--	--	0.3	--	4.6	13.2
Total liquid assets <u>1/</u> <u>6/</u>	"	704.6	-1.1	2.2	-1.9	3.8	6.6
Demand dep. & currency <u>1/</u>	"	193.8	0.2	0.6	1.2	4.0	6.1
Time & sav. dep., comm. banks <u>1/</u>	"	201.0	-1.5	-0.3	-8.9	-1.8	8.5
Savings, other thrift instit. <u>6/</u>	"	197.0	1.2	0.6	7.3	3.9	6.1
Other <u>6/</u> <u>7/</u>	"	112.8	-1.0	1.2	-10.5	13.6	5.2

N.S.A. -- not seasonally adjusted.

S.A. -- Seasonally adjusted.

e. Estimated by F.R.B. 1/ Average of daily figures. 2/ Average for statement week ending March 19. 3/ Latest figure is monthly average for Feb. 4/ End of week closing prices; yields are for Friday. 5/ Corporate security offerings include both bonds and stocks. 6/ Month-end data. 7/ U.S. savings bonds and U.S. Government securities maturing within 1 year. 8/ Adjusted to Aaa basis. 9/ Federal funds data are 7-day averages for week ending Sunday; latest figure is for week ending March 23. 10/ Reflects \$400 million reduction in member bank deposits resulting from withdrawal of a large country bank from System membership. Percentage annual rates are adjusted to eliminate this break in series.

U.S. BALANCE OF PAYMENTS
 (In millions of dollars)

	1967	1968				1969		
	Year	Year ^P	I ^r	II ^r	III ^r	IV ^P	Jan. ^P	Feb. ^P
	Seasonally adjusted							
Goods and services, net <u>1/</u>	4,769	1,965	298	622	854	193		
Trade balance <u>2/</u>	3,477	103	35	44	243	-219	10	
Exports <u>2/</u>	30,468	33,376	7,914	8,379	8,835	8,248	1,980	
Imports <u>2/</u>	-26,991	-33,273	-7,879	-8,335	-8,592	-8,467	-1,970	
Service balance	1,292	1,864	263	578	611	412		
Remittances and pensions	-1,275	-1,159	-266	-286	-315	-293		
Govt. grants & capital <u>3/</u>	-4,211	-3,977*	-1,164	-1,072	-938	-803*		
U.S. private capital	-5,505	-4,860*	-707	-1,448	-1,798	-908*		
Direct investment	-3,021	-2,743*	-374	-1,035	-1,168	-167*		
Foreign securities	-1,266	-1,288	-385	-83	-323	-497	-15 ^r **	
Banking claims	-459	254	303	196	-200	-45	384**	
Other	-759	-1,083	-251	-526	-107	-199		
Foreign capital, nonliquid	3,186	8,384	1,410	2,485	1,833	2,656		
Official foreign accounts	1,293	2,448	334	928	437	749		
Long-term deposits	839	524	122	148	129	125	5**	-19**
U.S. Govt. liabilities	454	1,924	212	780	308	624	133**	5**
International and regional organizations <u>4/</u>	299	159	-98	-19	56	220	89**	31**
Other <u>5/</u>	1,594	5,777	1,174	1,576	1,340	1,687		
Errors and omissions	-535	-195	-276	-483	419	145		
	Balances, with and without seasonal adjustment (- deficit)							
Liquidity balance, S.A.			-705	-182	55	990		
Seasonal component			443	255	-488	-210		
Balance, N.S.A.	-3,571	158	-262	73	-433	780	-270	-544
Official settlements bal., S.A.			-571	1,509	423	256		
Seasonal component			661	54	-350	-365		
Balance, N.S.A. <u>6/</u>	-3,405	1,617	90	1,563	73	-109	1,358	
	Reserve changes, N.S.A. (decrease -)							
Total monetary reserves	-52	880	-904	137	571	1,076	-256	45
Gold stock	-1,170	-1,173	-1,362	-22	74	137	-64	-27
Convertible currencies	1,024	1,183	401	-267	474	575	-190	61
IMF gold tranche	94	870	57	426	23	364	-2	11

1/ Equals "net exports" in the GNP, except for latest revisions.

2/ Balance of payments basis which differs a little from Census basis.

3/ Net of scheduled and non-scheduled repayments.

4/ Long-term deposits and Agency securities.

5/ Includes some foreign official transactions in securities.

6/ Differs from liquidity balance by counting as receipts (+) increase in liquid liabilities to commercial banks, private nonbanks, and international institutions (except IMF) and by not counting as receipts (+) increases in certain nonliquid liabilities to foreign official institutions.

* Data for 1968 marked (*) strictly confidential until released by the Commerce Dept.

** Not seasonally adjusted.

Note. Details may not add because of rounding.

THE ECONOMIC PICTURE IN DETAIL

The Nonfinancial Scene

Gross national product. Overall activity appears likely to be stronger this quarter and for the remainder of 1969 than we had anticipated earlier, although real growth is still expected to be somewhat below the fourth quarter 1968 rate. The major factor is the upward adjustment in planned spending by business for plant and equipment, especially in the first quarter. A larger-than-expected recovery in consumer spending from the weak yearend rate also has added to the firming of the economic outlook. With final sales up sharply, the inventory position of business has apparently improved and a lower rate of inventory accumulation now seems likely this quarter. The increase in current dollar GNP is now expected to total about \$15 billion this quarter, and with price increases continuing strong, the growth of real GNP should edge down to under a 3 per cent annual rate.

In the second quarter, the GNP increase in both dollar and real terms has been revised up to about the first quarter rate of growth, although easing should become apparent in several sectors. A smaller gain in business spending for fixed capital is called for after the first quarter, the rise in consumption is likely to slow somewhat in the upcoming period with only a relatively moderate increase anticipated in disposable income, and residential construction activity is expected to turn downward as the tightening monetary conditions of recent months begin to take effect. However, inventory accumulation is

not expected to decline further. The easing indicated in these areas of final sales will probably be offset in part by a sharp rebound of exports following settlement of the protracted dock strike.

The sharp upward adjustment in anticipated expenditures for business fixed investment reported in the February Commerce-SEC survey appears to be generally confirmed by increased new orders for durable goods and rising output in the machinery and equipment sectors. However, the \$5.8 billion increase in fixed capital outlays indicated for the current quarter seems excessively large in comparison with recently achieved quarterly gains. Typically in recent quarters, actual increases in business spending have fallen \$1 to \$2 billion behind anticipated levels, and we have assumed a similar shortfall this quarter, with the remainder carried over as a small increase in the second quarter rather than the dip indicated in the survey.

Our projections of consumption expenditures for the first quarter has been increased also, reflecting mainly recently revised retail sales figures. The new sales figures--the result of a revision of the seasonal adjustment factors--indicate that January and February sales had risen more from the fourth quarter than had been shown earlier. Consumer spending is now expected to rise by about \$10 billion this quarter. With the rise in disposable income sharply curtailed by higher social security taxes, the indicated gain in consumption is associated with a marked drop in the savings rate from 6.8 to 6.0 per cent, the lowest level for the figure since early 1966.

The consumption picture remains mixed in a number of respects. Total retail sales in February were only slightly higher than the 1968 high in September, but exclusive of autos, retail sales were up appreciably since then. Unit auto sales for the first 20 days of March suggest another dip after the February recovery; sales of domestic cars for the quarter should average about 8.5 million units, down from 8.8 million in the fourth quarter of 1968. In addition, sales of foreign cars have been curtailed by the dock strike. But sales of furniture and appliances, which had been tending down for several months, rebounded early in the year, and the nondurables goods group showed some recovery from its weak end-of-year performance.

We anticipate that consumer spending will rise somewhat less in the second quarter than in the first. Retroactive tax payments will continue to dampen gains in disposable income, so that even the smaller rise in consumption projected assumes a continuation of the relatively low first quarter saving rate. Little further change in unit auto sales is expected and gains in furniture and appliance sales are likely to be more moderate.

Residential construction activity thus far has remained a source of strength in the economy, with private housing starts expected to exceed a 1.7 million annual rate in the current quarter, up about 120,000 from the fourth quarter of last year. But the current level of starts probably involves some borrowing from the future, and mortgage funds have become increasingly scarce. Thus, a dip in housing starts is

still anticipated for the next quarter, though construction outlays-- which lag starts--are likely to decline only modestly.

A slower rate of inventory accumulation is indicated in this period following last quarter's rather high rate, apparently reflecting the greater-than-expected strength in final demands in conjunction with some moderation in the rise in industrial output. As a result, businessmen would appear to have less incentive to trim inventories significantly further, and we have projected little change in the rate of accumulation in the second quarter.

Quarterly changes in GNP are being affected substantially by erratic movements in net exports, reflecting the effects of the dock strike. Net exports were reduced significantly to \$1 billion in the fourth quarter of 1968, and were apparently below this low level in the current quarter. But, with the strike now largely over, a rebound is expected at a rate of about \$4-1/2 billion in the second quarter.

Federal purchases of goods and services are expected to be kept generally within budget guidelines, and little increase is likely in the first half of this year. But third quarter outlays will be stepped up, mainly as a result of the pay raise for the military and civilian employees. The budget surplus is expected to drop significantly then, and the impact of fiscal policy on the economy will be somewhat less restrictive, even assuming continuation of the surtax.

Given the same assumptions as to fiscal policy and monetary restraint that underlay the last chart show presentation, we have revised upward the projected increase in GNP for the second half. In significant

measure this reflects upward adjustment of business spending in fixed capital in response to the recent survey findings. Consumption also may be expected to expand moderately faster after midyear as increasing capital expenditures and a somewhat stronger employment picture boost disposable income more than we had projected earlier. The main effects of continued monetary restraint will be reflected in residential construction activity, which is likely to fall significantly in the second half, somewhat smaller increases in State-local capital spending than projected earlier, and some shortfall in business investment below survey findings. (Our current projection shows a year-over-year increase of 12 per cent in such outlays, versus the 13.9 per cent rise indicated by the survey.)

As a result of these changes, GNP should be greater than we had earlier expected--\$925 billion for the year 1969 compared with \$919 billion shown in the previous projection. This sharper expansion in GNP implies a lesser moderation in activities and inflationary pressures than we had hoped for. Real growth would average a little less than the first half year rate of less than 3 per cent. We now think that the unemployment rate will not rise above 4 per cent this year and that the GNP deflator will edge down only to about a 3-1/2 per cent rate of increase by the final quarter of the year.

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income
figures are billions of dollars, with quarterly figures at annual rates)

	1967	1968	1969 Proj.	1968		1969 - Projected			
				III	IV	I	II	III	IV
Gross National Product	789.7	860.6	924.8	871.0	887.4	902.5	917.0	932.5	947.0
Final sales	783.6	852.9	917.7	863.5	876.8	895.1	910.0	925.5	940.0
Private	605.2	655.7	705.4	663.9	673.8	688.6	701.0	710.5	721.5
Personal consumption expenditures	492.2	533.8	570.8	541.1	546.8	556.9	565.0	575.6	585.6
Durable goods	72.6	82.5	87.9	85.1	85.1	86.5	87.0	88.5	89.5
Nondurable goods	215.8	230.3	244.0	232.7	233.7	238.0	241.3	246.0	250.6
Services	203.8	221.0	238.9	223.4	228.0	232.4	236.7	241.1	245.5
Gross private domestic investment	114.3	127.7	138.8	127.1	136.6	138.6	138.4	138.6	139.6
Residential construction	24.6	29.9	31.0	29.5	31.6	32.7	31.9	30.1	29.1
Business fixed investment	83.6	90.0	100.7	90.1	94.3	98.5	99.5	101.5	103.5
Change in business inventories	6.1	7.7	7.1	7.5	10.6	7.4	7.0	7.0	7.0
Nonfarm	5.6	7.3	6.9	7.3	9.7	6.7	7.0	7.0	7.0
Net Exports	4.8	2.0	2.9	3.3	1.0	0.5	4.6	3.3	3.3
Gov't purchases of goods & services	178.4	197.2	212.3	199.6	203.0	206.5	209.0	215.0	218.5
Federal	90.6	100.0	104.1	101.2	101.7	102.5	102.2	105.4	106.0
Defense	72.4	78.9	81.6	79.6	80.0	80.3	80.5	82.7	82.9
Other	18.2	21.1	22.5	21.5	21.7	22.2	21.7	22.7	23.1
State & local	87.8	97.2	108.2	98.4	101.2	104.0	106.8	109.6	112.5
Gross national product in constant (1958) dollars	673.1	706.7	729.5	712.3	718.4	723.2	727.7	731.2	736.1
GNP implicit deflator (1958=100)	117.3	121.8	126.8	122.3	123.5	124.8	126.0	127.5	128.7
Personal income	628.8	685.8	738.9	694.3	708.2	720.5	732.5	745.5	757.0
Wages and salaries	423.4	463.5	502.9	469.0	479.0	489.8	498.5	507.2	516.0
Disposable income	546.3	589.0	624.1	592.7	602.4	608.6	617.7	630.7	639.4
Personal saving	40.2	40.7	38.0	37.1	40.9	36.3	37.6	39.8	38.3
Saving rate (per cent)	7.4	6.9	6.1	6.3	6.8	6.0	6.1	6.3	6.0
Corporate profits before tax	81.6	92.3	94.8	92.7	95.8	93.8	94.3	95.3	95.8
Federal government receipts and expenditures (N.I.A. basis)									
Receipts	151.2	176.9	198.3	182.1	187.1	195.8	198.5	198.3	200.8
Expenditures	163.6	182.2	194.2	184.9	186.9	190.0	191.3	196.9	198.7
Surplus or deficit (-)	-12.4	-5.3	4.1	-2.8	0.2	5.8	7.2	1.4	2.1
Total labor force (millions)	80.8	82.3	84.0	82.4	82.6	83.7	83.9	84.1	84.3
Armed forces "	3.4	3.5	3.5	3.6	3.5	3.5	3.5	3.5	3.5
Civilian labor force "	77.3	78.7	80.5	78.8	79.1	80.2	80.4	80.6	80.8
Unemployment rate (per cent)	3.8	3.6	3.6	3.6	3.4	3.3	3.5	3.7	3.8
Nonfarm payroll employment (millions)	66.0	68.1	70.3	68.3	69.0	69.8	70.1	70.4	70.7
Manufacturing	19.4	19.7	20.0	19.8	19.9	20.1	20.0	19.9	19.9
Industrial production (1957-59=100)	158.1	164.7	171.5	165.2	167.4	169.5	171.2	171.9	173.0
Capacity utilization, manufacturing (per cent)	85.3	84.5	83.3	84.0	84.2	84.0	83.5	83.0	82.6
Housing starts, private (millions A.R.)	1.29	1.51	1.49	1.55	1.60	1.72	1.53	1.35	1.35
Sales new domestic autos (millions, A.R.)	7.57	8.62	8.67	9.01	8.82	8.47	8.50	8.75	8.95

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1967	1968	1969 Proj.	1968		1969 - Projected			
				III	IV	I	II	III	IV
-----In Billions of Dollars-----									
Gross National Product	42.1	70.9	64.2	18.1	16.4	15.1	14.5	15.5	14.5
Inventory change	-8.6	1.6	-0.6	-3.2	3.1	-3.2	-0.4	0.0	0.0
Final sales	50.8	69.3	64.8	21.4	13.3	18.3	14.9	15.5	14.5
Private	28.6	50.5	49.7	17.5	9.9	14.8	12.4	9.5	11.0
Government	22.2	18.8	15.1	3.9	3.4	3.5	2.5	6.0	3.5
GNP in constant (1958) dollars	16.0	33.6	22.8	8.9	6.1	4.8	4.5	3.5	4.9
Final sales	24.0	32.4	24.1	12.0	3.2	8.3	5.1	3.3	4.7
Private	9.8	23.9	19.4	11.1	2.1	6.9	4.5	2.2	3.6
-----In Per Cent Per Year-----									
Gross National Product	5.6	9.0	7.5	8.5	7.5	6.8	6.4	6.8	6.2
Final sales	6.9	8.8	7.6	10.2	6.2	8.3	6.7	6.8	6.3
Private	5.0	8.3	7.6	10.8	6.0	8.8	7.2	5.4	6.2
Personal consumption expenditures	5.7	8.5	6.9	10.0	4.2	7.4	5.8	7.5	6.9
Durable goods	3.0	13.6	6.5	20.2	0.0	6.6	2.3	6.9	4.5
Nondurable goods	4.4	6.7	5.9	7.9	1.7	7.4	5.5	7.8	7.5
Services	8.2	8.4	8.1	8.6	8.2	7.7	7.4	7.4	7.3
Gross private domestic investment	-5.4	11.7	8.7	-0.6	29.9	5.9	-0.6	0.6	2.9
Residential construction	-0.8	21.5	3.7	0.0	28.5	13.9	-9.8	-22.6	-13.3
Business fixed investment	2.8	7.7	11.9	14.3	18.6	17.8	4.1	8.0	7.9
Gov't. purchases of goods & services	14.2	10.5	7.7	8.0	6.8	6.9	4.8	11.5	6.5
Federal	17.1	10.4	4.1	4.8	2.0	3.1	-1.2	12.5	2.3
Defense	19.5	9.0	3.4	3.0	2.0	1.5	1.0	10.9	1.0
Other	8.3	15.9	6.6	9.5	3.7	9.2	-9.0	18.4	7.0
State & local	11.4	10.7	11.3	11.7	11.4	11.1	10.8	10.5	10.6
GNP in constant (1958) dollars	2.4	5.0	3.2	5.0	3.4	2.7	2.6	1.9	2.7
Final sales	3.7	4.9	3.4	6.9	1.8	4.7	2.8	1.8	2.6
Private	1.9	4.5	3.5	8.2 ^{1/}	1.5	4.9	3.2	1.5 ^{2/}	2.5
GNP implicit deflator	3.1	3.8	4.1	3.4 ^{1/}	4.1	4.1	3.9	4.8 ^{2/}	3.5
Personal income	7.2	9.1	7.7	9.6	8.0	6.9	6.7	7.1	6.2
Wages and salaries	7.3	9.5	8.5	10.0	8.5	9.0	7.1	7.0	6.9
Disposable income	6.8	7.8	6.0	4.4	6.5	4.1	6.0	8.4	5.5
Corporate profits before tax	-4.7	13.1	2.7	1.7	13.4	-8.3	2.1	4.2	2.1
Federal government receipts and expenditures (N.I.A. basis)									
Receipts	5.7	17.0	12.1	23.5	11.0	18.6	5.5	-0.4	5.0
Expenditures	14.9	11.4	6.6	6.6	4.3	6.6	2.7	11.7	3.7
Nonfarm payroll employment	3.1	3.2	3.2	2.9	4.1	4.6	1.7	1.7	1.7
Manufacturing	1.0	1.5	1.5	2.0	2.0	4.0	-2.0	-2.0	0.0
Industrial production	1.2	4.2	4.1	2.4	5.3	5.0	4.0	1.6	2.6
Housing starts, private	10.9	16.3	-1.4	29.7	12.9	29.7	-45.8	-45.9	0.0
Sales new domestic autos	-9.7	13.9	0.5	27.3	-8.4	-15.9	1.5	11.8	10.0

^{1/} Excluding Federal pay increase, 2.8 per cent per year.

^{2/} Excluding Federal pay increase, 3.7 per cent per year.

Industrial production. The rate of growth in total industrial production from December 1968 to February 1969 was considerably smaller than during the latter part of 1968. As may be seen in the table, the smaller rate of overall growth resulted from widespread slowing in growth of production. A major exception was the faster increase in output of home goods. Production of defense equipment did not decline quite as sharply as earlier, but auto assemblies were reduced far more than in late 1968.

INDUSTRIAL PRODUCTION

	Per cent	Per cent change	
	change	annual rates	
	Dec. 1967	Sept. 1968	Dec. 1968
	to	to	to
	Dec. 1968	Dec. 1968	Feb. 1969
Total index	4.1	8.7	2.8
Consumer goods	4.6	7.1	3.4
Autos	- 0.3	- 8.4	-27.3
Home goods	6.7	10.8	16.2
Apparel & staples	4.2	6.9	1.6
Business equipment	4.1	12.1	9.1
Defense equipment	- 3.3	-19.6	-16.8
Durable materials	2.7	15.6	5.3
Iron & steel	-11.7	68.8	15.2
Construction materials	4.9	9.6	6.4
Nondurable materials	5.4	2.5	- 2.0

Auto assemblies thus far in March have been running at an annual rate of 8.4 million units, the same as in February, and preliminary output schedules for the second quarter are set at about an 8.5 million unit rate. In view of the recovery in new private housing

starts, output of home goods may expand further but at a slower rate than in the December to February period. Production of business equipment is expected to continue to increase rapidly, and the sharp decline in defense equipment--due in part to a strike--should moderate or level off. Steel production rose further in March, but the rate of increase in the second quarter should slow considerably as inventories at steel mills have been about built up again--by the end of January, such stocks were up 20 per cent from the liquidation low at the end of July 1968.

On balance, it is expected that industrial production in March and during the second quarter will continue to rise, probably at around the long-run average annual rate of 4 per cent. This would be less than half the rate of increase from September to December 1968, but somewhat more than in the opening months of the year.

Capacity utilization. The February rate of manufacturing capacity utilization was estimated to be 84.1 per cent, down only slightly from 84.2 per cent the previous month. Little change is expected in March.

The recent Commerce-SEC plant and equipment survey indicates that manufacturers anticipate investment outlays in 1969 totaling 16 per cent above 1968. If their investment plans are realized, the estimated manufacturing capacity growth rate would increase from the estimated 5.8 per cent of 1968 to about 6.5 per cent in 1969. This would still be slightly below the rates of growth which prevailed in 1965 and 1966.

The pattern of industry operating rates was little changed in early 1969. Recent utilization rates have been quite high in the rubber, nonferrous metals and paper industries, and above normal in aircraft, motor vehicles, petroleum, and textiles. Producers of most other manufactured products have appreciable amounts of unused capacity.

UTILIZATION RATES
(Per cent)

Industry	1967	1968						
	QIV	QI	QII	QIII	QIV	Dec.	Jan.	Feb.
Manufacturing	84.8	84.9	84.8	84.0	84.2	84.4	84.2	84.1
Primary processing industries	85.6	85.5	86.5	84.6	85.5	86.1	86.3	86.1
Advanced processing industries	84.3	84.4	83.6	83.5	83.3	83.2	82.7	82.6

Retail sales. Recently revised data indicate that total retail sales have shown a small net increase since September. On the basis of the newly revised seasonals, February retail sales are indicated to be unchanged from the new high reached in January at a level only a little above that of last September. When deflated by the all commodity retail price index, the new January-February level was down 1 per cent from September. (Prior to revision of the seasonal factors, the retail sales series had reached a 1968 high in August--rather than in September--and the advance figures for January had suggested a decline from August rather than the new high now shown.

It should be noted, however, that retail sales exclusive of the automotive group were appreciably larger in February than last September, as may be seen in the table. Sales of durable goods stores have trended downward since September as a result of a downdrift in auto sales. Auto sales might have been higher in February if the dock strike had not affected sales of foreign cars, by perhaps as many as 30,000 units. Sales of new domestic autos rose in the second ten days of March. For the first 20 days, sales were at a seasonally adjusted annual rate of about 8.3 million units, up 6 per cent from the corresponding period in February but down 3 per cent from a year earlier. Dealers' stocks changed seasonally in the first ten days of March at the advanced level first reached last November which is about one-fifth above a year earlier.

Sales of durable goods other than automobiles remained more or less on a plateau in the latter part of 1968. In the first 2 months of this year, however, they rose to a level 2.3 per cent above the second half of 1968 as furniture and appliance sales strengthened.

Nondurable goods sales rose in February to a level close to 1 per cent above their November 1968 peak. After a very strong rise in early 1968, most nondurable categories had changed little during the second half of the year.

RETAIL SALES

	February 1969 (millions \$)	Percentage Change to February from:	
		January 1969	September 1968
Total	29,021	0.0	0.4
Total, less automotive	23,537	0.4	2.3
Durables	9,355	- 1.3	- 3.4
Durables, less automotive	3,871	- 0.6	2.2
Nondurables	19,666	0.6	2.3
Total, adjusted for price changes*	24,636	- 0.4	- 1.0

* Deflated by the all-commodity component of the CPI.

Consumer credit. The increase in instalment credit outstanding during February may be somewhat larger than the \$7.7 billion rise (seasonally adjusted annual rate) in January, according to an estimate based on a limited number of reports from commercial banks. However, it is expected to be well below the monthly increase in late 1968. In January, credit extensions advanced moderately with the increase centered in automobile and personal loans; repayments rose substantially in nearly all categories and were at a record high.

On the surface, the January increase in auto credit extensions appears to be at odds with the decline in unit sales of new cars reported for the month. Part of the disparity is accounted for by a rise in the proportion of new cars (including imported models) sold on credit. After allowance for seasonal factors, the January rate of credit sales--nearly

72-1/2 per cent--was 6 percentage points above the fourth quarter rate and nearly 3 points above the relatively high year-earlier month. For the full year 1968, approximately 2 of every 3 new cars sold were financed. During their recent meeting at the Board, members of the Consumer Bankers Association reported that loan applications for auto purchases this winter have been more typical of the marginal type usually encountered late in the summer and near the end of the model year. This suggests that the widespread dealer sales contests during January and February led to credit purchases of new cars that normally would not have been made at this time of the year.

Another factor that bolstered auto credit extensions in January was a further increase in the size of the average note written for both new and used cars. The seasonally adjusted increase of more than \$20 in average new car notes from December to January may reflect the higher sticker prices associated with mandatory installation of certain safety features, since contract terms--both down-payment and maturity--were little changed. On the other hand, larger used car notes may be due to higher financing charges resulting from a 2 percentage point rise in the proportion of contracts over 30 months in length (from 44.8 per cent in December to 46.8 per cent in January), and an increase in the proportion of low down-payment contracts (from 28.3 per cent to 31.2 per cent). Seasonally adjusted used car prices were about unchanged from December to January.

AUTOMOBILE INSTALMENT CREDIT DEVELOPMENTS
(Seasonally adjusted)

		Extensions (Billions of dollars)	Average note (Dollars)	Number financed (Millions of units)	Per cent financed
		Annual rate		Annual rate	
<u>NEW CARS</u>					
1968:	I	18.4	2975	6.2	68.7
	II	18.7	3000	6.2	66.9
	III	20.0	3032	6.6	64.5
	IV	20.1	3065	6.6	66.2
1969:	Jan.	20.7	3095	6.7	72.3
<u>USED CARS</u>					
1968:	I	11.1	1553	7.2	
	II	11.0	1567	7.0	
	III	11.6	1576	7.4	
	IV	11.4	1585	7.2	
1969:	Jan.	11.4	1616	7.1	

Changes in other key components of consumer credit have been mixed this winter. Loan extensions and repayments for consumer goods other than autos have fluctuated in a narrow range since October; personal loan extensions, after a sharp drop in November have returned close to the October peak, and repayments reached a new high in January.

The Michigan Survey of Consumer Demand. The index of consumer sentiment rose significantly in February 1969, primarily as a result of an increase in the number of families expecting business conditions to improve in the next 12 months. In the past, changes in response to this question have been a better indicator of cyclical changes in demand

than the other 4 attitudinal questions used to compute the index of sentiment. The rise in the February index follows 2 surveys which reported almost no change, and moves the level back to that of February 1968. Intentions to purchase automobiles are also at about the same level as 12 months ago.

INDEX OF CONSUMER SENTIMENT
(February 1966 = 100)

1968:	February	95.0
	May	92.4
	August	92.9
	Nov. -Dec.	92.1
1969:	February	95.1

Regular, as well as special one-time, survey questions suggest that the improvement in consumer attitudes is still associated with some ambivalence. Thus, despite an increased number of families expecting an improvement in general business conditions, there was an unusually large number who expected an increase in unemployment during the year. Moreover, respondents were aware of higher interest rates and generally thought that the higher rates would be bad for business. The Survey Research Center suggests that the overall optimism may reflect faith in the new Administration's economic policies and less concern with international problems.

Moreover, despite the acceleration in price increases--and the very large number of families reporting that their higher money

incomes were offset by higher prices--there was a decrease in inflationary expectations and fewer unsolicited complaints about prices. Generally, families thought that it was a better time to buy large household goods, cars, and houses than in the previous survey. Although consumers expected the surtax to be extended, 84 per cent of the households interviewed thought that even with price increases they would be at least as well off a year from now--the highest percentage since November 1965.

INTENTIONS TO BUY CARS DURING NEXT 12 MONTHS
(Percentage of family units)

Surveys conducted in January-February of:	All Cars	New Cars	Used Cars
1964	15.1	8.0	7.1
1965	17.8	10.8	7.0
1966	18.6	10.5	8.1
1967	17.3	9.7	7.6
1968	17.2	9.0	8.2
1969	17.5	9.2	8.3

Personal income. The increase in personal income was sharp in February--\$5.3 billion, at an annual rate. Wage and salary payments increased \$4.2 billion, reflecting large employment and wage rate increases, with all major industry divisions contributing to the advance. In addition to the strong February gain, the estimated January payroll increase was revised up to \$3.2 billion from the \$2.4 billion reported last month.

On average, the rate of growth of wage and salary payments appeared to be slightly stronger in early 1969 than during late 1968.

The acceleration occurred in the nonmanufacturing activities. In manufacturing, increases in wage rates and employment have been offset to some extent by small but steady reductions in average hours of work. Income increases from other sources were mostly in line with late 1968 patterns.

On the average, gross personal income rose at an annual rate of nearly \$5 billion in January and February, continuing the pattern of stronger-than-expected income, output, and employment gains. But, because of the January increase in Social Security taxes (which are deducted from wage disbursements before calculating personal income) the increase of personal income in the first quarter of 1969 is likely to be slightly smaller than in late 1968.

Leading indicators. The preliminary Census composite index of selected leading indicators increased to a new high in February. Component series increasing in February were nonagricultural placements, durable goods new orders, building permits for private housing, industrial materials prices, and the ratio of price to unit labor cost in manufacturing. Stock prices, the manufacturing workweek, and contracts and orders for plant and equipment declined.

COMPOSITE CYCLICAL INDICATORS
1963 = 100

	12 Leading Indicators	5 Coincident Indicators	6 Lagging Indicators
1968:			
October	144.0	160.2	168.7
November	143.6	162.1	170.8
December	144.6	163.3	174.3
1969:			
January	144.0	164.6	177.9
February p	145.7	166.3	181.5

The leading indicator subgroups remain at high levels; three of the five are below their early 1966 highs, but none of them now shows the kind of downtrend that characterized all five throughout 1966.

Inventories. In January, the book value of manufacturing and trade inventories rose at a pace considerably below the fourth quarter average. Durable manufacturers continued to build inventories, especially in the machinery and equipment industries. Inventories declined at non-durable manufacturers, and trade inventories also declined, as a decrease at wholesale more than offset a small increase at retail. Inventory-sales ratios declined in manufacturing and trade, giving reason to anticipate continued inventory building over the first half of the year, although probably at rates somewhat lower than in the fourth quarter of 1968.

INVENTORY CHANGE (BOOK VALUE)
(Seasonally adjusted, millions of dollars)

	1968 QIV (Monthly average)	1969 January
Manufacturing and trade, total	1,045	282
Manufacturing	490	326
Durable	321	457
Nondurable	169	-131
Wholesale trade	144	-127
Retail trade	411	83
Durable	280	161
Nondurable	131	- 78

At retail , stock-sales ratios dropped back to around their November levels, which were moderate for nondurables and relatively high for durables. (For comparison, the table shows the monthly average ratios for 1964, before the Vietnam build-up, and the December 1966 ratios that preceded 1967's inventory slowdown.) In February, stocks of domestic autos were reduced somewhat but were still high in relation to sales.

SELECTED INVENTORY RATIOS

	1964 annual average	1966 Dec.	1968		1969 Jan.
			Nov.	Dec.	
<u>Inventories to Sales</u>					
Manufacturing, total	1.64	1.72	1.67	1.72	1.68
Durable	1.88	2.00	1.98	2.07	1.97
Nondurable	1.38	1.37	1.30	1.31	1.32
Home goods and apparel	1.74	1.98	2.15	2.07	1.93
Retail trade, total	1.40	1.51	1.47	1.50	1.47
Durable	1.87	2.11	2.08	2.11	2.07
Nondurable	1.19	1.22	1.19	1.21	1.18
<u>Inventories to Unfilled orders</u>					
Durable manufacturing, total	.71	.64	.69	.68	.69
Defense products industries	.29	.30	.35	.35	.35
Machinery & equipment industries	.66	.58	.63	.66	.64
<u>Manufacturing, total: Materials held and ordered to --</u>					
Sales of end products	1.79	2.08	1.79	1.86	1.80
Unfilled orders for end products	1.11	1.07	.99	.98	.98

At the time of the OBE quarterly survey in February, durable goods manufacturers anticipated that they would increase inventories faster than sales in both the first and second quarters. There was a sharp decrease in the proportion of durables manufacturers who reported that their inventories at the end of the previous quarter were too high relative to sales and unfilled orders. This may have resulted partly from a change in the questionnaire which may increase the tendency of reporters to record their inventory level as "about right," but it would also appear to be consistent with January's declines in some of

the inventory ratios, including those for materials. For example, inventories of steel mill shapes at producing mills and manufacturing consumers at the end of January were at a reduced level in relation to January's high level of steel use in manufacturing.

Nondurable manufacturers projected inventory increases in line with sales. There has been some decrease in the proportion of nondurable manufacturers considering their inventories low; though this could reflect the questionnaire change, it seems consistent with the recent increase in their inventory-sales ratio.

New orders for durable goods. The reported strength in new and unfilled orders for durable goods in January and February also supports the prospect that durable goods manufacturers are likely to add to their inventories in coming months. In total, durable goods orders rose 3 per cent in February and were above last October's peak. As in October, a significant amount of the increase was in defense orders. Fabricated metals orders recovered somewhat but were still below last autumn's highs.

NEW ORDERS FOR DURABLE GOODS
(Seasonally adjusted, billions of dollars)

	1968 QIV (Monthly average)	1969	
		Jan.	Feb.
Total durable manufacturers	29.7	29.7	30.7
Iron & steel	2.0	2.1	2.1
Motor vehicles & Parts	4.2	4.2	4.2
Consumer durables (exc. autos)	2.0	2.1	2.2
Machinery and equipment	6.3	6.2	6.3
Defense products industries (old series)	4.2	4.0	4.6
All other durable manufacturers	11.0	11.1	11.3
Defense products (new series)	2.2	1.8	2.5

Machinery and equipment orders and backlogs continued at high levels, and the anticipated second-half increase in plant and equipment expenditures raises the possibility of further increases, rather than decreases, in capital goods orders. Although inventory-backlog ratios for business and defense equipment seem quite high, these industries usually continue building inventories until after their backlogs have leveled off or declined.

Construction and real estate. Outlays for new construction put in place, which were revised upward by 2 per cent for January to \$89 billion, changed little in February, according to preliminary Census Bureau estimates. Residential construction, bolstered by an exceptionally strong starts performance in recent months, continued close to previous highs at a level 15 per cent above a year earlier. Outlays for commercial, industrial and other nonresidential structures also apparently changed little, after a sharp upward revision to a record rate in January.

Expenditures for public construction--though also little changed in February--were 3 per cent below their advanced year-earlier rate, reflecting in part slowing in State and local activity much of which is dependent on Federal financial assistance. With borrowing difficulties also apparently an increasingly limiting factor, new State and municipal construction projects reaching the architectural stage so far this year have been averaging about 7 per cent below a year earlier according to the Engineering News-Record.

NEW CONSTRUCTION PUT IN PLACE
(Confidential FRB)

	February 1969 (\$ billions) ^{1/}	Per cent change from	
		January 1969	February 1968
Total	88.8	--	+ 6
Private	61.3	--	+ 11
Residential	30.7	--	+ 15
Nonresidential	30.5	--	+ 7
Public	27.5	--	- 3

^{1/} Seasonally adjusted annual rates; preliminary. Data for the most recent month (February) are confidential Census Bureau extrapolations. In no case should public reference be made to them.

Seasonally adjusted housing starts dropped in February as expected. But the decline was associated with some upward revision (to an annual rate of 1.84 million units) in the already unusually high January rate and left the February rate at 1.7 million units, still moderately above the advanced fourth quarter average. Although multifamily starts also shared in the February decline, the rate remained particularly high, at a level more than 50 per cent above the reduced year-earlier level. The February decline in total starts was quite general, but the rate in the North Central states actually rose further to a new peak for the Census series which began in 1959.

Unlike starts, seasonally adjusted building permits turned upward again in February and exceeded the recent high reached last December. Partly reflecting the greater ability of multifamily builders to negotiate required financing under recent market conditions, all of the February rise in permits was concentrated in multifamily units.

These not only climbed to a new high but also accounted for a record share--56 per cent--of total permits in permit-issuing areas. Until last January multifamily permits had never accounted for as much as half of the total.

PRIVATE HOUSING STARTS AND PERMITS

	February 1969 (Thousands of units) ^{1/}	Per cent change from	
		January 1969	February 1968
Starts	1,700	- 8	+11
1-family	982	- 7	- 9
2-or-more-family	718	- 9	+55
Northeast	211	-29	+ 3
North Central	594	+ 8	+39
South	670	-12	+ 5
West	225	- 4	-17
Permits	1,506	+ 7	+ 8
1-family	661	- 1	- 9
2-or-more-family	845	+15	+26

^{1/} Seasonally adjusted annual rates; preliminary.

Despite the February upturn in building permits and the very large backlog of commitments still outstanding, some further drop in the rate of starts seems likely for March on technical as well as other grounds. Even so, with January-February already at a combined 1.77 million rate, indications now are that starts will hold at or above 1.70 million average for the first quarter as a whole.

Looking toward the spring quarter, availability of labor and materials--particularly lumber--should combine with financing problems to limit the normal seasonal rise of about three-fifths typical for the seasonally unadjusted series at this time. Nevertheless, pressures on builders to attempt to maintain schedules in response to pent-up shelter demands will also continue to be a significant factor in these developments. In January, the latest month for which data are available, such demands remained quite strong in the face of both higher interest rates and other costs. In that month, stocks of new homes offered by speculative builders turned downward again as sales of these homes held near their advanced December rate. Sales of used homes, moreover, averaged a sixth above the improved year-earlier level, with prices of the mix of homes sold running 7 per cent more than in January of 1968.

Business fixed capital spending. Outlays for new plant and equipment in 1969 will total \$73 billion--\$9 billion, or 13.9 per cent, more than last year--according to the Commerce-SEC survey of business plans in February. Plans for 1969 as reported in this survey are about 3.5 per cent higher than indicated in the unpublished and confidential Commerce-SEC survey taken in December. In 1968, business plant and equipment spending was 3.9 per cent above 1967, but little if any higher in real terms.

The relatively large year-to-year increase now indicated for 1969 includes a very large rise in the current quarter--\$5.8 billion, annual rate, or almost 10 per cent. (The \$5.8 billion increase being

planned in February for the first quarter compares with last November's planned increase of \$3.9 billion.) A decline in outlays is planned in the second quarter and then a rise in the last half of the year. Total spending in the July-to-December period would be 4.8 per cent above the total for the first half of the year.

The Commerce-SBC plant and equipment investment surveys have almost always correctly indicated the direction of change in such spending but not always the exact magnitude of the change. And recent experience suggests that the very large rise indicated for the first quarter may not be realized. Fixed capital outlays in the final quarter of last year were up only \$2.7 billion, although November plans had indicated an increase of \$3.8 billion, which in turn had exceeded August plans by \$1.3 billion. The short-fall of actual spending from that being planned about midway in the quarter had been \$1.6 billion in the third quarter last year and \$1.9 billion in the second quarter.

Increases in outlays now planned for 1969 by major industry groupings range upward from 7 per cent for the "commercial and other" category to nearly 30 per cent for railroads. Manufacturers--which generally account for more than two-fifths of total spending--anticipate a rise of almost 16 per cent, and this sharp increase contrasts with declines of about 1 per cent last year and also in 1967.

Following the large rise anticipated for the first quarter, second quarter plans indicate only a moderate increase by nondurable

BUSINESS PLANT AND EQUIPMENT EXPENDITURES*

	Years		Quarters			Half-years		
			1968	1969		1968	1969	
	1968	1969	IV	I	II	2nd Half	1st Half	2nd Half
Billions of Dollars; -----Quarterly and Half-year Figures at Annual Rates--								
All Business	64.08	72.96	65.90	71.65	70.85	64.55	71.25	74.70
Manufacturing	26.44	30.65	26.85	29.50	29.95	26.75	29.73	31.45
Durable Goods	13.51	15.48	13.90	15.30	15.15	13.75	15.23	15.70
Nondurable Goods	12.93	15.17	12.95	14.20	14.80	13.00	14.50	15.75
Nonmanufacturing	37.64	42.31	39.05	42.15	40.90	37.80	41.53	43.25
Mining	1.42	1.60	1.35	1.65	1.60	1.35	1.63	1.55
Railroads	1.34	1.73	1.15	1.45	1.60	1.18	1.53	1.95
Other Transportation	4.31	4.83	4.80	5.00	4.05	4.70	4.53	5.25
Public Utilities	11.54	13.16	12.00	13.40	13.35	11.45	13.38	13.00
Communications	6.36	7.44	6.95	7.60	7.00	6.55	7.30	7.60
Commercial & Other	12.67	13.56	12.75	13.10	13.35	12.55	13.23	13.85

	1967- 1968	1968- 1969	1968-IV 1969-I	1969-I 1969-II	1968-H2 to 1969-H1	1969-H1 to 1969-H2	1968-H2 to 1969-H2
-----Per Cent Change-----							
All Business	3.9	13.9	9.4	-2.1	10.4	4.8	15.7
Manufacturing	-0.9	15.9	10.2	0.7	11.1	5.8	17.6
Durable Goods	-1.4	14.6	10.4	-2.0	10.8	3.1	14.2
Nondurable Goods	-0.5	17.3	10.0	3.5	11.5	8.6	21.2
Nonmanufacturing	7.6	12.4	8.8	-4.0	9.9	4.1	14.4
Mining	0.0	12.7	22.2	-3.0	20.7	-4.5	14.8
Railroads	-12.4	29.1	30.4	6.7	29.7	27.5	65.3
Other Transportation	11.1	12.1	3.1	-19.2	-3.6	15.9	11.7
Public Utilities	16.8	14.0	13.3	-1.5	16.9	-2.8	13.5
Communications	7.6	17.0	9.4	-9.2	11.5	4.1	16.0
Commercial & Other	2.7	7.0	3.1	1.1	5.4	4.7	10.4

* - Figures for 1969 are planned expenditures.

goods manufacturers and declines by most other industry groups, including durable goods producers. Spending by most industry groups in the last half of the year will rise moderately, according to February plans.

Manufacturing and public utility firms reported that the value of their new projects started in the final quarter of last year (net of cancellation) exceeded their capital expenditures on projects underway. The value of new projects started in the fourth quarter by public utilities rose sharply, totaling more than at any time since the beginning of 1963, when the series began. New projects started by manufacturers declined a little following a very sharp rise to a record high in the third quarter. For both manufacturers and public utilities the amounts still to be spent on investment projects already underway were at all-time highs at the end of December.

Manufacturing companies owning 47 per cent of fixed assets in manufacturing at the end of 1968 reported the need for more facilities. The greatest need was reported by nondurable manufacturers. This 47 per cent proportion is still below the 51 per cent figure in the first quarter of 1966, but it is the highest proportion since the end of that year and reflects the third successive increase. Producers with 48 per cent of fixed assets in manufacturing viewed their facilities as "about adequate" for 1969 sales requirements.

Labor market. Employment posted another sharp advance in February, wages and personal income rose considerably, and the unemployment rate continued at a 15-year low of 3.3 per cent. Job gains were especially large in the nonmanufacturing industries, but in manufacturing increases (after allowance for strikes) were not as brisk as they had been in other recent months. Also the factory workweek was again down slightly.

Employment. Nonfarm employment increased by 380,000 in February, continuing the recent pattern of accelerated growth. Since September, employment has increased by 1.6 million (seasonally adjusted) or by an average monthly rise of 325,000. From January 1968 to September 1968, monthly employment gains had averaged 166,000.

In part, employment increases in recent months appear to be attributable to the retention of workers who would normally be laid-off during the winter and rehired over the spring months. In construction, for example, the usual sharp seasonal employment decline failed to occur in February and the seasonally adjusted employment figure rose by 110,000 to 3.5 million, a new high. However, further large employment gains in construction may be limited by sharply rising costs, mortgage fund limitations, and a shortage of skilled construction workers.

Manufacturing employment continued to rise in February, but less strongly than in other recent months. After allowance for the return of petroleum workers on strike the previous month, the increase was about 37,000. Growth rates slowed in primary metals,

machinery and fabricated metals--the industries that had contributed heavily to the earlier pick-up. The construction-related lumber and stone, clay and glass industries also added fewer employees in February than they had in other recent months and employment declined somewhat in apparel.

The average workweek of production workers in manufacturing edged down to 40.5 hours in February, for a total reduction of 0.6 hours from September 1968. Over the last several months, aggregate production worker manhours have risen very little because the steady easing of the workweek has offset much of the rise in employment. In fact, manhours of work have declined in consumer goods but have been offset by a pick-up in the producers' goods industries. On an industry basis, manhours have declined in autos, apparel, textiles, printing, and petroleum (due to the strike). Reflecting the rise in plant and equipment expenditures, manhours have continued to increase in fabricated metals, primary metals and machinery.

MANUFACTURING MANHOURS, EMPLOYMENT AND HOURS
 Percentage Changes
 (Seasonally adjusted)

Production workers	October 1968 to December 1968	December 1968 to February 1969
Employment	1.0	0.4
Average weekly hours	-0.7	-0.5
Manhours	0.3	0.1

Wages. In February, the hourly earnings of workers on private nonfarm payrolls averaged \$2.96, an increase of 6.5 per cent from a year earlier. This was smaller than the year-to-year gains of 7.3 per cent in the last three months of 1968. In manufacturing, hourly earnings in February averaged \$3.12, an increase of 6.1 per cent from a year earlier.

Labor force and unemployment. The rapid expansion in the civilian labor force which began late last year continued in February. With demands for labor strong and widespread, labor force growth was equaled by employment gains and the unemployment rate held steady at 3.3 per cent.

Unemployed workers totaled 2.9 million in February. Nearly one-fourth of these workers wanted part-time jobs only and the majority of the jobless had been unemployed for less than 5 weeks. Adult unemployment usually reaches its seasonal peak in February but with the labor market very tight and demand still strong, layoffs apparently have been smaller and less widespread than usual this winter. Jobless rates for worker groups most likely to be laid-off during seasonal slowdowns--construction workers, laborers, and nonwhite men--have dropped this winter and the layoff rate in manufacturing has been very low in recent months.

Collective bargaining. Relatively few major wage settlements have been concluded in the first quarter, but approximately 1.2 million workers received deferred wage increases provided by major contracts negotiated in 1968 or earlier years. The deferred increases

were relatively smaller than recently negotiated increases and went mainly to railroad workers (2 per cent) and to workers at glass and can factories (4 to 4-1/2 per cent). The median deferred increase due in 1969 as a whole is 4.1 per cent.

Relatively few of the 700,000 workers covered by contracts up for renegotiation in the current quarter have reached agreement so far. Prolonged bargaining on the railroad and airline contracts, which expired in the current quarter, is expected to lead to settlements at mid-year or later. It is apparent, however, that the airline negotiations will lead to substantial wage increases for 75,000 airline mechanics. Two settlements, one with the Flying Tiger Line and the other with American Airlines on March 19, following a 20-day strike, have provided average annual wage increases of about 8-1/2 per cent over the life of the contract. It is likely that this pattern will spread to the remaining settlements.

New negotiations are due in lumber and with the maritime unions in addition to the usual heavy spring schedule in construction, in the second quarter. Furthermore, more than 2.2 million workers will receive deferred wage increases in the second quarter. About 800,000 are construction workers and half of them will receive an increase of 7 per cent or more; most of the rest are telephone and trucking workers whose increases will average approximately 4-1/2 per cent. Relatively few of the workers are in manufacturing where the median boost due in 1969 is small, 3.8 per cent; in nonmanufacturing, the median deferred increase for the year as a whole is nearly 5 per cent.

Consumer prices. The consumer price index rose 0.4 per cent in February--an advance about the same as the average monthly increase over the past year. At 124.6 per cent of the 1957-59 average, the CPI was 4.7 per cent above a year earlier.

Food prices stabilized, following a sharp, contraseasonal rise over the preceding 2 months. The February index of retail food prices was close to the level anticipated by Agriculture Department experts for 1969 as a whole.

Average prices of non-food commodities showed a step-up in February, but the bulk of the February rise stemmed from a 6 per cent rise in used car prices recovering from a sharp decline in December and January. The validity of these large fluctuations in used car prices is debatable: the BLS has been having trouble maintaining the used car price series over the past year. The February level of used car prices was slightly below a year earlier.

Prices of services continued up at about a 6 per cent annual rate. (From February 1968 to February 1969 they rose 6.4 per cent.) But in February, as over the past year, a sizable boost in mortgage interest rates contributed significantly to the rise in the service component of the CPI. Other housing costs also rose substantially as did medical care. Prices of utilities and public transportation, which had jumped sharply from October through January, showed only a moderate further rise in February.

Wholesale prices. The BLS estimates sharp increases in wholesale prices of industrial commodities and of farm products between mid-February and mid-March and a rise of 0.5 per cent in the total wholesale price index, to 111.7 per cent of the 1957-59 average. At an estimated 111.7 the March WPI was 3.2 per cent above a year earlier, with farm products and processed foods and feeds up 3.6 per cent and industrial commodities up 3 per cent.

Industrial prices rose 0.4 per cent in March, with the distinct possibility--in view of experience with preliminary estimates in recent months--that the final figure will round up to an 0.5 per cent increase. The preliminary estimate for February was raised 0.1 to show a rise of 0.5 per cent. With the January index up 0.6 per cent, the rise in industrial prices during the first 3 months of the year was at an annual rate of 6 per cent plus.

In March, as in other recent months, sharp increases in lumber and plywood were major factors in the over-all industrial price rise. For the first 3 months these commodities accounted for about a third of the total price rise; excluding lumber and plywood, average industrial prices increased at an annual rate of about 4-1/4 per cent, which in itself represents a step-up from the average rate of increase in late 1968. The diffusion of increases thus far in 1969 has considerably exceeded that in the late months of 1968 and has about equalled the early 1968 experience. In addition to lumber, average prices of metals showed unusually large increases early this year, and in March there

were substantial boosts in petroleum and products and in machinery and equipment.

Recent sharp increases in lumber and plywood and sizable boosts in nonferrous metals have brought about an especially sharp rise in the Federal Reserve index of sensitive industrial materials--to a new 18-year high in March. Relative rates of increase in the special FR groupings of sensitive and other industrial materials and consumer industrial products and producers' equipment from last August through March (as estimated roughly) are shown in the table below.

WHOLESALE PRICES OF INDUSTRIAL COMMODITIES
(FR groupings of BLS data; 1957-59 = 100)

	1968		1969			Per cent change 8/68 to 3/69 ^e
	Aug.	Dec.	Jan.	Feb.	Mar. ^e	
Total	108.1	109.3	109.9	110.4	110.9	4.4
Materials	106.6	107.9	108.8	109.5	n.a.	5.5
Sensitive	106.6	110.1	112.4	114.4	115.6	14.5
Other	106.8	107.5	108.0	108.3	n.a.	2.9
Products	110.0	111.1	111.4	111.6	n.a.	3.1
Consumer nonfood	107.5	108.3	108.4	108.7	n.a.	2.4
Producers' equipment	115.4	117.1	117.6	117.8	n.a.	4.3

e. Estimated

Lumber prices. Average prices of lumber and plywood rose almost 4 per cent further in March and were about 40 per cent above a year earlier. This represents the sharpest increase in lumber and plywood prices of the past 42 years except for a period immediately following World War II. Within the past four months alone these prices have spurted 23 per cent.

Such increases provide a classic example of how extremely strong demands and inadequate supply interact to raise prices of sensitive industrial materials dramatically.

The main factors operative on the demand side have been the marked expansion in the construction and furniture industries, large purchases of logs by Japan, and heavy exports of lumber and plywood to Vietnam. Unfavorable weather, various strikes (including the East Coast dock strikes which reduced shipments from the West Coast), the reduced number of plywood plants, and freight car shortages have all been involved in limiting domestic supplies. According to industry sources, another significant factor has been underutilization of Federal timberland. Higher prices have contributed to increases in production amounting to about 8 per cent for lumber and 15 per cent for softwood plywood, over the year 1968.

In an attempt to alleviate domestic shortages and price increases, exports of logs from Federal timberlands will be reduced and the President has recently directed the Defense Department to keep purchases of lumber to a minimum, the Departments of Agriculture and Interior to release more timber from Government lands, and the Interstate Commerce Commission to take action to ease the boxcar shortage. Such actions to change underlying conditions together with the normal forces of the market can be expected to reverse the course of prices in coming months.

Commodity Credit Corporation expenditures. It appears that a substantial part of the surplus in the National budget projected for fiscal 1969 will be erased by Commodity Credit Corporation spending. The Corporation has exhausted its borrowing authority and will have to suspend payments in April unless its request for a billion dollars in supplemental funds is granted by Congress. Through January, the CCC had spent \$4.2 billion net for price support and had already exceeded the \$3.8 billion limit imposed for the entire fiscal year by the Supplemental Appropriations Act for 1969 enacted last fall.

The CCC dilemma stems from a shortfall in receipts and a very large increase in mandatory outlays for price support. Through January, receipts from sales from inventory were 75 per cent below the same period last year. Instead of providing a \$900 million offset to outlays as in fiscal 1968, net additions to inventories cost \$130 million, as shown in the table. Dock strikes caused some of the decline, but rising world surpluses of agricultural products were the major obstacle. Sales of certificates of interest to private lenders also lagged far behind a year earlier despite an increase in the interest rate to 6.625 in mid-January. Receipts from certificates sales through January provided an offset to expenditures of only \$324 million, compared with \$933 million in the corresponding period a year earlier.

Outlays for commodities going under price-support loan from the huge 1968 crops amounted to \$1.8 billion through January, nearly \$700 million more than in the same period a year earlier. Cotton and

NET PRICE SUPPORT EXPENDITURES OF THE CCC
For periods, July 1 through January 30

	1968	1969	Change
	(In millions of dollars)		
Inventory operations	<u>860</u>	<u>2,362</u>	<u>1,502</u>
July-January change in inventory	- 896	130	1,026
Losses on inventory operations	509	250	- 259
July-January change in loans	1,092	1,786	694
Interest and other expenses	155	196	41
Direct payments	1,717	2,214	497
Total, net expenditure	<u>2,577</u>	<u>4,576</u>	<u>1,999</u>
Certificates of interest, July-January increase in bank holdings (minus)	933	342	- 591
Total, net expenditure, less certificates	1,644	4,234	2,590

soybeans, and to a lesser extent, wheat, accounted for nearly all the increase in loans this year. Redemptions of price-support loans were small. Direct payments to farmers through January were a half billion higher than a year earlier, an outcome of the more attractive terms offered farmers to encourage them to hold 1968 feed grain, wheat, and cotton acreage out of production.

The CCC is currently estimating that net outlays for price support will amount to about \$4.7 billion for the fiscal year. Of course, if a large quantity of certificates are turned in for redemption, it will be more. The seasonal peak in outlays for price-support loans was reached in February when the movement of commodities under price-support loan tapered off. Major expenditures during the rest of the year will be for advance payments of about \$350 million due farmers signing up for the

1969 acreage diversion programs, and for purchases of manufactured milk and other products, and possibly redemption of some certificates of interest. Receipts from sales of inventory will provide more offsets than in the earlier part of the year.

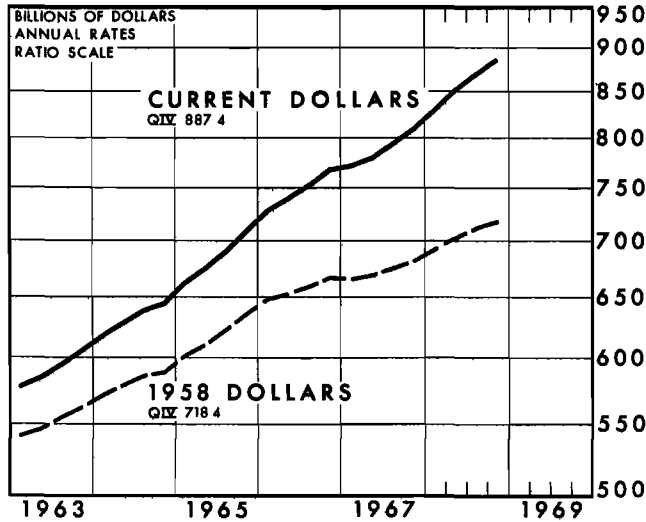
Prospective plantings of 1969 crops. Another year of large price-support operations is in prospect if farmers actually seed the somewhat larger acreage of spring-planted crops reported in the March 1 intentions report and the weather is favorable. According to their plans, acreages of feed grains and hay will be about the same as last year; cotton and flaxseed will be up sharply; and wheat and rice will be down. Major shifts in cotton and food grain acreages reflect grower compliance with changes in Federal programs. Cotton acreage is expected to be 10 per cent larger, all wheat, 13 per cent smaller, and rice, 9 per cent smaller.

Farmers reported an intended 3 per cent increase in soybean plantings in the March 1 survey. Now that the price support has been reduced from \$2.50 per bushel to \$2.25 in an effort to cope with mounting surpluses, it is hoped that some of this acreage will be shifted to other crops.

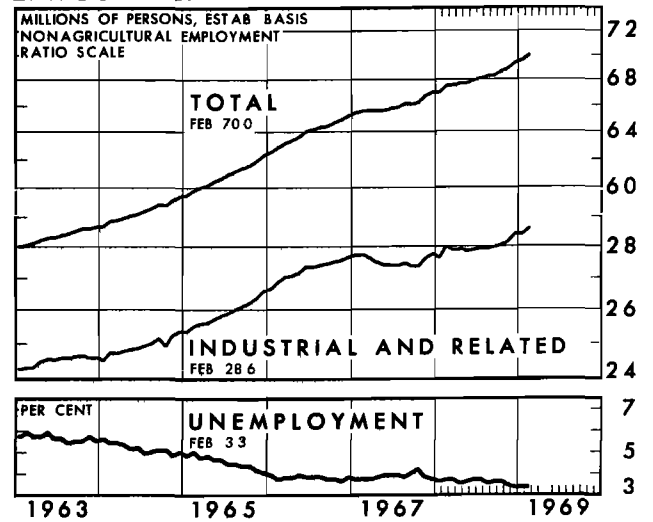
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

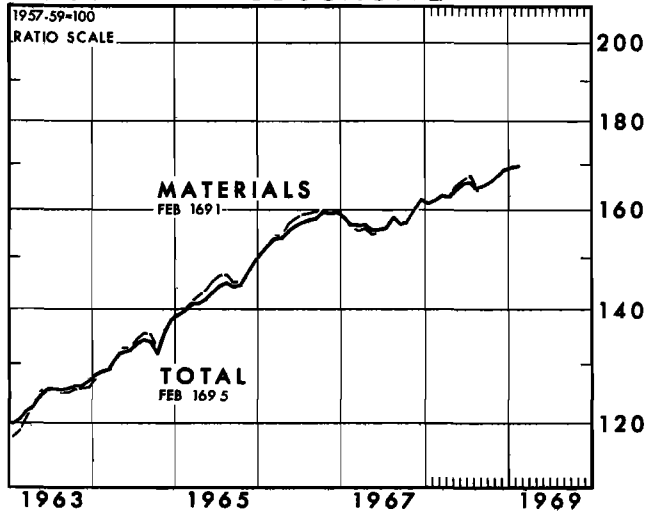
GROSS NATIONAL PRODUCT



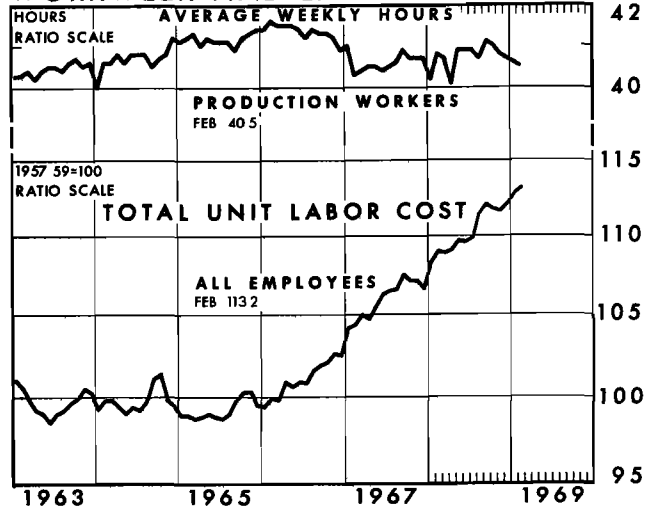
EMPLOYMENT AND UNEMPLOYMENT



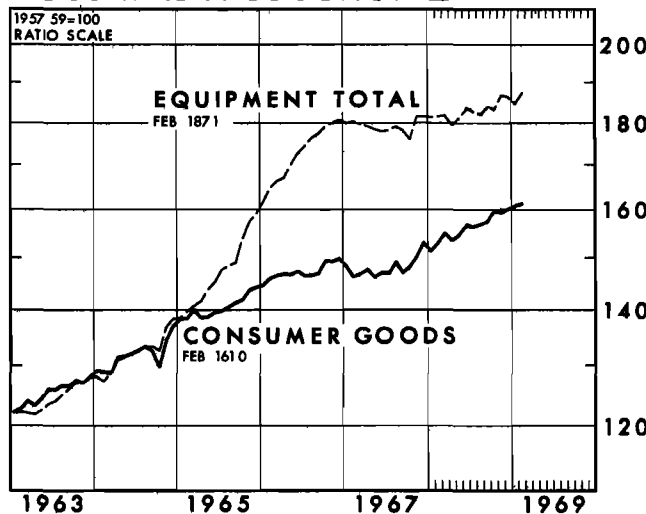
INDUSTRIAL PRODUCTION-I



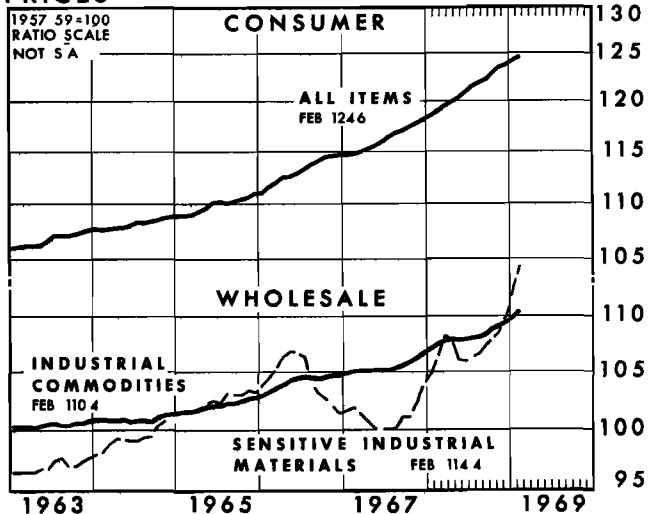
WORKWEEK AND LABOR COST IN MFG.



INDUSTRIAL PRODUCTION-II



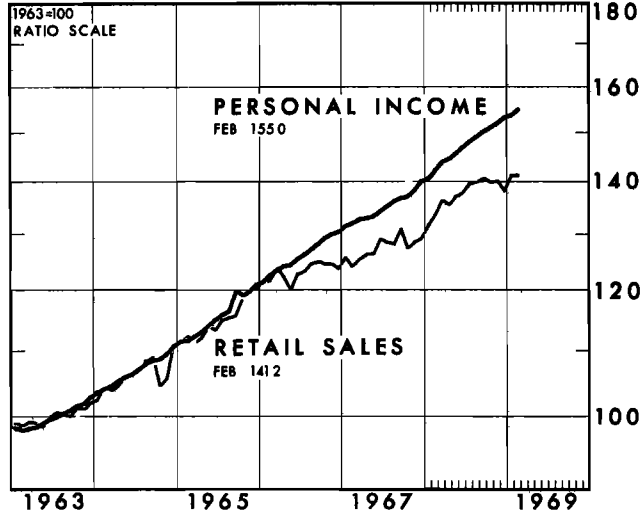
PRICES



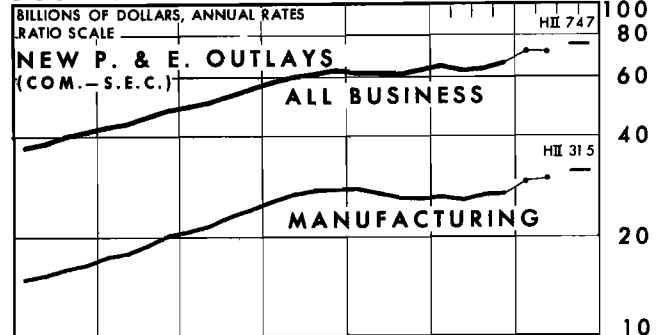
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

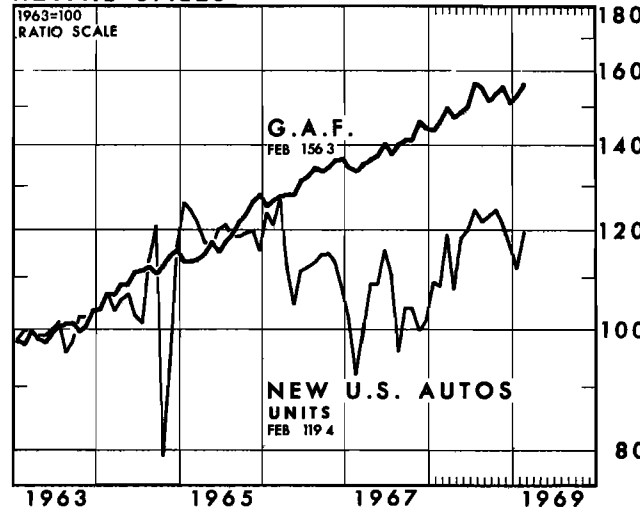
INCOME AND SALES



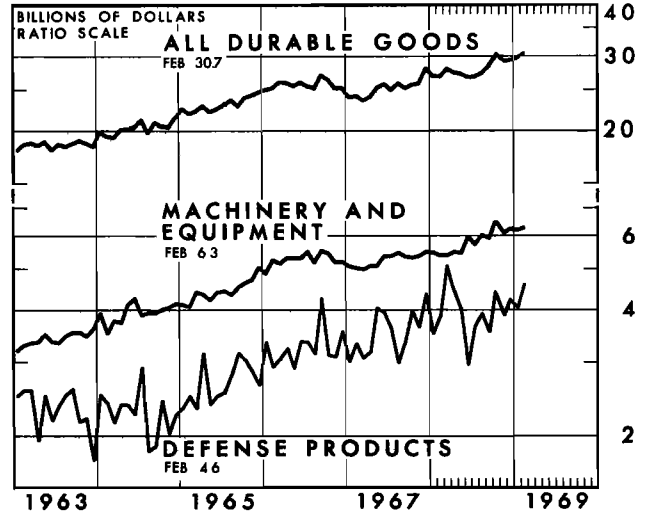
BUSINESS INVESTMENT



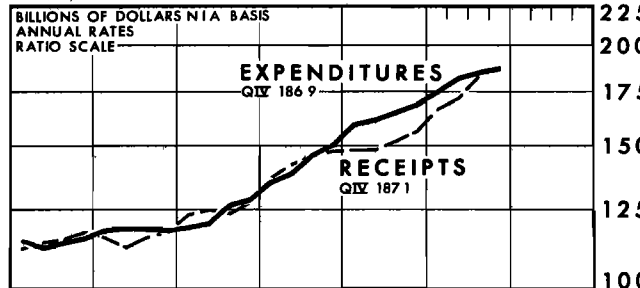
RETAIL SALES



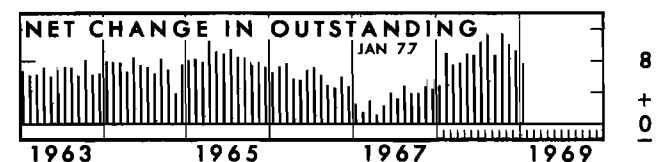
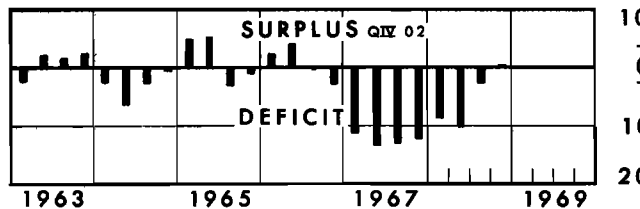
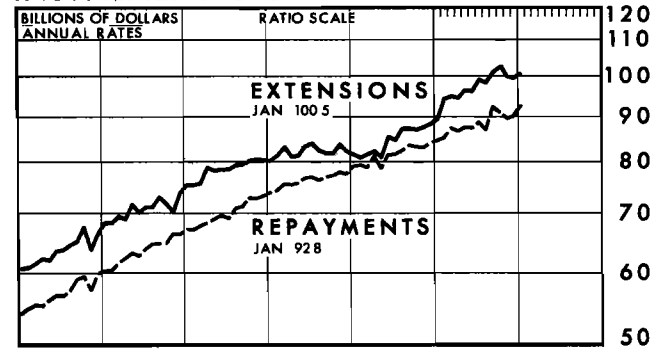
MANUFACTURERS' NEW ORDERS



FEDERAL FINANCE—N.I. ACCOUNTS



INSTALMENT CREDIT



DOMESTIC FINANCIAL SITUATION

Bank credit. As measured by the daily average credit proxy, adjusted to include Euro-dollar borrowings, member bank credit is projected to decline somewhat in March, following no net change over January and February. Thus, for the first quarter as a whole, this measure of bank credit would show a small decline.

The pressure on bank credit in recent months has been concentrated at large banks. From mid-December, when heavy CD attrition began, to mid-March, total loans and investments at weekly reporting banks have declined on balance--as indicated by the chart on the following page. The reduction in outstanding credit at these banks reflects liquidation of security holdings that more than offset further increases in loans, which have been buoyed by continued strong loan demands by businesses.

From mid-December to mid-March, weekly reporting banks have run-off nearly \$4.8 billion in holdings of U.S. Government securities--particularly Treasury bills--with about 45 per cent of this liquidation taking place at New York City banks. Although rising somewhat during the first week in March as banks underwrote nearly all of the \$1 billion Treasury bill strip, bank holdings of Governments resumed their decline in the following week.

Weekly reporting banks have also reduced their holdings of other securities since mid-December, although these holdings have shown little change in recent weeks. The total reduction over this period

LOANS AND INVESTMENTS AT WEEKLY REPORTING BANKS ^{1/}

Billions
of
Dollars

Total Loans and Investments

224

222

220

218

216

U.S. Government Securities

30

28

Other Securities

26

38

Loans

36

158

156

154

Business Loans

72

70

68

October

November
1968

December

January

February
1969

March

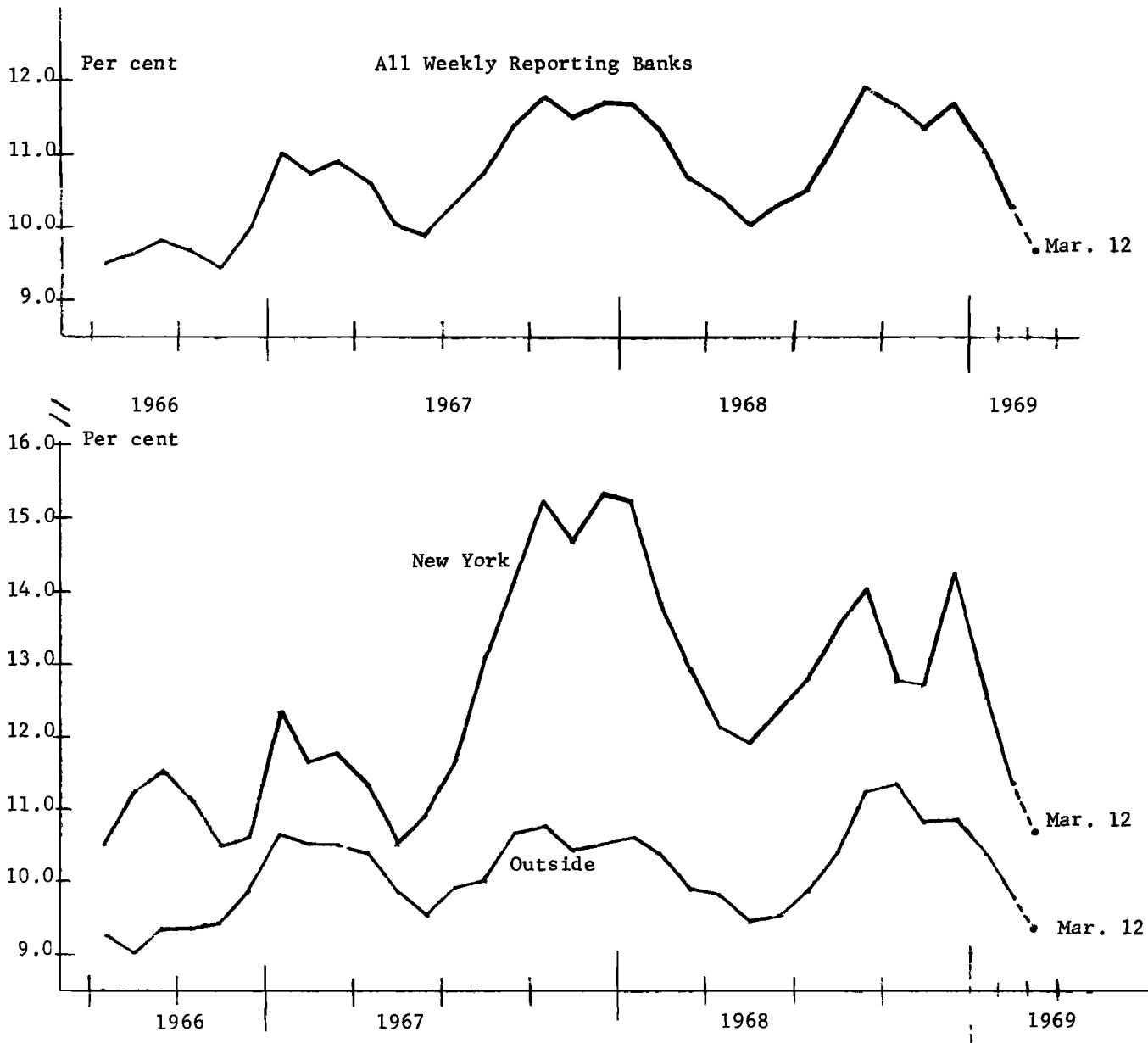
^{1/} Seasonally adjusted levels; experimental series based on preliminary seasonal factors

was concentrated at banks in New York City and reflected contraseasonal declines in short-term municipals and agency issues as well as much less than usual acquisitions of long-term municipals and participation certificates.

Following a substantial increase in late 1968 and early 1969, total loans at weekly reporting banks have risen only slightly, on balance, in recent weeks in spite of further increases in business loans. Of the other major loan categories, only consumer and real estate loans expanded further so far in March, maintaining approximately the advanced rate of growth of recent months. Broker-dealer loans continued to decline during the first half of March, and finance company loans, although fluctuating, have remained unchanged, on average, since mid-December.

Much of the growth in business loans during the first half of March was at New York City banks and was also fairly widespread among industry categories. But business borrowing at New York banks was extremely light during the week ending March 19, when corporate tax payments were due, which suggests that the early-March surge in business loans at these banks represented in large part earlier-than-usual tax borrowing, possibly in anticipation of the prime rate increase to 7.5 per cent that occurred on March 17. Moreover, tax-related business borrowing in New York may have been understated by the business loan figures during the tax week because of special factors, including large loan repayments by the New York Telephone Company--following their recent \$150 million bond issue--as well as transfers of domestic loans

LIQUID ASSETS/TOTAL LIABILITIES LESS CAPITAL ACCOUNTS ^{1/}



^{1/} Monthly averages of weekly figures, except for latest plot, which is a Wednesday figure. Liquid assets include Treasury bills, certificates, and notes and bonds maturing in one year, tax warrants and short-term municipals, bankers acceptances, balances with domestic banks, loans to domestic banks, and broker-dealer loans. Data not seasonally adjusted.

to foreign branches by one New York bank. For the first three weeks of March combined, business loan expansion at New York banks was nearly as large as in comparable periods of other recent years.

With continued CD attrition, bank accommodation of loan demands has entailed further reductions in their liquidity positions--as indicated by the chart on the following page. Current liquidity at all weekly reporting banks--measured by the ratio given here for the week ending March 12--is approaching the low point in late 1966, with liquidity at New York City banks having already reached that level.

At nonweekly reporting banks, changes in total loans and investments since mid-December have remained close to those in other recent years. With continued strong loan demands, these banks have made much larger than usual reductions in their holdings of U.S. Government securities, but they have continued to take other securities into portfolio at a pace well above that in comparable periods of other recent years.

Bank deposits. Total time and savings deposits at large banks continued to decline contraseasonally in the latter part of February and in the first half of March. This reduction reflects mainly further large CD attrition, since net inflows of consumer-type time and savings deposits--although still somewhat less than usual--have picked up substantially in recent weeks.

NET CHANGE IN TIME AND SAVINGS DEPOSITS
Weekly Reporting Banks
(Millions of dollars, not seasonally adjusted)

	1966	1967	1968	1969
	Feb. 9- March 9	Feb. 8- March 8	Feb. 14- March 13	Feb. 12- March 12
Total time & savings depts.	863	1,512	971	-623
Consumer-type deposits	n.a.	899	748	666
Savings deposits	55	255	284	211
Time deposits, IPC (other than CD's, IPC)	n.a.	644	464	455
Negotiable CD's	349	487	239	-1,089
All other time deposits ^{1/}	n.a.	126	-16	-200

MEMO:				
Euro-dollar borrowings ^{2/}	n.a.	n.a.	-118	565

^{1/} Consists primarily of time deposits held by State and local governments and by foreign institutions.

^{2/} Liabilities of major U.S. banks to their foreign branches, weekly averages of daily figures. These banks increased their Euro-dollar borrowings by \$220 million in the week ending March 19.

n.a. - Not available.

Outstanding CD's at weekly reporting banks declined by an additional \$573 million during the first half of March, bringing the total decline since mid-December close to \$4.9 billion. About 55 per cent of these run-offs took place in New York, and New York and Chicago banks lost another \$363 million in the week ending March 19. With the volume of maturing issues in March comparable to that in February, the attrition of CD's at all weekly reporting banks during the first half of March continued at about the February pace--measured either by the average weekly dollar volume or by the per cent of maturing issues.

In view of continued CD run-offs, banks with foreign branches borrowed an additional \$687 million in the Euro-dollar market during the first three weeks in March, bringing the total increase in head office liabilities to foreign branches to nearly \$2.3 billion since mid-December.

Following a contraseasonal outflow over January, consumer-type time and savings deposits expanded in February and in the first half of March, although still by somewhat less than in comparable periods of other recent years. Savings deposits inflows, however, have contributed to the increase in the first half of March, rising substantially-- although still less than usual--in contrast to net declines in the previous two months. And as has been the case since yearend, inflows of time certificates and open accounts in the first half of March continued at a pace somewhat reduced from that in comparable periods of past years. Country banks began experiencing savings deposit inflows in early February--as compared to outflows earlier in the year--resulting in an advanced, but still less than usual, rate of growth of total time and savings deposits at these banks recently.

The money stock, measured on a daily average basis, is expected to show little further change in March, after having grown at a sharply reduced 2.2 per cent annual rate in the previous two months. U.S. Government deposits are expected to decline in March, following substantial increases earlier in the year.

Nonbank depository institutions. Net new money inflows in February to the two major types of specialized thrift institutions were approximately the same as a year earlier, and fragmentary data suggest the same pattern persisted in the first half of March. On a seasonally adjusted basis, the acceleration shown in February--and probably the deceleration in January--is probably overstated as a result of seasonal measurement difficulties. Even so, it is clear that while inflows have apparently slowed since late last fall, this slowing is less than might have been expected on the basis of current record market yields. Desire for liquid assets, accumulation of funds for April tax payments, the convenience and safety of deposit-type claims, and the earlier shifts of the most interest sensitive deposits out of these institutions have been among the major factors sustaining inflows.

NET NEW MONEY FLOWS^{1/}
(\$ millions)
Not Seasonally Adjusted

	<u>Insured S&L's</u>			<u>MSB's</u>			<u>Both</u>		
	<u>Jan.</u>	<u>Feb.</u>	<u>Total</u>	<u>Jan.</u>	<u>Feb.</u>	<u>Total</u>	<u>Jan.</u>	<u>Feb.</u>	<u>Total</u>
1966	-65	505	440	144	179	323	79	684	763
1967	290	741	1,031	331	286	617	621	1,027	1,648
1968	-270	559	289	162	301	463	-108	860	752
1969 ^{p/}	-130	574	444	100	260	360	-30	834	804

^{1/} Net savings inflows less interest credited.

^{p/} Preliminary.

GROWTH IN SAVINGS^{1/}
 NONBANK DEPOSITARY INTERMEDIARIES
 (Seasonally adjusted annual rate in per cent)

	MSB's	S&L's	Both
1968 - I	7.1	5.6	6.1
II	6.7	5.7	6.0
III	6.5	5.9	6.1
IV	7.0	6.2	6.5
January-February average			
1968	6.8	4.5	5.2
1969	5.5	5.1	5.2
Monthly:			
1968 - October	6.9	7.1	7.0
November	7.5	5.7	6.3
December	6.4	5.7	5.9
1969 - January p/	4.1	4.9	4.6
February p/	7.0	5.2	5.8

^{1/} Data reflect FHLB revisions of the S&L series, and updating of seasonal factors for both.

p/ Preliminary.

In recent months, savings and loan association borrowing from the FHLB has risen only modestly as the sustained, though moderate, pace of inflows and a small increase in mortgage return flows have facilitated the step-up in their net mortgage acquisitions. After the one-time adjustment to new reduced requirements at mid-1968, the associations have also been able to maintain and lately to increase their liquidity position about in line with seasonal pressures.

CASH FLOW OF INSURED SAVINGS AND LOAN ASSOCIATIONS
January-February Combined
(\$ millions, not seasonally adjusted)

	1966	1967 ^{1/}	1968	1969 ^{p/}
<u>Sources</u>				
Net savings inflow	471	1,067	333	517
FHLB advances	-248	-1,111	-34	55
Gross mortgage return flows ^{2/}	2,400	1,860	2,220	2,255
Other ^{3/}	699	753	918	992
Total	3,322	2,569	3,437	3,819
<u>Uses</u>				
Gross mortgage acquisitions	3,341	1,949	3,147	3,537
Liquid items	-75	308	96	144
Other ^{4/}	56	312	194	138
Memo: <u>Net</u> mortgage acquisitions	941	89	927	1,282

^{1/} Patterns are distorted because of the S&L's post-1966 effort to rebuild liquid positions.

^{2/} Includes mortgage repayments, sales of loans and participations, plus some noncash items.

^{3/} Includes changes in loans in process, reserves and surplus, reserve for dividend payments, and non-FHLB borrowed funds.

^{4/} Generally miscellaneous "other asset" items, which includes changes in non-mortgage loans.

^{p/} Preliminary.

Outflows during the March-April reinvestment period may be large in view of the volume of projected April personal income tax payments and the considerable publicity given to the record level of long-term security yields.^{1/} With mortgage commitments remaining large

^{1/} Beginning April 1, S&L's are authorized to offer a 90-day notice account with a 5 per cent rate ceiling. The account/rate structure otherwise remains unchanged: with some geographical exceptions, S&L's may offer 4.75 per cent on regular accounts and 5.25 per cent on minimum term/balance accounts.

relative to cash flows, as discussed in the next section, at last the typical seasonal increase in borrowing from the FHLBanks will no doubt occur, and possibly more--the volume to depend, of course, on the reinvestment period experience. Further implications of such borrowings are discussed in Appendix A.

Mortgage market. Although the pace of net inflows to thrift institutions has moderated a little since late last year, new mortgage commitment activity remained strong in early 1969, at least for the S&L's, as mortgage yields continued to rise.

Yields in the sensitive secondary market for FHA and VA home mortgages edged higher in the most recent auction of March 24, as bidders increased their offerings and adjusted their bid prices to reflect the latest increase in the bank prime rate. In the two preceding auctions, yields had declined slightly as FNMA attempted to stabilize auction prices by setting the volume of accepted bids near record highs despite a sizable reduction in bids received. However, after the March 24 auction, the average yield on FNMA 6-month forward purchase commitments, at 8.09 per cent, was only 8 basis points below the high reached early in the month.

FNMA WEEKLY AUCTIONS

	Total bid received	Total bids accepted	Implicit private market yield (per cent) (6-month forward commitment)
1968 high - June 10	231.8	74.5	7.71
February 17	226.7	100.9	8.09
24	167.2	100.1	8.14
March 3	118.9	90.5	8.17
10	127.1	84.7	8.13
17	132.7	88.5	8.08
24	220.9	84.2	8.09

Note: Average secondary market yield after allowance for commitment fee and required purchase and holding of FNMA stock, assuming prepayment period of 15 years for 30-year Government-underwritten mortgages. Yields shown are gross, before deduction of 50 basis point fee paid by investors to services. The first auction date was May 6, 1968.

For February as a whole, home mortgage rates continued upward at a time of increased rate pressure throughout the capital markets. In the primary market, the average contract rate on conventional first mortgages rose further, although at a somewhat slower pace than in January--when upward rate pressures throughout the mortgage market were intensified by the sharp regulatory increase in contract rates on FHA and VA loans. In the private secondary market for FHA and VA mortgages, average yields in February moved moderately higher reaching a level just short of 8 per cent. Though the spread between yields on Federally-underwritten loans and new issues of high grade corporate bonds had improved considerably over the past two months, a sharp rise in corporate bond yields during the first three weeks in March has narrowed that

spread again. But future upward pressure on rates for both conventional and Federally-underwritten mortgages is anticipated as lenders adjust to the latest rise in the prime rate.

AVERAGE RATES AND YIELDS ON SELECTED NEW-HOME MORTGAGES

	Primary Market: Conventional loans		Secondary Market: FHA-insured loans		
	Level (per cent)	Yield spread (basis points)	Level (per cent)	Yield spread (basis points)	Discounts (points)
<u>1968</u>					
February	6.75	50	6.78	53	6.6
March	6.80	23	6.83	26	7.0
April	6.90	40	6.94	44	7.9
May	7.15	51	7.50 ^e	86 ^e	6.1 ^e
June	7.25	60	7.52	87	6.3
July	7.30	79	7.42	91	5.5
August	7.30	115	7.35	120	5.0
September	7.30	103	7.28	101	4.4
October	7.25	78	7.29	82	4.5
November	7.30	69	7.36	75	5.1
December	7.40	61	7.50	71	6.2
<u>1969</u>					
January	7.55	63	7.85 ^e	93 ^e	2.8 ^e
February	7.60	68	7.99	107	3.9

Note: FHA series: Interest rates on conventional first mortgages (excluding additional fees and charges) are rounded to the nearest 5 basis points. Secondary market yields and discounts are for certain 6 per cent, FHA-insured Sec. 203 loans through April 1968. Data for May 1968 estimated by Federal Reserve based on 6-3/4 per cent regulatory interest rate in effect through December 1968. Data for January 1969 estimated by Federal Reserve on 7-1/2 per cent regulatory interest rates, on which a change of 1.0 points in discount is associated with a change of 12 to 14 basis points in yield. Gross yield spread is average mortgage return, before deducting servicing fees, minus average yield on new issues of high grade corporate bonds with 5-year call protection.

Even though borrowing costs increased to new record highs in February, demands for residential mortgage credit continued stronger than usual at this seasonally slack time of the year. Sufficient funds to accommodate these demands continued to be available in most major areas, according to both FHA and FNMA field office reports, albeit at higher costs.

As shown in the table, the backlog of outstanding commitments at all Savings and Loan Associations and New York State Mutual Savings Banks continued to rise during February, after adjustment for seasonal variations. However, the more diversified New York State Mutual Savings Banks somewhat reduced the rate at which they were approving new commitments, according to Federal Reserve Board derived estimates. The Savings and Loan Associations, which in recent months have stepped up their mortgage commitment activity in an effort to lock-up high yields, further increased their new commitment volume in February to the highest level in almost two years.

The quality of outstanding mortgage debt generally improved again during the fourth quarter of last year, judging from such after-the-fact measures as delinquency and foreclosure rates relating to loans closed mainly in earlier periods. The composite delinquency rate on home mortgages rose less than usual during the fourth quarter, reflecting for the most part a slight rise in short-term delinquencies from a reduced level. Sixty-day-and-over delinquencies showed a further year-over-year decline to the lowest level in 8 years. The over-all foreclosure rate on nonfarm mortgages again edged down, and reached the lowest level since 1960.

RESIDENTIAL MORTGAGE COMMITMENTS OUTSTANDING AT SELECTED THRIFT INSTITUTIONS

Date	Outstanding Commitments			Month-to-Month Change		
	Total	All Savings & Loan Associations	Mutual Savings Banks (N.Y. State)	Total	All Savings & Loan Associations	Mutual Savings Banks (N.Y. State)
	(\$ billion, seasonally adjusted)			(per cent)		
<u>1968</u>						
January	8.4	5.8	2.6	-0.6	-0.1	-1.8
February	8.4	5.9	2.5	0.6	1.7	-2.0
March	8.6	6.1	2.5	2.2	2.7	1.0
April	8.7	6.2	2.5	1.3	1.9	0
May	8.6	6.0	2.6	-1.5	-2.4	0.8
June	8.6	5.9	2.6	-0.5	-1.7	2.3
July	8.8	6.1	2.7	2.2	1.8	3.2
August	9.0	6.1	2.9	2.8	1.3	5.9
September	9.1	6.2	2.9	1.3	1.2	1.4
October	9.5	6.4	3.0	3.8	3.6	4.4
November	9.7	6.5	3.2	2.8	1.6	5.5
December	9.7	6.6	3.1	0.4	0.8	-3.0
<u>1969</u>						
January	9.9	6.7	3.2	1.5	1.2	2.2
February	10.1	6.9	3.2	2.6	3.3	1.1

Note: Based on seasonally adjusted dollar volume. Data from Federal Home Loan Bank Board and Savings Banks Association of New York State. Reporting savings banks account for about 70 per cent of total mortgage lending in the industry. Data for savings banks and S&L's include a minor amount of nonresidential commitments. Subtotals may not add to totals because of rounding. S&L commitments include loans in process.

Corporate and municipal bond markets. Yields on corporate and municipal bonds advanced sharply to new peaks in recent weeks. New corporate bond yields increased more than 60 basis points since the end of February, while municipal bond yields rose about 25 basis points from their advanced level at month-end. Most recently, yield pressures have moderated reflecting peace rumors, a light calendar over the balance of the month, low dealer inventories, and the enthusiastic investor response to two attractively-priced utility offerings. On the basis of information available through mid-week, corporate new issue yields are estimated to have declined significantly in the week ended March 28. However, this week's volume of new issues is very light and yield developments may be a reflection of short-term technical and expectational factors. Even with this decline corporate new issue yields at the end of March remained 50 basis points above their February high.

BOND YIELDS

(Weekly averages, per cent per annum)

	Corporate Aaa		State and Local Government	
	<u>New</u> With call Protection	<u>Seasoned</u>	<u>S&P High</u> Grade	<u>Bond Buyers</u> (mixed qualities)
<u>1968</u>				
Low	6.13(8/30)	5.95(9/13)	4.15(8/9)	4.07(8/9)
High	6.92(12/13)	6.53(12/27)	4.93(12/27)	4.85(12/27)
<u>1969</u>				
Low	6.90(1/10)	6.55(1/3)	4.93(1/24)	4.82(1/24)
High	7.57(3/21)	6.93(3/21)	5.39(3/21)	5.29(3/21)
Week ending:				
February	7 6.97	6.63	5.07	4.96
	14 6.91*	6.66	5.07	4.96
	21 6.90	6.66	5.07	4.95
	28 6.93*	6.68	5.17	5.04
March	7 --	6.72	5.26	5.19
	14 7.23	6.75	5.30	5.26
	21 7.57	6.93	5.39	5.29
	28 7.48e	n.a.	n.a.	n.a.

* Includes some issues with 10-year call protection.
e/ Estimated.

In the corporate market, late additions of small convertible offerings about offset the \$170 million of postponements and issues reduced in size due to interest rate developments. Consequently, public offerings are now estimated at \$825 million in March, about the same as projected earlier. But a seasonal step-up in private placement take-downs and continued heavy volume of stock offerings will likely keep total corporate security offerings in March above the average pace of

last year. Indeed, over the first quarter, the staff estimates that total stock and convertible bond issues accounted for an unusually large 45 per cent of corporate security offerings--exceeded only in the last half of 1968. The high cost of bond financing and the apparent relatively higher financing requirements of medium-sized corporations have probably been the major factors associated with this changing composition of financing.

CORPORATE SECURITY OFFERINGS^{1/}
(Millions of dollars)

	Bonds				Stocks		Total bonds and stocks	
	Public Offerings ^{2/}		Private Placements					
	<u>1967</u>	<u>1968</u>	<u>1967</u>	<u>1968</u>	<u>1967</u>	<u>1968</u>	<u>1967</u>	<u>1968</u>
YEAR - Monthly avg.	1,249	894	580	554	237	382	2,066	1,830
	<u>1968</u>	<u>1969</u>	<u>1968</u>	<u>1969</u>	<u>1968</u>	<u>1969</u>	<u>1968</u>	<u>1969</u>
Q I - Monthly avg.	821	872e	574	597	330	501e	1,726	1,970e
January	903	980	546	591	332	453	1,771	2,024
February	796	810e	585	550e	226	550e	1,607	1,910
March	766	825e	593	650e	441	500e	1,799	1,975e
April	719	900e	438	550e	271	500e	1,428	1,950e

^{e/} Estimated.
^{1/} Data are gross proceeds.
^{2/} Includes refundings.

The ultimate total financing volume in April is expected to be about as large as in March, with an increase in public bond offerings to \$900 million about offsetting the seasonal decline in private placements.

As in March, convertible bonds and stock offerings are expected to account for a large proportion of the total. Actual April financing experience will thus depend not only on interest rate developments, but also on the course of stock prices.

In the tax-exempt market, an estimated \$400 million of postponements is expected to reduce the ultimate volume of offerings in March to about \$450 million, the lowest level in more than 5 years. Most of the postponements in March--as during the entire first quarter--have resulted from statutory interest rate ceilings, and considerable pressure has once again been building up in State legislatures to raise maximum permissible ceiling rates.

STATE AND LOCAL GOVERNMENT BOND OFFERINGS AND POSTPONEMENTS
(Millions of dollars) 1/

	Postponements		
	<u>1967</u>	<u>1968</u>	<u>1968</u>
Year - monthly average	1,230	1,381	86
	<u>1968</u>	<u>1969</u>	<u>1969</u>
QI - monthly average	1,245	913e	285e
January	1,178	1,239	181
February	1,155	975e	275
March	1,404	450e	400e
April	1,318	750e	--

e/ Estimated.

1/ Data are for principal amounts of new issues.

Postponements shown in the table understate the actual degree to which market developments have impeded financing since under recent market conditions many governmental units have not even attempted to market their bonds. It is likely that the current volume of postponements will have a more sizable impact on capital outlays than in earlier periods of monetary restraint since there are reasons to believe that the financial flexibility of State and local governments has been sharply reduced by three years of relatively high interest rates.

The cutback of offerings in March tended to moderate upward rate movements in the municipal market, but to distribute even the small volume of offerings, yields still advanced 25 basis points. Commercial banks--generally the largest buyers--are continuing to reduce their activity in the tax-exempt market, but have not yet become large net sellers. Press reports suggest that individuals and some fire and casualty companies have been important buyers of State and local government securities.

The volume of municipal offerings currently scheduled in April amounts to a sizable \$1.1 billion. After adjustment for an expected high rate of postponements, however, new offerings of tax-exempt bonds are estimated to total about \$750 million, well above the March volume. The increase from March primarily reflects several large issues that do not have interest ceilings or have recently had their ceiling rates raised (such as the State of California). Some of the scheduled offerings are planned by borrowers apparently without sufficient flexibility to await improved market conditions.

Stock market. With continued reduced trading volume, stock prices fluctuated in a narrow range through March, and by late in the month were near their lows for the year. The increase in the prime rate--which already had been discounted--had no apparent effect on prices. By late in the month, the major indices were running 7 to 9 per cent below the highs of last December and 4 to 8 per cent under the highs of mid-February. Blue chip stocks--as measured by the Dow-Jones Industrial Index--have declined less than stocks in general, in part because of upgrading of portfolios and in part because the price of such stocks had not increased as rapidly as stocks in general over the last year.

STOCK PRICE INDICES

	Dow-Jones Industrials	New York Stock Exchange Index	American Stock Exchange Index
<u>1968</u>			
December high	985.21(12/3)	61.14(12/2)	33.25(12/20)
<u>1969</u>			
High (Feb.)	952.70(2/13)	58.70(2/17)	32.69(2/4)
Low (Feb./Mar.)	903.97(2/24)	54.93(3/14)	29.48(3/14)
March high	923.11(3/5)	56.01(3/5)	30.23(3/5)
March 25	917.08	55.84	30.11
<u>Per cent change:</u>			
December high to March 25	-6.9	-8.7	-9.4
February high to March 25	-3.7	-4.9	-7.9
1969 low to March 25	+1.5	+1.7	+2.1

With volume continuing relatively low, failure to make timely delivery of securities by members of the New York Stock Exchange declined again in February from the December peak; the February rate of \$3.0 billion was the lowest since April 1968 when the series began. However, despite the lower March volume, "fails" might rise again this month because of technical difficulties associated with the New York Stock Exchange's computerized Central Certificate Service, which produced some bookkeeping delays.

AVERAGE WEEKLY TRADING VOLUME

	New York Stock Exchange (millions of shares)	American Stock Exchange (millions of shares)	Memo: Fails to Deliver by members of the New York Stock Exchange (billions of dollars)
<u>1968</u>			
October	61.5	26.3	3.4
November	58.7	26.4	3.3
December	60.6	32.7	4.1
<u>1969</u>			
January	58.4	32.8	3.3
February	52.6	26.1	3.0
Week ending:			
Feb. 21 <u>1/</u>	45.6	23.1	--
Feb. 28	53.3	24.4	--
March 7 ⁷	49.5	22.5	--
March 14	46.2	18.9	--
March 21	50.2	21.5	--

1/ Four-day trading week reflecting George Washington Birthday holiday.

Preliminary indications are that margin debt extended by broker-dealers on the New York Stock Exchange declined again in February,

this time by about \$200 million; at the end of the month such credit was almost 15 per cent below the mid-1968 peak of \$6.7 billion. By contrast, securities credit extended by banks last month rose \$60 million.

Policy loan activity at life insurance companies. After the relatively sharp January increase in net policy loans advanced by life insurance companies, activity in February leveled off, on balance. January-to-February patterns among individual companies of the fifteen reporting were mixed, however, with some experiencing fairly sharp increases during February which were offset by smaller increases at other firms. Policy loan volume so far in 1969 is considerably larger than in prior years; and there tends to be a seasonal increase in policy loans at the March-April income tax period. As of the end of 1968, life insurance companies expected policy loan volume to increase somewhat in the first two quarters of 1969, while expecting very little additional volume in total funds for investment.^{1/}

NET CHANGE IN POLICY LOANS
15 Life Insurance Companies*
(\$ millions)

	January	February	March	April
1965	20	25	35	37
1966	36	33	57	69
1967	70	56	64	60
1968	57	57	67	73
1969	81	82	--	--

* Companies account for about two-thirds of policy loans held by the industry.

^{1/} The Supplement will contain an analysis of commitment and investment activity of the life insurance companies in 1968.

U.S. Government securities market. Yields on Treasury bills have declined generally 20-30 basis points since the last meeting of the Committee, with the rate on the 3-month issue falling to about 5.90 per cent. While yields on longer-term Treasury coupon issues continued to advance during most of the period, more recently yields on all coupon issues have turned down. Those on intermediate-term issues are currently below levels prevailing at the last meeting, but yields on longer-term issues are still slightly above those levels.

MARKET YIELDS ON U.S. GOVERNMENT SECURITIES
(Per cent)

	1968		1969			
	Lows	Highs	Mar. 3	Mar. 12	Mar. 17	Mar. 25
<u>Bills</u>						
1-month	4.55 (1/2)	6.35 (12/23)	5.80	5.45	5.45	5.62
3-month	4.82 (1/29)	6.29 (12/24)	6.17	5.99	6.09	5.92
6-month	4.98 (1/29)	6.41 (12/24)	6.31	6.14	6.20	6.04
1-year	5.05 (8/1)	6.47 (12/24)	6.33	6.15	6.22	6.08
<u>Coupons</u>						
3-year	5.34 (8/19)	6.52 (12/23)	6.51	6.38	6.40	6.31
5-year	5.42 (1/12)	6.34 (12/24)	6.45	6.42	6.45	6.39
10-year	5.37 (8/8)	6.27 (12/24)	6.25	6.31	6.35	6.30
20-year	5.14 (8/2)	6.12 (12/24)	6.15	6.24	6.32	6.22

N.B. - Latest dates of high or low rates in parentheses.

The further decline of bill yields has been partly seasonal; reinvestment demands generated by cash redemptions of maturing March tax bills, and temporary bank buying over the quarterly statement and Cook County, Illinois, property tax dates usually create some downward

pressure on bill yields toward the end of March. Seasonal bill buying has been strongly reinforced this year, however, by the cumulative effect of swapping out of maturing bank CD's and by demands from investors seeking temporary liquidity in a period of general uncertainty about interest rates and stock prices. With dealers reluctant to accumulate any sizable positions, in view of the continuing high level of financing costs and expectations about possible further System tightening actions, investor demands have kept dealer holdings of bills at rather low levels.

The Treasury's recent announcement of a \$1.8 billion bill-strip, for auctioning on March 25, produced little perceptible upward movement in bill rates. Since settlement on the offering is due on the quarterly statement date and can be paid for wholly with tax and loan credit, banks bid aggressively in the auction forcing the average rate down to 5.03 per cent, 70-90 basis points below yields prevailing on the outstanding bills being augmented by the strip. With regular weekly and monthly bill auctions occurring just before and just after the strip auction, and with banks expected to liquidate acquisitions of strip bills fairly rapidly, dealers bill positions should be substantially enlarged in the period immediately ahead.

DEALER POSITIONS IN GOVERNMENT SECURITIES^{1/}
(Millions of dollars)

	March 3	March 10	March 17	March 24
Total	<u>1,978</u>	<u>1,556</u>	<u>1,810</u>	<u>1,851</u>
Treasury bills	<u>1,613</u>	<u>1,260</u>	<u>1,533</u>	<u>1,445</u>
Due in				
92 days or less	-75	3	211	736 ^{2/}
Over 92 days	1,689	1,257	1,321	709 ^{2/}
Coupon issues	<u>365</u>	<u>296</u>	<u>277</u>	<u>407</u>
Due within 1 year	174	181	210	285
1-5 years	38	-22	-53	-56
Over 5 years	153	137	120	178

^{1/} Monday figures.

^{2/} Change from March 17 reflects a maturity shift in the June tax bill.

The recent general down-turn of yields on Treasury coupon issues has developed primarily on professional activity. Reports that negotiations with the North Vietnamese have been occurring secretly were generally interpreted by market participants as improving the odds for a cease-fire. The rather sensitive reaction of bond markets to this interpretation--particularly in the corporate sector--apparently encouraged dealers to cover short-positions. Short-covering, along with the further decline of bill yields and the influence this has had on market expectations about System policy, has accentuated the dimensions of the yield reversal. But for the longer-run, the general concern about continuing inflationary pressures that had contributed to the steady updrift of yields on long-term bonds over the preceding three weeks, still appears strongly embedded in current market psychology.

Other short-term rates. Interest rates on bankers' acceptances and short-term Federal agency debt have declined somewhat since the last meeting of the Committee, responding to the lead of the Treasury bill market. Rates on commercial and finance company paper, secondary market CD's, and short-term municipal debt, however, have all risen further. Supplies of acceptances and commercial and finance paper outstanding all increased considerably in February. And, while data are not yet available for March, early indications suggest that this growth has continued, as pressure on banks have accumulated.

SHORT-TERM INTEREST RATES

	1968 ^{1/}		1969			
	Lows	Highs	Mar. 3	Mar. 12	Mar. 17	Mar. 24
<u>1-month</u>						
CD's (prime NYC)						
Highest quoted new issue	4.88 (2/8)	5.50 (12/31)	5.50	5.50	5.50	5.50
Secondary market	4.90 (1/31)	6.45 (12/26)	6.45	6.45	6.45	6.60 (3/20)
<u>3-month</u>						
Bankers' acceptances	5.25 (3/7)	6.50 (12/31)	6.75	6.75	6.63	6.62
Federal agencies	5.00 (2/9)	6.38 (12/26)	6.44	6.43	6.29	6.35 (3/20)
Finance paper	5.13 (3/7)	6.25 (12/31)	6.38	6.38	6.50	6.50
CD's (prime NYC)						
Highest quoted new issue	5.25 (2/8)	6.00 (12/31)	6.00	6.00	6.00	6.00
Secondary market	5.20 (1/3)	6.54 (12/26)	6.60	6.55	6.55	6.75 (3/20)
<u>6-month</u>						
Bankers' acceptances	5.38 (3/7)	6.62 (12/31)	6.88	6.88	6.75	6.75
Commercial paper.	5.50 (3/7)	6.25 (12/31)	6.75	6.75	6.75	6.88
Federal agencies	5.25 (2/9)	6.62 (12/26)	6.60	6.55	6.52	6.54 (3/20)
CD's (prime NYC)						
Highest quoted new issue	5.50 (3/7)	6.25 (12/31)	6.25	6.25	6.25	6.25
Secondary market	5.45 (1/31)	6.75 (12/26)	6.70	6.65	6.65	6.80 (3/20)
<u>1-year</u>						
Prime municipals	2.75 (8/8)	3.80 (12/26)	4.25	4.30	4.50	4.55 (3/20)

^{1/} Latest dates on which rates occurred are indicated in parentheses.

Federal finance. The \$1.8 billion Treasury bill strip auctioned March 25, for payment March 31, completes Treasury cash financing operations for the current fiscal year. This borrowing can be managed within the existing debt ceiling of \$365 billion because \$2 billion of March tax bills have been repaid and Federal trust funds will redeem more than \$1 billion of special issues near the end of the month to finance the mail out of benefit checks. Although the debt subject to ceiling reached an intra-monthly high of \$364.7 billion on March 14, by month-end it is expected to drop to around \$363 billion. Just prior to the redemption of April tax anticipation bills, however, the debt subject to limit will again rise to about \$365 billion as a result of further increases in special issues. In fact, unless Congress quickly completes action on the pending bill that increases the temporary debt ceiling to \$377 billion, the Treasury may have to resort to special measures to avoid breaching the ceiling in this period.

The end-of-March financing allows the Treasury only a minimum estimated cash balance of \$2.2 billion at mid-April. But heavy inflows of tax receipts thereafter will buoy the balance to almost \$10.0 billion by the end of April. Since seasonal tax receipts would tend to maintain an unusually high cash balance through most of the remainder of the fiscal year, the Treasury may decide to repay additional debt beyond the \$2.0 billion of tax bills maturing in April and the \$6.8 billion of tax bills maturing in June. This could be done by allowing some attrition in the refinancing of note and bond issues scheduled to mature in May and June.

The outlook for Budget receipts and outlays remains substantially the same as that shown in the last Greenbook, with receipts still expected to be about \$1.0 billion and outlays about \$1.7 billion larger than the Budget document estimate. Most of the \$1.7 billion difference in projected outlays stems from unexpected changes in CCC spending and interest costs. Because redemptions of bank-held CCC certificates and other CCC price support operations tend to fluctuate rather widely, the magnitude of total CCC outlays is difficult to project; nevertheless, the current staff estimate, at \$4.6 billion, exceeds the January Budget forecast by \$1.0 billion. Gross interest costs are expected to be \$0.6 billion above the Budget. Data on defense spending appear thus far to be conforming to earlier Budget Bureau estimates.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	Feb. ^{a/}	March	April	May-June
<u>Borrowing operations</u>				
New cash raised				
Weekly bills	--	2.8	--	--
Tax bills	--	-2.0	-2.0	-6.8
Coupon issues	--	--	--	--
PC's	--	--	--	--
Other (agency, debt repayment, etc.)	-1.9	--	-.1	-1.4
Total net borrowing from public	-1.9	.8	-2.1	-8.2
Plus: Other net financial sources ^{b/}	-.6	.9	.6	.1
Plus: <u>Budget surplus or deficit (-)</u>	.2	-1.1	6.2	6.7
Equals: <u>Change in cash balance</u>	-2.3	.6	4.7	-1.4
Memorandum: Level of cash balance end of period	4.9	5.5	10.2	8.8

^{a/} Actual and estimated data.

^{b/} Checks issued less checks paid and other accrual items.

NEW BUDGET AND FEDERAL SECTOR IN NATIONAL INCOME ACCOUNTS
(In billions of dollars)

	Fiscal years				1968		1969	
	Actual		Jan. budget	F.R. Bd	III	IV	I	II
	1967	1968	1969	1969				
<u>Quarterly data, unadjusted</u>								
New budget:								
Surplus/deficit	- 8.8	-25.2	2.4	1.7	- 3.2	- 7.1	-.8	12.9
Receipts	149.6	153.7	186.1	187.1	43.6	39.3	44.2	60.0
Total expenditures and net lending	158.4	178.9	183.7	185.4	46.9	46.3	45.1	47.1
Means of financing:								
Total borrowing from the public	2.9	23.1	- 3.1	1.3	7.7	3.4	.5	-10.3
Decrease in cash operating balance	5.2	.4	n.a.	- 3.5	-3.3	3.9	-.8	- 3.3
Other <u>1/</u>	.7	1.7	n.a.	.5	-1.1	-.2	1.1	.7
Cash operating balance, end of period	5.7	5.3	n.a.	8.8	8.6	4.7	5.5	8.8
<u>Seasonally adjusted annual rate</u>								
Federal surplus/deficit								
in national income accounts	- 6.7	-11.3	2.7	2.6	- 2.8	.2	5.8	7.2
Receipts <u>2/</u>	147.7	161.1	190.0	190.9	182.1	187.1p	195.8	198.5
Expenditures	154.4	172.4	187.3	188.3	184.9	186.9p	190.0	191.3

e--Projected.

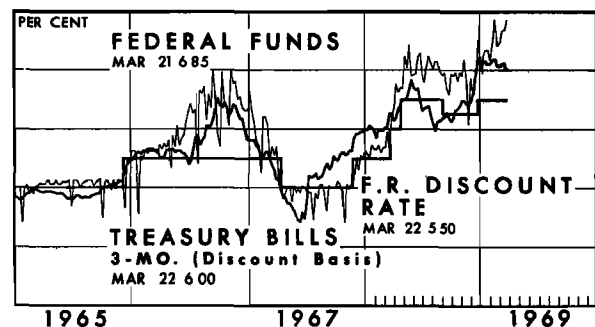
p--Preliminary.

1/ Includes various accrual items, such as deposit fund accounts and clearing accounts.

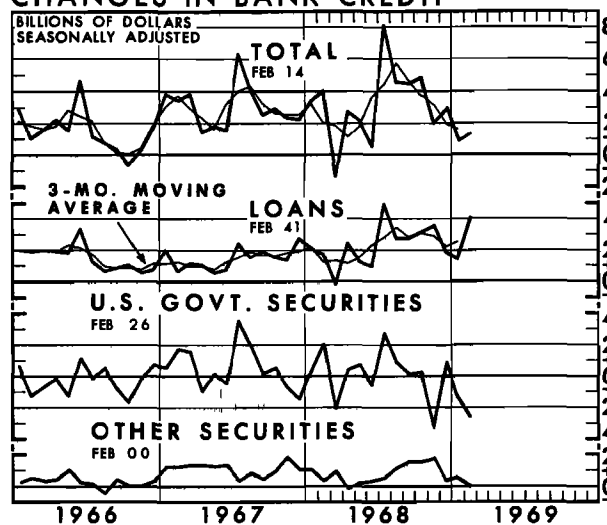
2/ Corporate tax accruals in first two quarters of 1969 assume extension of surtax through calendar 1969.

FINANCIAL DEVELOPMENTS - UNITED STATES

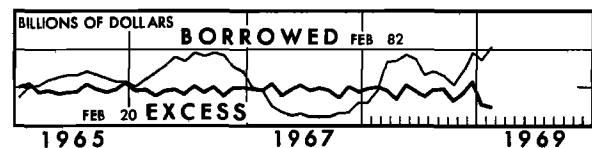
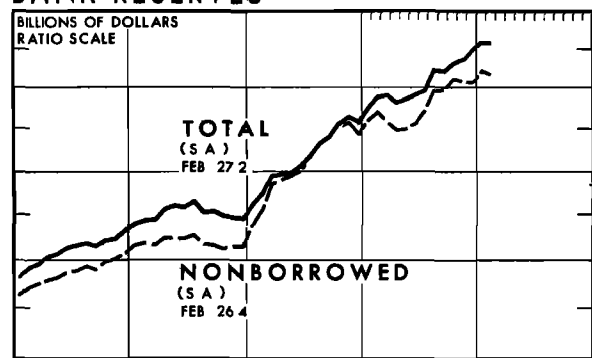
FREE RESERVES AND COSTS



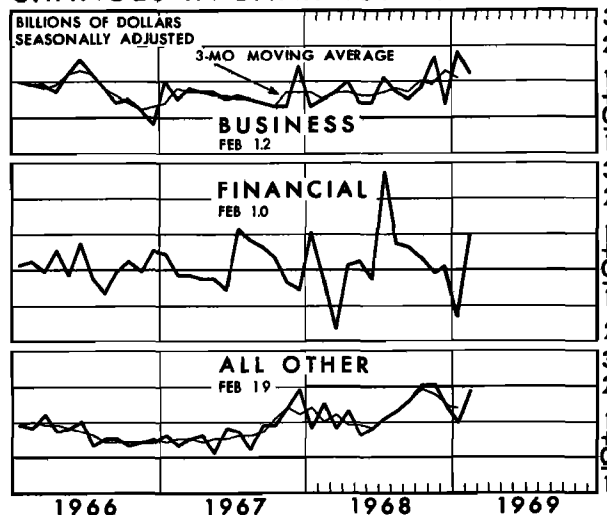
CHANGES IN BANK CREDIT



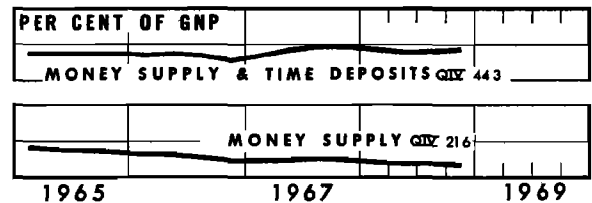
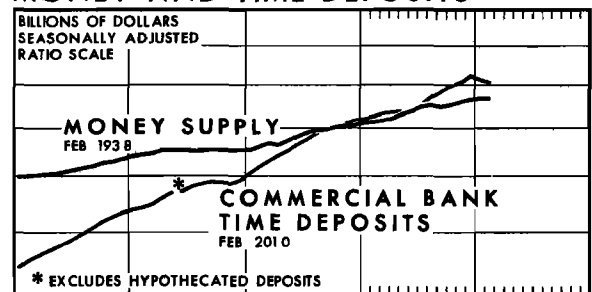
BANK RESERVES



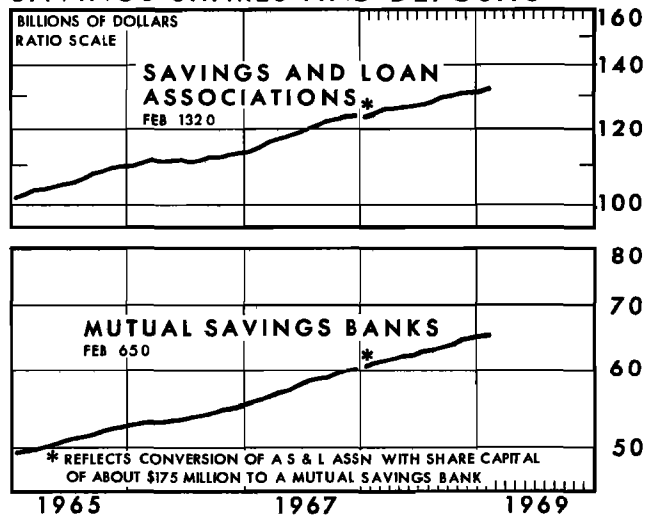
CHANGES IN BANK LOANS-BY TYPE



MONEY AND TIME DEPOSITS

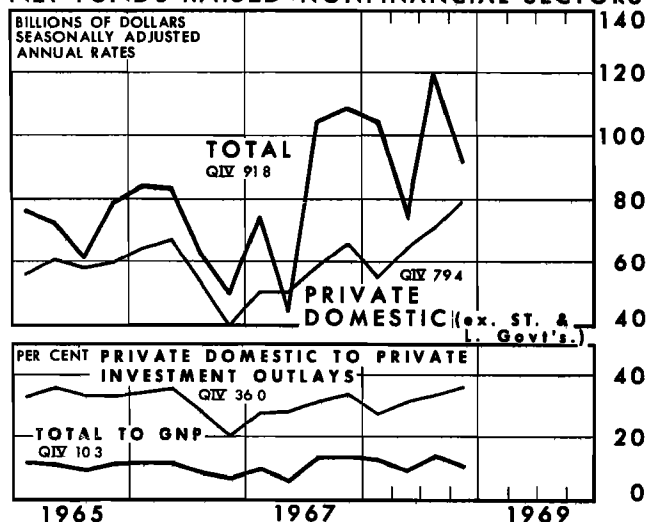


SAVINGS SHARES AND DEPOSITS

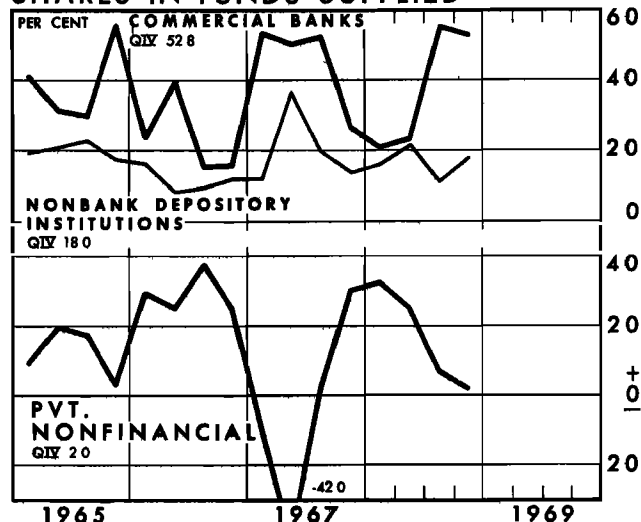


FINANCIAL DEVELOPMENTS - UNITED STATES

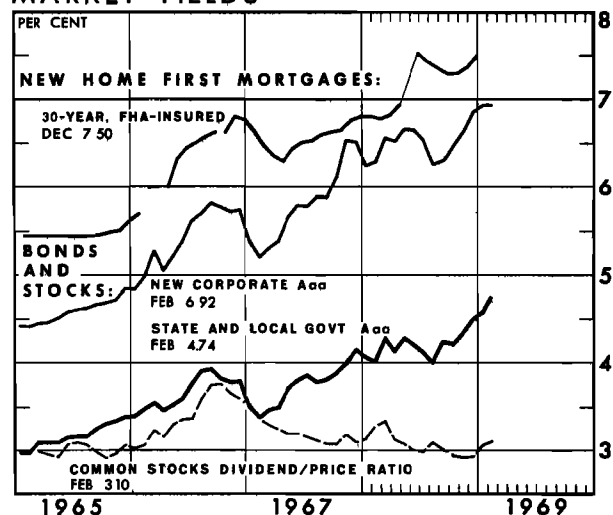
NET FUNDS RAISED - NONFINANCIAL SECTORS



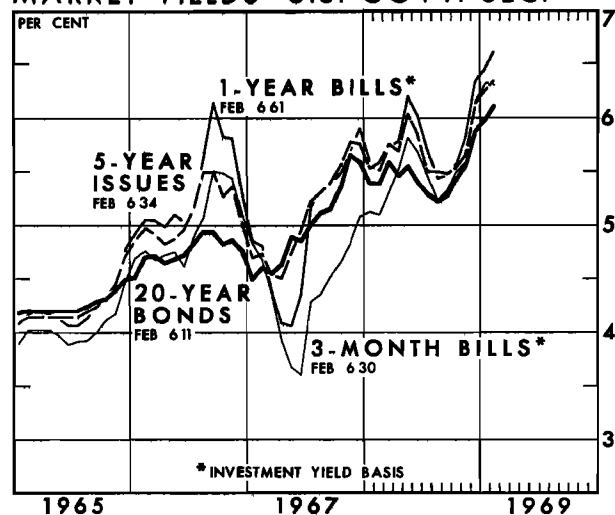
SHARES IN FUNDS SUPPLIED



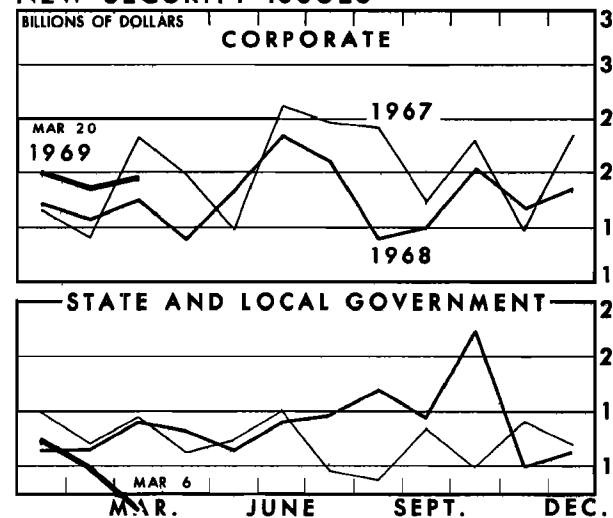
MARKET YIELDS



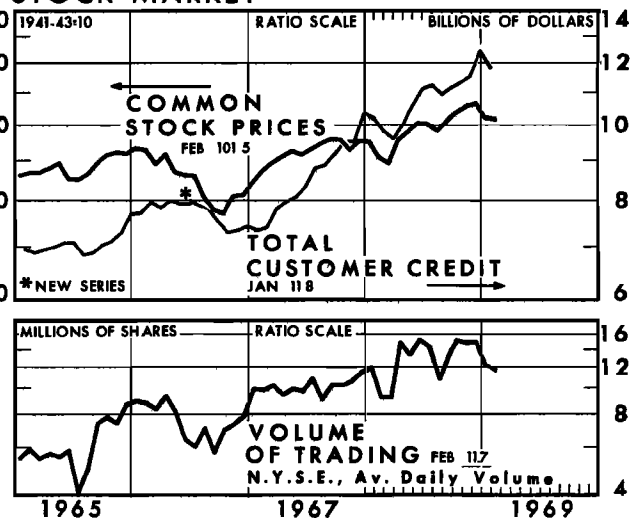
MARKET YIELDS—U.S. GOVT. SEC.



NEW SECURITY ISSUES



STOCK MARKET



 INTERNATIONAL DEVELOPMENTS

<u>Contents</u>	<u>Page</u>
U.S. balance of payments	IV - 1
Foreign trade	4
The 1968 balance of payments	5
The Euro-dollar market	11
Foreign exchange market developments	12
Financial developments in other industrial countries	15

U.S. balance of payments. It seems likely that the liquidity deficit in the first quarter of 1969 will be among the largest on record. Relatively complete figures for January and February show a deficit of about \$800 million (before seasonal adjustment) and incomplete weekly figures for March through the 19th would add a further deficit probably in excess of \$500 million. Since the first quarter is seasonally favorable, the seasonal adjustment will raise the recorded deficit for the quarter by some \$400 million. Thus, unless there is a turnabout in the final days of the quarter, the recorded deficit (seasonally adjusted) would be comparable to the \$1.7 billion registered in the final quarter of 1967.

Measured on the official settlements basis, however, the first quarter will show a very large surplus. Through March 19 this totaled about \$1.5 billion before seasonal adjustment, and about \$1 billion seasonally adjusted. The sharp contrast with the deficit on the liquidity basis results primarily from the rapid growth in liabilities to foreign branches of U.S. banks, which, however, was offset in part by a decline in U.S. liabilities to other commercial banks abroad. From the beginning

of the year through March 19, liabilities to U.S. branches increased by \$3.8 billion. This measurement tends to exaggerate the growth of these liabilities however; if measured from the previous peak on December 11 the increase would be \$2.4 billion.

The data currently in hand do not fully account for the great size of the liquidity deficit as compared with the year-ago first-quarter deficit of about \$700 million (seasonally adjusted). Foreign purchases of U.S. equity securities for instance, were very high this January at \$365 million, and partial figures for February indicate that although there was some decline the inflow was still on the order of \$200 million. Last year the two-month inflow to purchase corporate equities was only about \$250 million. Similarly, bank-reported claims on foreigners were reduced by \$384 million this January, and do not appear to have increased significantly in February; last year the inflow of banking capital for the two months was about \$175 million.

A major negative factor has been the squeeze on the trade balance resulting from the dock strike, which is discussed below. The net effect, as compared to the first quarter of last year, could be over \$1/2 billion. It is still expected that the shortfall in the trade balance caused by the strike will be made up in the second quarter.

There has been a reduction so far this year in receipts from foreign governments under special arrangements with the Treasury (including receipts under the German offset agreement). In the first quarter of 1968 such receipts totaled \$395 million, while through

March 19 this year they were only about \$50 million. A major problem this year, insofar as the published liquidity deficits are concerned, is the difficulty of replacing the \$2.7 billion of special receipts from foreign governments that reduced that deficit in 1968.

An alternative way of stating the balance of international transactions, which is still far from satisfactory but avoids some of the pitfalls of the two conventional methods, is to take the sum of official settlements and changes in liabilities to foreign commercial banks. For the year 1968 this sum showed a deficit of \$1.8 billion, and in the first quarter of 1968 \$1.2 billion (seasonally adjusted). On the same basis the deficit this year through March 19 was on the order of \$1-3/4 billion, with a rough seasonal adjustment.

This measure is not affected either by shifts between U.S. liabilities to foreign official reserve holders and U.S. liabilities to the Euro-dollar market (as the official settlements balance is) or by changes in the maturity of claims on the United States held by foreign monetary authorities (as the liquidity balance is). This measure serves, therefore, as a useful measure of the changes in all other international transactions, though not in itself as an indicator of the absolute degree of disequilibrium.

An adequate explanation of the first quarter deficit this year must wait until the data on merchandise trade are available and can be adjusted for the effects of the strike, and until there is some indication of the course of capital outflows by corporate investors during this period.

Foreign trade. As expected, U.S. exports and imports in January were badly distorted by the dock workers' strike which began on December 20, 1968. The strike lasted until February 15 in the port of New York; most other ports reopened by the end of February except for Boston and West Gulf ports which were still closed as of March 26.

In December the strike, and an anticipation of it, caused exports to be a little lower and imports a little higher than would otherwise have been recorded. In January there was a small trade surplus (on the balance of payments basis) as exports fell somewhat less from their December level than did imports--30 per cent versus 33 per cent.

In February^{1/}, imports began to recover more rapidly than exports, rising by more than one-third from the low January figures; exports advanced by less than 15 per cent. Consequently a large trade deficit was recorded in February. Evidently the huge backlog of cargo from the many vessels waiting to be unloaded had to be cleared from the port area before outbound cargo liftings could begin. In addition, the value of waterborne cargo imports through New York, which reopened earlier than other ports, is greater than for exports. It is expected that the value of both exports and imports will be exceptionally high in March, though with imports still in the lead, and also through most of the second quarter when an export surplus should emerge. The underlying trade trends may not be apparent for some time.

^{1/} February trade data are STRICTLY CONFIDENTIAL until released by the Bureau of the Census on March 27 or 28.

Exports of agricultural products were particularly hard hit by the strike; they fell by more than two-thirds from December to January. The bulk of these commodities are exported through Gulf ports, some of which are still on strike. As a result, the weakness in such exports, apparent even before the strike, may be accentuated as foreign buyers turn to other suppliers.

The 1968 balance of payments. Most of the highlights of the 1968 balance of payments are already generally familiar, but it may be useful to review the full set of data to be issued by the Commerce Department next week (Strictly Confidential until publication). Net exports of goods and services were a little under \$2 billion for the year as a whole, but at an annual rate of only about \$800 million in the fourth quarter. Income and fees from direct investments were somewhat lower than in the third quarter, though for the year as a whole these receipts rose by \$1/2 billion to \$6.2 billion. Military expenditures continued to rise, reaching an annual rate of \$4.7 billion in the fourth quarter, while military exports were down from their third quarter peak.

As may be seen in the following table, the balance on goods and services was very sharply reduced during 1968 with Europe (especially the E.E.C.), Canada, and Japan. Small gains were registered primarily in transactions with Latin America and the grouping of Australia, New Zealand and South Africa.

REGIONAL DISTRIBUTION OF TRANSACTIONS IN GOODS AND SERVICES
(in millions of dollars)

	1967	1968	Change
Balance of goods and services	4,768	1,965	-2,803
United Kingdom	227	-120	-347
E.E.C.	237	-664	-901
Other Western Europe	39	-104	-143
Eastern Europe	19	19	0
Canada	705	-86	-791
Other Western Hemisphere	1,420	1,614	+194
Australia, New Zealand, and South Africa	904	986	+82
Japan	-591	-1,403	-812
Other Asia and Africa	2,166	2,014	-512
International and unallocated	-359	290	+69

In most cases the year-to-year change reflected shifts in the merchandise trade balance. For Canada, heavy deterioration in the trade balance was offset somewhat by lower U.S. tourist expenditures and higher income on investments. There was a small increase in the trade balance with Latin America, as well as some gains in income receipts. With the area "Other Asia and Africa" our trade balance worsened by over \$500 million between 1967 and 1968, and military expenditures rose by nearly \$200 million, but there was an increase of nearly \$400 million in income receipts and a sizable increase in military sales.

In the capital accounts, the main new information given in the Commerce data relates to the behavior of U.S. corporate investors. The following table summarizes those categories of capital flows that reflect either investment abroad by direct investors or their activity

Balance-of-payments savings attributable to the control program were even greater than the \$1.6 billion decline in net outflow of U.S. funds for 1967 and 1968 shown in the table, for two reasons: The exempted net outflow to Canada included in these figures rose by about \$150 million, and the net return flow of liquid assets not covered in the table to meet the requirements of the program was probably over \$1/4 billion.

The tabulation also shows that in the first quarter of 1968, when the companies were not clear how the program operated, there was only a very minor net outflow of U.S. funds. In contrast, a considerable part of the large deficit in the first quarter of 1969 probably reflects a large net outflow of U.S. funds for direct investment. Certainly there is ample room under the 1969 restraint program for a substantial rise in corporate outflows. The ceilings themselves will be substantially higher; even the modifications proposed last November would have permitted an increase of about \$300 million, and further easing, both in absolute ceilings and in specific kinds of investment activity, is generally expected. To this must be added the very large carryover of unused investment allowable from 1968 to 1969--though not all of this will be used this year.

Plans by U.S. companies for expenditures abroad on plant and equipment in 1969 show a rise of 7 per cent after a slowdown in 1968 that was probably attributable in part to the new controls. Growth in investment outlays for manufacturing facilities in Canada slowed very abruptly beginning in 1967, and in Europe last year. The

continued strong growth in the extractive industries (which includes sizable outlays for tankers) shows up mainly in **Latin America and "Other areas"**.

CHANGES IN PLANT AND EQUIPMENT EXPENDITURES OF
FOREIGN AFFILIATES OF U. S. CORPORATIONS
(per cent)

	Actual		<u>Estimated</u> 1967-68	<u>Projected</u> 1968-69
	1965 to 1966	1966 to 1967		
Total	16	7	3	7
By industry				
Manufacturing	18	-2	-6	1
Mining and smelting	25	14	14	13
Petroleum	11	19	11	11
Other industries	14	9	9	22
By area				
Canada	28	-6	-4	3
Latin America	2	16	26	12
Europe	23	11	-10	2
Other areas	3	9	18	14

The levelling off in outlays for foreign manufacturing plants is heavily influenced by a decline for the chemical industry, which in recent years had been especially active. All other manufacturing sectors combined project a 9 per cent increase in outlays in 1969. These figures indicate that though the hectic pace of the pre-1967 foreign expansion has slowed, there is still a strong urge to expand abroad. The absolute amount of the increase in foreign plant and equipment expenditures this year is projected at about \$3/4 billion.

Foreign financing for these investments, and for working capital of the foreign affiliates, is now considerably less easy to

obtain than last year. Sales abroad of new issues to finance direct investments remained high in the first quarter at over \$1/2 billion, but in March such issues slowed down.

Another striking feature of the 1968 balance of payments was the dramatic increase in the flow of foreign private capital to the United States. As shown below, the inflow in nonliquid forms reached \$5.8 billion, nearly triple the already high amount for 1967. A large part of this (\$2.8 billion) has already been counted above as an offset to U.S. direct foreign investments. Other large inflows included \$1.9 billion to purchase outstanding U.S. corporate securities (mostly stocks), a record inflow of \$.4 billion for direct investments, and another record inflow of \$.7 billion to U.S. non-banking concerns. Some of the latter may have been used by direct investors, but another very large part--about \$300 million--is accounted for by an increase in accounts of foreigners with U.S. securities dealers and brokers. This was no doubt related to the increased volume of dealings in U.S. securities; it was partially offset by an increase of about \$200 million for the year in U.S. dealers' accounts due from foreigners.

INFLOW OF PRIVATE FOREIGN CAPITAL^{1/}
(in millions of dollars)

	1967	1968
Total	3,750	9,522
Non-liquid	2,076	5,772
Direct investments	250	363
Purchases of U.S. corporate securities	1,349	4,056
New issues to finance U.S. direct foreign investments	(446)	(2,190)
Other corporate securities	(903)	(1,866)
Long-term liabilities of U.S. non-banks	89	687
Short-term liabilities of U.S. non-banks	388	666
Liquid	1,675	3,750
Foreign commercial banks	1,262	3,382
Other private foreigners	413	368

^{1/} Excludes flows for foreign official accounts and international and regional organizations.

The Euro-dollar market. Euro-dollar interest rates have changed little during the first three and a half weeks of March, remaining at or close to their record levels established during the first few days of the month. One-, three- and six-month deposits have remained around 8-1/2 per cent per annum. One-year deposit rates have been relatively steady at about 8-3/8 per cent; call deposit rates have remained close to 7-7/8 per cent.

Since February 26 the liabilities of U.S. banks to their foreign branches have increased nearly \$1.0 billion and totaled \$9.8 billion on March 19. Supplies of funds to the Euro-dollar market in March have probably come from a wide range of sources. The German and Italian central banks have no longer been encouraging their commercial banks to place funds abroad, and indeed the Bank of Italy is now moving in the other direction (see page IV - 12 below). Early in the month, movements out of francs may have been a source of supply. The widespread weakness of European currency exchange rates in March suggests that the high Euro-dollar interest rates have exerted a pull on funds from many directions. It is possible--though confirmatory data are not available--that funds of U.S. corporations and investors withdrawn from domestic CD's have been moving indirectly into the Euro-dollar market. Placement of funds in U.S.-dollar deposits with Canadian banks is not contrary to any U.S. regulations or guidelines, and under the Canadian "pass-through" guidelines the banks there may have had some leeway to put funds in London. Similarly, U.S. funds could have

been moving to and through corporate affiliates abroad without contravening regulations, since the very large foreign borrowing done by direct investors and their affiliates last year generated large "carryovers" for companies to add to their 1969 "allowables."

SELECTED U. S. MONEY MARKET RATES
AND EURO-DOLLAR RATES
(weekly average of daily figures)

Average for week ending	(1) Call Euro-\$ Deposit	(2) Federal Funds	(3) = (1)-(2) Differ- ential	(4) 3-month Euro-\$ Deposit	(5) 3-month Treasury Bill	(6) =(4)-(5) Differ- ential
Jan. 8	7.67	6.43	1.24	7.45	6.18	1.27
Feb. 5	7.30	6.32	0.98	7.56	6.19	1.37
Feb. 26	7.80	6.43	1.37	8.24	6.06	2.18
Mar. 5	7.90	6.75	1.15	8.34	6.16	2.18
12	7.92	6.76	1.17	8.49	6.03	2.46
19	7.85	6.82	1.03	8.51	6.02	2.49
26	7.82	6.82 ^{p/}	1.00	8.48	5.94	2.54

p/ preliminary

Foreign exchange market developments. Most foreign currencies were generally under selling pressure during March, reflecting the continued pull of high Euro-dollar rates and seasonal payments imbalances in some cases. The major exception was the rate for the Swiss franc, which climbed to its upper limit early in the month in response to tightening financial markets in Switzerland. Late in the month demand for both the Canadian dollar and Italian lira strengthened moderately, the latter in response to measures taken by the Bank of Italy to contain the outflow of funds from Italy into the Euro-dollar market.

The market for sterling was generally weak during March. In late February and early March stronger demand for the pound pushed the exchange rate to its highest level since last May--\$2.3960. However, rumors of a franc devaluation during the first week of the month caused heavy selling pressures to develop against sterling. As the month came to a close sterling was displaying greater firmness. The discount on forward sterling widened sharply from 2.0 per cent per annum to 3.7 per cent at the time of growing anxiety over the French franc parity, but recently it has narrowed to 2.5 per cent.

The German mark was under fairly constant selling pressure throughout March, partly reflecting sales of marks for dollars by parties with maturing forward contracts to deliver dollars to the Bundesbank. The Bundesbank sold over \$1 billion on an outright spot basis and about \$250 million on a swap basis (although its swap rate was no more attractive than the market rate during the four weeks ending March 26.) However, receipts from maturing forward contracts totaled slightly more than \$1 billion, leaving Bundesbank reserves practically unchanged for the month as a whole.

Early in March selling pressure on the French franc increased in response to growing uncertainty about the outcome of wage negotiations and the scheduling of a one-day strike on March 11. At the high point of the anxiety about the franc, the discount on 3-month forward francs rose to 21 per cent per annum. By the end of the month, however, this discount had narrowed to 12 per cent.

The Bank of Italy allowed the lira exchange rate to drop to its lower limit early in March--the first time the lira rate had been that low in several years. Its support during the second and third weeks of March cost the Bank \$120 million. However, on March 24 the Bank of Italy announced measures to induce an inflow of short-term bank funds into the country, which gave a fillip to the lira market.

The price of gold in London rose to a new peak level of \$43.83 an ounce in early March, as French residents reportedly rushed to purchase gold illegally outside the country in the face of rising anxiety about developments in France. More recently the gold price has been around \$43.20 to \$43.30 an ounce.

Financial developments in other industrial countries. Financial markets have tightened in most industrial countries since last autumn because of domestic demand pressures and, in some instances, in reaction to capital outflows from these countries as a result of United States monetary policy and sharply rising Euro-dollar interest rates. Three-month Euro-dollar deposit rates rose by about 1-1/4 percentage points from end-December to mid-March, a direct result of the \$3.4 billion increase in American banks' borrowings from foreign branches during this period.

A substantial rise in short-term interest rates in all other industrial countries except Japan and Italy since late 1968 has accompanied the sharp increase in Euro-dollar rates. Several central banks, particularly those in countries experiencing inflationary pressures, recently have moved defensively by raising their discount rates: Belgium, Canada, the Netherlands, Sweden and the United Kingdom. France, facing a serious balance of payments problem, has since November been restraining short-term outflows through exchange controls as well as through monetary policy.

In Germany, short-term rates remain relatively low but the market has tightened somewhat in the past several weeks. To counter the tendency of rates to rise, the Bundesbank since late January has discouraged short-term capital outflows by the German commercial banks. Of all European countries Italy probably has experienced the least rise in its short-term interest rates, but the Bank of Italy's concern about its official reserve position has led it to take measures to force a reflow

SHORT-TERM INTEREST RATES IN INDUSTRIAL COUNTRIES^{1/}
(Per cent per annum)

	1968		Recent Dates					
	Low	High	12/6	1/3	1/31	2/28	3/14	3/21
Euro-dollar								
Call	4.50 (Jan.)	8.00 (Dec.)	6.56	7.50	7.12	7.88	7.88	8.12
3-month	5.44 (Feb.)	7.94 (Mar.)	7.06	7.25	7.56	8.44	8.50	8.50
United Kingdom								
Treasury bill	6.44 (Oct.)	7.38 (Feb.)	6.69	6.63	6.58	7.55	7.64	7.64
Local authority	6.94 (Nov.)	8.50 (June)	7.50	8.00	8.00	8.63	8.63	9.00
Germany								
Call money	1.00 (Nov.)	4.75 (Dec.)	2.00	3.12	3.50	3.50	3.44	3.94
3-month inter-bank	3.22 (Jan.)	4.75 (Oct.)	4.56	4.50	3.88	3.88	4.12	4.38
Switzerland								
3-month bank deposit	2.75 (May)	4.25 (Dec.)	4.25	4.00	4.00	4.38	4.38	4.75
France								
Call money	4.75 (Feb.)	15.00 (Nov.)	8.12	8.25	7.75	8.00	8.12	8.25
12-month Treasury bill	5.02 (Feb.)	8.41 (Dec.)	8.11	8.71	8.56	8.60	8.85	n.a.
Belgium								
3-month Treasury bill	3.75 (Sept.)	5.00 (Dec.)	4.50	5.00	5.40	5.70	5.95	5.95
Netherlands								
3-month local authority	4.44 (Sept.)	6.69 (Dec.)	6.13	6.25	5.94	6.56	n.a.	n.a.
Japan								
Call loans repayable on day's notice	7.30 (Nov.)	8.40 (Aug.)	7.30	n.a.	7.30	7.67	7.67	n.a.
Canada								
91-day Treasury bill	5.31 (Aug.)	6.79 (May)	5.54	6.15	6.18	6.24	6.43	6.43

^{1/} Rates shown are Friday rates or rates for the nearest date if Friday rates were not available.

LONG-TERM INTEREST RATES IN INDUSTRIAL COUNTRIES^{1/}
(Per cent per annum)

	1968		Recent Dates					
	Low	High	12/6	1/3	1/31	2/28	3/14	3/21
Euro-dollar bonds								
Foreign governments	7.38 (Feb.)	7.81 (July)	7.53	7.54	7.54	7.41	7.42	7.42
United Kingdom								
3-1/2% War Loan	7.12 (Jan.)	8.08 (Dec.)	8.01	8.05	8.46	8.54	8.75	8.82
Germany								
6% public authority	6.19 (Oct.)	6.88 (Mar.)	6.21	6.21	6.19	6.19	6.24	n.a.
France								
Public sector	6.45 (May)	7.06 (Dec.)	6.87	7.02	7.30	7.28	7.38	n.a.
Italy								
Composite ^{2/}	6.48 (Feb.)	6.55 (June)	6.52	n.a.	...	n.a.	n.a.	...
Belgium								
Government ^{3/}	6.44 (June)	6.63 (Dec.)	6.63	6.65	...	6.76	n.a.	...
Netherlands								
Government	6.21 (Jan.)	6.71 (Dec.)	6.50	6.71	6.83	7.01	n.a.	...
Japan								
Bank debentures ^{2/}	8.00 (Aug.)	8.84 (June)	8.67	8.82	...	n.a.	n.a.	...
Tel. & Tel. bonds ^{2/}	8.03 (Aug.)	8.83 (June)	8.66	8.71	...	n.a.	n.a.	...
Canada								
4-1/2% 1983	6.45 (Aug.)	7.48 (Mar.)	7.27	7.35	7.29	7.41	7.48	7.46
Government (average)	6.43 (Aug.)	7.30 (Dec.)	7.07	7.27	7.16	7.20	7.23	7.30

^{1/} Rates shown are Friday rates, or rates for the nearest date if Friday rates were not available.

^{2/} Monthly average.

^{3/} Beginning of month.

over the next several months of Italian funds from the Euro-dollar market. Swiss rates have also risen somewhat in reaction to Euro-dollar rates and rates in other money markets. Japanese interest rates are little changed, at levels which until recently were high enough to encourage Japanese importers to borrow abroad.

Long-term interest rates in the U.K., France and the Netherlands have increased substantially since early December, while elsewhere long rates have increased only slightly. The German bond market tightened in recent weeks, but the authorities are trying to moderate the rise in long-term rates. The future course of long-term rates in Germany is of particular significance since a major increase in German rates relative to those in other countries could undermine Germany's policy of attaining balance of payments equilibrium through the export of long-term capital.

There has been a definite tightening of short-term credit markets in Germany in the last several weeks. From November through February, German short-term rates had moved contrary to usual seasonal changes. During and just after the period of large speculative inflows to Germany, rates had been unusually low. After the turn of the year, instead of easing off seasonally, they rose as a result of the massive outflow of funds from Germany into the Euro-dollar market and the ebbing of speculation on the mark. Commercial banks increased their foreign assets by about \$900 million from end-November to end-January, while their liabilities to foreigners fell by nearly \$700 million. As the Bundesbank became concerned at the effect of this outflow on domestic liquidity, in late January it increased the cost of forward cover it would provide

through mark-dollar swaps with commercial banks. This greatly reduced the banks' incentives to export dollars on a covered basis, and in February the net foreign position of the German commercial banks fell by \$275 million. Banks, however, may be placing funds abroad on an uncovered basis.

Despite the rise in German short-term interest rates this year, they remain relatively low. The net advance to mid-March since August-September, for example, has been only from 3-1/2 per cent to 4-3/8 per cent for three-month interbank loans and from somewhat under 3 per cent to about 4 per cent for call loans.

Long-term interest rates have been essentially stable since September, but since the beginning of March yields on long-term government bonds have begun to creep upward again.

As the economy moves closer to capacity operation, the German authorities are switching from a moderately expansive to a cautiously restrictive policy stance, while endeavoring to hold back the rise in long-term interest rates. For the moment, policymakers are relying primarily on selective fiscal and trade measures to moderate the expansion. Following a March 18 Cabinet meeting, the Federal Government announced measures delaying government expenditures, accelerating tax collections, and raising certain import quotas.

Certain monetary control measures have also been taken recently. Just as the Bundesbank's policy on dollar-mark swaps tends to keep interest rates from rising, so these measures are largely precautionary, with

little immediate effect on rates. On March 3, the Bundesbank reached an agreement with the federal government and the railway and postal authorities to discontinue the use of central bank credit in supporting the prices of their bonds. This move had no immediate impact, since the Bundesbank had not been a net purchaser of bonds since October. On March 20, the central bank further announced a reduction in rediscount quotas for financial institutions, amounting to 20 per cent for commercial banks. This move, too, will have little immediate effect since banks at present are well below their quotas, but it is a clear sign of the Bundesbank's concern over the potential inflationary situation. In another small policy move, the Bundesbank raised its Lombard rate, at which it makes advances against securities, from 3.5 to 4 per cent.

It remains to be seen whether fiscal policy measures will effectively contain aggregate demand and upward price pressures within bounds that the German authorities regard as tolerable. It is reasonable to assume that the Bundesbank would prefer not to have to tighten its policy severely, since continued capital exports are necessary to prevent Germany's large current account surplus from straining the international monetary system.

The British government remains committed to a policy of credit restraint, and on several occasions in recent months the authorities have taken action to intensify restrictions on credit to the private sector. Installment purchase terms were tightened, effective November 2, and

from October through January there was a steady decrease in the amount of installment credit extended, reversing the upward trend of April through October.

At the end of November, the Bank of England sought to curtail bank lending to the private sector by requesting the clearing banks to reduce by mid-March their outstanding loans (seasonally adjusted) to 98 per cent of the amount outstanding in mid-November 1967. Certain loans for exports and shipbuilding were exempted from this ceiling.

This credit ceiling request met with strong opposition from the clearing banks, and the 98 per cent level was not reached by mid-March. Indeed, from mid-November to mid-February, total clearing bank loans (seasonally adjusted) increased by 4 per cent. While some of the increase was undoubtedly accounted for by exempt credits, the Bank of England has acknowledged that there was some increase even in loans subject to the ceiling. Despite the resistance from the banks, the government continues to insist that the target be reached, although it no longer specifies the date by which the reduction must be achieved.

Paradoxically, while urging the banks to restrict credit to the private sector, the Bank of England's support operations in the securities market at the time of the international currency crisis in November--when heavy purchases of short-maturity government bonds were made--had the effect of moderating the rise in short-term interest rates and facilitating bank credit expansion. On February 27, in a move explicitly characterized as an antidote to the increase in bank loans, the Bank

of England increased its discount rate from 7 to 8 per cent, bringing this rate back to the level set immediately following devaluation in November 1967. Loan rates of the banks are closely tied to the discount rate, and it is expected that the increase in rates should ease somewhat the banks' credit rationing task.

Short-term interest rates in the U.K. have been rising since end-November in line with attempts at credit restriction at home and rising rates in the Euro-dollar market. The yield on 90-day local authority deposits, which stood at 7.75 per cent just prior to the change in the discount rate, had climbed to 9 per cent by mid-March, almost 2 percentage points higher than at end-November. The covered interest differential was around 4 per cent in favor of Euro-dollar deposits over local authority deposits in December, but has since dropped to slightly under 3 per cent.

Long-term interest rates in Britain have also increased substantially in recent months, much more than in other industrial countries, despite a considerable improvement in the government's budget position. The yield on the 3-1/2 per cent War Loan was some 70 basis points higher in mid-March than at end-December. There does not seem to be any single reason for this increase in long rates, but the movement is consistent with heightened concern over continuing inflation and the future of sterling, as well as expectations of even higher short-term rates in the near future.

Interest rates in France, both short- and long-term, have shown sizable increases since the franc crisis in late November. This has resulted more from a restrictive credit policy domestically than from a flow of funds abroad, since French money and capital markets are largely isolated from foreign markets by the existence of tight exchange controls imposed after the November crisis--though some capital is being exported in the form of bank notes. In December, stringent regulations were issued regarding foreign exchange cover for import contracts. In January, the Bank of France acted to require commercial banks with net asset positions in foreign currency to deposit these net assets with the Bank of France in three installments.

Domestically, banks were instructed to reduce their short-term credits by mid-January to the level of September 30, and to expand such credits by no more than 4 per cent above this level by end-June.

Treasury bill rates increased by about 60 basis points from end-November to mid-January as a result of the French government's increased reliance on short-term borrowing to finance its sizable budget deficit, leaving more room in longer term markets for private and other public sector borrowers. Long-term public sector bonds nevertheless showed yield increases of over 40 basis points from end-November to mid-January. Neither long rates nor short rates showed much change from mid-January to early March. Call money rates, however, have risen in the last few weeks, and other short-term rates also registered some increases.

Short-term interest rates in Belgium have risen very rapidly since end-November, and the Belgian National Bank has raised its basic discount rate twice, from 3.75 to 4.50 per cent on December 19 and again to 5 per cent on March 6. The discount rate increases in both cases were aimed at reducing the loss of official external reserves. In connection with the March 6 increase, Governor Ansiaux also mentioned a need to moderate the rate of expansion of bank credit but there is little evidence that aggregate demand in Belgium is likely to become excessive in the near future. Belgian commercial banks' net foreign assets increased by \$48 million in the fourth quarter and a further \$42 million in January, reflecting the pull of high Euro-dollar rates.

Treasury bill rates increased by nearly 1-1/2 percentage points between end-November and mid-March, reflecting both the capital outflow and the discount rate increases. Long-term rates remain virtually unchanged with long-term government bonds yielding just below 6 per cent.

In the Netherlands, the picture is again one of sharply rising short-term rates, but here long-term rates have also shown a significant increase since end-November. Three-month local authority rates increased more than 60 basis points in the 3-1/2 months to mid-March, while long-term government yields increased by about 50 basis points.

The interest rate increases in the Netherlands were closely related to domestic inflationary developments and a move toward a policy of credit restriction, although they too had been responsive to the outflow of funds to the Euro-dollar market.

The Netherlands Bank increased its discount rate on December 20, and on December 31 imposed ceilings on bank credit to the private sector. These restrictive credit measures were part of a broader package including tax changes, government expenditure restraints, and a partial price freeze adopted to contain inflation in the domestic economy.

Interest rates in Switzerland have risen during the period under review because of the pull exerted by rising rates in the Euro-dollar market and some national money and capital markets outside Switzerland. After a seasonal easing of the money market in early January, call money rates moved up and reached the very high level of 8-1/2 per cent early in March before dropping back to 7 per cent. The changes in the three-month deposit rate have been less spectacular: after dropping from 4-1/4 to 4 per cent in the second week of January, this rate moved up to 4-3/8 at the beginning of February and to 4-3/4 per cent in mid-March.

Bond yields were quite steady for most of the period but rose somewhat in March, the composite yield on Federal government bonds advancing from 4.40 to 4.55 per cent between February 28 and March 14.

In the fourth quarter, Swiss commercial banks reduced their net foreign assets by \$620 million. They increased them in October and November, and then drew them down sharply in December to meet the year-end currency drain and window-dressing needs. This was done in the usual way by entering into dollar-franc swaps with the Swiss National Bank. In January these swaps were completely unwound.

Almost simultaneously with the British Bank rate increase on February 27, the Bank of Sweden raised its discount rate from 5 to 6 per cent, effective February 28. This increase brought the Swedish discount rate again to the level established in mid-December 1967, when the Swedish currency came under speculative attack in the wake of sterling devaluation. In 1968, the rate had been reduced to 5 per cent in two stages, in February and October.

The most recent changes was prompted by the disparity between Swedish interest rates and market rates elsewhere. Largely as a result of outflows of bank funds attracted to other money markets, Swedish official reserves declined by about \$160 million in the three months November-January. Sweden experienced a \$200 million drain in the comparable period in 1967-68, when the Swedish krona was under selling pressure.

For several months Italy has been experiencing upward pressure on short-term rates arising from the outflow of funds to the Euro-dollar market. The net outflow of private non-bank capital was \$430 million in the fourth quarter, up from \$230 million a year earlier. Commercial banks' net foreign assets increased by \$210 million in December and January, as rising Euro-dollar rates continued to pull funds abroad. This outflow was made easier by a liberalization in December of the Bank of Italy's policy on dollar-lira swaps with commercial banks whereby swaps were permitted for all banks and not just those with net liability foreign positions.

In February, the Bank of Italy became concerned about the magnitude of the outflow and progressively raised the premium on forward lire from 1 per cent to 5 per cent per annum. The Bank of Italy's concern stems from the decline in its external reserves rather than the effect of the capital outflow on domestic credit markets. In February banks stopped adding to their swaps with the central bank because of their high cost, and the banks' net foreign assets actually declined by \$26 million. On March 24, the Bank of Italy took the drastic action of requiring Italian banks to reduce their net foreign assets (presently about \$800 million) to zero by the end of June.

Long-term interest rates, have remained stable for several months, but are likely to experience upward pressure in coming months. The government's program to raise social security pensions will be financed in large part in 1969 by issuing Treasury bonds. Such new issues will amount to 13 per cent of net new issues by government and private borrowers in 1968. In view of the concern in Italy over the unsatisfactory rate of growth, however, the Bank of Italy may try to prevent long-term rates from rising substantially.

Interest rates in Japan have remained virtually unchanged in recent months at a level which until recently was high enough to encourage Japanese importers to borrow abroad. Bank credit expansion has been accelerating, but the country's large balance of payments surplus has provided liquidity to the banking system. Japanese importers are reportedly putting pressure on the authorities to permit more import financing from domestic sources owing to the sharply higher cost of

funds abroad. There are indications that the Bank of Japan and the Ministry of Finance may move in the direction of allowing more yen financing in view of Japan's very healthy external reserve position. Such a move could mean that interest rates in Japan will soon join in the upward trend of rates in other industrial economies. But there are some signs of slackening growth in the economy and it is doubtful that the Bank of Japan would permit a very sharp increase in domestic interest rates.

Short-term interest rates in Canada in mid-March were substantially higher than at end-November reflecting both a move toward monetary restraint by the Bank of Canada, and the apparent capital outflow from Canada during this period. The Bank of Canada raised its discount rate from 6 to 6-1/2 per cent on December 18, and again to 7 per cent on March 3.

The first increase, immediately following the increase in the Federal Reserve's discount rate, signaled a tighter monetary policy in the face of domestic inflation. The Bank of Canada had probably wanted to make such a move for some time, but did not want to attract short-term capital from the U.S. The Federal Reserve's action, plus the relaxation two days earlier of the Canada-U.S. agreement on Canada's official reserve ceiling allowed the Bank of Canada to act.

The March 3 discount rate increase served to bring the rate in line with market rates which had risen partly in response to higher rates abroad. Yields on 91-day Treasury bills increased by some 90 basis points in the 3-1/2 months to mid-March. The gross yield advantage

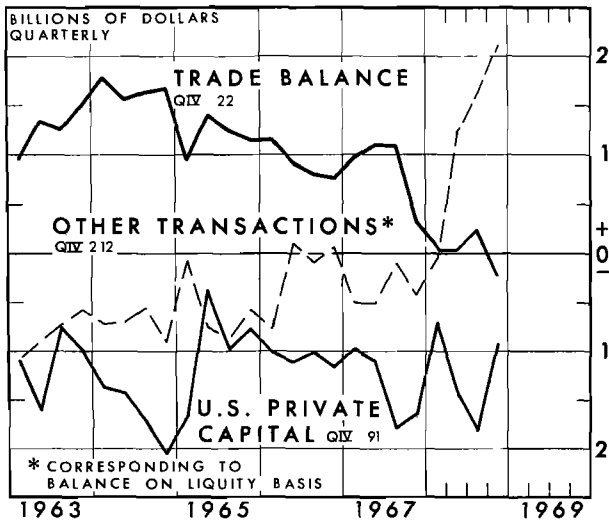
of Canadian bills over U.S. bills increased from nearly nil in February to about 1/2 per cent on March 21. The covered interest arbitrage moved from a few basis points in favor of New York in January to about 50 basis points in favor of Canada in late February and to 109 basis points on March 21.

In contrast to short-term interest rate movements, Canadian long-term rates have increased by only about 20 basis points since end-November, after having risen by over 50 basis points from end-August to end-November. In view of the government's improved budget position and consequently smaller government demands on the capital market for the remainder of this year, long-term rates are not likely to rise substantially over the next few months.

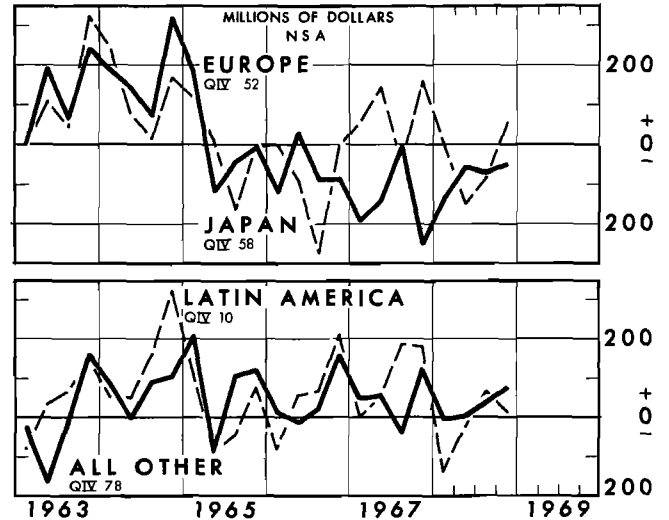
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED

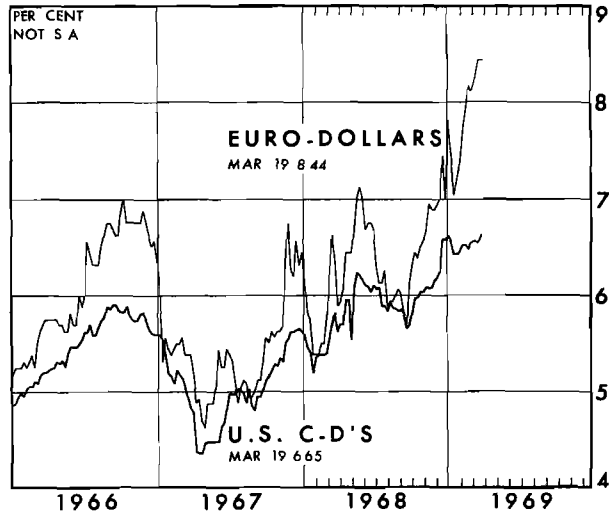
U.S. BALANCE OF PAYMENTS—CONT.



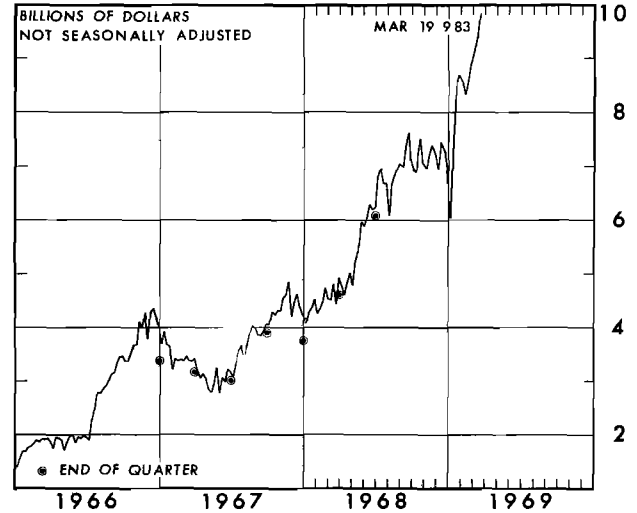
U.S. BANK CREDIT OUTFLOWS



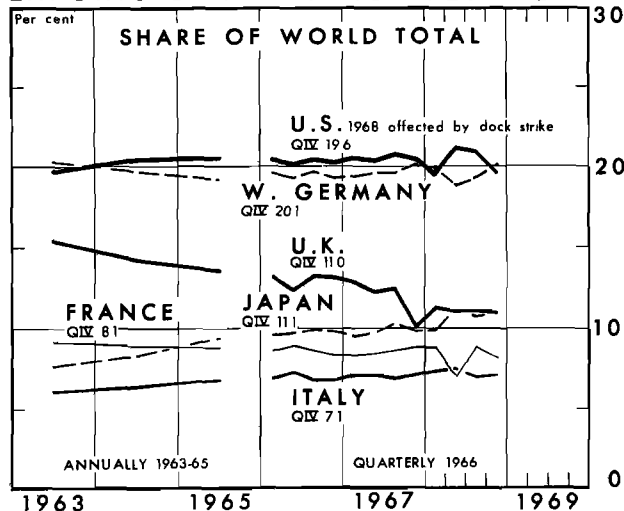
90-DAY RATES



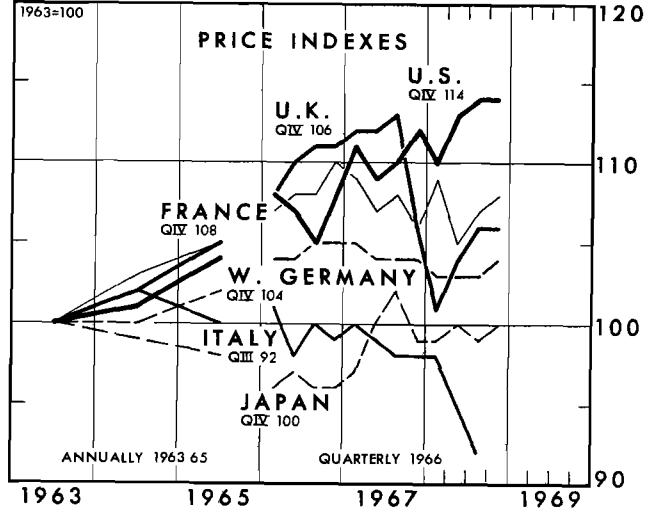
LIAB OF U.S. BANKS TO FOR. BRANCHES



EXPORTS OF MANUFACTURES — I



EXPORTS OF MANUFACTURES — II



APPENDIX A: PROSPECTIVE DEMANDS ON THE MONEY AND CAPITAL MARKETS BY THE
FEDERAL HOME LOAN BANKS AND THE FEDERAL NATIONAL MORTGAGE ASSOCIATION *

A feature of mortgage market developments in recent months has been the high level of commitment activity by the savings and loan associations and the Federal National Mortgage Association. However, the pattern of inflows to the S&L's and the potentially increased pressure on FNMA's resources--should lenders take down their commitments--point to the possibility of substantially increased borrowings by these institutions to meet their commitments over the period ahead. Consequently, the staff estimates that the total new funds required by the Federal Home Loan Banks and the Federal National Mortgage Association may amount to as much as \$3 billion during the next two quarters, of which borrowing would total about \$2 billion, with the balance coming from FHL Bank asset liquidations. The total volume of funds obtained from all sources is about the same as during the last period of credit stringency in 1966.

Savings and Loan Associations

Although experiencing more moderate inflows recently, the savings and loan associations have apparently continued to approve new commitments at an advanced rate. Since June, the seasonally adjusted annual rate of commitments outstanding at all savings and loan associations has increased each month through February, while the monthly volume of loans closed has remained relatively high. (See table in Financial Section of the Greenbook - "Mortgage Market".) The stimulus for such a high rate of new commitments arises in part from the desire of associations to lock-up attractive yields as well as assurance from the Federal Home Loan Bank Board that expansion advances would be granted.

The ability of S&L's to finance current take downs from the backlog of commitments, and to meet some part of future demand, depends of course on the pattern of future net savings inflows--especially during the March-April reinvestment period. If, for example, the S&L's suffer a serious loss of funds in April as a result of depositor withdrawals to meet 1968 income tax payments and to take advantage of higher yielding market securities, the association would be forced to borrow heavily from the Federal Home Loan Banks.

Taking a longer view, our best "guess" is that net inflows from share capital over the second and third quarters--assuming the current level of market yields--will be off about a third from the 1968 pace. With higher market interest rates expected to heighten borrower

* Prepared by Fred Taylor, Economist, Capital Markets Section, Division of Research and Statistics.

reluctance to repay debt ahead of schedule, repayment flows over the same period may total about \$7.2 billion--somewhat below the 1968 rate.

At the projected rate of take downs, S&L's would be required to finance about \$12 billion in new home loans over the next two quarters. If as seems possible, total inflows from savings capital and mortgage portfolios will aggregate no more than \$9.2 billion within the period, and assuming that associations will reduce liquid assets by no more than \$700 million, S&L's would need to borrow a net of over \$2 billion in the next 6 months. At present, the FHL Banks have enough resources to finance at least one-half of the \$2 billion total by liquidating their portfolio assets--mainly short-term bills. Assuming that the FHL Banks do not draw down their resources below \$300 million--the low for 1966--this will leave an additional \$1 billion of net new money to be borrowed.

Federal National Mortgage Association

The Federal National Mortgage Association, which helps to support the government-underwritten home mortgage market through its weekly forward commitment "auction" system, has come under increased demand for its funds over the past several months. Mortgage purchases by FNMA have risen in each month since October as bidders (for the most part mortgage companies) have found it increasingly difficult to obtain commitments for FHA and VA mortgages from other sources. As the volume of FNMA's outstanding commitments have increased, the ratio of takedowns to commitments scheduled to mature has advanced from 65 per cent to more than 96 per cent, the highest since the auction system began in the spring of last year. 1/

Since January, demand for FNMA's new commitments has intensified following the upward adjustment in the FHA and VA ceiling rate to 7-1/2 per cent on January 24, as bidders attempted to lock-up large volumes of FNMA's forward purchase commitments at what they considered to be favorable prices. Since this date, FNMA has raised its average weekly volume of accepted bids in a desire to accommodate the increased demand and to stabilize yields. FNMA's weekly commitment volume was increased to over \$90 million, over a third higher than during the earlier May-December period.

Taking account of the volume of outstanding commitments scheduled for near-term takedown, the recent takedown ratio, projected future offerings, and assuming no significant reduction in market interest rates, FNMA mortgage purchases during the second quarter may

1/ Ratio of takedowns to commitments is the per cent of commitments scheduled to expire during a month that were actually taken down.

average \$180 million a month. An additional \$230 million a month may be acquired during the third quarter. Of the total \$1.1 to \$1.3 billion projected to be taken down within the next two quarters, 80 per cent or nearly \$1.0 billion may have to be financed by issuing additional short-term and longer-term credit instruments. 2/

Table 1
Commitments and Takedown Under the FNMA
"Free Market System"
(millions of dollars)

	New Commitments	Takedowns	Commitment Backlog (End of month)
<u>1968</u>			
May	191.3	--	191.3
June	295.9	8.0	479.2
July	393.7	44.1	817.2
August	232.3	87.1	963.4
September	219.9*	85.6	1,039.1
October	169.8	124.7	1,091.4
November	211.9	130.3	1,166.5
December	289.3*	145.0	1,190.2
<u>1969</u>			
January	240.1	191.4	1,206.2
February	383.4	199.4	1,380.2
March	348.7e	210.0e	1,518.9e

* 5 Auctions were conducted during the month.
e/ Estimated.

Because higher interest rates have discouraged prepayments, FNMA cannot rely on repayments from its portfolio to finance a major portion of its mortgage purchases. In order to help accommodate take downs, FNMA has been issuing short-term discount notes (average maturity is less than three months) purchased primarily by State and local pension and retirement funds. By the end of February, these outstanding notes had increased by over \$1 billion since the end of 1967 and totaled more

2/ The remaining 20 per cent would be financed through FNMA earnings, funds derived through sale of stock, the commitment fees, and mortgage repayments.

than \$2.4 billion--with refinancing averaging nearly \$800 million a month. Although FNMA officials have expressed a desire to concentrate on short-term financing, the volume of current short-term borrowings may force FNMA to issue some long-term debt to cover at least part of any future takedown of commitments now on the books.

Table 2

FNMA DEBT OUTSTANDING
(Billions of Dollars)

End of Quarter	Total (Inc. Treas.)	Treasury	Market		
			Total	Short-term	Long-term
1967 - IV	4.7	--	4.7	1.3	3.4
1968 - I	5.6	.1	5.5	1.6	3.9
II	6.0	.1	5.9	2.0	3.9
III	6.3	.3	6.0	1.9	4.1
IV	6.7	.3	6.4	2.2	4.2
1969 - I (End of Feb.)	6.7	.1	6.6	2.4	4.2

Conclusion

While a somewhat more accurate projection may be made after April, based on the assumptions mentioned above demands for combined market borrowing by the Federal Home Loan Banks and the Federal National Mortgage Association during the second and third quarters of 1969 could total as much as \$2 billion.

As indicated in the first line of Table 3, this is somewhat less than in the similar period of 1966, for two offsetting reasons. First, the FHL Banks, now holding more liquid assets than in 1966, can obtain more of their funds by disposing of these assets in the market. Presumably, the impact of direct borrowing on the market is more than the market impact of bill liquidations; consequently, FHL Bank financing impacts should not affect the market as much as in 1966. On the other hand, FNMA is projected to do all of its borrowing directly, and will thus have a larger market impact than in 1966 when it obtained almost one-half of its funds directly from the Treasury. On balance,

from all sources, the two institutions combined are projected to require as much funds as in the second and third quarter of 1966. Roll-overs of maturing securities will also be about the same as during the previous period.

Table 3

BORROWING DEMAND AND ASSET LIQUIDATIONS OF THE FHL BANKS AND FNMA
(APRIL - SEPTEMBER)
(Billions of dollars)

	TOTAL		FHL BANKS		FNMA	
	1969p	1966	1969p	1966	1969p	1966
Borrowing from Market	2.0	2.2	1.0	1.7	1.0	.5
Borrowing from Treasury	--	.4	--	--	--	.4
TOTAL	<u>2.0</u>	<u>2.6</u>	<u>1.0</u>	<u>1.7</u>	<u>1.0</u>	<u>.9</u>
Asset Liquidations	1.0	.3	1.0	.3	--	--
TOTAL	<u>3.0</u>	<u>2.9</u>	<u>2.0</u>	<u>2.0</u>	<u>1.0</u>	<u>.9</u>

Memo:						
Refinancing	3.1	2.9	2.3	2.9	0.8	--

p/ Projected.