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CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

November 19, 1969

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SUMMARY AND OUTLOOK

Outlook for economic activity

The revised third quarter GNP figures indicate that final sales were weaker but inventory accumulation more rapid than officially estimated earlier. Moreover, business fixed investment expenditures rose faster than first reported. Profits fell significantly for the first time since early 1967. These developments offer further evidence of growing imbalance in key economic sectors, and it seems likely that GNP growth will slow appreciably in the fourth quarter.

Sluggishness in retail sales was again reported in October. With gains in personal income slowing rather sharply, increases in consumer expenditures should continue to be moderate, although some rebound cannot be ruled out. It is also anticipated that industrial production, which has declined for the third month in a row, will drop further as output is adjusted to current sales and inventory developments. Rising unemployment compensation claims through mid-November suggest that the unemployment rate is not likely to recede and will probably go higher before year end. In October, housing starts lost their earlier gains and building permits showed further weakness, tending to confirm the downward trend evident since early this year.

Demands in most sectors of the economy are expected to continue to ease in the first half of next year and bring real GNP growth to a

halt. The current tight credit conditions should be reflected in further deterioration in housing activity and relatively limited growth in capital outlays of State and local governments. Defense expenditures are expected to decline significantly further, consistent with official statements. Slowing employment gains, a declining workweek and reduction in overtime and other premium payments should largely offset the effects on disposable income of the expected reduction in the surcharge and higher social security payments early next year. Consumer expenditures are expected to increase only moderately with durable goods outlays showing little change from current levels.

With respect to business fixed investment, we have assumed that the rate of expansion will moderate progressively over coming quarters, even though new orders for machinery have been relatively large and business equipment output remains high. With economic activity moderating and profits falling, it seems unlikely that plans for capital spending indicated in recent private surveys for the year as a whole will be entirely realized.

It is doubtful that recent rates of inventory accumulation can be maintained for long in the face of weakening demands for goods and high credit costs. We anticipate that stock-building will slow early next year as final demands continue to ease.

Outlook for resource use and prices

Key measures of resource use eased further in October, and prospects are for further slackening well into next year. Industrial production is now expected to decline this quarter and through the first half of next year, though there may be moderate recovery thereafter. The manufacturing capacity utilization rate declined from around 84.5 per cent in the second quarter to 83 per cent in October and, with capacity continuing to grow, the rate is expected to decline further to about 80 per cent by mid-1970.

Indications persist of easing demands for labor. In October, the unemployment rate held near the 4 per cent September level and the manufacturing workweek declined along a broad front. In line with our GNP projection, nonfarm employment is projected to change little in the first half of next year, with manufacturing employment down somewhat, and then to resume a modest expansion. The unemployment rate is expected to continue to drift up irregularly, perhaps reaching the 5 per cent level by the end of next year.

Wage and benefit increases negotiated in major contract settlements have averaged significantly larger this year than last. But fewer workers have been involved, and this has helped to dampen the rise in average hourly earnings. Next year, many more workers will be involved in major contract negotiations. The increase in strike activity this quarter may foreshadow stormy bargaining and more strikes next year as employer resistance hardens under the

pressure of declining profits and as unions press to obtain wage increases to more than compensate for sizable advances in consumer prices. Nevertheless, some dampening of increases in average hourly earnings may be expected next year because of the effects of reduced demands for labor, a shorter workweek and less overtime premium pay, and a firm stance by management.

Continued upward pressure on prices will be exerted by prospective further increases in unit labor costs, as advances in hourly earnings outpace productivity gains, and by efforts to minimize declines in profits. But on balance we look for a moderate deceleration in the pace of price increase over the next year, mainly as a result of reduced demands and ample resource availability.

Among industrial commodities, large inventories and prospectively weaker demands suggest reduced pressure on prices in such key sectors as steel, nonferrous metals, and other materials. At the consumer level, also, the modest nature of further growth in demand combined with overbuilt inventory positions suggest some mild slowing in the price advance for goods. Food supply prospects suggest more or less offsetting changes in food prices this quarter and a relatively small advance in the first half of 1970.

Prospective financial developments

The banking system can be expected to remain under pressure through the turn of the year, as demands for bank credit continue fairly strong relative to the constricted sources of funds available. With outlays for inventories and plant and equipment expected to remain large, and corporate profits and liquidity squeezed, the somewhat larger volume of business borrowing that has developed at banks in recent weeks is likely to persist. If borrowing to pay quarterly income taxes should exceed seasonal proportions, as it may, total business demands for bank credit would show additional strength. Moreover, demands for bank credit are currently being augmented by the need to finance \$2.5 billion of Treasury tax bills just announced for auction on Friday and payment next week.

Given current money market conditions, banks will continue to be hard pressed to meet anticipated customer demands. Although recent trends suggest that total deposits may not be as weak as in the third quarter, there is not much prospect for deposit growth over the fourth quarter as a whole. To meet their loan commitments, therefore, banks on balance will probably have to continue to resort to sizable liquidation of securities and to seek additional non-deposit sources of funds. The extent to which banks will actually utilize commercial paper is somewhat conjectural in view of the Board's proposed regulatory action; hence pressure could focus more on the Euro-dollar market, Federal funds, and the discount window.

Bond markets. Some further near-term increase of bond yields from current advanced levels is a distinct possibility, given the currently weak technical state of corporate and municipal bond markets and the rather sizable calendar of new corporate and municipal offerings over the next few weeks. Dealers' positions in both corporate and municipal markets are still uncomfortably large despite a rash of recent syndicate terminations. The most recent new issues have received generally poor receptions, even though corporate yields have now risen to new records and tax exempt yields are rapidly approaching their earlier highs.

Bond yields may ease off again as markets move into the turn of the year, when new issue volume usually drops off and the availability of investment funds from some types of institutional lenders picks up. Any such tendency would be encouraged if there were significant new indications of a further slowing in the pace of economic activity, particularly since much of the renewed advance of yields recently has apparently resulted from the discrediting of earlier market expectations that monetary policy would soon ease.

At the same time, the likelihood of any sustained drop-off in new issue volume during the early months of 1970 seems limited. While the volume of tax exempt offerings has shrunk a little as yields have backed up again, it has remained well above the lows of last summer. This has apparently reflected both upward adjustments in municipal rate ceilings and the necessitous state to which earlier

deferrals of financing has brought many would-be municipal borrowers. While the immediate bond financing needs of business corporations appear to be less pressing than those of State and local governments, utility-financing demands are expected to remain large for some time, and the queue of industrial corporations planning long-term financing within the next six months to a year is reportedly also sizable. Thus, the potential volume of bond offerings available to brake any significant tendency for bond yields to decline is probably very large.

Mortgage markets. Barring a change in rate ceilings, the savings experience of thrift institutions is likely to continue to deteriorate into 1970. There could be some recovery in net saving flows in November and December, but savings losses are likely to be very large during the vulnerable January reinvestment period. To cover these anticipated losses, as well as the erosion of its own liquidity, the Home Loan Bank System will have to continue to sell substantial amounts of new debt.

Given the bleak outlook for savings growth, thrift institutions are likely to cut back further on new mortgage loan commitments. The ability of FNMA to continue to pump money into the FHA and VA mortgage market may become more limited as discounts deepen and lenders become less willing to originate insured mortgages. Already, the further general advance of capital market yields, and the resulting deepening of discounts on Government underwritten home loans, have forced a slackening in mortgage market activity.

Balance of payments outlook

The scanty information presently available on U.S. external transactions in September, October and the first part of November tends to support the projections of the balance of payments given to the Committee in late October. In particular, the overall deficit on the liquidity basis in the current quarter is likely to show substantial improvement from its average annual rate of over \$10 billion in the first three quarters. Probably an important factor in this improvement will be found to have been a reversal of earlier speculative flows into German marks, directly by U.S. holders or through U.S. direct investment affiliates abroad.

Improvement in the trade balance through September reflected mainly strong foreign demand for U.S. exports, which is expected to persist well into next year. Imports in September were somewhat below the very high August level, but clear evidence of a sharp slowing in the import growth trend such as has been projected is not yet at hand. Some lag in import reaction behind the leveling off in U.S. industrial activity would not be abnormal.

Concern in other industrial countries about inflationary pressures has brought widespread tightening of credit conditions this year and a general rise in interest rates in national money and capital markets. High rates in the Euro-dollar market have contributed to this tendency. (The marked easing of Euro-dollar rates in the latter half

of October proved very short-lived, and has now been completely reversed.) Since demand for capital and credit in most continental European economies and in Japan is likely to continue strong for some time ahead, there is a real danger that large reflows of funds to Europe could develop next year, if and when financial markets in this country turn easier.

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.)	Oct '69	81.5	81.4	78.8	3.4	4.4
Unemployment (mil.)	"	3.2	3.2	2.8	13.0	-3.5
Unemployment (per cent)	"	3.9	4.0	3.6	--	--
Nonfarm employment, payroll (mil.)	"	70.7	70.5	68.4	3.3	6.9
Manufacturing	"	20.2	20.2	19.8	1.8	4.5
Other industrial	"	8.5	8.5	8.2	3.6	5.7
Nonindustrial	"	42.0	41.8	40.4	4.0	8.5
Industrial production (57-59=100)	"	173.3	173.9	166.0	4.4	10.2
Final products	"	171.3	172.1	167.0	2.6	9.1
Materials	"	175.7	175.9	165.7	6.0	11.4
Wholesale prices (57-59=100) ^{1/}	"	114.0	113.6	109.1	4.5	7.4
Industrial commodities (FR)	"	112.8	112.2	108.8	3.7	6.5
Sensitive materials (FR)	"	113.5	113.5	107.9	5.2	12.3
Farm products, foods & feeds	"	114.3	114.3	107.4	6.4	9.8
Consumer prices (57-59=100) ^{1/}	Sep '69	129.3	128.7	122.2	5.8	10.4
Commodities except food	"	118.7	118.2	113.9	4.2	7.9
Food	"	127.5	127.4	120.4	5.9	10.0
Services	"	146.0	145.0	136.0	7.4	13.4
Hourly earnings, mfg. (\$)	Oct '69	3.25	3.24	3.07	5.9	13.6
Weekly earnings, mfg. (\$)	"	131.34	131.79	125.31	4.8	13.3
Personal income (\$ bil.) ^{2/}	"	763.1	760.7	706.2	8.1	19.4
Corporate profits before tax (\$ bil.) ^{2/}	QIII '69	92.4	95.4	91.5	1.0	16.2
Retail sales, total (\$ bil.)	Oct '69	29.4	29.2	28.7	2.3	12.4
Autos (million units) ^{2/}	"	8.4	9.1	9.1	-7.7	10.8
GAF (\$ bil.)	"	8.1	7.9	7.7	5.9	15.0
Selected leading indicators:						
Housing starts, pvt. (thous.) ^{2/}	"	1,342	1,533	1,570	-14.5	-10.3
Factory workweek (hours)	"	40.5	40.8	40.9	-1.0	-0.5
New orders, dur. goods (\$ bil.)	Sep '69	32.2	30.5	28.4	13.4	27.9
New orders, nonel. mach. (\$ bil.)	"	6.1	5.5	5.2	17.4	38.6
Common stock prices (1941-43=10)	Oct '69	95.52	94.51	103.76	-7.9	-0.1
Inventories, book val. (\$ bil.)	Sep '69	162.7	161.7	150.7	8.0	15.2
Gross national product (\$ bil.) ^{2/}	QIII '69	942.8	924.8	876.4	7.6	17.8
Real GNP (\$ bil., 1958 prices) ^{2/}	"	730.6	726.7	712.8	2.5	7.8

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

SELECTED DOMESTIC FINANCIAL DATA

	Week ended	4-week	Last 6 months				
	November 15, 1969		average	High	Low		
Money Market <u>1/</u> (N.S.A.)							
Federal funds rate (per cent)	9.21	8.80	10.18	8.11			
U.S. Treas. bills, 3-mo., yield (per cent)	7.14	7.04	7.14	5.93			
U.S. Treas. bills, 1-yr., yield (per cent)	7.15	7.09	7.41	5.96			
Net free reserves <u>2/</u> (\$ millions)	-939	-968	-349	-1,242			
Member bank borrowings <u>2/</u> (\$ millions)	1,244	1,192	1,634	740.			
Capital Market (N.S.A.)							
Market yields (per cent)							
5-year U.S. Treas. bonds <u>1/</u>	7.44	7.33	7.97	6.40			
20-year U.S. Treas. bonds <u>1/</u>	6.71	6.55	6.77	5.93			
Corporate new bond issues, Aaa <u>8/</u>	8.27	8.02	8.27	7.52			
Corporate seasoned bonds, Aaa <u>1/</u>	7.29	7.28	7.37	6.78			
Municipal seasoned bonds, Aaa <u>1/</u>	5.78	5.79	5.85	5.30			
FHA home mortgages, 30-year <u>3/</u>	--	8.40	8.40	8.05			
Common stocks, S&P composite series <u>4/</u>							
Prices, closing (1941-43=10)	97.07	97.69	105.94	93.19			
Dividend yield (per cent)	3.27	3.25	3.40	3.02			
<hr/>							
	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>	Nov. e	1,850	1,520	445	177		
State & local govt. public offerings	Nov. e	850	900	-171	-555		
Comm. & fin. co. paper (net change in outstandings) <u>6/</u>	Sept. '69	88	1,187	558	698		
<hr/>							
	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)		(per cent)			
Total reserves <u>1/</u>	Oct. '69	27.35	- 0.05	- 0.06	-11.6	- 2.6	- 0.5
Credit proxy <u>1/</u> <u>10/</u>	"	283.5	- 2.2	- 1.5	- 9.2	- 6.4	- 2.8
Bank credit, total <u>6/</u>	"	394.8	+ 0.1	- 0.3	+ 0.3	- 0.9	+ 2.8
Business loans	"	104.2	+ 0.2	+ 0.5	+ 2.3	+ 6.2	+11.6
Other loans	"	168.0	+ 1.6	+ 0.6	+11.5	+ 4.3	+ 6.1
U.S. Govt. sec.	"	53.4	- 1.1	- 1.1	-24.2	-22.6	-16.8
Other securities	"	69.1	- 0.7	- 0.4	-12.0	- 6.8	+ 1.2
Total liquid assets <u>1/</u> <u>6/</u> <u>11/</u>							
Demand dep. & currency <u>1/</u>	"	199.2	+ 0.2	--	+ 1.2	- 0.2	+ 3.9
Time & sav. dep., comm. banks <u>1/</u>	"	193.5	- 0.6	- 1.4	- 3.7	- 8.5	- 3.0
Savings, other thrift instit. <u>6/</u>	"	201.7	- 0.1	+ 0.6	- 0.6	+ 3.6	+ 4.2
Other <u>6/</u> <u>7/</u> <u>11/</u>	"	120.0	- 6.6	- 0.1	-62.6	- 0.7	+ 8.2

N.S.A. - Not seasonally adjusted. S.A. - Seasonally adjusted. e - Estimated.
1/ Average of daily figures. 2/ Average for statement week ending November 12. 3/ Latest figure is monthly average for September. 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 November 16. 10/ Reflects \$400 million reduction in member bank deposits resulting from withdrawal of a large country bank from System membership in January 1969. Percentage annual rates are adjusted to eliminate this break in series. 11/ Reflects \$1.7 billion increase beginning January 1969 in U.S. Government securities maturing within 1 year to conform to the new Budget concept. Percentage annual rates are adjusted where necessary.
r - Revised.

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

	Year	1 II	9 III	6 IV	8	1 I	9 II	6 III ^P	9 Aug. ^P	9 Sept. ^P
Good and services, net ^{1/}	2,516	841	909	301	363	283	n.a.	n.a.	n.a.	
Trade balance ^{2/}	626	264	313	-75	-103	-7	336	90	201	
Exports ^{2/}	33,598	8,395	8,879	8,383	7,469	9,588	9,567	3,250	3,217	
Imports ^{2/}	-32,972	-8,131	-8,566	-8,458	-7,572	-9,595	-9,231	-3,160	-3,016	
Service balance	1,890	577	596	376	466	290				
Remittances and pensions	-1,159	-274	-325	-285	-271	-286				
Govt. grants & capital, net	-3,955	-1,055	-968	-835	-793	-1,103				
U.S. private capital	-5,157	-1,537	-1,868	-947	-1,345	-1,962				
Direct investment	-3,025	-1,009	-1,262	-283	-928	-1,101				
Foreign securities	-1,266	-164	-337	-455	-323	-426	-583			
Banking claims	269	243	-90	-120	78	-473	185			
Other	-1,134	-607	-179	-89	-172	38				
Foreign capital	9,277	2,645	2,515	2,902	3,349	4,340				
Official foreign, nonliquid	2,407	937	433	709	-42	-272				
Official foreign, liquid	-3,099	-2,186	-55	22	-1,132	-578				
Int'l and reg., liq. & nonliq. ^{3/}	235	-97	78	273	96	21				
Foreign private non-bank, liq.	374	103	44	223	-23	-147	-191			
Foreign commercial banks, liq.	3,382	2,297	702	-74	2,959	4,787	1,263			
New direct invest. issues ^{4/}	2,129	585	586	378	401	145				
Other	3,849	1,006	727	1,371	1,090	384				
Errors and omissions	-642	-480	309	-60	-1,254	-973				
Balances, with and without seasonal adjustment (deficit -)										
Official settlements balance, S.A.		1,553	97	367	1,143	1,234	-933			
Seasonal component		-3	-25	-442	567	-29	-107			
Balance, N.S.A. ^{5/}	1,638	1,550	72	-75	1,710	1,205	-1,040	-633	-697	
Liquidity balance, S.A.		9	-139	862	-1,668	-3,850	-2,533			
Seasonal component		96	-269	-124	395	64	-355			
Balance, N.S.A.	168	105	-408	738	-1,273	-3,786	-2,888	-1,170	-469	
Adjusted over-all balance, S.A. ^{6/}		-751	-613	464	-1,824	-3,560	-2,204			
Seasonal component		96	-269	-124	395	64	-355			
Balance, N.S.A.	-1,744	-655	-882	340	-1,429	-3,496	-2,559	-1,058	-303	
Financed by: Liab. to comm. banks abroad, N.S.A. (decrease -)	3,382	2,205	954	-415	3,139	4,701	1,519	425	-394	
Official settlements, N.S.A. ^{7/}	-1,638	-1,550	-72	75	-1,710	-1,205	1,040	633	697	
Reserve changes, N.S.A. (decrease -)										
Total monetary reserves	880	137	571	1,076	48	299	686	259	548	
Gold stock	-1,173	-22	74	137	-56	317	11	10	10	
Convertible currencies	1,183	-267	474	575	73	-246	442	233	398	
IMF gold tranche	870	426	23	364	31	228	233	16	140	

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

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

^{3/} Long-term deposits and Agency securities.

^{4/} New issues sold abroad by U.S. direct investors.

^{5/} 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.

^{6/} Represents the net result of all international transactions of the U.S. other than changes in reserve assets, in all liabilities to foreign monetary authorities and in liabilities to commercial banks abroad (including U.S. bank branches) reported by banks in the U.S.

^{7/} Minus sign indicates decrease in net liabilities.

* Not seasonally adjusted.

THE ECONOMIC PICTURE IN DETAIL

Domestic Nonfinancial Scene

Gross national product. Although business optimism about the longer-run outlook apparently remains firm, there are increasing indications of near-term downward adjustments in activity in response to weakening in demand. Industrial production was off slightly in October for the third month in a row, employment growth has halted in manufacturing, the workweek has declined, and the unemployment rate has been rising irregularly. However, both current and anticipated expenditures for business fixed investment continue strong, although a drop of \$3 billion in corporate profits in the third quarter is expected to contribute to a slower growth in such spending in the future.

In overall terms, the estimated increase in gross national product for the third quarter was revised upward by Commerce from \$17.5 billion to \$18 billion. But final demands were revised down by almost \$1 billion while inventory accumulation was even larger than had been officially estimated earlier. Personal consumption expenditures were revised down sharply, as were estimates of State and local government purchases of goods and services. On the other hand, there was greater strength in business fixed investment than earlier reported. In real terms, third quarter GNP growth was at an annual rate of 2 per cent, about the same as in the preceding quarter.

GNP growth is likely to slow substantially in the current quarter, to about a \$12.5 billion increase. The lift provided by the

Federal pay raise in the third quarter will not be repeated and inventory investment is expected to change little following the sharp increase of the third quarter. A further slackening of demand should also be evident in some key areas. Residential construction activity is expected to decline by an additional \$1 billion in the fourth quarter, under the pressure of sharply curtailed fund availability and high interest rates. Savings outflows from the thrift institutions were large in October, and housing starts, which fell moderately in the third quarter, may well drop more sharply in the fourth quarter as outstanding mortgage commitments are run down. In fact, housing starts declined sharply in October.

In addition, the decline in Federal purchases of goods and services is expected to resume in the fourth quarter under Administration pressure to contain spending within the \$192.9 billion budget ceiling for fiscal 1970. Defense spending is expected to bear the brunt of curtailed outlays, with a decline of about \$1 billion projected in the current quarter. At the State and local levels, restricted credit availability, high interest rates, and legal interest ceilings in some States have forced these governments to curtail both their borrowing and spending. Some resurgence from the unusually low third quarter rate of growth of these expenditures is to be expected as some States raise their interest ceilings and increase taxes, but resumption of the earlier rate of expansion seems unlikely in the absence of a substantial easing of financial constraints.

The persisting weakness of consumer demand has also been a significant factor slowing growth in final demand over recent months. Personal consumption expenditures rose by only \$7 billion in the third quarter, despite a substantial increase in disposable income, as durable goods spending declined. The saving rate rose sharply--by a point and a half--to 6.7 per cent, so that some recovery in consumer demand and decline in the saving rate would seem a logical expectation for the current quarter. However, the initial monthly report on retail sales showed only a slight pickup in October, and auto sales dropped back again after their September post-introduction surge. Moreover, personal income now appears to be on a much less expansive course, thus tending to dampen prospects for any substantial rebound in consumer demand this quarter. Although industrial output of consumer goods is off somewhat, adjustments in production are likely to lag weakening final demand. Thus, inventory accumulation may continue at a relatively high rate, as in the third quarter, but with more of it involuntary.

The near term outlook for new plant and equipment expenditures now appears a little stronger than we had expected. The October McGraw-Hill survey--roughly in line with other recent private surveys--indicates that business is planning an increase of 8 per cent in capital spending for 1970. As a result, we have adjusted up somewhat our projections of plant and equipment expenditures for the fourth quarter and for early next year. But with sales likely to be disappointing and profits declining, and funds still assumed to be scarce and expensive, it seems likely that business investment plans will be revised downward,

particularly if the investment tax credit is removed by year-end. We are therefore projecting a decelerating rate of growth of business investment with these expenditures leveling off by mid-1970. For next year as a whole, we have projected an increase of 6 per cent.

It still appears likely that growth in real GNP in the first half of next year will show little or no gain. Declines in construction activity will probably be extended under the impact of continued monetary restraint, with starts projected to drop to about 1 million units by the second quarter. Financing difficulties are also expected to continue to inhibit the growth of State and local spending, and defense purchases are reported likely to be further curtailed. Growth of disposable income and consumption should be stimulated somewhat by the reduction of the surcharge to 5 per cent which we have assumed for January 1, as well as by an increase in Social Security benefits proposed for the second quarter. But these sources of strength in disposable income are likely to be offset in large part by slow growth of employment and further reductions in the workweek.

Moreover, it does not seem likely that the current rate of inventory accumulation will be maintained much longer, and we expect that inventory investment will begin to slow appreciably by early next year. With growth of real output halting, unemployment should rise significantly and capacity utilization rates decline. The easing of demand pressures should have some effect on the ability of markets to absorb price increases--whether or not cost induced--and a slowing in the rise of the GNP price deflator to under a 3-1/2 per cent rate is projected for the second quarter.

Some rebound in GNP growth seems probably after mid-1970 as residential construction activity begins to recover and inventory investment tends to stabilize. Consumer demand would be supported by the elimination of the remaining 5 per cent surcharge at midyear and by an expected Federal pay increase. Federal expenditures generally are expected to be more stimulative in the second half of next year, and the budget is projected to swing into deficit. Under these circumstances, a resumption of real GNP growth is expected, but perhaps at a rate somewhat less than the expected growth of resources. Further weakening in market receptivity to higher prices could thus result, which, along with some easing in cost pressures, should lead to a further moderation in price increases by the year's end.

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.)

	1968	1969 Proj.	1970 Proj.	1969*			1970*			
				II	III	IV	Projected			
							I	II	III	IV
Gross National Product	865.7	932.9	980.1	924.8	942.8	955.3	962.8	970.8	985.8	1000.8
Final sales	858.4	924.3	974.2	917.9	932.0	945.3	955.5	964.7	980.7	995.7
Private	658.1	709.5	749.9	705.0	715.0	726.0	735.1	743.7	754.3	766.3
Excluding net exports	655.6	707.2	746.4	703.4	712.3	722.6	731.9	740.0	750.8	762.9
Personal consumption expenditures	536.6	575.9	614.2	572.8	579.8	588.8	598.9	609.0	619.7	629.3
Durable goods	83.3	89.7	90.6	90.6	89.8	90.0	90.0	90.0	91.0	91.5
Nondurable goods	230.6	243.9	261.7	242.1	245.1	249.1	254.4	259.5	264.3	268.5
Services	222.8	242.4	261.9	240.1	244.9	249.7	254.5	259.5	264.4	269.3
Gross private domestic investment	126.3	140.0	137.9	137.4	143.3	144.3	140.0	136.8	136.2	138.7
Residential construction	30.2	31.9	26.8	32.7	31.4	30.3	28.2	25.4	25.5	28.0
Business fixed investment	88.8	99.4	105.4	97.8	101.1	103.5	104.8	105.6	105.6	105.6
Change in business inventories	7.3	8.7	5.8	6.9	10.7	10.5	7.0	5.8	5.1	5.1
Nonfarm	7.4	8.4	5.5	6.7	10.3	10.0	6.6	5.6	4.9	4.9
Net exports of goods and services	2.5	2.2	3.6	1.6	2.7	2.9	3.5	4.0	3.5	3.4
Gov't. purchases of goods & services	200.3	214.8	224.3	212.9	217.0	219.3	220.4	221.0	226.4	229.4
Federal	99.5	102.1	100.9	100.6	103.2	102.8	101.2	99.0	101.6	101.8
Defense	78.0	79.3	76.5	78.5	80.3	79.5	77.5	75.0	76.8	76.8
Other	21.5	22.7	24.4	22.1	22.9	23.3	23.7	24.0	24.8	25.0
State & local	100.7	112.8	123.4	112.3	113.8	116.5	119.2	122.0	124.8	127.6
Gross national product in constant (1958) dollars	707.6	728.4	735.7	726.7	730.6	733.2	732.4	732.4	736.1	742.0
GNP implicit deflator (1958=100)	122.3	128.1	133.2	127.3	129.0	130.3	131.5	132.5	133.9	134.9
Personal income	687.9	747.2	796.9	740.5	756.5	767.4	776.8	789.7	804.7	816.2
Wages and salaries	465.0	510.1	545.1	504.3	516.9	525.8	532.1	539.3	550.4	558.6
Disposable income	590.0	629.6	676.1	622.0	639.0	647.1	658.3	668.5	684.3	693.2
Personal saving	38.4	37.7	45.0	33.3	43.1	42.0	42.9	42.8	47.5	46.6
Saving rate (per cent)	6.5	6.0	6.7	5.3	6.7	6.5	6.5	6.4	6.9	6.7
Corporate profits before tax	91.1	93.5	82.8	95.4	92.4	90.5	86.5	82.5	80.5	81.5
Federal government receipts and expenditures (N.I.A. basis)										
Receipts	176.3	201.4	198.1	202.8	201.4	202.9	197.3	198.3	196.6	200.3
Expenditures	181.5	191.7	202.1	189.3	193.6	195.5	196.3	199.3	204.9	208.0
Surplus or deficit (-)	-5.2	9.7	-4.0	13.5	7.8	7.4	1.0	-1.0	-8.3	-7.7
Total labor force (millions)	82.3	84.2	85.4	83.8	84.6	84.8	85.0	85.3	85.6	85.9
Armed forces "	3.5	3.5	3.3	3.5	3.5	3.5	3.4	3.3	3.3	3.2
Civilian labor force "	78.7	80.7	82.1	80.3	81.1	81.3	81.6	82.0	82.3	82.7
Unemployment rate (per cent)	3.6	3.6	4.6	3.5	3.7	4.0	4.2	4.5	4.8	5.0
Nonfarm payroll employment (millions)	67.9	70.1	70.9	70.0	70.4	70.6	70.8	70.8	70.9	71.2
Manufacturing	19.8	20.2	19.9	20.1	20.2	20.2	20.1	19.9	19.8	19.9
Industrial production (1957-59=100)	165.4	172.6	172.7	172.6	174.3	173.2	172.5	172.0	172.8	173.5
Capacity utilization, manufacturing (per cent)	84.5	84.0	79.9	84.5	84.2	82.7	81.2	80.0	79.3	79.0
Housing starts, private (millions A.R.)	1.51	1.48	1.13	1.51	1.43	1.25	1.13	1.00	1.10	1.30
Sales new domestic autos (millions, A.R.)	8.62	8.44	8.51	8.54	8.45	8.40	8.40	8.40	8.50	8.75

* Assumes Administration's proposals for repeal of investment tax credit and extension of tax surcharge at 10% through 1969 and then at 5% through June 1970.

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1968	1969 Proj.	1970 Proj.	1969 *			1970 *			
				II	III	IV	Projected			
				I	II	III	IV			
-----In Billions of Dollars-----										
Gross National Product	72.2	67.2	47.2	16.1	18.0	12.5	7.5	8.0	15.0	15.0
Inventory change	-0.1	1.3	-2.7	0.3	3.8	-0.2	-3.5	-1.2	-0.7	0.0
Final sales	72.2	65.9	49.9	15.8	14.1	12.8	11.0	9.2	15.7	15.0
Private	52.0	51.4	40.4	12.9	10.0	10.5	9.9	8.6	10.3	12.0
Excluding net exports	54.7	51.6	39.2	12.8	8.9	10.3	9.3	8.1	10.8	12.1
Net exports	-2.7	-0.2	1.2	0.1	1.1	0.2	0.6	0.5	-0.5	-0.1
Government	20.2	14.5	9.5	2.9	4.1	2.3	1.1	0.6	5.4	3.0
GNP in constant (1958) dollars	33.0	20.8	7.3	3.6	3.9	2.6	-0.8	0.0	3.7	5.9
Final sales	33.3	19.8	9.8	3.5	0.6	2.7	2.2	0.6	5.1	5.6
Private	24.9	18.3	10.8	3.9	1.4	2.6	2.7	1.8	3.9	4.6
-----In Per Cent Per Year-----										
Gross National Product	9.1	7.8	5.1	7.1	7.8	5.3	3.1	3.3	6.2	6.1
Final sales	9.2	7.7	5.4	7.0	6.1	5.5	4.7	3.9	6.5	6.1
Private	8.5	7.8	5.7	7.5	5.7	5.9	5.5	4.7	5.5	6.4
Personal consumption expenditures	9.0	7.3	6.7	7.7	4.9	6.2	6.9	6.7	7.0	6.2
Durable goods	14.1	7.7	1.0	10.0	-3.5	0.9	0.0	0.0	4.4	2.2
Nondurable goods	7.2	5.8	7.3	5.9	5.0	7.5	7.5	8.0	7.4	6.4
Services	9.1	8.8	8.0	8.7	8.0	7.8	7.7	7.9	7.6	7.4
Gross private domestic investment	8.9	10.8	-1.5	6.5	17.2	2.8	-11.9	-9.1	-1.8	7.3
Residential construction	20.8	5.6	-16.0	-7.2	-15.9	-14.0	-27.7	-39.7	1.6	39.2
Business fixed investment	6.1	11.9	6.0	10.5	13.5	9.5	5.0	3.1	0.0	0.0
Gov't. purchases of goods & services	11.2	7.2	4.4	5.5	7.7	4.2	2.0	1.1	9.8	5.3
Federal	9.7	2.6	-1.2	-3.9	10.3	-1.5	-6.2	-8.7	10.5	0.8
Defense	7.7	1.7	-3.5	-2.5	9.2	-4.0	-10.1	-12.9	9.6	0.0
Other	16.8	5.6	7.5	-8.9	14.5	7.0	6.9	5.1	13.3	3.2
State & local	12.8	12.0	9.4	14.0	5.3	9.5	9.3	9.4	9.2	9.0
GNP in constant (1958) dollars	4.9	2.9	1.0	2.0	2.1	1.4	-0.5	0.0	2.0	3.2
Final sales	5.0	2.8	1.4	2.0	0.3	1.5	1.2	0.3	2.8	3.1
Private	4.7	3.3	1.9	2.8	1.0 ^{1/}	1.8	1.9	1.2	2.7 ^{2/}	3.2
GNP implicit deflator	4.0	4.7	4.0	5.1	5.6	3.9	3.6	3.3	4.1	2.9
Personal income	9.3	8.6	6.6	8.9	8.6	5.8	4.9	6.6	7.6	5.7
Wages and salaries	9.8	9.7	6.9	8.9	10.0	6.9	4.8	5.4	8.2	6.0
Disposable income	8.0	6.7	7.4	7.7	10.9	5.1	6.9	6.2	9.5	5.2
Corporate profits before tax	13.4	2.6	-11.5	0.4	-12.6	-8.2	-17.7	-18.5	-9.7	5.0
Federal government receipts and expenditures (N.I.A. basis)										
Receipts	16.7	14.2	-1.6	8.5	-2.8	3.0	-11.0	2.0	-3.4	7.5
Expenditures	10.8	5.6	5.4	1.7	9.1	3.9	1.6	6.1	11.2	6.1
Nonfarm payroll employment	3.0	3.2	1.1	2.9	2.3	1.1	1.1	0.0	0.6	1.7
Manufacturing	2.1	2.0	-1.5	0.0	2.0	0.0	-2.0	-4.0	-2.0	2.0
Industrial production	4.6	4.4	0.1	5.6	3.9	-2.5	-1.6	-1.2	1.9	1.6
Housing starts, private	16.7	-2.1	-23.3	-48.3	-21.5	-50.9	-39.1	-44.4	40.0	72.7
Sales new domestic autos	14.0	-2.1	0.8	8.4	-4.2	-2.5	0.0	0.0	4.8	11.8

* Assumes Administration's proposals for repeal of investment tax credit and extension of tax surcharge at 10% through 1969 and then at 5% through June 1970.

^{1/} Excluding Federal pay increase 4.3 per cent.

^{2/} Excluding Federal pay increase 3.1 per cent.

Industrial production. Industrial production edged off further in October and, at 173.3 per cent of the 1957-59 average, was down 0.4 per cent from September and 0.7 per cent from the July peak. The October decline reflected strikes in the automotive and electrical machinery industries as well as further declines of output for some other durable and nondurable goods.

Auto assemblies in October were at a seasonally adjusted annual rate of 8.4 million units, down 4 per cent from September. Production schedules for November and December are now posted at an annual rate of 8.2 and 7.6 million units, respectively. Output of home goods and apparel declined further as production of furniture, television sets (not due to the GE strike), some appliances, and apparel was curtailed. Output of consumer staples, however, changed little.

Revised data now indicate that output of business equipment rose to a new high in September. While production of electrical apparatus in October was curtailed by the GE strike, this was offset by a rise of output in other equipment industries.

Among industrial materials, production of steel and chemicals changed little in October, but output of textiles, paper, and some rubber products declined.

While the decline in the total index since July has been moderate--0.7 per cent--readjustments in output in a number of industries have been substantial.

PER CENT DECLINES IN SELECTED INDUSTRIES
From 1969 Highs

	Month of 1969 high	Per cent declines from 1969 high to October
Finished goods		
Autos	July	-8.2
Apparel	July	-5.0
Furniture, household	June	-4.7
Misc. home goods	June	-4.4
Defense equipment	May	-4.0
Materials		
Textiles	June	-3.7
Mining	June	-3.1
Construction materials	March	-3.0
Paper	August	-2.5
Rubber	August	-2.1
Industrial chemicals	July	-1.7

The declines listed above have been largely offset by increased output in some industries, such as business equipment, equipment parts for further processing, and electric and gas utilities. Moreover, output has leveled off in other industries, such as consumer staples, steel, and miscellaneous business supplies. Also, among some of the industries showing declines, the initial drop has been followed by little change in production in recent months. If this mixed pattern of change continues as industries adjust production to the high level of stocks and sluggish sales, the total index will probably decline somewhat further for the balance of the year.

Retail sales. Retail sales in October rose about 1/2 per cent from September, according to the initial monthly report, but the

level was no higher than in June and was only 2.3 per cent above a year earlier. In real terms, October apparently was the fifth month in a row in which sales were below year-earlier levels.

Sales of nondurable goods stores increased 1-1/2 per cent from September as all major types of stores reported larger volume. Department stores, which had been among the weakest groups in September, increased the most in October. Sales of durable goods stores declined 2 per cent, with the automotive group off 3 per cent.

September 1969 retail sales figures were revised downward by an unusually large amount, largely as a result of a change in the seasonal factor for the automotive group. The seasonal revision produced an even larger downward revision in the sales of the automotive group in September 1968, however, so that the recorded year-over-year gain was widened to 6.6 per cent.

Dealer deliveries of new domestic autos in the first 10 days of November advanced significantly from the October seasonally adjusted annual rate of 8.4 million units. Early November sales were still well below the rate of late September which reflected the new model introductions.

Stocks of new autos showed a seasonally adjusted increase of 5 per cent for the month of October to a level of 1.4 million units. This was equivalent to a seasonally adjusted stock/sales ratio of 61 days' supply--about the highest on record.

A spokesman for the Automobile Manufacturer's Association has stated that 10-day sales and stocks figures will no longer be

reported. In this event, this information will be available only on a monthly basis, probably four or five days following the end of the month.

Consumer credit. Consumer instalment credit outstanding rose at a seasonally adjusted annual rate of \$8.4 billion in September, after 2 months of relatively modest gains. The earlier sales dates for 1970 model autos may have exaggerated the increase in September this year. The expansion for the third quarter as a whole was at a \$7.7 billion annual rate, compared with a \$9 billion rate in the first half of the year and with a \$10 billion rate in the second half of last year.

Instalment credit extensions declined slightly from August to September as reductions in nonautomotive consumer goods and personal loans more than offset a sizable increase in extensions for auto purchases. Repayments fell moderately but were higher than in any other month except August.

NET CHANGE IN CONSUMER INSTALMENT CREDIT OUTSTANDING
(Billions of dollars, seasonally adjusted annual rates)

	Total	Automobile	Other consumer goods	Personal loans	Home repair and modernization
1968 - QI	\$ 7.0	\$2.8	\$1.9	\$2.4	\$ 0
QII	8.4	3.0	2.8	2.4	.1
QIII	10.0	3.9	2.6	3.3	.2
QIV	10.2	3.8	2.7	3.5	.2
1969 - QI	8.3	2.7	2.5	3.0	.2
QII	9.6	3.1	2.9	3.2	.4
QIII	7.7	1.9	2.6	3.1	0

Census consumer buying expectations. The October survey of consumer buying expectations suggests no substantial change in the conservative pattern of household expenditures which has prevailed since late 1968. The probability of a household purchasing a new car has declined since July and suggests that total dealer sales of new cars in the fourth and first quarters may average slightly less than from July to October of 1969. After rising sharply in the second quarter, the prospect of a household buying a house, either new or used, dropped back in the third quarter to the year earlier level. Income expectations were also less optimistic than in July, although still better than a year earlier.

Buying plans for furniture and appliances^{1/} were the only area to show improvement, and this anticipated gain is somewhat surprising in view of house purchase plans and the lower percentage of households planning to make major expenditures on home improvements. In the past, consumer surveys have been least reliable in foreshadowing developments in furniture and appliance sales.

CHANCE IN 100 OF BUYING WITHIN 6 MONTHS
(Seasonally adjusted)

	1967	1968	1969			
	October	October	January	April	July	October
Any car	8.7	8.9	9.0	9.4	9.4	9.2
New car	4.3	4.6	4.3	4.5	4.7	4.3
Any house	3.5	3.3	3.3	3.9	3.7	3.3
New house	1.7	1.5	1.6	1.8	1.7	1.4

Addendum:

Per cent of households reporting probably expenditures for:

Furniture & carpets	26.0	25.4	25.2	26.9	25.3	28.0
Major expenditure on home improvements	6.5	7.1	8.1	9.5	8.5	7.7

^{1/} Major appliances and TV's are not included in the table.

Inventories. Total business inventory accumulation in the third quarter is now estimated at a \$10.7 billion annual rate (GNP basis), higher than first reported and significantly more than the \$7 billion rate in the first half of the year. Inventory-building was substantial throughout the quarter at both manufacturing and retail establishments. The increase in retail auto stocks was particularly sharp in the third quarter.

INVENTORY RATIOS

	1966		1969	
	November	December	August	September
<u>Inventories to sales:</u>				
Manufacturing & trade, total	1.54	1.56	1.54	1.54
Manufacturing, total	1.69	1.72	1.70	1.67
Durable	1.95	2.00	2.00	1.96
Nondurable	1.38	1.37	1.31	1.30
Trade, total	1.38	1.39	1.37	1.38
Wholesale	1.21	1.22	1.18	1.17
Retail	1.49	1.51	1.51	1.53
Durable	2.10	2.10	2.16	2.14
Automotive	1.68	1.67	1.74	1.72
Nondurable	1.20	1.23	1.22	1.24
Manufacturing and retail inventories to retail sales:				
Home goods & apparel (G.A.F.)	3.50	3.54	3.53	3.60
Consumer staples	1.62	1.65	1.57	1.60
<u>Inventories to unfilled orders:</u>				
Durable manufacturing	.63	.64	.72	.72

Orders and sales increased in September at manufacturers and wholesalers, and their inventory ratios dropped back; however, durable manufacturing inventories remain at an advanced level relative to sales

and to order backlogs, mainly in the defense products industries. Inventory-building may continue at durables industries, particularly machinery and equipment, but recent employment cutbacks at defense products industries, including aircraft, suggest that a slowdown in accumulation may be near in this sector.

The downward revision of September retail sales brought the retail inventory-sales ratio clearly above the high level of late 1966. Auto inventories remained high relative to sales in September and were even higher relative to October's reduced sales rate. Stocks of other cyclical consumer goods (home goods and apparel) at factories and retail outlets are high and rising relative to retail sales.

Construction and real estate. Seasonally adjusted new construction outlays, which were revised upward for August and September, apparently edged higher in October to a record annual rate of \$93.1 billion. All of the year-to-year advance reflected increased costs; in physical volume, the October rate was about 4 per cent below the high reached last January.

While private residential construction outlays in current dollars rose further in October, they were no higher than a year earlier and appreciably under the peak reached last March. Private nonresidential expenditures apparently remained at the record rate achieved in September after a five-month rise.

Public construction outlays--already at a new high--continued to increase in October, according to initial Census Bureau projections.

However, the estimates for State and local outlays may be somewhat overstated for this period, judging by the most recent Federal Reserve Board survey of State and local Government borrowing and expenditures. The results of this survey, which will be summarized in the Supplement, suggest that developments in financial markets had already begun to have substantial impact on outlays of such Governmental units by the third quarter. Moreover, according to "Engineering News-Record," about half the states are reported to have pledged some reduction in future projects in response to Federal Government requests to help minimize pressures on available resources under prevailing inflationary conditions.

NEW CONSTRUCTION PUT IN PLACE
(Confidential FRB)

	October 1969 (\$ billions) ^{1/}	Per cent change from	
		September 1969	October 1968
Total	93.1	+1	+ 6
Private	62.9	+1	+ 6
Residential	29.7	+2	--
Nonresidential	33.2	--	+13
Public	30.2	+1	+ 6
Federal	3.4	+2	- 3
State and local	26.8	+1	+ 7

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

Seasonally adjusted private housing starts, which had turned sharply upward in September, reversed direction by more than a tenth in October and resumed their downtrend as expected. The annual rate of 1.34 million in October was the lowest for any month in nearly two years.

Both single-family and apartment units shared in the drop, which was most pronounced for apartments. Regionally, starts rose only in the Northeast states.

PRIVATE HOUSING STARTS AND PERMITS

	October 1969 (Thousands of units) <u>1/</u>	Per cent change from	
		September 1969	October 1968
Starts	1,342	-12	-15
1-family	765	- 9	-21
2-or-more-family	577	-16	- 5
Northeast	167	+ 8	-23
North Central	284	-24	-29
South	523	-15	-27
West	368	- 4	+13
Permits	1,119	- 7	-19
1-family	563	--	-19
2-or-more-family	556	-13	-19

1/ Seasonally adjusted annual rates; preliminary.

Building permits continued to decline in October and reached the lowest rate since early 1967. Given this development and the sustained downward pressure on mortgage commitment activity, a further sharp drop in starts is suggested for November, possibly to somewhat below a 1.2 million unit rate. For the quarter as a whole, however, starts may still average about a 1.25 million annual rate, compared with a third quarter average now reported at 1.43 million.

Seasonally adjusted sales of new homes by merchant builders in September were the lowest since early 1967. Although the number of

new homes available for sale changed little, it reached a relatively high 6.6 million supply at the currently reduced level of sales. Median prices of homes not yet sold continued to rise in September and, at \$26,200, were about 7 per cent more than a year earlier. Sales of existing homes have also apparently slackened in recent months, with prices of such homes continuing about a tenth above a year earlier.

Plant and equipment spending. Business spending on new plant and equipment is projected to increase by 8 per cent next year following an 11 per cent increase in 1969, according to the McGraw-Hill survey taken in October. These results are generally in line with those reported earlier by two other private surveys. Because capital goods prices are expected to rise by 7 per cent, the McGraw-Hill survey suggests that in real terms investment would grow only 1 per cent compared with an increase of 5 per cent estimated for 1969. The Commerce-SEC survey covering spending plans for early 1970 will be available in early December.

PLANT AND EQUIPMENT SPENDING

	Billions of dollars			Per cent change	
	1968 Actual	1969 Estimated	1970 Planned*	1968- 1969	1969- 1970
All business	64.08	70.85	76.71	10.6	8.3
Manufacturing	26.44	29.68	32.26	12.3	8.7
Durable goods	13.51	15.43	16.49	14.2	6.9
Nondurable goods	12.93	14.25	15.77	10.2	10.7
Nonmanufacturing	37.64	41.17	44.45	9.4	8.0
Mining	1.42	1.56	1.73	10.2	10.9
Railroad	1.34	1.47	1.10	9.8	-25.2
Non-rail transportation	4.31	4.52	5.31	4.9	17.5
Public utilities	11.54	12.74	14.18	10.4	11.3
Communication	6.36	7.55	8.00	18.7	6.0
Commercial and other	12.67	13.33	14.13	5.2	6.0

* McGraw-Hill October 1969 Survey.

Percentage increases in spending by manufacturing industries are projected to be about the same as in nonmanufacturing industries, both taken as a group. Within manufacturing, relatively large increases are planned by the shipbuilding, electrical and nonelectrical machinery, instruments, food, chemicals, and petroleum industries. Iron and steel, rubber, and textile producers are scheduling declines in new investment. In non-manufacturing, airlines are planning the largest percentage increase--nearly one-third--as they begin buying the new 747 jumbo jets; railroads are planning to cut spending by 25 per cent.

The McGraw-Hill Survey also reported that manufacturers as a group expect that their 1970 sales in terms of physical volume will be up 6 per cent from this year and that prices of their products will be up 3 per cent. If sales should deviate greatly from these expectations, investment outlays might be adjusted to reflect the changes in outlook.

The McGraw-Hill Survey in the past has provided a valuable early look at the direction of investment plans for the next year. But the record has been less accurate in assessing the magnitudes of change, especially in periods when activity levels were changing. In years of slowing economic activity, reported spending plans have tended to overstate actual spending, and in years of rising output the survey has tended to understate actual outlays. In the four years of declining output for which the survey results are available they have overestimated the change by an average of 5 percentage points while indicating the right direction in each case. Part of this error undoubtedly stems from the timing of the survey. Many investment plans are not formally ratified by boards of directors until late in the fourth quarter so that what is reported in October frequently represents preliminary plans which remain subject to change.

Labor market. Signs of easing labor demand continue to emerge in the volatile industrial sector. Although total nonfarm employment rose by nearly 200,000 in October, employment moved down somewhat in both construction and manufacturing--where the level was about the same as in June--while the factory workweek fell appreciably.

The unemployment rate showed little net change in October--edging down to 3.9 per cent--thus tending to confirm the step-up to the 4 per cent order to magnitude reported for September. A progressive rise in joblessness has been apparent since late in the first quarter. Insured unemployment also has been rising, with the most recent two weeks showing a year-over-year increase of more than 10 per cent in the number of persons receiving unemployment compensation.

UNEMPLOYMENT RATES
(Seasonally adjusted)

	IQ	IIQ	IIIQ	October
Total	3.3	3.5	3.7	3.9
Men, aged 20 and over	1.9	2.0	2.2	2.4
Women, aged 20 and over	3.5	3.7	3.9	4.0
Teenagers	12.1	12.3	12.6	13.0

The bulk of the increase in nonfarm payroll employment in October was in trade and services. Growth in these sectors is often erratic, but even with the larger employment increase of October the

average monthly rise of nonindustrial employment has been noticeably slower since March than it was in the first quarter. The additional slowing of total employment growth since June reflects a decline in construction and a leveling off in manufacturing.

NONFARM PAYROLL EMPLOYMENT
(In thousands, seasonally adjusted)

	1969 average monthly changes		
	December- March	March- June	June- October
Total	278	197	93
Government	33	42	11
Private industry	245	154	82
Construction	15	31	-15
Manufacturing	55	25	-2
All others	175	98	99

Manufacturing employment edged down in October, reflecting small declines in a number of individual industries, and the earlier September employment estimate was revised downward. Exclusive of the auto industry, where the early model changeover this year has confused the monthly movements, manufacturing employment has been on a plateau since June and the average workweek has been moving irregularly lower since last winter. The average workweek fell 0.3 hour to 40-1/2 hours in October, as compared with this year's high of 40.9 hours in March. The drop in average hours reflects small declines in almost all individual industries, while employment increases were few in

number and small in size. Thus, only a few of the manufacturing industries now show signs of continued gains in manhours of work. The G.E. strike did not influence the employment estimate for October because it began late in the month, but it will have an impact on the November estimates of employment and income.

Personal income. In October, personal income rose by only \$2-1/2 billion, or only about half as much as the average from January to August. The smaller growth in October was primarily a result of the reduction of average hours in manufacturing, where gross wage and salary payments were down slightly for the first time in 18 months. The expansion of private nonmanufacturing payrolls continued near the June-September average as employment and hourly earnings rose at about the same rate as over the summer. The October increase in Government payrolls was an outgrowth of hiring in State and local units; in the summer, Government payroll increases had been swelled by the Federal pay raise.

Income flows from dividends, interest and rent were not dramatically different in October than over the summer. Farm income continued about steady for the fourth successive month after a strong run-up earlier in the year.

PERSONAL INCOME
(Billions of dollars, seasonally adjusted)

	1969 average monthly changes			
	December- March	March- June	June- September	September- October
Personal income	4.9	5.1	4.9	2.4
Wage & salary disbursements	4.0	3.5	3.8	1.6
Government	0.5	0.5	1.4	0.5
Private	3.5	3.0	2.4	1.1
Manufacturing	1.0	1.0	1.0	-0.2
Nonmanufacturing	2.5	2.0	1.4	1.4
Other sources of income	0.8	1.7	0.9	1.1

Note: Totals may not add due to rounding.

Wages and industrial relations. Increased collective bargaining activity in the months ahead appears likely to intensify wage pressures. Thus far in 1969 growth in compensation per manhour in the private nonfarm economy has averaged slightly less than in 1968, largely because of the reduction in collective bargaining and the smaller impact in 1969 than in 1968 of the statutory increases in minimum wages. Only two million workers were covered by major collective bargaining settlements negotiated in the first nine months of this year compared with four million in the same period of 1968. Thus, the number of workers receiving large first-year pay increases declined, while the number of workers receiving deferred--usually smaller--increases rose. This redistribution of relative weights resulted in some abatement of upward pressures on average wages.

At the same time, however, wage increases provided in newly negotiated contracts have continued very large. First-year wage increases

negotiated in major collective bargaining agreements in private nonfarm industries averaged 8 per cent in the first nine months this year compared with a little over 7 per cent for the same period last year. Much of the upward push came from the substantial increases negotiated in construction, where median first-year wage increases covering nearly 300,000 workers were over 16 per cent. During this period, there were relatively few key settlements in manufacturing, where first-year wage increases averaged about 7 per cent compared to 10.4 per cent in non-manufacturing activities inclusive of construction, and an estimated 8 per cent exclusive of both construction and manufacturing.

WAGE CHANGES IN MAJOR COLLECTIVE BARGAINING SETTLEMENTS
(Annual rate of increase, per cent)

	Settlements concluded during:			
	Full year			1st 9 months
	1966	1967	1968	1969
First-year increases:	<u>4.8</u>	<u>5.7</u>	<u>7.2</u>	<u>8.0</u>
Manufacturing	4.2	6.4	6.9	6.9
Nonmanufacturing	5.0	5.0	7.5	10.4
Changes over life of contract:	<u>3.9</u>	<u>5.0</u>	<u>5.2</u>	<u>6.6</u>
Manufacturing	3.8	5.1	4.9	5.5
Nonmanufacturing	3.9	5.0	5.9	8.5

The strike of 147,000 General Electric workers called on October 27 continues. So far, G.E.'s policy of standing by its original offer (6 per cent in the first year with wage reopenings) has resulted in a stalemate and there are still no signs of movement toward

a settlement. In a related situation, Westinghouse employees have agreed to extend their contract on a day-to-day basis, but one local walkout has occurred and others may follow.

Shopcraft railway unions have turned down the recommendations of the Presidential Emergency Board so that the possibility remains of a strike upon expiration of the 60-day cooling off period December 3. If these workers elect to strike, it probably would involve three or four railroads and trigger an industry-wide lockout, thus shutting down the Nation's railroads. This, in turn, might lead the President to request special Congressional intervention. At year's end, other railroad contracts involving about 400,000 workers are expected to be reopened, and the unions reportedly are planning to ask for 12 to 15 per cent pay boosts.

The strike at American Motors over local issues continues, although the overall one-year contract covering economic issues has been settled. The contract reportedly provides a 6 per cent wage and cost-of-living increase, and a considerable "catch-up" on fringe benefits; such a settlement for this company can not be considered a pace-setter for the auto industry, where most contracts come up for renegotiation next September.

Wholesale prices. Wholesale prices rose 0.4 per cent from mid-September to mid-October as a result of an increase of 0.5 per cent in average industrial prices--the largest monthly rise since February--and little change in farm and food products. Recent price

announcements on increases in industrial prices, while numerous, do not give the impression of having the over-all importance of changes in recent months and suggest the possibility of a reduced rate of increase in the November index.

The rise of 3.2 per cent in new car prices accounted for about one-third of the increase in average industrial prices in October, although increases occurred in more than one-half of the product classes. Excluding passenger cars, the rise was about in line with the third quarter average rise for industrial commodities and below September's increase.

WHOLESALE PRICES
(Percentage changes at annual rates)

	Dec. 1968	1969		
	to March 1969	Mar.-June	June-Sept.	Sept.-Oct.
All commodities	6.8	5.2	1.6	4.8
Industrial commodities	6.4	0.8	3.6	6.0
Materials	8.4	0.4	4.4	3.6
Steel mill products	9.6	4.0	9.6	9.6
Nonferrous metals	20.8	17.2	23.6	10.8
Lumber and plywood	61.2	-78.4	-28.0	- 7.2
Products	2.8	2.4	2.8	8.4
Food and foodstuffs	9.2	18.8	- 4.4	- 1.2

Increases for metals and for machinery and equipment together accounted for about two-fifths of the October increase in industrial prices, with price advances for aluminum ingot, aluminum and copper mill shapes, and steel mill products, and for construction and metal working machinery. Important increases also were reported

for apparel and automobile tires. Lumber prices continued to decline for the sixth consecutive month although plywood rose further.

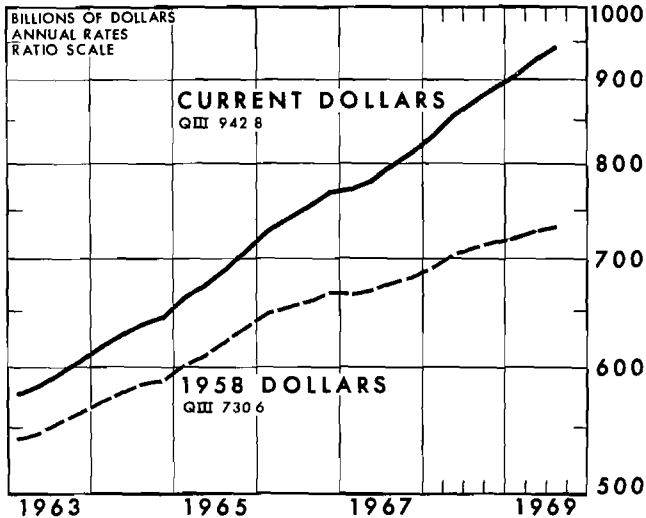
Farm and food products were expected to decline seasonally in October by about 1 per cent, but the index showed little change as many offsetting movements occurred. Hog prices rose, but cattle prices continued down and meats and fresh fruits were lower.

If the 6 per cent increase in railroad freight rates authorized by the ICC for November 18 is stands--as seems likely--it will add to the costs of such bulk-shipped commodities as coal, grain, steel, scrap and also of many other items. The over-all contribution of the railroad industry to the GNP has been declining and in 1968 was only about 1.8 per cent. However, 3.2 cents on every dollar of the inputs of the steel industry represented rail transport costs in 1968. The 6 per cent increase is expected to add about \$600 million to gross revenues of the industry.

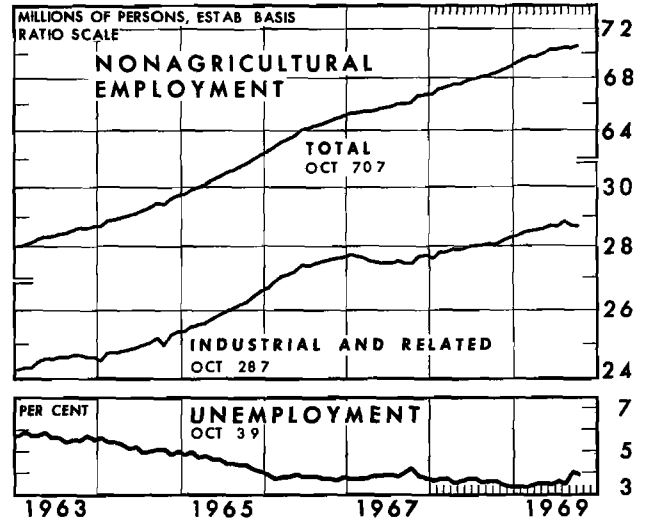
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

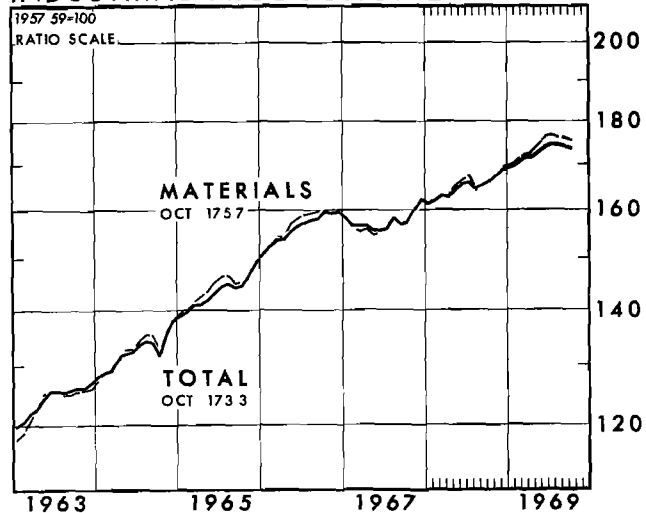
GROSS NATIONAL PRODUCT



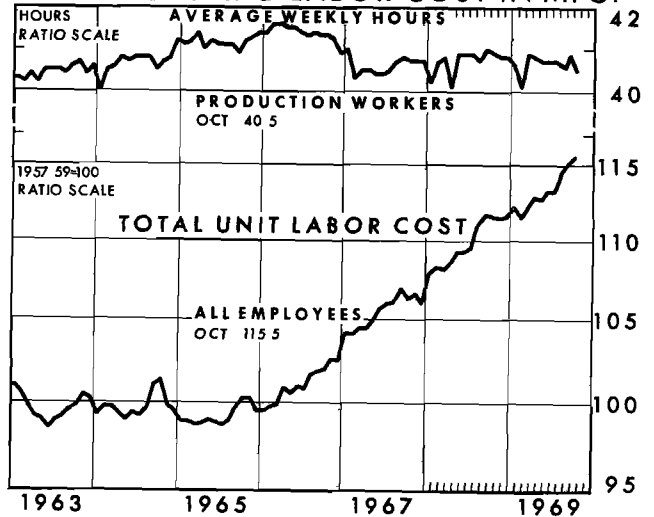
EMPLOYMENT AND UNEMPLOYMENT



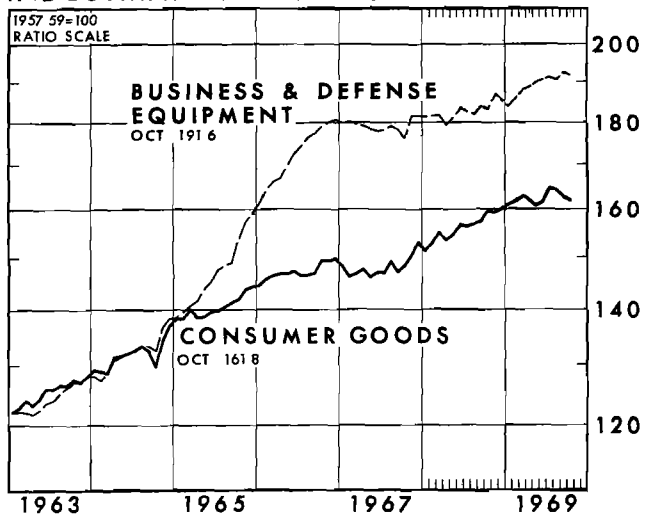
INDUSTRIAL PRODUCTION-I



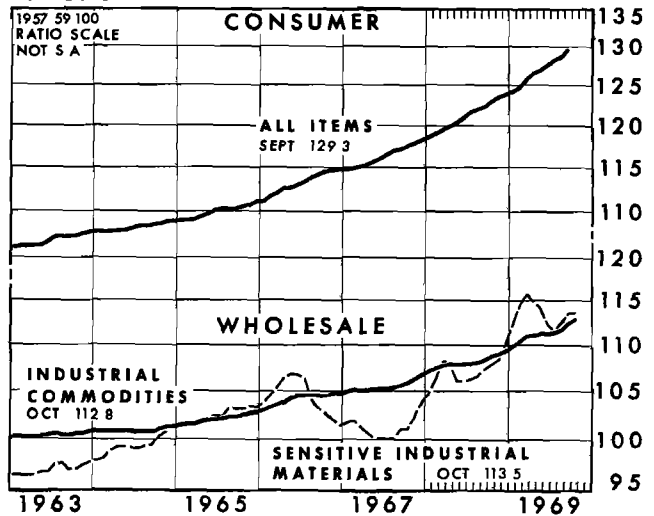
WORKWEEK AND LABOR COST IN MFG.



INDUSTRIAL PRODUCTION-II



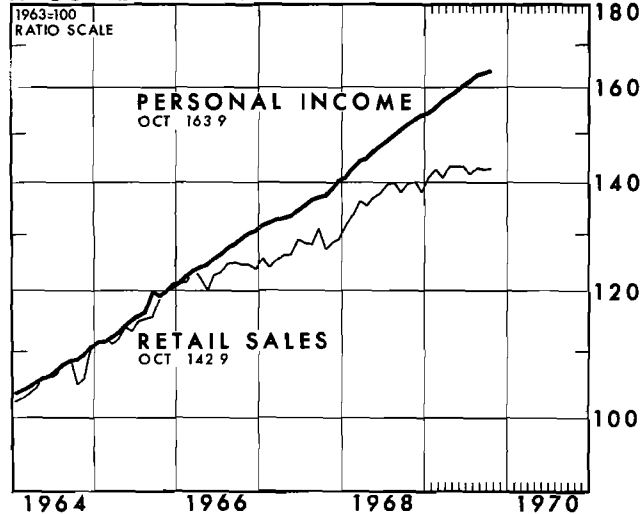
PRICES



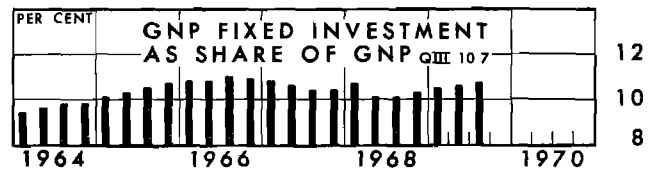
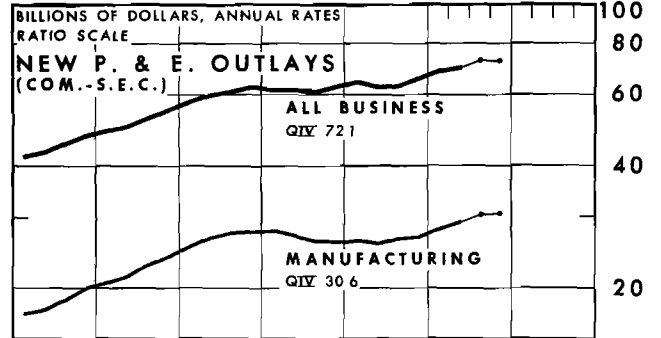
ECONOMIC DEVELOPMENTS - UNITED STATES

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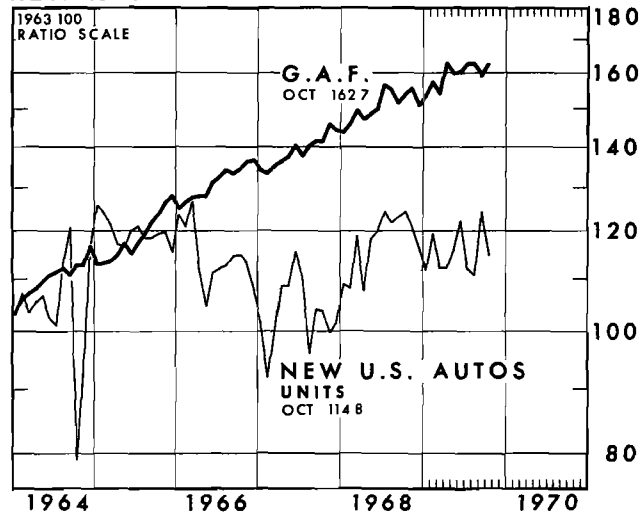
INCOME AND SALES



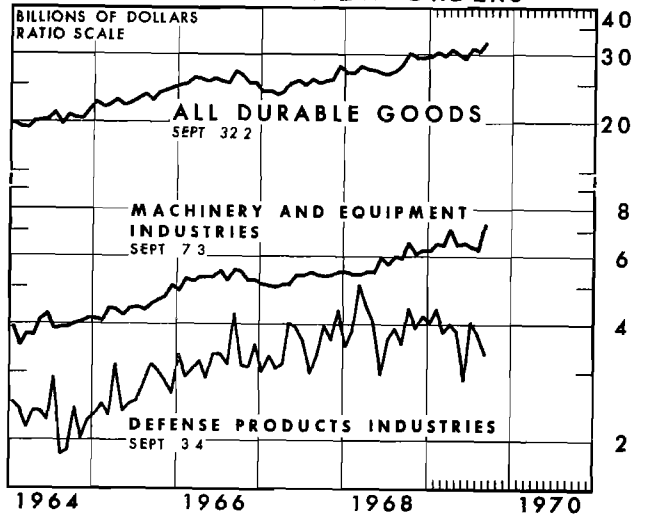
BUSINESS INVESTMENT



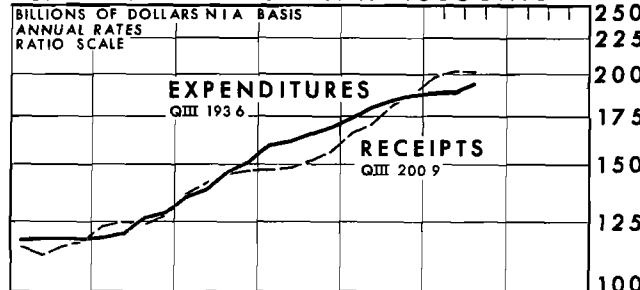
RETAIL SALES



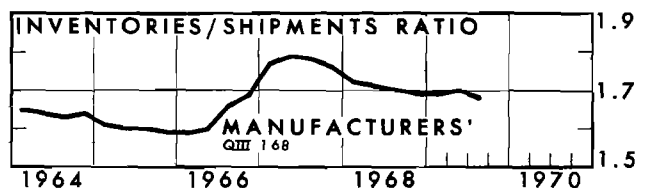
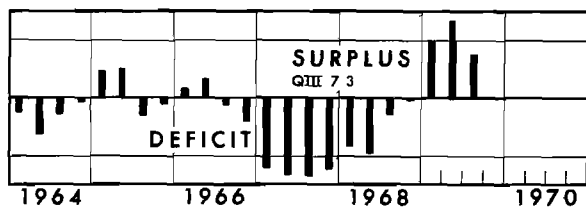
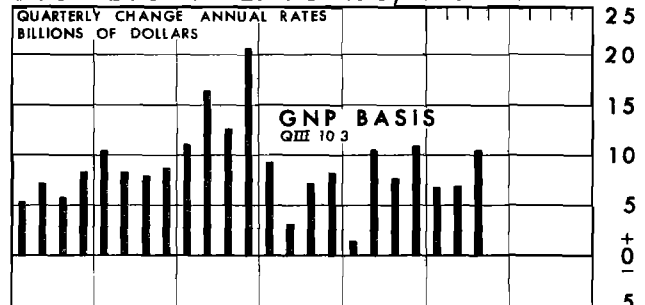
MANUFACTURERS' NEW ORDERS



FEDERAL FINANCE—N.I. ACCOUNTS



BUSINESS INVENTORIES, NONFARM



THE ECONOMIC PICTURE IN DETAIL

Domestic Financial Situation

Bank credit. Outstanding bank credit rose slightly in October, but still remained below the level at the end of May. Banks continued to run off holdings of U.S. Government securities in volume-- in spite of two large tax bill financings by the Treasury--and reduced considerably further their holdings of other securities as well. Loan expansion was somewhat greater than in recent months, largely the result of a substantial rise in security loans associated with the financings. And, if the sizable October increase in the outstanding amount of loans sold by banks to their own holding companies, affiliates, and subsidiaries is added to the change in bank loans, the October rise in this total of loans approximates the rapid expansion in the first five months of the year. However, the average monthly increases since May in total bank credit, total loans, and business loans, adjusted by the addition of loans sold to affiliates are still only one-half to one-third of those earlier in the year.

NET CHANGE IN BANK CREDIT
All Commercial Banks
(Seasonally adjusted percentage change, at annual rates)

	1968	1969		
	Year	1st 5 months	June - October	October
Total loans & investments ^{1/}	11.0	3.9	- 0.5	0.3
U.S. Gov't securities	3.0	-21.5	-11.1	-24.2
Other securities	16.4	--	- 7.4	-12.0
Total loans	11.6	11.2	3.5	8.0
Business loans	11.1	16.8	3.7	2.3
Other loans	11.9	7.7	3.3	11.5
Memo:				
Total loans plus loan sales ^{2/}	11.6	12.6	6.2	11.8
Business loans plus business loan sales ^{3/}	11.1	19.2	8.6	10.1

^{1/} Last Wednesday of month series.

^{2/} Includes outright bank sales of loans to their own holding companies, affiliates, and subsidiaries.

^{3/} Includes outright bank sales of business loans to their own holding companies, affiliates, and subsidiaries.

Banks reduced their holdings of securities by \$1.8 billion in October, or by about the same amount as in September. Even though banks underwrote two Treasury bill financings totaling \$5 billion, their holdings of U.S. Government securities fell by \$1.1, representing mainly the run-off of maturing bond issues. Banks resumed reduction in holdings of other securities--mainly municipals--at close to the rapid rate of July and August, following a small increase in holdings during September. Consequently, bank liquidity positions fell further in October, reaching new lows well below those in late 1966.

Nearly one-half of the October increase in bank loans went to brokers and dealers, apparently to finance increases in their inventories of securities stemming from the two Treasury financings. With the exception of consumer loans--which expanded at the somewhat increased rate of September--most other major loan categories, including business loans, continued to increase very little. However, there was also a large rise--\$900 million--in October, in the outstanding amount of loans sold by banks to affiliates, with \$750 million of this rise in business loans. The October increase in business loans, including the rise in these loan sales, was somewhat larger than in recent months, but still was well below average monthly expansion in the first five months of the year.

Bank sources of funds. Member bank deposits fell sharply further in October, reflecting largely a substantial drop in U.S. Government demand deposits, although time and savings deposits and private demand deposits also declined. In early November, however, deposits at these banks rose markedly in response to a sizable increase in U.S. Government demand deposits associated with the late October Treasury financing. While banks did not, on balance, supplement their deposits with any additional borrowings in the Euro-dollar market during October and the first week in November, their affiliates did acquire during this period a large amount of funds from the commercial paper market that was used to purchase loans from the banks.

CD attrition accounted for a much smaller proportion of the outflow of time and savings deposits since the end of September than earlier in the year. CD's held by individuals, partnerships, and corporations continued to decline at about the rate prevailing in recent months--by \$750 million in the 6 weeks ending November 5-- but this reduction was offset in large part by increases in outstanding CD's held by foreign official institutions. The latter apparently were mainly purchases of CD's by the Bank of International Settlements--primarily from banks in New York City--and largely represented switches from Euro-dollar deposit holdings.

NET CHANGE IN SELECTED SOURCES OF FUNDS
Weekly Reporting Banks
(Millions of dollars, not seasonally adjusted)

	Dec. 11-Sept. 24 ^{1/}			Sept. 24-Nov. 5 ^{1/}		
	1967	1968	1969	1967	1968	1969
Total time & sav. deps.	12,899	5,259	-14,738	708	2,221	-1,158
Consumer-type	7,486	4,049	- 977	407	852	- 534
Savings	1,363	- 222	- 2,239	152	239	- 123
Other time ^{2/}	6,123	4,271	1,262	255	613	- 411
Negotiable CD's	4,490	1,145	-12,515	538	1,147	- 278
All other time	923	65	- 1,246	-237	222	- 346
Euro-dollar borrowings ^{3/}	- 290	2,470	6,993	501	- 173	9
Commercial paper ^{4/}	--	--	2,546	--	--	1,188

^{1/} Dates are for 1969; corresponding dates used for other years.

^{2/} Time deposits, IPC, other than CD's, IPC.

^{3/} Through foreign branches.

^{4/} Issued by a bank holding company, affiliate, or subsidiary.

The runoff of consumer-type time and savings deposits at large banks, on the other hand, accelerated following quarterly interest crediting at the end of September. Moreover, time deposits other than

CD's and other than consumer-type at these banks also fell substantially during this period, reflecting in large part the continued reduction in holdings of these deposits by State and local governments. Country banks, too, experienced sizable attrition of time and savings deposits in recent weeks, following a considerable net outflow over the third quarter.

However, banks have acquired a large amount of funds from nondeposit sources since the end of September. In the 6 weeks ending November 5 their affiliates raised almost \$1.2 billion in the commercial paper market. On the other hand, funds obtained by banks from loans sold under repurchase agreement continued to fall--by about \$200 million--and, on balance, banks borrowed virtually no additional funds in the Euro-dollar market during this period, either through foreign branches or directly.

Demand deposits held by the public fell in October, for the third consecutive month. But further expansion in their currency holdings resulted in some net growth--at an annual rate of about 1.2 per cent--in the money stock, following virtually no increase during the third quarter. So far this year, the money stock has risen at an annual rate of 2.7 per cent, as compared with 7.2 per cent during 1968.

Nonbank depository institutions. During October, outflows from the savings and loan associations, according to sample data, were unusually large, with net withdrawals continuing even after the end of the reinvestment period. About half of the outflow occurred in the San Francisco District, with the remainder generally dispersed geographically. Most observers were surprised at the size of the attrition (almost \$450 million, before seasonal adjustment), but the continued attraction of high market yields was the apparent major factor during the month.

DEPOSIT FLOWS
NONBANK THRIFT INSTITUTIONS
(Seasonally adjusted annual rate, per cent)

		Mutual Savings Banks	Savings & Loan Associations	Both
1968	IV	7.1	6.2	6.5
1969	I	6.2	6.1	6.1
	II	4.3	3.5	3.8
	III(p)	1.9	2.2	2.1
	October(p) ^{1/}	0.3	- 1.5 ^{2/}	-0.9

Memo:	Sept.-Oct. 1969(p) ^{1/}	1.7	1.5 ^{2/}	1.6

(p) Preliminary

^{1/} Because of seasonal adjustment difficulties, monthly patterns may not be significant.

^{2/} Based on sample.

For probably the same reason, mutual savings banks in October, showed practically no deposit expansion after seasonal adjustment. On an unadjusted basis, New York State institutions suffered net outflows, which were offset only in part by expansion at institutions in other States. New York State savings banks have shown particular weakness since mid-year, and less than seasonal growth continued during the first 15 days of November at the largest New York City institutions.

DEPOSIT INFLOWS
15 LARGEST NEW YORK CITY MUTUAL SAVINGS BANKS
FIRST FIFTEEN DAYS OF NOVEMBER
(Millions of dollars, not seasonally adjusted)

	1966	1967	1968	1969
Net inflow, excluding dividends credited	46	53	48	22
New inflows, adjusted for passbook loans made	36	32	35	11

To offset deposit losses and supplement lendable funds, the FHLB's advanced a sizeable \$600 million to member associations in October, and another \$100 million in the first two weeks of November. The level of such advances in early November stood at \$8.5 billion, an increase of \$3.3 billion since the beginning of 1969. To prepare themselves for further assistance to the associations, the FHLB borrowed \$600 million of new money in November and may have to enter the market again in December for a moderate amount of new cash--an unprecedented event for that month.^{1/} In an additional effort to support mortgage activity, the FHLBB in mid-November reduced the required liquidity ratio from 6.0 to 5.5 per cent, the second reduction

^{1/} Assuming that the FHLB does borrow about \$300 million in December, their total net borrowings in 1969 will amount to \$3.9 billion, \$3.0 billion in the second half of the year.

this year. In the aggregate, this frees about \$650 million of S&L resources, but the distribution of liquidity suggests that perhaps only as much as half of this will be used.

Very few of the mutual savings banks, most of which have not joined the FHLB System, have borrowing recourse at a Federal agency, but they can, and do, borrow from commercial banks--through direct loans or RP's, and mortgage warehousing credits. The New York State savings banks, which have been most severely affected by rising market yields, did borrow about \$100 million in the third quarter, mostly from commercial banks, and may have borrowed about that much again from banks in late October and early November.

No significant improvement in net savings flows is expected over the balance of the year, and the staff expects considerable attrition at thrift institutions in the coming December-January reinvestment period. At S&L's the potential for this development is enlarged by heavy December-January maturities of certificate accounts. Such accounts represent one-third of total savings capital, and a recent confidential Savings and Loan League sample survey indicated that almost one-half of these are scheduled to mature in December and January. This maturity concentration apparently reflects a seasonal profile produced by shifting from regular to special accounts during previous reinvestment periods; the bulk of December-January maturities were probably originally issued for 6-month terms at mid-1969. While certificate accounts thus do not represent unusually "hot" money at

S&L's, the fact that they have been shifted from regular savings indicates a certain interest rate sensitivity; and even a rate of attrition as low as 10 per cent among maturing December-January maturities would amount to almost \$2 billion.

Mortgage market. With savings inflows to the thrift institutions particularly weak in October, the mortgage commitment activity of these institutions was probably somewhat more restricted. Hopefully, October commitment data for all savings and loan associations and New York State mutual savings banks will be available in time for the Greenbook Supplement.

In addition to the anticipated reduction in commitment activity at the thrift institutions, FNMA support of the Government-underwritten sector of the mortgage market has recently become somewhat more limited. Following a sharp drop in the amount of bids received during the second half of October, the weekly volume of forward purchase commitments accepted by FNMA fell in early November to the lowest level in nine months, as FNMA continued to set its auction limits so that it would acquire no more than approximately 60 per cent of the bids it receives.

The drop in bids received during October reflected in part the inability of a number of mortgage companies to originate FVA and VA loans carrying the 7-1/2 per cent interest rate ceiling, due to the resultant size of the discount--as high as 8 points--associated with the FNMA auction price. Also contributing to the

October decline in bids was the fact that some bidders had expected the mortgage market to improve in the near term and, given the existing range of FNMA prices, were unwilling to bid. More recently, the volume of bids received has risen back to September levels as expectation prompt easing in the mortgage market diminished. However, the volume of bids accepted has not recovered to the same extent, apparently because FNMA is not convinced that the most recent volume of bids received will be sustained.

FNMA WEEKLY AUCTIONS

	<u>Amount of total offers</u>		<u>Implicit private market yield 6-month commitments</u>
	<u>Received</u>	<u>Accepted</u>	
	<u>(Millions of dollars)</u>		<u>(Per cent)</u>
<u>Highs</u>			
1968	\$ 232 (6/3)	\$ 89 (7/1)	7.71 (6/10)
1969	410 (6/16)	152 (9/8)	8.63 (10/20)
Sept. 2	253	151	8.34
8	243	152	8.36
15	242	145	8.40
22	247	145	8.44
29	258	144	8.48
Oct. 6	251	147	8.52
13	218	146	8.59
20	162	135	8.63
27	121	118	8.60
Nov. 3	230	82	8.49
10	267	102	8.49
17	243	123	8.51

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 servicers. The first auction date was May 6, 1968.

Due to the record level of support provided by FNMA in 1969, its demand for funds has risen sharply throughout the year.^{1/} Through the first eleven months of this year, FNMA has borrowed \$2.9 billion in net new money through the issuance of long-term debentures and expects to obtain an additional \$200 million in December. Given the backlog of its outstanding mortgage commitments, now totaling nearly \$3 billion, FNMA is estimated by the staff to require at least \$700 million in new money financing during the first quarter of 1970.

The implicit private market yield on FNMA 6-month forward purchase commitments declined near the end of October in a lagged response to the sharp drop in corporate bond yields. However, by the November 17 auction, yields had again begun to rise, though uncertainty engendered by the extent of the existing discount caused bidders to move quite slowly in further reducing their bid prices.

The average yield in the private secondary market for FHA-insured home mortgages rose again in October as the accompanying discounts reached a near-record 7.7 points. The average contract rate in the primary market for conventional first-mortgages also advanced in October. Regionally, in the West, where usury ceilings have not been a limiting factor and where demand for housing has been exceptionally strong, the average conventional contract rate increased to 9 per cent, the highest rate ever reported by the FHA.

^{1/} For a detailed analysis of the FNMA mortgage market support in 1969 as well as that of the FHLBB, see Greenbook Appendix A.

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)	Discount (points)
<u>1968</u>					
Low	6.75(Jan.Feb.)	23(Mar.)	6.78(Feb.)	26(Mar.)	4.4(Sept.)
High	7.40(Dec.)	115(Aug.)	7.52(June)	120(Aug.)	7.9(Apr.)
<u>1969</u>					
Low	7.55(Jan.)	27(Sept.)	7.85 ^{e/} (Jan.)	42(Sept.)	2.8 ^{e/} (Jan.)
High	8.30(Oct.)	69(Feb.)	8.48(Oct.)	108(Feb.)	7.7(Oct.)
<u>1969</u>					
April	7.75	58	8.06	89	4.5
May	7.75	53	8.06	84	4.5
June	8.00	42	8.35	77	6.7
July	8.10	47	8.36	73	6.8
August	8.20	55	8.36	71	6.8
September	8.25	27	8.40	42	7.1
October	8.30	41	8.48	59	7.7

Note: FHA series: Interest rates on conventional first mortgages (excluding additional fees and charges) are rounded to the nearest 5 basis points. Data for FHA loans in January 1969 estimated by Federal Reserve for 7-1/2 per cent regulatory interest rate, 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 service fees, minus average yield on new issues of high grade corporate bonds with 5-year call protection.

^{e/} Estimated.

Corporate security and municipal bond markets. Corporate and municipal bond yields have advanced substantially since mid-October, with yields on new corporate bonds most recently surpassing previous peaks. The sharp reversal in bond yields--which began to occur before the President's Vietnam speech--reflected the heavy current and prospective volume of new offerings and limited fund availability at several major institutional investors. Although underwriters pursued aggressive pricing policies through October, buyers generally became increasingly cautious about the outlook for yields, given mixed economic statistics and declining hope of a near-term shift in monetary policy; the President's speech may also have revised some earlier expectations regarding the peace outlook. In this atmosphere, many new bond issues sold poorly and in the first half of November underwriters attempted to reduce rising inventories by cutting prices; since the end of October, 8 corporate issues have been released to free market trading with upward yield adjustments ranging from 10 to 20 basis points. Municipal underwriters also cut prices on slow moving issues adding upward pressure to rates in that market. In both markets, even after syndicate terminations, dealer inventories apparently remained uncomfortably high.

STOCK PRICES AND BOND YIELDS

	Stock Prices 1/		Bond Yields	
	NYSE	AMEX	New Corporate Aaa 2/	Long-term State and local Bonds 3/
<u>1968</u>				
Low	48.66(3/4)	21.58(3/5)	6.13(8/30)	4.07(8/9)
High	61.27(11/29)	33.25(12/20)	6.92(12/13)	4.85(12/29)
<u>1969</u>				
Low	49.31(7/29)	25.02(7/29)	6.90(1/10)	4.82(12/24)
High	59.32(5/14)	32.91(1/3)	8.27(11/14)	6.37(9/5)
<u>Week of:</u>				
Oct. 17	53.72	27.66	7.95	5.92
24	54.89	28.37	7.82	6.07
31	54.45	28.37	7.87	6.13
Nov. 7	55.07	28.61	8.13	6.11
14	54.56	28.31	8.27	6.17

- 1/ Prices as of the day shown. NYSE is New York Stock Exchange. AMEX is American Stock Exchange.
- 2/ With call protection (includes some issues with 10-year call protection).
- 3/ Bond Buyer (mixed qualities).

The stock market continued its October rally through the first week in November, ignoring the renewed softness in bond markets since mid-October, and despite persistent indications that previous expectational shifts regarding monetary policy had been premature. For example, at the close on November 7, the NYSE Index stood 10.5 per cent above its July low, having recovered nearly half of the decline from its record peak of December 1968. However, during the week

ended November 14, both prices and trading volume on the NYSE and AMEX declined moderately. Trading volume on the NYSE averaged 13.2 million shares per day during October, considerably above the 10.5 million share average for the third quarter.

Although fragmentary reports from margin panel firms suggest that margin debt increased somewhat during October, and thus that individual investor trading contributed to increased demand, the major impact on the market appears to have been the result of renewed institutional activity. The liquidity of mutual funds, which stood at an unusually high 9 per cent of assets at the end of September (the latest data available), suggests that the funds had been holding back from the market in anticipation of a turn in prices. There is also fragmentary evidence that some of these funds shifted their purchases from bonds to stocks in October and early November.

An increased volume of stock offerings was associated with the general improvement in stock prices. This accounted in part for the continued rapid pace of total corporate security offerings. The staff's estimated volume of stock issues has been revised upward for both October and November to about \$100 million above the average third quarter volume. Public bond offerings in November are estimated at \$1.2 billion, \$0.2 billion above earlier estimates due to the shift of some issues from late October into November and a modest pickup of convertible issues. Included in the November volume are two large nonconvertible industrial issues, a type of offering absent from the calendar since early in the third quarter.

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

	Public Bond Offerings		Private Bond Offerings		Stocks		Total	
	1968	1969	1968	1969	1968	1969	1968	1969
Year	894	1,011e	554	547e	382	628e	1,830	2,177
Q I	821	886	574	513	330	674	1,726	2,073
Q II	1,035	1,136	548	526	319	709	1,902	2,371
Q III	869	1,070e	454	547e	389	560e	1,711	2,177
Q IV	852	953e	641	600e	491	567e	1,984	2,087
October	1,009	960e	595	500e	525	650e	2,129	2,110
November	939	1,200e	362	500e	466	650e	1,767	2,250
December	607	700e	965	800e	483	400e	2,055	1,900

e/ Estimated.

1/ Data are gross proceeds.

Looking ahead to December--when new flotations traditionally cease after mid-month--public bond offerings now scheduled aggregate about \$0.6 billion and are expected ultimately to total \$0.7 billion. Making a rough allowance for the usual seasonal lull in December, this volume is comparable to over \$1 billion for other months. The bulk of the scheduled volume is in public utility bonds. Underwriters do not report any concrete signs of large industrial firms about to enter the market, although the squeeze on corporate liquidity may prod some firms to enter the market in the near-term. Taking account of private bond offerings and equity issues, total corporate

security offerings in December are estimated at a sizable \$1.9 billion. For the full year, total corporate security offerings are tentatively estimated at about \$26 billion, a record and more than \$1 billion above the previous high in 1967.

Total municipal bond and note offerings in November are estimated slightly above the almost \$1.3 billion volume during October. However, there is a substantial switch between short and long-term issues in these two months, with long-term volume nearly one-third less than October, a time when interest rates fell below 6 per cent. The increase in interest rates so far in November accounts, in part, for the sharp rise in short-term offerings. But the volume of long-term issues has been maintained above the low during other months this year. This reflects the relaxation of rate ceilings in some areas, enlarged borrowing by units without ceiling constraints, and increased emphasis on shorter average maturities of bond offerings.^{1/} Rates have also not risen as high as during the third quarter, reflecting the virtual end of discussion about taxing municipal bond interest. But earlier cut backs in long-term issues will keep total gross long-term offerings in 1969 to under \$12 billion as compared with the \$15 billion of nonindustrial revenue issues in 1968.

^{1/} The composition of issues on the calendar is heavily weighted in areas with rate ceilings above 6 per cent or no ceilings at all. Currently, 19 States have rate ceilings on State G.O.'s of 6 per cent or below and 27 States have such ceilings applicable to local G.O.'s. Local G.O.'s, moreover, are often rated below the highest quality and presently bonds rated A yield considerably more than 6 per cent. About 24 States still have rate ceilings of 6 per cent or less on local agencies, such as school districts. As will be indicated in the appendix to the supplement, these units were particularly affected by the rising level of rates in the third quarter.

STATE AND LOCAL GOVERNMENT OFFERINGS
 Monthly or Monthly Averages
 (Millions of dollars)

	Long-Term 1/		Net Short-Term 2/		Total 3/	
	1968	1969	1968	1969	1968	1969
Year	1,381	962	-20	--	1,361	--
Q I	1,246	930	-51	302	1,195	1,232
Q II	1,285	1,208	11	344	1,296	1,552
Q III	1,537	810	-73	366	1,464	1,176
Q IV	1,455	900e	33	n.a.	1,488	n.a.
October	2,230	1,250e	250	30e	1,980	1,280e
November	1,021	850e	413	500e	1,434	1,350e
December	1,115	600e	-565	n.a.	1,680	n.a.

e/ Estimated.

1/ Data are for principal amounts of new issues.

2/ EXCLUDES note offerings of Housing Assistance Administration and Renewal Assistance Administration.

3/ Combines GROSS long-term and NET short-term issues.

Municipal bond volume in December is estimated at \$600 million, relatively high for this month--except for December 1968 which was bulged by industrial revenue issues. Even though long-term municipal volume for the fourth quarter as a whole is likely to be larger than during the quarter earlier, actual borrowing will fall significantly short of the roughly \$5 billion of borrowing desired by governmental units, as of September 30, for the three months ended in December. An appendix to be issued in the supplement will discuss further recent survey results of State and local Government borrowing plans and expenditure cutbacks.

Government securities market. Yields on longer-term U.S. Government securities have shared in the general advance in capital market interest rates that began around the third week in October. In the case of Governments, however, only part of the sharp rate declines that had occurred earlier in October were retraced. Intermediate-term yields in particular have stayed well below their previous highs. Nevertheless, rates on most notes and bonds have risen 30 to 60 basis points since the turnaround, while Treasury bill yields have advanced on balance by some 15 to 40 basis points, with the 3-month issue reaching a new high of 7.20 per cent on November 13.

MARKET YIELDS ON U. S. GOVERNMENT SECURITIES^{1/}
(Per cent)

	Lows	Highs	Oct. 27	Nov. 10	Nov. 17
<u>Bills</u>					
1-month	5.30 (3/25)	7.20 (9/22)	6.80	6.92	6.68
3-month	5.87 (4/30)	7.20 (11/13)	6.99	7.12	7.07
6-month	5.96 (4/30)	7.55 (11/17)	7.23	7.41	7.55
1-year	5.86 (1/16)	7.47 (7/1)	7.10	7.12	7.24
<u>Coupons</u>					
3-year	6.02 (1/20)	8.14 (10/1)	7.35	7.53	7.72
5-year	6.11 (1/20)	8.04 (10/1)	7.28	7.35	7.55
7-year	6.09 (1/16)	7.76 (10/1)	6.99	7.03	7.16
10-year	5.95 (1/20)	7.52 (10/1)	5.93	6.99	7.13
20-year	5.91 (5/5)	6.81 (10/1)	6.48	6.65	6.76

^{1/} Latest dates of high or low rates in parentheses.

With no new Treasury financings in the one- to seven-year area expected before February, yields on intermediate-term issues have reversed only about half of their early October declines. Increased supply, however, has been forthcoming in the Federal Agency market, and the recent \$1.1 billion Federal Home Loan Bank financing (raising \$600 million of new money) put some upward pressure on Government security yields. The long term Government market continued to be influenced by recent weakness in the corporate sector, with reports of some investor switching into corporates at their recent record high yields.

Total dealer inventories of bills rose from a low of around \$600 million on October 6 to a recent high of nearly \$3.6 billion on November 5. Factors contributing to the build-up of positions included the need to absorb bank liquidation of the \$5 billion of tax bills auctioned in October, end-of-month awards in the monthly bill auction, and large net acquisitions of bills from foreign accounts-- notwithstanding the fact that the Federal Reserve itself bought \$1.3 billion of bills directly from foreign accounts in reserve-supplying operations. Prior to the President's speech on Vietnam, dealers absorbed bills without much upward pressure on bill yields. Since then, however, dealer bill holdings have been reduced to about \$2.5 billion as foreign accounts have moved to the buy side of the market and the System has continued to purchase bills to provide reserves. Despite this buying, yields have advanced significantly. To some

extent, this has reflected the general shift in market expectations since the President's speech. In addition, with their bill position still at relatively high levels, with financing costs higher, and with the Treasury about to sell an additional \$2.5 billion of tax bills, dealers have become increasingly reluctant to take on bills at prevailing yields.

DEALER POSITIONS IN GOVERNMENT SECURITIES
(In millions of dollars)

	October 27	November 10	November 17
Total	<u>2,788</u>	<u>3,264</u>	<u>2,804</u>
Treasury bills (total)	<u>2,267</u>	<u>2,807</u>	<u>2,475</u>
Due in 92 days or less	82	-23	-25
93 days or over	2,185	2,831	2,500
Treasury notes and bonds (Total)	<u>520</u>	<u>457</u>	<u>330</u>
Due within 1 year	82	120	66
1-5 years	242	168	137
over 5 years	196	169	127

Other short-term credit markets. Yields on commercial paper and bankers' acceptances declined somewhat during the last week in October with rates for 3-month commercial paper reaching 8.25 per cent, the lowest level since August. By mid-November, however, rates had turned up again, along with yields on Treasury bills, and the quote on 3-month and 6-month commercial paper had moved back to 8.50 per cent. Rates on 3-month finance paper have remained at their relatively high level of 8.13 per cent since early October as the automobile model changeover continued to exert pressure on this market.

SELECTED SHORT-TERM INTEREST RATES
(Friday Quotation--Discount Basis)

	October 17	October 31	November 4
<u>3-month</u>			
Commercial paper	8.63	8.25	8.50
Finance paper	8.13	8.13	8.13
Bankers' acceptances	8.25	8.00	8.00
Federal agencies (secondary market) ^{1/}	7.39	7.66	7.61
Treasury bill	6.97	7.00	7.09
<u>6-month</u>			
Commercial paper	8.50	8.25	8.50
Finance paper	7.75	7.75	7.75
Bankers' acceptances	8.25	8.00	8.00
Federal agencies ^{1/}	7.77	7.83	8.08
Treasury bill	7.30	7.31	7.46
<u>12-month</u>			
Prime municipals ^{1/}	5.45	5.45	5.45
Treasury bill	7.18	7.03	7.17

^{1/} Bond yield basis.

In the secondary market for short-term Federal agency debt, rates have been drifting steadily higher since mid-October. By November 14 issues due within 6 months were quoted at about 8.08 per cent, some 30 basis points above their mid-October lows. In the market for new agency debt, yields on shorter maturities have also risen substantially. For example, a 6-month Bank for Cooperatives issue was priced to yield 8.45 per cent on November 18, 40 basis points above a comparable issue one month earlier. On the other hand, rates on new longer-term issues-- due in one year or more--have increased only slightly since mid-October. For example, Federal Home Loan Bank issues with one year and 25-month maturities were offered to yield 8.25 per cent and 8.20 per cent respectively on October 15. But when the agency returned to market to offer 10-month and 24-month issues on November 13, reoffering yields of 8.38 and 8.20 per cent were considered sufficient although both issues moved to somewhat higher yields in initial secondary market trading.

NEW FUNDS OBTAINED FROM THE PUBLIC
IN THE FEDERAL AGENCY MARKET

	1966	1967	1968	1969
July	494	272	822	755
August	234	- 28	-145	1,101
September	-306	- 83	111	393
October	-123	- 53	354	1,776
November	72	829	204	600 (as of 11-14)

NOTE: In September, the latest month for which data are available, the volume of commercial and finance paper outstanding increased by \$1,386 million to a total of \$30.2 billion. Almost 30 per cent, or \$1,103 million, of the increase was accounted for by directly placed paper reflecting pressure on automobile finance companies during the model changeover. Bank-related paper increased to \$2.5 billion at the end of September and subsequently to \$3.7 billion by November 5.

COMMERCIAL AND FINANCE PAPER AND BANKERS'
ACCEPTANCES OUTSTANDING
(In millions of dollars)

	July	August	September
Commercial & finance paper <u>1/</u>			
Total	27,812	28,862	30,243
Placed through dealers	10,314	11,019	11,302
Placed directly <u>2/</u>	17,498	17,843	18,946
Note: Bank related paper (unadjusted)	1,869	2,210	2,496
Bankers' acceptances	4,991	5,145	5,232

1/ Data for commercial and finance paper are seasonally adjusted, in contrast to similar data published in the Bulletin that are seasonally unadjusted.

2/ As reported by companies that place paper directly with investors. As of June 1969, these figures include for the first time directly placed commercial paper issued by bank related companies. Dealer totals have always included paper issued by bank related companies.

Federal Finance. Expenditures data for September indicate that defense outlays in that month were \$.6 billion lower and CCC spending was \$.2 billion less than the Staff had estimated in the last Greenbook.

In addition, total outlays during October and November appear to be more modest than had been anticipated. While other signs point toward offsetting increases in social insurance and veterans' benefits later in the year, the Administration's fiscal year spending total of \$192.9 billion may be achievable, although it is still toward the low end of the range of reasonable projections. However, estimates of receipts have also been adjusted downward and the budget surplus now expected for this fiscal year is somewhat smaller than that shown in the last Greenbook. September receipts, mainly individual withheld taxes, were \$.8 billion lower than the Staff had predicted. Reflecting this shortfall, forecasts of receipts over the next few months have been revised downward by \$.5 billion.

As a result of lower than expected receipts, the Treasury's fourth quarter cash positions is slightly less comfortable than the Staff had projected. The cash balance at the end of October was \$5.5 billion, but it should increase to about \$6.6 billion by the end of November as a result of Treasury cash financing. In addition to \$400 million of new money to be raised by adding \$100 million to each of the month's four weekly bill auctions, the Treasury has announced \$2.5 billion of borrowing, in the form of \$1.0 billion of April and \$1.5 billion of June tax bills for payment on November 26. This new cash, plus continued \$100 million supplements to the weekly bills

in December, is expected to maintain the cash balance above \$3 billion even at its seasonal low on December 15. Strong corporate tax payments should carry the balance to about \$6.5 billion by the end of the calendar year, and the end of January balance could approach \$7.5 billion.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	Oct.	Nov.	Dec.	Jan.
<u>Borrowing operations</u>				
New cash raised:				
Weekly and monthly bills	--	.4	.4	.2
Tax bills	5.0	2.5	--	--
Coupon issues	--	--	--	--
Other (agency, debt repayment, etc.)	-1.1	--	-2.5	--
Total net borrowing from public	3.9	2.9	-2.1	.2
Plus: Other net financial sources ^{a/}	.6	-1.0	--	.8
Plus: <u>Budget surplus or deficit (-)</u>	-5.6	-0.8	2.0	-0.1
Equals: <u>Change in cash balance</u>	-1.1 ^{b/}	1.1	-0.1	0.9
Memoranda: Level of cash balance end of period	5.5 ^{b/}	6.6	6.5	7.4
Derivation of budget surplus or deficit				
Budget receipts	12.0	14.3	17.6	16.2
Budget outlays	17.6	15.1	15.6	16.3

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

^{b/} Actual

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

	FY 1969	Calendar	Fiscal 1970		II	IIIe/	IVe/	Ie/	IIe/
	Actual	year 1969e/	Summer Review	Budget F.R. Board					
<u>Quarterly data, unadjusted</u>									
New budget:									
Surplus/deficit	3.1	6.4	5.9	2.4	15.3	-2.5	-4.4	-3.6	12.9
Receipts	187.8	196.7	198.8	195.3	60.8	47.9	43.9	44.2	59.3
Total expenditures and net lending	184.8	190.3	192.9	192.9	45.5	50.4	48.3	47.8	46.4
Means of financing:									
Total borrowing from the public	-1.4 ^{1/}	-4.5		-1.4	-12.6	3.2 ^{2/}	4.7	2.4	-11.7
Decrease in cash operating balance	-.6	-1.8	n.a.	-0.1	-1.1	-.7	.1	.5	--
Other ^{3/}	-1.1	-.2		-0.9	-1.7	--	-.4	.7	-1.2
Cash operating balance, end of period	5.9	6.5		6.0	5.9	6.6	6.5	6.0	6.0
<u>Seasonally adjusted annual rate</u>									
Federal surplus/deficit									
in national income accounts	4.9	9.7	5.1	3.8	13.5	7.8	7.4	1.0	-1.0
Receipts	192.3	201.4	201.2	200.0	202.8	201.4	202.9	197.3	198.3
Expenditures	187.4	191.7	196.1	196.2	189.3	193.6	195.5	196.3	199.3
High employment budget surplus/deficit ^{4/}	2.7	9.3	n.a.	7.3	12.6	7.8	8.9	5.9	6.5

*--Actual

e--Projected. Assumes extension of surcharge at 5 per cent from January to June 1970. Also assumes discontinuance of investment tax credit effective, retroactively, April 1969.

n.a.--Not available.

^{1/} Excludes effect of conversion of agencies to private ownership.

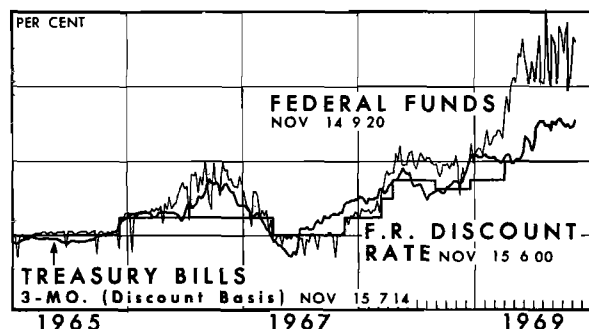
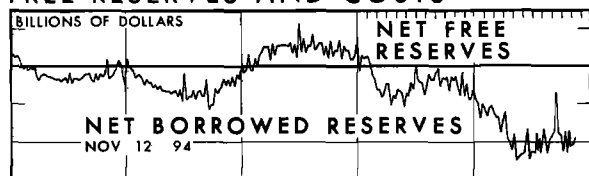
^{2/} Excludes effect of reclassification of \$1.6 billion of CCC certificates of interest from Budget transactions to borrowing from the public.

^{3/} Includes such items as deposit fund accounts and clearing accounts.

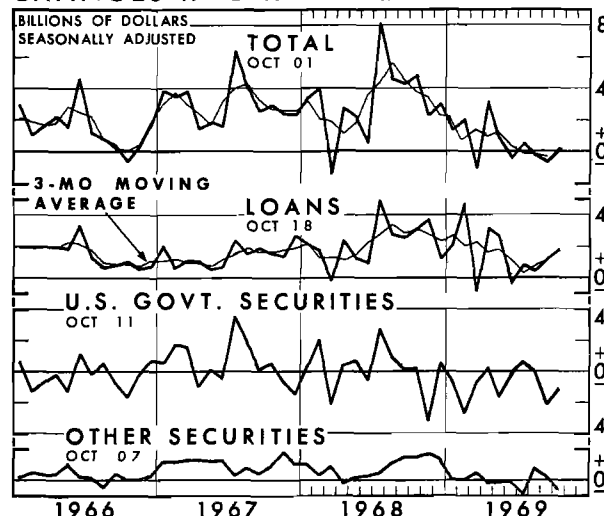
^{4/} National Income account translation estimated by Federal Reserve staff.

FINANCIAL DEVELOPMENTS - UNITED STATES

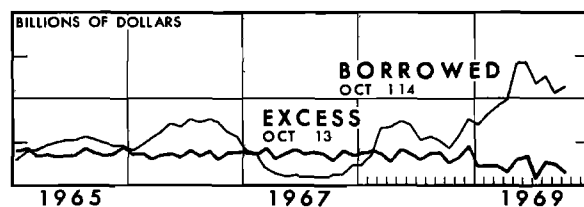
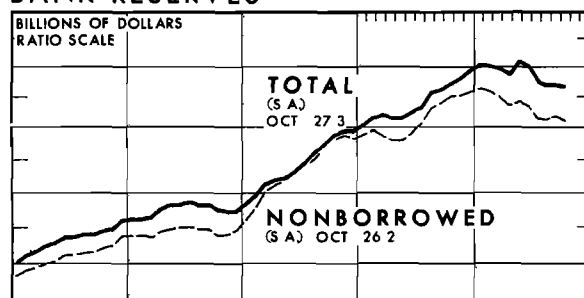
FREE RESERVES AND COSTS



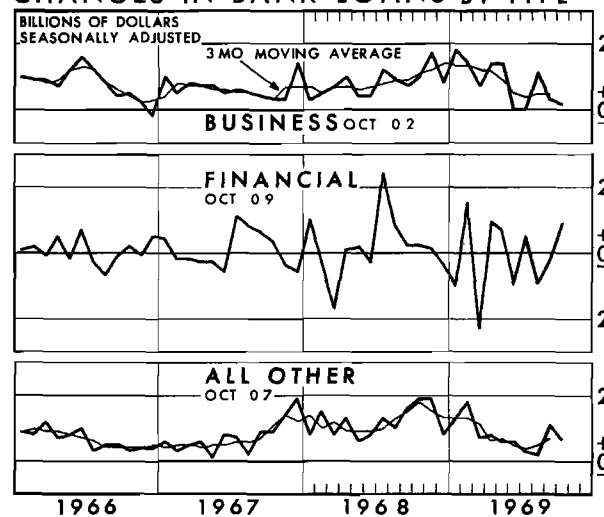
CHANGES IN BANK CREDIT



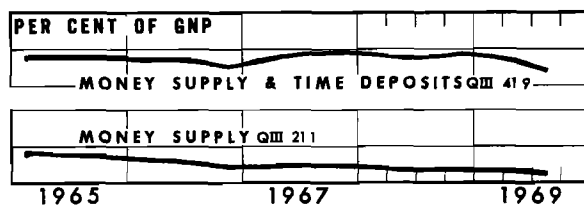
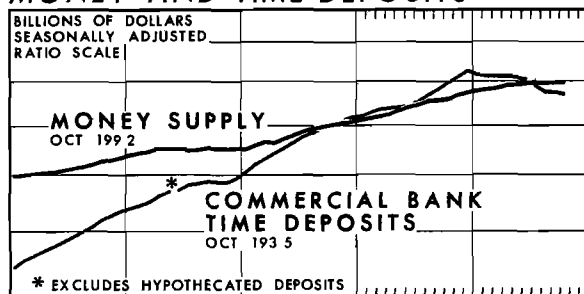
BANK RESERVES



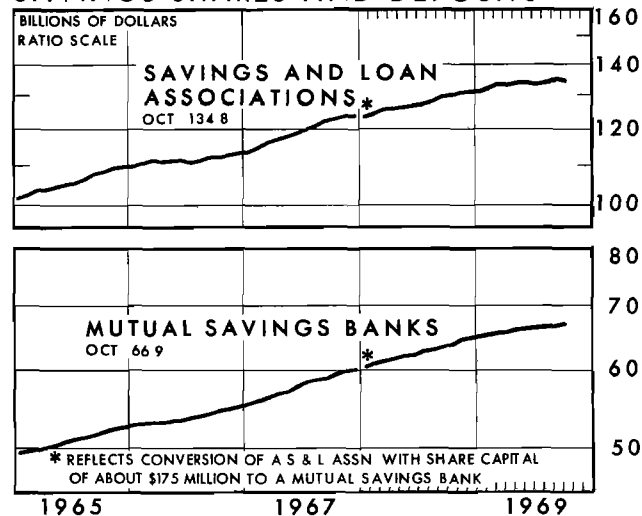
CHANGES IN BANK LOANS-BY TYPE



MONEY AND TIME DEPOSITS

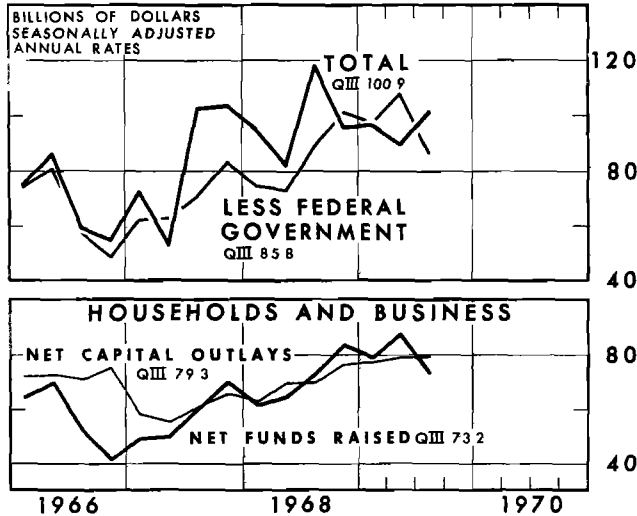


SAVINGS SHARES AND DEPOSITS

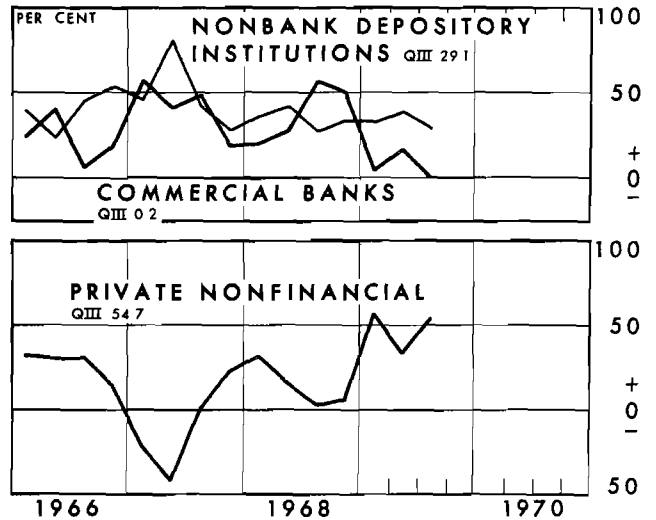


FINANCIAL DEVELOPMENTS - UNITED STATES

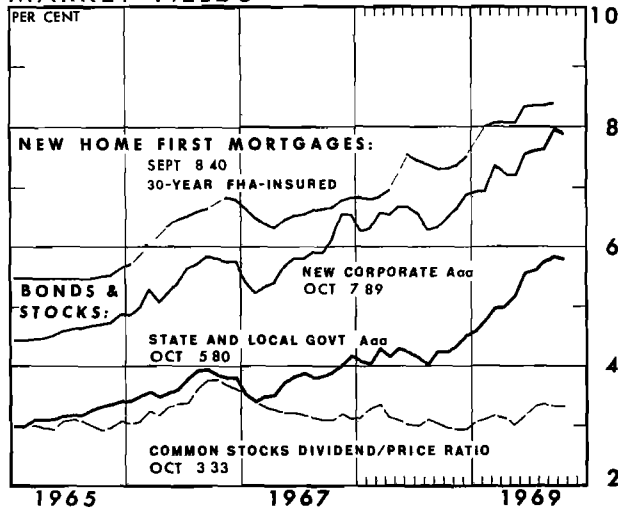
NET FUNDS RAISED-NONFINANCIAL SECTORS



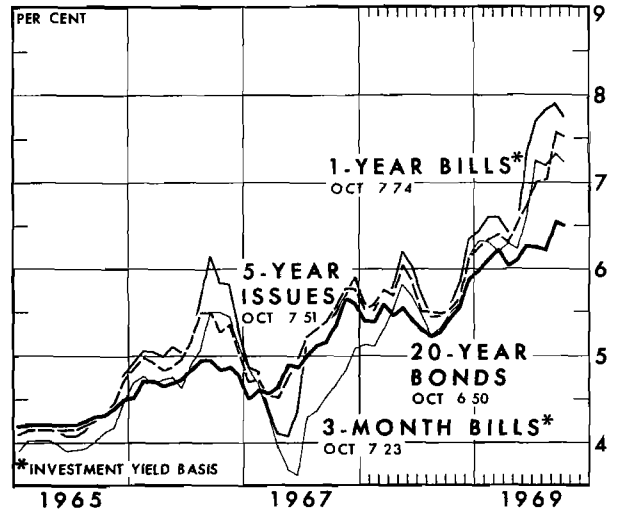
SHARES IN FUNDS SUPPLIED



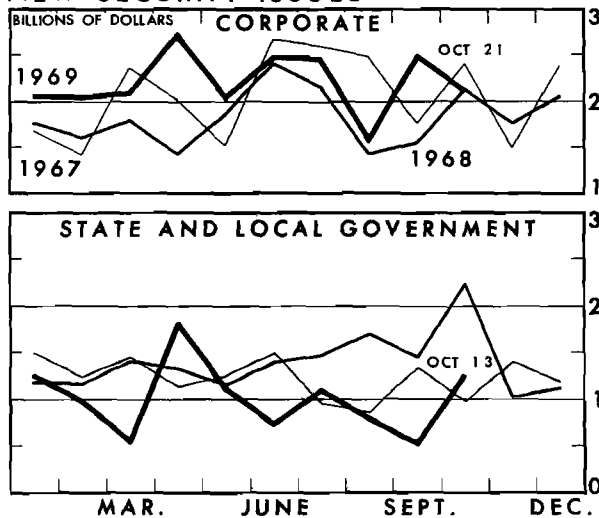
MARKET YIELDS



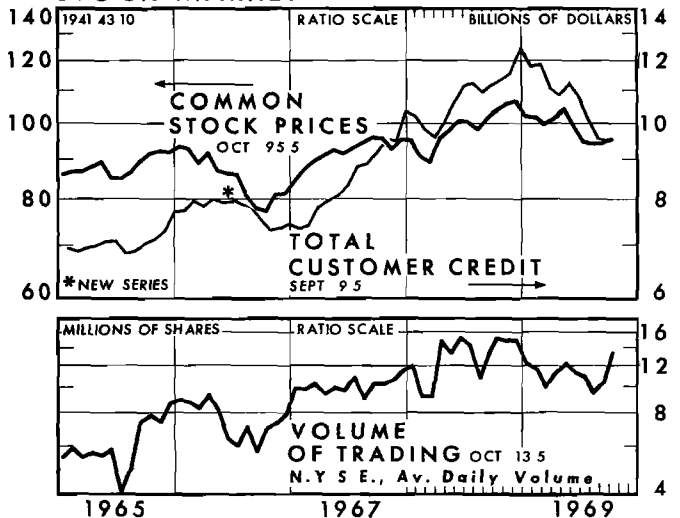
MARKET YIELDS-U.S. GOVT. SEC



NEW SECURITY ISSUES



STOCK MARKET



 THE ECONOMIC PICTURE IN DETAIL

International Developments

U.S. balance of payments. Beginning in September the rate of the liquidity deficit has been considerably lower than in the preceding eight months, if adjustments are made for adverse seasonality and certain special factors. Of course, the most recent figures are quite tentative, as are the monthly seasonal adjustments, but the following pattern indicates the extent of the shift that is appearing (in millions of dollars):

	<u>IQ</u>	<u>IIQ</u>	<u>IIIQ</u>	<u>July- Aug.</u>	<u>Sept.</u>	<u>Oct.^P</u>
Liquidity deficit, NSA	-1,273	-3,786	-2,888	-2,419	-469	-690
Seasonal element	395	64	-355	-405	50	-450
Liquidity deficit, SA	-1,668	-3,850	-2,533	-2,014	-519	-240
"special" transactions	230	-350	-547	-294	-253	40
Liquidity deficit (SA) before "special" transactions	-1,898	-3,500	-1,986	-1,720	-266	-280

Weekly data for November, through the 12th, show a sizable surplus, though this is also a seasonally adverse month. The lower deficits since August probably depend in part on a reversal of earlier speculative outflows of capital. Thus, to establish the level for the underlying deficit a considerable upward adjustment is probably necessary.

The factors in this turn for the better are not yet clear from any actual statistical measurement, but several are very likely at work. One is the gain in the trade account, discussed below, that showed up in

the August-September reports and is perhaps continuing. Another factor is probably a reduced level of U.S. private capital outflows, apart from speculative movements. Bank-reported claims were reduced in the third quarter; sketchy coverage of October transactions indicates there may have been a further reduction. Sales of new issues of foreign bonds in the U.S. market have been sharply reduced from \$550 million (seasonally adjusted) in the third quarter to about \$75 million in October and about \$100 million so far in November. There are also some indications that foreign investors were purchasing fairly sizable amounts of U.S. equities in October.

A reduction in direct-investment outflows had been expected in the fourth quarter, but last year's pattern suggested that this might not occur until the last weeks of the year. However, both direct investors and others may have begun to unwind their Deutschmark positions at an accelerating pace in October and November. In addition, the flow of U.S.-resident funds to the Euro-dollar market may have diminished.

The preliminary report on the third quarter balance of payments (see following table) shows that the residual item in which short-term speculative flows, together with direct investments and many other items, would be reflected, was reduced below the inflated amounts of the first two quarters, though it was still above the quarterly average of 1967 or 1968.

Balance of Payments ^{1/}
(millions of dollars, seasonally adjusted)

	Year	1 9 6 8	I	II	III	IV	1 9 6 9	I	II ^{r/}	III ^{p/}
Merchandise excluding military										
Exports	33,598	7,941	8,395	8,879	8,383	7,469	9,588	9,567		
Imports	-32,972	-7,817	-8,131	-8,566	-8,458	-7,572	-9,590	-9,231		
Net	626	124	264	313	-75	-103	-2	336		
U.S. purchases (-) of foreign sec.	-1,267	-311	-164	-337	-455	-323	-426	-583		
U.S. banking claims (increase(-))	269	236	243	-90	-120	78	-473	185		
Foreign purchases of U.S. corp. stocks	2,084	309	530	459	786	751	127	155		
Foreign purchases of other U.S. sec., excluding Treasury issues	2,276	530	586	656	504	622	202	223		
Selected Government transactions										
Nonscheduled debt repayments	269	42	3	55	169	44	34	-150		
Nonliquid U.S. bank liabilities ^{2/}	590	56	175	119	240	-50	-173	-258		
Nonliquid U.S. Government liabilities	2,010	273	772	409	556	95	-171	-115		
Liquid liab. to private foreign accts.	3,811	540	2,314	765	192	2,848	4,716	1,080		
Liquid liab. to official foreign accts.	-3,099	-880	-2,186	-55	22	-1,132	-567	2,139		
U.S. reserve assets (increase(-))	-880	904	-137	-571	-1,076	-48	-299	-686		
Other transactions (derived as <u>residual</u>)	-6,689	-1,823	-2,400	-1,723	-743	-2,782	-2,968	-2,326		
Balances (deficit(-))										
Official settlements balance	1,638	-379	1,553	97	367	1,143	1,234	-933		
Liquidity balance	168	-564	9	-139	862	-1,668	-3,850	-2,533		
Adjusted over-all balance	-1,744	-844	-751	-613	464	-1,824	-3,560	-2,204		

^{p/} Preliminary. ^{r/} Revised.

^{1/} Items available, or partially estimated, for third quarter of 1969 as of November 18, 1969.

^{2/} Includes some non-official transactions.

Movements in the official settlements balance have become erratic as U.S. commercial banks adjusted their borrowings from the Euro-dollar market to cope with changing circumstances, and as foreign official holders of dollars shifted some funds out of Euro-dollars into time deposits in the United States. This balance showed a sizable deficit in August as U.S. banks drew only a moderate amount from the Euro-dollar market and liabilities to official accounts (mainly German) expanded sharply. In September, U.S. banks reduced their Euro-dollar liabilities, and the official settlements deficit exceeded the liquidity deficit. During October the banks with foreign branches first drew heavily from the Euro-dollar market, probably in part to be sure of obtaining additional reserves to cover the increased requirements under Regulation M. Then in the latter half of the month they greatly reduced their liabilities to branches, partly because of the shift of official funds to time deposits, but also in response to the increased cost of such borrowing subject to the new reserve requirement as well as the increased use of other sources of non-deposit funds. Early in November this downward adjustment was arrested as proposed regulations affecting sales of commercial paper by bank affiliates once more shifted the focus of borrowing toward Euro-dollars. As a result of these fluctuations, the official settlements balance may have registered an October deficit comparable to that on the liquidity basis, but then reverted to a surplus in early November.

U.S. foreign trade. The merchandise export surplus in the third quarter was at an annual rate of \$1.3 billion, balance of payments basis. This compares with a small deficit in the first half of the year and is the best showing in nearly two years. Particularly noteworthy were the increasing monthly surpluses during the quarter, with the surplus in September accounting for more than one-half of the quarterly total. Exports, which had shown virtually no change from the last half of 1968 to the first half of 1969, increased sharply in the third quarter -- to a level 12 per cent above that of the first half. Imports in the third quarter also advanced but more slowly, by 7.5 per cent.

Still uncertain is how much of the improvement in the trade surplus represents a strengthening in our basic trade position and how much is a post dock-strike effect. Exports had been more adversely affected by the strike than imports, and part of the recent sharp rise in exports may represent goods that otherwise would have been shipped earlier in the year.

The export advance in the third quarter was broadly based, both by commodity categories and by principal foreign markets. Shipments of both agricultural and nonagricultural products were considerably higher than in the first half. Agricultural exports, which had slumped badly, principally because of the strike, increased to a level slightly above that recorded for the second half of 1968. Grain shipments were up sharply despite some slippage in P.L. 480 shipments and lower wheat prices.

The full impact of the wheat price cuts has yet to be reflected in exports. This, together with a disappointing cotton crop this year, makes it questionable whether the third quarter rate of agricultural shipments can be sustained.

Exports of all types of nonagricultural products (except commercial aircraft) were sharply higher in the third quarter than in the first half. Industrial supplies (paper, chemicals, steel), machinery,

U.S. Merchandise Trade
(billions of dollars, seasonally adjusted, annual rates)

	1 9 6 8		1 9 6 9	
	1st Half	2nd Half	1st Half	3rd Qtr. ^{p/}
<u>Balance of payments basis</u>				
Exports, total	32.7	34.5	34.1	38.3
(Agricultural)	(6.4)	(6.2)	(5.5)	(6.3)
(Nonagricultural)	(26.3)	(28.3)	(28.6)	(32.0)
Imports, total	31.9	34.1	34.3	36.9
Balance	0.8	0.5	-0.2	1.3
<u>Census basis</u>				
Imports, total	32.0	34.2	34.6	37.2
Foods and beverages	5.1	5.4	5.0	5.3
Industrial supplies	14.0	14.2	13.8	14.6
Iron and steel	2.0	2.2	1.8	2.0
Capital equipment	2.7	2.9	3.2	3.6
Auto. vehicles & parts	3.9	4.7	4.9	6.0
From Canada	2.4	2.9	3.2	3.8
From other areas	1.5	1.9	1.8	2.2
Consumer goods	5.0	5.5	6.3	6.8
All other	1.3	1.2	1.4	1.6

^{p/} Preliminary

automotive equipment to Canada, and other nonfood consumer goods all increased. With industrial output continuing to expand sharply in Europe and Japan, and capacity-utilization rates in manufacturing in many of these countries at peak rates, further advances in shipments of these products can be expected. Foreign orders for U.S. machinery rose again in September; new orders in the third quarter as a whole were nearly 20 per cent greater than the average rate in the first half of the year. Deliveries of commercial aircraft in September were the lowest in two years but advance information suggests a substantial pickup in October, with total deliveries in the fourth quarter expected to be greater than in the third quarter.

Exports to all areas were sharply higher in the third quarter than on average in the first half. The advance in shipments to Europe and Latin America was in nonagricultural commodities; shipments of agricultural goods to these areas showed little or no change from the relatively low level to which they had previously fallen. The growth in exports to Japan and to the less-developed countries of Asia and Africa was in both agricultural and nonagricultural commodities.

While there was a further rise in shipments of automobiles and parts to Canada, this was more than offset by declines in all other major categories of nonagricultural products, possibly reflecting the decline in industrial activity in Canada.

The import expansion in the third quarter was also widely distributed. Purchases of foreign consumer goods and machinery, which had increased sharply in the first half of the year despite the dock strike, rose further. In addition, arrivals of foodstuffs and industrial materials, which had declined in the first half from the levels in the last half of 1968, also advanced in the third quarter. The import/GNP ratio was a very high 3.9 per cent, slightly higher than in the first half and in calendar 1968.

Arrivals of foreign capital equipment, mainly machinery, were particularly strong in the third quarter, and more than kept pace with the sharp rise in total domestic expenditures on producers' durable equipment. Imports of nonfood consumer goods (other than automobiles) increased further in the third quarter, although somewhat more slowly than in the two preceding half-years, and continued to account for a rising portion of total expenditures on such goods. Arrivals of automobiles and parts also accelerated in the third quarter; imports both from Canada and other sources were at a rate more than one-fifth greater than in the first half. In the third quarter, foreign cars (other than from Canada) were 12.5 per cent of all new domestic car registrations compared with about 10.5 per cent in 1968 and in the first half of 1969. Preliminary reports for October indicate that sales of cars from Europe and Japan were over 100,000 units for the first time. Sales of Volkswagens, which had been running below those of 1968, turned up sharply in October to a new record.

Despite the levelling off in domestic industrial output, imports of almost all major categories of industrial materials -- paper, textiles, steel and other metals, and fuels -- were higher than in the first half of the year. This followed a dip in purchases of such imports from the last half of 1968 to the first half of this year. The principal exception to this general upturn in imports of materials was in building materials, reflecting lower lumber prices and the slowdown in housing starts. The increase in food imports was largely in meats, fish and cocoa.

Euro-dollar market. October's declining trend in Euro-dollar rates continued until just before the month end; the three-month deposit rate declined to 8-11/16 per cent per annum on October 27 -- its lowest level since May of this year -- and rates in all other maturities were well below 9 per cent. Since late October, however, there has been a sharp and generally steady advance in Euro-dollar rates, particularly in the three-month and longer maturities. The three-month rate advanced to about 11 per cent on November 19 while call and one-month funds were quoted around 9-1/2 per cent; and six- and twelve-month funds were 10-11/16 per cent and 10-1/4 per cent, respectively.

U.S. banks resumed active bidding for Euro-dollar funds just before the month-end, after having allowed their Euro-dollar borrowings through foreign branches to run off by about \$1.3 billion in the two weeks ended October 29. From October 29 to November 12, U.S. banks' liabilities to their foreign branches increased by over \$700 million

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

Average for week ending Wednesday	(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
Oct. 1	10.00	9.11	0.89	11.08	7.07	4.01
8	9.60	9.43	0.17	10.65	7.00	3.65
15	9.16	9.68	-0.52	10.39	7.02	3.37
22	8.90	8.68	0.22	9.63	6.94	2.69
29	8.58	8.39	0.19	9.10	7.00	2.10
Nov. 5	9.05	9.07	-0.02	9.89	7.01	2.88
12	8.80	9.32	-0.52	10.01	7.14	2.87
19	9.45	9.07 ^{p/}	0.38	10.71	7.12 ^{p/}	3.59

^{p/} Preliminary

(although foreign branch participations in head office domestic loans declined by about \$230 million). Data available through November 18 indicate a further rise in U.S. banks' borrowings of Euro-dollars.

It should be noted that part of the October decline in borrowings probably reflected a shifting of foreign official funds from branch to head office books -- largely in response to a bidding up, relative to Euro-dollar rates, of rates offered by U.S. banks for foreign official time deposits. (These deposits are not subject to Regulation Q and carry a reserve requirement of only 6 per cent, compared with the 10 per cent marginal rate on liabilities to branches.) Rates offered for these deposits (see table below) exceeded comparable Euro-dollar rates by 40 to 50 basis points in the last two weeks of October, and U.S. banks' time deposit (including C/D) liabilities to

foreign official institutions increased by about \$500 million during that period. Since the turn of the month the rates offered for these deposits have become less competitive with Euro-dollar rates and official time deposits have increased less rapidly -- by \$200 million in the two weeks ended November 12. This slowdown may also reflect the pressures put on total foreign official holdings of dollars by the large surpluses on the U.S. official settlements balance since the end of October.

Comparison of Euro-dollar Rates with Rates Offered by
Prime Banks in New York for Foreign Official Time Deposits

<u>Average for week ending Wednesday</u>	(1) 3-month Euro-\$ Deposit	(2) Foreign <u>1/</u> Official Time Dep. Rate	(3)=(1)-(2) Differ- ential
1968 - Dec. 25	7.33	6.25	1.08
1969 - June 28	11.11	9.00	2.11
Sept. 3	11.25	10.00	1.25
17	11.14	10.25	0.89
Oct. 1	11.08	10.75	0.33
15	10.39	10.13	0.26
22	9.63	10.13	-0.50
29	9.10	9.50	-0.40
Nov. 5	9.89	9.50	0.39
12	10.01	10.00	0.01

1/ Rates (most often quoted) by Prime New York banks and one Boston bank on 90-179 day funds; quoted as of the Monday prior to the dates in the table.

The continued very large-scale reflows of funds from the German mark, reflected in a \$1.8 billion decline in Bundesbank reserves from the end of October to November 19, offset by only about \$425 million of net purchases of dollars by other major central banks, may have contributed significantly to the availability of Euro-dollar funds for taking by the branches of American banks, although -- as noted in the discussion of the U.S. balance of payments -- much of the reflow from marks may have been directly to the United States.

Foreign exchange markets. Exchange market activity has been relatively calm since the German Government fixed the mark's new parity at 27.32 cents three-and-a-half weeks ago. The flow of speculative funds from marks has been large, and there has been some reflow of funds from Dutch guilders -- funds which had moved into guilders in anticipation of revaluation along with the mark. Demand for sterling has been strong -- at times quite buoyant; demand for the Italian lira has been firmer; and selling pressure on the French franc has moderated.

The German mark has been under fairly persistent selling pressure since October 27 -- the day the new parity became effective -- and the Bundesbank has sold about \$3 billion, holding the mark's rate at its lower limit. Since September 30 -- when the floating mark arrangement went into effect -- the Bundesbank has sold spot a total of \$4.1 billion. The Bundesbank's reserves of gold and foreign exchange have fallen to about \$7.8 billion, their lowest level since April. In addition, the

Bundesbank currently has outstanding forward contracts to receive dollars totalling slightly more than \$900 million, all of which mature before the end of the year.

Strong demand for sterling pushed the exchange rate up to just below \$2.399 during the first week of November, its highest level since April 1963. The greater demand for sterling was associated with the favorable prospects for further improvement in the British balance of payments, particularly since revaluation of the German mark, and some of the buying of sterling early in the month was in anticipation of announcement of the October trade figures. The U.K. trade account -- on the balance of payments basis -- continued in surplus for the third consecutive month, but the October surplus was only £3 million, down sharply from very favorable £25 million and £40 million surpluses in September and August, respectively. Since the trade figures announcement on November 13 sterling has turned softer and the Bank of England has not been able to purchase any dollars. From October 27 to November 12 it purchased \$500 million. The market for forward sterling continues to reflect increased confidence in the pound. The discount on 3-month sterling narrowed to around 1 per cent per annum before the end of October and has narrowed further in November, to about 0.30 per cent per annum on November 13.

Among other major currencies, the Netherlands Bank has sold about \$280 million since the mark's revaluation, about 40 per cent of

its dollar purchases during a four-week period of speculation on a guilder revaluation. Firming of demand for the French franc -- on the other hand -- enabled the Bank of France to purchase an estimated \$200 million between October 27 and November 18, which largely offset its dollar sales earlier in October. The market for Italian lire also turned around following the mark revaluation; the lira moved up to a level slightly above par -- its highest level in nine months -- and the Bank of Italy purchased about \$150 million, largely offsetting its early October dollar sales.

The price of gold has fallen sharply during the past four weeks. On November 19 the London fixing price was \$36.65 an ounce, down \$3.50 from October 27. The current price is the lowest gold has been since the two-tier gold arrangement has been in effect.

Financial market conditions in other industrial countries

In recent months monetary policy has assumed a more firmly anti-inflationary posture in virtually every part of the industrialized world except the United Kingdom, where policy had already become very restrictive. Since early July, nine important industrial countries have raised their official discount rate, and some have taken further measures to restrain credit expansion. For purely domestic reasons the discount rate has been increased in Germany, Switzerland, Canada, and Japan. The German authorities also increased reserve requirements--although they later reduced them after the mark revaluation--while in Switzerland credit expansion has been subjected to quantitative ceilings.

The discount rate has been raised also in France, Belgium (twice), Italy, Sweden, and the Netherlands. In each of these countries internal demand has been excessive, especially in France, where as a result the external accounts have remained in deficit, and where other restrictive measures have been taken lately in addition to the discount rate hike. In Belgium, Italy, and Sweden as well, there has been concern over the balance of payments and a desire to influence capital movements in a way favorable to those countries' official reserves.

Interest rates were already rising in most industrial countries during the first half of the year; they have since received further upward impetus from restrictive policy actions while economic activity and prices were rising. In some countries rates have held about steady since

June, but the only instance of an actual decline has been in bond yields in Britain, a drop--from an extraordinarily high peak--associated with the recent improvement in that country's balance of payments. During September speculative flows into German marks mitigated upward pressures on interest rates in Germany but added to such pressures in the many countries where the run to the mark caused a decline in official net foreign assets. Conversely, since the mark was set free to float on September 29 (a step followed by the establishment on October 26 of a new parity 9.3 per cent above the old one), flows of funds out of marks, and inflows into certain currencies that for a while were considered to be candidates for revaluation (the currencies of Belgium, the Netherlands, and Switzerland) have eased conditions in some centers while requiring the German authorities to move against an undesired tightening.

At this juncture it is impossible to point to an important industrial country where monetary conditions seem likely to become less tight in the near future. For Germany, it is true, the mark revaluation will ease the pressure of demand on resources, and in fact German officials have been saying they do not believe monetary conditions will tighten at all in the foreseeable future. But credit seems certain to become scarcer in France, and in Italy a pronounced shift in the direction of restraint has been indicated. And while the mark revaluation comes as a highly welcome event for international payments adjustment, it will intensify inflationary pressures in countries where increases in exports to Germany

could significantly affect national resource availability or where imports from Germany are an important item of national expenditure. The Netherlands, Belgium, Switzerland and Austria seem likely to feel these pressures the most.

Measures to restrain credit expansion in Germany would probably have been more severe than they were if the authorities had not wished to consider the desirability of maintaining the net outflow of long-term and other nonspeculative capital. Discount rate increases of one percentage point in April and June preceded the latest rise, also of one percentage point, to 6 per cent on September 11. Reserve requirements were increased 10 per cent effective August 1, following an increase of 15 per cent in June. The September discount rate increase was accompanied by a rise in the Bundesbank's Lombard rate (on advances) from 6 to 7.5 per cent. German money market rates rose from March to early October more or less in line with the discount rate.

German bond yields, which had risen appreciably during the second quarter, advanced scarcely further in most of the third. But they rose very sharply in the last two weeks of September in the wake of the discount rate increase. Net new issues of bonds by German and foreign borrowers in the German capital market averaged DM 1.9 billion per month in the third quarter, only a little above the average in the first half of the year. Foreign borrowers, continuing to find Germany an important source of new long-term funds, took almost a third of the total. They

SELECTED FINANCIAL YIELDS, MAJOR INDUSTRIAL COUNTRIES, 1969
(in per cent)

	Short-Term ^{a/}				Long-Term ^{b/}			
	Low	High	End- June	Latest	Low	High	End- June	Latest
Germany	3.88 2/28	7.50 11/13	6.00 6/27	7.50 11/13	6.19 2/28	7.13 11/13	6.69 6/27	7.13 11/13
France	7.75 2/7	9.88 6/27	9.88 6/27	9.50 11/8	7.02 3/1	7.78 10/31	7.55 6/27	7.78 10/31
Italy	--	--	--	--	6.46 Jan.	6.84 Sept.	6.55 June	6.84 Sept.
Netherlands	4.91 1/2	6.00 11/7	5.50 6/30	6.00 11/7	6.70 1/10	8.27 10/3	7.67 6/27	7.82 11/7
Belgium	5.00 1/13	8.50 11/17	6.55 6/30	8.50 11/17	6.65 1/2	7.86 10/1	7.16 7/1	7.82 11/1
Sweden	5.32 2/28	8.15 8/31	6.61 6/30	7.90 9/30	6.27 1/15	7.29 7/15	6.98 6/15	7.28 9/15
Switzerland	4.00 2/7	5.00 11/5	5.00 6/30	5.00 11/5	4.37 1/24	5.40 10/3	4.69 6/27	5.25 10/31
United Kingdom	6.53 2/14	7.71 6/20	7.58 6/27	7.61 10/31	8.05 1/2	9.66 6/12	9.47 6/26	8.81 11/6
Japan	6.94 6/27	8.25 11/8	7.30 6/30	8.25 11/8	8.71 1/31	8.96 4/30	8.80 6/30	8.76 8/31
Canada	6.01 2/14	7.53 10/3	6.89 6/27	7.43 11/13	7.17 1/22	8.15 11/12	7.55 6/25	8.15 11/12
Euro-dollar deposit	6.83 1/29	11.25 11/18	10.50 6/30	10.94 11/19	--	--	--	--

^{a/} Rates quoted are generally for 3-month funds, as follows: for Treasury bills in Belgium, the Netherlands, the United Kingdom, Sweden and Canada; for interbank loans in Germany; and for bank deposits in Switzerland. For France and Japan, the call loan rate is shown.

^{b/} All yields apply to long-term government bonds; most are composite yields, but yields on specific issues are shown for the United Kingdom and Canada.

floated bonds at an annual rate of DM 6.4 billion during the first nine months of this year (a \$1.6 billion rate at the old parity of 4 marks per dollar), up 20 per cent from a year earlier.

About \$500 million was added to German net official reserves in August and a further \$1.3 billion in September, increasing in like amount the reserve base of the German banking system and thereby permitting a substantial reduction of borrowings from the central bank and a generation of excess reserves. After the mark was floated and then revalued, profit-taking by speculators together with the continuing deficit on current and long-term capital account caused official reserves to decline \$1.5 billion in October and a further \$1.8 billion in the first 19 days of November. On November 6, to prevent expected further reserve losses from tightening the money market, the Bundesbank lowered reserve requirements by 10 per cent and abolished the 100 per cent marginal reserve requirement against foreign liabilities that had been imposed on December 1, 1968. Interest rates in Germany declined in October but rose again in early November.

In the Netherlands the Treasury bill yield climbed approximately a full percentage point, and government bond yields about 60 basis points, between the end of June and the end of September; the discount rate was raised from 5-1/2 to 6 per cent on August 2. A new agreement between the Netherlands Bank and the Dutch commercial and agricultural banks permits the banks to expand outstanding short-term credits to the private sector at no more than a 10 per cent annual rate, seasonally adjusted, in the

final four months of 1969; the same rate of increase had been allowed in the first eight months. Violations of the ceilings have occurred despite penalties.

In October, prior to the mark revaluation, Dutch net official reserves increased about \$750 million as speculation on a guilder revaluation mushroomed after the earlier floating of the mark. The resultant flood of liquidity to the banking system brought both short- and long-term interest rates down, particularly the call loan rate. After the Dutch Government's announcement on October 27 that the guilder would not be revalued, reserves decreased nearly \$300 million through November 12.

The Swiss National Bank raised its discount rate from 3 per cent to 3.75 per cent on September 15. The rate for 3-month bank deposits has not changed since June, but the composite yield on Swiss government bonds rose about 70 basis points in the third quarter before falling back around 15 points in October. The weakening of bond prices was probably related to the conclusion of a new agreement between the Swiss National Bank and Swiss commercial banks concerning credit expansion, a type of credit control device previously employed in Switzerland from 1962 to 1967. The new agreement limits credit expansion to 9 per cent over the 12 months from July 31, compared with an annual rate of increase in the region of 15 per cent in the first seven months of this year.

A variety of new actions have been taken in France in further attempts to cool off a badly overheated economy. After the devaluation of the franc on August 3 the National Credit Council raised interest rates

on many types of loans made by public lending agencies. In particular, the rate of interest on loans by the Crédit National (medium- and long-term loans to industry for purchase of equipment) was raised from 7.25 to 8.75 per cent. To curb consumer buying, the terms of installment credit were again tightened in September and are now very severe. On purchases of new automobiles, for example, the minimum downpayment was increased from 30 to 50 per cent, and the maximum repayment period was shortened from 21 to 15 months. The immediate effect of this tightening will be enhanced by the authorities' declaration that the terms will revert to their former, less severe condition after next January.

Quantitative restrictions on bank credit expansion have been extended from the year-end through June 1970. Short-term credit outstanding at the end of next June can be only 2.9 per cent more than at the end of June 1969, an allowed rise that compares with an actual increase of over 11 per cent in the 12 months to last June. French banks have been operating under credit ceilings since the beginning of this year, and while the ceilings have not yet had much if any effect on total spending in France it is believed they will do so soon. Penalties against banks violating the ceilings were introduced in September and made more severe recently. The ceilings on short-term loans will be supplemented with new directives designed to stop practices that have allowed them to be partially circumvented. To this end, formal ceilings have now been placed on banks' medium-term loans, which play an important role in the

French credit picture. In addition, equipment loans by the Crédit National will be severely restricted (as well as more costly), and credit expansion by consumer finance houses will be held more tightly in check.

The Bank of France has kept short-term interest rates at very high levels. The call money rate of 9.5 per cent on November 8 was indicative of the levels that have prevailed since June; the latest tender rate for 1-year Treasury bills was 10.1 per cent. The increase in the discount rate from 7 to 8 per cent on October 8--the highest level in more than a century--had no perceptible effect on money market rates because of the much higher level of the latter, a gap now diminished but still large. The discount rate rise led to a one percentage point increase in the banks' lending rate to prime borrowers, which now stands at 9.75 per cent. A rise in bond yields in October probably reflected anticipation of the new quantitative credit controls.

Increases in the discount rate of the National Bank of Belgium on July 31 and September 18 were the sixth and seventh since December 1968 and took the rate from 6 to 7-1/2 per cent. The Treasury bill rate rose approximately two full percentage points in the third quarter and the composite yield on government bonds about 70 basis points. In raising the discount rate the National Bank was concerned with both strong demand pressures at home and the high levels of Euro-dollar rates which, over the past year, have pulled a substantial volume of funds from Belgium.

The September action was also influenced by the adverse speculation that assailed the Belgian franc after the French franc was devalued, and by the prospect of speculative flows from Belgian francs to German marks. As it happened, Belgian net official reserves were unchanged for September as a whole. In October, reserves rose about \$300 million as speculators in marks took profits and also moved funds to Belgium in expectation of a possible upward revaluation of the franc. This increase helped stabilize short-term interest rates, while bond yields dipped.

Monetary policy has tightened in Italy after five years of relative ease. The increase on August 14 from 3-1/2 to 4 per cent in the basic rate for rediscounts and (more importantly) advances by the central bank was the first in 11 years. Simultaneously, the penalty discount rate introduced July 1 (applicable to most rediscounts now being made) was hiked from 5 to 5-1/2 per cent, and increases of 1/2 per cent were also made in the penalty rates applied to excessive advances, which now range from 4-1/2 to 5-1/2 per cent. In July and August, Italian commercial banks raised their prime rate in two steps by a total of 1.25 percentage points. Bond yields, which had been held nearly stable by the monetary authorities for 3 years, have advanced considerably, the composite yield on all bonds except Treasury bonds advancing from a monthly average of 6.50 per cent in May to 6.84 per cent in September.

Price increases in Italy have accelerated this year. Important wage negotiations are under way or will soon be, which according to estimates may raise hourly earnings in 1970 as much as 12 per cent over

1969 and add about 7 per cent to unit labor costs. Recent actions by the Bank of Italy may have reflected the belief that a less easy monetary atmosphere would temper the size of eventual wage increases. In addition, the outflow of capital has continued at a very heavy rate that will mean an overall balance of payments deficit this year in the neighborhood of \$1.5 billion. Even though capital outflows may be in large measure a consequence of conditions unrelated to the current state of financial markets, higher interest rates in Italy relative to those abroad would presumably reduce the outflow.

According to reports, a statement by Treasury Minister Colombo on October 31 announced a severe tightening of monetary policy. The Minister is alleged to have said that the Bank of Italy will now keep the money supply from rising faster than real GNP. Output of goods and services in Italy will increase in 1970 by about 6-1/2 per cent according to OECD projections. The money supply was expanding by around 15 per cent a year up to last June, before slowing down in July-August.

The Swedish authorities raised the discount rate from 6 to 7 per cent on July 11 because of both overly strong internal demand and declines in official reserves in the first half of the year. This move was accompanied by the reintroduction of cash reserve requirements and of ceilings on Riksbank advances to the commercial banks. The Treasury bill rate has risen since June by more than the rise in the discount rate, and bond yields have also risen. The prospect of continued intense pressure on resources in the near future makes monetary relaxation improbable.

Monetary policy in the United Kingdom remains restrictive notwithstanding improvement in the balance of payments, which is thought to have been in surplus (current and long-term capital accounts) at an annual rate of about \$1.2 billion in the second and third quarters. In mid-October the clearing banks' outstanding advances were still in excess of the ceiling laid down by the Bank of England. The clearing banks' advances to the private sector are subject to a ceiling equal to 98 per cent of the level in November 1967, but the actual level is now 102 per cent. The absence of a critical Bank of England reaction to this latest violation of its guideposts should not, however, be interpreted as a move in the direction of easier credit policy. Rather, it may be looked upon as appropriate now that the import deposit plan has been extended for another year, instead of lapsing on December 4 as had been scheduled, and given the authorities' success in keeping overall domestic credit expansion within targets announced last spring. The plan has been liberalized by reducing the required deposits from 50 per cent of imports to 40 per cent, but its retention will nevertheless lock up funds that were previously expected to be added to firms' readily usable cash balances.

In September the clearing banks broke with tradition by raising their prime rate from 8-1/2 per cent to 9 per cent, a full percentage point above the discount rate instead of the customary half point.

Even though no relaxation of curbs on credit, and no reduction of short-term interest rates, seem in the offing in Britain, there has been a substantial decline in bond yields since mid-September. The

8.81 per cent yield on War Loan compares with nearly 9-1/2 per cent in early September, prior to reports of improvements in Britain's balance of payments and trade position. In October the trade surplus (balance of payments basis), though smaller than in August or September, was still more favorable than for several years prior to August.

The money supply in the United Kingdom, seasonally adjusted, declined 0.7 per cent from December 1968 to June 1969, in contrast with increases of 3.1 per cent and 3.4 per cent during the first and second halves of 1968, respectively. The change reflects in part a greater determination to control domestic credit expansion, in particular a greater willingness of the Bank of England to refrain from supporting the government bond market, or to sell bonds on the open market (with offsetting absorption of bills) even though bond sales would depress prices. In previous years, concern over bond prices frequently meant pumping money into the economy and liquidity into the banking system when "tight money" was supposedly the order of the day.

Monetary policy in Japan took a restrictive turn with the raising of the discount rate from 5.84 per cent to 6.25 per cent on September 1. This step, which was accompanied by increases of 0.25 or 0.50 percentage points in reserve requirements, caused the call loan rate to jump 0.30 point. With private credit demands continuing to expand briskly, the average rate on bank loans and discounts moved up a bit in August and September. Booming business conditions entailing accelerating price and wage increases have convinced the government of the

need for higher yields on new bond issues, which in Japan are controlled by the government through its rationing of borrowers' access to the new issues market. The yield on new issues of grade A industrial bonds is due to be raised from 8.2 per cent to 8.4 per cent in December, and higher yields are also planned for government bonds, bank debentures, and government-guaranteed bonds issued primarily by utilities and other public corporations.

The degree of restrictiveness of Canadian monetary policy has not changed perceptibly since the discount rate was increased from 7-1/2 per cent to 8 per cent on July 16. Present policy has kept the money supply nearly stable: as defined to include time deposits denominated in Canadian dollars, the money supply expansion during August-October was 0.6 per cent at an annual rate. Bank liquidity positions are extremely tight. The ratio of banks' "more liquid" assets (which include cash reserves, call loans, all government securities, and net foreign assets) to their total assets declined from the so-called normal level of 30 per cent last March to 27 per cent in June, and shrank slightly further to 26.5 in October, a level thought to be an historic low.

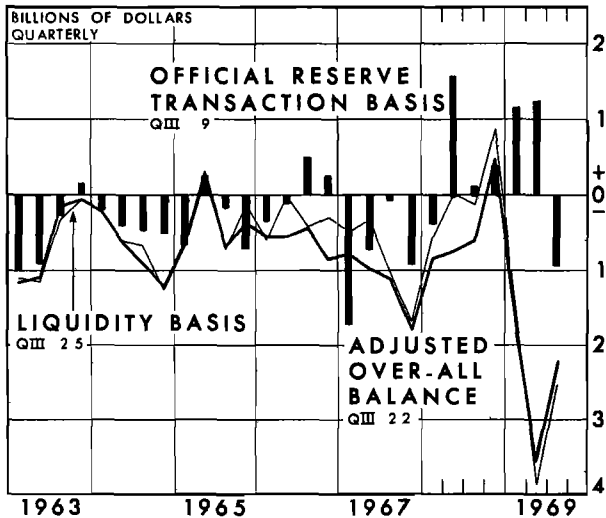
The bill rate changed little in the third quarter after the discount rate increase, but dipped in October when Canada's official reserves rose \$95 million in reflection of an increased flow of funds from the United States into Canadian finance company paper and a fairly large volume of conversions of new bond issues by Canadian borrowers in the U.S. market. Recent remarks by Governor Rasminsky strongly imply that

an easing of monetary restraint is nowhere in sight. Following declines in October, Canadian bond yields touched new highs during the first half of November.

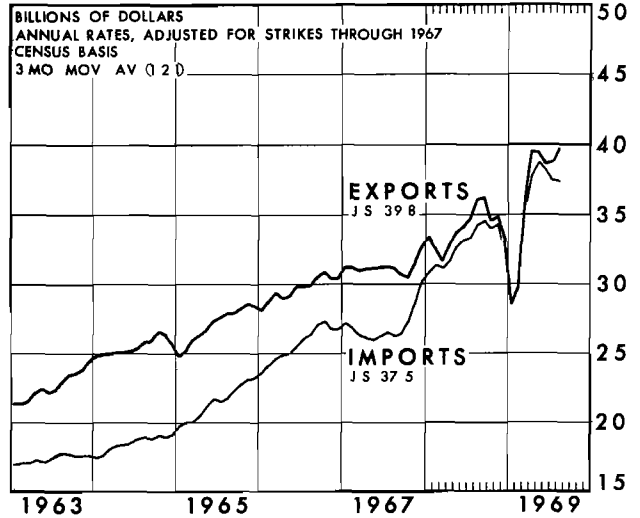
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

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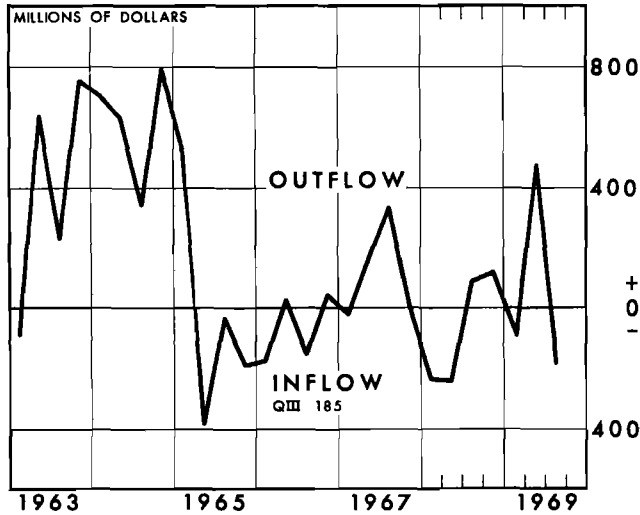
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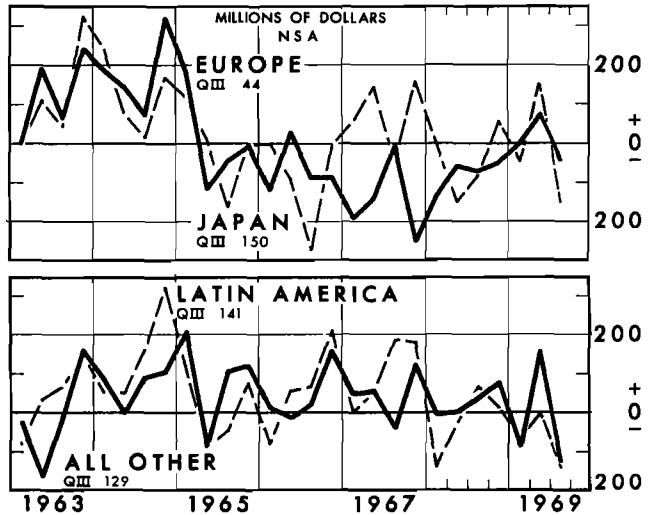
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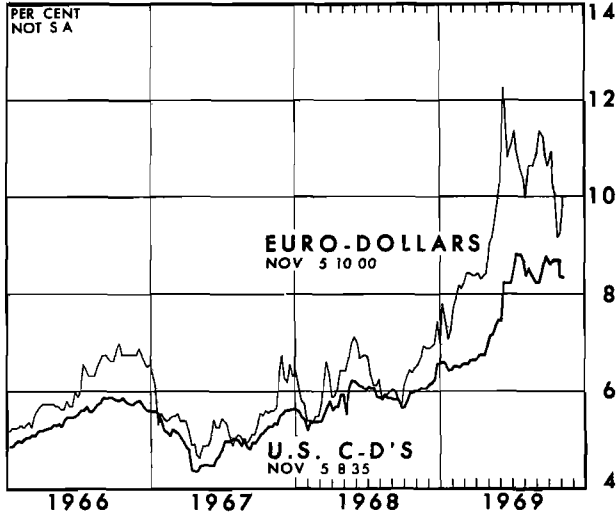
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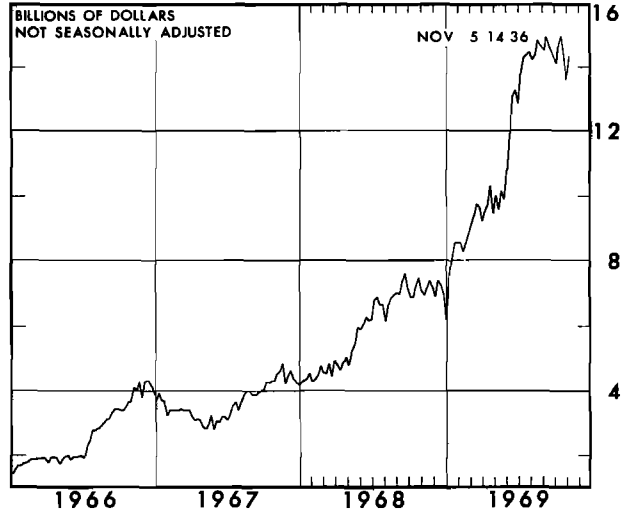
U.S. BANK CREDIT OUTFLOWS



90-DAY RATES



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APPENDIX A: TWO SPECIAL MORTGAGE MARKET DEVELOPMENTS IN 1969*

Many market analysts believe that trends in private housing starts depend heavily on net savings flows to S&L's and savings banks. So far in 1969, however, a number of developments in the mortgage market and elsewhere have changed this dependence at least temporarily. Among these developments has been greater reliance by S&L's on non-deposit sources of funds furnished through the FHLBank System. Another has been increased credit made available by a non-deposit intermediary--FNMA. Both developments have helped to maintain mortgage commitments and housing starts at higher levels than could have been supported solely by the sharply reduced net savings inflows to the thrift institutions.

S&L borrowing. While net savings inflows to S&L's during the first nine months of 1969 declined less sharply than in the same period of 1966, as shown in the upper panel of Chart 1, they have followed a similar downtrend. However, as shown in the second panel of the chart, S&L cash flow other than borrowing from the FHLBanks--that is, net savings flows plus mortgage repayments and reductions in liquid asset holdings--has dropped less drastically than in 1966, reflecting in part more lenient liquidity regulation by the FHLBank Board. And as indicated in the lower panel of the chart, S&L total cash flow, including substantial borrowing from the FHLBanks, has remained considerably above 1966 levels.

Partly as a result, S&L mortgage commitments against both new and existing properties have continued stronger than in 1966. FHLBank Board pronouncements in late 1968 and early 1969, suggesting that FHLBank advances would remain available, were an important factor in helping to limit the extent of the decline in S&L commitment activity so far this year.

FNMA. In its changed role as a semi-private corporation, FNMA has auctioned off a record amount of mortgage purchase commitments in 1969, and its commitment backlog has expanded to new highs. During 1966, by contrast, this type of market support was minimal. Operating then as a wholly Government-owned agency, FNMA generally limited its commitments to very short terms, and restricted them severely because of budgetary as well as statutory constraints.

As one measure of its market support in the present circumstances, FNMA's total new mortgage commitments made during the first three quarters of 1969 have amounted to as much as a third of all commitments approved by insured S&Ls, as shown in the upper panel of Chart 2. In contrast, over the same period of 1966, FNMA's restricted volume of new commitments came to only a sixth of the severely reduced S&L total. This year, also, FNMA's outstanding commitments--some for long-delayed takedown--have risen by \$2.1 billion to a level more than one-half that

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