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CONFIDENTIAL (FR)

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

March 15, 1972

By the Staff
Board of Governors
of the Federal Reserve System

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DOMESTIC NONFINANCIAL SCENE

March 14, 1972

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SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally adjusted)

	1971		1972		Per Cent Change* From		
	Nov.	Dec.	Jan.	Feb.	1 mo. ago	3 mos. ago	Year ago
Civilian labor force (mil.)	85.1	85.2	85.7	85.5	-0.2	0.5	2.6
Unemployment rate (%)	6.0	6.0	5.9	5.7	--	--	5.9 4/
Insured unempl. rate (%) 5/	4.2	3.8	3.4	n.a	--	--	3.7 4/
Nonfarm employment, payroll (mil.)	71.0	71.2	71.6	71.7	0.1	0.9	1.8
Manufacturing	18.6	18.6	18.6	18.6	0.1	0.1	0.3
Nonmanufacturing	52.4	52.6	53.0	53.1	0.1	1.2	2.6
Industrial production (1967=100)	107.0	107.6	108.2	109.0	0.7	1.9	3.1
Final products, total	105.9	105.6	106.0	106.7	0.7	0.8	3.6
Consumer goods	118.2	117.7	118.3	119.0	0.6	0.7	5.4
Business equipment	97.0	97.0	97.6	98.3	0.7	1.3	2.4
Materials	106.0	107.5	108.4	109.7	1.2	3.5	2.7
Capacity util. rate, mfg.	73.7	73.8	74.0	74.2	--	--	74.9 4/
Wholesale prices (1967=100) 1/	114.5	115.4	116.3	117.3	0.9	2.4	4.0
Industrial commodities (FR) 5/	114.7	115.2	115.8	n.a.	0.5	0.9	3.4
Sensitive materials (FR) 5/	115.3	116.1	117.8	n.a.	1.5	2.1	8.2
Farm products, foods & feeds	113.6	115.9	117.4	119.6	1.9	5.3	5.3
Consumer prices (1967=100) 1/ 5/	122.6	123.1	123.2	n.a.	0.1	0.7	3.4
Food	119.0	120.3	120.3	n.a.	0.0	1.2	4.2
Commodities except food	118.1	118.1	117.7	n.a.	-0.3	-0.3	2.2
Services	130.4	130.8	131.5	n.a.	0.5	1.2	4.1
Hourly earnings, pvt. nonfarm ($)	3.48	3.52	3.54	3.54	0.0	1.7	5.7
Hourly earnings, mfg. ($)	3.60	3.68	3.68	3.71	0.8	3.1	5.7
Weekly earnings, mfg. ($)	144.72	147.81	148.15	149.45	0.9	3.3	7.3
Net spend. weekly earnings, mfg. (3 dependents 1967 $) 1/ 5/	102.78	105.81	105.11	n.a.	-0.7	2.6	3.3
Personal income ($ bil.) 2/ 5/	874.9	883.9	891.1	n.a.	2.3	0.8	7.4
Retail sales, total ($ bil.)	35.6	34.9	35.0	34.9	-0.2	-1.9	6.3
Autos (million units) 2/	7.2	6.6	6.6	6.4	-2.5	-11.1	5.8
GAAF ($ bil.) 3/	9.3	9.2	9.4	9.4	0.3	1.4	8.7
12 leaders, composite (1967=100) 5/	130.3	131.8	134.8	n.a.	2.3	4.3	13.6
Selected leading indicators:							
Housing starts, pvt. (thous.) 2/ 5/	2,228	2,433	2,549	n.a.	4.8	25.1	40.8
Factory workweek (hours)	40.1	40.3	40.0	40.4	1.0	0.7	1.5
Unempl. claims, initial (thous.) 5/	304	268	264	n.a.	1.8 6/	15.8 6/	7.0 6/
New orders, dur. goods, ($ bil.) 5/	32.6	32.1	35.3	n.a.	9.7	13.3	11.3
Capital equipment	8.4	8.5	8.9	n.a.	4.0	9.3	9.0
Common stock prices (41-43=10)	92.78	99.17	103.30	105.08	1.7	13.3	8.2

* Based on unrounded data. 1/ Not seasonally adjusted. 2/ Annual rates.
3/ Gen'l. merchandise, apparel, and furniture and appliances. 4/ Actual figures.
5/ Per cent calculated to January, 1972. 6/ Sign reversed.

DOMESTIC NONFINANCIAL SCENE

Summary and GNP outlook. Recent data continue to suggest an increase in real GNP in the first quarter at an annual rate of about 6 per cent. The post-freeze bulge in prices has been somewhat larger than anticipated, however, and the projected GNP deflator for the first quarter has been raised. Projected growth in nominal GNP has also been lifted to $31 billion.

On the expansive side, the index of industrial production rose 0.7 per cent in February, with increases widespread in consumer goods, business equipment, and materials. The January index was revised up, and for both months combined the advance was at an annual rate of close to 8 per cent. Recent surveys of plant and equipment spending plans have lifted earlier anticipations. Manufacturers' new orders for durable goods rose sharply, with orders for capital equipment up further. The inventory-sales ratio for manufacturing and trade fell in January to the lowest level in more than five years. Residential construction activity has continued to advance strongly, with housing starts in January at a new high.

On the other hand, retail sales have remained on the sluggish side; sales were little changed in January and February. Unit sales of domestic-type autos through early March this year were at an 8.5 million annual rate, only a little above the rate prevailing in 1971 before the major August changes in economic policy. Sales of imported cars have been strong.

The labor market recently has shown signs of improvement. The unemployment rate declined in February, to 5.7 per cent from 5.9 per cent in January, in part reflecting a decline in the labor force. Nonfarm payroll employment rose somewhat in February, and the January figures were revised to show a substantial advance. The increase has been concentrated in non-industrial activities; manufacturing employment, however, has shown little change. The rise in average hourly earnings slowed to quite moderate proportions from December to February, following the post-freeze bulge in December.

Wholesale prices have continued to rise rapidly. In February an exceptionally large increase occurred for farm products and foods, which are largely uncontrolled. The rise in prices of industrial commodities continued close to the 5 per cent annual rate of January.

Gross national product--outlook. Recent data suggest a stepped-up pace of growth in industrial activity this year, tending to confirm earlier staff expectations of a sizable expansion in aggregate output. For the year 1972 as a whole, nominal GNP is now projected to be about $98 billion larger than in 1971, a slightly greater increase than last time, while real GNP is projected to increase 5.6 per cent, the same as in our previous projection. From late 1971 to late 1972, though, real GNP growth is projected at around 6-1/2 per cent, and the unemployment rate is expected to decline gradually to 5.4 per cent in the fourth quarter.

GNP PROJECTIONS

	Change in Nominal GNP $ billion		Per cent increase, annual rate: Real GNP		Per cent increase, annual rate: Private GNP fixed weight price index		Unemployment rate	
	2/9/72	Current	2/9/72	Current	2/9/72	Current	2/9/72	Current
1971-IV 1/	19.6	19.5	6.1	5.8	1.5	1.8	5.9	5.9
1972-I	30.0	31.1	5.9	5.9	4.0	4.4	5.8	5.8
1972-II	26.5	27.0	6.5	6.3	3.1	3.2	5.7	5.7
1972-III	25.5	26.5	6.1	6.5	2.9	2.8	5.6	5.6
1972-IV	27.6	27.5	6.7	6.7	2.8	2.8	5.4	5.4

1/ Published Commerce estimate.

Business fixed investment is projected to increase about 11 per cent for the year 1972--rather than the previous 9 per cent--in line with indications from the most recent Commerce-SEC and McGraw-Hill Surveys. Residential construction activity is expected to level off in the second half of the year, following the unexpectedly large first quarter gain, as housing starts drift down from recent record levels. Consumer spending is projected roughly to keep pace after the disappointing first quarter with the substantial increase expected in disposable income.

Recent price developments have led the staff to raise the GNP price deflator for the second quarter, as well as the first, but the index is still projected to slow to an annual rate of increase of less than 3 per cent in the second half of the year. This expectation is based on evidence that the rise in wage rates is moderating, the sizable projected rise in real product and associated productivity gains, and a judgment that recent price developments represented a temporary bulge.

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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.)

	1971	1972 Proj.	1971 III	1971 IV	1972 Projected I	1972 Projected II	1972 Projected III	1972 Projected IV
Gross National Product	1046.8	1144.4	1053.4	1072.9	1104.0	1131.0	1157.5	1185.0
Final purchases	1044.5	1137.2	1054.6	1070.4	1100.0	1126.0	1149.3	1173.3
Private	811.5	881.2	820.8	829.6	852.0	871.3	891.1	910.4
Excluding net exports	811.5	880.7	820.8	834.2	853.0	870.8	889.9	909.2
Personal consumption expenditures	662.1	711.1	668.8	677.2	687.9	702.7	718.4	735.4
Durable goods	100.5	111.7	102.8	103.6	107.1	110.0	113.0	116.5
Nondurable goods	278.6	295.4	280.2	283.3	285.3	291.7	298.7	306.0
Services	282.9	304.0	285.8	290.3	295.5	301.0	306.7	312.9
Gross private domestic investment	151.6	176.9	150.8	159.4	169.1	173.1	179.7	185.5
Residential construction	40.6	49.0	42.7	44.4	48.6	49.1	49.5	48.8
Business fixed investment	108.7	120.6	109.3	112.6	116.5	119.0	122.0	125.0
Change in business inventories	2.2	7.2	-1.2	2.4	4.0	5.0	8.2	11.7
Nonfarm	1.7	7.2	-2.0	2.0	3.8	5.0	8.2	11.7
Net exports of goods and services	0.0	0.5	0.0	-4.6	-1.0	0.5	1.2	1.2
Exports	65.3	72.4	68.2	60.4	70.1	71.6	73.1	74.9
Imports	65.3	72.0	68.2	65.0	71.1	71.1	71.9	73.7
Gov't. purchases of goods & services	233.0	256.0	233.8	240.8	248.0	254.7	258.2	262.9
Federal	97.6	106.7	97.6	100.3	105.0	108.2	107.2	106.4
Defense	71.4	75.7	70.2	71.4	74.5	76.5	75.9	75.9
Other	26.2	31.0	27.4	28.9	30.5	31.7	31.3	30.5
State & local	135.5	149.3	136.2	140.5	143.0	146.5	151.0	156.5
Gross national product in constant (1958) dollars	739.4	781.0	740.7	751.3	762.4	774.4	787.0	800.1
GNP implicit deflator (1958 = 100)	141.6	146.5	142.2	142.8	144.8	146.0	147.1	148.1
Personal income	857.0	922.8	864.6	876.7	897.5	913.6	931.6	948.3
Wage and salary disbursements	574.2	625.0	577.3	587.0	606.5	619.2	630.8	643.4
Disposable income	741.3	797.1	748.5	755.0	771.9	790.1	806.2	820.2
Personal saving	60.5	66.5	61.0	59.0	64.9	68.0	68.1	64.8
Saving rate (per cent)	8.2	8.4	8.2	7.8	8.4	8.6	8.5	7.9
Corporate profits before tax	85.2	100.1	85.8	85.0e	91.0	96.5	103.0	110.0
Corp. cash flow, net of div. (domestic)	80.8	96.5	82.4	82.1e	90.2	94.6	96.8	104.5
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	198.7	217.2	197.8	203.1e	212.8	213.4	218.5	223.9
Expenditures	221.9	248.2	224.6	228.7	239.0	248.5	251.9	253.4
Surplus or deficit (-)	-23.1	-31.1	-26.7	-25.6e	-26.2	-35.1	-33.4	-29.5
High employment surplus or deficit (-)	2.9	-5.9	1.3	6.6	2.0	-6.9	-9.9	-8.7
Total labor force (millions)	86.9	88.8	87.0	87.7	88.3	88.5	88.9	89.4
Armed forces "	2.8	2.5	2.8	2.7	2.6	2.5	2.5	2.5
Civilian labor force "	84.1	86.3	84.2	85.0	85.7	86.0	86.4	86.9
Unemployment rate (per cent)	5.9	5.6	6.0	5.9	5.8	5.7	5.6	5.4
Nonfarm payroll employment (millions)	70.7	72.3	70.6	71.0	71.6	72.1	72.5	73.1
Manufacturing	18.6	18.8	18.5	18.6	18.6	18.7	18.8	18.9
Industrial production (1967 = 100)	106.3	112.6	105.9	107.0	109.1	111.3	113.7	116.3
Capacity utilization, manufacturing (per cent)	74.4	75.5	73.9	73.8	74.3	75.0	75.9	76.9
Housing starts, private (millions, A.R.)	2.05	2.25	2.11	2.23	2.40	2.30	2.20	2.10
Sales new autos (millions, A.R.)	10.13	10.63	10.27	10.43	10.35	10.50	10.70	10.90
Domestic models	8.68	9.09	8.74	9.18	8.75	9.00	9.20	9.40
Foreign models	1.46	1.53	1.53	1.25	1.60	1.50	1.50	1.50

NOTE: Projection of related items such as employment and industrial production index are based on projection of deflated GNP. Federal budget high employment surplus or deficit (N.I.A. basis) are staff estimates and projections by method suggested by Okun and Teeters.

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CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1971	1972 Proj.	1971 III	1971 IV	1972 Projected I	1972 Projected II	1972 Projected III	1972 Projected IV
	---Billions Of Dollars---							
Gross National Product	72.7	97.6	13.4	19.5	31.1	27.0	26.5	27.5
Inventory change	-0.6	5.0	-5.8	3.6	1.6	1.0	3.2	3.5
Final purchases	73.2	92.7	19.2	15.8	29.6	26.0	23.3	24.0
Private	59.6	69.7	15.0	8.8	22.4	19.3	19.8	19.3
Excluding net exports	63.2	69.2	15.1	13.4	18.8	17.8	19.1	19.3
Net exports	-3.6	0.5	-0.1	-4.6	-3.6	1.5	0.7	0.0
Government	13.6	23.0	4.2	7.0	7.2	6.7	3.5	4.7
GNP in constant (1958) dollars	19.4	41.6	4.9	10.6	11.1	12.0	12.6	13.1
Final purchases	19.6	37.9	9.5	7.7	10.5	10.8	10.2	10.3
Private	19.8	32.7	6.9	4.1	10.4	8.6	10.3	9.9
	---In Per Cent Per Year---							
Gross National Product	7.5	9.3	5.2[1/]	7.6[1/]	11.6	9.8	9.4	9.5
Final purchases	7.5	8.9	7.4	6.0	11.1	9.5	8.3	8.4
Private	7.9	8.6	7.4	4.3	10.8	9.1	9.1	8.7
Personal consumption expenditures	7.5	7.4	7.0	5.0	6.3	8.6	8.9	9.5
Durable goods	13.4	11.1	14.9	2.7	13.5	10.8	10.9	12.4
Nondurable goods	5.3	6.0	3.5	4.4	2.8	9.0	9.6	9.8
Services	7.8	7.5	7.6	6.3	7.2	7.4	7.6	8.1
Gross private domestic investment	12.0	16.7	-5.5	22.8	24.3	9.5	15.2	12.9
Residential construction	33.6	20.7	27.0	15.9	37.8	4.1	3.3	-5.7
Business fixed investment	6.5	10.9	3.7	12.1	13.9	8.6	10.1	9.8
Gov't. purchases of goods & services	6.2	9.9	7.3	12.0	12.0	10.8	5.5	7.3
Federal	0.4	9.3	6.7	11.1	18.7	12.2	-3.7	-3.0
Defense	-5.3	6.0	-6.7	6.8	17.4	10.7	-3.1	0.0
Other	19.6	18.3	45.5	21.9	22.1	15.7	-5.0	-10.2
State & local	10.9	10.2	7.8	12.6	7.1	9.8	12.3	14.6
GNP in constant (1958) dollars	2.7	5.6	2.7[1/]	5.8[1/]	5.9	6.3	6.5	6.7
Final purchases	2.7	5.1	5.2	4.2	5.6	5.7	5.3	5.3
Private	3.4	5.5	4.6	2.7	6.9	5.6	6.6	6.2
GNP implicit deflator	4.7	3.5	2.5[1/]	1.7[1/][3/]	5.6[4/]	3.4	2.8	2.8
Private GNP fixed weight index[2/]	5.3	3.3	3.6[1/]	1.8[1/]	4.4	3.2	2.8	2.8
Personal income	6.6	7.7	5.2	5.6	9.5	7.2	7.9	7.2
Wage and salary disbursements	6.1	8.8	4.4	6.7	13.3	8.4	7.5	8.0
Disposable income	7.8	7.5	4.8	3.5	9.0	9.4	8.2	6.9
Corporate profits before tax	13.0	17.5	-5.1	-3.7	28.2	24.2	26.9	27.2
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	3.8	9.3	0.2	10.7	19.1	1.1	9.6	9.9
Expenditures	8.2	11.9	5.8	7.3	18.0	15.9	5.5	2.4
Nonfarm payroll employment	0.1	2.3	-0.2	2.3	3.4	2.8	2.2	3.3
Manufacturing	-3.9	1.1	-2.4	2.2	0.0	2.2	2.1	2.1
Industrial production	-0.4	5.9	-3.4	4.2	7.7	8.2	8.6	9.1
Housing starts, private	43.4	9.8	36.5	22.7	30.5	-16.7	-17.4	-18.2
Sales new autos	21.3	4.9	19.0	6.2	-3.1	5.8	7.6	7.5
Domestic models	21.9	4.7	22.7	20.1	-18.7	11.4	8.9	8.7
Foreign models	18.7	4.8	-1.0	-73.2	112.0	-25.0	0.0	0.0

1/ At compound rates.

2/ Using expenditures in 1967 as weights.

3/ Excluding the first $1.2 billion, annual rate, of the volunteer army pay increase, 1.2 per cent per year.

4/ Excluding the remaining $1.2 billion, annual rate, of the volunteer army pay increase and the general Federal employees pay increase, 4.4 per cent per year.

Industrial production. The production index increased 0.7 per cent further in February from a January level revised upward by 0.3 per cent. Gains were widespread among final products and materials and the index was up at an annual rate of nearly 8 per cent from December. The total index in February was only 3 per cent above a year ago and still 2.6 per cent below the September 1969 high.

Output of consumer durable goods rose over 2 per cent in February, with auto assemblies up 3.5 per cent to an annual rate of 8.4 million units. Auto assemblies are scheduled to change little in March and to edge up to an 8.8 million rate in April and May. Output of most major groups of home goods is estimated to have increased further. Output of television sets, after rising almost one-fifth from November to January, leveled off at that advanced rate in February. Production of consumer nondurable goods apparently was little changed in February, following an advance of about 5 per cent over the past year.

Production of business equipment, which had changed little from August to December, picked up in January and rose more broadly in February. This has been the first general rise in the capital goods industries since the initial limited recovery in the spring of last year, and in February output was 4 per cent above the May 1971 low. Meanwhile, output of defense equipment industries has leveled off in recent months, after a sharp and sustained decline since the fall of 1969.

Output of materials rose further in February with increases widespread, including steel, textiles, and chemicals.

INDUSTRIAL PRODUCTION
(1967=100, seasonally adjusted)

	1972		Percentage change to Feb 1972 from		
	pJan	eFeb	Jan 1972	Feb 1971	Sept 1969*
Total index	108.2	109.0	.7	3.1	-2.6
Consumer goods	118.3	119.0	.6	5.4	6.0
Autos	102.8	106.4	3.5	-5.7	-8.7
Home goods	116.3	118.4	1.8	11.2	6.1
Apparel & staples	119.3	119.4	.1	4.9	7.3
Business equipment	97.6	98.3	.7	2.4	-10.9
Defense equipment	74.3	74.7	.5	-4.4	-27.0
Intermediate products	115.5	116.1	.5	3.2	3.6
Construction products	116.8	117.3	.4	4.8	4.8
Materials, total	108.4	109.7	1.2	2.7	-4.1
Durable	102.2	103.5	1.3	1.9	-9.9
Steel	95.2	96.5	1.4	-7.9	-17.3
Nondurable	115.8	117.4	1.4	4.7	3.2

* Pre-recession peak for the total index.
e Estimated.
p Preliminary.

<u>Retail sales.</u> Sales in February were essentially unchanged from January, according to the advance report. The January-February average was slightly lower than in the fourth quarter, but excluding auto and nonconsumer items, sales showed a small increase. Compared with a year ago, February sales were up 6.3 per cent.

More complete sample counts for December and January resulted in upward revisions for both months, especially in the GAAF groups. Sales in December are now indicated to have declined 1.9 per cent rather than 2.6 per cent, while January sales remain virtually unchanged from December.

RETAIL SALES
(Seasonally adjusted)

	Billions of dollars			Percentage change from previous month		
	Dec. 1971	Jan. 1972	Feb. 1972	Dec. 1971	Jan. 1972	Feb. 1972
Total sales	34.9	35.0	34.9	-1.9	.2	- .2
Durable goods	11.3	11.5	11.3	-4.6	1.4	-2.0
Nondurable goods	23.6	23.5	23.6	- .5	- .4	.7
GAAF	9.2	9.4	9.4	-1.3	2.5	.3
Total deflated by all commodities CPI	29.4	29.4	n.a.	-2.2	.0	n.a

<u>Unit sales of consumer durables.</u> February sales of new domestic type autos were at an 8.7 million unit rate, slightly above January and up 5 per cent from a year earlier. Sales picked up

sharply late in the month, but dropped back in early March. Dealer inventories at the end of February, represented a 55 day supply, equal to the January ratio and 5 per cent above a year ago.

Sales of foreign cars in February were at an annual rate of 1.7 million units, up 7 per cent from January and 15 per cent from a year earlier. The import share of total sales amounted to 14 per cent for the month, about the same as in January and also in February last year.

According to preliminary estimates, unit sales of major home durables in February continued seasonally strong at about the high January rate, and were substantially above a year ago for a number of important items. Sales of dishwashers, electric ranges and refrigerators were especially high relative to last year, with color TVs and driers also continuing to show gains. Monochrome TVs and radios were unchanged from last year's levels, while sales of washers, freezers, and air conditioners were down slightly.

Consumer credit. Consumer instalment credit outstanding increased $7.6 billion in January, seasonally adjusted annual rate, following a rise of $10.8 billion in December and a record $15.2 billion in November. The slower expansion in January was most pronounced for nonautomotive consumer goods credit, but growth in automobile credit also slackened.

Extensions of instalment credit edged up in January, after seasonal adjustment, with increases in all types except personal loans. Repayments, which had declined in December, rose sharply in January and were substantially above the previous peak in November. Much of the increase in repayments occurred in nonautomotive consumer goods credit.

Cyclical indicators. The Census trend adjusted composite index of leading indicators rose 2.3 per cent in January, continuing an uninterrupted rise from its cyclical low in October 1970.

Series increasing in January were initial unemployment claims (inverted), new orders for durable goods, contracts and orders for plant and equipment, ratio of price to unit labor cost, industrial materials prices, and common stock prices. The workweek and building permits declined. January's big defense shipbuilding orders had a greater-than-warranted influence on the index. being reflected--somewhat misleadingly--in "contracts and orders for plant and equipment" as well as in total durable goods orders.

The preliminary coincident and lagging composites also increased further in January.

CHANGES IN COMPOSITE CYCLICAL INDICATORS
January 1972 (Preliminary)

	Per cent change from:	
	Previous month	Three months earlier
12 Leading (trend adjusted)	2.3	4.3
12 Leading, prior to trend adjustment	1.9	3.2
5 Coincident	0.9	2.3
5 Coincident, deflated	0.9	2.2
6 Lagging	0.5	1.6

Leading series now available for February are the workweek, materials prices, and common stock prices, all of which advanced.

Inventories. Book value of business inventories rose at a quite moderate $5.4 billion annual rate in January (preliminary), a little below the downward-revised December rate of $6.4 billion and not much different from the average rate in the last half of 1971. Durable goods manufacturers added to stocks at the highest rate in more than a year, as primary metals plants increased their inventories in response to a revival in orders. Elsewhere, inventory growth was modest. Nondurable goods producers continued to ship goods out of inventories built up earlier. Wholesale inventory accumulation slowed, while retail stocks were unchanged, with continued liquidation of auto stocks offsetting increases at other outlets.

CHANGE IN BOOK VALUE OF BUSINESS INVENTORIES
Seasonally adjusted annual rate, billions of dollars

	1971			1972
	QIII	Q IV (rev.)	Dec. (rev.)	Jan. (prel.)
Manufacturing and trade	6.1	4.1	6.4	5.4
Manufacturing, total	-1.1	1.1	-2.9	2.4
Trade, total	7.2	2.9	9.3	3.0
Wholesale	1.9	4.4	8.1	3.0
Retail	5.2	-1.5	1.2	.0
Durable	4.4	-2.6	-2.2	-2.8
Nondurable	.9	1.1	3.3	2.8

NOTE: Detail may not add to totals because of rounding.

With sales increasing strongly in manufacturing and wholesale trade, the inventory-sales ratio fell to 1.50, the lowest since September 1966. At durable goods manufacturers, inventories declined relative to unfilled orders for the fourth month in a row.

INVENTORY RATIOS

	1970	1971		1972
	Dec.	Jan.	Dec. (rev.)	Jan. (prel.)
Inventories to sales:				
Manufacturing & trade	1.62	1.60	1.54	1.50
Manufacturing, total	1.84	1.81	1.70	1.64
Trade, total	1.39	1.37	1.37	1.35
Wholesale	1.28	1.25	1.26	1.20
Retail	1.47	1.45	1.45	1.44
Durable	2.23	2.07	2.04	1.99
Nondurable	1.15	1.18	1.16	1.18
Inventories to unfilled orders:				
Durable manufacturing	.841	.827	.856	.843

Inventory plans. When surveyed in February, manufacturers anticipated adding to their inventories at a $4.0 billion annual rate in the current quarter (book value) as compared with actual accumulation at a $1.1 billion rate in the fourth quarter. In the second quarter, accumulation was expected to slow to a $1.6 billion rate. Manufacturers also anticipated a sharp increase in sales this quarter and a smaller further increase in the second quarter, with the inventory-sales ratio falling to 1.63. This anticipation survey has been characterized in the past by misses in direction and by large errors of amount, but the available January data do suggest an upturn in both sales and stocks. The January increase in the order backlog also suggests favorable conditions for further inventory growth.

Manufacturers' orders and shipments. New orders for durable goods rose sharply--nearly 10 per cent--in January (preliminary). Of the $3.1 billion increase, $1.1 billion was in defense contracts. Large defense shipbuilding orders raised the Census "producers'capital goods industries" series by 18 per cent, while the FR series on "capital equipment" orders, which excludes defense ship orders but includes non-defense aircraft and communications equipment orders, rose 4 per cent in January. Capital equipment orders have increased fairly strongly since mid-1971 and are consistent with business plans for higher plant and equipment expenditures in the first half of 1972. In January there were also substantial increases in orders for iron and steel, other primary metals, motor vehicles and parts, and construction materials.

MANUFACTURERS' NEW ORDERS FOR DURABLE GOODS
Per cent change

	Jan. 1972 from Dec. 1971 (preliminary)	Jan. 1972 from 1971-IV average (preliminary)
Durable goods, total	9.7	10.4
Excluding steel and defense	6.8	7.2
Primary metals	8.1	11.2
Motor vehicles and parts	14.2	8.7
Household durables	1.5	3.0
Defense products	55.8	54.7
Capital equipment	4.0	6.2
All other durables	6.0	7.1

The durable goods order backlog rose 2 per cent in January, mainly for defense products but also at primary metals plants. For capital equipment, however, shipments were even greater than the high level of incoming orders, and the backlog declined.

Plant and equipment spending plans. Two recent surveys indicate that business has scaled upward planned expenditures for new plant and equipment in 1972 from those reported earlier. The Commerce survey and a special McGraw-Hill survey, both taken in the January-February period, indicate plans for an increase in spending of about 11 per cent over 1971.

EXPENDITURES FOR NEW PLANT AND EQUIPMENT BY U.S. BUSINESS
(Per cent change from prior year)

	1971 (Actual)	1972 McGraw-Hill (Oct. 1971)	Comm-SEC (Dec. 1971)	McGraw-Hill (Feb. 1972)	Commerce1/ (Feb. 1972)
		--------Anticipated--------			
All Business	1.9	6.9	9.1	11.4	10.5
Manufacturing	-6.1	8.4	4.0	12.0	8.7
Durable goods	-10.4	8.7	5.1	13.1	13.9
Nondurable goods	-1.9	8.2	3.0	11.1	4.2
Nonmanufacturing	7.2	5.9	12.1	11.0	11.6
Transportation	-18.4	13.3	18.3	23.6	16.0
Electric utilities	20.8	2.0	16.1 2/	8.0	13.4 2/
Communications	6.6	10.0	12.8 2/	10.0	14.2 2/
Commercial and other	8.8	4.0	7.3 2/	11.0	8.1 2/

1/ Beginning with the February 1972 survey, the Commerce Department has assumed the entire responsibility for this survey.
2/ Confidential, not published separately.

Total spending in the first half of 1972 is anticipated in the Commerce survey to increase at an annual rate of 15 per cent from the last half of 1971, with growth slowing to about a 6 per cent annual rate in the second half. Most of the second half slowing is in manufacturing. New capital appropriations in manufacting, which tend to lead spending by about three quarters, did decline slightly in the fourth quarter of 1971 but preliminary reports indicate a resumption of increase in the first quarter of 1972.

Construction and real estate. Seasonally adjusted outlays for new construction advanced slightly further in February to a new high of about $119 billion. Among the major sectors, only residential construction increased in February.

NEW CONSTRUCTION PUT IN PLACE
(Confidential FRB)

	February 1972	Per cent change from	
	$ Billions 1/	Jan. 1972	Feb. 1971
Total	119.2	+1	+17
Private	88.1	+2	+25
Residential, inc. farm	50.6	+4	+39
Nonresidential	37.5	-2	+ 9
Public	31.1	-1	- 1

1/ Seasonally adjusted annual rates, preliminary. Data for February are confidential Census Bureau extrapolations. In no case should public reference be made to them.

Private housing starts, which provided the basis for the upsurge in residential outlays throughout 1971, rose 5 per cent further in January to a record seasonally adjusted annual rate of 2.55 million units. The rise in starts in January was concentrated in single-family structures, although multi-unit starts continued at an extraordinarily high rate despite a sharp reduction in the number of subsidized units.

Private housing starts for the first quarter are expected to average somewhat below the January rate but moderately above the advanced fourth quarter rate.

PRIVATE HOUSING STARTS AND PERMITS
(Seasonally adjusted annual rates, in millions of units)

	1971				1972
	QII	QIII	QIV (p)	Dec. (p)	Jan. (p)
Starts 1/	2.00	2.11	2.23	2.43	2.55
1-family	1.14	1.18	1.25	1.34	1.45
2-or-more family	.86	.94	.99	1.09	1.10
Permits	1.80	1.99	2.14	2.29	2.19
MEMORANDUM:					
Mobile home shipments 1/	.49	.53	.51	.50	n.a.

1/ The Census Bureau has reviewed its seasonal factors and has revised the seasonally adjusted starts and mobile home shipments series back to January 1969.

Reflecting the continued strong demand for new single-family homes, sales by merchant builders rose to a record seasonally adjusted annual rate of 713,000 units in January. The stock of unsold homes also rose, but the level was not particularly high relative to sales. The median price of new homes sold in January declined for the second consecutive month.

<u>Labor market</u>. The labor market has shown signs of strengthening in recent months. The unemployment rate fell in February to 5.7 per cent from 5.9 per cent in January. Nonfarm payroll employment rose 83,000 in February, but with the January level revised sharply upward, the average monthly increase since the October low-point amounted to 210,000. Trade, finance and State and local government have accounted for most of the recent rise in employment; employment in goods producing industries--particularly manufacturing--has continued to expand little.

NONFARM PAYROLL EMPLOYMENT, 1971-72
(Seasonally adjusted, in thousands)

	Jan. 1971-May 1971	May 1971-Oct. 1971	Oct. 1971-Feb. 1972	Jan. 1972-Feb. 1972
	-----------(Average	Monthly	Change)----------	
Total	79	16	210	83
Goods producing	-11	-46	26	-68
Manufacturing	-11	-28	17	16
Mining	- 1	-20	23	- 2
Contract construction	1	3	-14	-82
Service producing	90	61	183	151
Transportation & public utilities	3	-15	14	-12
Trade	27	24	61	63
Services and finance	25	37	59	56
Government	35	15	49	44
Federal	2	2	- 2	0
State and local	33	14	51	44

Average weekly hours of production and nonsupervisory workers on private payrolls recovered 0.2 hour in February to 37.2 hours, the same as the December level. In manufacturing, the workweek rebounded 0.4 hour in February to a relatively high 40.4 hours after dropping 0.3 hour in January; advances were widespread. The factory workweek has shown an irregular uptrend since September and in February was 0.2 hour above a year ago.

Unemployment. Unemployment among both male and female adult workers declined in February with the rate for married men edging down for the third consecutive month to its lowest level since the summer of 1970. The teenage jobless rate, however, rose further and at 18.8 per cent equaled the previous post-World War II highs. Unemployment among Negroes showed little change and the Negro-white jobless rate ratio moved above 2 to 1.

SELECTED UNEMPLOYMENT RATES
(Seasonally adjusted)

	1971		1972	
	February	September	January	February
Total	5.9	6.0	5.9	5.7
Men aged				
20 to 24 years	9.9	10.2	10.4	9.2
25 and over	3.5	3.5	3.2	3.2
Women, aged 20 and over	5.6	5.7	5.5	5.0
Teenagers	16.9	16.9	17.8	18.8
Married men	3.2	3.3	3.0	2.8
White workers	5.4	5.4	5.3	5.1
Negroes and other races	9.6	10.4	10.6	10.5

The drop in total unemployment in February was accompanied by a decline in the labor force and no change in total household employment. Unemployment declines since December have largely reflected a slowdown in the growth of the civilian labor force from the very high rate in the last half of 1971--a monthly increase of 155,000 from December to February as compared to a rise of 300,000 per month from June to December.

Earnings. After an initial post-freeze surge in December, the rise in average hourly earnings has slowed considerably. Average hourly earnings of production workers on private nonfarm payrolls (adjusted for inter-industry shifts) increased at an annual rate of 3.1 per cent from December to February; this compares to a 6.7 per cent annual rate during the pre-freeze months of 1971 and 2.1 per cent during the freeze months August to November. (The February earnings data may be revised upward, however, when the BLS receives more complete data, as was the case in January.) Since December, the annual rate of increase has been below the Pay Board's 5.5 per cent guideline in all industry categories except construction and transportation.

The Pay Board announced that the cumulative weighted average for approved wage increases through March 3 for category I and II cases (firms with over 1000 employees) was 4.1 per cent for 4.6 million workers. For category I cases only (5000 or more employees), the weighted average increase approved for new contracts and pay practices (effective after November 13, 1971) was 3.7 per cent, while for contracts existing before November 13, and those involving retroactive increases, the average increase was 4.3 per cent.

HOURLY EARNINGS INDEX FOR
PRODUCTION AND NONSUPERVISORY WORKERS*
(Per cent change; seasonally adjusted, annual rate)

	1971 Jan.- Aug.	1971 Aug.- Nov.	1971 Nov.- Dec.	Dec. 1971- Feb. 1972	Feb. 1971- Feb. 1972
Private nonfarm	6.7	2.1	17.3	3.1	5.9
Manufacturing	6.1	.6	24.2	3.2	5.9
Mining	7.9	-9.3	62.8	- .9	6.8
Construction	9.0	5.7	5.1	6.3	7.5
Transportation & p.u.	7.9	7.0	25.2	6.6	8.9
Trade	6.4	1.2	15.7	.9	5.3
Finance	7.7	-1.6	14.1	1.4	4.6
Services	4.3	2.7	10.9	2.3	4.3

* Adjusted for inter-industry shifts, and in manufacturing for overtime hours as well.

Industrial relations. Voting began March 8 on approval of the tentative agreement reached in early January by East Coast longshoreman at North Atlantic ports and in early March at Gulf Coast ports. Most local unions have ratified the contract. The East Coast settlement provides for $1.50 in wage increases, or 32.6 per cent, over a three-year period ending October 1, 1974. The first increase of 70 cents, or 15 per cent, on a $4.60 wage base is retroactive to November 14, 1971, or a month and a half after the old three-year contract expired. On the West Coast, longshoremen approved a new contract on February 19 ending a strike which began January 17. The contract provides $1.12 in wage increases, or 26.2 per cent, over 18-months. The first increase of 72 cents, or 16.8 per cent on a $4.28 wage base, is retroactive to December 25, 1971, or six months after expiration of the old five year contract. When the differences in "catch-up" features and fringe benefits in the East and West Coast contracts are taken into account, the total cost may be fairly close. The contracts must be approved by the Pay Board and the unions are emphasizing the large gains in productivity achieved in the industry over recent years in defense of the above-guideline increases.

UAW workers at the GM Vega plant at Lordstown, Ohio, with 7,800 employees, went on strike March 5 over production standards and a long list of other grievances.

Wholesale prices. Wholesale prices rose at a seasonally adjusted annual rate of 9.1 per cent between January and February as prices of farm and food products spurted and those for industrial commodities advanced at about the same rapid rate as in January.

Over the first three months of Phase II, exceptionally large increases occurred in prices of farm and food products. The increase in prices of industrial commodities was appreciable but was not unexpected immediately following the price freeze; and it was slower than the increase registered in the two months just prior to the freeze.

WHOLESALE PRICES
(Percentage changes, seasonally adjusted annual rates)

	Pre-stabilization period		Phase I	Phase II	
	Dec. 1970 to June 1971	June 1971 to Aug. 1971	Aug. 1971 to Nov. 1971	Nov. 1971 to Feb. 1972	Jan. 1972 to Feb. 1972
All commodities	5.0	5.7	-1.8	7.7	9.1
Farm and food 1/	7.2	2.1	6.0	17.4	23.7
Industrial commodities	4.1	7.7	-1.3	4.2	4.7
Crude and intermediate materials 2/	5.4	9.7	- .9	3.8	5.2
Finished goods 3/	2.3	4.1	-1.6	4.5	2.8
Producer	3.3	4.7	-2.7	6.3	6.3
Consumer	1.8	3.8	-1.1	3.6	1.1

1/ Farm products and processed foods and feeds.
2/ Excludes foods, plant and animal fibers, oilseeds, leaf tobacco, and intermediate materials for food manufacturing and manufactured animal feeds.
3/ Excludes foods.

Increases in prices of livestock and meats were of particular importance in the January and February rise in the index of farm and food products.

Further increases in prices of metals and metal products, textile products, hides and skins, and lumber and plywood along with large increases for machinery and equipment, paper and allied products and household furniture and appliances pushed the index of industrial commodities appreciably higher in February.

From December to early March, the weekly index of prices of sensitive raw industrial materials increased about 8 per cent, indicating a tighter demand-supply situation in materials markets. Prices of scrap metals, textiles and fibers, and hides have continued to move up in recent weeks.

Consumer prices. Consumer prices rose in January at an annual rate of 3.3 per cent, seasonally adjusted. Food prices declined because of a sharp drop in fresh vegetable prices. However, large advances occurred for meats, new cars, property taxes and utility and public transportation rates. Items exempted from regulation had no measurable net effects on price change, as advances in taxes and house prices offset declines for raw agricultural products, used cars and mortgage interest rates.

CONSUMER PRICES
(Percentage changes, seasonally adjusted annual rates)

	Pre-stabilization period		Phase I	Phase II	
	Dec 1970 to Jun 1971	Jun 1971 to Aug 1971	Aug 1971 to Nov 1971	Nov 1971 to Dec 1971	Dec 1971 to Jan 1972
All items	4.0	3.3	1.7	4.7	3.3
Food	6.2	1.0	1.7	8.3	-2.0
Commodities less food	3.0	2.6	.0	4.2	2.1
Services 1/	4.2	5.7	3.1	3.7	6.6
Addendum:					
All items less mortgage costs 2/	5.0	3.5	1.3	5.0	2.0
Services less home finance 1/ 2/	7.4	4.9	1.9	3.8	5.8
Commodities less food, used cars, home purchase 3/	3.0	2.1	.0	3.1	3.1

1/ Not seasonally adjusted.
2/ Confidential: Home financing costs excluded from services reflect property taxes and insurance rates as well as mortgage costs, which in turn move with mortgage interest rates and house prices. The index for property taxes rose 6.7 per cent between August 1971 and January 1972.
3/ Confidential.

For several components, there are indications that the post-freeze bulge is not yet over. The retail cost of the U.S.I.A.'s market basket of foods rose 1.7 per cent from January to February with substantial increases for beef, pork and fresh vegetables and fruits. A further though much smaller increase has occurred this month according to U.S.I.A. The January index does not fully reflect the price increases for new cars approved by the Price Commission. Rent advances are expected to be larger in February, when increases granted on controlled units in New York will be included. Utility rate rises, on the other hand, have been postponed by a Price Commission freeze until March 25, pending decision on new regulations.

DOMESTIC FINANCIAL SITUATION

SELECTED DOMESTIC FINANCIAL DATA

	Averages 1971			1972		
	QII	QIII	QIV	Jan.	Feb.	Week ended March 8
Interest rates, per cent						
Federal funds	4.56	5.47	4.75	3.50	3.29	3.43
3-mo. Treasury bills	4.26	5.01	4.22	3.38	3.20	3.52
3-mo. Federal agencies	4.43	5.29	4.40	3.59	3.36	3.32
3-mo. Euro-dollars	6.72	7.77	6.41	5.37	5.02	4.68
3-mo. finance co. paper	4.74	5.52	4.88	3.95	3.78	3.88
4-6 mo. commercial paper	5.05	5.74	5.04	4.08	3.93	3.98
Bond buyer municipals	5.74	5.75	5.16	5.12	5.29	5.29
Aaa corporate-new issues	7.83	7.68	7.19	7.07	7.16	7.25
20-year Treasury bonds	6.24	6.24	5.93	6.01	6.06	6.02
FHA mortgages, 30-year	7.67	7.91	7.65	7.49	n.a.	--

	1971			1972	
	QII	QIII	QIV	Jan.	Feb.
Change in monetary aggregates (SAAR, per cent)					
Total reserves	10.0	7.1	2.2	20.2	-4.2
Nonborrowed reserves	9.0	6.0	6.9	23.1	-2.0
Credit proxy	11.8	8.1	10.0	10.1	7.3
Credit proxy + nondep. funds	8.4	7.6	9.7	9.9	6.2
Money supply	10.6	3.7	1.1	3.2	14.2
Time and savings deposits	14.7	8.2	15.9	20.0	16.3
Deposits at S&L's and MSB's	17.3	13.7	12.8	23.8	n.a.
Bank credit, end-of-month 1/	10.3	9.7	8.7	17.5	12.4
Treasury securities	11.1	-18.5	2.7	-9.9	26.1
Other securities	17.4	12.0	17.7	20.8	12.5
Total loans 1/	8.3	14.7	7.0	21.6	9.9
Business 1/	4.2	15.7	-1.0	4.1	9.1

	1971			1972	
	QII	QIII	QIV	Jan.	Feb.
Change in commercial paper ($ millions)					
Total (SA)	-874	96	1,174	186	n.a.
Bank-related (NSA)	41	167	74	114	62

	1970	1971			1972	
	QI	Jan.	Feb.	QI	Jan.	Feb.
New security issues (NSA, $ millions)						
Total corp. issues	7,977	3,115	3,000	12,190	3,350 e	3,425 e
Public offerings	6,715	2,522	2,725	10,675	2,660 e	2,875 e
State and local government bond offerings	4,109	2,732	1,851	6,841	1,762	1,900 e
Fed. sponsored agency debt (change)	3,635	-171	-556	-1,031	-157	500 e
Fed. govt. debt (change)	1,981	664	240	1,575	134	300 e

n.a. - Not available. e - Estimated. p - Preliminary.
SAAR - Seasonally adjusted annual rate. NSA - Not seasonally adjusted.
1/ Adjusted for loans sold to bank affiliates.

DOMESTIC FINANCIAL SITUATION

Summary and outlook. Since the last Committee meeting, money market yields generally have risen 25 to 70 basis points, with much of the increase occurring in the past week. The largest advance developed in the bill market, due partly to continued increases in weekly bill issues, and the auctioning of a $3 billion bill strip in early March. In addition, bill rates have been strongly influenced by the substantial recent rise in Federal funds and dealer loan rates.

Despite the rise in short-term rates, capital market yields were stable to declining, on balance, over the intra-meeting interval. The spread between short- and long-term rates has been wide by historical standards, indicating that some increase in short-term rates had already been discounted in long-term markets. In addition, financial institutions continue to have a considerable volume of funds to invest in securities markets. Casualty companies--with widening underwriting profits--have stepped up their purchases of tax-exempt issues, savings banks continue to acquire corporate bonds in volume, and life insurance company acquisitions of corporate private placements continue high. In very recent days, however, the more marked rise in short-rates has been reflected in some back-up of bond yields as well.

The continued high rate of inflows to banks and nonbank thrift institutions, although moderating somewhat in February, has kept mortgage commitments high and contributed to a downtrend in mortgage rates. Commercial banks, in addition to acquiring a sizable volume of mortgages, have continued to invest relatively heavily in municipal, and Federal agency securities. Business loans at banks rose rather rapidly in February, but the increase was not broadly based by industrial category, and only a moderate rise seems in prospect over the next few months in view of the improving cash flow and liquidity position of corporations.

Outlook. Treasury net cash borrowing over the remainder of the fiscal year--will be substantially larger than seasonal. Some of this need will probably have to be met in early April, but the amount and maturity area are still uncertain. While it seems clear that banks, nonfinancial corporations, and other institutions will be able to absorb a significant volume of new Tresaury securities, the size of the Treasury's need between now and mid-year is likely to result in some further upward pressure on short- and intermediate-term rates.

It is not clear to what extent any rise in short-term rates from current levels will be transmitted to capital markets. On the demand side, corporate and State and local government demands on bond markets are expected to moderate. However, significant further increases in short-term rates will contribute to the view that monetary policy is becoming more restrictive, and may well adversely affect investor attitude toward longer-term securities at least in the short-run.

Of all long-term markets, the mortgage market may be most immune to upward rate pressures. Even with a rising level of short-term yields, inflows to nonbank thrift institutions could be expected to remain relatively high, given the wide existing rate advantage of deposits over short-term market securities. Indeed, the FHLB expects to be retiring debt, in light of repayments of advances from the S&L's, and FNMA has scaled down its planned borrowing for the second quarter.

Monetary aggregates. M_1 advanced at an annual rate of about 14 per cent in February, the most rapid increase since May of last year. While a significant part of the acceleration from the low rates of growth in recent months probably reflected the temporary effect of a rapid rundown in U. S. Treasury balances, demand for money has presumably been strengthened by the recent step-up in business activity and the lower level of interest rates prevailing since fall. With the strong advance in M_1, M_2 and M_3 also expanded more rapidly in February, even though growth in the thrift deposit components of these aggregates diminished somewhat from the very rapid January pace.

The reduced rate of growth in commercial bank thrift deposits in February may reflect in part some reductions in offering rates. Inflows into such deposits continued at a relatively high rate, however, about matching the fast pace in the fourth quarter of last year. Growth in these deposits continued to be broadly based in February, with comparatively strong increases recorded by both large and small banks in both passbook and certificate accounts.

Large negotiable CD's grew moderately in February as commercial banks obtained a fairly large volume of funds from the sale of CD's to state and local governments and to foreign governments. However, with the substantial drop in Treasury balances, a further modest decline in Eurodollar liabilities and the slower rate of growth for consumer type time deposits, the expansion in the adjusted credit proxy was lowered to a 6.2 per cent annual rate in February.

MONETARY AGGREGATES
(Seasonally adjusted changes)

	1971 QI	1971 QII	1971 QIII	1971 QIV	1972 Jan.	1972 Feb. p
	(Annual percentage rates)					
1. M_1 (Currency plus private demand deposits)	9.1	10.6	3.7	1.1	3.5	14.2
2. M_2 (M_1 plus commercial bank time and savings deposits other than large CD's)	18.1	12.4	4.4	8.0	13.4	15.1
3. M_3 (M_2 plus savings deposits at mutual savings banks and S&L's)	18.9	14.4	7.8	9.6	15.0	16.8
4. Adjusted bank credit proxy	10.9	8.4	7.6	9.7	9.9	6.2
5. Time and savings deposits at commercial banks						
a. Total	28.8	14.7	8.2	15.9	21.0	15.8
b. Other than large CD's	27.5	14.0	5.3	14.7	25.0	18.5
Memorandum:	(Change in $ billions)					
a. U. S. Government demand deposits	-2.4	0.3	2.3	-0.4	0.1	- 2.6
b. Negotiable CD's	2.6	1.3	2.3	1.8	-0.2	0.6
c. Nondeposit sources of funds	-4.6	-2.6	-0.4	--	--	-0.4

p - Preliminary and partially estimated.

Bank credit. Total loans and investments at all commercial banks continued rising rapidly from the end of January to the end of February, although the rate was reduced from the strong January pace. As had been generally true in other recent months, a large portion of the growth in total bank credit was in security holdings. U. S. Treasury securities, in particular, rose sharply,1/ and other securities advanced markedly, although at a rate below that in January and the fourth quarter of last year.

COMMERCIAL BANK CREDIT ADJUSTED FOR LOANS
SOLD TO AFFILIATES 1/
(Seasonally adjusted percentage changes at annual rates)

	1971		1972	
	QIII	QIV	January	February
Total loans & investments 2/	9.7	8.7	17.5	12.4
U. S. Treasury securities	-18.5	2.7	- 9.9	26.1
Other securities	12.0	17.7	20.8	12.5
Total loans 2/	14.7	7.0	21.6	9.9
Business loans 2/	15.7	- 1.0	4.1	9.1
Real estate loans	13.7	13.2	13.3	11.7
Consumer loans	13.3	13.6	11.0	10.9

1/ Last-Wednesday-of-month series.
2/ Includes outstanding amounts of loans reported as sold outright by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.

Total loans expanded substantially in February, although their rate of increase was well below the very rapid January pace, as strong gains were recorded in most major loan categories. Real estate loans

1/ Without seasonal adjustment, Treasury security holdings declined about $800 million or about $1.3 billion less than the normal seasonal decline in these holdings.

and consumer loans continued to rise sharply and loans to nonbank financial institutions and to security brokers and dealers also increased, although by considerably less than in January. A comparatively strong gain was also recorded in business loans.

The growth in loans to brokers and dealers was concentrated largely in extensions for the purchase of securities other than U. S. Treasury securities. Inquiries by Reserve Bank personnel suggest that the growth in the "other" security loans occurred in loans secured by a number of types of collateral including bankers' acceptances, commercial paper, municipal securities and common stock. Growth in nonbank financial institution loans was, in part, the result of a significant rise in loans to borrowers other than sales finance companies, mainly mortgage brokers.

The February growth in business loans was the strongest since last summer when credit demands were stimulated by borrowing to hedge against adjustments in foreign exchange rates. The increase in business loans in February was not broadly based, however. At those banks reporting an industry breakdown of business loans, larger than seasonal growth was recorded only in loans to construction firms, food processors, public utilities and firms in the primary metals industry. A large part of the increase was at banks outside New York City. Some strength was displayed in business loans at New York City banks early in February, but this was counterbalanced during the latter part of the month and in early March by smaller than seasonal increases.

<u>Nonbank financial institutions and mortgage markets</u>. Deposit inflows to nonbank thrift institutions during January and February were even stronger than earlier indications had suggested. While deposit growth at both S&Ls and MSBs slowed in February from the exceptionally rapid January pace, the rate of growth nonetheless remained above that recorded in the second half of 1971. The relative attractiveness of thrift claims was greatly enhanced by the declines in short-term market rates from last summer through the first part of this year. Even though rates on short-term securities have risen recently, the yield advantage of thrift deposits remains quite large.

DEPOSIT GROWTH AT NONBANK THRIFT INSTITUTIONS
(Seasonally adjusted annual rates, in per cent)

	Mutual Savings Banks	Savings and Loan Associations	Both
1971 - QI	16.3	24.6	21.9
QII	15.0	18.4	17.3
QIII	9.6	15.7	13.7
QIV	10.6	13.8	12.8
December*	12.5	14.2	13.7
1972 - January* p/	14.0	28.4	23.8
February* e/	10.7	18.8	16.2

* Monthly patterns may not be significant because of difficulties with seasonal adjustment.
p/ Preliminary.
e/ Estimate.

Deposits at nonbank thrift institutions have also become more attractive relative to consumer-type time and savings deposits at commercial banks, given the rate cuts on such bank deposits in certain geographic areas. There is no evidence of rate reductions by savings and loan associations. However, some mutual savings banks in New York have made changes in nonrate terms by no longer offering 90-day to one-year time deposits. On the other hand, some New York savings banks have effectively increased rates by compounding interest-dividends more frequently.

Savings and loan associations continued to use some of their inflows to repay FHLB advances, with net repayments for February totaling about $700 million out of a total $7.2 billion outstanding at the end of January. In addition to these repayments of borrowed money, S&Ls increased their liquid asset position by about $800 million in February. Moreover, according to FHLBB estimates, new commitment activity was stepped up during the month.

With flows of funds into nonbank thrift institutions continuing large, mortgage yields have generally edged down further, even though demands for mortgage credit have begun to quicken with the advent of the spring building season. In the primary mortgage market, although the average contract interest rate for conventional loans remained unchanged during February at 7.60 per cent on new homes, it declined slightly for existing homes, which account for most purchases of 1-family dwellings. These averages were 25 to 35 basis points below their levels of last August, according to the FHA series.

Yields on Government-underwritten home mortgages in the private secondary market declined a little further in February, dropping to 7.46 per cent, 51 basis points below last summer's high. The downward movement apparently persisted into the early part of this month, judging from FNMA's latest auction results (March 6).[1/] Relative to yields on new issues of high-grade corporate bonds, average returns on home mortgages have continued to offer little attraction, if any, to diversified investors, once allowance is made for higher mortgage servicing costs.

Owing to an active real estate market, the ready availability of warehousing credit at attractive rates, and some uncertainty about the future course of mortgage yields, mortgage companies have continued to hold large inventories of loans pending future delivery or sale to others.

The average delinquency rate on home mortgages (MBA series) increased further during the fourth quarter of 1971, but apparently by less than usual for that time of year. This measure of credit quality reached the highest unadjusted level in the 18-year history of the series, which largely reflects experience with FHA and VA mortgages. The average foreclosure rate also rose to a record high.

Short-term security markets. Yields on short-term securities have risen from 25 to 70 basis points over the last four weeks. The most pronounced rise occurred in short-term Treasury bills, reflecting in part the increased supply from the continuing $300 million addition to weekly bill issues and the $3.0 billion bill strip auction on March 1, and the resultant rise in dealer inventories. The market

1/ On February 14, FNMA initiated its periodic auction of forward purchase commitments for conventional home loans prepared on FNMA-approved mortgage forms. Based on a slim volume of bids, yields in the first three auctions averaged 7.74 per cent (Feb. 14), 7.64 per cent (Feb. 28), and 7.61 per cent (March 13).

AVERAGE RATES AND YIELDS ON 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)
1971 - Low	7.55	-36	7.32	-36	2.5e
- High	7.95	71	7.97	56e	7.8
Oct.	7.80	51	7.75	46	6.1
Nov.	7.75	56	7.62	43	5.1
Dec.	7.70	61	7.59	50	4.8
1972 - Jan.	7.60	53	7.49	42	4.0
Feb.	7.60	44	7.46	30	3.8

NOTE: FHA series; interest rates on conventional first mortgages (excluding additional initial fees and charges) are rounded to the nearest 5 basis points. On FHA loans carrying the 7 per cent ceiling rate in effect since mid-February 1971, a change of 1.0 points in discount is associated with a change of 12 to 14 basis points in yield. Gross yield spread is average mortgage return, before deducting servicing costs, minus average yield on new issues of high-grade corporate bonds with 5-year call protection.

e-Estimate.

has also been influenced recently by concern and uncertainty about foreign exchange market developments; Treasury financing announcements were taken as confirmation of market expectations that the Treasury would stress sales of short-term instruments because of international considerations, among other factors.

These same considerations also led many market participants to the conclusion that the System was conducting a "twist" policy. The actual pattern of System open market transactions since the beginning of the year would not be inconsistent with such a market attitude. The System has bought nearly $1 billion of Treasury coupon and Agency issues over the past two and one-half months, while selling $1.5 billion of Treasury bills. Most of the bill sales were, of course, in response to the sharp decline in the Treasury balance at the Federal Reserve Banks in February.

SELECTED SHORT-TERM INTEREST RATES

	Feb. 16	Mar. 8	Mar. 13	Change (Feb. 16-Mar. 8)	Change (Feb. 16-Mar. 13)
Federal funds 1/	3.43	3.43	3.83 2/	--	.40
Treasury bills					
3-month	3.06	3.56	3.75	.50	.69
1-year	3.93	4.18	4.42	.25	.50
Federal agency, 1-year	4.38	4.41	4.64	.03	.26
90-119 day commercial paper	3.75	3.88	4.00	.13	.25
60-89 day CD's	3.34	3.41	n.a.	.07	n.a.

1/ Weekly average.
2/ 5-day average.

Long-term securities markets. Since the preceding meeting, yields on most long-term securities have declined from 5 to 20 basis points. The volume of long-term public corporate bond issues stabilized in January and February at monthly average levels somewhat below those of late 1971. This moderation in the long-term corporate and municipal calendar, an apparently ample supply of investment funds, and decreasing concern in recent weeks about the impact of the Treasury deficit financing on long-term markets led to some price improvement in both the new issue and secondary markets. Underwriters were able to reduce inventory positions in early March, even with rates declining moderately. However, continued uncertainty about inflation and the future course of short-term rates apparently still inhibits institutional investors.

SELECTED LONG TERM INTEREST RATES
(Per cent)

	New Aa Corporate bonds 1/	Long-term State and Local bonds 2/	U.S. Gov't. (10-year constant maturity)
1971			
Low	6.76 (1/25)	4.97 (10/21)	5.42 (3/76)
High	8.23 (5/21)	6.23 (6/24)	6.89 (7/30)
1972			
Low	6.86 (1/14)	4.99 (1/14)	5.87 (1/14)
High	7.30 (2/11)	5.29 (3/3)	6.11 (2/11)
Week of:			
February 4	7.22	5.35	6.08
11	7.30	5.27	6.11
18	7.10	5.24	6.08
25	7.11	5.28	6.07
March 3	7.16	5.29	6.03
10	7.12	5.18	6.02p

1/ With call protection (includes some issues with 10-year protection)
2/ Bond Buyer (mixed qualities)

Stock prices continued to rally through February and into March, with the NYSE and AMEX indices rising by 4 per cent and 6 per cent, respectively, since early February. The NYSE index is now within 1 per cent of its historical high. These recent gains have been broadly based. Trading volume for the last five weeks has increased slightly over the already relatively high December-January

RELATIVE PERFORMANCE OF STOCK PRICE INDICES

	1971 Highs	Stock prices as of 11/26/71	Stock prices as of 2/1/72	Stock prices as of 3/13/72	Per cent change from 11/26/71 to 3/13/72	Per cent change from 2/1/72 to 3/13/72
NYSE	57.76 (4/28)	50.57	57.77	59.82	18.0	4.0
AMEX	26.68 (4/28)	23.63	27.20	28.16	19.0	4.0
NASDAQ	114.12 (12/31)	101.64	119.58	127.34	25.0	6.0
D-J Ind.	950.82 (4/28)	816.59	901.70	928.66	14.0	3.0

levels. Following the record $480 million net acquisitions of U.S. stock in December, foreign purchasers bought a net $234 million in January.

The volume of publicly offered corporate bonds was about $1.8 billion in February, only slightly larger than in January. It now appears that the March and April increase in volume will be less than seasonal. The timing pattern of bond issues over the next few months is made uncertain, however, by the very tentative scheduling of a $300 million oil company issue. Takedowns of private placements are expected to remain at a high level over the next few months, as life insurance companies are still reported to have large fund flows and are eager to invest in this market. New equity issues also continue to be large, undoubtedly reflecting both a favorable stock market and continued need for funds by smaller, lower-rated firms.

Issues of tax-exempt long-term bonds continue to remain below the record 1971 levels, in part because of the lower volume of school bond offerings. Yields on municipal bonds were essentially stable throughout February, but by mid-March the Bond Buyer index had dropped almost 20 basis points below its early February high. Much of the recent volume has been of very high quality, and the long-term end of the market has been supported by heavy purchases by casualty insurance companies. Commercial bank acquisitions are reported to have moderated somewhat in recent weeks.

Offerings of pre-refunding municipal bonds and industrial pollution control bonds may become significant later in the second quarter, but the staff expects the volume of long-term bond issues by

CORPORATE AND MUNICIPAL SECURITY OFFERINGS
(Monthly or monthly averages in millions of dollars)

	1971	1972			
	Monthly Average	Jan.e	Feb.e	Mar.e	Apr.e
Corporate Securities Total	3,535	3,560	3,425	3,700	3,350
Public	2,065	1,760	1,825	1,900	2,000
Private	613	900	550	800	550
Stock	1,080	900	1,050	1,000	800
State and Local Governments					
Long-term	2,080	1,762	1,900	1,800	1,800
Net short-term	345	406	711	-1,500	n.a.

e/ Estimated

NOTE: Long-term offerings are gross. Short-term offerings are Federal Reserve Board estimates of net sales.

State and local governments to remain at about the $1.8 billion level during March and April. The Survey of State and Local Borrowing Anticipations and Realizations, which will be analyzed in an appendix to the Green Book Supplement, shows long-term borrowing plans of about $5 billion for the second quarter, significantly below the initial quarterly anticipations data reported on a comparable basis in previous surveys.

Federal finance. On a unified budget basis, the staff is still projecting a fiscal year 1972 deficit of about $34 to $35 billion. On the spending side, total outlays in January and February seem to have been about as projected by the staff. However, the staff projection for the fiscal year involves considerably increased spending levels in the second quarter, and it is still uncertain whether these levels will be attained. In absolute terms, the greatest increase in budget spending is slated for defense procurement, but the defense data for the first quarter so far look somewhat weak. On an NIA basis, our first-quarter estimate for defense purchases has been reduced by $500 million (SAAR).

Treasury receipts in January were larger than expected earlier, but February receipts were somewhat lower than expected. These cross-currents do not suggest any substantial change in the outlook for receipts.

Current Congressional debate on the budget for fiscal year 1973 centers on the social security benefit and welfare bill and general revenue sharing. The staff has been assuming that a general revenue sharing bill would pass, affecting outlays in the coming fiscal year, but not retroactive to January as in the Budget. The House Ways and Means Committee is presently reported to be favoring a revenue-sharing plan that would be retroactive to January 1 and that would give considerable aid to the cities, although there is still some disagreement over the method of distribution of funds to the localities. As for the social insurance bill, passage is expected but the extent of the rise in benefits is far from settled--the 20 per cent increase advocated by some seems unlikely, but there might be a 10 per cent increase instead of the 5 per cent proposed in the Budget and assumed in the staff estimates.

The Treasury cash balance for the end of March is now projected to be $6.4 billion. Staff estimates indicate that in order to maintain minimal cash balances around mid-April, the Treasury will need to borrow about $2.0 billion, with payment early in April. This would be in addition to the on-going $0.3 billion weekly increments in regular Treasury bill auctions. The expected early April borrowing operation could take the form of a note issue sold at auction.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	Feb.	March	Apr.
Total net borrowing	.3	4.2	-.8
Weekly and monthly bills	.6	4.5	1.2
Tax bills	--	--	-4.0
Coupon issues	--	--	--
As yet unspecified new borrowing	--	--	2.0
Other (debt repayments, etc.)	-.3	-.3	--
Plus: Other net financial sources[a]	-.6	.6	.5
Plus: Budget surplus or deficit (-)	-3.7	-5.5	2.2
Equals: Change in cash balance	-4.0[b]	-.7	1.9
Memoranda: Level of cash balance end of period	7.1[b]	6.4	8.3
Derivation of budget surplus or deficit:			
Budget receipts	15.3	14.2	22.1
Budget outlays	19.0	19.7	19.9
Maturing coupon issues held by public	3.7[c]	--	--
Net agency borrowing	0.5	0.3	0.4

a/ Checks issued less checks paid and other accrual items.
b/ Actual.
c/ The February refunding fell short of its goal by $1.2 billion.

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

	Fiscal 1972 e/		FY 1973 e/	Calendar Years		Calendar Quarters				
							F.R.B. Staff Estimates			
							1972			
	Jan. Budget	F.R. Board	Jan. Budget	1971 Actual	1972 F.R.B.	IV*	I	II	III	IV
Federal Budget										
(Quarterly data, unadjusted)										
Surplus/deficit	-38.8	-34.6	-25.5	-24.8	-37.4	-10.6	-11.1	-5.1	-9.3	-11.9
Receipts	197.8	199.7	220.8	194.0	209.5	44.6	47.1	59.4	53.9	49.1
Outlays	246.6	234.3	246.3	218.8	246.9	55.2	58.2	64.5	63.2	61.0
Means of financing:										
Net borrowing from the public	39.5	31.3	27.5	24.8	30.6	12.5	4.6	5.1	8.3	12.6
Decrease in cash operating balance	--	1.8	--	-3.2	4.3	-1.3	4.9	-.6	--	--
Other 1/	-.7	1.5	-2.0	3.2	2.5	-.6	1.6	.6	1.0	-.7
Cash operating balance, end of period	8.8	7.0	8.8	11.3	7.0	11.3	6.4	7.0	7.0	7.0
Memo: Net agency borrowing 2/	n.a.	5.4	n.e.	1.1	n.e.	1.4	0.7	1.6	n.e.	n.e.
National Income Sector										
(Seasonally adjusted annual rate)										
Surplus/deficit	-35.0	-28.4	-28.0	-23.1	-31.1	-25.6	-26.2	-35.1	-33.4	-29.5
Receipts	202.8	206.8	227.9	198.8	217.2	203.1	212.8	213.4	218.5	223.9
Expenditures	237.8	235.2	255.9	221.9	248.2	228.7	239.0	248.5	251.9	253.4
High employment surplus/deficit (NIA basis) 3/	n.a.	.8	n.a.	2.9	-5.9	6.6	2.0	-6.9	-9.9	-8.7

* Actual e--projected n.e.--not estimated n.a.--not available

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

2/ Federally-sponsored credit agencies, i.e., Federal Home Loan Banks, Federal National Mortgage Assn., Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.

3/ Estimated by F.R. Board Staff.

INTERNATIONAL DEVELOPMENTS

III -- T - 1
U.S. Balance of Payments
In millions of dollars; seasonally adjusted

	1971				1972p/
	Year	II	III	IV	Jan.*
Goods and services, net 1/	699	6	56	-514	
Trade balance 2/	-2,879	-1,061	-540	-1,526	-365
Exports 2/	42,769	10,706	11,475	9,572	4,185
Imports 2/	-45,648	-11,767	-12,015	-11,098	-4,550
Service balance	3,578	1,067	596	1,012	
Remittances and pensions	-1,459	-355	-385	-377	
Govt. grants & capital, net	-3,860	-1,060	-891	-883	
U.S. private capital (- = outflow)	-9,585	-2,201	-3,455	-1,694	
Direct investment abroad	-4,526	-1,393	-1,404	-358	
Foreign securities	-910	-388	-248	79	-276
Bank-reported claims -- liquid	-580	31	-407	-119	6
" " " other	-2,389	-359	-1,171	-814	114
Nonbank-reported claims -- liquid	-509	55	-150	-189	
" " " other	-672	-147	-75	-293	
Foreign capital (excl. reserve trans.)	-5,400	-3	-2,406	-726	
Direct investment in U.S.	-192	-16	-388	120	
U.S. corporate stocks	836	-3	231	529	234
New U.S. direct investment issues	1,137	263	200	357	
Other U.S. securities (excl. U.S. Treas.)	278	-64	151	28	
Liquid liabilities to:	-6,705	-33	-2,325	-1,632	432
Commercial banks abroad	-6,902	-84	-2,113	-1,638	259
Of which liab. to branches	(-4,942)	(-117)	(-1,817)	(-923)	(-106)
Other private foreign	-478	-147	-368	-35	18
Intl. & regional institutions	675	198	156	41	155
Nonliquid liab. to banks and others	-754	-150	-275	-128	
Foreign official reserve claims	27,419	5,088	10,991	6,472	845
U.S. monetary reserves (increase, -)	3,065	838	1,373	-8	-2
Gold stock	866	456	300	1	--
Special drawing rights 3/	468	196	150	-3	--
IMF gold tranche	1,350	252	851	-8	-2
Convertible currencies	381	-66	72	2	--
Errors and omissions	-10,878	-2,313	-5,283	-2,270	
BALANCES (deficit -) 3/					
Official settlements, S.A.		-5,926	-12,364	-6,464	
" " , N.S.A.	-30,484	-6,462	-12,704	-5,883	-843
Net liquidity, S.A.		-5,979	-9,482	-4,524	
" " , N.S.A.	-22,690	-6,598	-10,082	-3,446	
Liquidity, S.A. 4/		-5,893	-10,039	-4,832	
" , N.S.A.	-23,779	-6,592	-10,566	-3,721	-1,275

* Monthly, only exports and imports are seasonally adjusted.

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

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

3/ Excludes allocations of SDRs as follows: $717 million on 1/1/71 and $710 million on 1/1/72.

4/ Measured by changes in U.S. monetary reserves, all liabilities to foreign official reserve agencies and liquid liabilities to commercial banks and other foreigners.

INTERNATIONAL DEVELOPMENTS

Summary and outlook

Recurrent speculative flurries against the dollar have enlarged the deficit in the U.S. balance of payments on the official settlements basis in recent weeks. In the first two months of 1972 the deficit was about $2 billion (not seasonally adjusted), and in the first two weeks of March there has been a further adverse balance of nearly $1 billion. It seems likely that since the turn of the year there have been sizable net abnormal capital outflows, since the underlying deficit on current account and normal capital transactions in these 2-1/2 months is unlikely to have reached $3 billion even with considerable direct investment outflows following the year-end repatriations. The cumulated deficit from December 22 is now about $1-1/4 billion (including an estimate for the week through March 15). Before the year-end there had been a sizable surplus, reflecting not only rebuilding of foreign commercial bank balances and large purchases of U.S. corporate stocks as we have previously reported, but also -- it now appears -- U.S. direct investment transactions.

New information on the makeup of the fourth-quarter balance of payments, reflected in summary data being released by the Commerce Department today, indicates larger year-end inflows both of direct investment capital and of income from direct-investment affiliates than had previously been estimated. Consequently the net outflow of U.S. direct investment capital in 1971 as a whole was only a little larger than the 1970 outflow. Correspondingly, negative errors and omissions were larger than previously thought in the fourth quarter of 1971, and exceeded $10 billion for the year.

The available information on details of transactions in 1972 thus far -- including a further large trade deficit in January, continuing buying of U.S. corporate stocks on a diminishing scale in January and February, seasonal repayments of U.S. bank credit, and little net change in total liabilities to U.S. bank branches -- give no indications of any great change in the underlying state of the balance of payments.

The staff projection of net exports of goods and services for the year 1972 is still $1/2 billion. With so small a goods and services surplus as that, the adverse balance on current account and long-term capital, plus an allowance for a "normal" amount of errors and omissions, could be around $8 or $9 billion. Provided that confidence in the viability of the Smithsonian settlement can be re-established, it is still possible that a substantial part of this basic deficit may be offset by unwinding of leads and lags and other reflows of capital that moved out for speculative reasons in 1971.

Foreign exchange markets. In the past four weeks the dollar has again come under considerable, though intermittent, pressure in the exchanges. The dollar depreciated by another 3/4 percent against the unweighted average of nine major currencies, and foreign central banks purchased over $1-3/4 billion. The major dollar purchasers were the central banks of Germany, Japan, the Netherlands, and Belgium. Each of these countries, following its large dollar intake, took some sort of selective control measures /for details see pages III-7-13 below/ aimed at reducing the inflows into their currencies, and in each instance, the enactment of these measures appeared to have relieved much of the upward pressure on those currencies.

Following these actions, the dollar generally strengthened on the exchange markets, firming fairly sharply on March 14 following press reports that Chairman Burns had commented at Basle that the outlook was for higher short-term interest rates in the United States. Markets remained nervous, however, evidenced by the fact that three-month forward rates for guilders, Belgian francs, DM, and yen are still quoted above the upper limits on the spot rates.

On March 7, the EEC announced that it would take the first steps toward achieving a monetary union by narrowing the margins among its currencies to ± 1-1/8 percent as of July 1. The lira, which had been below its central rate against the dollar, firmed sharply, and as of March 15, all of the EEC currencies are within 2-1/4 percent of each other and all are above their central rates against the dollar.

Euro-dollar market. As shown in the table, the spread between Euro-dollar and U.S. money market rates narrowed in the three weeks ended March 8 as Euro-dollar rates eased and competitive U.S. interest rates firmed slightly. This trend was interupted last week as Euro-dollar rates firmed sharply in response to uncertainty over the exchange value of dollar-denominated claims. With the return of relative calm in exchange markets after the weekend, Euro-dollar interest rates began to move down, but remained firm relative to the previous three week period.

SELECTED EURO-DOLLAR AND U.S. MONEY MARKET RATES

Average for month or week ending Wednesday		(4) 1-month Euro-$ Deposit 1/	(5) 30-59 day CD rate (Adj.) 2/	(6)= (4)-(5) Differential	(7) 3-month Euro-$ Deposit 1/	(8) 60-89 day CD rate (Adj.)	(9)= (7)-(8) Differential
1972							
January		5.02	3.81	1.21	5.36	3.86	1.50
February		4.46	3.43	1.03	5.02	3.52	1.50
February	23	4.54	3.33	1.21	5.01	3.45	1.58
March	1	4.59	3.42	1.17	4.95	3.52	1.43
	8	4.40	3.42	0.98	4.68	3.59	1.09
	15p	5.17	3.42	1.75	5.27	3.59	1.68

1/ All Euro-dollar rates are noon bid rates in the London market.
2/ Offer rates (median, as of Wednesday) on large denominated CD's by prime banks in New York City; daily rate are carried forward from the previous Wednesday; CD rates adjusted for the cost of required reserves.

U.S. balance of payments. The official settlements deficit is estimated to have been about $1-1/4 billion (not seasonally adjusted) in February, up from the $3/4 billion deficit in January. A swing in liabilities to commercial banks abroad -- increasing in January and decreasing in February -- was a principal factor in this change. As a result of last week's flareup in foreign exchange markets, the official settlements deficit in the first two weeks of March probably approached $1 billion.

The trade deficit in January was $365 million -- an annual rate of $4.3 billion, about the same as the average of the last 9 months of 1971. Both exports and imports were extremely high, probably reflecting a catch-up in shipments delayed by dock strikes last fall. On the plus side, there were large net purchases of U.S. stocks by foreigners in January, totaling $250 million, and early indications are that purchases in February were probably over $150 million. Following the large outflow of U.S. bank credit in December, there was a seasonal reversal in such flows in January and February. Bank-reported claims on foreigners in January declined by $125 million (mainly on Japan) and there was a further smaller reduction in February according to weekly member bank statistics.

It is quite likely that there was a sizable outflow of U.S. direct investment capital in January and February. The OFDI announcement of December 10, 1971 postponing the year-end deadline under this program to the end of February did little to change U.S. companies' usual practice of reducing outflows in the closing months of the year and then increasing them after year-end. Preliminary estimates for the fourth quarter of 1971 indicate that net outflow of U.S. direct investment in that period was less than $1/2 billion (seasonally adjusted) far below the near $1-1/2 billion outflow reported in each of the first three quarters of 1971. For 1971 as a whole, U.S. direct investment outflow was about the same as in 1970. A decline of $3/4 billion in outflows to Canada was offset by increased investment in other areas.

Income receipts from U.S. direct investments abroad rose steeply -- by over $500 million -- to a record breaking $2.2 billion in the fourth quarter of last year. For the year 1971 these income receipts totaled $7-1/4 billion, about $1-1/4 billion more than in 1970.

Recent financial developments abroad. The developments in foreign exchange markets in recent weeks reflected a renewal of speculative capital movements. Interest rate differentials have generally been moving in favor of the dollar in recent weeks, as foreign interest rates have declined more than Euro-dollar rates, while U.S. short-term rates have begun to rise. However, uncovered differentials remain large, and, because most foreign currencies are at a forward premium, incentives to move funds on a covered basis out of dollars are in many cases very substantial.

Recent monetary policy measures abroad have been aimed at reducing interest rates, mainly to discourage capital inflows and thereby to avoid upward pressure on exchange rates and further accumulation of reserves. In most countries, notably the United Kingdom, Belgium, Italy and Japan, monetary ease is also appropriate on domestic grounds.

In Germany, concern about inflation and increasing optimism regarding the course of economic activity have again presented the monetary authorities with a possible conflict between policies appropriate for external balance and those needed to maintain internal stability. On February 25, the Bundesbank's rediscount and Lombard rates were cut to 3 per cent and 4 per cent, respectively, and minimum reserve requirements on nonresident bank deposits were raised. At the same time, however, the Bundesbank decreased rediscount quotas in order to prevent a net easing of monetary conditions internally. Key short-term interest rates, such as the 30- and 90-day interbank loan rates, which had been declining since the end of December, have shown little change since the policy measures were introduced.

To discourage borrowing abroad by German nonbank enterprises, beginning March 1 such enterprises must deposit, interest free, with the Bundesbank (subject to certain apparently not inconsiderable exceptions) an amount equal to 40 per cent of the excess of liabilities to nonresidents over the amount outstanding on January 1.

Lower rates in Germany without a corresponding reduction in the Netherlands would have heightened upward pressure on the guilder. Consequently, the Netherlands Bank lowered its discount rate from 4-1/2 to 4 per cent on March 1. But capital inflows continued, apparently stimulated by the announcement of an agreement to limit the range of fluctuation among EC currencies. In the four days March 6 through March 9, the Netherlands Bank was forced to buy almost $450 million, $310 million of it on March 9.

On that date the Netherlands Bank took two measures to deal with "the speculative influx of foreign exchange." First, a ban was imposed on the placing of guilders in time deposits in the Netherlands by nonresidents except with central bank authorization, which is likely to be granted only in very exceptional cases. Existing time deposits held by nonresidents are not to be renewed upon expiration. Second, interest may no longer be paid by Netherlands banks on demand deposits of nonresidents.

A first step toward relaxing monetary policy was taken on March 7 when credit ceilings on short-term lending were suspended.

In announcing the move, the Dutch central bank indicated concern over recent declines in fixed private capital investment. However, the move is at best likely to have psychological effect; the banks have been below their ceilings since August 1970. It has been suggested that the ceilings would have been lifted earlier had not key wage negotiations been in progress. With inflationary pressures in the Netherlands still severe, a significant easing of domestic monetary policy seems unlikely.

Following the reduction of official rates in Germany, the Bank of France lowered its intervention rate in the money market by 5/8 percentage points to 4-1/2 per cent. The move was apparently motivated mainly by a desire to discourage inflows of foreign short-term capital. Recently, however, there has been some concern about the rate of expansion of economic activity. On March 10, the French government announced measures designed to stimulate investment: a reduction of minimum reserve requirements from 10 to 8 per cent on demand deposits and from 4 to 3 per cent on savings deposits, and a cut of 1/4 percentage point in coupon rates on long-term public and corporate bond issues. Banks also reduced their lending rates last week.

Although Bank rate in the United Kingdom has not been reduced since December, interest rates still remain fairly near the lows to which they had fallen by the year end. The three-month local authority rate has risen about 50 basis points from its December-January lows to stand at 4.94 per cent on March 14. The three-month Treasury bill rate was 4.35 per cent on that date. Bank rate at 5 per cent is farther above the bill rate than used to be customary.

Long-term interest rates, which declined throughout 1971, have fluctuated since the beginning of the year at a level that is still relatively high in relation to short-term rates. The yield on the 3-1/2 per cent War Loan was 8.50 per cent on March 10, down about one percentage point from its year-earlier levels. Presumably it still reflects a substantial inflation premium.

The Budget is to be announced on March 21 and is expected to be expansionary.

The primary objective of monetary policy in Italy at this time is to create conditions appropriate to a recovery of economic activity. The demand for bank loans weakened sharply in late 1971, this being undoubtedly the major influence making for reductions in the "prime" commercial bank lending rate from 9 per cent in August to 8 per cent at the end of January. Although time deposit rates (which are subject to cartel arrangements) have been unchanged (at 4-3/4 per cent), interbank loan rates have also drifted down since August. Yields on bonds have declined since last summer, but they remain higher than in most other industrial countries.

The National Bank of Belgium reduced its discount rate by 1/2 point each time on January 6, February 3, and March 2, the rate standing at 4 per cent after the most recent cut. The discouragement of reserve increases related to net capital inflows and the encouragement of domestic spending were both important reasons for the moves.

The Bank has not been entirely successful in regard to its external goals: the franc rose sharply on the exchange markets in January and February and official intervention has been required to keep it within the ceiling. A new regulation prohibits banks from reducing their net foreign positions (excluding financial franc deposits) below March 9 levels. Belgian authorities are also concerned about the rate of economic activity; fixed investment spending declined in 1971, and a sharper decrease is expected this year.

Short-term market interest rates have moved down since the beginning of the year in response to the discount rate reductions, the 3-month bill rate dropping from 4.8 per cent to 3.75 per cent as of March 7. But bond yields have declined only a few basis points this year.

In Switzerland, short-term rates have fallen to new lows; the 3-month deposit rate was slashed from 1.5 per cent to 0.5 per cent in February, compared to a peak of 5-1/4 per cent early in 1971. Although there have been no changes in Swiss reserves as a result of exchange market intervention since last August, the Swiss banks are still extremely liquid and loan demand has slackened.

In reaction to the steady upward pressure on the yen for several weeks prior to February 25, the Japanese authorities took measures on that date to inhibit further capital inflows. The ban on advance conversion of export proceeds was reimposed. Foreign banks can no longer bring in funds from abroad to extend credit in Japan; as a measure of compensation, they will be allowed freer access to local sources of funds, such as the call money market.

At the same time, the Bank of Japan continues to promote revival in economic activity. Its basic discount rate was reduced on December 29, 1971, to 4.75 per cent. Interest rates have in general been declining since late 1970. The banks have reduced their borrowing from the central bank by about two-thirds since last summer to the lowest level in more than a decade, indicating that lack of liquidity is no barrier to loan expansion.

The covered interest rate differential vis-à-vis Canada has also been moving in favor of the United States, partly due to the emergence of a substantial discount on the forward Canadian dollar. Thus, for the moment there is no incentive to move short-term capital to Canada. In the future, however, if the Bank of Canada wants to allow the exchange rate to float freely and at the same time wishes to keep the exchange rate down, it will probably have to continue an expansionary monetary policy.