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CONFIDENTIAL (FR)

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

November 15, 1972

By the Staff
Board of Governors
of the Federal Reserve System

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DOMESTIC NONFINANCIAL SCENE

SELECTED DOMESTIC NONFINANCIAL DATA
AVAILABLE SINCE PRECEDING GREENBOOK
(Seasonally adjusted)

	Latest Data-1972			Per Cent Change From		
	Period	Release Date	Data	Preceding Period	Three Periods Earlier	Year Earlier
				(At Annual Rates)		
Civilian labor force	Oct.	11/3	87.3	3.1	3.7	3.0
Unemployment rate	Oct.	11/3	5.5	5.5 1/	5.5 1/	5.8 1/
Nonfarm employment, payroll (mil.)	Oct.	11/3	73.5	5.0	4.8	3.8
Manufacturing	Oct.	11/3	19.1	8.0	6.0	3.5
Nonmanufacturing	Oct.	11/3	54.3	3.9	4.4	3.9
Private nonfarm:						
Average weekly hours (hours)	Oct.	11/3	37.3	37.3 1/	37.2 1/	37.0 1/
Hourly earnings ($)	Oct.	11/3	3.72	9.8	2.2	6.6
Output per manhour (1967=100)	QIII	11/3	113.2	3.7	--	4.3
Compensation per manhour (1967=100)	QIII	11/3	142.2	4.2	--	5.7
Unit labor cost (1967=100)	QIII	11/3	125.6	0.5	--	1.3
Manufacturing:						
Average weekly hours (hours)	Oct.	11/3	40.7	40.7 1/	40.6 1/	39.9 1/
Unit labor cost (1967=100)	Sept.	10/27	120.5	3.0	1.7	3.3
Industrial production (1967=100)	Oct.	11/15	116.7	10.4	9.8	9.3
Consumer goods	Oct.	11/15	124.9	9.7	9.5	7.1
Business equipment	Oct.	11/15	106.2	21.9	16.1	8.1
Defense & space equipment	Oct.	11/15	80.0	4.5	5.6	5.7
Materials	Oct.	11/15	119.6	8.1	9.6	12.2
Wholesale prices (1967=100)	Oct.	11/2	120.5	0.9	4.0	4.9
Industrial commodities	Oct.	11/2	118.8	-1.1	1.9	3.3
Farm products & foods and feeds	Oct.	11/2	124.8	-1.0	8.5	8.9
Consumer prices (1967=100)	Sept.	10/20	126.2	5.5	4.5	3.3
Food	Sept.	10/20	124.7	7.7	6.9	4.8
Commodities except food	Sept.	10/20	120.4	5.0	4.0	2.5
Services 2/	Sept.	10/20	134.1	2.7	3.0	3.3
Personal income ($ bil.) 3/	Sept.	10/17	945.7	7.3	9.9	8.4
				(Not at Annual Rates)		
Plant & equipment expen. ($ bil.)	1973	11/10	98.6	--	--	10.7
Mfrs. new orders dur. goods ($ bil.)	Sept.	11/2	36.8	3.0	3.3	24.1
Capital goods industries:	Sept.	11/2	11.7	9.3	-3.8	28.7
Nondefense	Sept.	11/2	9.4	2.5	2.3	26.4
Defense	Sept.	11/2	2.3	50.7	-22.9	39.1
Inventories to sales ratio:						
Manufacturing and trade, total	Sept.	11/14	1.50	1.49 1/	1.52 1/	1.60 1/
Manufacturing	Sept.	11/2	1.66	1.66 1/	1.69 1/	1.82 1/
Trade	Sept.	11/14	1.34	1.32 1/	1.36 1/	1.38 1/
Ratio: durable goods inventories to unfilled orders	Sept.	11/2	.874	.894 1/	.898 1/	.958 1/
Retail sales, total ($ bil.)	Oct.	11/14	38.8	2.8	3.8	10.8
GAAF	Oct.	11/14	10.2	2.4	3.2	11.8
Auto sales, total (mil. units) 3/	Oct.	11/6	11.29	-4.1	0.8	1.3
Domestic models	Oct.	11/3	9.83	-3.7	0.0	-0.2
Foreign models	Oct.	11/6	1.46	-6.4	6.6	13.2
Housing starts, private (thous.) 3/	Sept.	10/18	2,352	-4.1	0.9	15.9
Leading indicators (1967=100)	Sept.	10/27	146.2	0.4	3.1	13.8

1/ Actual data. 2/ Not seasonally adjusted. 3/ At annual rate. 4/ McGraw-Hill October survey of business capital spending plans.

DOMESTIC NONFINANCIAL DEVELOPMENTS

The pace of economic expansion appears to have accelerated in recent months and staff projections indicate a rise in real GNP at an annual rate of 7.5 per cent this quarter, compared to 6 per cent (or perhaps a little more after the forthcoming revision) in the third quarter. All major demand categories, except for residential construction, are expected to increase more rapidly in the fourth quarter than in the third, with the largest gains expected in consumer spending and inventory investment. Federal defense purchases are projected to rise moderately following a sharp decline in the third quarter.

Heightened demands have been accompanied by sizable gains in industrial production and employment. Industrial output increased by almost 1 per cent in October, with advances widespread among consumer goods, business equipment, and materials. From July to October, the rise in the index was at an annual rate of 10 per cent. Gains in nonfarm employment were substantial in October, for the third consecutive month, with manufacturing contributing appreciably to the overall rise. However, the unemployment rate in October remained at 5.5 per cent as the labor force also increased strongly.

Consumer spending recently has been especially expansive. Retail sales were up almost 3 per cent in October according to the advance report, following the September decline. Unit sales of domestic-type autos have remained strong through early November. Recent surveys of consumer attitudes and buying intentions indicate an upsurge in optimism. Housing starts were still at an exceptionally high level in September.

The business sector also has been strong. Book value of inventories increased considerably further in September, and for the third quarter as a whole the increase was almost half again larger than in the second quarter. Sales were also up sharply, and stock sales ratios remained at the lowest levels in a number of years. Manufacturers' new orders for durable goods rose further in September, as did unfilled orders. The recent McGraw-Hill survey of business plans to spend for plant and equipment indicates a rise of 11 per cent for 1973, with a sharper gain in prospect for manufacturing.

Wage increases have been larger in recent months than earlier. However, the rise in wholesale prices slowed in October to an annual rate of only 1 per cent. The rise in prices of farm products and foods moderated considerably and industrial prices were virtually unchanged, primarily because of a decline in prices of autos and trucks associated with quality improvements in the new models. Consumer prices increased rapidly in September, reflecting continued sharp advances for food and a sizable rise for other commodities.

<u>Outlook</u>. Staff expectations, as before, are for continuing strong expansion in the economy in the remainder of this year. For 1973, also, our projections are relatively little changed overall from five weeks ago, following a thorough review of the underlying statistics and despite modifications in some major assumptions.

Specifically, we no longer assume expiration of the price-wage controls program at the end of April, but rather continuation of a reasonably effective program throughout the year. Also, the current GNP projection assumes Federal expenditures of $253 billion in fiscal 1973 on a unified budget basis, well below the projection of five weeks ago but still somewhat above the Administration's target. Third, we have taken into account the sizable boost in social security taxes associated with "reform" legislation passed at the end of the Congressional session. Monetary policy, however, is still assumed to produce growth in the monetary aggregates at rates consistent with 6 per cent expansion in M_1 during 1973.

The quarterly pattern of GNP growth in 1973, as shown in the table, continues to be for gradual moderation in real terms, with the rate of price inflation accelerating appreciably less rapidly than in our preceding projection over the course of the year.

STAFF 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 rat	
Date	10/11/72	Current	10/11/72	Current	10/11/72	Current	10/11/72	Curre
1971[1/]	74.0	74.0	2.7	2.7	4.5	4.5	5.9	5.9
1972	101.3	100.5	6.4	6.4	3.2	3.2	5.6	5.6
1973	117.6	114.4	6.7	6.4	3.3	3.4	5.0	5.1
1972-I[1/]	31.0	31.0	6.5	6.5	4.5	4.5	5.8	5.8
1972-II[1/]	30.3	30.3	9.4	9.4	2.5	2.5	5.7	5.7
1972-III[1/]	24.0	22.8	6.0	5.9	2.9	2.7	5.6	5.6
1972-IV	31.5	30.6	8.1	7.5	2.8	3.1	5.4	5.4
1973-I	32.5	32.0	7.1	6.6	3.2	3.5	5.2	5.2
1973-II	28.0	28.4	5.6	5.7	3.6	3.7	5.0	5.1
1973-III	28.0	25.4	4.8	4.5	4.2	3.9	4.9	5.0
1973-IV	27.5	26.0	4.3	4.3	4.3	3.9	4.8	4.9

1/ Actual; for 1972-III current GNP figures are preliminary Commerce estimates.

The quarterly projection for 1973 will, as usual, be presented in detail at next week's Chart Show. We note here in summary that most demand sectors--residential construction being the only exception--are expansive in the first half of 1973. Consumer spending is especially strong, in part because of the large tax refunds in prospect. Business spending on fixed capital maintains a fairly rapid advance, as suggested by recent surveys. And inventory investment is expected to rise further in line with final sales of goods.

In the second half of the year, demand forces are likely to be losing some of their upward momentum. The bulk of the tax refunds will have been completed, inventory investment is expected to show little further increase from the pace reached by mid-year, and residential construction is projected to be declining. The unemployment rate is expected to decline to just under 5.0 per cent in the fourth quarter, about the same rate as projected earlier.

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.	1973 Proj.	1971 IV	1972 I	1972 II	1972 III	1972 Proj. IV
Gross National Product	1050.4	1150.9	1265.3	1078.1	1109.1	1139.4	1162.2	1192.8
Final purchases	1046.7	1145.7	1252.8	1076.4	1108.6	1134.4	1156.6	1183.3
Private	813.9	890.1	977.5	835.5	859.2	880.3	900.0	920.9
Excluding net exports	813.2	893.9	978.7	837.6	863.8	885.5	903.4	923.0
Personal consumption expenditures	664.9	720.6	791.0	680.5	696.1	713.4	728.1	744.8
Durable goods	103.5	115.8	130.1	106.1	111.0	113.9	118.4	120.0
Nondurable goods	278.1	299.1	327.5	283.4	288.3	297.2	301.4	309.3
Services	283.3	305.7	333.3	290.9	296.7	302.4	308.3	315.5
Gross private domestic investment	152.0	178.5	200.2	158.8	168.1	177.0	181.0	187.7
Residential construction	42.6	53.3	53.0	47.3	51.6	52.8	54.2	54.7
Business fixed investment	105.8	120.0	134.8	109.8	116.1	119.2	121.1	123.5
Change in business inventories	3.6	5.2	12.5	1.7	0.4	5.0	5.7	9.5
Nonfarm	2.4	4.8	12.5	0.8	0.1	4.3	5.3	9.3
Net exports of goods and services 1/	0.7	-3.8	-1.2	-2.1	-4.6	-5.2	-3.4	-2.1
Exports	66.1	73.6	84.5	63.0	70.7	70.0	75.0	78.8
Imports	65.4	77.4	85.7	65.1	75.3	75.2	78.4	80.9
Gov't. purchases of goods and services	232.8	255.6	275.3	240.9	249.4	254.1	256.6	262.4
Federal	97.8	106.8	107.1	100.7	105.7	108.1	106.2	107.0
Defense	71.4	76.6	76.9	71.9	76.7	78.6	75.2	76.0
Other	26.3	30.1	30.3	28.7	28.9	29.6	31.0	31.0
State & local	135.0	148.9	168.2	140.2	143.7	146.0	150.4	155.4
Gross national product in constant (1958) dollars	741.7	788.9	839.2	754.5	766.5	783.9	795.3	810.1
GNP implicit deflator (1958 = 100)	141.6	145.8	150.8	142.9	144.7	145.3	146.1	147.0
Personal income	861.4	935.0	1019.8	881.5	907.0	922.1	939.5	971.2
Wage and salary disbursements	572.9	626.3	684.6	585.9	608.0	620.5	630.4	646.4
Disposable income	744.4	794.5	876.9	785.5	770.5	782.6	798.7	826.2
Personal saving	60.9	54.8	66.1	59.3	55.7	50.1	51.3	61.9
Saving rate (per cent)	8.2	6.9	7.5	7.8	7.2	6.4	6.4	7.5
Corporate profits before tax	83.3	94.8	110.3	83.2	88.2	91.6	97.3	102.0
Corp. cash flow, net of div. (domestic)	78.2	92.0	104.9	82.7	85.9	90.8	93.7	97.5
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	199.1	228.1	247.5	202.8	221.4	224.9	230.2	235.8
Expenditures	220.8	248.0	270.9	227.5	236.3	246.5	243.1	265.9
Surplus or deficit (-)	-21.7	-19.9	-23.4	-24.7	-14.8	-21.6	-12.9	-30.1
High employment surplus or deficit (-)	3.7	-2.0	-8.3	6.8	8.6	-2.4	2.2	-16.5
Total labor force (millions)	86.9	89.1	90.9	87.7	88.4	88.8	89.2	89.8
Armed forces "	2.8	2.4	2.4	2.7	2.5	2.4	2.4	2.4
Civilian labor force "	84.1	86.6	88.5	85.0	85.9	86.4	86.8	87.4
Unemployment rate (per cent)	5.9	5.6	5.1	5.9	5.8	5.7	5.6	5.4
Nonfarm payroll employment (millions)	70.7	72.8	75.0	71.0	71.8	72.5	73.0	73.7
Manufacturing	18.6	18.9	19.7	18.6	18.7	18.9	18.9	19.2
Industrial production (1967 = 100)	106.8	113.8	122.9	107.4	109.9	113.3	114.9	117.4
Capacity utilization, manufacturing (per cent)	75.0	77.5	80.5	74.6	75.3	77.4	78.0	79.1
Housing starts, private (millions, A.R.)	2.05	2.35	2.08	2.24	2.51	2.26	2.34	2.28
Sales new autos (millions, A.R.)	10.13	10.76	11.45	10.48	10.05	10.30	11.28	11.38
Domestic models	8.68	9.37	10.07	9.20	8.65	8.91	9.90	10.00
Foreign models	1.45	1.39	1.38	1.28	1.40	1.39	1.38	1.38

1/ Revisions in underlying balance of payments data for 1972-II, not yet reflected in the GNP data, indicate a $1 billion larger deficit in net exports of goods and services for that and following quarters.

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1971	1972 Proj.	1973 Proj.	1971 IV	1972 I	1972 II	1972 III	1972 Proj. IV
	---Billions Of Dollars---							
Gross National Product	74.0	100.5	114.4	21.2	31.0	30.3	22.8	30.6
Inventory change	-1.3	1.6	7.3	0.4	-1.3	4.6	0.7	3.4
Final purchases	75.2	99.0	107.1	20.8	32.2	25.8	22.2	27.1
Private	61.4	76.2	87.4	13.5	23.7	21.1	19.7	21.3
Excluding net exports	64.3	80.7	84.8	16.0	26.2	21.7	17.9	19.6
Net exports	-2.9	-4.5	2.6	-2.5	-2.5	-0.6	1.8	1.7
Government	13.8	22.8	19.7	7.3	8.5	4.7	2.5	5.8
GNP in constant (1958) dollars	19.6	47.2	50.3	12.0	12.0	17.4	11.4	14.8
Final purchases	21.1	45.8	51.2	12.1	12.5	13.7	10.8	11.7
Private	22.5	39.7	41.8	8.6	11.4	12.0	11.1	10.2
	---Per Cent Per Year---							
Gross National Product	7.6	9.6	9.9	8.3 1/	12.0 1/	11.4 1/	8.0	10.5
Final purchases	7.7	9.5	9.3	7.9	12.0	9.3	7.8	9.4
Private	8.2	9.4	9.8	6.6	11.3	9.8	9.0	9.5
Personal consumption expenditures	7.8	8.4	9.8	5.8	9.2	9.9	8.2	9.2
Durable goods	14.4	11.9	12.3	0.0	18.5	10.5	15.8	5.4
Nondurable goods	5.2	7.6	9.5	7.0	6.9	12.3	5.7	10.5
Services	8.2	7.9	9.0	6.7	8.0	7.7	7.8	9.3
Gross private domestic investment	10.9	17.4	12.2	17.3	23.4	21.2	9.0	13.9
Residential construction	36.5	25.1	-0.6	25.2	36.4	9.3	10.6	3.7
Business fixed investment	4.9	13.4	12.3	13.2	23.0	10.7	6.4	7.9
Gov't. purchases of goods & services	6.3	9.8	7.7	12.5	14.1	7.5	3.9	9.0
Federal	1.3	9.2	0.3	11.4	19.9	9.1	-7.0	3.0
Defense	-4.9	7.3	0.4	10.3	26.7	9.9	-17.3	4.3
Other	22.3	14.4	0.7	12.9	2.8	9.7	18.9	0.0
State & local	10.2	10.3	13.0	13.3	10.0	6.4	12.1	13.3
GNP in constant (1958) dollars	2.7	6.4	6.4	6.7 1/	6.5 1/	9.4 1/	5.9 1/	7.5
Final purchases	2.9	6.2	6.5	6.5	6.6	7.2	5.5	5.9
Private	3.9	6.6	6.5	5.7	7.4	7.7	7.0	6.3
GNP implicit deflator	4.7	3.0	3.4	1.5 1/	5.1 1/	1.8 1/	2.2 1/	3.0
Private GNP fixed weight index 2/	4.5	3.2	3.4	1.7 1/	4.5 1/	2.5 1/	2.7 1/	3.1
Personal income	6.8	8.5	9.1	6.3	11.6	6.7	7.5	13.5
Wage and salary disbursements	5.7	9.3	9.3	6.9	15.1	8.2	6.4	10.2
Disposable income	8.0	6.7	10.4	4.3	6.3	6.3	8.2	13.8
Corporate profits before tax	12.1	13.8	16.4	-4.3	24.0	15.4	24.9	19.3
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	3.9	14.6	8.5	7.4	36.7	6.3	9.4	9.7
Expenditures	8.0	12.3	9.2	9.5	15.5	17.3	-5.5	37.5
Nonfarm payroll employment	0.1	2.9	3.1	2.5	3.8	4.1	2.5	3.8
Manufacturing	-3.9	1.7	3.3	1.3	2.2	5.5	1.4	6.3
Industrial production	0.2	6.6	8.0	3.4	9.3	12.4	5.6	8.8
Housing starts, private	43.1	14.5	-11.4	24.2	48.5	-39.8	13.8	-11.3
Sales new autos	21.3	6.2	6.4	7.4	-14.9	20.3	37.9	3.5
Domestic models	21.9	7.9	7.5	20.1	-28.4	12.1	44.4	4.0
Foreign models	17.9	-4.4	-0.7	-76.9	50.6	-3.0	-4.9	0.0

1/ At compound rates.

2/ Using expenditures in 1967 as weights.

Industrial production. Industrial production increased 0.9 per cent in October and at 116.7 per cent (1967=100) was 9.3 per cent above a year earlier. The gains in output in October were widespread among consumer goods, equipment, and materials. The September and August indexes each have been revised upwards by 0.5 points, to 115.7 and 115.0, respectively. Growth in output has been unusually rapid since July, at an annual rate of 10 per cent.

Auto assemblies rose 7 per cent in October, to an annual rate of 9.1 million units. Production schedules for November and December indicate a further increase of about 6 per cent. If these schedules are realized, auto output in 1972 would total 8.8 million units compared with 8.5 million units in 1971. Output of furniture and nondurable consumer goods rose again in October, but production of appliances changed little.

Output of business equipment continued to rise strongly and was 8 per cent above a year ago; it was 12 per cent above the 1971 low but still 4 per cent below its 1969 peak. Production of defense equipment changed little in October, and, although up 8 per cent from the January 1972 low, was still one-fourth below its 1969 peak. Output of construction products and steel, textiles, and chemicals advanced further.

INDUSTRIAL PRODUCTION
(1967=100, seasonally adjusted)

Item	1972		Per cent changes	
	Sept.(r)	Oct.(e)	Oct. 1971 to Oct. 1972	Sept. 1969* to Oct. 1972
Total index	115.7	116.7	9.3	4.3
Consumer goods	123.9	124.9	7.1	11.2
Autos	109.6	116.9	8.4	.3
Home goods	126.3	126.1	10.7	13.0
Apparel & staples	123.0	123.7	6.1	11.1
Business equipment	104.3	106.2	8.1	-3.7
Defense equipment	79.7	80.0	5.7	-21.6
Intermediate products	121.1	122.7	8.4	9.5
Construction products	120.5	122.5	8.6	9.5
Materials, total	118.8	119.6	12.2	4.5
Durable	115.4	116.3	13.8	1.2
Steel	111.8	114.1	27.6	-2.5
Nondurable	123.2	123.9	7.7	8.9

* Pre-recession peak for total index.
r Revised.
e Estimate.

Retail sales. Sales in October rose by an unusually large amount, 2.8 per cent, according to the advance report. Advances were widespread by store type. Further, more complete sample counts raised earlier estimates of retail sales in August and September, and the third quarter increase is now reported to be 2.5 per cent--a very large increment on top of the substantial 3.3 per cent gain in the second quarter. These changes suggest the likelihood of an upward revision in third quarter personal consumption expenditures in the GNP accounts.

In October, all major types of outlets showed moderate to strong increases. Durable goods sales increased 3.9 per cent from September, with the automotive group reporting a 5 per cent gain. Non-durable goods sales were 2.3 per cent higher, with food sales up 2.2 per cent and general merchandise sales up 3.1 per cent.

RETAIL SALES
(Percentage change from previous period)

Item	1972					
	I Q	II Q	III Q	August	September	October
All retail stores	1.2	3.3	2.5	1.7	- .8	2.8
Durable	.3	4.2	3.9	3.0	-1.9	3.9
Auto	-3.1	6.4	4.6	4.4	-2.7	5.0
Furniture & appliance	9.2	- .5	2.0	.9	-2.6	.9
Nondurable	1.6	2.9	1.9	1.0	- .2	2.3
Food	1.7	3.6	1.7	1.0	- .6	2.2
General merchandise	2.3	2.7	2.6	.2	.6	3.1
GAAF	3.0	2.4	2.0	.4	.3	2.4
Total, less autos & nonconsumer items	2.1	2.9	1.8	.9	- .2	2.1
Real*	.3	2.7	1.5	1.4	-1.4	n.a.

* Deflated by seasonally adjusted all commodities CPI.

<u>Unit sales of consumer durables</u>. October sales of new domestic-type autos were at a 9.8 million unit rate, slightly below September but the same as a year earlier. Sales have been especially strong in the past four months, averaging a 9.9 million unit rate. In the first 10 days of November, sales were at a 9.6 million rate. Dealer inventories amounted to only a 45-day supply at the end of October, 9 per cent above the reduced September levels, but 13 per cent below the low level a year earlier.

Sales of imported cars in October were at a 1.5 million unit rate, down slightly from a month earlier, but up a sixth from October last year, when dock strikes and Phase I measures sharply curtailed import sales. The October import share, on a seasonally adjusted basis, was 13.4 per cent, approximately the same as in September, but well below the share prior to the adjustment in exchange rates last year.

Truck sales in October are estimated at a 2.4 million unit annual rate, up 7 per cent from both a month and a year earlier.

Data for most of October indicate that retailers' unit purchases of major home appliances were below the levels of both a month and a year earlier. All appliances in the index, with the exception of freezers, either remained at or declined from September levels.

UNIT PURCHASES OF HOME GOODS BY RETAILERS
Seasonally adjusted, 1967=100

	1971	1972			Per cent change	
	Oct.	Aug.	Sept.	Oct.	Month ago	Year ago
TVs 1/	121	139	149r	135	-10	12
Radios	106	80	98r	84	-14	-20
Home appliances 2/	135	139r	140r	130e	-7	-4

1/ Includes foreign-made units sold under U. S. brand names. Foreign-made sold under foreign brands not included.

2/ Weighted average of indexes for dishwashers, driers, freezers, electric ranges, gas ranges, room air conditioners, refrigerators, washing machines and vacuum cleaners.

Consumer credit. In September, total consumer credit outstanding expanded at a reduced seasonally adjusted annual rate of $15.9 billion. The sharp drop from the August high of $22.2 billion was widespread by both type of credit and lender, and partly reflected the early date of Labor Day and a decline in the proportion of retail purchases financed with credit. Scattered trade reports indicate that net credit extensions rebounded substantially in October.

During the third quarter, the net increase in total consumer credit edged up to a new high of $18.7 billion. The rise in instalment credit accelerated further but the advance in the noninstalment sector was smaller than in the preceding quarter.

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

	Total	Instalment	Noninstalment
1971 - Q I	7.3	5.5	1.8
Q II	9.9	7.8	2.1
Q III	12.9	10.8	2.2
Q IV	13.7	11.8	1.9
1972 - Q I	13.1	13.2	-.1
Q II	18.0	14.8	3.2
Q III	18.7	16.1	2.6
July	18.0	13.1	4.9
August	22.1	19.7	2.5
September	15.9	15.4	.4

Growth in auto credit has accounted for an increasing proportion of the quarterly net gains in instalment credit outstanding this year. In the first quarter, auto credit rose at a seasonally adjusted annual rate of $3.9 billion and accounted for 29 per cent of the total growth in instalment debt; the second and third quarters showed increases of $5.0 billion (33 per cent) and $5.9 billion (37 per cent), respectively. Since the end of last year the average instalment contract has risen about $65 for new cars and nearly $125 for used cars. In September, finance rates for new cars were one-quarter of a point below the year earlier level; used car rates have shown an apparent seasonal rise throughout the model year but were still slightly below the September 1971 level.

Mobile home credit is becoming an increasingly significant part of consumer financing activity at commercial banks and finance companies. At the end of September, mobile home loans outstanding at these institutions had reached a total of $8.3 billion, up 24 per cent from the year earlier total of $6.7 billion. Mobile home loans, although still a relatively small part of total consumer credit outstanding, now constitute 36 per cent of nonautomotive consumer goods credit outstanding at banks and 46 per cent at finance companies. The $200 million increase during September in mobile home credit outstanding amounted to one-half of the total increase in other consumer goods financing.

One reason for the rapid growth in mobile home balances has been the increase in average price and contract size due to market acceptance of "14-wides" and double-wide units. At finance companies, the average amount financed per contract during September was over $6,500, up nearly $600 since last spring. Bank contracts have shown an even larger increase.

Census consumer purchase and income expectations. The October Census survey indicates an unusually large increase in consumer optimism--confirming the latest Michigan Survey Research Center report and the attitudinal questions from the current Conference Board survey. Buying plans for autos rose sharply, as did purchase plans for homes. Both intentions to buy major appliances and expected purchases of furniture and carpets were up almost as strongly.

Actual income changes and expectations of future income increases were also more favorable. Higher current income was reported by 40.8 per cent of all households, up sharply from the 34.3 per cent of the July survey. The response is comparable to the favorable income developments reported during 1968. Income expectations improved more modestly but households in the July survey had already indicated a very marked increase in income expectations.

HOUSEHOLD PURCHASE AND INCOME EXPECTATIONS

	1971	1972			
	October	Jan.	April	July	October
SEASONALLY ADJUSTED INDEXES OF EXPECTED UNIT PURCHASES (Jan. 1967-April 1967 = 100)					
All households:					
New cars	103.4	98.8	103.5	99.6	109.9
Houses	95.5	98.9	110.4	110.1	123.5
ACTUAL AND EXPECTED CHANGES IN INCOME					
Current income compared to income of one year ago:					
All households:					
Per cent reporting higher current income	34.9	35.2	35.7	34.3	40.8
Per cent reporting lower current income	13.7	12.7	12.5	10.9	12.0
Difference	21.2	22.5	23.2	23.4	28.8
Mean expectations of substantial changes in income:					
All households:					
Increase	15.7	15.9	16.1	19.9	20.1
Decrease	6.7	6.2	6.7	6.4	6.1
Difference	9.0	9.7	9.4	13.4	14.0
EXPECTATIONS TO BUY FURNITURE, APPLIANCES, AND HOME IMPROVEMENTS WITHIN 12 MONTHS					
Number of major appliances reported likely to be bought per 100 households	26.1	25.6	27.6	26.0	28.7
Per cent of households reporting probable major expenditures on--					
Furniture and carpets	26.1	26.7	28.8	25.8	28.8

Anticipated plan and equipment spending. Three recent private surveys indicate that business now reports plans to increase spending for new plant and equipment by about 9-11 per cent in 1973. The McGraw-Hill survey indicates that 1973 spending by manufacturers is programmed to rise at a more rapid pace (14 per cent) than that of nonmanufacturing concerns (9 per cent); in contrast, in 1971 and 1972 nonmanufacturing firms showed much sharper gains. Electric utilities and communication firms continue to plan further sizable gains in new capital spending. Historically, the November McGraw-Hill survey taken at this stage of an economic recovery has tended to understate the actual change by /about 3 percentage points. Surveys, taken earlier, by Lionel D. Edie and Rinfret-Boston show generally similar results, although the magnitude of change is slightly smaller than in the McGraw-Hill survey.

PLANT AND EQUIPMENT EXPENDITURES
(Per cent change from preceding year)

	1971	1972 1/ (Antic.)	1973 McGraw-Hill (November)	1973 Rinfret-Boston (October)	1973 Lionel D. Edie (October)
Total	1.9	9.7	11	9	10
Manufacturing	-6.1	5.6	14	13	13
Durable goods	-10.4	10.9	15	10	14
Nondurable goods	-1.9	.8	12	17	12
Nonmanufacturing 2/	7.2	12.1	9	7	9
Railroad	-6.0	8.3	-1	-6	12
Other Transportation	-23.5	19.0	-9	23	-5
Electric utilities	20.8	13.3	13	6	13
Gas utilities	-2.0	12.6	6	-6	-9
Communication	6.6	11.4	9	10	12
Commercial	8.8	10.7	10	4	9

1/ U.S. Department of Commerce Survey--September 1972.
2/ Includes industries not shown separately.

<u>Cyclical indicators.</u> The Census composite index of leading indicators rose slightly further in September, following a strong increase in August. Leading series increasing included the workweek, new orders for durable goods, contracts and orders for plant and equipment (which exceeded its previous high), housing permits and industrial materials prices. Series declining were unemployment initial claims (inverted), common stock prices and the ratio of price to unit labor cost.

CHANGE IN COMPOSIT CYCLICAL INDICATORS
(per cent change from previous month)

	June	July	Aug.	Sept. (p)
12 Leading (trend adjusted)	- .1	.1	2.6	.4
12 Leading, prior to trend adjustment	- .4	- .4	2.3	.0
5 Coincident	.4	.7	1.2	.9
5 Coincident, deflated	.4	.6	1.0	.7
6 Lagging	.9	.6	.9	1.1

p - Preliminary

<u>Construction and real estate.</u> Seasonlly adjusted value of new construction put in place, which was revised downward somewhat for September, edged off further in October but remained near the August peak. Within the private sector, a further rise in residential expenditures was more than offset by a reduction in nonresidential construction outlays. Outlays for public construction apparently rose in October, with the rise entirely in Federally owned projects.

The Census Bureau's composite construction cost index in October remained at the 139 per cent level (1967 equals 100) reached in September, holding the year-to-year increase to less than 5 per cent for the fifth consecutive month. This compares with a year-to-year rise of nearly 7.5 per cent in 1971 as a whole and 7 per cent in 1970.

NEW CONSTRUCTION PUT IN PLACE
(Seasonally adjusted annual rates, in billions of dollars)

	1972				
	QII(r)	QIII(p)	Aug.(r)	Sept.(r)	Oct.1/
Total - current dollars	121.2	122.1	123.1	122.9	122.0
Private	92.1	93.5	94.0	94.7	93.4
Residential	52.6	54.3	54.3	55.1	55.4
Nonresidential	39.4	39.2	39.8	39.6	38.0
Public	29.1	28.5	29.1	28.2	28.6
State and local	24.6	24.4	25.1	24.2	24.2
Federal	4.5	4.1	4.0	4.0	4.3
Total - 1967 dollars	88.8	88.3	89.0	88.7	87.9

1/ Data for October 1972 are confidential Census Bureau extrapolations. In no case should public reference be made to them.

Seasonally adjusted private housing starts, which had expanded sharply in August, dipped only 4 per cent in September to an annual rate of 2.35 million units. As a result, the average for the third quarter as a whole held above the second quarter pace and, except for this year's first quarter average, was the highest on record. While housing starts may move downward during the fourth quarter, the advanced rate of building-permits and mortgage-commitments in recent month suggests that the decline will be limited.

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

	1972					
	QI	QII	QIII	July(r)	Aug.(r)	Sept.(p)
Starts	2.51	2.26	2.34	2.22	2.45	2.35
1-family	1.35	1.27	1.35	1.29	1.40	1.38
2-or-more-family	1.16	.99	.99	.93	1.06	.97
Permits	2.09	2.04	2.16	2.11	2.24	2.25
Completions	1.98	1.90	1.94	1.89	2.00	1.93
MEMORANDUM: Mobile home shipments	.57	.60	.54	.57	.53	.50

p - Preliminary

Although completions of new housing units have been at a record rate this year, they have continued appreciably below the extraordinary level of starts, reflecting, in part, capacity constraints--particularly for lumber and related materials. Meanwhile, based on sales data through September, demands for both new and existing dwellings have remained very strong. Consequently, rental vacancy rates moved only moderately higher in the third quarter to an average of 5.8 per cent of units available for use. This was still below the third quarter rate in 1968 and well below the record for the series reached in 1965. In the case of home-owner units, the vacancy rate actually was below the year-earlier level.

RESIDENTIAL VACANCY RATES

	Average for the third quarter:					
	1965	1968	1969	1970	1971	1972
Rental units	7.8	5.9	5.5	5.3	5.6	5.8
Northeast	5.0	3.7	3.0	3.1	3.0	3.2
North Central	6.8	5.8	5.9	5.9	5.6	6.2
South	8.7	7.5	7.1	7.1	7.4	7.3
West	11.3	6.5	5.9	5.2	6.5	6.7
Homeowner units	1.6	1.2	1.1	1.1	1.0	3.9

<u>Manufacturers' orders and shipments</u>. New orders for durable goods rose 3 per cent (p) in September. Most of the increase resulted from a rebound in the volatile defense orders series, but there was also a 2.5 per cent increase in orders for nondefense capital goods. For the third quarter as a whole, new orders were up 2.9 per cent, which was about half the second quarter rate of increase. Defense orders were down sharply and nondefense capital goods rose more slowly than in the second quarter, but orders for motor vehicles and primary metals accelerated.

MANUFACTURERS' NEW ORDERS FOR DURABLE GOODS
(Per cent changes)

	1972		
	Q II from Q I	Q III from Q II (p)	Sept. from Aug. (p)
Durable goods, total	5.7	2.9	3.0
Excluding defense	5.8	4.3	.9
Primary metals	6.8	9.7	- .9
Motor vehicles and parts	1.2	12.4	- .3
Household durables	8.4	.4	2.4
Capital goods industries:			
Nondefense	8.7	2.6	2.5
Defense	4.3	-17.8	50.7
Construction & other durables	4.3	.1	.6

Durable goods shipments also rose in September but remained below the level of incoming orders, and unfilled orders rose a strong 2.4 per cent, with increases for every reported industry and market category. The durable goods order backlog has now risen 14 per cent above its July 1971 low, somewhat more than the comparable expansion in 1968-69 but only half the 1965-66 increase.

Inventories. Book value of manufacturing and trade inventories rose at a $14.7 billion (p) annual rate in September, not far below the upward-revised August rate of $18.3 billion. For the quarter as a whole, the rate was $12.8 billion, well above the second quarter rate of $8.7 billion and the highest in four years. About $2 billion of this amount was an unusual increase at wholesale farm and raw materials dealers; this apparently reflected both higher wheat prices and movement of grains into warehouses in anticipation of shipment to Russia.

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

	1972			
	Q II	Q III (Prel.)	Aug. (Rev.)	Sept. (Prel.)
Manufacturing and trade	8.7	12.8	18.3	14.7
Manufacturing, total	4.2	7.1	15.0	1.8
Durable	3.3	4.8	10.8	.9
Nondurable	.9	2.3	4.2	.8
Trade, total	4.5	5.6	3.3	12.9
Wholesale	1.9	4.2	1.3	6.3
Retail	2.6	1.5	2.0	6.6

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

The outlook for sustained increases in inventory investment remains good. In September, the inventory-sales ratio for manufacturing and trade rose slightly but remained near the lowest level in many years. The ratio of inventories to unfilled orders at durable goods manufacturers dropped further.

INVENTORY RATIOS

	1971		1972	
	August	Sept.	August (Rev.)	Sept. (Prel.)
Inventories to sales:				
Manufacturing and trade	1.58	1.60	1.49	1.50
Manufacturing, total	1.79	1.82	1.66	1.66
Durable	2.14	2.22	1.97	1.96
Nondurable	1.36	1.36	1.28	1.28
Trade, total	1.38	1.38	1.32	1.34
Wholesale	1.23	1.23	1.20	1.21
Retail	1.48	1.48	1.40	1.42
Inventories to unfilled orders:				
Durable manufacturing	.956	.958	.894	.874

Labor market. Demand for labor continued strong in October as both payroll and total employment advanced by over a quarter million. But the civilian labor force increased sharply as well and the unemployment rate remained unchanged.

Employment expansion has been brisk in the past three months following a relatively slack interval during the summer. Much of the recent strength has been in manufacturing where employment increases had lagged during the first year of the recovery, spurted in the early months of 1972, and then remained on a plateau in the late spring and early summer. Recent gains have been concentrated in durable goods-primarily metal and metal-using industries. Outside of manufacturing, employment advances have continued appreciable in trade, services and finance, and State and local government.

NONFARM PAYROLL EMPLOYMENT
(Seasonally adjusted, in thousands)

	Oct. 1971- May 1972	May 1972- July 1972	July 1972- Oct. 1972	Sept. 1972- Oct. 1972
	Average Monthly Change			
Total	247	35	291	303
Government	49	3	67	38
Federal	0	-22	5	0
State and local	49	25	62	38
Private	198	31	224	265
Manufacturing	57	-16	94	126
Mining	12	-3	2	1
Construction	9	-23	19	0
Transportation	12	-9	13	22
Trade	55	30	52	64
Services & finance	54	52	44	52

The manufacturing workweek remained at 40.7 hours in October. The factory workweek has been stable since June, after having risen from a nine-year low reached in September 1970. Average overtime hours in manufacturing also have changed little in recent months, but have been substantially more than a year ago.

Unemployment and labor force. The unemployment rate remained at 5.5 per cent (seasonally adjusted) in October, about the same as in the previous four months. Jobless rates for most groups showed little or no change. Compared with a year ago, when the overall unemployment rate was 5.8 per cent, unemployment was down moderately for adult men, teenagers, and white workers, while rates remained about the same for household heads, adult women, and Negro workers. The unemployment situation for Vietnam era veterans has improved considerably in recent months, and in October the rate for veterans 20 to 29 years of age was about the same as the non-veteran rate.

SELECTED UNEMPLOYMENT RATES
(Seasonally adjusted)

	1971	1972			
	Oct.	April	June	Sept.	Oct.
Total	5.8	5.9	5.5	5.5	5.5
Men 20 years and over	4.3	4.3	4.0	3.8	3.9
Women 20 years and over	5.5	5.4	5.5	5.4	5.5
Teenagers	16.7	17.3	14.5	16.5	15.3
Household heads	3.5	3.4	3.6	3.3	3.4
White workers	5.3	5.4	5.0	5.0	5.0
Negro workers	10.4	9.6	9.4	10.2	10.1
Veterans 20 to 29 years	8.0	8.6	7.2	6.6	6.4
Nonveterans 20 to 29 years	7.3	7.6	6.5	6.1	6.6

The civilian labor force increased substantially in October. Compared to a year earlier, the civilian labor force was up by 2.2 million; about 300,000 of the increase resulted from declines in the armed forces.

Earnings. Average hourly earnings of production workers on private nonfarm payrolls (adjusted for overtime in manufacturing and inter-industry shifts) have been rising at a quickened pace recently; estimates for September have been revised up, and with substantial increases also in October the increase in earnings in the last two months has averaged around 8 per cent (annual rate). Increases have been very rapid in several industries--especially services, manufacturing and construction. Since January, nonfarm earnings have increased at a 5.5 per cent rate, but the increase since July has been at nearly a 7 per cent rate.

HOURLY EARNINGS INDEX
(Per cent change; seasonally adjusted, annual rate)

	Jan. 1971-Aug. 1971	Jan. 1972-Oct. 1972	July 1972-Oct. 1972
Total	6.6	5.5	6.9
Manufacturing	6.0	5.6	6.8
Mining	8.3	4.2	3.9
Construction	8.8	4.4	6.6
Transportation	8.2	9.0	7.9
Trade	6.2	4.4	4.3
Finance	7.1	5.2	5.9
Services	5.5	4.7	8.7

Collective bargaining. Wage increases in major nonfarm collective bargaining settlements averaged 6.6 per cent over-the-life of the contract in the first nine months of 1972 as compared to the 8 per cent rise in 1971. Settlements in both manufacturing and non-manufacturing industries were well below wage rate changes negotiated a year ago, with the construction industry showing a marked slowing. First year increases have been substantially smaller, indicating a movement away from the widespread practice of front-end loading of contracts. In addition, contracts this year have a shorter average duration--about three months on average less than previously--indicating a tendency toward shorter contracts during the stabilization period, especially in the construction industry. Wage and benefit increases together averaged 7.6 per cent over-the-life of the contract, compared with 8.8 per cent in 1971.

The new settlements cover nearly 1.5 million workers, primarily in the aerospace, railroad, construction, and maritime industries--significantly fewer than the 2.8 million covered in the first nine months of 1971. The Pay Board and the Construction Industry Stabilization Committee have yet to act on agreements affecting an additional 872,000 workers.

WAGE INCREASES PROVIDED BY MAJOR CONTRACT SETTLEMENTS*
(Mean wage adjustment--annual rate
of increase, per cent)

	Year		First 9 months	
	1970	1971	1971	1972
Average over life of contract				
Total	8.9	8.1	8.0	6.6
Manufacturing	6.0	7.3	7.1	5.6
Nonmanufacturing	11.5	8.9	9.0	7.2
Construction	14.9	10.8	11.7	6.6
First year				
Total	11.9	11.6	11.8	7.2
Manufacturing	8.1	10.9	10.7	6.9
Nonmanufacturing	15.2	12.2	13.0	7.3
Construction	17.6	12.6	13.5	7.1

*Applies to settlements affecting 1,000 or more workers.

<u>Wholesale prices</u>. Wholesale prices rose between September and October at a seasonally adjusted annual rate of 0.9 per cent, the smallest monthly increase since last March. Prices of industrial commodities changed little, and the increase for farm and food products was the smallest in recent months.

Lower seasonally adjusted prices of automobiles and trucks more than offset substantial increases for lumber and plywood, textile products and apparel, hides, skins, leather, and iron and steel scrap. If the transportation equipment group were excluded, industrial commodities would have shown an annual rate of increase of about 2-1/2 per cent, seasonally adjusted.

On a seasonally unadjusted basis, prices of passenger cars fell about 2 per cent and trucks more than 1 per cent. In the case of passenger cars, the BLS allowance for quality improvements in 1973 models was larger than the price rise resulting from the discontinuance of rebates to dealers and from price increases allowed by the Price Commission to cover costs of optional equipment made standard on the new models. After adjustment for seasonal influences the decline in prices amounted to about 5 per cent for passenger cars and 3 per cent for trucks.

Although the increase in prices of farm and food products in October was the smallest in 6 months, consumer finished foods rose markedly as seasonally adjusted prices of meat, poultry, egg, and dairy products moved higher.

During the first 11 months of Phase II, wholesale prices rose at an annual rate of about 5 per cent, the same rate as in the 8 months of 1971 preceding the freeze. However, prices of industrial commodities advanced at a more moderate pace--3.5 per cent--while farm and food products moved up more rapidly than in the pre-stabilization period.

WHOLESALE PRICES
(Percentage changes at seasonally adjusted annual rates)

	1972			Pre-stab. period	Phase II
	Dec. 1971 to June 1972	June to Sept.	Sept. to Oct.	Dec. 1970 to Aug. 1971	Nov. 1971 to Oct. 1972
All commodities	4.9	6.7	.9	5.2	5.2
Farm products1/	5.9	17.4	1.9	6.5	9.6
Industrial commodities	4.5	3.2	-1.1	4.7	3.5
Crude materials2/	9.2	10.6	15.4	3.3	9.6
Intermediate materials3/	5.2	2.4	4.1	6.5	4.1
Finished goods4/	3.2	3.3	-7.9	2.7	2.1
Producer	2.7	2.0	-7.0	3.7	2.5
Consumer	2.7	3.9	-8.4	2.2	2.2

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

Consumer prices. Consumer prices rose at a seasonally adjusted annual rate of 5.7 per cent in September and were 3.3 per cent above a year earlier. The September advance, the largest since February, included continued sharp increases for food--at an 8 per cent rate--and an accelerated rate of rise of about 5 per cent for other commodities. The increase in service costs continued moderate.

CONSUMER PRICES
(Percentage changes, seasonally adjusted annual rates)

	1972			Pre-stab. period	Phase II
	Dec. 1971 to June 1972	June to Sept.	Aug. to Sept.	Dec. 1970 to Aug. 1971	Nov. 1971 to Sept. 1972
All items	2.9	4.6	5.7	3.8	3.5
Food	3.5	7.0	8.0	5.0	4.9
Commodities less food	2.6	4.1	5.1	2.9	3.0
Services 1/	3.7	3.1	2.7	4.5	3.5
Addendum:					
All items less mortgage costs 2/	2.9	4.8	5.9	4.6	3.7
Services less home finance 1/ 2/ 3/	3.5	2.5	2.8	6.7	3.2
Commodities less food, used cars, home purchase 3/	2.2	3.4	6.3	2.5	2.6
Gasoline and motor oil	-3.1	17.5	25.7	.1	3.3

1/ Not seasonally adjusted.
2/ 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.
3/ Confidential.

The sharp rise in food costs in September was largely attributable to fresh fruit and vegetable prices which dropped much less than seasonally, as in August, because of short supplies. Beef prices fell, for the first time since May, but this was more than offset by advances for pork and poultry.

The increase in apparel prices in September--the first month in which fall and winter clothing are priced--followed three months of (seasonally adjusted) declines. Gasoline and motor oil prices rose again in September, bringing the 3-month advance since June to the fastest rate since 1962.

Among durables, prices of 1972-model cars continued to rise on a seasonally adjusted basis, bringing the increase over the year to almost 4 per cent. The quality adjustment on 1973-model cars should affect October retail prices, but by much less than it affected wholesale prices; the impact will be spread over more than one month to reflect the proportion of 1973 models in retail auto sales, and the weight of new cars in the CPI is considerably less than in the WPI.

Agricultural developments. Prices received by farmers increased 1 per cent in the month ending October 15, led by cattle, milk, wheat, oranges, and cotton. Lower prices for hogs, eggs, lettuce, and potatoes were partly offsetting. October red meat and poultry production was unchanged from the previous month and both the beef and pork components were unchanged. In recent weeks, increases in cattle marketings have reduced liveweight prices about 5 per cent since mid-October, while hog prices have remained at about the October 15 level.

Wet weather in late October and early November has delayed harvests and increased prices of corn, soybeans, and cotton. Corn is deteriorating in some areas and cotton quality has been hurt. Corn and soybean prices are already above last year because of increased exports, but cotton prices are running 10 per cent lower because of an expected 30 per cent increase in production.

DOMESTIC FINANCIAL SITUATION

SELECTED DOMESTIC FINANCIAL DATA
(Dollar amounts in billions)

Indicator	Latest data: Period	Latest data: Level	Net change from: Month ago	Net change from: Three months ago	Net change from: Year ago
Monetary and credit aggregates			SAAR (per cent)		
Total reserves	October	33.8	16.2	8.1	9.5
Reserves available (RPD's)	October	31.0	3.9	8.3	8.4
Money supply					
M1	October	242.5	4.5	5.2	6.5
M2	October	505.2	8.1	8.2	10.2
M3	October	795.1	10.2	10.5	12.5
Time and savings deposits (Less CDs)	October	262.7	11.5	11.1	13.9
CDs (dollar change in billions)	October	40.7	0.4	2.6	8.0
Savings flows (S&Ls + MSBs)	October	289.9	12.4	14.6	16.8
Bank credit (end of month)	October	542.6	11.4	14.0	13.0
Market yields and stock prices			Percentage or index points		
Federal funds	wk. endg. Nov. 8	5.25	+.10	+.56	+.32
Treasury bill (90 day)	" Nov. 8	4.71	+.11	+.87	+.54
Commercial paper (90-119 day)	" Nov. 8	5.13	--	+.50	+.23
New utility issue Aaa	" Nov. 1	7.28	-.20	-.12	-.02
Municipal bonds (Bond Buyer)	1 day Nov. 9	5.10	-.06	-.30	-.09
FNMA auction yield	wk. endg. Nov. 13	7.71	-.01	.10	-.01
Dividends/price ratio (Common stocks)	" Nov. 8	2.74	-.06	-.10	-.55
NYSE index (12/31/65=50)	end of day Nov. 13	62.33	.50	2.29	11.48
Credit demands		Net change or gross offerings			
		Current month		Year to date	
		1972	1971	1972	1971
Business loans at commercial banks	October	2.2	0.3	11.5	6.7
Consumer instalment credit outstanding	September	1.3	1.1	9.9	5.0
Mortgage debt outst. (major holders)	September	4.9[e]	4.2	40.8[e]	29.9
Corporate bonds (public offerings)	September	1.9[e]	3.2	21.1[e]	29.4
Municipal long-term bonds (gross offerings)	September	1.7[e]	2.1	17.7[e]	18.9
Federally sponsored Agcy. (net borrowing)	October	0.4[e]	1.0	2.8[e]	0.8
U.S. Treasury (net cash borrowing)	November	5.3[e]	2.6	11.1[e]	16.3
Total of above credits		17.7	14.5	114.9	107.0

e - Estimated

DOMESTIC FINANCIAL SITUATION

The more favorable climate emerging in securities markets at the time of the last Committee meeting has continued, contributing to general--although relatively modest--interest rate declines. Recently, market rates generally have been 10-35 basis points below the 1972 highs reached, in most cases, during September and October. Much of the recent improvement in market atmosphere has, of course, reflected expectational factors--stemming from negotiations on Vietnam, the apparent resolve of the Administration to hold the line on spending (despite the failure of Congress to adopt a fixed expenditure ceiling), and evidence of slower growth in the monetary aggregates.

In short-term markets, increased demands for funds have, nevertheless, tended to blunt much of the downward pressure on rates resulting from the better market sentiment--although pressures from Federal borrowing have been less severe than anticipated. Several types of private borrowing--including business loans at banks, consumer credit, and commercial paper issued by non-financial corporations--showed sizable increases in October, and in the case of business loans increased further in early November. The decision to defer retroactive revenue-sharing payments until early December reduced the size of the November Treasury refinancing, and the announcement of Treasury plans to meet its large December-January cash requirements through a combination of relatively routine bill and note financings also helped to calm market expectations.

In bond markets, demands for funds have continued to moderate, and rate declines generally have been more pronounced than in short-term markets. Improved tax receipts and the prospect of added near-term flows from revenue-sharing payments account for the more moderate State and local government borrowing demands, while expanding flows of internal funds and greater reliance on alternative forms of external financing explain the continued moderation of business demands.

Mortgage markets also appear to have been under less pressure recently, as inflows of funds to thrift institutions have remained large. In addition, with other institutional lenders seeking outlets for long-term funds--at a time when yields on bonds have been easing off and mortgage demands have been slackening seasonally--some speculative warehousing of mortgages has reportedly reappeared among mortgage bankers.

Outlook. During the remainder of 1972 the weight of borrowing in short-term markets seems likely to lead to some updrift in short-term rates. Business loan demands at banks and possibly also in the commercial paper market should remain strong, as the recent acceleration of inventory accumulation continues. Most forecasters see consumer loan growth continuing large. And Federal net cash borrowing from mid-November through the end of January is expected to total about $7-1/2 billion. However, a partial offset to short-term market demand pressures will be provided by State and local government investment of some of the proceeds of $5 billion in revenue sharing funds paid out in early December and early January.

In accommodating these sizable credit demands, banks will likely continue to be aggressive issuers of large negotiable CD's and can be expected to hold back on acquisitions of securities. Inflows of other time and savings deposits may continue moderately favorable, but tax and loan accounts are likely to decline substantially by early winter as the Treasury seeks to squeeze through its period of peak deficit. Some of the drop in tax and loan balances, of course, might be offset by a more rapid expansion of private demand deposits.

So long as short-term rates experience no more than a modest rise into early 1973, prospective supply-demand relationships in long-term markets suggest that continued stability and possibly further declines of long-term rates can be expected. However, any marked rise in short-term rates that seemed likely to be sustained would soon be reflected in long rates as well.

Only in the State and local government sector of bond markets have rates recently tended to rise, and these adjustments followed a period of several weeks of decline. Sizable additions to the December bond calendar, at a time when market professionals held large secondary inventories of other issues, explain the recent market weakening. But the longer-run outlook is for moderate offerings of new State and local government issues, partly because the $5 billion of revenue sharing payments will cover some portion of future State and local government outlays. In the corporate bond market, there is little reason to expect much change in the factors accounting for the recent moderation of new issue volume, although some borrowers have reportedly begun to add to the calendar for January when institutional investment flows typically show a seasonal expansion.

Rates in the primary mortgage market, where demands for funds continue large, seem unlikely to move up in the financial environment contemplated. Indeed, there could be some further decline in secondary market rates, especially if corporate bond prices experience a turn of the year rally as they often do.

Monetary aggregates. Data now available from the demand deposit ownership survey[1/] for the third quarter of 1972 suggest that a significant proportion of the growth of M_1 in that period was accounted for by increased holdings of demand balances by nonfinancial businesses. As can be seen in the table, gross demand deposits of these businesses are estimated to have increased considerably more in the third quarter of 1972 than in comparable periods of the previous two years. An increased demand for transaction balances by such firms is to be expected during a period of rapid economic expansion and there also have been reports that banks--in line with the expanding utilization of credit lines--have been pressing corporate borrowers for higher compensating balances.

Consumers also increased their holdings of demand balances over the third quarter more than in the third quarters of 1970 and 1971--with most of the strength at smaller banks. However, holdings of financial businesses and foreign depositors showed little change.

1/ The demand deposit ownership survey collects sample data for gross demand deposits (i.e., before deductions for cash items in the process of collection) only for individuals, partnerships and corporations. Insufficient data have been collected to seasonally adjust the ownership series. The lack of seasonal adjustment, the collection of data only for deposits owned directly by individuals, partnerships, and corporations (IPC), and the collection of data on a gross basis make it impossible to compare the survey results directly with the seasonally adjusted money supply, but the DDOS is helpful in giving insight concerning changes in M_1.

CHANGES IN GROSS IPC DEMAND DEPOSITS BY OWNERSHIP CATEGORY
AT ALL COMMERCIAL BANKS

(Billions of dollars, not seasonally adjusted)

Sector	Third quarters* 1970	1971	1972
Financial business	--	--	.1
Nonfinancial business	2.7	1.6	4.1
Consumers	2.4	1.5	2.6
Foreign	-.2	-.1	--
All other	.4	-.9	.5
Total	5.3	2.1	7.4

*Figures may not add to totals because of rounding.

In October, M_1 is estimated to have expanded at a 4.5 per cent seasonally adjusted annual rate. This increase was close to the 5.5 per cent pace registered in August and September, but sharply below that in July. Although October growth in M_1 was slightly slower than in September, M_2 grew at about the same rate, as time deposits other than large certificates of deposit continued to expand relatively rapidly. The incraase in consumer-type time and savings deposits appeared strong at both country and reserve city banks.

The increase in outstanding negotiable CD's (seasonally adjusted) was the smallest since March. In large part because of the substantial increase in Treasury deposits, banks did not need to rely as heavily on CD sales for funds. In general, offering rates on CD's edged downward during the month in unison with rates on competing financial assets in comparable maturity ranges.

MONETARY AGGREGATES

(Seasonally adjusted changes)

	1972					
	QI	QII	QIII	August	Sept.	Oct.p
		Per cent at annual rates				
M_1 (Currency plus private demand deposits)	9.3	5.3	8.5	5.5	5.5	4.5
M_2 (M_1 plus commercial bank time and savings deposits other than large CD's)	13.3	8.6	9.3	8.0	8.4	8.1
M_3 (M_2 plus savings deposits at mutual savings banks and S&L's)	15.5	10.8	11.6	10.7	10.4	10.2
Adjusted bank credit proxy	11.3	11.1	10.7	9.3	10.2	9.8
Time and savings deposits at commercial banks						
a. Total	14.8	15.7	13.2	13.9	13.7	12.0
b. Other than large CD's	17.1	11.8	10.1	9.9	11.6	11.5
		Billions of dollars 1/				
Memorandum:						
a. U.S. Government demand deposits	-.1	-.8	--	-.7	.7	.7
b. Negotiable CD's	-.1	3.7	3.2	1.2	1.0	.4
c. Nondeposit sources of funds	-.3	--	.3	.3	-.1	.2

p - Preliminary and partially estimated.

1/ Month-to-month and last-month-in-quarter to last-month-in-quarter changes in averages, not annualized.

The slower growth in demand and total time deposits in October was offset in part by a rise in the level of U.S. government deposits. Consequently, growth in the adjusted bank credit proxy was only marginally below that of September and the third quarter.

Bank credit. Total bank credit (seasonally adjusted, last Wednesday of the month series) expanded at a moderately higher rate in October than in September.[1/] Following a slow-down in September, total loans increased rapidly, while bank holdings of securities declined. Almost all loan categories showed strength during the month, with business loans and loans to nonbank financial institutions experiencing the largest increases; real estate and consumer loans continued to rise at close to the relatively high third quarter rates.

It should be noted that over the last five months, there have been large monthly fluctuations in the growth rate of business loans, suggesting that seasonal adjustment or other technical problems may be affecting the month-to-month changes. Hence, the underlying trend in business loans is probably better measured by the relatively strong 12 to 14 per cent average growth rate of recent months, than by the increase for any one month. This substantial growth in business loans in recent months is consistent with the increasing working capital needs of firms in an expanding economy. Indeed, in October the rise in business loans was accompanied by a sharp increase in dealer placed commercial paper, an increase only slightly less than the surge in June.

1/ After adjustment is made for a Federal Reserve matched sale-purchase transaction on the last Wednesday of September.

COMMERCIAL BANK CREDIT ADJUSTED FOR
LOANS SOLD TO AFFILIATES 1/

(Seasonally adjusted changes at annual percentage rates)

	1972					
	QI	QII	QIII	AUG.	SEPT.	OCT.
Total loans and investments 2/	15.7	9.5	13.6(13.0) 3/	18.3	11.9(10.1) 3/	11.4(13.2) 3/
U.S. Treasury securities	10.5	5.8	-7.6	-17.3	11.7	-40.6
Other securities	16.8	6.2	9.8	11.9	10.7	--
Total loans 2/	16.3	11.2	18.8(17.9) 3/	27.0	12.4(9.7) 3/	23.5(26.2) 3/
Business loans 2/	10.6	8.0 4/	12.4	24.4	5.7	21.0
Real estate loans	18.7	19.2	17.5	19.9	14.3	16.7
Consumer loans 5/	11.9	14.2	18.0	22.1	16.3	17.9

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.
3/ Adjusted to exclude an $800 million matched sale-purchase transaction by the Federal Reserve on the last Wednesday of September.
4/ Second quarter figures have been adjusted to exclude a reclassification of loans by a major New York City bank in June.
5 Data revised to conform with major revisions in Consumer Credit statistics.

In recent weeks, the increased business loan demand at banks appears to be broadly based geographically and across industry groups. However, at large banks in October, borrowing by public utilities and trade concerns seemed especially strong, after allowance for the usual seasonal factors.

Borrowings by finance companies and other nonbank financial institutions also were strong during the month. The increase in bank borrowing by nonbank financial institutions was associated in part with a large September sale of mortgages by GNMA to mortgage companies for delivery in October. In addition, it is reported that mortgage companies were increasing their inventory positions in speculation on future price rises.

Total holdings of securities declined in October, largely reflecting a sizable drop in holdings of Government securities. The decline in Governments was concentrated exclusively at large banks, while small banks increased their holdings. Smaller than usual net cash borrowing by the Treasury, together with the increasing loan demand, contributed to the net decline in acquisitions of Treasury securities at large banks. Bank holdings of other securities showed no net increase for the first time since June; an increase at large banks offset a decline at smaller banks--where bank loans and holdings of Treasury issues rose sharply.

Over-all liquidity positions of larger commercial banks still remained high. New York City weekly reporting banks maintained liquidity ratios near this year's peak levels, while the liquidity positions of other weekly reporting banks have been essentially unchanged since early in the year.

Short-term interest rates. A generally calm atmosphere has prevailed in short-term security markets since the October 17 FOMC meeting, and interest rates have edged slightly lower. In the market for U.S. Treasury bills, rates declined on balance from about 6 basis points in the 3-month maturity area to 22 basis points in the one-year area. Market professionals, observing the recent shift toward moderation in money supply growth, have apparently concluded that the Federal Reserve may not be under pressure to tighten for awhile. Announcement of the Treasury's decision to auction $2 billion of April tax bills November 17 for payment November 24, and $2.5 billion of June tax bills November 29 for payment on December 5, both with full tax and loan account credit, had been generally anticipated and exerted only a slight impact on bill rates.

Rates on private short-term securities also edged lower since the last Committee meeting. Commercial paper and commercial bank CD's in the 90 to 119 day maturity areas, for example, dropped about 1/8 of a percentage point, offsetting rate increases recorded during early October. With the drop in open market rates, two banks that follow a floating prime rate policy lowered their rates by 1/8 of a percentage point to 5-3/4 per cent, bringing them into line with rates charged by other major banks.

The generally improved outlook in securities markets ensured a highly successful mid-November Treasury refinancing. In this operation a single 6-1/4 per cent 4-year note was auctioned to redeem $1.3

billion of maturing issues and raise $1.7 billion of new money. Subscriptions to the offering exceeded $7 billion and the average rate was set at 6.20 per cent. Since then, the yield on the issue declined to 6.11 per cent in when-issued trading.

SELECTED SHORT-TERM INTEREST RATES
(Per cent)

	1972				Change
	Oct. 16	Oct. 30	Nov. 6	Nov. 13	Oct. 16-Nov. 13
Treasury bills					
3-month	4.80	4.74	4.68	4.74	-.06
6-month	5.13	5.14	4.99	5.08	-.05
1-year	5.40	5.36	5.14	5.18	-.22
Federal agency					
1-year	5.80	5.78	5.58	5.61	-.19
Commercial paper					
90-119 days	5.25	5.12	5.12	5.12	-.13
Large negotiable CD's 1/					
60-89 days	5.00	5.00	4.95	5.00	--
90-119 days	5.25	5.25	5.12	5.12	-.13
Bank prime rate - most prevalent	5.75	5.75	5.75	5.75	--
	Statement Week Ended				Change--week ending Oct. 18 to week ending Nov. 14
	Oct. 18	Nov. 1	Nov. 8	Nov. 14 2/	
Federal funds (daily average)	4.91	5.06	5.25	5.12	+.21

1/ Rate is for closest preceding Wednesday.
2/ Average for first 6 days of the week.

<u>Nonbank financial institutions.</u> According to sample data, the estimated annual rate of deposit growth at thrift institutions slowed during October to 12-1/2 per cent from the 15-1/2 per cent rate recorded in September and the third quarter as a whole. But net inflows to S&L's continued relatively strong by historical standards with high-yielding certificate accounts attracting the major portion of new funds. At the end of September, certificate accounts constituted nearly half of total savings capital, up from 44 per cent a year ago.

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
1972 - QI	14.3	23.4	20.5
QII	11.1	16.0	14.5
QIIIe	10.7	18.8	15.6
August p/	9.2	13.7	12.3
September p/	11.5	17.3	15.5
October e/	8.4	14.2	12.4

p/ Preliminary.
e/ Estimated on the basis of sample data.

Total sources of funds at insured S&L's reached a record third quarter volume this year. Nearly all of these funds were used to acquire mortgages, as shown in the following table.

SOURCES AND USES OF FUNDS AT INSURED SAVINGS AND LOAN ASSOCIATIONS
(Not seasonally adjusted, billions of dollars)

	Third quarter			
	1969	1970	1971	1972
Sources				
Deposit accounts, net 1/	- .2	2.8	5.2	7.3
Borrowed funds	1.5	.2	.5	.8
Subtotal	1.3	3.0	5.7	8.1
Gross mortgage repayments 2/	3.6	4.0	6.4	8.0
Other sources, net 3/	.3	.8	.4	.8
Total	5.2	7.8	12.5	16.9
Uses				
Net increase in liquid assets 4/	- .8	.6	- .7	.1
Gross mortgage acquisitions	6.0	7.2	13.2	16.8
Total	5.2	7.8	12.5	16.9
Memoranda				
Mortgage refinancings (included above in repayments)	.3	.5	1.2	1.3
Average ratio of outstanding mortgage commitments to recent cash flow 5/	1.12	.89	.99	1.00

1/ Net change in deposits, including interest credited.
2/ Includes, in addition to repayments, proceeds from sales of loans and participations and miscellaneous credits. Excludes interest, taxes, etc.
3/ Includes net changes in loans in process, reserves and surplus, and other liabilities minus the net changes in miscellaneous loans and assets not set out separately in the "uses" statement.
4/ Reflects all eligible liquid assets according to FHLB requirements. For 1968, includes only cash and U. S. Government securities. Since 1968, includes also Federal agency issues maturing within five years.
5/ Represents the average of the monthly ratios produced by dividing outstanding commitments plus loans in process by the sum of cash flow in the current month and previous two months.

<u>Mortgage market</u>. Net mortgage debt expanded at an estimated record seasonally adjusted annual rate of $66 billion in the third quarter, with savings and loan associations particularly large lenders. Residential mortgage debt formation rose to another record high, while formation of nonresidential mortgage debt showed little change. In addition to the larger number of dwelling units financed, a higher rate of loan refinancing as well as an increase in average loan amount have contributed to the rise in residential mortgage debt during recent quarters. According to FHLBB data, the average size of conventional home loans closed in the third quarter of 1972 was 5 per cent higher for new and 9 per cent higher for existing-home loans, as compared to the third quarter of last year.

Outstanding mortgage commitments on all types of properties, which normally indicate future trends in mortgage debt formation, rose further at savings and loan associations and at New York State mutual savings banks in September, reaching a record seasonally adjusted total of over $23 billion--7 per cent above the level at the end of the second quarter and 42 per cent above a year earlier. In addition to larger loan amounts, the rise in outstanding commitments at S&L's appears to reflect, in part, a further rise in their share of total mortgage lending.

Rates on home mortgages were virtually unchanged in October, according to HUD (FHA). In the primary market, the average rate on conventional first mortgages remained at 7.70 per cent for new-home loans, and 7.75 per cent for existing-home loans. In the secondary market for Government-underwritten new-home loans, the average yield edged up 1 basis point further to 7.57 per cent.

AVERAGE RATES AND YIELDS ON NEW-HOME MORTGAGES

	Primary market: conventional loans		Secondary market: FHA-insured loans		
	Level (per cent)	Spread (basis points)	Level (per cent)	Spread (basis points)	Discounts (points)
1971 - Low	7.55	-36	7.32	-27	2.5e
High	7.95	52	7.97	31	7.8
1972 - Low	7.55	15	7.45	5	3.7
High	7.70	39	7.56	28	4.7
July	7.65	27	7.54	16	4.4
Aug.	7.65	28	7.55	18	4.5
Sept.	7.70	30	7.56	16	4.6
Oct.	7.70	32	7.57	19	4.7

NOTE: FHA series: interest rates on conventional first mortgages (excluding additional initial fees and charges) are rounded by FHA 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 Aaa utility bonds.

e/ Estimated.

In the latest FNMA auction held on November 13, the average yield on the forward purchase commitments for FHA and VA underwritten home loans edged down 1 basis point to 7.71 per cent, the first decline since mid-August. In addition, bids received by FNMA dropped sharply further to the lowest amount in 5 months, reflecting a recent change in the outlook of mortgage companies from an expectation that mortgage prices would continue to decline to an anticipation of a rise in prices by year end.

Long-term security markets. Yields on long-term securities have declined from 6 to 20 basis points since the October Committee meeting, as apparent agreement on a Vietnam peace settlement sparked a rally. At the same time, favorable expectations on the future course of interest rates were being generated by relatively light forward calendars, the slowed growth of M_1, and an edging down of most short-term interest rates. Moderation of fears about rising interest rates stimulated acquisition of bonds by long-term investors and enabled corporate dealers, particularly, to lighten inventory positions that became heavy in late October. The improved market atmosphere also contributed to the relative ease with which the Treasury has been able to initiate borrowing to meet its fourth-quarter cash requirements.

SELECTED LONG-TERM INTEREST RATES
(Per cent)

	New Aaa 1/ utility bonds	Long-term 2/ State and local bonds	U. S. Gov't. (10-year constant maturity)
1971			
Low	7.02 (2/5)	4.97 (11/21)	5.42 (3/26)
High	8.26 (7/30)	6.23 (6/24)	6.89 (7/20)
1972			
Low	7.08 (3/10)	4.99 (1/14)	5.87 (1/14)
High	7.60 (4/21)	5.54 (4/14)	6/61 (9/28)
Week Ending:			
Oct. 6	7.44	5.22	6.53
13	7.48	5.16	6.49
20	7.30	5.23	6.48
27	7.34	5.13	6.43
Nov. 3	7.27	5.04	6.37 r
10	--	5.10	6.28 p

r/ Revised.
p/ Preliminary.
1/ FRB series.
2/ Bond Buyer (mixed qualities).

From mid-October to mid-November there was a decline of about 20 basis points in yields on high-grade utility bonds, while yields on long-term U. S. Government securities fell 15 to 20 basis points. Yields on municipal bonds declined only about 6 basis points, on balance, over the period as some back-up in tax-exempt yields occurred in response to the announcement on November 9 of a $1 billion increase in the 30-day visible supply. Current levels of yields on private long-term bonds are only about 20 basis points higher than their 1972 lows. However, yields on Treasury bonds are 40 basis points above their yearly low, reflecting the impact of significant debt lengthening accomplished by the Treasury since mid-year.

The stock market began to rally in mid-October, apparently on the basis of the Vietnam peace reports. During the first two weeks of November, the rise in equity prices on the major exchanges continued, with the Dow-Jones Industrial Index showing a particularly strong gain. Most major indices are now at or near all-time highs. Volume on the major exchanges has surged recently, with the NYSE averaging over 21 million shares for the first 9 business days of November.

RECENT CHANGES IN STOCK PRICES

	Level of prices as of:			Per cent change from:	
	Oct. 16	Oct. 30	Nov. 14	Oct. 16 to Nov. 14	Oct. 30 to Nov. 14
D-J Ind.	921.66	946.42	1,003.16	8.8	6.0
NYSE	58.49	61.12	62.94	7.6	3.0
AMEX	25.69	25.87	26.11	1.6	.9
NASDAQ	125.87	129.46	132.90	5.6	2.7

The forward calendar for new corporate securities continues to indicate a greater-than-seasonal decline in public bond offerings in the fourth quarter. October volume, which was swelled by several large finance company issues, was about $1.7 billion. With the continued lack of filings by industrial corporations and the relatively small volume of utility debt offerings, the staff estimates that November volume will be about $850 million and the December total, $1 billion. Takedowns of private placements are projected at a monthly average of over $700 million. Insurance companies and other institutional investors are reported to be still actively seeking private placements. New equity issues, while expected to decline somewhat, especially around the year-end holiday season, will probably remain close to the $1 billion monthly average.

CORPORATE AND MUNICIPAL LONG-TERM SECURITY OFFERINGS
(Monthly or monthly averages, in millions of dollars)

	Year 1971	1st eight months	Sept.[e/]	Oct.[e/]	Nov.[e/]	Dec.[f/]
Corporate securities Total	3,758	3,411	2,750	3,500	2,400	2,500
Public bonds	2,065	1,664	850	1,650	850	1,000
Privately placed bonds	613	660	800	650	650	800
Stock	1,080	1,086	1,100	1,200	900	700
State and local Government securities	2,080	2,004	1,693	1,850	1,600	1,400

Although market participants were surprised by the sudden increase in schedulings of tax-exempt securities for late November and December, the staff estimates that total offerings of long-term debt by State and local governments, including these recent additions, will decline in the fourth quarter. Thus, monthly average volume may be significantly below the $2 billion level which has prevailed for almost 2 years. Commercial banks appear to have slackened the pace of their acquisitions recently, especially in the maturity range beyond 7 years. However, casualty companies continue to be a major purchaser in the long-term tax-exempt market, having experienced an unusually favorable cash flow this year.

Federal finance. In light of the Administration's recent statements that it intends to hold down fiscal year 1973 spending, the staff has revised downward its projection of outlays to $253.0 billion. This, combined with an upward revision of receipts to $226.5 billion, results in a revised deficit of $26.5 billion, a figure $4.0 billion below that shown in the October Greenbook.

Since the last Greenbook, a number of bills were enacted that increased estimated outlays. Among these are water pollution control ($700 million), and social security liberalization and medicare, HR-1 ($900 million). New legislation and developments in "uncontrollable" outlays would have raised estimated outlays to $258 billion, as shown in the table on the next page. However, we assume $4 billion of savings attributable to the Administration's efforts at controlling spending, and approximately $1 billion more as the result of the expected settlement of the Vietnam War.

Our estimate of receipts has been increased by about $2.0 billion since the October Greenbook largely as the result of the increase in social insurance tax rates incorporated in HR-1. On a calendar year basis, this tax rate increase amounts to $3.5 billion and, together with previously legislated increases effective January 1973, it will raise social insurance receipts by $10 billion (annual rate).

The staff is holding to its earlier projection of $6.5 billion in extra withholding for calendar year 1972, which together with the correction for previous underwithholding, results in an $8 billion year-to-year increase in refunds payable in the first two quarters of calendar 1973. However, since monthly withholding receipts for September and October have been lower than projected, there is the possibility of a moderate downward revision in these figures.

These changes in estimated receipts and expenditures resulted in rather substantial reductions in our projections of the high employment deficit--$4.3 billion for fiscal 1973 and $6.8 billion for calendar 1973. We are currently projecting a high employment deficit of $12.0 billion for fiscal 1973 and one of $8.3 billion for calendar 1973. For calendar year 1972 our estimate shows a deficit of $2.0 billion. A sharp move toward fiscal restraint is foreseen for the last two quarters of calendar 1973 with the budget going from a deficit of $16.1 billion (annual rate) in 1973 II to a surplus of $2.2 billion (annual rate) in 1973 IV. The following table indicates the major factors accounting for these shifts.

HIGH EMPLOYMENT BUDGET SUMMARY--NIA BASIS
(In billions of dollars at annual rates)

	1972		1973			
	III	IV	I	II	III	IV
High employment surplus before special programs shown below:	-4.3	-3.4	-4.5	2.4	2.6	6.9
Effect of 20% social security benefit increase and HR-1	--	-8.0	-8.6	-9.0	-11.3	-11.7
Effect of wage base increase to to $10,800 and rate increase to 5.85%	--	--	10.0	10.0	10.0	10.0
Net effect of overwithholding	6.5	5.5	-4.0	-13.5	3.0	3.0
Revenue sharing	--	-10.6	-10.6	-6.0	-6.0	-6.0
Total surplus/deficit(-)	2.2	-16.5	-17.7	-16.1	-1.7	2.2

BUDGET OUTLAYS FOR FISCAL YEAR 1973
(Billions of dollars)

Total outlays, January 1972 Budget		246.3
Changes due to enacted budget amendments		2.9
Defense supplemental for Vietnam speed-up	1.2	
Disaster relief, Hurricane Agnes	1.5	
Other	.2	
Changes due to Congressional action or inaction		6.3
Coal miner benefits	.9	
General revenue sharing, shift of fiscal 1972 request to fiscal 1973	2.3	
General revenue sharing above request	1.0	
Social Security benefit increase (20% vs. 5%)	4.1	
Social Security liberalization and medicare (HR-1)	-1.0	
Defense appropriations	-1.7	
Water pollution control	.7	
Other, net	.0	
Uncontrollable" outlays		2.5
Interest on debt	.5	
Public service grants, after allowance for Congressional ceiling of $2.5 billion	1.3	
Agriculture price supports	-.3	
Other, net (including delay in asset sales and reduced unemployment compensation)	1.0	
Total outlays, excluding Administration economies		258.0
Assumed Administration economies, etc.		-5.0
General revenue sharing, postponement of one payment until fiscal year 1974	-1.5	
Defense, Vietam settlement	-1.0	
Nondefense purchases	-1.0	
Grants	-1.5	
Total outlays, current staff estimate		253.0

The end-of-October Treasury cash balance was $8.0 billion. On November 10, the Treasury announced the sale of $4.5 billion of tax anticipation bills, as mentioned previously. In addition, a $2 billion two-year note issue is expected to be auctioned in late December, and additions to the weekly bill auctions are projected to be continued. Borrowing in the first quarter of calendar 1973 is still expected to be large for that period of the year. Our current first quarter estimate is $9.0 billion.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	Oct.	Nov.	Dec.	Jan.
Total net borrowing	3.0	5.3	2.1	3.0
Weekly and monthly bills	1.2	1.1	0.8	1.0
Tax bills	--	2.0	2.5	--
Coupon issues	2.0	3.0	--	--
As yet unspecified new borrowing	--	--	--	2.0
Special issues to foreigners	-.6	--	--	--
Agency transactions, debt repayment, etc.	.4	-.8	-1.2	--
Plus: Other net financial sources a/	1.5	-.9	-1.0	1.6
Plus: Budget surplus or deficit (-)	-6.3	-3.6	-2.9	-5.4
Equals: Change in cash balance	-1.8 b/	0.8	-1.8	-0.8
Memoranda: Level of cash balance end of period	8.0 b/	8.8	7.0	6.2
Derivation of budget surplus or deficit:				
Budget receipts	14.2	17.6	18.8	19.1
Budget outlays	20.5	21.2	21.7	24.5
Maturing coupon issues held by public c/	--	1.3	1.2	--
Net borrowing by gov't-sponsored agencies	0.4	0.4	0.4	0.3

a/ Checks issued less checks paid and other accrual items.
b/ Actual
c/ In the August prefunding, $.9 billion and $1.1 billion, respectively, were exchanged for the November and December maturities, leaving $1.3 billion and $1.2 billion to be redeemed in cash.

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

	Fiscal Year 1972*	Fiscal Year 1973 Adm. 1/ Estimate	Fiscal Year 1973 F.R. Board	Calendar Years F.R. Estimates 1972	Calendar Years F.R. Estimates 1973	F.R.B. Staff Estimates Calendar Quarters 1972 III*	1972 IV	1973 I	1973 II	1973 III	1973 IV
Federal Budget						Unadjusted data					
Surplus/deficit	-23.2	-25.0	-26.5	-19.8	-21.9	-2.0	-12.8	-13.3	1.7	-1.5	-8.8
Receipts	208.6	225.0	226.5	221.7	244.5	55.6	50.6	52.6	67.7	65.5	58.7
Outlays	231.9	250.0	253.0	241.4	266.4	57.6	63.4	65.9	66.0	67.0	67.5
Means of financing:											
Net borrowing from the public	19.4	n.a.	21.9	13.3	18.0	5.0	10.4	9.0	-2.5	2.0	9.5
Decrease in cash operating balance	-1.3	n.a.	3.6	4.3	0.5	0.3	2.8	1.3	-0.8	--	--
Other 2/	5.1	n.a.	1.0	2.2	3.4	-3.3	-.4	3.0	1.6	-.5	-.7
Cash operating balance, end of period	10.1	n.a.	6.5	7.0	6.5	9.8	7.0	5.7	6.5	6.5	6.5
Memo: Net agency borrowing 3/	4.7	n.a.	n.e.	3.5	n.e.	0.7	1.2	0.9	n.e.	n.e.	n.e.
National Income Sector						Seasonally adjusted, annual rates					
Surplus/deficit	-22.1	n.a.	-27.0	-19.9	-23.4	-12.9	-30.1	-33.0	-32.0	-15.8	-12.8
Receipts	211.0	n.a.	234.9	228.1	247.5	230.2	235.8	239.5	234.1	255.6	260.8
Expenditures	233.1	n.a.	261.9	248.0	270.9	243.1	265.9	272.5	266.1	271.4	273.6
High employment surplus/deficit (NIA basis) 4/	4.1	n.a.	-12.0	-2.0	-8.3	2.2	-16.5	-17.7	-16.1	-1.7	2.2

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

1/ Revised Administration estimates were disclosed by Secretary Shultz in testimony before the House Ways and Means Committee on September 18, 1972.

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

3/ 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.

4/ Estimated by F.R. Board Staff.

INTERNATIONAL DEVELOPMENTS

11/15/72

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

	1971	1972p/			
	Year	QI	QII	QIII	Sept.*
Goods and services, net 1/	726	-1,188	-1,561	-1,100	
Trade balance 2/	-2,689	-1,687	-1,943	-1,668	-560
Exports 2/	42,770	11,791	11,445	12,272	4,133
Imports 2/	-45,459	-13,478	-13,388	-13,940	-4,693
Service balance	3,416	499	382	568	
Remittances and pensions	-1,530	-389	-377		
Govt. grants & capital, net	-4,422	-944	-652		
U.S. private capital (- = outflow)	-9,782	-3,240	-290		
Direct investment abroad	-4,765	-1,266	-200		
Foreign securities	-909	-393	-344	242	44
Bank-reported claims -- liquid	-566	-533	312	-449	398
" " " other	-2,372	-765	114	-705	-108
Nonbank-reported claims -- liquid	-506	-159	-93	e/-99	
" " " other	-664	-124	-79		
Foreign capital (excl. reserve trans.)	-4,551	1,484	2,773		
Direct investment in U.S.	-68	-360	346		
U.S. corporate stocks	849	695	164	374	172
New U.S. direct investment issues	1,161	296	747	352	
Other U.S. securities (excl. U.S. Govt.)	272	76	29	-71	
Liquid liabilities to:	-6,691	551	1,178	410	764
Commercial banks abroad	-6,908	476	968	294	643
Of which liab. to branches 3/	(-4,942)	(-199)	(399)	(34)	(277)
Other private foreigners	-465	53	280	150	202
Intl. & regional institutions	682	22	-70	-34	-81
Other nonliquid liabilities	-74	226	309		
Liab. to foreign official reserve agencies	27,417	2,827	1,081	4,724	-533
U.S. monetary reserves (increase, -)	3,065	607	-53	122	-93
Gold stock	866	544	--	3	1
Special drawing rights 4/	468	--	7	--	--
IMF gold tranche	1,350	-1	185	-15	-5
Convertible currencies	381	64	-245	134	-89
Errors and omissions	-10,927	829	-935		
BALANCES (deficit -) 4/					
Official settlements, S.A.		-3,434	-1,028	-4,846	
" " , N.S.A.	-30,482	-3,221	-749	-5,574	626
Net liquidity, S.A.		-3,293	-2,425	e/-4,708	
" " , N.S.A.	-22,719	-3,062	-3,062	e/-5,337	
Liquidity, S.A. 5/		-3,985	-2,206	-5,256	
" N.S.A.	-23,791	-3,810	-2,924	-5,809	-138

* Monthly, only exports and imports are seasonally adjusted. e/ Estimate.
1/ Equals "net exports" in the GNP, except for latest revisions.
2/ Balance of payments basis which differs a little from Census basis.
3/ Not seasonally adjusted.
4/ Excludes allocations of SDRs as follows: $717 million on 1/1/71 and $710 million on 1/1/72.
5/ 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. The U.S. balance of payments was in deficit on official settlements by about $3/4 billion in the five weeks ended November 8. U.S. reserve liabilities to Japan have risen by much more than this amount, while reserve liabilities to other countries have declined on balance.

The outlook for the U.S. balance of payments in the remainder of 1972 is dependent on short-term flows associated with developements in exchange markets - and in particular in the market for the yen. In the absence of such flows, the customary seasonal reflows could be expected to hold down the deficit on official settlements.

The third quarter deficit on official settlements of $4.7 billion (seasonally adjusted) reflected outflows in July following the floating of the pound, but, for the 3 months August-October, it appears that the official settlements deficit was on the order of $1 billion (not seasonally adjusted). As in the spring, this result reflected a large underlying deficit, offset to a considerable extent by private capital flows, including further short-term inflows through banking channels and foreign purchases of U.S. stocks.

The trade deficit continued large through September. Imports of industrial materials were strong in the third quarter, reflecting accelerated domestic activity; however, lack of growth in most groups of finished goods imports may indicate some impact of last year's realignment of exchange rates. Export expansion in the third quarter was very strong and included growth in most major commodity categories.

Increased exports to Western Europe and Canada accounted for most of the expansion.

Revised projections of an inter-agency committee point to a reduction in the deficit on goods and services from about $4-3/4 billion this year to about half that amount next year. Essentially all of this improvement is expected on merchandise trade -- reflecting the effects of exchange rate realignment, as well as larger exports of argricultural commodities and aircraft (both of which will involve larger outflows of Government-related capital). Little improvement is expected in the service balance, since interest payments on a larger stock of foreign liquid dollar assets are likely to increase. Moreover, projected increased outflows of U.S. Government grants and credits and of private long-term capital (as direct investment increases from depressed levels) suggest that the basic balance -- current account plus government and private long-term capital -- will be little changed in 1973 from the $11-12 billion range expected this year.

This projection is based on the assumption of further recovery and expansion abroad. The OECD Secretariat projects strong growth in the major European industrial countries and in Japan through the end of next year, with some narrowing of margins of excess capacity.

Foreign exchange and Euro-dollar markets. During the past five weeks sterling and the Japanese yen have been the foci of attention in the exchange markets. Sterling declined by about 3 percent between October 11 and November 14, while the yen required massive intervention by the Bank of Japan to keep it from soaring above its ceiling rate.

Rates for continental European currencies declined slightly, on balance, and the Canadian dollar weakened in the first few days following the inconclusive Canadian Parliamentary elections on October 30.

Sterling began the period at around $2.42, eased moderately over the next week, then plunged precipitously from October 19 to October 27, reaching a low of $2.32 on the latter date. The stimulus for the selling of sterling appeared to be the threat of a power workers' strike and subsequent market rumors and press speculation that sterling would be re-pegged as low as $2.25, this against the background of an acceleration of Britain's wage-price inflation. The Bank of England did little to cushion the drop in the rate, selling only about $134 million in market intervention. In the last two days of October and in early November sterling staged a modest recovery, with the rate rising more than one full cent on November 6 when Prime Minister Heath proposed a stationary wage-price freeze to Parliament. The Bank of England purchased about $50 million as sterling rallied. In recent days the pound has fluctuated fairly narrowly around the $2.35 level.

The Bank of Japan purchased $18 billion in the five weeks ended November 14, bringing its total intervention purchases since sterling was floated to $4.8 billion. On October 20 Japan announced a five-point program to reduce its swollen trade surplus which included, <u>inter alia</u>, tariff cuts, import quota increases and proposed quantitative limits on exports by commodity by country. The announcement of these proposals had little effect on market expectations of an early yen appreciation, however, and Bank of Japan intervention continued in sizeable amounts. Forward yen quotes are currently at substantial premiums, with yen for delivery in April currently quoted at nearly 10 per cent above par.

Continental European currencies as a group have eased modestly over the period. The effects of higher interest rates in Europe have apparently been overshadowed by a general bullishness towards the dollar as a result of the movement towards a Vietnam settlement and the re-election of the President. The German Federal Bank sold $244 million between October 12 and November 8. Other continental central banks (probably excepting Italy) did not intervene in recent weeks, though the System continued its small daily purchases of Swiss and Belgian francs in order to effect swap repayments.

The Canadian dollar, which had been holding steady at around $1.0180, dropped by about 2/5 of one cent in the first few days after the Canadian elections with the Bank of Canada providing some $80 million in market support. In recent days the rate has stabilized around $1.0140 and the Bank of Canada has not done much in the market.

In the Euro-dollar market, the overnight rate has declined slightly over the past month. A rise in the Federal funds rate during this period has raised the differential favoring U.S. bank's borrowing of reserve-free overnight Euro-dollars to a current level of 1/2 per cent. However, overnight Euro-dollar borrowings subject to the 20 per cent reserve requirement are still about 60-70 basis points more costly

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

Average for month or week ending Wednesday	(1) Over-night Euro-$1/	(2) Federal Funds2/	(3) Differ-ential (1)-(2)(*)		(4) 1-month Euro-$ Deposit1/	30-59 day CD rate (Adj.)3/	Differ-ential (4)-(5)(*)	
1972 - May	3.79	4.27	-0.48	(0.47)	4.25	4.21	0.04	(1.10)
June	4.07	4.46	-0.37	(0.64)	4.82	4.50	0.32	(1.53)
July	5.20	4.55	0.65	(1.95)	5.34	4.72	0.62	(1.96)
Aug.	4.47	4.80	-0.33	(0.79)	5.18	4.73	0.45	(1.75)
Sept.	4.54	4.86	-0.33	(0.79)	5.15	4.96	0.19	(1.48)
Oct.	4.77	5.05	-0.28	(0.91)	5.10	5.10	0.00	(1.28)
Oct. 4	4.62	5.18	-0.56	(0.60)	5.01	5.07	-0.06	(1.19)
11	4.87	5.09	-0.22	(1.00)	5.16	5.13	0.03	(1.32)
18	4.89	4.91	-0.02	(1.20)	5.09	5.13	-0.04	(1.23)
25	4.57	5.01	-0.44	(0.70)	5.13	5.13	0.00	(1.28)
Nov. 1	4.71	5.06	-0.35	(0.83)	5.01	5.00	0.01	(1.26)
8	4.74	5.25	-0.51	(0.68)	5.04	5.00	0.04	(1.30)
15p	4.80	5.13	-0.33	(0.87)	4.95	5.00	-0.05	(1.19)

1/ All Euro-dollar rates are noon bid rates in the London market; overnight rate adjusted for technical factors to reflect the effective cost of funds to U.S. banks.
2/ Effective rate.
3/ Offer rates (median, as of Wednesday) on large denomination CD's by prime banks in New York City; CD rates adjusted for the cost of required serves.
*/ Differentials in parentheses are after adjustment of Euro-dollar rates for the 20 percent marginal reserve requirement (relevant to banks with borrowings in excess of their reserve-free bases).
p/ Preliminary

than Federal funds borrowings. The rates on Euro-dollar deposits of one-and three-month maturity have also softened slightly since mid-October, but approximately equal declines in CD rates of comparable maturity have kept the relative cost to U.S. banks of these potential sources of funds unchanged, with the reserve-free cost of one-month Euro-dollars equal to that for one-month CD's and the three-month Euro-dollar rate exceeding the three-month CD rate by about 2/3 per cent.

The daily average of U.S. banks' liabilities to their foreign branches has continued stable during the past month at a level slightly above the Regulation M reserve free base. Continuing the pattern of the previous month, liabilities of U.S. agencies and branches of _foreign banks_ to foreign commercial banks have risen further since mid-October, increasing by about $800 million in the four week period ended November 8.

Balance of payments. The U.S. payments deficit on official settlements showed a deficit in October and early November of about $3/4 billion -- roughly the size of the September surplus. For the three months August-October the deficit has been on the order of $1 billion (not seasonally adjusted) -- little changed from the rate of deficit that has obtained since early spring, apart from the extra-ordinary outflow in July following the decision of the United Kingdom to float the pound.

These relatively low rates of official settlements deficit in the face of a persisting large current account deficit reflect continued private capital inflows. Agencies and branches of foreign banks were increasing their outstanding foreign borrowings through early November. Foreign purchases of U.S. stocks amounted to $170 million in September and according to preliminary indicators continued large in October. An additional inflow in September was a reduction of $400 million in bank-reported claims on Canada -- probably in good part customers' claims.

U.S. foreign trade. In September the trade deficit was slightly larger than in August as exports slipped while imports were unchanged. For the third quarter the deficit was at an annual rate of $6-3/4 billion (balance of apyments basis), down from $7-3/4 billion in the second quarter but about the same level as in the first quarter Exports in the third quarter were about 7 percent higher than in the second quarter, all in volume as prices (unit-values) rose only marginally. Imports in the third quarter also increased but more moderately -- 4 percent -- with about a third of the increase accounted for by higher prices, principally in foods.

The trade deficit in the third quarter was still very high, with shifts in the commodity composition of trade indicating that an increasingly important element is the strong growth in domestic business activity. The bulk of the increase in imports from the second to the third quarter was in industrial materials -- particularly petroleum, but also in paper, steel and other metals and textiles. Almost all of the increase in imports of industrial materials represented higher volumes. The value of imports of foodstuffs also increased in the third quarter but this was largely because of higher prices for coffee, meat and fish.

In contrast to the upturn in these classes of imports, imports of finished goods -- capital equipment, automobiles and other durable consumer goods -- all fell or showed little change from the second to the third quarter, both in value and in real terms. Only in the non-durable consumer goods sector were imports higher. Of even greater significance is that in the third quarter imports of each of these classes of finished goods, again with the exception of nondurable consumer goods, was a decreasing portion of total domestic expenditure on thes types of goods. The absolute levels of imports of finished products are still very high by any past standard, perhaps in part because movements of these goods may still be affected to some degree by the disrupting effects of domestic strikes that occurred last year. The third quarter data, however, suggest that the exchange-rate changes of the Smithsonian Agreement may be beginning to slow the long-term rise in the ratio of imports to total domestic expenditures for such goods.

The steep rise in <u>exports</u> in the third quarter was broadly based across commodity categories and included increases in agricultural products, industrial materials, machinery, consumer goods, and automobile parts to Canada. Shipments of agricultural commodities accounted for about one-fourth of the total rise, reflecting not only heavier grain shipments to the Soviet Union but also larger exports of rice, hides and skins, and tobacco to other countries. Grain movements to Russia, however, have proceeded rather slowly because of transportation problems and movement of the $1-1/4 billion of grain and soybeans sold to that country is certain to accelerate in the coming months. Particularly encouraging in the pattern of exports in the third quarter was the steep rise in deliveries of machinery and a wide variety of nonagricultural industrial materials -- chemicals, steel, metals. Foreign orders for U.S. machinery are holding up well and the expectations of stronger economic activity abroad, particularly in Japan, should stimulate further advances in exports of these commodities. Exports of commercial aircraft slumped in the third quarter but a sharp pickup is expected in the current quarter as deliveries of the new DC-10's to foreign airlines begin and an increased number of jumbo jets are exported.

Exports to all major areas increased from the second to the third quarters with shipments to the Western European countries particularly strong. The rise in exports to Canada was virtually all in automotive equipment while the near doubling of exports to the Soviet Union resulted from the heavy movement of grains.

<u>The short-term outlook for economic activity in the major industrial countries</u>. Economic activity in all the major industrial countries has recovered this year from the generally slow pace in 1971. The growth of output is generally expected to continue next year -- in most cases at an accelerated rate. This past year private consumption expenditures, and, to a lesser extent, government expenditures, have been the main factors contributing to growth, but in 1973 private investment expenditures in most countries are expected to expand more rapidly and to become relatively more important.

This is the view expressed by the OECD Secretariat in a set of forecasts prepared in October for the recent Short-Term Forecasters' and Economic Policy Committee meetings. The Secretariat expects a rate of growth of real GNP for the seven major OECD countries[1/] of around 6-1/2 per cent through the end of 1973 -- compared to the long-run average rate of growth of about 5-1/2 per cent. It also expects that existing margins of excess capacity will be reduced, in some countries to the point where aggregate demand pressures may become a matter of policy concern before the end of next year.

Our own assessment of the outlook for economic activity in the major countries is in substantial agreement with that of

1/ Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.

the Secretariat on two points: (1) the cyclical upswing is generally expected to continue at least through next year, and (2) current rates of price increase are clearly too high in many countries and inflation may even become more of a problem next year. However, large margins of unemployed resources do exist in most countries. With the impact of fiscal policies expected to be somewhat less expansionary next year in any case, and with the Common Market countries (including the United Kingdom) presumably committed to slowing down rates of growth of monetary aggregates in those countries, it seems premature to suggest that further actions to restrict the growth of demand will soon be desirable.

For the major industrial countries other than Canada and the United States, the rate of growth of GNP forecast for 1973 is not significantly different from the average rate observed from 1958-59 to 1969-70. Moreover, because the current expansion follows an extended period of slow growth or recession, it is accompanied by historically high rates of productivity increase. Consequently, increases in unit labor costs are moderating in many countries, despite continued relatively high wage settlements in some cases. In Germany and the Netherlands, for example, unit labor costs have flattened out completely and are beginning to decline. In short, output expansion at this stage of the cycle tends to reduce costs rather than to increase them, at least in the short run.

Economic activity in Germany surged strongly in the first quarter of this year, reflecting partly exceptionally strong construction activity due to the mild weather, and partly a recovery from output levels which were depressed in late-1971 by international uncertainties and strikes. In the second quarter growth of output fell back, so that real GNP in the first half of 1972 as a whole increased at an annual rate of 5.7 per cent.

Real GNP is expected to grow more slowly in the second half of this year, and then to pick up somewhat in 1973 to a rate of a little more than 5 per cent. The pick-up next year is based on an assumption that business fixed investment will be stronger. Favorable export prospects, an improvement in company profits, and relatively high rates of capacity utilization for this stage of the cycle -- as well as recent business surveys -- suggest that the business climate is favorable. Inventories, which have been falling the last two years, are also expected to be built up to more normal levels as growth continues. Residential construction should remain buoyant, but will show slowing rates of growth due to the exceptionally large output in the first half of this year.

Both private consumption expenditures and net exports are expected to contribute about the same amount to real growth in 1973 as in 1972. Consumption should remain fairly strong, bolstered by an accelerated growth in earnings and transfers from the public sector; this will be offset only partially by a faster rise in prices. German exports may increase rapidly next year as Germany's export markets expand, but German imports will accelerate as well as the cycle progresses.

Consumer expenditures in the United Kingdom recovered strongly in the first half of this year. Fixed investment expenditures also showed some strength, with an upswing in private residential investment, especially, offsetting continued declines in investment expenditures by the manufacturing industry. This increase in demand, however, was reflected in only moderate growth of output, as inventories were run down significantly.

The outlook for activity in the United Kingdom is clouded by uncertainties over the effects of the wage/price freeze imposed by the Heath Government on November 6 (see Appendix A). However, recent surveys suggest that private investment expenditure by the manufacturing sector will turn up, despite the continued existence of considerable excess capacity. In addition, there is likely to be some rebuilding of inventories, given the historically low stock/output ratios, although it does seem that there has been a permanent shakeout of inventories (i.e., desired normal stock/output ratios may now be permanently lower than was previously the case).

Two big questions remain as a result of the freeze. (1) Will fixed investment and stockbuilding be sufficiently strong to sustain growth at something like the current 5 per cent annual rate in the face of somewhat slower growth of government expenditures and, perhaps, less buoyant consumer demand (as the freeze retards the growth of real income)? (2) How much, if at all, will the foreign sector contribute to the growth of aggregate demand next year?

The recovery in Japan which began around the turn of the year was fueled by a sharp recovery in private consumption and strong government investment. Both of these factors resulted in large part from the Supplementary Budget for FY 1971 (ending March 1972), which provided for a sizable increase in expenditure and a reduction in taxes. The strength of private consumption, in real terms, also reflected a slowdown in the rate of increase of prices while wages and employment rose more rapidly. Private fixed investment expenditures, with the exception of investment by the manufacturing industry, has also been strong. But stockbuilding was weak, and the foreign balance deteriorated significantly (in constant yen prices), so that the growth of real GNP has been limited in 1972 to about 9 per cent -- or moderately lower than pre-recession levels.

In 1973 real GNP is now expected to increase by about 11 per cent. This forecast has recently been revised upward in light of a Supplementary Budget for FY 1972 (ending March 1973) that was approved by the Cabinet on October 20. The strong advance in real consumption expenditures is not expected to continue, in spite of rapidly rising nominal disposable income and a possible fall in the saving ratio, largely because consumer prices may accelerate. Residential construction is assumed to remain very strong, although this assumption may be overly optimistic. Business investment may recover, but business confidence is depressed by considerable uncertainty concerning the trend of exports and the future course of public policies (an election is scheduled for December 10, following the dissolution of the Diet on November 13). Finally, both the trade and current account surpluses are expected to decline somewhat from the high 1972 levels, with exports forecast to rise, but with imports forecast to rise considerably more rapidly. The net contribution of the foreign sector to the growth of total demand will remain negative in 1973 (i.e., net exports in volume terms will become smaller) -- in marked contrast to 1971.

In Canada, output growth accelerated sharply in the second quarter of this year. The growth rate of real GNP has averaged about 7 per cent (annual rate) in the six quarters ending in mid-1972. The second-quarter acceleration reflected primarily a 10-1/2 per cent (annual rate) increase in consumer expenditures -- based, in turn, on a sharp rise in government transfer payments -- and a strengthening of the external sector.

Growth of real GNP is expected to continue next year at about the same rate as in 1972 -- a little over 6 per cent -- although forecasts both by the OECD Secretariat and by some Canadian observers suggest that growth may peak around mid-year. Consumer expenditures should remain strong, with only a gradual deceleration from current high rates of growth. Residential construction activity may decelerate, but only gradually. Business investment, particularly in machinery and equipment, should show considerable strength, and an increase in inventories from very low inventory/shipment levels is expected. Rising economic activity abroad -- especially in the United States -- should stimulate Canadian exports, but imports are also likely to grow rapidly. In spite of continued rapid output growth, unemployment is expected to remain a problem in 1973; the unemployment rate stood at 6.7 per cent in the third quarter of this year.

APPENDIX A: THE WAGE/PRICE FREEZE IN THE UNITED KINGDOM*

On November 6, Prime Minister Heath introduced into Parliament the Counter-Inflationary (Temporary Provisions) Bill, which provides that essentially all prices, wages, rents, and dividends are to be frozen as of November 6. The freeze initially will last 90 days from the date on which the Bill is passed and receives Royal Assent. Since passage is expected to take several weeks, at least, the freeze will last roughly 4 months, and can be extended a further 60 days. That is, it could last until May of next year.

Some of the details of the "Phase I" freeze, based on a white paper entitled "A Programme for Controlling Inflation", are as follows:

A. Prices. The standstill applies to prices and charges for goods and services supplied to the home market by either the private or the public sector. Increases announced, but not implemented, prior to November 6 are not allowed. Enterprises that believe their costs (either import costs or domestic costs) have risen so much that they cannot be absorbed may request an exemption; exemption will ordinarily be granted only in cases where raw materials or raw agricultural produce account for a high proportion of total costs.

Wholesalers and retailers are expected to do everything possible to avoid any increases in prices; in particular they should not increase their cash margins during the freeze.

Certain prices -- especially those for fresh food such as fruit, vegetables, meat and fish and for imported raw materials -- are subject to fluctuations arising from external or seasonal causes. When such prices rise, enterprises handling these products without applying any manufacturing process to them may raise their prices by the same amount. When there are price reductions, enterprises will be expected to pass them on in full.

B. Employment Incomes. The standstill applies to all increases in pay and to other improvements in the terms and conditions of employment (e.g., hours and holidays). The term "pay" covers all

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rates of pay, including, in addition to the basic rate, rates of pay for overtime or weekend work, piece rates, and all allowances normally considered as pay. The standstill will not apply to increases in earnings resulting directly from extra effort or output under existing arrangements (e.g., increases in piece work earnings based on increased output), nor will it apply to individual pay increases resulting from genuine promotions.

In all cases where a settlement was reached before the freeze, and the operative date of increase was on or before November 6, the increase can be implemented. Otherwise, the operative date of such increases must be deferred until the standstill ends. Similarly, any increase resulting from negotiations or arbitrations which take place during the standstill must be deferred, and will be subject to the policy in force after the standstill.

The standstill will also apply to salaries and other forms of remuneration not determined by collective bargaining, as well as to charges and fees for services by self-employed persons.

C. Rents. Rents on private accommodations, as well as on business premises and land, are subject to the standstill provisions. Increases in rent which are already scheduled must be deferred until the end of the standstill.

D. Dividends. The standstill will apply to dividends declared by companies incorporated in the U.K. These companies will not be allowed to declare dividends in excess of the corresponding amount in the same calendar period a year ago.

E. Interest rates are not subject to the freeze.

F. Enforcement. The Government is relying on the public to notify them of violations. Fines will be imposed in cases where an individual or company fails to comply with a Government order to roll back prices, incomes, charges, or dividends or withholds information, and also where anyone acts to force an increase contrary to the provisions of the freeze. Orders can be given prohibiting the raising of dividends or rents.[1] Fines for breach of any order can be up to £400 on summary convictions, and up to an unspecified amount on conviction

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1/ Strictly speaking, one cannot be fined for raising prices or wages, but rather for refusing to roll them back upon request.

on indictment. Refusing to supply information, or giving false information, will carry a fine up to £100.

If unions strike against an order, they will be liable to fines as corporations, not as groups of individuals. (This provision is designed to avoid having to deal with "martyrs" as the Government did in conjunction with the Industrial Relations Act.) If individual workers are fined, the fines can be collected by "attachment of earnings" orders on their employers.

The freeze was imposed after the tripartite talks -- among the Government, the Confederation of British Industry, and the Trade Unions Congress -- broke down on November 2.

The tripartite talks, which were sought as a "more sensible way of settling our differences" in the wake of the miners' strike in February, began on July 18. On September 26, Prime Minister Heath put forward a proposal designed to sustain growth of real income, to improve the relative position of lower paid workers, and to restrain the rate of inflation. The main points of the proposal included a commitment to a 5 per cent rate of real growth, a 5 per cent limit on retail price increases, a £2 per week flat-rate pay increase, and threshold agreements.

The talks finally broke down at the beginning of November, partly because the unions were unhappy with a flat-rate increase in general, and a £2 limit in particular, and also because the unions were not prepared to adopt a voluntary wage policy unless there were stronger guarantees -- preferably statutory -- that price rises would not exceed the limits. The CBI, in turn, was not prepared to accept a statutory price policy and insisted that price rises -- even at the retail level -- would be restrained.

With the season of wage settlements approaching, with sterling floating, and with entry into the Common Market scheduled for January 1, some action to restrain wage and price inflation was clearly called for. This freeze, therefore, can properly be viewed as a means of buying time for a longer-term wage/price policy to be worked out. The Heath Government is still hopeful that the tripartite talks will continue -- despite the unions' insistence that they will not participate -- and that a workable "Phase II" program can be agreed upon in that forum. Otherwise, a statutory policy will be forthcoming. In either case, the expectation now is that the "Phase II" program will resemble the proposals Prime Minister Heath put forward in September.

In order to ease pressures during the period of the freeze, and to make the freeze more palatable to labor, several large[2] wage settlements were reached immediately prior to November 6, and the Prime Minister announced several measures, in conjunction with the freeze, that involve transfer payments to low-income persons (this is aimed at the second of the objectives of the Government's September proposal). The fact that the price freeze follows 15 months of self-imposed price restraint on the part of the CBI has raised some objections, but this is not expected to affect seriously the freeze.

2/ "Large" in the sense of number of workers involved; the amounts of the settlements were reasonably moderate, i.e., less than the 14-16 per cent of recent months, but more than the 8 per cent or so that the Government would like to see.