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Content last modified 6/05/2009.

Part II

CONFIDENTIAL (FR)

CURRENT ECONOMIC and FINANCIAL CONDITIONS

Prepared for the
Federal Open Market Committee

By the Staff
BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM

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of the Federal Reserve System

October 9, 1974

TABLE OF CONTENTS

DOMESTIC NONFINANCIAL SCENE

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

	Latest Data			Per Cent Change From		
	Period	Release Date	Data	Preceding Period	Three Periods Earlier	Year Earlier
				(At Annual Rates)		
Civilian labor force	Sept.	10/4/74	91.9	10.4	4.1	2.8
Unemployment rate (per cent)	Sept.	10/4/74	5.8	5.4 1/	5.2 1/	4.7 1/
Insured unemployment rate (%)	Sept.	10/4/74	3.4	3.3 1/	3.4 1/	2.6 1/
Nonfarm employment, payroll (mil.)	Sept.	10/4/74	77.1	.0	.2	1.6
Manufacturing	Sept.	10/4/74	19.9	1.4	-1.9	- .1
Nonmanufacturing	Sept.	10/4/74	57.3	.2	1.0	2.1
Private nonfarm:						
Average weekly hours (hours)	Sept.	10/4/74	36.8	36.6 1/	36.7 1/	37.2 1/
Hourly earnings ($)	Sept.	10/4/74	4.29	11.3	8.6	8.3
Manufacturing:						
Average weekly hours (hours)	Sept.	10/4/74	40.1	40.1 1/	40.1 1/	40.8 1/
Unit labor cost (1967=100)	Aug.	9/30/74	134.9	13.5	14.4	10.2
Industrial production (1967=100)	Aug.	9/13/74	125.2	-4.8	-1.6	-1.0
Consumer goods	Aug.	9/13/74	129.9	-2.8	.6	-1.0
Business equipment	Aug.	9/13/74	128.2	-20.2	-6.1	2.9
Defense & space equipment	Aug.	9/13/74	78.1	-68.1	-20.0	-2.0
Materials	Aug.	9/13/74	128.9	4.7	- .6	-1.5
Consumer prices (1967=100)	Aug.	9/20/74	150.0	16.0	12.3	11.2
Food	Aug.	9/20/74	161.7	17.3	5.5	9.0
Commodities except food	Aug.	9/20/74	140.3	18.2	16.9	13.1
Services 2/	Aug.	9/20/74	154.2	13.4	12.9	10.7
Wholesale prices (1967=100)	Aug.	9/12/74	167.1	46.4	33.0	17.8
Industrial commodities	Aug.	9/12/74	161.6	30.3	30.8	27.6
Farm products & foods & feeds	Aug.	9/12/74	183.0	90.2	39.9	- .6
Personal income ($ billion) 3/	Aug.	9/18/74	1165.2	6.9	10.6	9.1
				(Not at Annual Rates)		
Mfrs. new orders dur. goods ($ bil.)	Aug.	10/2/74	49.4	3.6	5.8	17.7
Capital goods industries:	Aug.	10/2/74	15.0	6.0	8.3	23.4
Nondefense	Aug.	10/2/74	11.8	-7.8	.0	14.8
Defense	Aug.	10/2/74	3.2	134.4	55.3	70.1
Inventories to sales ratio:						
Manufacturing	Aug.	10/2/74	1.63	1.63 1/	1.61 1/	1.59 1/
Ratio: Mfrs.' durable goods inventories to unfilled orders	Aug.	10/2/74	.678	.689 1/	.703 1/	.741 1/
Retail sales, total ($ bil.)	Aug.	10/8/74	46.8	.9	4.2	10.4
GAF	Aug.	10/8/74	11.8	-1.2	- .6	7.9
Auto sales, total (mil. units) 3/	Sept.	10/7/74	9.8	-10.6	6.0	-13.3
Domestic models	Sept.	10/7/74	8.1	-14.2	.4	-17.1
Foreign models	Sept.	10/7/74	1.7	11.2	43.4	9.9
Plant & equipment expen. ($ bil.) 4/						
All industries	1974	9/5/74	112.17	--	--	12.5
Manufacturing	1974	9/5/74	45.69	--	--	20.2
All industries	3Q '74	9/5/74	113.00	1.4	--	12.0
Manufacturing	3Q '74	9/5/74	46.21	2.0	--	19.1
All industries	4Q '74	9/5/74	116.16	2.8	--	12.0
Manufacturing	4Q '74	9/5/74	47.72	3.3	--	17.5
Housing starts, private (thous.) 3/	Aug.	9/18/74	1,126	-15.4	-23.5	-44.5
Leading indicators (1967=100)	Aug.	9/30/74	176.8	-1.2	.3	7.1

1/ Actual data. 2/ Not seasonally adjusted. 3/ At annual rate. 4/ Planned--Commerce

DOMESTIC NONFINANCIAL DEVELOPMENTS

Activity has continued sluggish in recent weeks with evidence of weakness becoming more widespread. Meanwhile price and wage pressures have continued intense and appear to be further eroding business and consumer confidence.

While data are still fragmentary, it seems likely that the industrial production index remained unchanged or increased only slightly in September following a .4 per cent decline in August. Preliminary data also indicate the third quarter average was unchanged from the second. Auto assemblies were 7.7 million units (annual rate) in September, down from the 7.9 million unit rate in August. Auto producers report assemblies are still hampered by parts shortages caused by strikes. Output continued to fall in other consumer durable goods and in construction materials.

Production of business equipment apparently recovered in September because of the settlement of a labor dispute. Output of materials apparently also rose further in September, benefiting from the continued strength of steel and the settlement of work stoppages in the copper and coal industries.

Staff estimates derived from weekly data suggest a drop of about one half per cent in total retail sales in September following the 0.9 per cent increase in August. The September decline reflected the weakening of auto sales; excluding autos and nonconsumer items, retail sales rose slightly. But, in real terms non-auto sales declined in August and probably in September.

Unit sales of domestic-type autos dropped to an 8.1 million annual rate in September, as sales were off sharply in the last 10 days. This compares with the 9.4 million rate in August and was approximately the same level as in last June and July. Sales of foreign autos also rose, reaching a 1.7 million unit annual rate in September, up from 1.6 in August and 1.2 in the second quarter. The recent relative strength in foreign auto sales probably reflects the temporary price advantage of foreign autos arising from the earlier introduction of higher priced 1975 models by domestic producers.

Although third quarter sales for domestic-type autos was significantly ahead of the second quarter, to a considerable extent the surge in sales appears to reflect consumer efforts to beat the large price increase announced for 1975 models, and the third quarter pace is not expected to be sustained.

The most recent consumer surveys by the Michigan Survey Research Center and the Conference Board suggest further reductions in discretionary consumer expenditures. On the basis of responses in late August and early September, the Michigan index of sentiment was substantially lower than in any previous cyclical downturn. There is now greater fear of a recession and less evidence of intentions to "buy in advance of expected price increases" than in the first half of 1974. The Conference Board survey, taken in late July and early August was also pessimistic, but somewhat less so than the later Michigan survey. Nevertheless, intentions to purchase homes and major appliances were at record lows.

Further substantial weakness in the labor market was indicated by recent data. The overall unemployment rate rose sharply to 5.8 per cent in September, up from 5.4 per cent in August, as a strong increase in the civilian labor force far outpaced a rise in total employment. Although unemployment rose most sharply in September among teenagers and adult women, the jobless rate also increased significantly for males 25 years and older and for heads of households. The trend in unemployment also supports the view that increased joblessness has not been limited primarily to teenagers; unemployment for all blue collar workers rose sharply in the past few months.

Nonfarm payroll employment continued virtually unchanged in September and was no higher than last May. Manufacturing and construction employment declined by more than 200,000 in this period, with offsetting increases in services and State and local government. Initial claims for insured unemployment continued to rise in September to a level about 50 per cent above a year earlier, portending further increases in the unemployment rates of experienced workers.

Total new orders for durable goods rose strongly--by 3.6 per cent--in August but excluding defense, the total was down slightly. In real terms, the August level of total new orders was slightly below the second quarter average and the level, excluding defense, was down sharply from the second quarter.

Recent data on business fixed investment suggest a smaller third quarter increase than expected earlier. Incoming data on shipments indicate reduced growth in the third quarter and expenditures for nonresidential construction show a sharp decline.

Orders for nondefense capital goods dropped sharply in August after recording a strong increase in July. Contracts (measured in square feet) for commercial and industrial buildings have recovered somewhat, although they still remain about 12 per cent below the July 1973 peak.

There continue to be reports that capital spending plans for 1975 and beyond are being reduced by many firms in response to rising costs, tight financial conditions and reduced demands; the electric utilities industry apparently is being particularly hard hit. But results of two private surveys of business capital spending intentions for 1975 (confidential) report increases for all industries of 10 per cent for Edie and 14 per cent for Rinfret, with outlays continuing strong in manufacturing, particularly for producers of nondurable goods. The Edie survey has had the substantially better track record of the two. Recent price rises for machinery, equipment, and structures suggest that percentage increases in outlays of this magnitude would mean little real gain for the year.

Although the rise in the book value of manufacturers' inventories was somewhat smaller in August than in July, limited data for the two months suggest that the third quarter book value increase will be larger than in the second quarter. But much of this additional inventory spending appears to be attributable to inflation, and on an

NIA basis inventory investment was probably smaller in the third quarter than in the second.

There are continuing reports that business firms are making increased efforts to prevent further inventory accumulation as demand slackens, delivery times shorten and shortages ease. Thus there are likely to be additional layoffs as firms cut production to trim excessive stocks, Nevertheless, there probably is planned inventory building still in progress. Attempts are being made to stock coal and other materials in anticipation of a strike by miners in mid-November, and there may be additional stockpiling in anticipation of further price increases.

Private housing starts dropped sharply again in August. Even if total starts show some rise in September, the third quarter average most likely will not be much above an annual rate of 1.2 million units--the lowest quarterly average in seven years, and somewhat below our estimate of last month. Although declines continue to be largest for multifamily units, starts of single family units have declined sharply since June.

The outlook appears bleak for avoiding some further deterioration of activity in this sector. Mortgage market conditions remain comparatively unfavorable to builders with interest rates for construction and permanent financing near or at recent peaks. Mortgage commitments at thrift institutions have deteriorated further. However, Government support programs should help to temper the situation over the period ahead, especially for single family units. Multifamily units under construction this summer were still relatively high, and at the end of July merchant builder stocks of unsold new single family homes equaled as much as 10 months' supply. Even if net depositary inflows at savings institutions improve over the next few months, many savings institutions will not be in a position to step up commitments significantly until they have reduced their borrowing and restored their liquidity.

Both consumer and wholesale prices in August recorded their sharpest advances in a year. Prices at retail for nonfood consumer commodities accelerated and retail food prices, which had declined moderately in July, rebounded at a rate greatly exceeding the second quarter rise. Meats contributed most to the rise in food prices but many other foods increased as well. Prices of consumer services continued to rise at an increasing rate under pressure from medical costs, utility charges and higher rates on mortgages. A fall in gasoline prices for the first time since last September was a moderating factor.

The outlook for an improvement in retail price performance has been dampened by the sharp jump in wholesale prices recorded in both July (3.7 per cent) and August (3.9 per cent). Price hikes at wholesale were especially sharp in these months for farm products and processed foods and feeds, which nearly reached the August 1973 peak. In addition to the advance in meat prices, the index of consumer prices in September will be affected by the sharp boost in 1975 model automobile prices.

However, there is some hope for easing of food prices in the months ahead; prices received by farmers declined 2 per cent in the month ending September 15, following a 3 per cent increase in August, and are now 7 per cent below the August 1973 peak. In addition, reduced worldwide demand is gradually bringing down prices of many basic industrial commodities. Scrap prices for both ferrous and nonferrous metals have declined and prices of refined copper have also fallen. Among nonmetals, lumber and plywood have dropped sharply and manmade fiber prices are weakening following earlier sharp drops in natural fibers.

Wage increases continued at a rapid pace in September as labor attempted to maintain purchasing power. The average hourly earnings index rose at an 11-1/2 per cent annual rate in the third quarter compared to about 7-1/2 per cent in the first half of 1974, with strong gains in both trade and manufacturing.

Recent consumer price increases have intensified pressures for large wage settlements in upcoming labor negotiations. Boeing recently reached an agreement with its 60,000 aerospace employees on a new three year contract which provides a 13 per cent immediate pay increase and 3 per cent additional in each succeeding year, plus a liberalized cost of living escalator and improvements in pensions and medical insurance. Agreements at five other major aerospace companies, involving 50,000 employees, are due to expire this month and next. Other major bargaining contracts are yet to be concluded this year; contracts expire in coal in mid-November and with the railroads at the end of December. The railroad contract involves 500,000 workers and announced wage demands are very large.

The miners are reportedly asking for very large wage increases but the most difficult points to negotiate seem to be nonwage issues such as improvements in mine safety that could adversely affect productivity, and improvements in pension and welfare funds. The outcome is uncertain, however, because the recent reorganization of the United Mine Workers permits the union rank and file to vote on the contract. If the miners strike the impact would be felt quickly by steel producers, who have low stocks of coal and coke, and by a number of utilities.

TABLE 1

RETAIL SALES
Per cent change from previous period

	1974					
	QIV to QI	QI to QII	QII to QIIIe	June	July	Aug.
Total sales	1.5	2.9	4.3	- .7	4.0	.9
Durable	-2.8	4.4	6.4	-1.7	6.5	2.3
Auto	-8.1	5.5	11.8	- .3	9.4	5.1
Furniture & appliance	4.2	3.7	.4	-3.5	4.7	-2.6
Nondurable	3.5	2.3	3.3	- .2	2.8	.2
Food	4.3	1.7	4.2	- .1	3.1	.9
General merchandise	3.8	2.0	.9	-1.4	1.2	- .6
Gasoline stations	3.9	8.8	5.0	3.3	.9	1.3
Total, less auto and nonconsumption items	3.6	2.6	3.0	- .6	2.8	.2
Real*	-2.1	.1	n.a.	-1.6	3.4	- .6

* Deflated by all commodities CPI, seasonally adjusted.

TABLE 2

SELECTED UNEMPLOYMENT RATES
(Per cent; seasonally adjusted)

	1973	1974			
	Sept.	March	June	Aug.	Sept.
Total	4.7	5.1	5.2	5.4	5.8
Males 20+	3.0	3.4	3.5	3.8	3.9
Females 20+	4.8	5.0	5.1	5.2	5.7
Teenagers	14.3	15.0	15.6	15.3	16.7
Household heads	2.7	3.0	3.1	3.1	3.4
Married men	2.1	2.4	2.6	2.6	2.8
Blue collar	5.1	6.1	6.2	6.5	6.8
White collar	2.9	2.8	3.1	3.1	3.5
White	4.2	4.6	4.8	4.8	5.3
Negro and other	9.2	9.4	8.8	9.2	9.8
State insured	2.6	3.4	3.4	3.3	3.4

TABLE 3

CHANGES IN PAYROLL EMPLOYMENT
(In thousands; seasonally adjusted)

	Employment (Sept. 1974)	Average monthly change			
		Aug. 1974- Sept. 1974	June 1974- Sept. 1974	Mar. 1974- Sept.1974	Sept.1973- Sept. 1974
Total nonfarm	77,146	33	15	57	99
Goods-producing	24,041	-22	-61	-32	-14
Construction	3,502	-50	-32	-37	-16
Manufacturing	19,864	23	-32	2	-2
Service-producing	53,105	55	76	89	113
Trade	16,651	-12	16	27	22
Services	13,442	11	26	34	37
State-local gov't.	11,512	45	27	24	39

TABLE 4

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

	1973	1974		
	QIV from QIII 1/	QI from QIV 1/	QII from QI 1/	August from July (p)
Durable goods, total	2.3	-1.6	9.5	3.6
Excluding defense	1.5	-1.9	10.2	- .3
Excluding primary metals & motor vehicles and parts	5.1	2.2	4.4	.9
Primary metals	.3	-3.4	32.3	14.0
Motor vehicles & parts	-7.2	-17.1	10.7	2.8
Household durables	4.2	1.1	4.8	-2.3
Nondefense capital goods	5.7	2.1	6.0	-7.8
Defense capital goods	22.4	5.7	-6.1	134.4
Construction & other durables	2.8	2.0	4.4	-3.3
Durable goods total, in 1967 $	.8	-4.9	3.2	.9
Nondefense capital goods, in 1967 $	4.1	.0	1.5	-11.1

1/ Changes between quarters are based on quarterly average levels.

TABLE 5

NEW HOUSING UNITS
(Seasonally adjusted annual rates, in millions of units)

	1974				Per cent change in August from:	
	QI	QII (r)	July (r)	Aug. (p)	Month ago	Year ago
Permits	1.34	1.17	1.02	.91	- 10	- 49
Starts	1.63	1.57	1.33	1.13	- 15	- 45
1-family	.94	.98	.95	.82	- 13	- 26
2- or more-family	.69	.59	.38	.30	- 21	- 67
Under construction 1/	1.56	1.48	1.45	n.a.	- 2 2/	- 15 2/
Completions	1.90	1.74	1.65	n.a.	- 11 2/	- 17 2/
MEMO:						
Mobile home shipments	.46	.44	.38	.37	- 3	- 32

1/ Seasonally adjusted, end of period.
2/ Per cent changes based on July.

TABLE 6
PRICE BEHAVIOR
(Percentage changes, seasonally adjusted annual rates)[1/]

CONSUMER PRICES

	Relative importance Dec. 1973	Dec. 1972 to Dec. 1973	Dec. 1973 to Mar. 1974	March to June 1974	June to July 1974	July to Aug. 1974
All items	100.0	8.8	14.2	10.9	9.1	16.0
Food	24.8	20.1	19.4	3.1	-4.5	17.3
Commodities less food	38.6	5.0	16.0	15.8	15.8	18.2
Services[2/]	36.5	6.2	9.2	11.0	12.7	13.4
Addendum						
All items less food and energy components[3/4/]	68.8	4.7	8.6	12.8	14.4	15.9
Petroleum products[3/5/]	4.0	23.4	99.3	26.6	6.9	-4.1
Gas and electricity	2.4	6.9	28.2	16.1	18.3	19.6

WHOLESALE PRICES

	Relative importance Dec. 1973	Dec. 1972 to Dec. 1973	Dec. 1973 to Mar. 1974	March to June 1974	June to July 1974	July to Aug. 1974
All commodities	100.0	15.5	24.5	12.2	44.6	46.4
Farm products and processed foods and feeds	31.69	26.9	10.8	-29.3	78.1	90.2
Industrial commodities	68.31	10.7	32.3	35.7	32.9	30.3
Materials, crude and intermediate	52.46	13.3	36.9	40.6	39.0	35.7
Finished Goods:						
Consumer foods	14.29	22.7	17.3	-16.7	43.7	38.5
Consumer excluding foods	17.63	7.4	28.3	25.3	21.7	15.3
Producer	8.50	5.3	13.2	27.2	25.1	33.1

1/ Not compounded for one-month changes.

2/ Not seasonally adjusted.

3/ Confidential--not for publication.

4/ Excludes food, gasoline and motor oil, fuel oil and coal, and gas and electricity.

5/ Includes coal.

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		September	37.3	7.2	8.1	9.3
Reserves available (RPD's)		September	35.3	6.0	8.1	9.3
Money supply						
M1		September	280.7	-.4	1.6	5.7
M2		September	602.9	1.4	4.5	8.3
M3		September	938.2	1.9	3.9	7.4
Time and savings deposits (Less CDs)		September	322.3	3.4	7.3	10.6
CDs (dollar change in billions)		September	86.0	1.3	2.7	19.3
Savings flows (S&Ls + MSBs)		September	335.3	3.2	2.6	5.9
Bank credit (end of month)		September	686.5	-8.8	4.5	9.9
Market yields and stock prices			Percentage or index points			
Federal funds	wk. endg.	10/2/74	11.04	-.60	-2.51	.32
Treasury bill (90 day)	"	10/2/74	6.53	-2.65	-.92	-.69
Commercial paper (90-119 day)	"	10/2/74	10.50	-1.44	-1.45	.87
New utility issue Aaa	"	10/4/74	10.61p	.30	.30	2.86
Municipal bonds (Bond Buyer)	1 day	10/3/74	6.68	-.20	.04	1.64
FNMA auction yield	FHA/VA	10/7/74	10.32	-.27	.67	1.21
Dividends/price ratio (Common stocks)	wk. endg.	9/30/74	5.50	.26	1.36	2.46
NYSE index (12/31/65=50)	end of day	10/1/74	33.39	-3.51	-7.87	-25.03

Credit demands		Net change or gross offerings: Current month 1974	Current month 1973	Year to date 1974	Year to date 1973
Business loans at commercial banks	September	.1	.3	24.2	25.2
Consumer instalment credit outstanding	August	1.5	1.9	8.5	14.9
Mortgage debt outst. (major holders)	July	3.7	5.4	29.5	38.7
Corporate bonds (public offerings)	September	1.0e	1.0	17.0e	8.6
Municipal long-term bonds (gross offerings)	September	1.6e	1.7	16.7e	17.3
Federally sponsored Agcy. (net borrowing)	September	2.6	2.3	11.2	13.1
U.S. Treasury (net cash borrowing)	October	2.3	1.4	3.7e	2.6
Total of above credits		12.8	14.0	110.8	120.4

e - Estimated

DOMESTIC FINANCIAL SITUATION

Short-term interest rates have fallen sharply since the September 11 meeting, as business demands for short-term funds have slackened and as the further decline in the Federal funds rate has fostered expectations of an easing of monetary restraint. Continued sluggishness of the monetary aggregates has strengthened this market sentiment.

The Federal funds rate has declined nearly 3/4 percentage point on a weekly average basis, and yields on most private money market instruments have fallen 1-1/2 to 2 percentage points. Short-dated Treasury bills have recorded even larger yield declines. Most large banks have lowered their prime lending rate from 12 to 11-3/4 per cent--the first general reduction in seven months.

In contrast, long-term rate movements have been mixed. Rates on new corporate issues have risen over 30 basis points to a new high but tax-exempt and Treasury yields have declined slightly. With non-bank thrift institutions remaining under pressure, residential mortgage markets have tightened further, and rates have reached record levels.

Monetary aggregates. Preliminary data indicate little change in the levels of the various money stock measures during September. M_1 may actually have declined slightly, with moderate growth of the currency component offsetting most of the shrinkage in private demand deposits. Between June and September, M_1 grew at an annual rate of only 1-1/2 per cent, as the public gradually adjusted its cash balances in response to the sharp advance in interest rates over the preceding months.

MONETARY AGGREGATES[1/]
(Seasonally adjusted changes)

	1974					
	QI	QII	QIIIp	July	Aug.	Sept. p
			Per cent at annual rates			
M_1 (Currency plus private demand deposits)	5.6	6.4	1.6	1.7	3.4	-.4
M_2 (M_1 plus commercial bank time and savings deposits other than large CD's)	9.0	7.7	4.5	5.4	6.6	1.4
M_3 (M_2 plus time and savings deposits at mutual savings banks and S&L's)	8.9	6.4	4.9	4.8	4.8	1.9
Adjusted bank credit proxy	8.5	20.9	6.4	9.4	5.4	4.2
Time and savings deposits at commercial banks						
a. Total	15.6	23.7	8.4	13.2	5.3	6.5
b. Other than large CD's	12.2	8.7	7.3	9.5	9.0	3.4
			(Billions of dollars)[2/]			
Memoranda:						
a. U. S. Government demand deposits	-.4	--	.7	-1.2	2.8	.4
b. Negotiable CD's	1.6	5.2	2.7	2.1	-.7	1.3
c. Nondeposit sources of funds	.4	.6	-.1	.9	-.7	-.4

1/ Staff estimates.
2/ Change in average levels month-to-month or average monthly change for the quarter, measured from last month in quarter to last month in quarter, not annualized.
p/ Preliminary

Although yields on most short-term market instruments have moved lower since July, they continue to exceed the rates payable on small denomination deposits. This is reflected in M_2 and M_3, which are estimated to have expanded at annual rates of 1-1/2 and 2 per cent, respectively, in September. During the month, commercial bank time and savings deposits other than large negotiable CD's expanded at the slowest rate since 1970, and most--if not all--of this expansion appears to have been in large denomination non-negotiable CD's. Deposits at nonbank thrift institutions showed a small seasonally adjusted increase, as quarterly interest crediting offset the continued large volume of deposit withdrawals.

With other deposit categories increasing little, banks purchased a sizable volume of funds--at declining interest rates--in the negotiable CD market. Use of nondeposit sources of funds declined slightly over the same period, as banks reduced their borrowing from foreign branches in response to the decline of domestic rates relative to Euro-dollar rates. On a monthly average basis, the adjusted credit proxy increased at a 4 per cent rate in September.

Bank credit and commercial paper. The slowing of bank liability growth in September was accompanied on the asset side by declines in both loans and investments, judging from figures for the last-Wednesday-of-the-month series. Measured on this basis, total bank credit fell $5.1 billion, seasonally adjusted, as holdings of

Treasury securities declined $3 billion and loans to securities dealers dropped $2.9 billion.[1/]

COMMERCIAL BANK CREDIT[1/]
(Seasonally adjusted changes at annual percentage rates)

	1974					
	QI	QII	QIII	July	Aug.	Sept.
Total loans and investments[2/]	15.9	11.5	4.5	13.1	9.4	- 8.8
U.S. Treasury securities	25.8	6.4	-37.8	-35.7	-15.2	-65.8
Other securities	6.8	9.1	.3	--	.9	--
Total loans[2/]	17.4	12.7	10.7	22.4	14.5	- 5.0
Business loans[2/]	22.2	23.0	13.1	19.7	18.7	.7
Real estate loans	12.2	12.2	6.7	7.6	7.6	4.7
Consumer loans	5.4	4.4	9.7	10.1	8.6	10.0
	(Average monthly change, billions of dollars)					
Memorandum:						
Security loans	- .1	- .1	--	2.2	.8	-2.9

1/ Last-Wednesday-of-month series except for June and December, which are adjusted to the last business day of the month.
2/ Includes outstanding amounts of loans reported as sold outright by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.

Particularly striking is the negligible growth of loans to businesses in September. Part of this weakness may be attributed to

1/ The decline in security loans was caused primarily by a reduction in the volume of Desk sale-purchase transactions outstanding on the last-Wednesdays of August and September. Security loans rise as dealers increase their borrowing to finance sale-purchase transactions with the Federal Reserve. Sale-purchase transactions outstanding on August 28 totaled $4.6 billion; on September 25, $1.0 billion.

the decline in commercial paper rates--especially after the mid-month tax date--which induced some borrowers to switch to the paper market. In addition, there is evidence that bank lending policies have become progressively more restrictive in recent months.[1/] However, the moderation of total short-term business credit expansion to a 7 per cent rate--as measured by the total of business loans and dealer-placed paper--suggests at least the possibility of a more fundamental change in business demand for credit related to reduced inventory accumulation and general economic slack. Borrowing at banks by wholesale and retail trade concerns and by housing-related industries was particularly weak in September. Among the few strong sectors were public utilities, which are having difficulty borrowing elsewhere, and machinery manufacturing. While some further retrenchment in aggregate short-term credit demands had been expected, the September figures may overstate the decline; in early October, business loans at New York City banks showed a much more than seasonal increase.

Bank borrowing by nonbank financial institutions declined moderately in September, but finance companies continued to borrow in

1/ A report on bank lending policies, based on recent Federal Reserve Bank staff conversations with commercial bankers, will appear in an Appendix to the Greenbook Supplement. Briefly, it was found that banks have tightened both their price and nonprice terms. Loans and lines of credit to established customers are being limited, and few new customers are being accommodated.

RATE SPREADS AND CHANGES IN BUSINESS LOANS AND COMMERCIAL PAPER
(Amounts in billions of dollars, seasonally adjusted monthly changes)

	Prime rate less 30-59 day commercial paper rate (per cent)	Business loans at all commercial banks 1/	Dealer placed commercial paper 2/	Total	Annual rate of change in total (per cent)
		Average monthly changes			
1974--QI	--	2.9	.4	3.3	23.7
QII	--	3.2	.1	3.3	22.1
QIII	--	1.9	.7	2.6	16.6
July	+ .04	2.9	.7	3.6	22.7
Aug.	+ .22	2.8	.3	3.1	19.2
Sept.	+ .53	.1	1.1e/	1.2e/	7.3e/
Weekly pattern:					
Sept. 4	+ .06				
11	+ .23				
18	+ .25				
25	+ .83				
Oct. 2	+1.28				

1/ Changes are based on last-Wednesday-of-month data and are adjusted for outstanding amounts of loans sold to affiliates.
2/ Measured from end-of-month to end-of-month.
e/ Partially estimated.

the commercial paper market. Total outstanding commercial paper of all issuers rose $1.6 billion, seasonally adjusted, in September, as highly-rated issuers found significant cost savings in the direct and dealer-placed markets as compared to commercial bank lending rates. However, lower-rated commercial paper issuers and firms with weak earnings reports did not benefit as much as prime borrowers from the market rally.

COMMERCIAL PAPER OUTSTANDING
(Seasonally adjusted, billions of dollars)1/

	Change in outstanding during: 1974					Outstanding Sept. 30, 1974 e
	August	Sept. e	QI	QII	QIII	
Total commercial paper outstanding	.9	1.6	3.0	.8	3.1	48.6
Bank-related	- .1	- .1	1.2	.9	- .1	6.8
Nonbank-related	1.1	1.7	1.8	-.1	3.2	41.8
Dealer	.3	1.1	1.3	.4	2.2	15.9
Direct	.8	.6	.6	-.5	1.1	25.9

1/ Seasonally adjusted figures are unavailable for bank-related paper. The unadjusted data for bank-related paper are combined with seasonally adjusted nonbank-related data to obtain the total for commercial paper outstanding.
e/ Estimated.
NOTE: Components may not add to totals due to rounding.

Real estate loans at commercial banks--which include many construction loans as well as long-term credit--weakened further, but consumer loan growth continued at about the same pace as in July and

August. The greater strength of consumer loans in the third quarter than in the first half of the year was due in large measure to increased sales of 1974-model autos.

<u>Short-term securities markets</u>. There has been a significant shift in money market psychology since the September meeting. Market participants have become more firmly convinced of a significant and lasting easing of monetary policy. The continued decline in the Federal funds rate, the weak incoming data on economic activity, the widespread calls at the economic summit meetings for lower interest rates, and the marked slowing of growth in the monetary aggregates began to alter the market view. Desk intervention points were tracked closely, and as the Desk's accepted Federal funds range was lowered further, a consensus developed that short-term rates had passed their cyclical highs. The decline in short-term rates was intensified when the supply pressures that had pushed Treasury bill rates upward in August were alleviated by Treasury redemptions and by purchases for foreign and domestic official accounts.

Rates on most private money market instruments have fallen much more than the 3/4 per cent drop registered by the Federal funds rate. Most recently, commercial paper rates have stood about 1-1/2 percentage points below their September 11 levels; large CD rates have declined over 2 points.

SELECTED SHORT-TERM INTEREST RATES

	August highs	Sept. FOMC (Sept. 11)	Sept. 17	Sept. 24	Oct. 1	Oct. 7
Federal Funds (weekly average)	12.23	11.48	11.41	11.12	11.04	10.75 1/
Treasury bills						
3-months	9.74	9.06	8.09	6.99	6.69	6.52
6-months	9.86	8.83	8.33	8.01	7.74	7.46
1-year	9.65	8.63	8.64	8.22	8.06	7.39
Commercial paper						
1-month	12.00	11.75	11.75	11.00	10.75	10.25
6-months	11.88	11.63	11.38	10.63	10.25	10.00
Large neg. CD's						
3-months	12.55	11.85	11.65	10.90	10.40	9.75
6-months	12.50	12.00	11.50	10.38	10.25	9.75
Federal agencies						
1-year	10.18	9.77	9.68	9.17	8.83	8.79 3/
Bank prime rate	12.00	12.00	12.00	12.00	12.00-11.75	11.75

1/ First 6 days of statement week ending October 9.
2/ Highest quoted new issues.
3/ As of October 3.

In the Treasury market, the greatest rate declines have occurred at the shortest end of the maturity spectrum. For example, the 3-month bill rate has fallen fully 2-1/2 percentage points, while the 6-month and 1-year bill rates have fallen 1-1/4 to 1-1/2 points.

Bill rates--especially short-dated bills--have been under special downward pressures. On the supply side, $1.5 billion of September TABs matured, and the Treasury allowed net pay-downs of $200 million in the weekly auctions on September 16 and 23. On the demand side, foreign official accounts have purchased $973 million (net) of bills through the Desk since September 12, while the System has acquired $411 million (net). Reflecting these influences, dealer bill positions have declined from $2.5 billion to about $1.0 billion since the September meeting. Noncompetitive tenders remain high, but they have tapered off with the decline in yields--from a peak of $1,011 million on September 12 to $672 million on October 3.

The Treasury added $200 million to the weekly bill auctions on October 7 and 11, and such additions may continue. Beyond this, immediate supply pressures appear to be confined to the possibility of a Federal Financing Bank issue. Larger Treasury borrowing needs will arise in early November, however. For the fourth quarter as a whole, it is estimated that the Treasury and Federal Financing Bank will borrow, net, about $6 billion. Borrowing by sponsored credit agencies is projected to continue at a high level in the near-term, with subsequent developments depending on interest rates and new government policies (particularly in the residential housing area).

PROJECTION OF FEDERAL BORROWING--MONTHLY
(In billions of dollars--not seasonally adjusted)

	Sept.e/	Oct.	Nov.	Dec.
Derivation of borrowing				
Budget surplus or deficit (-)	3.0	-6.5	-.7	-.8
Plus: Other sources a/	-.2	.9	-1.3	-.1
Less: Increase in cash balance	3.3 b/	-3.3	1.4	-.4
Total net Treasury borrowing	.5	2.3	3.4	.5
Weekly and monthly bills	2.0 c/	.8	.2	--
Tax bills	--	--	2.5	3.0
Coupon issues, net	--	--	--	--
As yet unspecified new borrowing	--	--	5.0	--
Federal Financing Bank	--	1.5	--	--
Debt repayment and other	-1.5	--	-4.3	-2.5
Memo items:				
Maturing coupon issues held by the public	1.8 d/	--	4.3	2.0
Net borrowing by government--sponsored agencies	2.6	1.6	.7	1.8
Level of cash balance, end of period	8.7 b/	5.4	6.8	6.4

e -- Estimated.
a/ Checks outstanding less checks paid and other accrual items.
b/ Actual.
c/ Sale of 299-day bills maturing June 30, 1975.
d/ Two-year notes totaling $2 billion were sold to refund the 6 per cent notes that matured on September 30, 1974.

Long-term securities markets. Despite the decline in short-term rates, corporate bond rates moved to new highs and the Treasury and tax-exempt bond markets staged only modest rallies. Investors apparently are reluctant to extend into longer maturity obligations in the current uncertain economic environment. This lack of confidence is nowhere more strikingly illustrated than in the equity markets, where share prices have traded recently at a 12 year low.

Prices in the Treasury coupon market came under some slight downward pressure in mid-September when, in the absence of inflows of Arab oil monies to special issues, the Treasury found it necessary to refinance $2.0 billion of maturing notes. In auctioning $2 billion of new 2-year notes, the Treasury set a minimum denomination of $10,000 in order to reduce the likelihood of disintermediation. In contrast to the August note auction when noncompetitive tenders accounted for 54 per cent of the notes sold to the public, only 20 per cent of the September notes went to noncompetitive tenders.[1/]

The volume of corporate securities marketed in September was much lower than expected. The decline in short-term rates led to some hesitance by borrowers who were hoping that long rates also would ease somewhat. These hopes may have faded as the build-up of massive forward

1/ In the September auction, the Treasury employed a new technique whereby bidding was on a yield basis and the coupon was set at the 1/8 point nearest to the average accepted bid that would result in a price at or below par. It was believed that this technique would prevent the sort of problem that arose in August when the coupons were set so high that large premiums developed in the bidding.

SELECTED LONG-TERM INTEREST RATES

		New Aaa utility bonds 1/	Recently offered Aaa utility bonds 1/	Long-term State and local bonds 2/	U. S. Government bonds (20-year constant maturity)
1970-73	High	9.43 (6/19/70)	9.20 (6/26/70)	7.12 (5/28/70)	7.80 (8/8/73)
	Low	6.99 (11/24/72)	7.15 (12/1/72)	4.96 (12/7/72)	5.74 (3/24/71) (11/22/72)
1974 -	High	10.61 (10/4)	10.47 (10/4)	6.95 (7/12)	8.68 (8/30)
	Low	8.05 (2/6)	8.13 (1/4)	5.16 (2/7)	7.40 (1/4)
Sept.	6	10.31	10.24	6.88	8.65
	13	10.27	10.30	6.79	8.60
	20	10.37	10.26	6.76	8.63
	27	10.46r	10.30r	6.72	8.53

1/ FRB series.
2/ Bond Buyer.
3/ Preliminary.
r/ Revised.

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

	1973	1974				
	Year	1st half e/	QIII f/	Sept f/	Oct. e/	Nov. e/
Corporate securities - Total	2,779	3,047	2,600	2,000	4,200	3,600
Public bonds	1,125	1,950	1,767	1,000	2,800	2,800
Privately placed bonds	725	543	467	600	400	400
Stock	929	555	367	400	1,000	400
State and local government securities	1,942	2,113	1,367	1,600	2,100	1,800

e/ Estimated.
f/ Forecast.

calendars for October and November resulted in a sharp increase in corporate rates. Public bond sales of $1.0 billion in September were the lightest since September 1973, but public offerings are expected to approximate $2.8 billion in both October and November. If realized, these would be the largest volumes since March 1971. In addition, public utilities will be issuing a large volume of common and preferred stock in October, mainly because the current financial structures of some utilities preclude the incurrence of additional debt.

Utilities, communications, and financial firms dominate the September and October bond calendars. Underwriters report that there is a heavy volume of potential long-term debt financing by manufacturers, but that these firms have sufficient flexibility to await more favorable market conditions. Should the bond markets rally, a sizable number of manufacturing issues might come to market in November and December.

The volume of municipal bond offerings is beginning to build up again from the low summer levels, and the October calendar includes a $475 million offering by New York City, the largest municipal issue in history. Relatively large proportions of new offerings are being sold to individual investors, as institutional demand in this market remains light.

<u>Nonbank thrift institutions and the mortgage market</u>. Deposit flows at nonbank thrift institutions appear to have improved slightly in September. FHLBB estimates indicate that deposit losses at S&L's (before interest crediting) were about $1.0 billion in September, compared to $1.2 billion in August. On a seasonally adjusted basis, including interest credited, S&L deposits are estimated to have grown at a 6.5 per cent annual rate.[1/] At mutual savings banks, September deposit losses were about equal to those in August, and the seasonally adjusted growth rate is estimated to have been only 1.0 per cent.

S&L's continued to borrow heavily from FHL Banks. FHL Bank advances outstanding rose $1.1 billion in September--the same as in August. Despite this Federal support, S&L mortgage commitment activity has continued to wane. New commitments in August were only 40 per cent of the recent high level in April, and outstanding commitments at the end of August were off 20 per cent from the spring high. Interest rates on new commitments for conventional home mortgages at sample S&L's rose about 30 basis points from the end of August to an average of 10.02 per cent on October 4--above usury ceilings in 34 states.

Direct and indirect support by the Federal and related credit agencies has been quite strong recently and promises to remain substantial in the period ahead. For FNMA and FHLMC alone, mortgage purchase commitments outstanding at the end of August exceeded $12.5 billion,

1/ This figure probably exaggerates the improvement in deposit flows, because the seasonal adjustment factor employed appears not to reflect adequately the volume of quarterly interest crediting.

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

	Mutual savings banks	Savings and loans associations	Both
1974 - QI	5.2	10.1	8.7
QII	1.9	5.3	4.3
QIII e/	0.0	3.5	2.5
July	-1.5	3.0	1.7
August p/	0.3	1.8	1.4
September e/	1.0	6.5	4.5

p/ Preliminary.
e/ Estimated.

CONVENTIONAL HOME MORTGAGES
AT 120 S&L's

	Average going rate on 80% loans (per cent)	Basis point change from month or week earlier	Spread 1/ (basis points)	Federal Home Loan Bank districts with funds in short supply
1973 - High	8.85 (9/28)	- -	107 (9/12)	12 (Aug. - Sept.)
Low	7.43 (1/26, 2/2, 2/9)	- -	-12 (8/8)	0 (Jan. - Mar.)
1974 - High	10.03 (9/27)	- -	41 (2/15)	12 (May, July-Oct.)
Low	8.40 (3/15, 3/22)	- -	-106 (7/12)	0 (Feb. - Mar.)
Sept. 6	9.88	+14	-43	12
13	9.92	+ 4	-35	12
20	10.00	+ 8	-37	12
27	10.03	+ 3	-43	12
Oct. 4	10.02	- 1	-59	12

1/ Average mortgage return before deducting servicing costs minus average yield on new issues of Aaa utility bonds paying interest semi-annually and with 5-year call protection. Mortgage yields shown may be converted to equivalents of semi-annual interest investments by adding 16 basis points to the gross yields between 8.59 and 8.85 per cent, and 17 basis points to yields above this level.

up more than 25 per cent from a year earlier. Increases in the maximum size of residential mortgages that may be bought by GNMA, FHLMC, and FNMA, authorized under recent legislation, should broaden the secondary market support by these agencies. However, offerings in the FNMA forward purchase commitment auctions have been light recently; the average yields on accepted bids have declined slightly in the last two auctions, apparently reflecting some limited optimism engendered by the lower level of short-term interest rates.

FNMA AUCTION RESULTS
HOME MORTGAGE COMMITMENTS

Date of auction	Government-underwritten Amount (In millions of dollars)			Conventional Amount (In millions of dollars)		
	Offered	Accepted	Average yield	Offered	Accepted	Average yield
1973 - High	551	289	9.37	171	88	9.68
Low	25	17	7.69	9	7	7.84
1974 - High	1155	333	10.59	164	63	10.71
Low	39	30	8.43	22	11	8.47
1974 - Sept. 9	176.1	98.6	10.59	46.5	30.9	10.71
23	57.2	38.2	10.56	22.1	19.0	10.66
Oct. 7	46.6	29.7	10.32	26.1	23.3	10.46

NOTES: Average secondary market yields are gross before deduction of the fee of 38 basis points paid for mortgage servicing. They reflect the average accepted bid yield for home mortgages assuming a prepayment period of 12 years for 30-year loans, without special adjustment for FNMA commitment fees and FNMA stock purchase and holding requirements on 4-month commitments. Mortgage amounts offered by bidders relate to total bid received.

Fiscal policy. The staff has projected outlays of $299.5 billion for fiscal year 1975--the same as in the September Greenbook. The specific spending and tax rate assumptions incorporated in the projection will differ to some degree from the Administration's proposals, which were unavailable at the time the projection was made.

PROJECTION OF FEDERAL BORROWING--MONTHLY
(In billions of dollars--not seasonally adjusted)

	Sept.[e/]	Oct.	Nov.	Dec.
Derivation of borrowing				
Budget surplus or deficit (-)	3.0	-6.5	-.9	-1.0
Plus: Other sources	-.2	.9	-1.3	-.1
Less: Increase in cash balance	3.3[a/]	-3.3	1.2	-.6
Total net Treasury borrowing	.5	2.3	3.4	.5
Weekly and monthly bills	2.0[b/]	.8	.2	--
Tax bills	--	--	2.5	3.0
Coupon issues, net	--	--	--	--
As yet unspecified new borrowing	--	--	5.0	--
Federal financing bank	--	1.5	--	--
Debt repayment and other	-1.5	--	-4.3	-2.5
Memo items:				
Maturing coupon issues held by the public	1.8	--	4.3	2.0
Level of cash balance, end of period	8.7[a/]	5.4	6.6	6.0
Net borrowing by government-sponsored agencies	2.6	1.6	.7	1.8

e--Estimated.
a/ Actual.
b/ Sale of 299-day bills maturing June 30, 1975.

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

	Fiscal Year 1974*	Fiscal 1975 e/ Adm. Est. 5-30-74	Fiscal 1975 e/ F.R. Board	Calendar Years 1973 Actual	Calendar Years 1974 FRB e/	F.R.B. Staff Estimates, Calendar Quarters 1974 I*	1974 II*	1974 III	1974 IV	1975 I	1975 II
Federal Budget											
Surplus/deficit	-3.5	-11.4	-7.2	-7.9	-8.1	-7.1	9.7	-2.3	-8.4	-6.4	9.8
Receipts	264.8	294.0	292.3	250.4	278.3	60.5	80.1	72.3	65.4	66.7	87.8
Outlays	268.3	305.4	299.5	258.3	286.4	67.6	70.4	74.6	73.8	73.1	78.0
Means of financing:											
Net borrowing from the public	3.0	n.a.	11.3	7.9	7.6	3.4	-6.4	4.4	6.2	3.7	-3.0
Decrease in cash operating balance	3.4	n.a.	--	.7	4.4	2.0	-.8	.5	2.7	1.7	-4.9
Other 1/	-2.9	n.a.	-4.0	-.7	-3.9	1.7	-2.5	-2.6	-.5	1.0	-1.9
Cash operating balance, end of period	9.2	n.a.	9.2	10.4	6.0	8.4	9.2	8.7	6.0	4.3	9.2
Memo: Sponsored agency borrowing 2/	14.8	n.a.	16.5	16.3	15.4	--	5.5	5.7	4.1	3.5	3.1
National Income Sector						Seasonally adjusted, annual rate					
Surplus/deficit	-4.7 p/	-12.8	-6.9 3/	-5.6	-2.6	-1.5	-1.3	-3.1	-4.4	-7.3	-10.5
Receipts	273.3 p/	304.3	304.6 3/	258.5	293.4	279.4	290.3	300.3	303.6	307.1	309.8
Expenditures	278.0 p/	317.1	311.5	264.2	296.0	281.0	291.6	303.4	308.0	314.4	320.3
High Employment surplus/deficit (NIA basis) 4/	-3.9	n.a.	8.8	-6.6	-1.3	-3.0	-3.5	-4.0	5.5	12.7	21.0

n.a. -- not available p -- preliminary * Actual e -- projected

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

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

3/ Quarterly average exceeds fiscal year total by $.6 billion for fiscal 1975 due to spreading of wage base effect over calendar year.

4/ Estimated by F.R. Board Staff.

INTERNATIONAL DEVELOPMENTS

CONFIDENTIAL (FR)

IV -- T - 1

10/9/74

U.S. Balance of Payments
(In millions of dollars; seasonally adjusted)

	1973	1974p/			
	YEAR	1Q	2Q	July*	Aug.*
Goods and services, net 1/	4,391	2,928	-122		
Trade balance 2/	471	-74	-1,631	-815	-1,275
Exports 2/	70,277	22,299	24,089	8,187	8,275
Imports 2/	-69,806	-22,373	-25,720	-9,002	-9,550
Service balance	3,920	3,002	1,509		
Remittances and pensions	-1,943	-390	-461		
Govt. grants & capital, net	-3,471	-1,218	-1,007		
U.S. private capital (- = outflow)	-14,101	-8,585	-9,528		
Direct investment abroad	-4,872	-627	-1,552		
Foreign securities	-807	-646	-357	-151	-128
Bank-reported claims -- liquid	-1,103	-2,239	-1,246	-195	-396
" " " other	-4,773	-2,958	-6,081	-1,085	-1,262
Nonbank-reported claims -- liquid	-841	-361	126	-102	
" " " other	-1,704	-1,754	-418		
Foreign capital (excl. reserve trans.)	12,444	7,118	4,610		
Direct investment in U.S.	2,537	1,281	1,516		
U.S. corporate stocks	2,758	376	10	-1	79
New U.S. direct investment issues	1,223	24	67		
Other U.S. securities (excl. U.S. Treas.)	69	287	320		
Liquid liabilities to:	4,436	4,630	2,821	1,990	2,882
Commercial banks abroad	2,978	4,616	1,977	1,688	2,642
Of which liab. to branches 3/	(309)	(3,379)	(-1,120)	(-495)	(2,830)
Other private foreigners	1,082	599	557	207	17
Intl. & regional organizations	376	-585	292	95	223
Other nonliquid liabilities	1,420	520	-123		
Liab. to foreign official reserve agencies	5,095	-852	4,887	1,078	-263
U.S. monetary reserves (increase, -)	209	-210	-358	25	-605
Gold stock	--	--	--	--	--
Special drawing rights	9	--	-29	-38	-8
IMF gold tranche	-33	-209	-244	-19	-385
Convertible currencies	233	-1	-85	82	-212
Errors and omissions	-2,624	1,209	1,979		
BALANCE (deficit -)					
Official settlements, S.A.		1,062	-4,529		
" " , N.S.A.	-5,304	1,495	-4,104	-1,103	868
Net liquidity, S.A.		-968	-6,229		
" " , N.S.A.	-7,796	-158	-6,609	-2,991	
Liquidity, S.A. 4/		-3,568	-7,349		
" , N.S.A.	-9,740	-2,900	-7,778	-3,093	-2,014
Basic balance, S.A.		1,786	-2,740		
" " , N.S.A.	-896	2,163	-2,692		

* Monthly, only exports and imports are seasonally adjusted.
1/ Equals "net exports" in the GNP, except for latest revisions.
2/ Balance of payments basis which differs a little from Census Basis.
3/ Not seasonally adjusted.
4/ Measures by changes in U.S. monetary reserves, allliabilities to foreign official reserve agencies and liquid liabilities to commercial banks and other foreigners.
5/ "Commercial banks abroad" includes "Other private foreigners."

Foreign exchange markets. The weighted average exchange value of the dollar rose in early September, but has since declined slightly each week. As of the first week in October, the weighted average value of the dollar was about 1 per cent below its level in mid-September, but still about 3-1/2 per cent above the low hit in May of this year. The decline in interest rates on U.S. dollar obligations, both here and in Euro-dollar markets, was a factor in the recent weakening of the dollar.

After large sales of dollars by Japan and Italy in early September, there was little further central bank intervention in dollars until the beginning of October. Since that time, there have been central bank sales of more than $450 million, primarily by the Bank of Italy, because of pressure on the lira associated with the fall of the government. On the opposite side of the market, the Bank of France has purchased more than $100 million and the System has purchased a substantial amount of dollars (against marks) thus far in October.

The Japanese yen strengthened in mid-September with the news that the Japanese had arranged to borrow more than $1 billion on a long-term basis from an Arab country. Since the beginning of October, the yen has weakened once again and is currently trading at its mid-September levels.

The French and Swiss francs advanced sharply in early October, as many banks covered their short positions in francs which materialized when Banca Privata in Italy was closed and it was unclear whether its forward contracts to deliver French and Swiss francs would be honored.

During the past month, the German mark has strengthened against the dollar, but has remained generally weak against currencies in the snake, requiring very substantial intervention, first against the Dutch guilder and more recently against the Norwegian krone. In the past few days, pressures in the snake have subsided as Dutch money market rates have fallen in response to central bank swap activities and Norway has officially denied any intentions to revalue.

Euro-dollar market. Rates on Euro-dollar deposits have continued to decline, largely in response to falling short-term rates in the United States and much-reduced demand by Japanese banks. Declines in Euro-dollar rates have been especially rapid during the past week. On October 9 the 3-month rate was 10.94 per cent, down about 2 percentage points from a month earlier, and the excess of that rate over the U.S. 60-89 day CD rate narrowed to less than one per cent on that date. Until the past few weeks the quoted overnight Euro-dollar rate tended to fall less rapidly than the Federal funds rate, and U.S. banks reduced their gross liabilities to foreign branches from an average of $3.7 billion in the week of September 4 to $2.8 billion in the week of October 2. However, sharp declines in the overnight Euro-dollar rate during the week of October 9 reduced the excess of their cost relative to the Federal funds rate to about the same level as four weeks before.

Since the end of August the cost of short-term Euro-dollar loans to prime nonbank borrowers has declined very sharply compared with the cost of bank loans in the United States, as seen in the attached table.

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

Average for month or week ending Wednesday	(1) Over-night Euro-$	(2) Federal Funds	(3) Differ-ential (1)-(2)(*)	(4) 3-month Euro-$ Deposit	(5) 60-89 day CD rate	(6) Differ-ential (4)-(5)(*)
1974-June	11.40	11.75	-0.35 (0.64)	12.04	11.08	0.96 (1.04)
July	12.18	12.88	-0.70 (0.36)	13.52	11.70	1.82 (1.98)
Aug.	11.29	12.01	-0.72 (0.26)	13.57	11.63	1.94 (2.11)
Sept.	11.07	11.34	-0.27 (0.69)	12.41	11.17	1.18 (1.35)
1974-Sept. 4	11.21	11.64	-0.43 (0.54)	13.73	11.63	2.10 (2.28)
11	11.14	11.48	-0.34 (0.63)	12.99	11.44	1.55 (1.69)
18	11.05	11.40	-0.35 (0.61)	12.18	11.25	0.93 (1.01)
25	10.80	11.12	-0.32 (0.62)	11.60	10.38	1.22 (1.33)
Oct. 2	11.35	11.04	0.31 (1.30)	12.03	10.13	1.90 (2.07)
9 p/	10.47	10.63	-0.16 (0.75)	11.64	10.13	1.51 (1.64)

*/ Differentials in parentheses are adjusted for the cost of required reserves.
p/ Preliminary

SELECTED EURO-DOLLAR AND U.S. COSTS FOR PRIME BORROWERS
(1974; Friday dates)

	Aug. 30	Sept. 13	Sept. 27	Oct. 9 d/
1) 3-mo. Euro-$ loan a/	14.63	13.13	13.00	11.69
2) 90-119 day com'l. paper b/	12.13	11.88	10.75	10.13
3) U.S. bank loan:				
a) predominant prime rate	12.00	12.00	12.00	12.00
b) with 15% comp. bal's. c/	14.12	14.12	14.12	14.12
c) with 20% comp. bal's. c/	15.00	15.00	15.00	15.00
Differentials:				
(1) - (2)	2.50	1.25	2.25	1.56
(1) - (3a)	2.63	1.13	1.00	-.31
(1) - (3b)	.51	-.99	-1.12	-2.43
(1) - (3c)	-.37	-1.87	-2.00	-3.31

a/ 3/4 per cent over deposit bid rate.
b/ offer rate plus 1/8 per cent.
c/ prime rate adjusted for compensating balances.
d/ Wednesday

The volume of outstanding Euro-dollar deposits, which had increased very rapidly until May, has since shown a small decline from May to August according to data on the London component of the market (35-40 per cent of the total). There are indications that the halt to expansion principally reflects a reduction in interbank deposits within the market and in lesser degree perhaps some slowing of the inflow of deposits from oil-exporting countries. Further slowing has also occurred in arrangements of medium-term-Euro-currency loans, which averaged only $1.65 billion per month in July-August compared with $3.3 billion a month in the first half of the year according to Bank of England estimates.

U.S. Balance of Payments. U.S. liabilities to foreign official agencies increased in September by an estimated \$1-1/4 billion. Most of this increase appears to have been in liabilities to oil-exporting countries. (In addition to adding substantially to their dollar holdings in the United States, oil-exporting countries provided a total of \$635 million to a number of countries under the IMF oil facility; half of this went to Italy.) The increase in U.S. liabilities was partly offset by a rise of \$.4 billion in U.S. reserve assets.

For the third quarter as a whole U.S. liabilities to foreign official agencies are estimated to have increased by around \$2.0 billion, with liabilities to the oil-exporting countries alone rising by over \$4.0 billion. The largest single change in official holdings in the United States of other countries during the third quarter was a decline of \$3.8 billion in holdings of Germany; about half of this resulted from Germany's loan to Italy secured by gold.

In the third quarter U.S. reserve assets increased by \$1.0 billion. The U.S. reserve position in the IMF increased as Italy and other countries drew dollars from the IMF; SDR holdings rose as Italy and other countries sold SDRs to the U.S. Treasury; and System holdings of convertible currencies increased as a result of a swap drawing by Mexico.

In July and August there was a net inflow of private capital reported by U.S. banks. In August this amounted to about \$1-1/2 billion. For the two months combined the net inflow of \$2.0 billion represented a sharp reversal from the $3.5 billion net outflow recorded in the second quarter. This shift reflected both a slowdown in bank lending to foreigners and an increase in capital inflows from foreigners.

The balance on transactions in securities continued to be a net outflow in August though at a lower level than in July, as foreigners resumed their net purchases of U.S. stocks in the amount of $80 million.

Complete data on U.S. balance of payments transactions in the second quarter show that the balance on goods and services in that period was a small deficit -- the first since the first quarter of 1973 -- as the trade deficit increased and the net surplus on services declined. This decline resulted principally from a sharp drop in net investment income receipts. The balance on long-term capital transactions also shifted to a net outflow in the second quarter from a net inflow in the first quarter. Net long-term outflows reported by U.S. banks rose quite sharply in the second quarter; there was virtually no outflow in the first quarter.

U.S. merchandise trade. The U.S. trade deficit in August reached an annual rate of nearly $15-1/2 billion (balance on payments basis), up from a $10 billion deficit rate in July and a (revised) $6-1/2 billion deficit rate in the second quarter. Apart from fuel imports and agricultural exports, however, the July-August deficit rate was $2.2 billion, slightly higher than the second-quarter rate, but lower than the deficit rates for the first quarter and for each quarter of 1973.

U.S. MERCHANDISE TRADE, BALANCE OF PAYMENTS BASIS
(billions of dollars, seasonally adjusted annual rates)

	1973	1974		
	Year	Q-1	Q-2	July-Aug.
EXPORTS	70.3	89.2	96.4r	98.8
Agric.	17.9	23.6	22.8r	20.9
Nonagric.	52.4	65.6	73.5r	77.9
IMPORTS	69.8	89.5	102.9	111.3
Fuels	8.8	20.4r	28.2r	31.2
Nonfuels	61.0	69.1r	74.6r	80.1
TOTAL BALANCE	+0.5	-0.3	-6.5r	-12.5
BALANCE excl. fuel imp. and agric. exp.	-8.6	-3.5r	-1.1r	-2.2

Note: r = Revised.

The increase in petroleum imports in July-August was all in volume, with imports averaging about 7 million barrels per day in each month, compared with 6-1/2 million in the second quarter; in July-August 1973, petroleum imports averaged 6-2/3 million barrels per day. Import prices for petroleum have held at about $11.70 per barrel since April.

In value terms, nonfuel imports were at a rate 7 percent higher in July-August than in the second quarter. Roughly one-third of this growth was due to automotive imports from Canada, which increased in volume by 25 percent; this strong percentage increase, however, occurred from an unusually low second-quarter volume. The volume of automotive imports from countries other than Canada declined in July-August, and may continue to do so for several months as dealers work off large inventories of 1974 models. Imports of nonfuel industrial supplies in July-August were 8 percent higher in price and 9 percent greater in volume than in the second quarter. Half of this volume growth was due to imports of iron and steel products which, with an easing of supply pressures abroad, rebounded to levels slightly higher than those registered a year earlier.

The volume of agricultural exports in July-August was roughly 8 percent below the second-quarter rate, with sharp drops in exports of corn and soybeans. It is possible that disruptions in Great Lake traffic (caused by Canadian maritime strikes and the temporary closing of the Welland Canal) were partially responsible for the low August volumes. Prices of soybeans and corn jumped in August, although the unit value of all agricultural exports in July-August changed little from the second-quarter unit value. On October 7, the Department of Agriculture announced that large export sales of wheat and certain feedgrains (corn, sorghum, soybeans and soybean meal) will require prior governmental approval in the future.

Nonagricultural exports in July-August were slightly below the second-quarter rate in volume terms, but 6 percent higher in value terms. Price increases were particularly large for exports of industrial materials and machinery, exceeding 10 percent for metals, fertilizer, bituminous coal and wood pulp. Exports of industrial materials dropped 6 percent in volume, while machinery exports increased by 2-1/2 percent.

There is some indication, however, that machinery exports may also begin to decline in volume in the near future. While unfilled export orders for U.S. durable goods (excluding motor vehicles and parts) have continued to rise in value to a level almost 30 percent higher in August than a year earlier, the volume of these unfilled orders seems to have declined steadily from an apparent peak in May.

Financial conditions and monetary policy in major industrial countries. Short-term interest rates have generally declined slightly in recent weeks, while long-term rates in those countries for which September data are available have either decreased or held steady. (See Table 1.) These developments apparently reflect continued flatness in economic activity and attendant weakening of credit demand in most countries. In some instances a moderate easing of monetary policy may also have contributed to the softening of yields.

Despite the recent drop, interest rates remain at historically very high levels and -- with a few exceptions -- are substantially above their levels of a year ago. As has been true since early 1973, long-term rates remain lower than short-term rates, implying that, in the long-run at least, some abatement of inflationary pressures is anticipated.

Associated with the high and, until recently, rising level of interest rates has been a continuing slide in stock prices everywhere, as many investors have moved their funds out of equities to earn a high nominal rate of return in alternative, and less risky, assets. The decline in stock prices in major industrial countries during the third quarter ranged from 11 per cent in Germany to 27 per cent in the United Kingdom. Interest rate movements were of course not the only cause of the weakness of stock prices, such factors as widespread pessimism about the business outlook also having helped to drive them down.

TABLE 1
INTEREST RATES FOR MAJOR COUNTRIES
(Per cent per annum, at or near end of month)

	Short-term Rates						Long-term Rates					
	1973	1974					1973	1974				
	Sept.	Mar.	June	Aug.	Latest	(date)	Sept.	Mar.	June	Aug.	Latest	(date)
U.K	13.38	16.00	13.00	12.63	11.88	(10/4)	11.45	14.67	15.41	15.81	15.45	(10/4)
Germany	13.75	11.50	9.60	9.80	9.80	(10/1)	9.11	9.92	9.87	9.82	10.09	(10/1)
France	11.80	11.88	14.50	13.75	13.13	(10/9)	9.29	10.35	10.87	11.01	11.06	(9/13)
Italy	8.50	13.00	20.00	17.88	--	(8/31)	7.28	7.75	9.78	10.08	--	(8/31)
Belgium	7.65	9.40	11.50	12.00	12.00	(10/1)	7.62	8.36	8.86	9.26	--	(8/31)
Netherlands	5.64	6.00	7.00	7.50	7.38	(9/26)	8.01	9.04	9.62	9.65	9.48	(9/27)
Switzerland	4.50	6.50	6.50	7.00	7.00	(9/13)	5.79	7.09	7.24	7.36	7.36	(9/6)
Japan	9.00	12.50	12.63	13.50	13.00	(9/27)	8.23	9.77	9.96	10.18	--	(8/31)
Canada	8.75	9.00	11.00	11.75	10.75	(10/7)	7.72	8.91	9.46	9.84	9.67	(9/27)
U.S.	6.94	8.34	7.38	8.84	6.29	(10/7)	6.95	7.38	7.62	8.14	7.94	(9/27)

Notes:
Short-term rates: U.K. - 90-day local authority deposits; Germany - 3-month interbank loan rate; France - call money rate against private paper; Italy - interbank deposits of up to one-month maturity; Belgium - rate on 4-month Treasury bills; Netherlands - 3-month Treasury bill rate at mid-month; Switzerland - 3-5 month deposit rate; Japan - call money rate, unconditional; Canada - Canadain finance company paper; U.S. - U.S. Treasury bill.
Long-term rates: U.K. - 3-1/2% war loan; Germany - 6% public authority bond yield; France - public sector bonds; Italy - composite yield on all bonds except Treasury bonds (monthly average); Belgium - long-term government bonds, composite yield; Netherlands - average of three 4-1/4 - 4-1/2% government loans; Switzerland - Swiss government composite yield; Japan - 7-year industrial bonds; Canada - Government long-term average yield; U.S. - Government 10-year constant maturity bond yield.

Most monetary authorities continue to pursue the restrictive policies introduced in 1972 or 1973 to reduce inflationary pressures through damping of aggregate demand. One reflection of the generally tight monetary stance has been a slower rate of growth in both M1 and M2 in most countries during 1973 and 1974 as compared with the very rapid rate of increase in 1972. (See Table 2.) However, in the United Kingdom and Canada, expansion of the more broadly defined money supply did not decelerate until this year.

Recently, three countries -- the United Kingdom, Germany, and Japan -- have taken actions that suggest a move toward a less restrictive monetary stance. The extent of the policy change has been less pronounced in Germany and Japan than in the United Kingdom. In the former two countries, the monetary authorities continue to stress that policy remains restrictive in intent and that priority continues to be accorded to price stabilization goals. Their recent actions have apparently been aimed not at stimulating economic activity but at preventing further discouragement of it. In the United Kingdom, on the other hand, though slowing inflation -- which remains severe -- is still a prime policy target, the authorities evidently have changed the emphasis of policy toward a moderate expansion of aggregate demand, as output is flagging and productivity increases are virtually nil.

The diminution or absence, at least temporarily, of a serious balance of payments constraint in all three countries may have helped

TABLE 2
PERCENTAGE GROWTH RATES IN MONEY SUPPLY
FOR SELECTED INDUSTRIAL COUNTRIES
(Seasonally Adjusted - Annual Rates)

		Change during		Average of Monthly Changes			
		1972	1973	Latest 12 mos.	Latest 6 mos.	Latest 3 mos.	Latest Month
U.K.							
	M1	13.8	4.5	0.3	6.0	6.7	August
	M3	27.7	28.8	16.7	8.8	15.9	
Germany							
	M1	14.3	2.0	7.2	8.8	8.7	July
	M2	16.9	14.0	7.1	2.4	-6.7	
France							
	M1	14.4	9.4	10.7 a/	10.9 a/	n.a.	June
	M2	18.4	15.0	17.5 a/	16.6 a/	n.a.	July
Canada							
	M1	13.0	11.9	7.3	7.2	-11.4	August
	M2	15.8	18.4	19.4	14.6	15.8	
Japan							
	M1	24.7	16.8	12.5	14.1	22.0	July
	M2	24.7	16.8	11.5	10.8	12.5	
U.S.							
	M1	8.7	6.1	5.3	5.6	4.3	August
	M2	11.1	8.9	8.2	7.1	7.5	

a/ Due to absence of data because of strikes in the banking system, French figures are not average monthly changes. The change in M2 is represented by July 74/July 73 and July 74/Jan 74; the changes in M1 -- by June 74/June 73 and June 74/Dec 73.

For each country M2 includes M1 plus private time and savings deposits, with the following exceptions: Germany: time deposits of over 4 years maturity and all savings deposits are excluded; Japan: public sector deposits are included, as are contract shares in mutual savings and loan associations; United States: negotiable DC's in amounts greater than $100,000 are excluded.

In the U.K. the Bank of England's series on M2 has been discontinued. The M3 series has been used. This includes, in addition to M1, all sterling and non-sterling deposits in the U.K. banking sector held by both public and private U.K. residents. All money supply data are from national sources.

convince policymakers of the feasibility of easing up on the brakes. Japan has made significant progress toward eliminating its current account deficit, and the trade balance has been back in surplus since June. Britain, though its current account is in substantial deficit, is not losing reserves, thanks largely to sizable placements in sterling assets by oil-producing nations. The downturn lately in short-term rates elsewhere has permitted the United Kingdom to lower its own rates without fear that such action would trigger capital outflows. In Germany, though foreign exchange reserves have declined in recent months, the current account has been recording a substantial surplus and, in fact, reducing this surplus may be an important motivation for adopting the recent easing measures. In Germany and Japan, some slowing in the inflation rate has further enhanced the feasibility of relaxing monetary restraint to advance the objectives of either stimulating or ceasing to inhibit expansion of output.

Details on major countries follow:

Unlike movement elsewhere, short-term interest rates in Germany have held steady in recent weeks -- perhaps in part in reaction to capital outflows and to the decline in the premium on the forward mark -- and long-term rates have risen. But, in contrast to the pattern in other countries, short-term yields have declined substantially since the beginning of the year -- by almost three percentage points.

The behavior of monetary aggregates this year attests to the combination of the tightness of monetary policy and the sluggish pace of economic activity in Germany. In the first seven months of 1974, M1 increased at the relatively moderate annual rate of about 6 per cent, and M2 (M1 plus time deposits in commercial banks with less than four years' maturity) at the even slower annual rate of about 3-1/2 per cent. (In the corresponding period in 1973, M2 had increased by 16 per cent, annual rate, while M1 was simultaneously undergoing a slight decline. These divergent movements in 1973 reflected a heavy flow into short-term time deposits, the yields on which rose very sharply while the rates on other short-term financial assets, such as savings deposits, were far stickier.)

Bank credit to the private, non-bank sector expanded at an annual rate of about 8 per cent in January-July, down from the 13 per cent annual rate of increase in the same period of 1973. Within 1974, credit has expanded somewhat more rapidly recently than in the first four months of the year, mainly because of stepped up loan demand to finance German exports, repayment by German borrowers of loans from overseas lenders, and, possibly, financial distress in some firms whose cash inflow was cut by the decline in business activity.

German monetary authorities have taken several easing measures in the last three months. In July, the effective Lombard rate was lowered and quantitative limitations on Lombard borrowing were suspended. At the same time, banks' rediscount quotas were liberalized. Reserve requirements have been reduced twice, by 10 per cent on September 1 and by 8 per cent on October 1. Furthermore, the 20 per cent deposit requirement on non-bank borrowing from abroad was eliminated on October 1.

The authorities have represented these measures as aimed not at easing the overall degree of restraint but at offsetting the adverse effect on bank liquidity of recent capital outflows. German foreign exchange reserves have in fact fallen by about DM 6 billion since the end of May. Nevertheless, Germany's easing measures may have been motivated by considerations other than the officially expressed desire to counterbalance exogenous contractionary developments. Easier money can be expected to further such goals as forestalling a wave of business and bank failures in the wake of the collapse of Bankhaus I. D. Herstatt at the end of June and at a time of greatly increased bankruptcies in general; reducing a large, persistent and embarrassing current account surplus; and, possibly, lowering unemployment, which currently exceeds 3 per cent, seasonally adjusted.

Germany is in a particularly advantageous position to adopt a somewhat more expansionary posture, since not only is its underlying balance of payments position strong, but its inflation rate is the lowest among industrialized countries. The principal inhibition to a more active easing of policy at this juncture is apprehension that forthcoming wage settlements will exceed the 10 per cent guideline.

Fears that wages will rise steeply next year, in response to past and anticipated price increases, is probably a major barrier to more stimulative policies in most industrialized countries.

Recent developments suggest some easing of monetary policy in the United Kingdom. Short-term interest rates, which declined sharply last spring (when sterling was recovering in the exchange markets) and which have since fluctuated, moved downward in August and September in conjunction with the decline in U.S. and Euro-dollar rates. Furthermore, there has been some acceleration in the growth of the British money supply following a period of very slow expansion in the first half of this year. It is clear that the Bank of England approves of these interest rate and money supply movements, having expressed concern in September that bank lending to companies for investment purposes had been unduly discouraged.

The speedier growth of the money supply this summer has been influenced by such factors as heavy government borrowing needs and, in the case of the money supply broadly defined to include bank deposits of all U.K. residents (M3), by an exceptionally large increase in Euro-dollar deposits of British oil companies. But an upturn in the demand for bank credit -- primarily to finance inventory accumulation at higher prices -- also contributed.

Over the year as a whole, loans to the manufacturing sector have risen strongly, but advances to other sectors have declined.

Consequently, most banks have been able to stay under the credit ceiling imposed last December that requires banks to make interest-free deposits with the Bank of England on the excess of interest-bearing liabilities above some specific amount.

It is Britain's large banks whose activity is most likely to be inhibited by the ceiling, since growth of interest-bearing liabilities has been heavily concentrated in such banks, as there has been some erosion of confidence in smaller banks.

Rising interest rates and deceleration in the growth of the money supply and of credit expansion indicated a progressive tightening of Japanese monetary policy during 1973 and through August of this year. In September, however, the authorities took two steps that imply a moderate easing of monetary stringency. First, the Bank of Japan abolished the 10 per cent marginal reserve requirement on increases in non-resident free yen account liabilities. Second -- and more significant as a barometer of relaxation of restraint -- the Bank liberalized the ceiling on credit expansion for the fourth quarter.

The sharp decline in economic activity coupled with improvement in the current account of the balance of payments apparently prompted the movement in the direction of a less restrictive monetary stance.

During September, short-term interest rates in Japan softened, but long-term rates continued to rise. The call money rate at the end of September was 13 per cent, down from 13-1/2 per c nt a month earlier but 4 percentage points above its level a year earlier. Long-term rates have risen about 2 percentage points over the last year.

In response to rampant inflation and a huge balance of payments deficit, the Italian authorities substantially tightened monetary policy this year. The key elements in the series of restrictive measures adopted in 1974 have been credit ceilings that limit loan expansion in general for the year ending March 31, 1975 to 15 per cent for industry and 12 per cent for borrowers in so-called "non-productive" categories.

The authorities have placed great stress on controlling the "monetary base," and promoting this objective was a prime reason for the introduction of a 50 per cent import deposit requirement in April. However, efforts to limit expansion of the monetary base have been frustrated by the Bank of Italy being forced to finance the government's deficit, because of the reluctance of commercial banks -- in the face of rising interest rates -- to buy Treasury bills and because of the weakness of the bond market.

The improvement in the balance of payments, coupled with steep rises in both short- and long-term interest rates suggest that the restrictive measures are having a substantial impact. However, inflation continues at a rapid rate. (Data on monetary aggregates are not available beyond early 1974.)

In France a tight monetary policy continues to be pursued. It is directed primarily at restricting growth of bank credit by means of ceilings. In conjunction with a series of moves to tighten fiscal policy, credit ceilings have been lowered this year and penalties for violations stiffened.

However, largely because of the bank strike last spring, the credit controls appear to have been widely violated, at least through mid-year. Nevertheless, money has been sufficiently tight to substantially affect the business climate, as is evidenced by a steep 23 per cent rise in bankruptcies this year compared to 1973. Construction firms have been particularly hard hit.

The French policy of monetary restraint is aimed both at slowing inflation and at encouraging capital inflows to ameliorate the balance of payments deficit. The Bank of France has sought to further both objectives by forcing up interest ratss. To this end, the bank has raised its discount rate since early 1973 from 7-1/2 to 13 per cent. To improve the balance of payments, the Bank abolished reserve requirements on non-resident accounts and exempted export credit from the credit ceilings.

Financial conditions in Canada have become progressively tighter during the past 18 months, reflecting both restrictive monetary policy and heavy demand for credit from the private sector. From the end of 1972 through mid-1974, the Bank of Canada raised its bank rate eight times, from 4.75 to 9.25 per cent. Rates on short- and long-term debt also climbed steeply, though short-term rates and yields on long-term government debt peaked during the summer and have since declined. Since the end of 1972, there has also been a sharp decline in the banking system's net free liquidity ratio, adjusted for foreign currency borrowings.

Monetary policy is expected to remain relatively tight, at least until the end of the year, but strains in financial markets have eased recently, in response to stagnation in economic activity, which has improved the balance between the supply of and demand for credit. The Bank of Canada continues to restrain growth of the money supply. For the three months ending in September, increases in the monetary base were very small (C$ 125 million), and although the seasonally adjusted annual rate of increase in M2 from the previous three months remained at about 13 per cent, M1 grew only slightly.

Fund/Bank Meetings. Four problems dominated discussions at the I.M.F./World Bank Annual Meetings held in Washington September 30 - October 4: world inflation, world recession, financing oil deficits, and the plight of the non-oil-exporting developing nations.

Most Governors in their speeches pledged their countries to a continuation of the struggle against inflation, while giving emphasis to the need to avoid policies that would produce a prolonged world recession.

On the general question of means of financing countries' massive, oil-related, current account imbalances, some speakers called for a modest expansion of the I.M.F.'s present, concessional Oil Facility; other speakers led by U.K. Chancellor Healey stressed the need for the establishment of a much larger recycling facility operating at commercial terms; a third group expressed doubts that any new recycling mechanisms were necessary. It was decided, however, that the I.M.F.'s new Interim Committee, the successor body to the Committee of Twenty, should give urgent attention to the recycling question. It asked the Executive Directors of the I.M.F. to prepare a study of the need for further governmental involvement, either through the I.M.F. or otherwise, in facilitating the recycling process. The Committee will meet on January 15-16, 1975, to consider this study, as well as to discuss in more detail other issues that were raised at the I.M.F. meetings such as the enlargement of I.M.F. quotas, amendments to the I.M.F. Articles of Agreement, and the working of the balance-of-payments adjustment process.

Study of the problems facing those developing countries most seriously affected by the present world economic situation was assigned to a new joint I.M.F./World Bank Development Committee.