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CONFIDENTIAL (FR)

November 14, 1979

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

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

	Latest Data			Percent Change from		
	Period	Release Date	Data	Preceding Period	Three Periods Earlier	Year earlier
				(At annual rate)		
Civilian labor force	Oct.	11-2-79	103.5	-.3	1.6	2.4
Unemployment rate (%) 1/	Oct.	11-2-79	6.0	5.8	5.7	5.8
Insured unemployment rate (%) 1/	Oct.	11-2-79	3.0	3.0	2.9	3.2
Nonfarm employment, payroll (mil.)	Oct.	11-2-79	90.2	4.1	2.0	3.1
Manufacturing	Oct.	11-2-79	21.0	.2	-2.3	1.6
Nonmanufacturing	Oct.	11-2-79	69.2	5.3	3.3	3.6
Private nonfarm:						
Average weekly hours (hr.) 1/	Oct.	11-2-79	35.5	35.7	35.6	35.8
Hourly earnings ($) 1/	Oct.	11-2-79	6.28	6.26	6.18	5.84
Manufacturing:						
Average weekly hours (hr.) 1/	Oct.	11-2-79	40.1	40.1	40.2	40.5
Unit labor cost (1967=100)	Sept.	10-30-79	176.6	1.4	6.0	7.7
Industrial production (1967=100)	Sept.	10-16-79	152.3	6.3	-.8	2.5
Consumer goods	Sept.	10-16-79	149.9	12.1	-5.0	-.6
Business equipment	Sept.	10-16-79	172.4	9.8	2.1	5.3
Defense & space equipment	Sept.	10-16-79	94.0	7.7	7.4	5.6
Materials	Sept.	10-16-79	156.2	1.5	-.8	3.3
Consumer prices all items (1967=100)	Sept.	10-26-79	223.1	13.0	12.6	12.0
All items, excluding food & energy	Sept.	10-26-79	211.5	12.0	11.1	9.9
Food	Sept.	10-26-79	237.1	10.7	4.1	9.8
Producer prices: (1967=100)						
Finished goods	Oct.	11-1-79	223.3	12.5	14.7	12.1
Intermediate materials, nonfood	Oct.	11-1-79	256.2	22.4	19.5	15.7
Crude foodstuffs & feedstuffs	Oct.	11-1-79	251.1	5.8	6.8	10.3
Personal income ($ bil.) 2/	Sept.	10-17-79	1955.2	7.5	10.5	11.3
				(Not at annual rates)		
Mfrs. new orders dur. goods ($ bil.)	Sept.	10-31-79	78.4	5.4	3.4	8.3
Capital goods industries	Sept.	10-31-79	27.1	12.0	11.7	17.3
Nondefense	Sept.	10-31-79	22.4	5.9	3.0	13.0
Defense	Sept.	10-31-79	4.7	54.5	87.6	43.2
Inventories to sales ratio: 1/						
Manufacturing and trade, total	Sept.	11-13-79	1.40	1.42	1.43	1.42
Manufacturing	Sept.	11-31-79	1.54	1.54	1.54	1.52
Trade	Sept.	11-13-79	1.28	1.31	1.33	1.32
Ratio: Mfrs.' durable goods inventories to unfilled orders 1/	Sept.	10-31-79	.556	.563	.548	.595
Retail sales, total ($ bil.)	Oct.	11-9-79	75.5	-1.7	4.3	9.4
GAF 3/	Oct.	11-9-79	16.4	-.8	3.0	10.1
Auto sales, total (mil. units.) 2/	Oct.	11-5-79	9.4	-12.1	-11.1	-15.8
Domestic models	Oct.	11-5-79	7.1	-17.4	-13.4	-23.2
Foreign models	Oct.	11-5-79	2.4	8.5	-3.5	18.4
Housing starts, private (thous.) 2/	Sept.	10-17-79	1,881	4.2	-2.2	-7.1
Leading indicators (1967=100)	Sept.	10-30-79	141.3	.8	.6	-1.1

1/ Actual data used in lieu of percent changes for earlier periods.
2/ At annual rate.
3/ Excludes mail order houses.

DOMESTIC NONFINANCIAL DEVELOPMENTS

The third quarter ended with economic activity on a vigorous note, with considerable strength in September outlays by both consumers and businesses. In October, however, consumer demand eased considerably as auto sales fell sharply and nonauto sales were flat in nominal terms. It is difficult to determine at this point the effects of the Federal Reserve's October 6 actions; however, there have been reports of a sharp curtailment of housing activity in recent weeks and a significant tightening of consumer credit. Through October inflation continued at about the same rapid pace as earlier this year.

Employment and Production

Nonfarm payroll employment increased 300,000 in October, following a rise of 85,000 in September. Most of the gain occurred in private service-producing industries. Total factory employment, strike-adjusted, rose somewhat in October, but remained 80,000 below its July peak. The factory workweek--at 40.1 hours--was unchanged for a third straight month. Since the October labor market survey week, automakers have announced another 10,000 permanent layoffs, bringing the industry total to nearly 98,000; in addition, Ford and Chrysler plan to close plants in the second week of November, temporarily idling 33,500 workers.

The unemployment rate edged up to 6 percent in October, the upper end of the 5.6 to 6 percent range that has prevailed since the

CHANGES IN EMPLOYMENT 1/
(Thousands of employees; based on seasonally adjusted data)

	1978	1979 QI	QII	QIII	Sept.	Oct.
		- - - Average monthly changes - - -				
Nonfarm payroll employment 2/	334	302	196	73	83	306
Strike adjusted	318	304	205	76	75	326
Manufacturing	69	64	-3	-36	-3	4
Durable	57	56	3	-6	28	-56
Nondurable	12	8	-6	-30	-31	60
Construction	39	48	16	1	-9	28
Trade, Finance and Services	169	150	113	80	94	232
Private nonfarm production workers	256	230	111	9	46	308
Manufacturing production workers	50	44	-19	-46	3	24
Total employment 3/	275	329	-29	253	613	-220
Nonagricultural	268	344	-2	206	535	-108

1/ Changes are from final month of preceding period to final month of period indicated.
2/ Survey of establishments. Not strike adjusted, except where noted.
3/ Survey of households.

SELECTED UNEMPLOYMENT RATES
(Percent; based on seasonally adjusted data)

	1973	1979 QI	QII	QIII	Sept.	Oct.
Total, 16 years and older	4.9	5.7	5.7	5.8	5.8	6.0
Teenagers	14.5	15.8	16.2	16.1	16.4	16.6
20-24 years old	7.8	8.7	8.8	9.2	9.2	9.5
Men, 25 years and older	2.5	3.2	3.2	3.4	3.4	3.4
Women, 25 years and older	4.0	4.9	4.9	4.8	4.6	4.9
White	4.3	5.0	4.9	5.1	5.1	5.2
Black and other	8.9	11.4	11.6	10.8	10.6	11.7
Fulltime workers	4.3	5.2	5.2	5.4	5.4	5.5
White collar	2.9	3.4	3.3	3.4	3.3	3.5
Blue collar	5.3	6.5	6.7	7.2	7.1	7.3

middle of 1978. The number of unemployed persons rose nearly 200,000 in October to 6.2 million, with the increases concentrated among adult women and black workers. Jobless rates were essentially unchanged for adult men and full-time workers. Total employment, as measured by the household survey, declined 220,000, after a rise of more than 600,000 in September. Monthly movements in this measure of employment have been somewhat erratic in recent months, and the October level was not much different than in July.

Industrial production was about unchanged in October, continuing on the plateau it has held since the spring. A moderate rise occurred in the production of consumer nondurable goods while strikes contributed to a decline in the output of business equipment. Automobile assemblies were unchanged in October; however, auto producers have announced plans to significantly reduce production rates in November and December in the face of lagging sales. Output of basic steel declined further in October. Overall, manufacturing industries operated at about 85 percent of capacity in October, close to the September rate and approximately 2 percentage points below the peak level reached in March. Since March, most of the reduction in the utilization rates has reflected sharp declines in operating rates for the motor vehicle and steel industries.

Personal Income and Consumer Spending

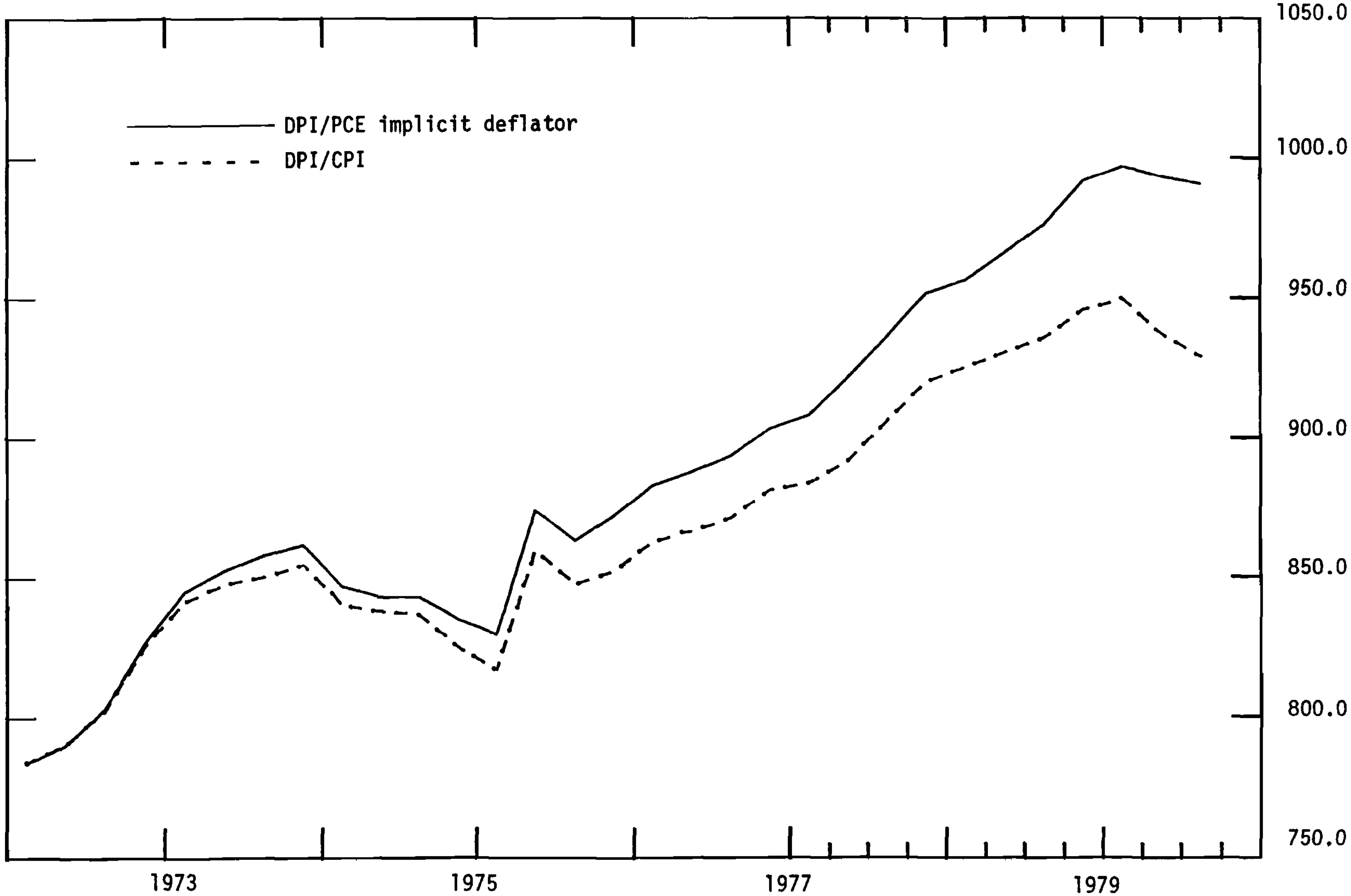
Personal income grew at a 7-1/2 percent annual rate in September, roughly the same rate as in August. A pickup in the growth of private wage and salary disbursements was offset by declines in property income,

PERSONAL INCOME
(Based on seasonally adjusted annual rate data)

	1977	1978	1979 QI	1979 QII	1979 QIII	1979 August	1979 Sept.
	- - Average monthly change, in billions of dollars - -						
Total personal income	$13.9	$17.8	$15.1	$11.0	$16.7	$11.1	$12.1
Nonagricultural income	12.6	17.1	15.3	11.4	18.5	13.2	14.0
Agricultural income	1.2	.7	-.2	-.4	-1.8	-2.1	-1.9
Wage and salary disbursements	8.4	11.5	11.8	6.1	8.5	5.7	10.5
Private	7.0	10.1	10.8	4.9	7.6	4.3	9.9
Manufacturing	2.5	3.2	3.5	.5	1.0	-1.8	2.6
Other income	6.0	7.1	5.6	5.2	8.7	5.6	2.2
Transfer payments	1.2	1.5	1.8	1.8	6.3	2.8	2.3
	- - Percentage change, compound annual rates 1/ - -						
Total personal income							
Current dollars	11.5	12.9	11.4	8.9	11.2	6.9	7.5
Constant dollars 2/	4.5	3.6	.4	-4.2	-1.5	-5.7	-5.5
Wage and salary disbursements							
Current dollars	11.2	12.8	12.7	8.0	8.4	5.6	10.2
Constant dollars 2/	4.2	3.5	1.5	-4.9	-4.0	-7.0	-2.8
Memorandum:							
Real per capita disposable income	4.5	3.4	1.2	-2.3	-2.0	n.a.	n.a.

1/ Changes over a period longer than one quarter are from final quarter of preceding period to final quarter of period indicated. Monthly percent changes at annual rates, not compounded.
2/ Deflated by the CPI for all urban consumers, seasonally adjusted.

REAL DISPOSABLE PERSONAL INCOME
(Billions of 1972 dollars)



partly due to storm damage in the South. Despite sizable nominal gains, income growth continues to lag inflation. Most measures of real income--before or after tax--peaked at the turn of the year; however, the extent of the subsequent decline is sensitive to the measure used for deflation. For instance, disposable personal income deflated by the consumer price index has fallen 2 percent from the peak; this contrasts with a 1/2 percent drop for the same income series adjusted by the implicit deflator for personal consumption.

Consumer demand was quite strong during the third quarter despite the losses in real income. From June to September retail sales rose 6.9 percent (4.8 percent in real terms). In October, however, retail sales declined 1.7 percent, as automobile purchases fell sharply. Excluding autos and nonconsumption items, nominal retail sales were about unchanged in October. Within this grouping, sales at general merchandise, apparel, furniture, and appliance (GAF) stores, which are largely discretionary items, declined 0.8 percent. In real terms, retail sales in October probably fell more than 2-1/2 percent.

Unit auto sales were at a 9.4 million annual rate in October, the slowest pace since the strike-affected fourth quarter of 1976. The annual sales rate for domestic models fell nearly 1-1/2 million units to a 7.1 million unit annual rate in part due to the ending of rebates and price discounts which buoyed purchases in August and September. Initial response to the 1980 models--introduced a month later than usual because of overhangs of 1979 models--was considered disappointing by

RETAIL SALES
(Percent change from previous period;
based on seasonally adjusted data)

	1979		1979		
	QII	QIII	Aug.	Sept.	Oct.(p)
Total sales	.5	4.1	3.3	2.6	-1.7
(Real) 1/	-2.0	2.1	3.0	1.5	n.a.
Total, less auto and nonconsumption items	2.4	4.1	1.9	2.3	-.1
GAF 2/	2.4	5.4	3.2	.5	-.8
Durable	-2.7	4.9	6.0	3.6	-4.5
Auto	-7.1	3.6	8.8	4.5	-8.2
Furniture & appliances	2.3	8.6	3.9	.7	-2.0
Nondurable	2.3	3.7	2.0	2.1	-.2
Apparel	.8	5.8	3.6	-2.9	-2.8
Food	2.5	2.0	-1.2	4.2	-.6
General merchandise 3/	3.1	4.0	2.8	1.8	.5
Gasoline	7.2	6.8	9.2	.7	1.6

1/ BCD series 59.
2/ General merchandise, apparel, furniture and appliance stores.
3/ General merchandise excludes mail-order nonstores; mail-order sales are also excluded in the GAF composite sales summary.

AUTO SALES
(Millions of units; seasonally adjusted annual rates)

	1979						
	QI	QII	QIII	July	Aug.	Sept.	Oct.
Total	11.5	10.6	10.8	10.6	11.0	10.7	9.4
Imports	2.4	2.6	2.3	2.5	2.2	2.2	2.4(p)
Domestic	9.1	8.0	8.5	8.1	8.8	8.5	7.1
Small	3.7	3.9	3.5	3.8	3.3	3.6	3.2
Intermediate & Standard	5.4	4.1	4.9	4.4	5.4	4.9	3.9

Note: Components may not add to totals due to rounding.

industry sources. In contrast, sales of foreign models--apparently held down this summer by inventory shortages--rose by 200,000 units (annual rate) in October.

Surveys of consumer confidence in October reported mixed results. The Conference Board's composite index of consumer attitudes rebounded strongly in October to the level reported last spring, although it is still below the readings reported in late 1977 and early 1978. On the other hand, the generally more reliable University of Michigan Survey Research Center index of sentiment declined slightly, and is in the general range reported during the last recession. There was no obvious explanation for the divergent movements in the two surveys; however, the wording of the questions in the surveys varies, and significant differences between the two measures have occurred in the past. Both surveys continued to report relatively favorable attitudes toward market conditions for buying large durable goods and houses. But the Michigan survey reported that attitudes about conditions for buying big ticket items were somewhat less favorable among respondents interviewed after the System's October 6 action than among those interviewed earlier.

Residential Construction

Notwithstanding tightening financial conditions during the late summer, private housing starts edged up to a 1.9 million unit annual rate in September--near the top of the range that has prevailed since May. However, reports from several sources suggest that home sales and building activity late in October were severely curtailed by developments associated with the System's recent policy actions. Potential home purchasers were apparently discouraged by increased financing costs and diminished credit availability--partly due to usury ceilings--while builders' costs increased as a result of higher borrowing rates.

Demands for housing--spurred by the attractiveness of homes as an investment in an inflationary environment--remained strong through September. For the third quarter as a whole, existing home sales were 4 percent higher than the second quarter and only 1 percent below the relatively high 1978 average. New-home sales were unchanged in September, with the third quarter pace down by only 6 percent from the 1978 monthly average. Single-family starts stayed at a 1.2 million annual rate in September, marking 7 consecutive months of stability in this series. Multifamily starts were up more than 10 percent, in part due to the usual fiscal year-end bulge in government subsidized units (HUD, Section 8).

Business Fixed Investment

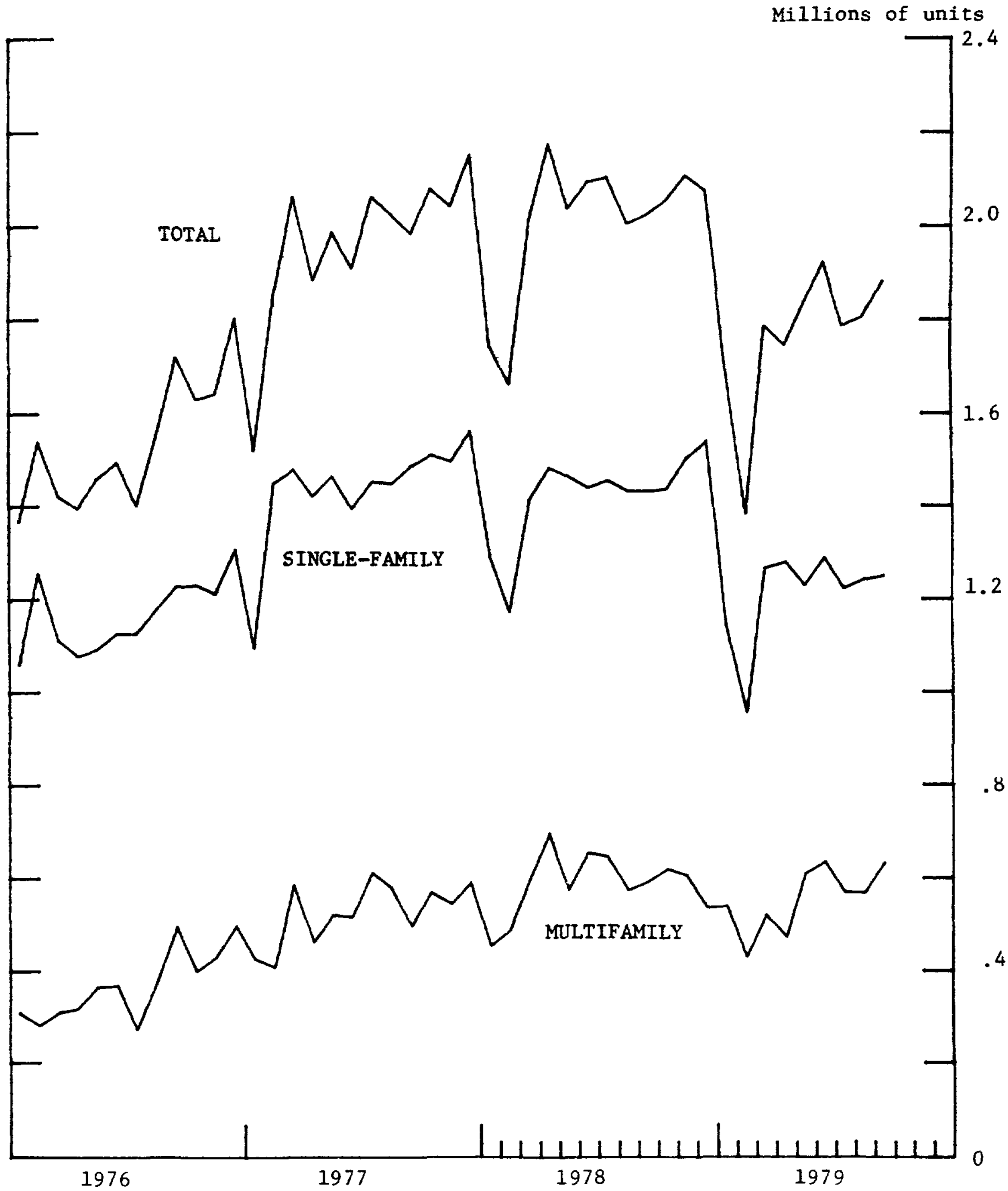
Spending for business capital equipment in September continued to advance following the reduced levels of the spring, as shipments of nondefense capital goods rose 1.6 percent. For the third quarter as a whole, these shipments were up 5.7 percent--the highest rate of growth in a year. In contrast to capital equipment, outlays for other investment items have shown less strength. Expenditures on nonresidential construction from July to September were on a plateau about 4 percent above

PRIVATE HOUSING ACTIVITY
(Seasonally adjusted annual rates, millions of units)

	1978		1979				
	Annual	QIV	QII	QIII	July 1/	Aug. 1/	Sept. 2/
Total							
Permits	1.80	1.82	1.59	1.65	1.53	1.65	1.78
Starts	2.02	2.08	1.83	1.82	1.79	1.81	1.88
Single-family							
Permits	1.18	1.22	1.03	1.02	1.00	1.03	1.02
Starts	1.43	1.49	1.26	1.24	1.22	1.24	1.25
Sales							
New homes	.82	.84	.71	.77	.78	.76	.76
Existing homes	3.91	4.27	3.73	3.88	3.77	3.85	4.01
Multifamily							
Permits	.62	.60	.56	.64	.53	.62	.61
Starts	.59	.59	.57	.59	.57	.57	.63
Mobile home shipments	.28	.29	.27	n.a.	.28	.28	n.a.

1/ Regular monthly revision.
2/ Preliminary estimates except permits which reflect first monthly revision.

PRIVATE HOUSING STARTS
(Seasonally adjusted annual rate)



the second quarter average. Business spending on motor vehicles, moreover, has declined as sales of heavy weight trucks fell off sharply in August and September from the advanced July level.

Capital spending commitments continue to suggest some moderation of the recent strong spending growth in the near term. Although new orders for nondefense capital goods rose 10.8 percent from July to September, they still remain below the first quarter level. Similarly, private building and nonbuilding contracts in September remained near the levels that have prevailed since the start of the year.

The McGraw-Hill survey of 1980 business capital spending plans reports that business plans to increase fixed investment by 9.6 percent in 1980. Adjusting this rise for the capital goods price increases expected by the survey respondents, the results suggest no change in real outlays after three years of substantial growth, which is broadly consistent with the commitments data. For the most part, this survey was teken before the October 6 Federal Reserve policy actions, which could lead to some retrenchment in spending plans. Historically this survey has had a tendency to underestimate spending growth during cyclical expansions and overestimate during recessions.

Inventory Investment

Strong sales in the third quarter along with some production adjustments, particularly in the automobile industry, have helped avoid the development of any serious inventory overhangs. The book value of all manufacturing and trade stocks increased at an exceptionally slow

BUSINESS INVESTMENT SPENDING
(Percent change from preceding comparable period, based on seasonally adjusted data)

	1979						September 1978 to September 1979
	QI	QII	QIII	July	Aug.	Sept.	
Nondefense capital goods shipments	5.2	-.6	5.7	3.3	2.8	1.6	13.1
Nonresidential construction put-in-place	0.0	8.0	4.5	1.9	-0.1	-0.4	17.0
Building	0.6	10.9	5.4	2.1	-1.4	0.1	22.3
Nonbuilding	-0.7	4.3	3.4	1.6	1.6	-1.1	10.7

CAPITAL GOODS ORDERS
(Percent change from preceding comparable period, based on seasonally adjusted data)

	1979						September 1978 to September 1979
	QI	QII	QIII	July	Aug.	Sept.	
Nondefense capital goods	12.0	-7.0	.5	-7.0	4.6	5.9	13.0
Machinery	6.1	-5.2	2.2	-5.0	6.3	2.6	9.9
Nonmachinery	26.9	-10.7	-3.3	-11.4	0.7	13.9	20.5

PLANT AND EQUIPMENT EXPENDITURES
(Percent change from prior year)

	Anticipated for 1979 — Commerce Department 1/ August Survey	Anticipated for 1980 — McGraw-Hill Fall Survey
All business	13.2	9.6
Manufacturing	14.6	13.5
Durables	18.5	12.6
Nondurables	11.2	14.4
Nonmanufacturing	12.0	6.3

1/ Results are adjusted for systematic bias. Without this adjustment, the August Commerce survey showed a 15.2 percent increase.

PAST REPORTS OF PLANT AND EQUIPMENT SURVEYS
(Percent change from prior year)

Year	Actual	McGraw-Hill Fall Survey	Merrill Lynch 1/ Fall Survey
1957	6.2	11.0	9
1958	-15.9	-6.7	-8
1960	9.5	10.0	8
1961	-2.3	-2.7	-5
1970	5.5	7.8	10
1974	12.7	13.6	12
1975	0.3	11.8	10
1976	6.8	8.8	3
1977	12.7	13.0	14
1978	13.3	11.1	10

1/ Prior to 1976 this survey was taken by Lionel D. Edie and Company, Incorporated.

$4.8 billion annual rate in September. The book value of manufacturers inventories increased at an annual rate of $20.5 billion in September, well below the average rate during the first eight months of the year. The inventory-sales ratio for all manufacturers remained at 1.54, the level which has prevailed since June. Total trade stocks declined at a $15.7 billion annual rate in September, the first reduction since October, 1976. A decline in retail inventories--concentrated in the automotive area--more than offset a small increase at wholesale. The inventory-sales ratio for all trade fell to 1.28.

The overall pattern of inventory investment recently has been heavily influenced by sizable swings in automobile stocks. Excessive inventories had accumulated by the end of July in the motor vehicle industry due to this summer's gasoline shortages and price increases. By the end of September, summer sales promotions and production cutbacks had been largely successful in liquidating the July overhang at auto dealers. In October, however, dealers' stocks of domestic autos rose once again as sales weakened, and further production adjustments are planned.

Government Sector

Reported federal budget totals for fiscal year 1979 indicate that the unified budget deficit was $27.7 billion, down sharply from $48.9 billion for the preceding fiscal year. Outlays totaled $493.6

BUSINESS INVENTORIES
(Billions of dollars; annual rate of change
in seasonally adjusted book values)

	1978	1979 QI	QII	QIII	Aug.	Sept.
Manufacturing and trade	41.5	49.1	56.3	45.4	37.7	4.8
Manufacturing	18.1	30.2	35.0	25.8	25.8	20.5
Durable	13.7	24.2	25.7	15.9	19.3	8.3
Nondurable	4.4	6.0	9.3	10.0	6.5	12.2
Trade, total	23.5	18.9	21.3	19.5	11.8	-15.7
Wholesale	12.8	13.2	4.7	15.1	7.0	3.4
Retail	10.7	5.6	16.6	4.5	4.8	-19.1

r = Revised.
p = Preliminary.

INVENTORY TO SALES RATIOS

	1978	1979 QI	QII	QIII	Aug.	Sept.
Manufacturing and trade	1.42	1.41	1.44	1.43	1.42	1.41
Manufacturing	1.52	1.49	1.55	1.55	1.54	1.54
Durable	1.85	1.82	1.94	1.97	1.95	1.97
Nondurable	1.15	1.11	1.11	1.10	1.09	1.09
Trade, total	1.33	1.33	1.33	1.31	1.32	1.28
Wholesale	1.29	1.23	1.18	1.17	1.17	1.15
Retail	1.45	1.43	1.48	1.44	1.46	1.41

r = Revised.
p = Preliminary.

billion, around $3 billion less than the Administration's July estimate. This smaller growth resulted for larger-than-anticipated-loan-repayments from farmers to the Commodity Credit Corporation, by a reduced fill rate for the Strategic Petroleum Reserve, and by a delay in the processing of small business and farm disaster loans. In addition, revenues were higher than anticipated, reflecting stronger than expected income growth, large final settlements on 1978 tax liabilities, and larger overwithholding of 1979 income.

For fiscal year 1980, the Administration now is forecasting a deficit of $33 billion, about $3 billion higher than the figure approved by conferees on the Second Concurrent Budget Resolution. These estimates, however, are considered by OMB to be highly tentative and are quite sensitive to revenue assumptions about economic activity, energy related outlays, and changes in tax laws.

Current hiring increases by State and local governments remain quite moderate, as these units try to limit the operating deficits that have re-emerged in this sector. Preliminary employment figures indicate that State and local employment was about unchanged in October. Further pressure has been placed on State and local governments by the tightening of financial markets in October, as poor market conditions caused the withdrawal or postponement of about one-fifth of scheduled new bond issues.

RECENT CHANGES IN PRODUCER PRICES
(Percent change at compound annual rates; based on seasonally adjusted data)1/

	Relative Importance 2/ Dec. 1978	1978	Dec. 78- Oct. 79	1979 Aug.	1979 Sept.	1979 Oct.
Finished goods	100.0	9.2	12.3	13.9	17.1	12.5
Consumer foods	25.4	11.9	5.9	14.6	22.0	-1.1
Consumer nonfood	45.2	8.4	18.4	21.3	22.6	19.4
Energy	7.2	8.0	69.5	69.9	81.2	56.1
Exc. energy	38.1	8.5	9.1	10.5	8.5	9.1
Capital equipment	29.4	8.0	8.8	1.7	3.3	14.3
Intermediate materials 3/	94.6	8.3	16.9	16.7	18.4	22.4
Exc. food and energy	83.5	8.9	13.3	10.8	12.2	20.1
Crude food materials	58.6	18.3	10.9	-2.9	17.5	5.8
Crude nonfood	41.4	15.6	25.5	5.8	35.1	33.7
Exc. energy 4/	11.2	21.3	17.6	-31.0	3.2	52.5

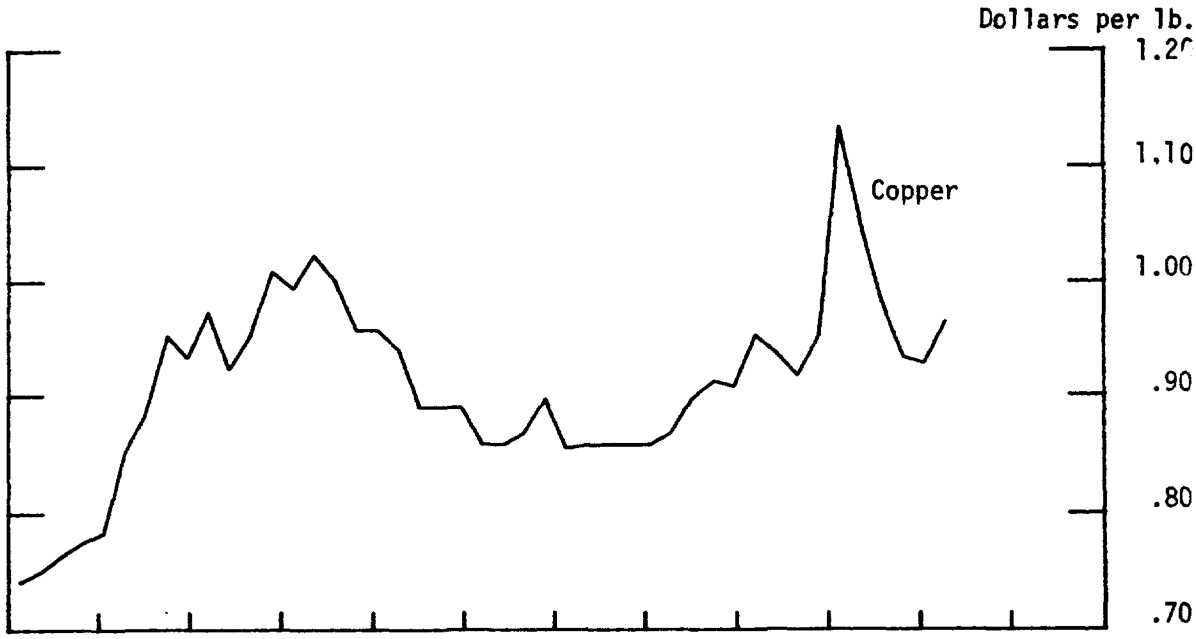
1/ Changes are from final month of preceding period to final month of period indicated. Monthly changes are not compounded.
2/ Relative importance weights are on a stage of processing basis, as a percentage of respective totals for finished goods, intermediate materials, and crude materials.
3/ Excludes intermediate materials for food manufacturing and manufactured animal feeds.
4/ Also excludes agricultural nonfood materials.

RECENT CHANGES IN CONSUMER PRICES 1/
(Percent change at compound annual rates; based on seasonally adjusted data) 2/

	Relative importance Dec. 1978	1978	Dec. 78- Sept. 79	1979 July	1979 Aug.	1979 Sept.
All items	100.0	9.0	13.2	11.7	12.6	13.0
Food	18.2	11.8	9.6	1.5	.0	10.7
Energy 3/	8.5	8.0	46.7	51.0	38.5	32.4
All items less food and energy 3/	73.3	8.5	10.7	8.7	12.2	12.0
Commodities	35.9	7.6	8.4	7.8	7.8	7.7
Services	37.4	9.4	12.3	12.0	14.4	13.2
Memoranda:						
Gasoline	4.2	8.5	61.6	60.3	47.8	41.8
Homeownership	23.6	12.4	18.0	16.7	20.1	16.6

1/ Based on index for all urban consumers.
2/ Changes are from final month of preceding period to final month of period indicated. Monthly changes are not compounded.
3/ Energy items: gasoline and motor oil, fuel oil and coal, gas and electricity. Not seasonally adjusted.

TUESDAY SPOT PRICES FOR COPPER AND SILVER



Latest data plotted are November 6, 1979.

Excluding food and energy, movements in the consumer price index continue to be dominated by homeownership costs which rose at more than a 16 percent annual rate in September after a 20 percent rate of advance in August. These large increases reflect rising house prices as well as advances in mortgage interest rates. Price increases have accelerated in recent months for several other categories, notably apparel, rent, and public transportation; fuel prices were probably an important contributing factor for the last two. In September the price increases for these items was offset somewhat by declines in used car prices and a slowing in new car price rises associated with incentive and rebate programs. Outside the consumer area, prices for metals and related products increased on a broad front during September and early October; however, spot prices for some nonferrous metals, including precious metals, generally levelled off or declined through the end of October and early November.

Productivity and Labor Costs

Labor cost pressures remained intense last quarter because of another relatively poor productivity performance. Output per hour in the nonfarm business sector was virtually unchanged in the third quarter of this year, following two quarters of decline. Productivity has declined by 1-1/2 percent over the last year.

Hourly compensation in nonfarm business rose at an 8-1/4 percent annual rate in the third quarter; this increase, combined with the small productivity advance, drove unit labor costs up at an 8 percent annual

PRODUCTIVITY AND COSTS
(Percent change from preceding period at compound annual rates;
based on seasonally adjusted data)

	1978	1979			1976:QIV-	1977:QIV-	1978:QIII
	QIV	QI	QII	QIII	1977:QIV	1978:QIV	1979:QIII
Output per hour							
Total private business	.3	-3.0	-2.2	.1	1.4	.8	-1.2
Nonfarm business	.8	-3.2	-4.1	.2	1.2	1.1	-1.6
Manufacturing	2.0	-2.4	2.9	3.2	2.6	1.6	1.4
Durable	1.2	-3.2	2.9	-.2	1.9	.9	.1
Nondurable	3.4	-.9	2.7	8.6	3.6	2.6	3.4
Compensation per hour							
Total private business	8.5	11.1	9.3	8.5	7.3	9.1	9.4
Nonfarm business	8.8	10.4	7.9	8.2	7.5	9.1	8.8
Manufacturing	9.3	10.3	9.8	8.0	8.0	8.7	9.4
Durable	9.6	10.3	9.7	8.0	8.3	8.4	9.4
Nondurable	7.8	10.0	10.6	7.9	7.1	8.7	9.1
Unit labor costs							
Total private business	8.1	14.6	11.8	8.3	5.8	8.3	10.7
Nonfarm business	8.0	14.0	12.5	7.9	6.2	7.9	10.6
Manufacturing	7.1	13.0	6.7	4.6	5.3	7.1	7.8
Durable	8.3	13.9	6.6	8.2	6.2	7.4	9.2
Nondurable	4.2	11.0	7.7	-.7	3.4	6.0	5.5

HOURLY EARNINGS INDEX 1/
(Percent change at compound annual rates;
based on seasonally adjusted data) 2/

	Oct. 77- Oct. 78	Oct. 78- Oct. 79	1979 QI	QII	QIII	Sept.	Oct.
Total private nonfarm	8.3	7.7	8.5	7.1	8.4	10.3	3.6
Manufacturing	8.3	8.8	8.5	9.7	8.2	9.0	8.3
Contract construction	7.1	6.6	7.7	7.6	6.5	6.6	1.0
Transportation and public utilities	7.5	8.5	8.6	3.5	15.6	11.4	2.1
Total trade	9.4	7.3	10.3	5.8	7.1	7.5	1.5
Services	7.6	6.8	7.5	5.4	7.3	15.8	2.9

1/ Excludes the effect of interindustry shifts in employment and fluctuations in overtime pay in manufacturing.
2/ Monthly percent changes at annual rates, not compounded.

MAJOR COLLECTIVE BARGAINING SETTLEMENTS
(Percent change at annual rates)

	Average adjustment 1975	1976	1977	1978	1979 QI	QII	QIII
Wage-rate settlements (1,000 or more workers)							
First year adjustments	10.2	8.4	7.8	7.6	4.8 2/	9.0	6.6
Average over life of contracts 1/	7.8	6.4	5.8	6.4	6.6	7.0	4.8
Wage and benefit settlements (5,000 or more workers)							
First year adjustments	11.4	8.5	9.6	8.3	2.5	10.6	9.0
Average over life of contracts 1/	8.1	6.6	6.2	6.3	5.2	7.7	6.0
Effective wage-rate adjustments (1,000 or more workers)	8.7	8.1	8.0	8.2	1.4	2.4	2.9
Current settlements	2.8	3.2	3.0	2.0	.2	1.0	.8
Prior settlements	3.7	3.2	3.2	3.7	.6	.9	1.0
Escalator provisions	2.2	1.6	1.7	2.4	.6	.5	1.0

1/ Excluding cost-of-living adjustments.
2/ The first-year change data do not reflect the pay increase received by a large number of railroad workers in the first quarter of 1979 because their contracts were retroactive to January 1978; under BLS practices this was reported as a second-year wage adjustment.

rate to a level 10-1/2 percent higher than a year earlier. Wage rates for nonfarm production workers, as measured by the index of average hourly earnings, rose at a 3-1/2 percent annual rate in October to a level 7-3/4 percent above a year ago. Manufacturing wages increased at an 8-1/4 percent annual rate in October, about the same as in the third quarter, while the increases for most other industries were smaller.

First-year wage-rate increases in major collective bargaining settlements (1,000 or more workers) were 6.6 percent in the third quarter, and have averaged 7-1/2 percent during the first 9 months of 1979, about the same as the average for all of 1978. Over the life of the contracts, annual wage advances excluding potential increases under cost-of-living escalator (COLA) clauses were 4.8 percent in the third quarter, and have averaged 6.1 percent so far this year--about the same as in 1978. In larger units where data are reported on fringe benefits as well as wages, settlements in the third quarter provide first-year increases of 9.0 percent--6.0 percent over the life of the contract (excluding COLAs). "Effective" wage rate increases for workers covered by major contracts, including deferred increases and COLA payments, have been relatively moderate given the acceleration of prices; they were 2.9 percent in the third quarter, bringing the increase to 6-3/4 percent (not at an annual rate) over the first 9 months of 1979--about the same as the average for the same period in 1978. COLA increases have accounted for about a third of effective wage changes in major contracts so far this year--up from one-fourth during the same period last year.

Prices

Inflationary pressures, which have increased considerably this year, have shown little sign of abating. Consumer prices rose at an annual rate of 13 percent in September--about the same as since early this year. An acceleration in food price increases offset a slight easing in energy inflation. At the producer level, finished goods prices rose at a 12 percent annual rate in October--less than the 17 percent rate in September, largely due to a decline in consumer food prices.

Energy prices are still increasing about three times the overall rate of inflation. At the consumer level, the index of directly purchased energy items (e.g., gasoline, fuel oil, natural gas, and electricity) rose at an annual rate of nearly 47 percent from December 1978 through September of this year, compared with an 8 percent increase over all of 1978. Moreover, the continued diffusion of energy price hikes throughout the economy has been evident in sharp markups for petroleum-based products such as industrial chemicals, fertilizers, plastics, and synthetic fibers.

Food prices, by contrast, have shown a mixed picture in recent months. The food index rose at a 10-3/4 percent annual rate at retail in September following a three month respite. However, at the producer level a drop in meat prices contributed to a slight decline in finished food prices in October after substantial increases in August and September. At the farm level, feedgrain spot prices--a key determinant of long-run livestock supplies and prices--declined through October, reflecting an abundant harvest and a large carry-over of these grains from previous crops.

III-T-1
SELECTED DOMESTIC FINANCIAL DATA

Indicator	Latest data		Net Change from:		
	Period	Level	Month ago	Three months ago	Year ago
	$ billions		Per cent at annual rates		
Monetary and credit aggregates 1/					
Total reserves	October	42.5	20.5	13.2	1.9
Nonborrowed reserves	October	40.5	0.9	5.0	0.2
Money supply					
M1	October	378.6	2.5	6.9	4.8
M2	October	938.6	8.6	10.7	7.9
M3	October	1,604.3	7.5	9.5	8.0
Time and savings deposits (less CDs)	October	560.0	12.8	13.3	10.0
CDs 2/	October	91.1	3.0	6.4	2.5
Thrift deposits (S&Ls + MSBs + Credit Unions)	October	665.7	6.0	7.8	6.0
Bank credit	October	1,134.0	8.0	13.9	13.5

Indicator		Latest data		Net Change from:		
		Period	Per cent or index	Month ago	Three months ago	Year ago
Market yields and stock prices						
Federal funds	wk. endg.	11/7/79	13.77	1.86	3.11	4.01
Treasury bill (90 day)	"	11/7/79	12.16	.93	2.79	3.31
Commercial paper (90-119 day)	"	11/7/79	14.26	1.83	4.22	4.25
New utility issue Aaa	"	11/9/79	11.50	1.28	2.10	2.20
Municipal bonds (Bond Buyer)	1 day	11/8/79	7.27	.15	1.14	1.10
FNMA auction yield (FHA/VA)		10/29/79	13.29	2.05	2.64	3.09
Dividend price ratio (common stocks)	wk endg.	11/7/79	5.88	.62	.43	.44
NYSE index (12/31/65=50)	end of day	11/5/79	57.81	-5.58	-1.52	5.09

	Net Change or Gross Offerings				
	Period	Latest Data	Year ago	Year to Date 1979	Year to Date 1978
Credit demands					
Business loans at commercial banks 1/	October	3.4	3.5	42.6	29.8
Consumer instalment credit outstanding 1/	September	4.4	3.7	29.5	31.6
Mortgage debt outstanding (major holders) 1/3/	August	7.5	9.9	59.6	73.2
Corporate bonds (public offerings)	October	2.7e	1.7	22.5e	17.0
Municipal long-term bonds (gross offerings)	October	4.2e	3.2	35.4e	40.5
Federally sponsored agcy. (net borrowing)	October	2.9e	1.9	19.7e	19.3
U.S. Treasury (net cash borrowing)	October	1.3e	6.5	19.7e	44.8

1/ Seasonally adjusted.
2/ $ billions, not at annual rates
3/ Includes comm'l banks, S&Ls, MSBs, life ins. cos, FNMA, and GNMA.
e - Estimated

DOMESTIC FINANCIAL DEVELOPMENTS

Interest rates have climbed and stock prices have fallen since the System's October 6 policy announcement. Financial markets have been adjusting not only to the System's one percentage point boost in the discount rate and establishment of marginal reserve requirements on certain managed liabilities, but also to the greater variability of money market interest rates associated with the Desk's pursuit of a reserves operating target. The federal funds rate averaged around 15 percent in the second half of October, but most recently fed funds have traded around 13-1/2 percent, more than 1-1/2 percentage points higher than in early October. Treasury bill rates have climbed, on balance, around 1-1/4 percentage points for 3- and 6-month maturities, while commercial paper yields have increased by much larger amounts. Commercial banks have raised the prime rate to 15-1/2 percent. Responding to the pressures associated with both the rise in short-term rates and concerns about further tightening actions, long-term yields also have moved substantially higher. Bond yields have climbed 3/4 to 1-1/4 percentage points since early October, and average rates on new home-mortgage commitments have risen by 1-1/2 percentage points. Stock prices generally have declined 8 to 10 percent.

Financial markets were very unsettled in the period immediately following the October 6 announcement. The sharp increases in interest rates, uncertainties about future interest rate movements, and the System's new operating procedures made many security dealers reluctant to take positions. Bid-asked and underwriting spreads widened, and prices were exceptionally volatile on relatively thin trading in most markets. Investor caution was evidenced by substantially wider risk premia, and a large number of scheduled

SELECTED FINANCIAL MARKET QUOTATIONS
(percent)

	1974 High 1/	1978 Jan.4 1/	1979 Jan.3 1/	1979 2/ FOMC Oct. 5	1979 2/ Oct. 23	1979 2/ Nov. 13	Change from: Oct. FOMC	Change from: Oct. 23
Short-term rates								
Federal funds 1/	13.55	6.69	10.59	11.91	15.14	13.46p	1.55	-1.68
Treasury bills								
1-month	9.88	5.81	8.93	10.40	12.60	12.32	1.92	-.28
3-month	9.63	6.16	9.30	10.70	13.01	12.06	1.36	-.95
6-month	9.75	6.45	9.49	10.63	12.76	11.90	1.27	-.86
1-year	9.54	6.55	9.68	10.28	12.19	11.06	.78	-1.13
Commercial paper								
1-month	12.25	6.62	10.32	11.73	13.91	13.94	2.21	.03
3-month	12.25	6.68	10.57	11.86	14.13	14.02	2.16	-.11
6-month	12.00	6.70	10.62	11.84	14.14	13.61	1.77	-.53
Large negotiable CDs 3/								
1-month	12.58	6.62	10.37	12.09	14.51	13.79	1.70	-.72
3-month	12.64	6.76	10.93	12.50	14.89	13.96	1.46	-.93
6-month	12.30	7.01	11.51	12.80	15.07	13.93	1.13	-1.14
Eurodollar deposit 1/								
1-month	13.78	6.89	11.14	12.45	14.74	14.58	2.13	-.16
3-month	14.01	7.25	11.81	12.79	15.14	15.43	2.64	.29
Bank prime rate	12.00	7.75	11.75	13.50	15.00	15.50	2.00	.50
Intermediate- and long-term rates								
U.S. Treasury (constant maturity)								
3-year	8.84	7.38	9.61	10.01	11.98	11.02	1.01	-.96
7-year	8.52	7.72	9.23	9.67	11.19	10.75	1.08	-.44
20-year	8.69	8.00	9.00	9.44	10.44	10.39	.95	-.05
Municipal (Bond Buyer) 4/	7.15	5.64	6.58	6.64	7.18	7.27	.63	.09
Corporate Aaa								
New issue 5/	10.61	--	--	10.22	11.05	11.50p	1.28	.45
Recently offered 6/	10.52	8.48	9.51	10.25	11.00	11.46p	1.21	.46
Primary conventional mortgages 6/	10.03	9.00	10.38	11.35	11.75	12.85	1.50	1.10
	1974 Low 7/	**1978 Jan.6 7/**	**1979 Jan.5 7/**	**FOMC Oct. 5**	**Oct. 23**	**Nov. 13**	**Oct. FOMC**	**Oct. 23**
Stock prices								
Dow-Jones Industrial	577.60	807.43	821.42	897.61	806.83	814.08	-83.53	7.25
NYSE Composite	32.89	51.34	54.74	63.39	56.70	58.59	-4.80	1.89
AMEX Composite	58.26	125.20	154.98	235.15	195.76	213.33	-21.82	17.57
NASDAQ (OTC)	54.87	103.13	119.92	152.29	132.61	137.14	-15.15	4.53

1/ Daily averages for statement week except where noted.
2/ One-day quotes except as noted.
3/ Secondary market.
4/ One-day quotes for preceding Thursday.
5/ Averages for preceding week.
6/ One-day quotes for preceding Friday.
7/ Calendar week averages.

corporate and municipal security offerings were postponed. Market conditions improved somewhat in late October and early November, however, when revised data showed a slowing in the growth of the monetary aggregates.

M-1 grew at a 2-1/2 percent annual rate in October, a sharp fall-off from September's 11-1/4 percent increase. The slowdown in M-1 also caused a moderation in M-2 expansion. Growth in the interest-bearing component of this aggregate was unchanged from September's rate, as rapid outflows from savings accounts were offset by stronger flows into both small and large time deposits included in M-2. Deposit flows at nonbank thrift institutions weakened, contributing to a deceleration of M-3 growth.

Aggregate credit flows appear to have contracted in October, reflecting the sharply higher interest rates, unsettled market conditions, and declining economic activity. Business borrowing at commercial banks and in the commercial paper market moderated in October, while longer-term security offerings were about unchanged from the previous month's pace. Household borrowing likely decreased also; consumer credit expansion probably eased off with the drop in auto purchases, and mortgage market borrowing was discouraged both by sharply higher interest rates and by reduced availability of funds at many lenders. The cancellation of several short-term financings reduced gross credit demands of state and local borrowing units, but federal government borrowing picked up.

Monetary Aggregates and Bank Credit

The cumulative impact of recent increases in interest rates, both before and after the System's October 6 announcement, and the apparent slackening in overall economic activity probably accounted for the sharp slowdown in M-1 growth in October and early November. Diversion of demand deposits

MONETARY AGGREGATES
(Seasonally adjusted annual rates of growth) 1/

	1978 QIII	1978 QIV	1979 QI	1979 QII	1979 QIII	1979 Sept.	1979 Oct.e	Oct. '78 to Oct. '79e
Major monetary aggregates								
1. M-1	7.9	4.1	-2.1	7.6	9.7	11.2	2.5	4.8
2. Currency	9.6	10.6	9.1	8.1	11.1	13.9	5.7	9.9
3. Demand deposits	7.3	1.7	-6.2	7.5	9.2	10.2	1.3	3.0
4. M-2	9.8	7.6	1.8	8.6	12.0	12.2	8.6	7.9
5. M-3	10.3	9.3	4.7	7.9	10.5	10.9	7.5	8.0
Bank time and savings deposits								
6. Total	11.3	12.3	8.4	1.2	9.0	15.1	16.6	8.9
7. Other than large negotiable CDs at weekly reporting banks	11.0	10.2	4.5	9.3	13.6	12.9	12.8	10.0
8. Savings deposits	2.9	0.2	-9.6	-3.1	5.5	0.0	-16.9	-3.7
9. Individuals 2/	4.1	0.0	-9.4	-2.9	6.3	1.2	-15.7	-3.0
10. Other 3/	-10.1	0.0	-13.0	-8.1	-2.7	-8.3	-33.6	-12.0
11. Time deposits	17.9	18.2	15.6	18.5	19.2	21.2	32.0	20.9
12. Small time 4/	12.7	15.8	16.5	36.3	26.9	17.9	28.9	27.3
13. Large time 4/	26.9	22.4	13.6	-12.1	4.5	27.0	38.5	9.6
14. Time and savings deposits subject to rate ceilings (8+12)	6.9	7.0	2.2	15.1	15.9	9.0	6.2	10.1
Deposits at nonbank thrift institutions 5/								
15. Total	11.1	11.6	8.8	6.8	8.4	8.9	6.0	8.3
16. Savings and loan associations	12.3	13.1	11.3	7.8	9.2	10.0	7.6	9.8
17. Mutual savings banks	6.8	7.8	4.6	3.1	2.2	4.2	1.7	3.4
18. Credit unions	13.7	10.1	0.8	8.3	19.3	12.7	4.2	9.5
MEMORANDA: Monthly changes in billions of $								
19. Total U.S. govt. deposits 6/	1.1	-0.4	-2.0	1.5	0.7	-0.1	-0.1	-0.4
20. Total large time deposits 7/	2.9	4.7	1.3	-6.3	2.5	4.6	6.5	1.0
21. Nondeposit funds	1.6	2.2	5.3	5.0	5.6	2.1	n.a.	n.a.
22. Other 8/	0.9	1.6	2.0	1.2	1.5	-3.8	n.a.	n.a.
23. Net due to related foreign institutions	0.7	0.6	3.3	3.7	4.0	5.8	n.a.	n.a.

e--estimated. n.a.--not available.
1/ Quarterly growth rates are computed on a quarterly average basis.
2/ Savings deposits held by individuals and nonprofit organizations.
3/ Savings deposits of business, government, and others, not seasonally adjusted.
4/ Small time deposits are time deposits in denominations less than $100,000. Large time deposits are time deposits in denominations of $100,000 and above excluding negotiable CDs at weekly reporting banks.
5/ Growth rates computed from monthly levels are based on average of current and preceding end-of-month data.
6/ Includes Treasury demand deposits at commercial banks and Federal Reserve Banks and Treasury note balances.
7/ All large time certificates, negotiable and nonnegotiable, at all CBs.
8/ Other nondeposit borrowings of commercial banks from nonbank sources include Federal funds purchased and security RPs plus other liabilities for borrowed money (including borrowings from the Federal Reserve), and loans sold, less interbank borrowings.

into ATS and New York NOW accounts is estimated to have reduced M-1 growth by only 1/4 percentage point in October, about the same as in September.

M-2 expansion slowed to an 8-1/2 percent annual rate in October, down from 12-1/4 percent in the previous month. Savings deposits at commercial banks contracted at a record pace, as market interest rates reached unprecedented levels. The publicity surrounding the rise in rates undoubtedly enhanced awareness of the opportunity cost of holding liquid assets in savings accounts. Offsetting the runoff in savings accounts, however, was an acceleration in the small and large time deposit components of M-2. Small time deposits grew at their fastest pace since June, likely reflecting larger net inflows to record yielding MMCs.

Deposit inflows at nonbank thrift institutions weakened noticeably in October and left M-3 growth at a 7-1/2 percent annual rate, the slowest since May. MMCs and large CDs evidently continued to account for the growth in deposits at S&Ls in October. MMCs outstanding increased $14 billion (NSA), and at month end accounted for 24.6 percent of total S&L deposits outstanding. Information available from a sample of S&Ls suggests that passbook deposits declined appreciably in October, following the 26 percent (SAAR) runoff of these accounts in September, and that small time deposits other than MMCs also fell again last month. A portion of the latter decline is attributable to early withdrawals from existing accounts, as it became profitable for more savers to accept premature withdrawal penalties and reinvest at higher prevailing yields.

Accompanying the reduced growth in October of deposits subject to fixed ceilings at banks and thrifts was a pickup in the flow of funds into alternative short-term investment outlets. Money market mutual fund shares increased by $3.9 billion (NSA), the second largest monthly increase on record and nearly twice the gain in September. Short-term unit investment trust assets outstanding rose $1.4 billion in October, $200 million more than in the previous month. In addition, noncompetitive tenders at 3- and 6-month Treasury bill auctions were strong in October and in early November.

With the slowing of inflows to demand deposits and interest-bearing accounts subject to rate ceilings, commercial banks had to increase their reliance on managed liabilities in October to finance the expansion of bank credit. Large time deposits rose by $6.5 billion, a sizable pickup from the strong $4.6 billion gain in September. RP agreements with the nonbank public expanded a further $1.9 billion. Net Eurodollar borrowings by member banks from their foreign branches declined by $1.6 billion in October, but net of weekend transactions it appears that member banks stepped up their reliance on this source of funds.[1] Conversations with representatives of large banks suggest two explanations for the October strength in managed liabilities in the face of newly imposed marginal reserve requirements. First, many banks contend that they were not able to select and implement new liability management strategies until the latter part of the month. Second, some banks stepped up their use of managed liabilities in mid-October to compensate for a temporary decline in nonreservable Treasury note balances.

Required reserves expanded at an 18-1/4 percent annual rate (SA) in October, up from 12-1/2 percent in September (see table on page III-7).[2] Average excess reserves were somewhat larger in October than in the previous

1/ Increased volatility in the federal funds market since October 6 seems to have discouraged weekend Eurodollar transactions by large member banks. These banks had been using the transactions regularly to increase their cash items deductions and thereby to decrease their reservable deposits.
2/ The new marginal reserve requirements resulted in required reserves of $356 million in the week ending October 31. Growth rates of reserve measures are not affected since they are adjusted to remove discontinuities associated with regulatory changes in reserve requirements.

MEMBER BANK RESERVES

	1979 QI	QII	QIII	Sept.	Oct. p/
Seasonally adjusted annual rates of growth 1/					
1. Required reserves	-2.9	-4.8	6.0	12.5	18.3
2. Total reserves	-3.0	-5.0	6.3	11.5	20.5
3. Nonborrowed reserves	-3.4	-8.8	8.2	4.2	0.9
4. Monetary base	5.6	4.0	9.8	13.7	10.8
Monthly average levels, millions of dollars 2/					
5. Borrowed reserves	989	367	199	1,341	2,024
6. Excess reserves	194	179	208	190	270

1/ Includes required reserves of Edge Act corporations. Reserve series have been adjusted to remove discontinuities associated with regulatory changes in reserve requirement ratios.
2/ Monthly averages are prorated averages of weekly data.
p/ Preliminary.

month, owing in part to a bulge early in the month when banks were highly uncertain about the implications of the October 6 announcement. The growth in nonborrowed reserves was minimal in October, contributing to a relatively wide differential between fed funds and the discount rate over much of the month, and to a substantial boost in discount window borrowings.[1]

Growth of bank credit slowed in October, reflecting a reduced expansion of investments, a slower pace of business lending, and a decline in security loans. Reductions in security holdings by dealers in the face of declining security prices and the increase in borrowing costs likely contributed to the weakness in security loans; also, some banks reportedly pared security loans to meet other borrowers' demands. A sizable portion of the slowing of growth in business loans was due to a large reduction in holdings of bankers acceptances. Excluding changes in acceptances, business lending by banks only decelerated to an 18 percent annual rate in October, slightly slower than the average pace in the first nine months of 1979.

Bank lending policies apparently tightened in October. Reports suggest that standards of credit worthiness were applied more stringently and that some banks became more reluctant to lend to new customers. Below-prime lending at very large banks apparently dropped markedly following the October announcement; the elimination of certain reserve-free managed liabilities probably has discouraged these lending practices. There is also some indication

1/ A spread between rates on reservable and nonreservable fed funds and RPs emerged in mid-October. Although initially much wider, it averaged between 25 and 50 basis points over the second half of the month.

COMMERCIAL BANK CREDIT
(Per cent changes at annual rates, based on seasonally adjusted data) 1/

		1978		1979					12 months ending
		QIII	QIV	QIP	QIIP	QIIIP	Sept.p	Oct.e	Oct.e
1.	Total loans and investments 2/	13.3	12.7	13.3	11.9	15.8	21.7	8.0	13.5
2.	Investments	6.4	-1.8	7.6	5.4	8.5	14.2	6.4	5.3
3.	Treasury securities	1.2	-21.1	2.1	3.8	1.7	14.0	2.5	-2.8
4.	Other securities	9.4	9.5	10.5	6.2	12.1	14.2	8.3	10.0
5.	Total loans 2/	15.9	18.2	15.2	14.2	18.2	24.2	8.5	16.6
6.	Business loans	12.7	14.2	20.5	16.6	22.7	25.9	14.1	19.5
7.	Security loans	-16.7	-23.3	33.0	38.1	8.7	26.1	-137.9	6.1
8.	Real estate loans	20.4	17.7	14.6	13.0	14.7	14.5	15.9	15.7
9.	Consumer loans	17.9	15.9	16.3	12.4	7.5	9.4	n.a.	n.a.
	MEMORANDA:								
10.	Business loans net of bankers acceptances	12.6	14.4	20.4	16.6	21.7	24.0	18.0	19.6
11.	Commercial paper issued by nonfinancial firms 3/	23.1	17.5	33.5	65.7	69.7	48.5	12.7	51.3
12.	Sum of items 6 & 11	13.3	14.2	21.4	20.2	26.5	27.9	14.0	21.8
13.	Finance company loans to business 4/	5.5	25.0	16.6	17.7	9.4	-15.3	n.a.	n.a.
14.	Sum of items 12 and 13	11.8	16.3	20.6	19.7	23.3	19.9	n.a.	n.a.

e--estimated. p--preliminary. n.a.--not available.

1/ Average of Wednesdays for domestic chartered banks and average of current and preceding ends of months for foreign-related institutions.

2/ Loans include outstanding amounts of loans reported as sold outright to a bank's own foreign branches, unconsolidated nonbank affiliates of the bank, the bank's holding company (if not a bank), and unconsolidated nonbank subsidiaries of the holding company.

3/ Average of Wednesdays.

4/ Based on average of current and preceding ends of months.

of loan rate concessions for smaller businesses that are less able to absorb higher interest charges.

Business Sector Finance

The overall slowdown in business loan growth in October was concentrated at large banks, and it was accompanied by a more moderate issuance of nonfinancial commercial paper.[1] The sharp increase in commercial paper interest rates and the widening spread between quality ratings probably accounted for the more modest rise. Paper dealers also report that investors exhibited a strong preference for shorter maturities.

Public offerings of corporate bonds have diminished since October 6. For the month as a whole, the volume of new issues rose slightly to $2.45 billion (SA), but $1 billion of this total was attributable to an I.B.M. note and bond financing that was brought to market just before October 6; underwriters suffered large losses on the I.B.M. and several smaller issues that were still in syndicate at the time of the Fed's policy announcement. Eighteen debt financings amounting to $650 million, mostly by lower-rated concerns, were cancelled or postponed in October.

Yields on prime-rated corporate bonds have climbed 1 to 1-1/4 percentage points since October 6. The Board's index of recently offered bonds (Aaa-rated, utility basis) rose to 11.46 percent in early November, about 70 basis points above its previous all-time high in October 1974. Risk premia have increased sharply since October 6, despite some decline late in the month. For example, A-rated utility bonds currently yield 100 basis points

1/ Business loans at finance companies declined $800 million in September. This decline is attributable to a $1.3 billion runoff in wholesale auto loans reflecting the delayed introduction of 1980 models by the major auto manufacturers.

GROSS OFFERINGS OF CORPORATE AND FOREIGN SECURITIES
(Monthly totals or monthly averages, in millions of dollars)

	1978	1979					
	Year	HI	QIII	Sept.p/	Oct.p/	Nov.f/	Dec.f/
			Seasonally adjusted				
Corporate securities--total	3,936	4,335	4,250	4,000	4,075	3,250	3,600
Publicly offered bonds	1,651	2,125	2,325	2,300	2,450	1,450	2,000
Privately placed bonds	1,422	1,555	900	1,000	1,000	1,000	1,000
Stocks	863	655	1,025	700	625	800	600
			Not seasonally adjusted				
Publicly offered bonds--total	1,651	2,280	2,025	2,000	2,650	1,500	1,700
By quality 1/							
Aaa and Aa	853	1,225	1,250	1,025	1,550	--	--
Less than Aa 2/	798	1,055	800	975	1,100	--	--
By type of borrower							
Utility	610	700	575	750	1,265	--	--
Industrial 3/	526	635	825	950	1,310	--	--
Financial	515	945	550	300	75	--	--
Foreign securities--total 4/	504	408	491	890	275	300	300

1/ Bonds categorized according to Moody's bond ratings.
2/ Includes issues not rated by Moody's.
3/ Includes equipment trust certificates.
4/ Includes both publicly offered and privately placed issues.
p/ Preliminary.
f/ Forecast.

more than Aaa-rated issues; this spread averaged 55 basis points in September and climbed to a record 174 basis points in mid-October (see chart on page III-13).

Stock prices declined sharply following the October 6 announcement, reflecting investor concern that higher interest rates and reduced credit availability will detract significantly from economic activity and corporate profits over coming quarters. The fall in stock values prompted several corporations to postpone or cancel scheduled equity offerings. The number of margin calls increased substantially, but the volume of such calls was less than that associated with the market plunge in October 1978, partly because a rapid build-up in customer equity occurred as stock prices reached their highs for the year just prior to October 6. Moreover, representatives of major brokerage firms indicate that there has not been a notable increase in the proportion of calls met by forced selling. Reportedly, many margin account customers have voluntarily liquidated some or all of their stockholdings because of the recent sharp increase in the cost of such borrowing.[1] Margin credit outstanding fell by $690 million during October, to $11.3 billion.

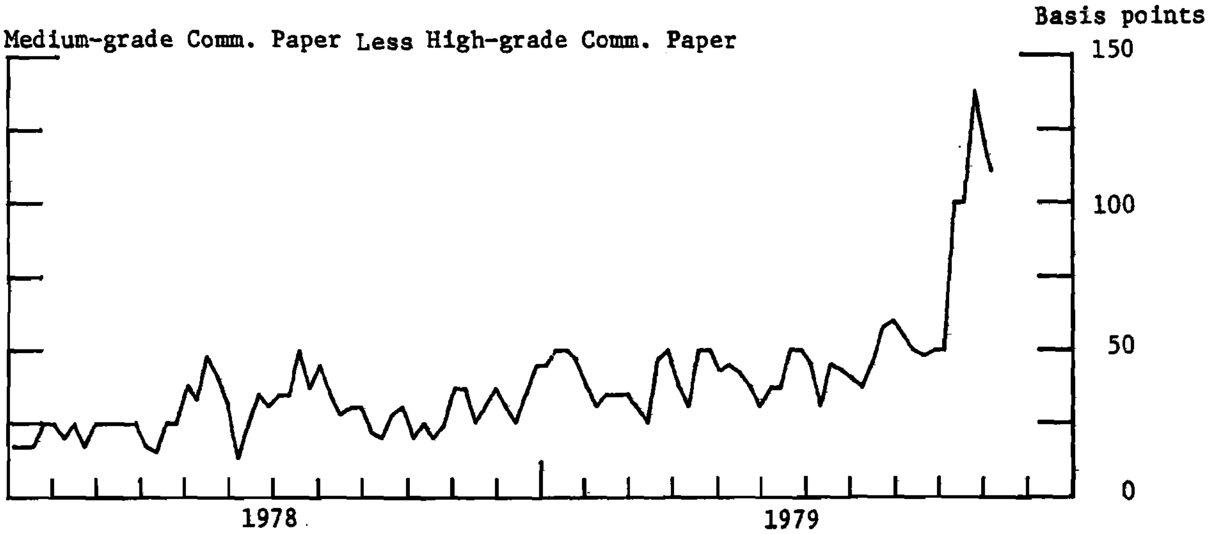
Government Debt Markets

As in other markets, the sharp upward movement in interest rates on U.S. government securities following the October 6 announcement was accompanied by a substantial increase in day-to-day and intra-day rate volatility. Single-day fluctuations in Treasury bill rates of 25 or more basis points and changes in long-term bond yields of 10 to 20 basis points were common, and bid-asked

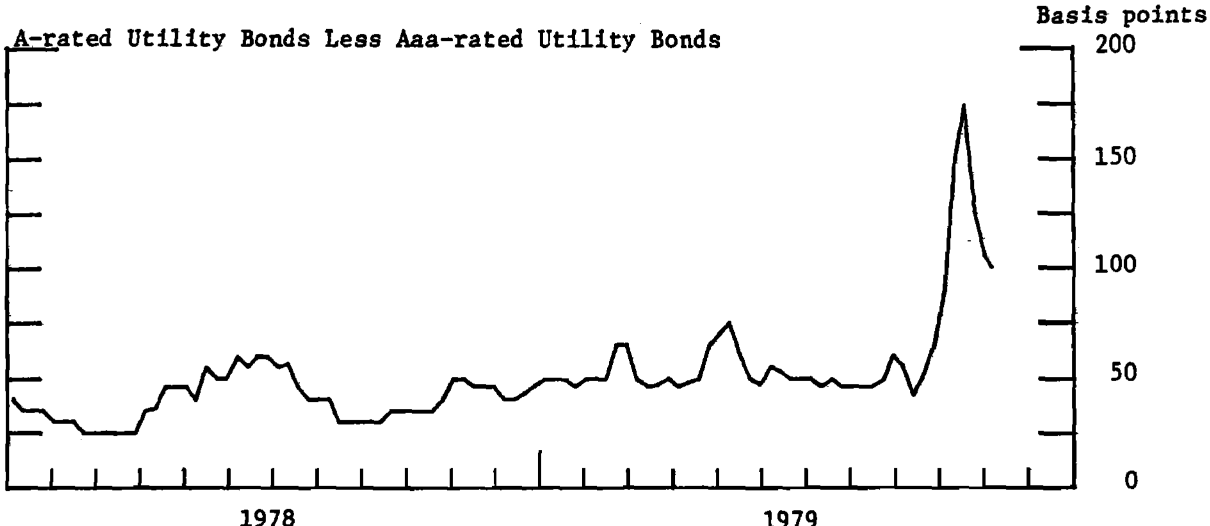
1/ The interest rate charged by most brokerage firms for margin accounts usually is set at 1 to 2-1/2 percentage points above the "call money" loan rate. As a result, margin account customers are typically paying 16 to 18-1/2 percent on their current borrowings.

SELECTED MEASURES OF RISK PREMIA
(Weekly)

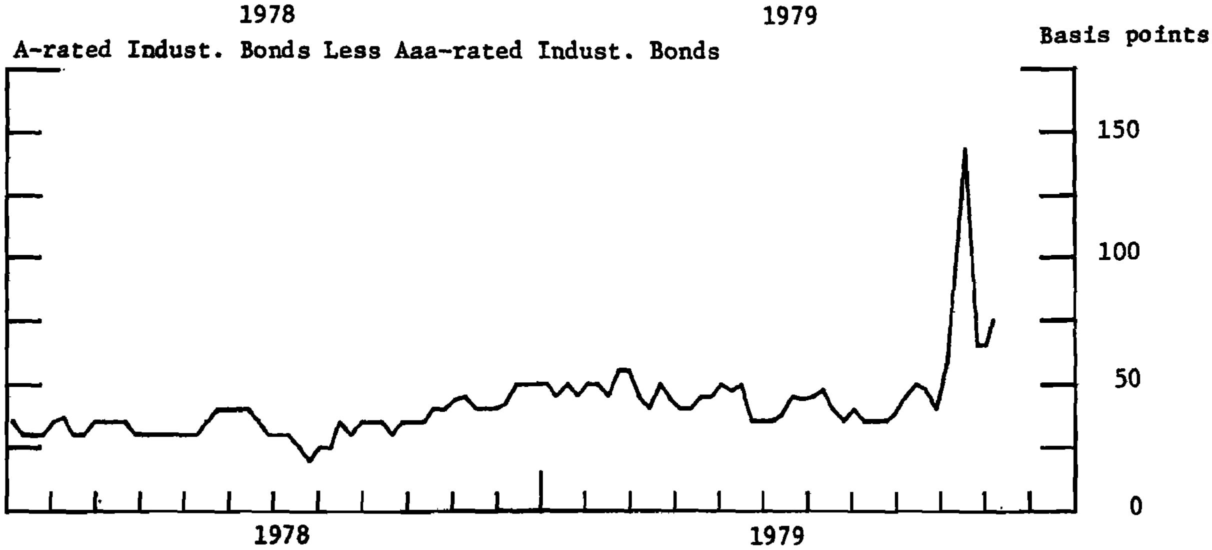
Medium-grade Comm. Paper Less High-grade Comm. Paper



A-rated Utility Bonds Less Aaa-rated Utility Bonds



A-rated Indust. Bonds Less Aaa-rated Indust. Bonds



Latest data shown: November 9, 1979.

spreads on Treasury bills widened.[1] Since the publication of revised data for the monetary aggregates in late October and more recent information suggesting a deceleration in their rates of growth, most Treasury security interest rates have retraced a portion of the recent sizable increases.

On the whole, primary government securities dealers appear to have fared satisfactorily since the October 6 announcement, and there are no reports of dealers experiencing portfolio losses that might threaten their viability. Dealers that regularly report their holdings to the System apparently suffered capital losses from net long positions in bills, but these were offset by gains on net short positions in coupon issues (these firms currently do not report their futures and forward market positions).

The Treasury raised $1.4 billion (NSA) of net new money in its three-part quarterly financing package in late October. In addition, the Treasury raised $1.5 billion with 15-year bonds, added about $700 million to the outstanding supply of bills through its weekly auctions, and sold $2 billion of 167-day cash management bills in early November.[2] Foreign official holdings of bills have declined about $5.5 billion since early October, in part reflecting the increase in the foreign exchange value of the dollar.

1/ Exchange-traded financial futures displayed substantial volatility as well, and on several occasions reached previously established single-day trading limitations: 50 basis points on bill futures (IMM) and one full point on bond futures (CBOT). As a result, the CBOT doubled its one-day limit on bond futures prices and both exchanges raised initial and maintenance margin requirements.

2/ The Treasury sold about $1.1 billion of mark-denominated 2-1/2- and 3-1/2-year notes in Germany in early November. The Treasury warehoused the proceeds of these offerings with the System, thereby reducing its need for other borrowing to cover the Federal deficit.

GOVERNMENT SECURITY OFFERINGS
(Monthly totals or monthly averages, in millions of dollars)

	1978	1979					
	Year	H1	QIII e/	Sept. e/	Oct. e/	Nov. f/	Dec. f/
			Seasonally adjusted				
State and local government securities, gross offerings							
Total	5,851	5,087	5,478	5,185	4,670	5,100	4,700
Long-term	4,042	3,367	3,566	3,150	4,250	3,400	3,200
Short-term	1,809	1,720	1,912	2,035	420	1,700	1,500
U.S. government securities, net offerings							
U.S. Treasury 1/	2,337	3,278	1,688	-979	1,372	8,245	-1,488
Sponsored agencies	1,930	2,219	734	130	3,184	2,886	2,661
			Not seasonally adjusted				
State and local government securities, gross offerings							
Total	5,851	5,409	5,246	5,250	4,500	5,000	3,800
Long-term	4,042	3,527	3,362	2,700	4,200	3,400	2,600
Short-term	1,809	1,882	1,884	2,550	300	1,600	1,200
U.S. government securities, net offerings							
U.S. Treasury 1/	2,337	1,966	2,168	-1,400	3,520	10,200	700
Sponsored agencies	1,930	2,090	1,308	1,091	3,474	2,500	2,100

1/ Marketable issues only.
e/ Estimated.
f/ Forecasted.

Borrowing by federally sponsored credit agencies increased to $3.2 billion (SA) in October, more than four times the pace of the third quarter. The housing agencies raised an increased volume of funds with which to support the mortgage market, and the Farm Credit System responded to enlarged agricultural credit demands associated with sizable grain harvests.

State and local government security market conditions also were unsettled following the October 6 announcement. With short- and long-term yields climbing as much as one percentage point, large losses on syndicate and dealer positions were widely reported. Secondary market trading was thin, and $1.8 billion of scheduled issues were cancelled or postponed. Short-term note offerings fell sharply, as interest rate ceilings forced a number of cancellations.[1] Ceilings were a less significant factor for long-term offerings, and these totaled $4.25 billion (SA) in October, one of the largest totals thus far this year.

Mortgage Markets

Mortgage market conditions have tightened substantially since the System's October 6 policy actions. For example, average interest rates at sampled S&Ls on new commitments for 80 percent conventional home mortgages have risen 1-1/2 percentage points to 12.85 percent. At this level, usury ceilings have become more binding for certain lenders in nearly two dozen states. Secondary market yields on mortgage instruments also have climbed

1/ Over three-fourths of the cancellations were HUD housing project notes. HUD first raised and then abandoned its self-imposed interest rate ceiling on such project notes, but the agency still rejected all bids at its most recent auction on the grounds that the interest rates were excessive.

INTEREST RATES AND SUPPLY OF MORTGAGE FUNDS
AT SELECTED S&Ls

Period	Conventional home mortgages: Average rate on new commitments for 80% loans (percent)	Basis point change from month or week earlier	Spread (basis points) 1/	Percent of S&Ls with mortgage funds in short supply 2/
1979--High	12.85	—	+172	88
Low	10.38	—	+64	54
1979--June	11.04	+35	+154	79
July	11.09	+5	+157	75
Aug.	11.09	0	+160	77
Sept. 7	11.20	+7	+150	78
14	11.30	+10	+143	86
21	11.35	+5	+143	84
28	11.35	0	+138	82
Oct. 5	11.35	0	+116	82
12	11.45	+10	+66	83
19	11.75	+30	+75	84
26	12.00	+25	+64	84
Nov. 2	12.80	+80	+138	85
9	12.85	+5	+139	88

1/ Average mortgage rate minus average yield on recently offered Aaa utility bonds.
2/ Percent reporting supply of funds slightly or substantially below normal seasonal patterns.

SECONDARY HOME MORTGAGE MARKET ACTIVITY

Period	FNMA auctions of forward purchase commitments: Conventional: Amount ($ millions) Offered	Conventional: Amount ($ millions) Accepted	Conventional: Yield to FNMA 1/	Government-underwritten: Amount ($ millions) Offered	Government-underwritten: Amount ($ millions) Accepted	Government-underwritten: Yield to FNMA 1/	Yields on GNMA-guaranteed mortgage-backed securities for immediate delivery 2/
1979--High	454	172	13.80	1,035	448	13.29	11.77
Low	36	28	10.92	37	19	10.42	9.51
1979--Oct. 1	195	127	11.99	891	361	11.66	10.65
9							11.02
15	401	166	12.75	1,017	448	12.60	11.21
22							11.77
29	454	139	13.80	1,035	321	13.29	11.58
Nov. 5							11.73
13							11.51

1/ Average gross yield before deducting fee of 38 basis points for mortgage servicing. Data, based on 4-month FNMA purchase commitments, reflect the average accepted bid yield for home mortgages, assuming a prepayment period of 12 years for 30-year loan without special adjustment for FNMA commitment fees and related stock requirements. Mortgage amounts offered by bidders relate to total eligible bids received.
2/ Average net yields to investors assuming prepayment in 12 years on pools of 30-year FHA-VA mortgages carrying the prevailing ceiling rate on such loans.

sharply since early October. Yields on pass-through securities have risen, on balance, about one percentage point.[1]

A special FHLBB survey of 125 large S&Ls in late October indicated that a substantial and widespread firming of nonrate terms on home mortgage commitments also occurred after October 6. Nearly one-fourth of the surveyed S&Ls stopped making new commitments, and an additional one-half ceased issuing commitments for certain types of loans or borrowers. About one-fifth of respondents stopped making firm-rate commitments, and one-fifth increased downpayment requirements (generally to 25 percent or more). In terms of new commitment activity, three-fourths of surveyed S&Ls reported that the volume of commitments made during the 15 days ending October 26 was substantially smaller than during the same period last year; this is more than double the proportion reporting a cutback in activity before October 6.

In September, net mortgage acquisitions at S&Ls remained at a relatively weak $3.5 billion pace but outstanding mortgage commitments increased by about $1 billion to $32.8 billion (SA). Confronted with weaker deposit flows in October, S&Ls stepped up their reliance on FHLBs to meet existing mortgage commitments. Outstanding FHLB advances increased by $1.7 billion (SA) in October, more than double the September rise and one of the biggest net changes since April 1978.

To help relieve pressure on member institutions and on the residential mortgage markets, the FHLBB agreed in October on a proposed rule to ease

1/ GNMA dealers apparently have been reluctant to issue commitments to purchase or sell loans for delayed delivery. The recent volatility of the GNMA market, as well as heightened concern about the willingness and ability of some market participants to follow through on their commitments have contributed to these conditions. More dealers have enacted or boosted margin requirements on forward delivery transactions.

restrictions on outside borrowings.[1] The FHLBB also indicated that it intends to maintain a policy of assisting member associations in meeting net deposit withdrawals and current loan commitments, but district FHLBs are closely reviewing requests for advances to finance new commitments for housing. In addition, effective November 1, the minimum liquidity requirement for insured S&Ls was lowered from 6 to 5-1/2 percent; the industry average liquidity ratio at the end of September was 9.1 percent (SA), well above the 1974 low of 7.6 percent. FHLBs will probably continue to encourage S&Ls to reduce liquidity before coming to the advances window.

The recent sharp increase in short-term interest rates has widened the unfavorable spread for warehousing mortgage loans, thereby contributing to a lower level of loan origination activity at mortgage companies. With mortgage bankers acting to hedge against exceptional uncertainties, bidding in FNMA's forward commitment auctions has been extremely heavy and resulted in cumulative increases of 163 and 181 basis points for FHA/VA and conventional loans, respectively. Construction financing also has become much more costly, and less readily available in numerous areas. In response to the increase in mortgage yields and tightened mortgage market conditions, the ceiling rate on FHA/VA home loans was boosted--effective October 26--from 10-1/2 to 11-1/2 percent. Even so, discounts averaged more than 10 points in FNMA's October 29 commitment auction.

1/ Insured S&Ls currently are allowed to borrow an amount equal to as much as 10 percent of deposits from outside sources; these include security RPs, bank loans, and commercial paper. The limitation is 15 percent when mortgage-backed bonds are included. The proposed rule would increase the maximum outside borrowing to 20 percent of assets.

Consumer Credit

A surge in automobile lending and a large increase in revolving credit balances caused the growth of consumer installment credit to accelerate in September. For the third quarter as a whole, however, growth slowed to a 13 percent annual rate versus 15 percent in the first six months of the year. Adjusted for inflation, consumer credit expanded only slightly in the first half of 1979 and declined in the third quarter. This pattern is similar to the early months of the last two economic contractions (see chart on page III-22). Delinquency rates at commercial banks rose to 2.50 percent in the third quarter, the highest quarterly level in four years.

In October, consumer credit flows reportedly were affected by a general tightening in nonrate terms, as some lenders adopted more stringent loan approval criteria, confined loans to established customers, raised downpayments, and shortened maturities. Finance rates also were raised in some areas, but increases are precluded by statutory ceilings in many states.[1]

Credit union deposit growth was 12-3/4 percent in September, about in line with the average pace this year. Loan-to-share ratios at these intermediaries continued to increase, and credit union liquidity declined further. The Central Liquidity Fund (CLF), managed by the NCUA and owned by its member credit unions, began operating on October 1. The maximum borrowing capacity of the CLF is 12 times its subscribed capital stock and surplus, and it will borrow initially through the Federal Financing Bank. After about one month of operation, the CLF's legal borrowing limit was only about $150 million. It will likely be several more months before the CLF acquires enough capital to meet any substantial liquidity demands from credit unions.

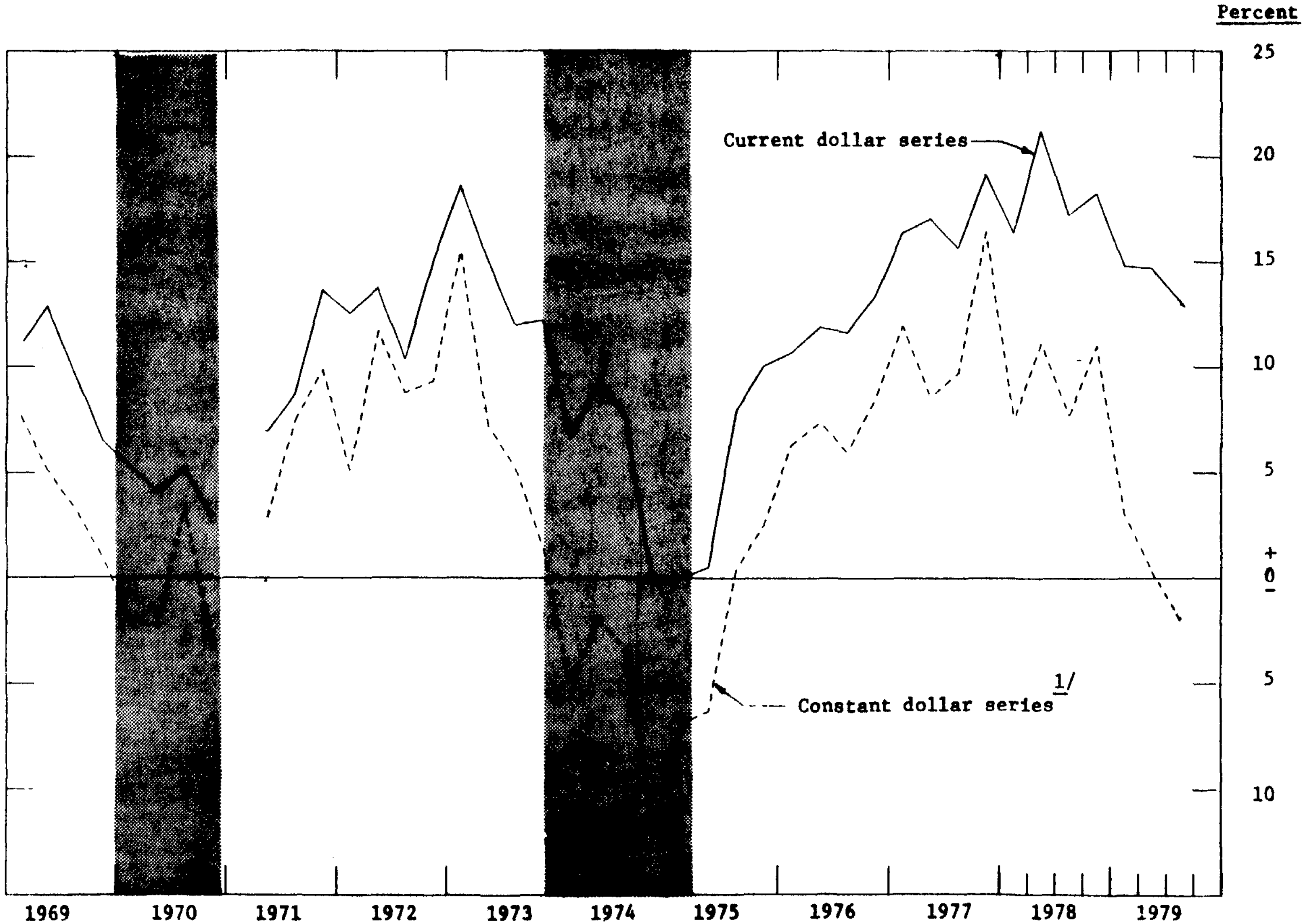
1/ The maximum new-car loan rate is currently below the bank prime lending rate in 31 states.

CONSUMER INSTALLMENT CREDIT 1/

	1977	1978	1979 QI	1979 QII	1979 QIII	1979 Aug.	1979 Sept.
Total							
Change in outstandings							
Billions of dollars	35.3	44.8	41.0	39.9	37.3	29.4	53.4
Percent	18.2	19.4	15.0	14.1	12.8	10.0	18.0
Bank share (percent)	52.9	53.1	43.1	47.8	32.7	35.4	34.2
Extensions							
Billions of dollars	254.1	298.3	314.1	324.2	332.3	331.0	343.6
Bank share (percent)	46.4	47.8	47.1	47.9	45.9	46.0	46.0
Liquidations							
Billions of dollars	218.8	253.5	273.1	284.3	294.9	301.6	290.3
Ratio to disposable income	16.8	17.5	17.4	17.7	18.0	18.3	17.6
Delinquency rate at banks							
30 days or more (percent)	2.37	2.41	2.25	2.42	2.50	2.47	2.59
Automobile Credit							
Change in outstandings							
Billions of dollars	15.2	19.6	18.9	13.2	12.1	7.1	21.9
Percent	22.5	23.6	18.5	12.3	11.0	6.4	19.6
Extensions							
Billions of dollars	75.6	89.0	92.4	93.7	94.2	92.0	101.2

1/ Quarterly and monthly dollar figures and related percent changes are seasonally adjusted annual rates.

CONSUMER INSTALLMENT CREDIT GROWTH RATES
(Seasonally adjusted annual rates)



* Series break due to inclusion of gasoline companies.
1/ Deflated by consumer price index.

Foreign exchange markets. Exchange market reactions to the October 6 measures were generally favorable for the dollar. From its low reached at the beginning of October through November 13 the value of the dollar on a weighted-average basis rose about 4 percent, first in anticipation of, and then in reaction to, the Federal Reserve's actions. The dollar rose against all major foreign currencies, with the yen under considerable downward pressure, and the pound declining in late October.

In early November exchange markets have focussed on developments in Iran; there was little net impact on the dollar, but the vulnerability of Japan to potential oil price developments led to a further weakening of the yen, while the virtual self-sufficiency of the U.K. in oil brought some recovery of the pound. The decision on November 14 to freeze all Iranian assets in U.S. banks generated further uncertainties in exchange markets with some downward pressure on the dollar.

The depreciation of the yen against the dollar since October 6 (and since the beginning of October) has been more than 8-1/2 percent and over 25 percent since the beginning of the year. During the past five weeks, as uncertainties associated with the oil situation and the Japanese elections weakened the yen, the Bank of Japan raised its discount rate one percentage point

The U.K. pound has declined 4 percent on balance since early October, with the recovery in early November offsetting much of the earlier losses. The primary source of downward pressure on the pound was the lifting on

October 24 of all exchange controls on U.K. residents' foreign exchange transactions

•

Since the beginning of October, several central banks have raised their discount rates and tightened money market conditions, citing concern over inflationary developments at home and worldwide. With the recent relative weakness of the Swiss franc against the mark, the Swiss National Bank not only raised its discount rates, but also reduced its negative interest charges on deposits held by foreigners from 10 percent to 2-1/2 percent per quarter. France also took measures to restrain cerdit expansion. The result of the tightening of monetary policy abroad, was to reduce slightly the differential between U.S. 3-month interest rates and an average of foreign rates, although this differential had widened considerably since the summer and remains over 3-1/2 percentage points.

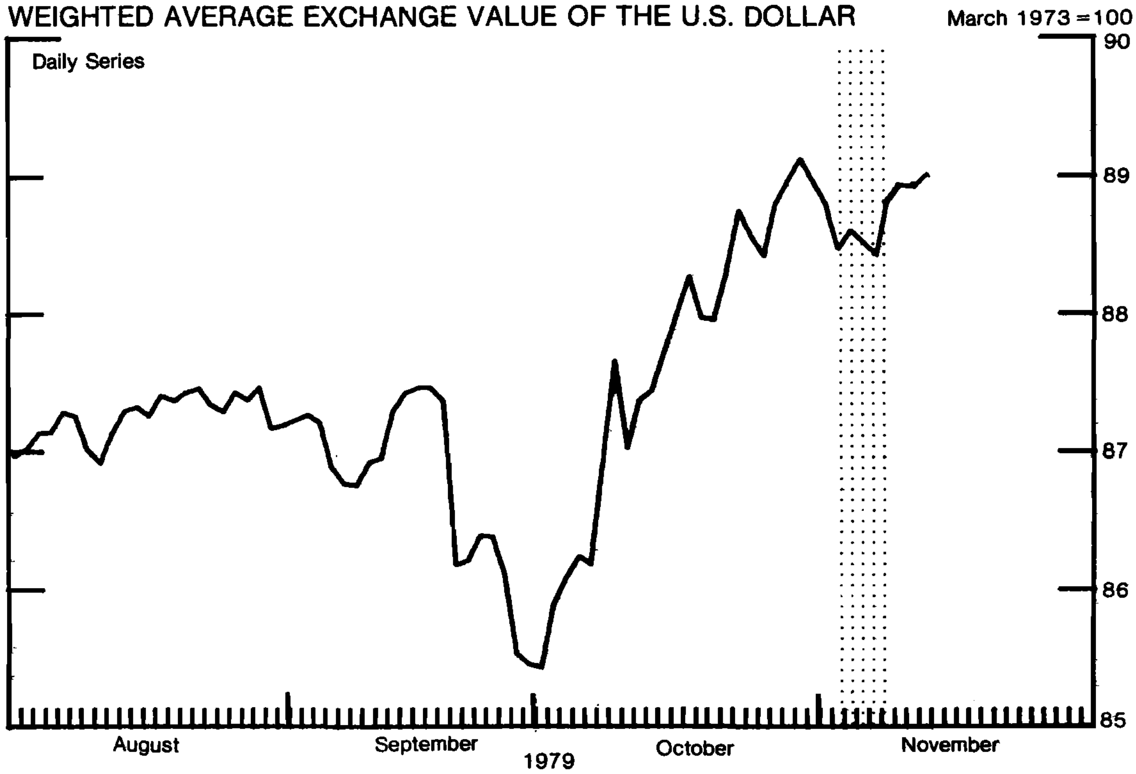
Discount Rates

	Current Rate	Date Effective	Previous Rate	Date Effective
Belgium	10.0	Oct. 4, 1979	9.0	June 13, 1979
United States	12.0	Oct. 8, 1979	11.0	Sept. 18, 1979
Italy	12.0	Oct. 8, 1979	10.5	Sept. 4, 1979
Canada	14.0	Oct. 25, 1979	13.0	Oct. 9, 1979
Germany	6.0	Nov. 1, 1979	5.0	July 13, 1979
Netherlands	8.5	Nov. 1, 1979	8.0	July 13, 1979
Japan	6.25	Nov. 2, 1979	5.25	July 24, 1979
Switzerland	2.0	Nov. 5, 1979	1.5	July 14, 1977

Chart 1

STRICTLY CONFIDENTIAL (FR)
Class II - FOMC
November 13, 1979

WEIGHTED AVERAGE EXCHANGE VALUE OF THE U.S. DOLLAR



Financial market uncertainties prior to the October measures were also reflected in the gold price, which rose spectacularly in late September and reached nearly $450 per ounce around the beginning of October. Thereafter, the speculative burst receded. The price of gold fell below $400 an ounce and tended to remain there, although it fluctuated from day to day over a much greater range than usual. In part the instability in the gold price was related to market participants; uncertainties about future inflation and interest rates, but potential changes in U.S. gold-sales policies also added uncertainty to the marketplace. On October 17, there was a sharp break in the price after the Treasury announced that it was replacing its regular monthly auction of a fixed quantity of gold with auctions at varied times with varied quantities offered. Another sharp decline occurred after the Treasury announced an auction of 1.25 million ounces of gold for November 1.

Since the October 6 FOMC meeting, the System has acquired more than $550 million equivalent of marks and Swiss francs, primarily through correspondents. The System's outstanding swap commitments in marks have been reduced to approxaimately $3.3 billion and the Swiss franc swap drawing was completely repaid. The Treasury acquired a small quantity of marks early in October. On November 5, the U.S. Treasury announced a further issue of DM-denominated securities at 2-1/2 and 3-1/2 year maturities yielding 8.55 and 8.50 percent, respectively. Payment for about DM 2 billion ($1.1 billion) was received on November 12 and the proceeds were warehoused with the System. A further issue of about DM 2 billion will be made in January.

U.S. and Eurodollar market borrowing costs. Since the second quarter of this year the cost of short-term credit to nonbank borrowers has risen more in the Eurodollar market than in the United States, particularly when compared with the cost of bank loans in the United States for borrowers who qualify for the prime rate or rates below prime. The changes in comparative borrowing costs reportedly are inducing some borrowers to try to shift from Eurodollar pricing terms to terms based on the U.S. prime rate. Since the beginning of November differentials between Eurodollar and U.S. interest rates have moved back slightly towards pre-midyear levels.

In the first and second quarters of 1979, the cost to prime nonbank borrowers of 90-day loans from banks in the Eurodollar market was above the cost of financing through commercial paper or bankers acceptances in U.S. financial markets, but was below the cost of bank credit in the United States. The attached table shows costs to prime borrowers of 90-day funds in terms of ranges, reflecting the lack of uniformity in spreads on Eurodollar loans and commercial paper issues, in acceptance commissions, and in compensating balance requirements on U.S. bank loans; the ranges shown are believed to encompass costs faced by most borrowers in each market.

As measured by the midpoints of the ranges, the cost of short-term Eurodollar bank loans in the first half of this year exceeded the cost of issuing commercial paper by about 70-75 basis points, and was also generally higher than the cost of acceptance financing although by a smaller differential. In contrast, Eurodollar credit was considerably

Prime Borrowers' Short-term Borrowing Costs in 1979
(average of daily rates; percent per annum)

90-day borrowing	Average cost range in period				
				Week ending	
	QI	QII	Sept.	Nov. 2	Nov. 9
Eurodollar bank loan: at LIBOR, with spread up to 1/2%	10.99 to 11.49	10.75 to 11.25	12.74 to 13.24	15.76 to 16.26	15.74 to 16.24
U.S.: commercial paper, with dealer spread up to 1/8%	10.43 to 10.56	10.24 to 10.37	12.14 to 12.27	14.90 to 15.03	14.97 to 15.10
U.S.: bankers' acceptances, with commission up to 1%	10.48 to 11.48	10.46 to 11.46	12.22 to 13.22	14.83 to 15.83	14.93 to 15.93
U.S.: bank loan, at prime rate with 5% compensating balances	11.75 to 12.37	11.72 to 12.34	12.90 to 13.58	15.10 to 15.89	15.30 to 16.11
Excess of midpoint of Eurodollar loan range over midpoint of range for:					
Commercial paper	.75	.70	.79	1.05	.95
Bankers acceptances	.26	.04	.27	.68	.56
Bank loan	-.82	-1.03	-.34	.50	.28

Note: Commercial paper and bankers acceptance rates, normally quoted on a bank discount basis, have been converted to investment yield equivalents in computing the borrowing costs shown above.

<u>less</u> costly than borrowing from a bank in the United States, by a margin of about 80-105 basis points. The cost range shown here for the U.S. bank loan is not representative for those borrowers who were able to borrow at rates below the prime rate and who also were not required to hold compensating balances. However, even the upper bound of the Eurodollar loan cost range was below the prime rate itself by 25 to 50 basis points in the first half of this year. That differential suggests that Eurodollar credit was the cheaper source of finance even for the majority of those borrowers who could borrow from a U.S. bank at less than the prime rate.

Since the second quarter, the prinicpal change in borrowing cost differentials has been the greater rise in the cost of Eurodollar credit relative to the cost of credit in U.S. markets in general and at U.S. banks in particular. This change was most pronounced in the weeks following the Federal Reserve measures of October 6. In the Eurodollar market the London interbank offer rate (LIBOR), the base rate on which loans are priced, in the week ending November 2 averaged 5 percentage points higher than the second quarter average. This increase was about 1/2 percentage point more than the increase in the U.S. commercial paper rate, and 5/8 percentage point more than the rise in the cost range for acceptance financing, over the same period. Market reports state that the greater rise in 90-day Eurodollar rates was caused by the intensification of expectations in the Eurodollar market that Eurodollar interest rates would move higher over the forthcoming several months. This change in expectations led many banks to try to lengthen the average maturity of their deposits by increasing the percentage of the total consisting of deposits of 90 days and longer maturities while reducing the portion consisting of very short maturities, thereby intensifying the upward pressures on the rates for the longer maturities while mitigating the upward pressures on the shorter rates.

Because of these recent changes and because the U.S. prime rate has lagged behind the increases in open-market rates in the United States, the relationship between the cost of Eurodollar credit and the cost of bank credit in the United States has changed markedly since mid-summer. The relatively lower cost of Eurodollar credit became less evident in the third quarter and disappeared in October; by the week of November 2 the midpoint of the cost range for Eurodollar loans averaged 50 basis points higher than the midpoint of the cost range for U.S. bank loans, a reversal of the relationship that was customary for several years prior to a few weeks ago.

Since about the first of November there has been some tendency for the relationships between Eurodollar interest rates and U.S. interest rates to revert back to the pattern seen prior to last July. Eurodollar rates have leveled out while U.S. rates have edged up, so that the relatively higher cost of Eurodollar credit in the week ending November 9 was reduced about 10-20 basis points from the previous week's average. However, it would appear that for most prime borrowers Eurodollar credit is still significantly more costly than bank credit in the United States. With the change in rate relationships, some large U.S. banks report that in recent weeks there has been a shift to prime-rate financing from financing that those banks had been extending themselves under various arrangements, or which had been extended by U.S. agencies and branches of foreign banks, at rates linked to Eurodollar rates.

The U.S. merchandise trade deficit was $28 billion at an annual rate in the third quarter (international accounts basis), down from $31 billion in the second quarter. This improvement occurred despite a large increase in the value of petroleum imports.

Agricultural exports increased sharply in the third quarter. They are expected to continue at about $38 billion (annual rate) through June 1980. Non-agricultural exports also grew substantially (by 8 per cent). Large gains were recorded for exports of industrial materials (particularly chemicals), civilian aircraft, and machinery.

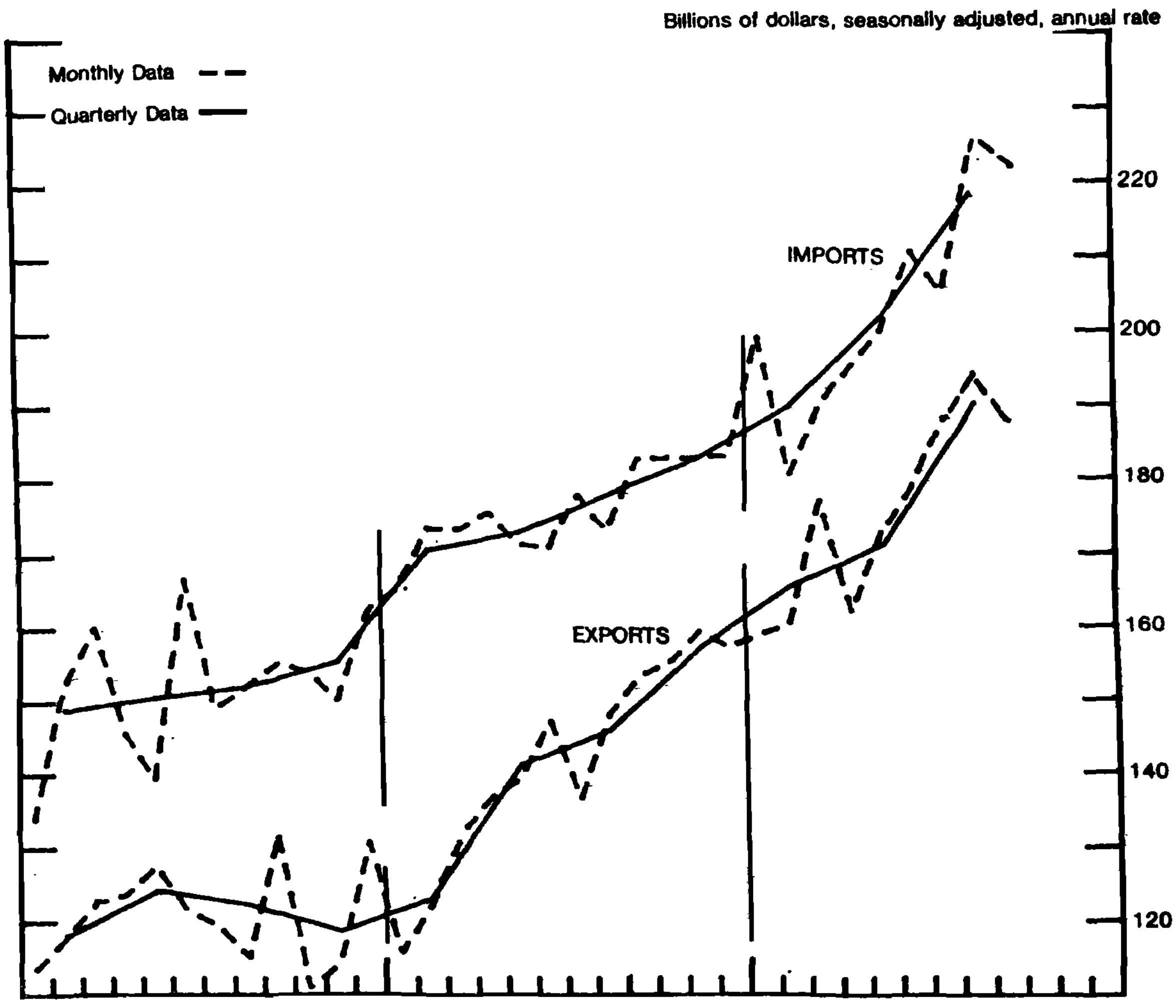
The increase in imports in the third quarter was almost entirely due to higher petroleum prices. The value of non-oil imports was close to the second quarter level. Increases in imports of industrial materials and consumer goods were offset by declines in foods and other commodities. The value of foreign car imports was about the same as in the second quarter.

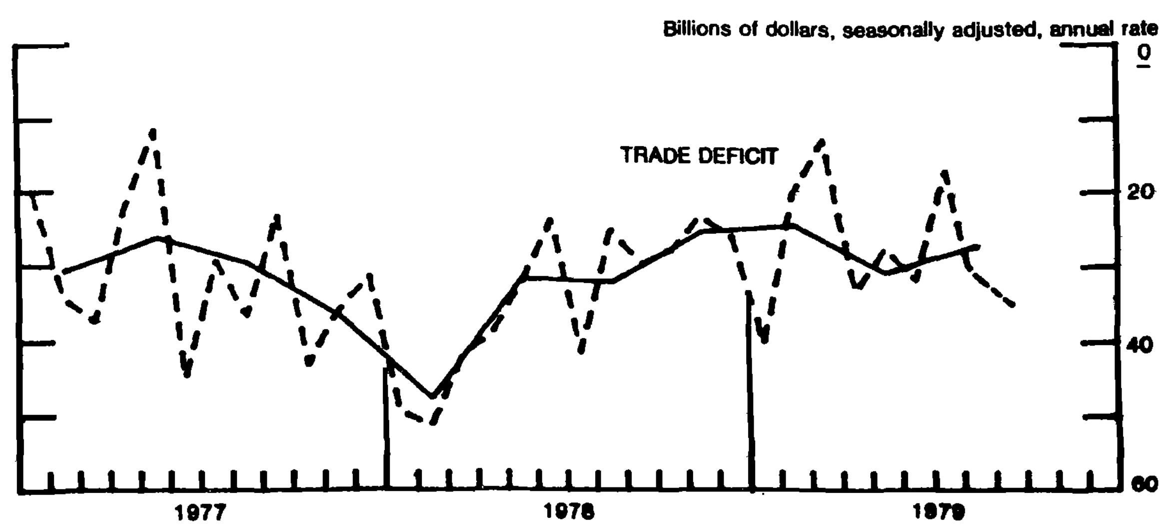
U.S. Merchandise Trade, International Accounts Basis
(billions of dollars, seasonally adjusted annual rates)

	1978	1978		1979				
	Year	3Q	4Q	1Q	2Q	3Q	Aug. r*	Sept. *
EXPORTS	141.9	146.0	157.3	165.4	171.2	190.3	194.9	187.9
Agric.	29.9	31.7	31.3	30.6	30.9	38.4	37.4	39.1
Nonagric.	112.0	114.2	126.0	134.8	140.2	151.9	157.5	148.8
IMPORTS	176.1	178.0	182.7	189.9	202.0	218.2	225.6	223.7
Petroleum	42.3	43.5	43.2	46.6	51.6	66.5	66.6	71.8
Nonpetroleum	133.8	134.5	139.5	143.3	150.4	151.7	159.0	151.9
BALANCE	-34.2	-32.0	-25.5	-24.5	-30.9	-27.8	-30.7	-35.8

NOTE: Details may not add to totals because of rounding.
r/ Revised
*/ The monthly International Accounts figures are only rough estimates and are subject to considerable revision.

U.S. Merchandise Trade
International Accounts Basis





The volume of imported oil was 8.6 million barrels per day in the third quarter, compared with 8.7 and 9.3 million barrels per day in the second and first quarters respectively. Oil import prices rose nearly 30 per cent to average $20.97 per barrel in the third quarter. Both higher contract prices and larger spot market purchases contributed to the increase in average price.

The cost of imported oil is likely to continue to go up in the fourth quarter. During the past three weeks several countries, accounting for about two-thirds of U.S. oil imports, have announced contract price increases of between 6 and 13 per cent. In addition, a larger percentage of U.S. imports is likely to be purchased on the higher priced spot market because of the cutoff in imports from Iran and because other producing countries are channeling a larger percentage of their output from the contract to the spot market. The volume of U.S. oil imports in the fourth quarter may also reflect any stock build-up due to anticipated OPEC price increases or fears of cutbacks in Iranian production.

Turning now to capital movements in the third quarter, substantial foreign and U.S. intervention to support the dollar was reflected in changes in foreign and U.S. reserve assets. The holdings of the G-10 countries and Switzerland in the United States grew by almost $5 billion net in the third quarter in contrast to a decline of $18.5 billion net in the first half of 1979, U.S. reserve assets

RESTRICTED

U.S. International Transactions
(in millions of dollars; receipts, or increase in liabilities, +)

		1977	1978	1978	1979			1979		
		Year	Year	Q4	Q1	Q2	Q3	July	Aug.	Sept.
1.	Trade balance 1/	-30,873	-34,187	-6,369	-6,115	-7,716	-6,962	-1,418	-2,557	-2,987
2.	Merchandise exports	120,816	141,884	39,315	41,348	42,792	47,580	15,685	16,239	15,656
3.	Merchandise imports	-151,689	176,071	-45,684	-47,463	-50,508	-54,542	-17,103	-18,796	-18,643
4.	Change in net foreign positions of banking offices in U.S. (excl. liab.to foreign official inst.)	-3,909	-14,924	-13,697	14,558	4,921	700	-1,353	9,531	-7,478
	Through interbank transactions with									
5.	a) Own offices in foreign countries	-2,718	4,940	-3,221	15,291	6,790	7,920	-1,629	16,647	-7,098
6.	b) Unaffiliated banking offices in foreign countries	-2,204	-4,520	-6,423	743	-1,190	-2,243	2,288	-4,956	425
	Through nonbank transactions									
7.	a) Claims on nonbanks in foreign countries (increase,-)	-424	-16,431	-4,829	-1,018	-2,005	-5,123	-1,871	-2,171	-1,081
8.	b) Liabilities to private nonbanks in foreign countries (inc. custody liab.)	1,436	1,089	776	-458	1,327	147	-140	11	276
9.	Private securities transactions,net (excl. U.S. Treas. Oblig.)	-3,068	-688	-116	-537	-77	-1,959	-465	-563	-931
10.	Foreign net purchases of U.S. corp. bonds	1,112	1,117	506	*	278	6	-52	-47	105
11.	Foreign net purchases of U.S. corp. stocks	1,326	1,686	297	424	274	142	-2	127	17
12.	U.S. net purchases (-) of foreign securities	-5,506	-3,491	-919	-961	-629	-2,107	-411	-643	-1,053
13.	Foreign net purchases of U.S. Treasury obligations 2/	534	2,251	1,546	2,564	-239	1,577	1,386	227	-36
14.	Change in foreign official reserve assets in U.S. (increase +)	35,448	31,471	16,853	-8,257	-10,293	5,354	3,815	634	905
	By Area									
15.	G-10 countries and Switzerland	29,414	29,955	15,574	-7,101	-11,613	4,818	3,562	239	1,017
16.	OPEC	5,743	-1,074	1,073	-1,645	248	1,453	888	1,383	-818
17.	All other countries	291	2,590	206	489	1,072	-917	-635	-988	706
	By Type									
18.	U.S. Treasury securities	30,266	23,869	13,309	-7,965	-12,799	4,980	3,253	987	740
19.	Other 3/	5,182	7,602	3,544	-292	2,506	374	562	-353	165
20.	Change in U.S. reserve assets (increase -)	-237	662	200	-3,008 4/	446	2,712	1,223	0	1,489
21.	All other transactions and statistical discrepancy	2,105	15,416	1,583	795	12,958	-1,421	-3,186	-7,273	9,038
MEMO:	Current Account (bil. $. seasonally adj., annual rates)	-14.1	-13.9	-1.3	1.7	-3.9	n.a.	n.a.	n.a.	n.a.

1/ International accounts basis, seasonally adjusted.
2/ Includes U.S. Treasury notes publicly issued to private foreign residents.
3/ Includes deposits in banks, commercial paper, bankers' acceptances, and borrowing under repurchases agreements.
4/ Includes $1,103 million of newly allocated SDR's.
5/ Less than $500,00.

declined $2.7 billion in the third quarter.

In October, exchange rate pressures reversed again,

; holdings of the G-10 countries and Switzerland at the FRBNY fell by $2.5 billion.

OPEC holdings in the United States increased approximately $1.5 billion in the third quarter, compared with a very small increase in the second quarter, and a decrease in the first quarter.

Net private capital flows in the third quarter also reflected the reappearance of downward pressure on the value of the dollar. In contrast to the large net private inflows recorded earlier in 1979, the sum of net private capital flows reported by banks and securities dealers was very small in the third quarter. Although banks in the United States continued to raise additional funds from offshore banks, this was offset by increased lending to foreign nonbanks, particularly by U.S. agencies and branches of foreign banks.

In the three weeks following the Board's October 6 actions, the net Eurodollar borrowings of member banks from their branches averaged $2.4 billion less than in the two week base period. This decline is more than accounted for by a reduction in weekend borrowing of clearinghouse funds from own branches. As a result of this reduction in weekend Eurodollar activity, reserve liabilities against demand deposits increased by more than $.6 billion.

Partial data indicate that the recent rapid growth of U.S. nonbank dollar-denominated deposits in foreign banking offices may have slowed in September. Such deposits in the foreign branches of member banks dropped by $2 billion in September, although the Eurodollar CD holdings of open-ended money market mutual funds and short-term unit investment trusts grew by $1.7 billion in September and again in October. U.S. (nonbank) residents' Eurodollar assets held in the two forms above increased from about $17 billion to roughly $30 billion in the first three quarters of 1979.

<u>Foreign Economic Developments</u>. Economic growth abroad, supported primarily by private domestic demand, was generally strong in the second quarter. Real GNP in Japan, currently the most vigorous of the major economies, continued to expand steadily. Germany's GNP rebounded sharply after a temporary lull in the first quarter. Real output recovered in both the United Kingdom and France after having declined in the preceding quarter. However, in Canada a deterioration in the balance of goods and services, and sluggish personal consumption, led to a fall in real GNP in the second quarter. GNP also declined in Italy, primarily because of strikes. Data on industrial production during the third quarter suggest some recent moderation in the average rate of GNP growth in these countries.

Inflation continues at a high rate in nearly all major foreign countries. A partial exception is Germany, where both consumer and wholesale prices rose at markedly slower rates in the third quarter than they had earlier in the year. Retail prices rose at a much slower rate in August and September in the United Kingdom, after having accelerated sharply in July as a result of an increase in the rate of value added taxation (VAT). In Japan, the most recent data indicate a continuation of large increases in wholesale and consumer prices, due in part to the depreciation of the yen and higher oil prices. Inflationary pressures show no signs of easing in Canada and France, and in Italy inflation rose in the latest two months through September.

In the face of continuing high inflation rates, and following the increase in the U.S. discount rate in early October, discount rates have been increased in Belgium, Canada, Germany, Italy, the Netherlands, Japan and Switzerland. For further information of these actions, see page IV-2 above.

The current-account deficits of Germany and Japan widened at a rapid rate in the third quarter, mainly because of higher oil prices. The large reduction in the U.K. current-account deficit in the third quarter reflected primarily a decline in the value of imports from the abnormally high level in the second quarter. Recent trade deficits in France and Italy suggest that their current-account surpluses will be reduced from last year. The small third-quarter Canadian trade surplus indicates that the current-account deficit will probably not be reduced below the second-quarter level.

Individual Country Notes. In Japan, the strength in domestic demand in the first two quarters appears to be continuing. While industrial production declined in September, most leading indicators of private investment activity suggest little diminution so far of the resurgence of investment seen earlier in the year. Despite a progressive tightening of monetary conditions during the year, corporate credit appears to have remained generally available.

In the past year the role of sustaining real GNP growth in Japan has shifted away from government expenditure and net exports and toward private domestic demand. In the fourth quarter of 1978 and the first quarter of this year, both private consumption and fixed investment strengthened significantly. Although second-quarter growth rates for these two components declined somewhat, both were still stronger than other sectors of the economy. Government expenditure, on the other hand, has advanced more slowly than expected. In the external sector, the strong upward trend in real imports has continued, with real exports showing some recent signs of strength after sharp declines during 1978 and early 1979.

Real GNP and Incustrial Production in Major Industrial Countries
(percentage change from previous period, seasonally adjusted)

		1976	1977	1978	1978 Q3	1978 Q4	1979 Q1	1979 Q2	1979 Q3	1979 May	1979 Jun	1979 Jul	1979 Aug	1979 Sept
Canada:	GNP	5.4	2.4	3.4	1.1	0.7	1.6	-0.7	n.a.	*	*	*	*	*
	IP	5.1	4.0	5.3	1.8	2.6	1.4	-1.2	n.a.	0.1	-1.1	2.4	-0.2	n.a.
France:	GDP	4.5	3.1	3.7	0.0	1.7	-0.2	0.6	n.a.	*	*	*	*	*
	IP	9.5	2.0	1.9	-0.3	1.8	0.0	0.3	n.a.	1.5	-0.8	3.1	0.0	n.a.
Germany:	GNP	5.5	2.6	3.5	1.0	0.8	0.5	2.0	n.a.	*	*	*	*	*
	IP	7.9	2.7	2.0	3.2	0.8	0.3	2.5	1.3	1.6	0.0	3.2	-3.9	0.8
Italy:	GDP	5.9	2.0	2.6	0.6	2.9	0.9	-0.6	n.a.	*	*	*	*	*
	IP	12.4	1.1	1.9	1.0	6.1	1.7	-3.3	1.0	-3.1	-4.2	3.1	0.0	5.9
Japan:	GNP	6.4	5.4	5.6	0.8	1.7	1.7	1.5	n.a.	*	*	*	*	*
	IP	11.1	4.2	6.2	1.3	2.2	1.8	2.4	2.3	2.1	0.2	1.1	0.9	-0.7
United Kingdom:	GDP	2.9	2.2	2.6	1.1	-0.1	-1.5	2.4	n.a.	*	*	*	*	*
	IP	1.9	3.8	3.7	0.8	-1.4	-0.4	5.3	-2.4	.9	2.0	-1.0	-4.2	-1.4
United States:	GNP	5.9	5.3	4.4	0.9	1.4	0.3	-0.6	0.6	*	*	*	*	*
	IP	10.7	5.9	5.8	1.9	1.9	1.0	-0.1	0.1	1.1	0.3	-0.1	-0.7	0.5

* GNP data are not published on monthly basis.

Consumer and Wholesale Prices in Major Industrial Countries
(percentage change, from previous period or as indicated)

	1976	1977	1978	1978 Q2	1978 Q3	1978 Q4	1979 Q1	1979 Q2	1979 Q3	Latest 3 Months from: Previous 3 Months (at Ann. Rate)	Latest 3 Months from: Year Ago	Latest Month
Canada: CPI	7.5	8.0	8.9	2.4	2.5	1.6	2.3	2.6	2.0	8.1	8.7	Sept
WPI	5.1	7.9	9.2	2.8	2.1	3.3	4.5	3.1	2.7	11.2	14.3	Sept
France: CPI	9.6	9.5	9.2	2.9	2.7	2.1	2.2	2.8	3.2	13.6	10.7	Sept
WPI	7.4	5.6	4.3	1.9	1.9	2.9	4.4	3.8	2.8	11.8	14.6	Sept
Germany: CPI	4.6	3.9	2.6	0.9	0.0	0.1	2.1	1.6	1.2	3.4	5.2	Oct
WPI	5.8	1.8	-0.3	0.3	-0.6	0.1	3.4	3.3	1.7	7.1	8.8	Sept
Italy: CPI	16.8	18.4	12.1	3.0	2.4	3.0	3.9	3.8	3.3	13.9	14.6	Sept
WPI	22.9	17.4	8.4	2.3	1.8	2.2	4.4	4.6	4.3	18.2	16.4	Sept
Japan: CPI	9.7	8.3	4.3	2.0	0.8	0.2	-0.2	2.2	0.9	3.4	3.1	Oct
WPI	5.0	1.9	-2.5	-0.3	-1.7	-0.6	1.9	4.1	4.9	20.0	12.8	Oct
United Kingdom: CPI	16.6	15.8	8.3	2.7	1.7	1.7	3.1	3.7	6.7	29.6	16.0	Sept
WPI	17.3	19.8	9.1	1.8	1.9	1.7	2.7	4.0	5.0	17.4	14.4	Oct
United States: CPI	5.7	6.5	7.6	2.6	2.4	2.0	2.5	3.4	3.3	13.9	11.7	Sept
WPI	4.6	6.1	7.8	3.0	1.5	2.3	3.6	3.6	3.0	13.7	13.7	Oct

Trade and Current-Account Balances of Major Industrial Countries[a]
(billions of U.S. dollars; seasonally adjusted)

		1977	1978	1978 Q2	1978 Q3	1978 Q4	1979 Q1	1979 Q2	1979 Q3	1979 Jul	1979 Aug	1979 Sept
Canada:	Trade	2.7	3.1	0.6	0.6	0.7	0.5	0.4	0.5	0.0	-0.1	0.6
	Current Account	-4.1	-4.6	-1.1	-1.2	-1.5	-1.4	-1.5	n.a.	*	*	*
France:	Trade[b]	-2.4	0.6	0.2	0.2	0.1	0.3	-0.4	-1.4	-0.2	-0.7	-0.4
	Current Account[b]	-3.3	3.8	1.4	1.2	1.3	0.6	0.7	n.a.	*	*	*
Germany:	Trade	16.5	20.6	4.9	5.4	5.6	4.3	3.8	n.a.	0.7	1.0	n.a.
	Current Account[c]	4.3	8.9	1.8	0.2	4.8	1.4	-1.1	-4.1	-1.1	-1.7	-1.3
Italy:	Trade	-2.8	-0.2	0.3	-0.8	0.5	-0.4	-0.7	-1.2	-1.0	0.2	-0.3
	Current Account[c]	2.5	6.4	1.7	2.5	1.7	1.1	n.a.	n.a.	*	*	*
Japan:	Trade	17.4	24.7	6.8	6.7	3.9	2.7	1.9	-0.9	-0.2	-0.2	-0.5
	Current Account	10.9	16.5	4.8	4.5	1.7	0.3	-0.7	-3.8	-1.3	-1.1	-1.4
United Kingdom:	Trade	-3.0	-2.2	-0.3	-0.7	-0.1	-3.2	-2.3	-0.4	0.0	-0.2	-0.2
	Current Account[d]	0.7	2.0	0.7	0.6	1.2	-2.3	-2.3	-0.7	0.0	-0.2	-0.2
United States:	Trade	-30.9	-34.2	-7.9	-8.0	-6.4	-6.1	-7.7	-7.0.	-1.4	-2.6	-3.0
	Current Account	-14.1	-13.9	-3.4	-3.2	-0.3	0.4	-1.0	n.a.	*	*	*

a/ The current account includes goods, services, and private and official transfers.
b/ French annual data is not seasonally adjusted.
c/ Not seasonally adjusted.
d/ Monthly data do not add to quarterly totals because of rounding.
* Comparable monthly current account data are not published.

Another large increase in wholesale prices occurred in October (a 1.1 percent gain over the September level), even though the pass-through of early summer oil price increases had been largely completed. The strong upward trend in consumer prices has also continued, but at a somewhat more moderate rate than in previous months, partly reflecting seasonal factors.

The rapid expansion in Germany in the second quarter was generated by a rebound in the construction sector, which expanded by 17.5 percent (quarterly rate) after a substantial decline in the first quarter arising from a severe winter. Partly in response to this rapid expansion, construction costs have risen 10 percent above their level a year ago, whereas the CPI has increased about 5 percent.

The increase in Germany's growth rate in the first half of this year resulted from expanding domestic demand. Private consumption and investment in equipment have shown sustained strength in the first two quarters, increasing at 1.5 and 2.5 percent quarterly rates respectively. Government expenditure increased at a 1.5 percent average quarterly rate, while net foreign demand for goods and services has declined.

Preliminary indicators suggest a continuation of strength in demand into the third quarter. Industrial production in the three months through September was 1.3 percent above the preceding three-month period. The rate of unemployment in September fell slightly to 3.6 percent (s.a.) and remained at this low level in October. Moreover, German officials at a recent OECD meeting estimated that GNP grew 1-1/4 percent in the third quarter.

In the latest three months through October, the CPI was 5.3 percent above its level last year. In a month-to-month comparison, however, the CPI has been almost flat since July.

When the Bundesbank raised both its discount and Lombard rates by 1 percentage point on November 1, it also increased rediscount quotas by DM 4 billion.

The pattern of economic activity in Italy this year has been distorted by widespread strike activity, mostly in the second quarter, when GDP fell by 0.6 percent after rising nearly 1 percent in the first quarter. On the basis of estimates, it appears that personal consumption has been the strongest component of demand so far this year, although business investment has also shown signs of strength. The trade balance has made a negative contribution to GDP growth in the first three quarters of the year. Activity in July started to rebound from the effects of the strikes, and industrial production rose 9 percent between June and September.

After several months in which inflation had moderated, consumer prices in Italy rose in September by 2.5 percent (n.s.a.), the largest monthly increase this year, and there are early indications that it will also rise by about 2 percent in October. Higher administered prices of petroleum products and electricity are a major reason for the acceleration of inflation, and the government's recent decision to raise taxes on gasoline is adding further upward impetus to the price level.

On October 6, the Bank of Italy increased its discount rate from 10.5 percent to 12 percent. Later in the month the ceilings on bank credit were extended for the period October 1, 1979, to July 31, 1980. Both measures are designed to counter the rise in the inflation rate and were taken in the face of rising interest rates abroad, which had discouraged foreign borrowing by Italian banks.

In the United Kingdom much of the increase in real GDP in the second quarter reflected a recovery of the output lost through adverse weather conditions and industrial disputes in the first quarter. In fact, there has been little change in the level of real output between the last half of 1978 and the first half of 1979. Recent business surveys, a fall in industrial production of 2.4 percent in the third quarter, and a reduction in third-quarter real consumption expenditures of 3.5 percent indicate that there has been a significant decline in real output in the third quarter.

While real GDP was essentially unchanged between the first half of this year and the last half of 1978, real final domestic demand rose by roughly 1-1/2 percent over the same period. This increase reflected a 3 percent rise in consumer spending, a nearly 2 percent fall in gross fixed capital formation, and an unchanged level of government current expenditures. With total output unchanged, the expansion in domestic demand was accommodated by an increase in real imports of goods and services of 13 percent from the last half of 1978 to the first half of this year. The volume of exports of goods and services, on the other hand, fell in the same period by 3 percent.

Inflation has accelerated sharply this year in the United Kingdom. The year-over-year inflation rate jumped from 11.5 percent in June to 15.5 percent in July, when the June 12 increase in the VAT was reflected in the CPI. However, in August and September consumer prices rose on average by only about 1 percent on a month-to-month basis.

On October 24 all exchange controls (except on the purchase of Rhodesian securities) were abolished in the United Kingdom. This action, which followed liberalization of outward direct investment and portfolio investment in EEC currencies in June and July, means that U.K. residents now have full freedom to engage in all kinds of foreign currency transactions.

In France, output growth was less than 1 percent (s.a.a.r.) in the first half year, considerably below the 3.7 percent annual rate of growth in 1978. On the basis of trade data, surveys and policy developments, the sources of strength are likely to be the same in 1979 as in 1978, namely, exports and consumption. In the first half of this year export volume grew by 8 percent over the same period last year, undoubtedly making it the strongest source of demand. Real import growth, however, exceeded that of exports, amounting to over 12 percent in the first half of this year compared to the first half of last year. Real private consumption growth is likely to be weaker this year than in 1978 as a result of the July increase in employee social security contributions, the rapid pass-through of energy price increases, and the stagnation in the level of employment.

Investment has been an area of concern to the authorities for the past several years. Despite attempts to stimulate this sector, including the partial relaxation of price controls, income tax deductions for equity purchases by individuals, and a $1-1/3 billion investment incentive program (in April), private investment will probably remain weak this year.

In the week of October 1, the authorities expanded the coverage of credit controls in an attempt to hold monetary growth to 11 percent for 1980. Export financing, housing, and infrastructure investment credits will be subject to greater control than heretofore. In response to interest rate increases in other financial markets, the Bank of France is in the process of raising the rates at which it intervenes on the money market. The initial increase in these rates on November 2 was 1/2 percent, and a further increase is likely.

In Canada, GNP declined in the second quarter in part because real consumption spending remained unchanged after rising by over 1.5 percent in the first quarter. Contributing to the first-quarter strength in consumption spending was anticipatory buying by consumers to avoid expected new car price increases. In the second quarter business gross fixed investment increased 2.5 percent in volume as investment in plant and equipment rose nearly 3.5 percent.

The source of greatest weakness in the Canadian economy in the first half of this year was the foreign sector. Real goods-and-services exports fell almost 7 percent in that period, while imports declined by only 1 percent. Competitive gains achieved by last year's depreciation of the Canadian dollar appear to have been overwhelmed by the effects of the U.S. slowdown on the Canadian export sector.

Recently, the Conservative Government announced a program of reduced taxes on mortgage interest and property taxes that will be phased in over four years. The Government does not foresee any additional tax cuts this year.