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August 11, 1993

RECENT DEVELOPMENTS

Prepared for the Federal Open Market Committee
By the staff of the Board of Governors of the Federal Reserve System

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DOMESTIC NONFINANCIAL DEVELOPMENTS

Surveys suggest a continued erosion of consumer and business optimism about the prospects for economic growth, but this has not been mirrored in the most recent indicators of employment and production. July figures point to a rise in hours worked and industrial output, and, with an increase in motor vehicle assemblies slated for this month, a decent gain in goods production appears in train for the current quarter. Key price measures for July will be published in the next few days; at this time, we see no evidence of a change in the trend of inflation.

Employment and Unemployment

Labor demand continues to expand at a moderate rate. Nonfarm payroll employment rose 162,000 in July, after only a small gain in June, and the civilian unemployment rate declined from 7.0 percent to 6.8 percent. Hours of production or nonsupervisory workers rose 0.3 percent last month to a level 0.2 percent above the second quarter average. The BLS reported that these labor market data revealed little disruption, as of mid-July, from the flooding in the Mississippi basin.

The effects of the flooding may have shown through, however, in higher levels of unemployment insurance claims later in the month. In addition, the two-week layoff of about 250,000 workers at General Motors contributed to a spike in claims for the week ended July 24. The data in hand--which are based in part on rough estimates from Michigan and may be revised substantially--indicate that about 100,000 GM workers filed claims under either regular or emergency programs. By the end of July, claims had returned to the weekly level that had prevailed last spring.

In private industry, employment rose 158,000 in July, about equal to the average monthly gain in the first six months of the

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

	1991	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June	1993 July
	------------Average monthly changes---------							
Nonfarm payroll employment[2]	-72	80	135	162	179	238	44	162
Private	-88	59	123	155	163	219	26	158
Manufacturing	-44	-26	-12	7	-54	-36	-55	-13
Durable	-39	-22	-9	3	-44	-43	-35	-13
Nondurable	-5	-5	-3	5	-10	7	-20	0
Construction	-33	-5	4	7	30	60	-7	24
Trade	-30	20	35	62	50	69	30	50
Finance, insurance, real estate	-9	-2	3	0	5	3	0	12
Services	39	78	92	77	139	122	74	79
Health services	30	29	36	29	25	28	12	21
Business services	4	31	47	31	40	31	22	37
Total government	17	22	12	7	16	19	18	4
Private nonfarm production workers	-71	74	132	149	152	277	-9	143
Manufacturing production workers	-29	-13	1	16	-38	-23	-38	-10
Total employment[3]	-62	130	196	85	218	857	-54	82
Nonagricultural	-53	122	182	145	237	847	-8	67
Memo:								
Aggregate hours of private production workers (percent change)	-.1	.1	.2	.1	.4	1.2	-.8	.3
Average workweek (hours)	34.3	34.4	34.4	34.4	34.5	34.7	34.4	34.5
Manufacturing (hours)	40.6	41.1	41.2	41.3	41.4	41.4	41.2	41.4

1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments.
3. Survey of households.

SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES
(Percent; based on seasonally adjusted data)

	1991	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June	1993 July
Civilian unemployment rate (16 years and older)	6.7	7.4	7.3	7.0	7.0	6.9	7.0	6.8
Teenagers	18.7	20.0	19.4	19.6	20.1	19.7	19.8	18.2
20-24 years old	10.8	11.3	11.1	11.0	10.8	11.4	10.4	10.6
Men, 25 years and older	5.7	6.4	6.3	5.9	5.8	5.7	5.9	5.9
Women, 25 years and older	5.1	5.7	5.8	5.4	5.4	5.3	5.6	5.3
Fulltime workers	6.5	7.1	7.0	6.6	6.6	6.6	6.6	6.7
Labor force participation rate	66.0	66.3	66.2	66.0	66.2	66.3	66.2	66.1
Teenagers	51.7	51.3	51.2	51.5	51.9	52.7	51.4	51.9
20-24 years old	76.8	77.1	77.0	77.3	77.4	78.0	77.4	77.5
Men, 25 years and older	76.7	76.7	76.4	76.1	76.2	76.3	76.4	76.3
Women, 25 years and older	56.5	57.0	57.1	56.8	56.8	56.9	57.1	56.8

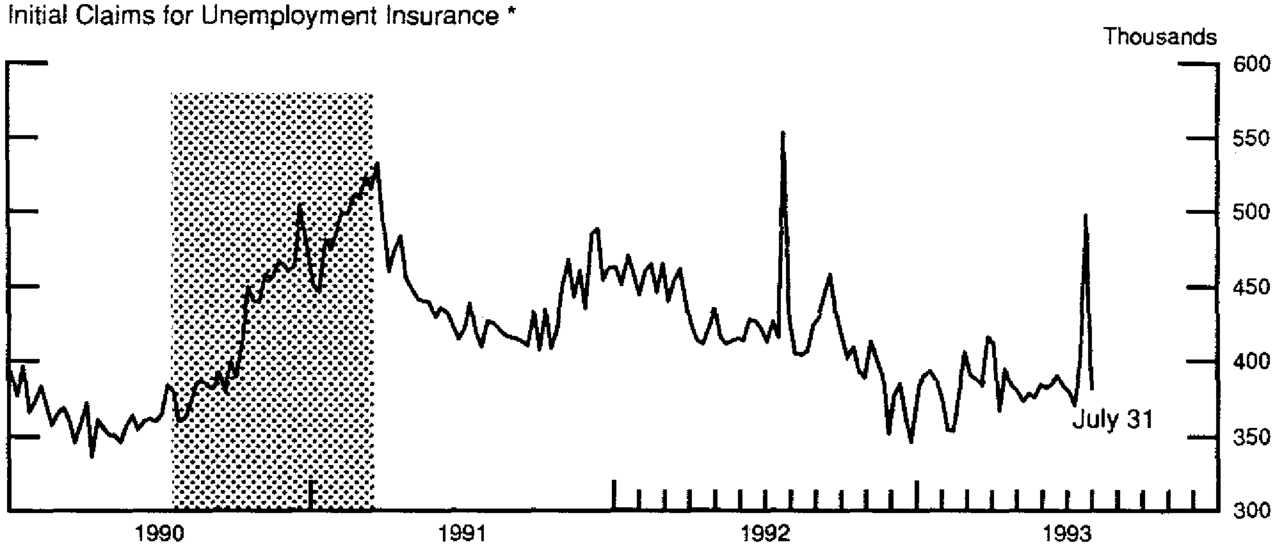
year. The services industry provided half the July job increase, led, again, by business services. In turn, most of the hiring by business services occurred at personnel supply firms (which include temporary help agencies). Continued hiring was also evident in wholesale and retail trade and in finance, insurance, and real estate. Construction employment moved up in July, after a small decline in the preceding month. Manufacturers shed another 13,000 jobs in July, a smaller decline than in recent months. Total factory job losses have cumulated to more than 150,000 so far this year. In the government sector, local government payrolls declined 16,000 despite the temporary addition of an estimated 15,000 federally funded summer jobs.

Employment as measured by the household survey moved up 82,000 in July after edging down in June. Regarding the overall unemployment rate, the BLS emphasized that the July decline was statistically insignificant: On an unrounded basis, the rate declined only one-tenth of a percentage point; and with concurrent seasonal adjustment, the rate has been flat at 6.9 percent for the past three months. Other indicators from the household survey, such as involuntary part-time employment and the number of permanent job losers, also have changed little over the past few months. With a labor market that jobseekers still perceive is offering only limited opportunities, the labor force participation rate has continued to hover only a little above its cyclical low in 1991; rates for both adult men and adult women are below the levels of last summer.

The relatively strong increases in employment and hours in the second quarter were not reflected in production. According to initial estimates, productivity in the nonfarm business sector fell at a 2-1/2 percent annual rate in the second quarter, after a 1-1/2 percent decline in the first quarter. In the latter part of

LABOR MARKET INDICATORS

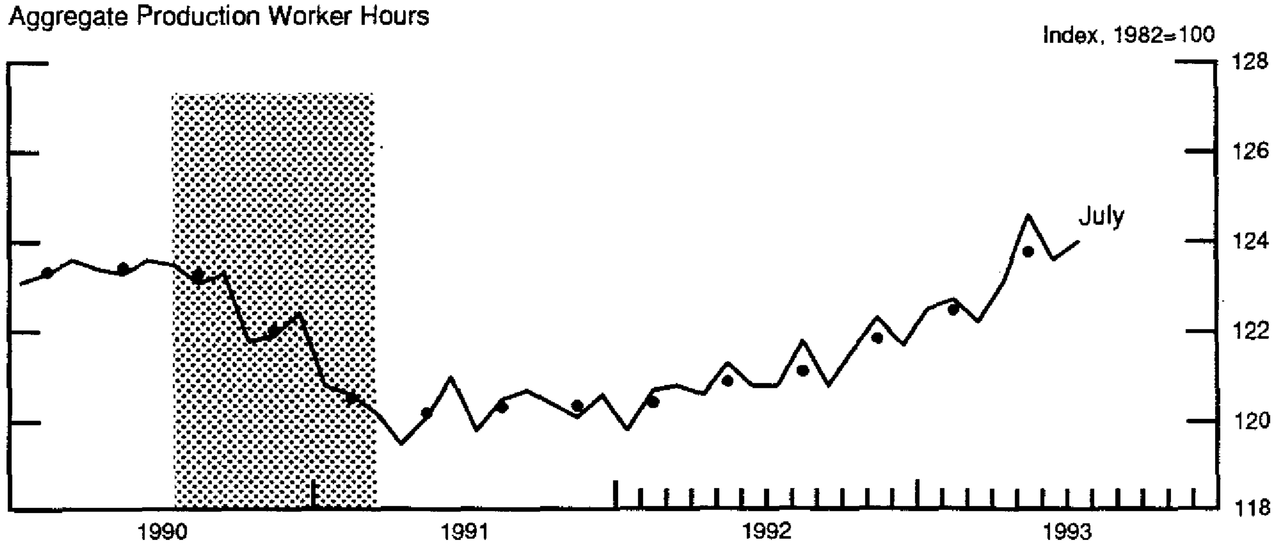
Initial Claims for Unemployment Insurance *



* Adjusted for EUC program.

Civilian Unemployment Rate

Aggregate Production Worker Hours



1992, hiring had lagged behind the rapid increases in output, and as a result some retrenchment in productivity early this year seemed reasonable, especially in light of the sluggish growth of output. But the apparent sharpness of the drop in productivity now estimated for the second quarter of 1993, which brought the level of productivity below the staff's estimate of its recent trend level, was surprising, given the reported focus of businesses on improving efficiency. One possible explanation is that recent output levels are currently underestimated--an issue that could be resolved, at least in part, by the upcoming revisions to the NIPAs. But the recent drop in productivity could also suggest that employers will turn more cautious about hiring in coming months as they attempt to restore labor efficiency gains.

Industrial Production

Industrial production slackened in the spring. The slowdown was widespread but also reflected the coal strike and a cutback in output of motor vehicles and parts. With factory production lackluster, capacity utilization in manufacturing fell back 0.5 percentage point between April and June (top panel of chart).

The available indicators for July suggest that industrial production firmed somewhat last month. Although coal output declined further and motor vehicle assemblies dropped again (see below), other weekly physical product indicators show a gain, on balance. Electricity generation jumped, after a large rise in June; paper and paperboard, basic steel and steel products, and lumber posted smaller increases. Elsewhere, among most upstream producers of durable goods, the factory workweek returned to the high rates posted in April. On balance, excluding motor vehicles, manufacturing production worker hours increased 0.2 percent last month (middle panel of chart).

GROWTH IN SELECTED COMPONENTS OF INDUSTRIAL PRODUCTION
(Percent change from preceding comparable period)

	Proportion in total IP 1992:4	1992[1]	1993 Q1	1993 Q2	1993 Apr.	1993 May	1993 June
			-Annual rate		---Monthly rate----		
Total index	100.0	3.2	5.5	1.9	.3	.0	-.2
Manufacturing	84.6	3.7	6.4	2.6	.5	-.1	-.3
Motor vehicles and parts	4.9	10.2	37.4	-6.3	.7	-1.6	-2.5
Mining	7.3	-.9	-5.7	.2	1.2	.6	-.7
Utilities	8.2	2.0	4.6	-2.0	-2.4	.0	1.3
MANUFACTURING EXCEPT MOTOR VEHICLES AND PARTS	79.7	3.3	4.7	3.2	.5	.0	-.2
Consumer goods	22.1	2.1	2.0	-.1	.1	-.2	-.6
Durables	3.6	3.7	15.4	4.0	.3	.0	-1.4
Nondurables	18.4	1.7	-.6	-1.0	.0	-.2	-.5
Business equipment	14.5	9.9	8.9	9.9	.8	.4	.5
Office and computing	3.2	31.1	31.5	39.1	2.9	2.8	2.5
Industrial	4.0	6.1	5.6	6.0	.9	.1	-.1
Other	7.1	4.2	.8	-.3	-.2	-.5	-.2
Defense and space equipment	3.3	-7.8	-7.7	-8.1	-.3	-.9	-1.3
Construction supplies	4.8	4.5	6.2	.4	-.4	.9	-.7
Materials	28.2	3.2	7.4	3.8	.7	.0	.0
Durables	18.9	3.6	9.4	3.1	.5	.1	-.1
Nondurables	9.0	2.3	4.2	5.3	.9	-.1	.2

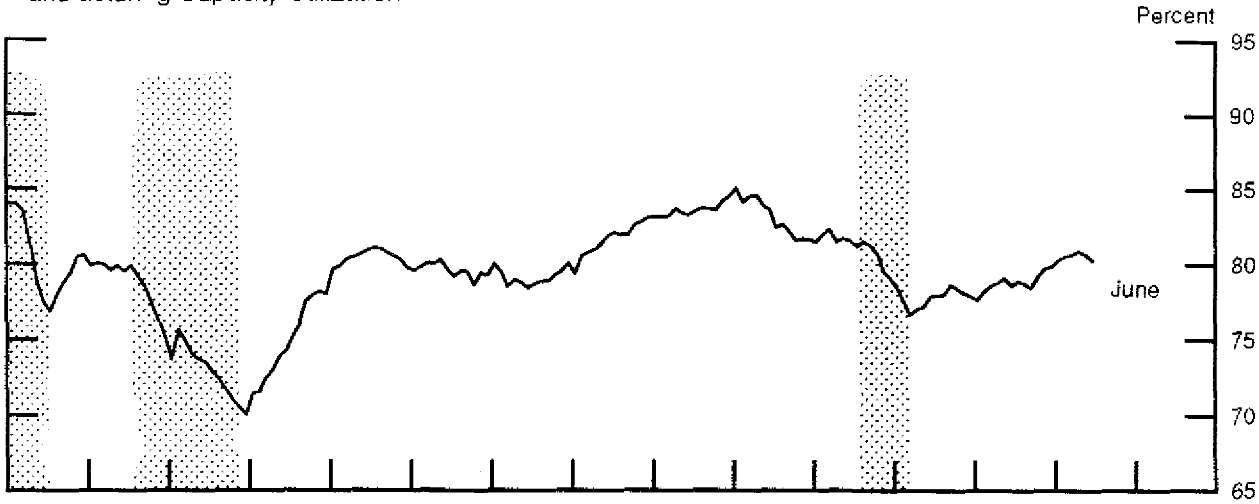
1. From the final quarter of the previous period to the final quarter of the period indicated.

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

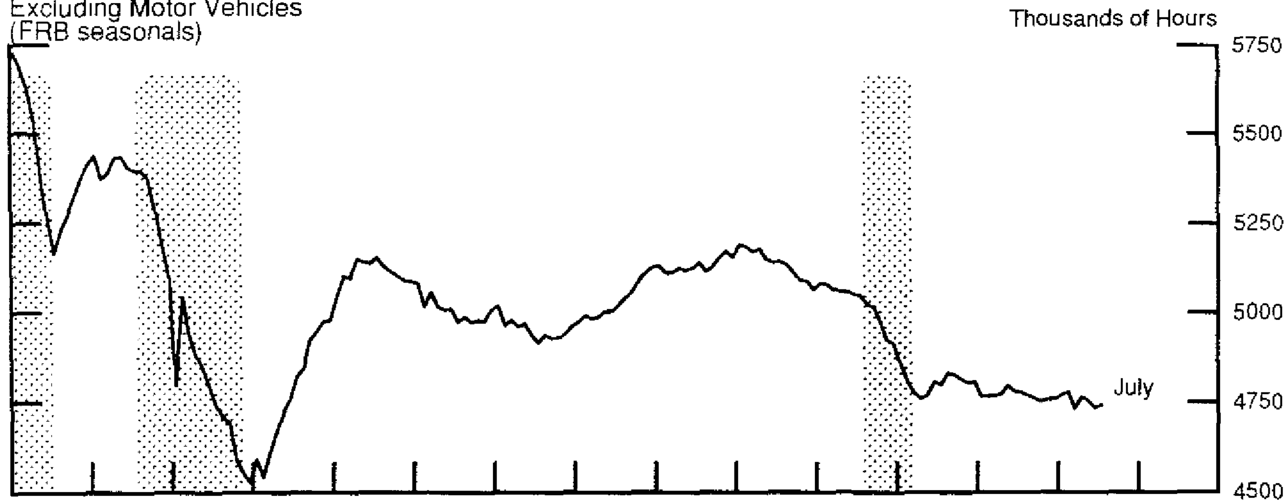
	1967-92 Avg.	1992 Avg.	1993 Q1	1993 Q2	1993 Apr.	1993 May	1993 June
Total industry	81.9	79.8	81.4	81.5	81.7	81.5	81.2
Manufacturing	81.2	78.8	80.5	80.6	80.9	80.7	80.3
Primary processing	82.2	82.2	83.9	84.0	84.2	84.1	83.8
Advanced processing	80.7	77.3	79.0	79.2	79.5	79.2	78.8

Indicators of Manufacturing Activity

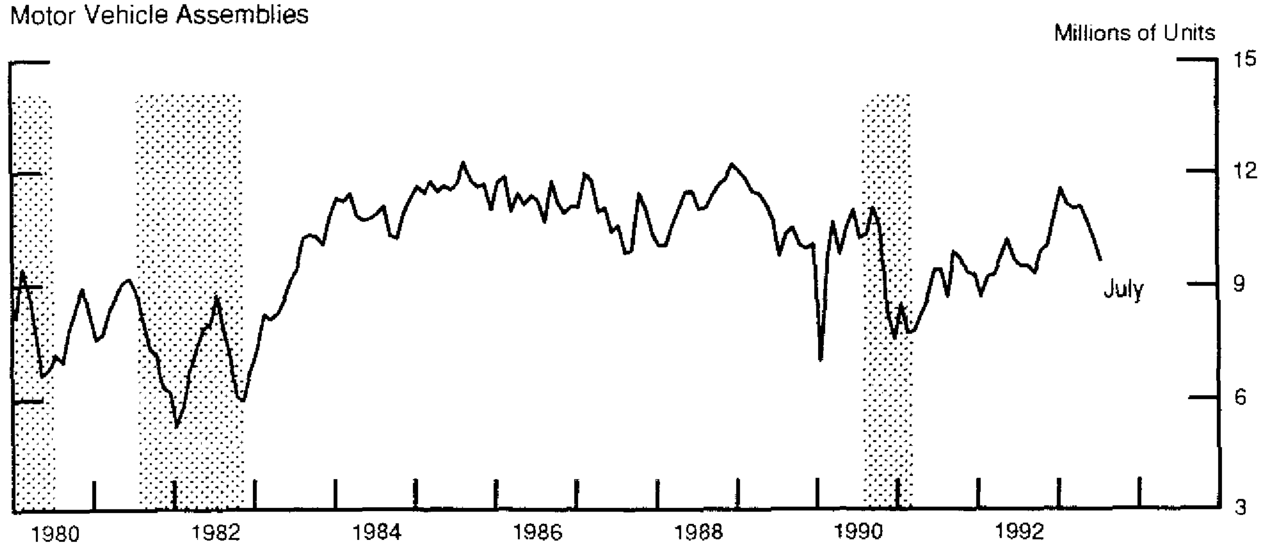
Manufacturing Capacity Utilization



Manufacturing Production Worker Hours
Excluding Motor Vehicles
(FRB seasonals)



Motor Vehicle Assemblies



PERSONAL INCOME
(Average monthly change at an annual rate; billions of dollars)

	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June
Total personal income	20.8	37.7	22.3	11.8	27.7	-2.5
Wages and salaries	10.8	20.8	4.0	13.3	30.9	-4.1
Private	8.9	18.6	2.2	11.3	28.9	-6.1
Other labor income	1.4	1.4	1.5	1.4	1.4	1.5
Proprietors' income	4.1	8.2	10.0	-9.0	-7.8	-4.9
Farm	.5	3.4	8.4	-11.4	-10.9	-6.2
Rent	1.4	2.6	.4	3.6	.6	1.6
Dividend	1.2	2.0	.6	.3	.3	.4
Interest	-3.7	.0	-.7	-.4	-.4	-.3
Transfer payments	6.7	4.0	7.8	3.3	4.5	2.9
Less: Personal contributions for social insurance	1.1	1.5	1.3	.7	1.7	-.5
Less: Personal tax and nontax payments	2.0	5.4	2.3	3.9	7.1	.7
Equals: Disposable personal income	18.7	32.2	20.0	8.0	20.6	-3.1
Memo: Real disposable income	7.1	18.5	5.2	1.0	12.0	-3.1

REAL PERSONAL CONSUMPTION EXPENDITURES
(Percent change from the preceding period)

	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June
		------Annual rate-----			Monthly rate	
Personal consumption expenditures	3.4	5.1	.8	3.8	.3	.6
Durable goods	9.2	14.0	-.8	14.2	2.3	.5
Excluding motor vehicles	10.0	8.9	3.3	5.6	1.1	.9
Nondurable goods	3.3	6.8	-2.7	2.4	-.1	.7
Excluding gasoline	3.6	8.0	-3.0	2.6	-.5	1.0
Services	2.2	2.1	3.2	2.2	-.1	.6
Excluding energy	2.3	1.9	3.3	2.7	.2	.2
Memo:						
Personal saving rate (percent)	4.8	4.4	4.9	4.3	4.6	3.9

Production of motor vehicles slipped to a 9.7 million unit annual rate in July (lower right panel of chart) as carmakers closed out the 1993 model year with somewhat lower production than they scheduled a month ago. Dealers' inventories of new domestic autos, which had shrunk to an estimated 67 days' supply in June, remained comfortable in July, as sales moved back to about the same pace as production last month. Stocks of light trucks were toward the low end of the historical range. Assemblies of both autos and trucks are scheduled to be much higher in August and September than in July.

PRODUCTION OF DOMESTIC AUTOS AND TRUCKS
(Millions of units at an annual rate; FRB seasonal basis)[1]

	1993					
	Apr.	May.	June	July	Aug.	Sep.
					--scheduled--	
U.S. production	11.1	10.7	10.2	9.7	11.7	11.2
Autos	6.3	6.0	5.8	5.4	6.7	6.3
Trucks	4.8	4.7	4.4	4.3	5.0	4.8
Days' supply[2]						
Autos	72.9	71.5	66.8	68.0		
Light Trucks	71.4	70.0	66.5	67.2		

1. Components may not sum to totals because of rounding.
2. BEA seasonal basis, end of month.

Personal Income and Consumption

Real personal consumption expenditures picked up in the second quarter, increasing 3.8 percent at an annual rate. This increase followed almost no growth in the first quarter, when winter storms disrupted sales of motor vehicles and spending on consumer goods generally ebbed after the fourth-quarter surge. Cutting through these gyrations, real consumer spending grew moderately over the first half of the year, about in line with growth in real income.

Real expenditures on motor vehicles and parts posted a sizable gain in the first six months of the year, rising more than 9 percent at an annual rate. Although sales of new cars and light trucks declined about 3 percent in July, to 13.9 million units (annual rate), part of this weakness reportedly reflected a shortage of some popular models as well as some small disruptions of sales in the Mississippi basin region.

SALES OF AUTOMOBILES AND LIGHT TRUCKS[1]
(Millions of units at an annual rate; BEA seasonals)

	1991	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June	1993 July
Total	12.30	12.85	13.24	13.12	14.35	14.41	14.41	13.86
Autos	8.39	8.38	8.38	8.30	9.04	9.11	9.10	8.73
Light trucks	3.91	4.46	4.86	4.82	5.31	5.30	5.31	5.13
North American[2]	9.73	10.51	11.02	10.92	12.05	12.00	12.27	11.66
Autos	6.14	6.28	6.38	6.32	6.94	6.91	7.14	6.74
Big Three	4.99	5.10	5.18	5.29	5.73	5.70	5.86	5.31
Transplants	1.14	1.18	1.20	1.04	1.21	1.21	1.28	1.43
Light trucks	3.59	4.23	4.64	4.60	5.11	5.09	5.13	4.92
Foreign produced	2.57	2.34	2.22	2.20	2.30	2.40	2.15	2.20
Autos	2.25	2.11	2.01	1.97	2.10	2.20	1.96	1.99
Light trucks	.32	.23	.21	.23	.20	.20	.19	.21
Memo:								
Domestic nameplate								
Market share, total	.70	.72	.73	.74	.75	.74	.75	.73
Autos	.63	.63	.64	.66	.66	.65	.67	.64

Note: Data on sales of trucks and imported autos for the current month are preliminary and subject to revision.
1. Components may not add to totals because of rounding.
2. Excludes some vehicles produced in Canada and Mexico that are classified as imports by the industry.

The higher level of motor vehicle demand this year follows two years in which total sales fell roughly 2-1/2 million units per year short of the average pace of sales during the late 1980s. In addition to replacement demand, sales have been supported by the continuation of low finance rates and by the modest size of price increases, on average, despite noticeable price hikes for Japanese imports. In June, the CPI for new cars rose 0.2 percent, and was only 2-1/4 percent higher than a year earlier. Prices of new trucks increased 0.4 percent in June and have risen 3-1/4 percent over the past year.

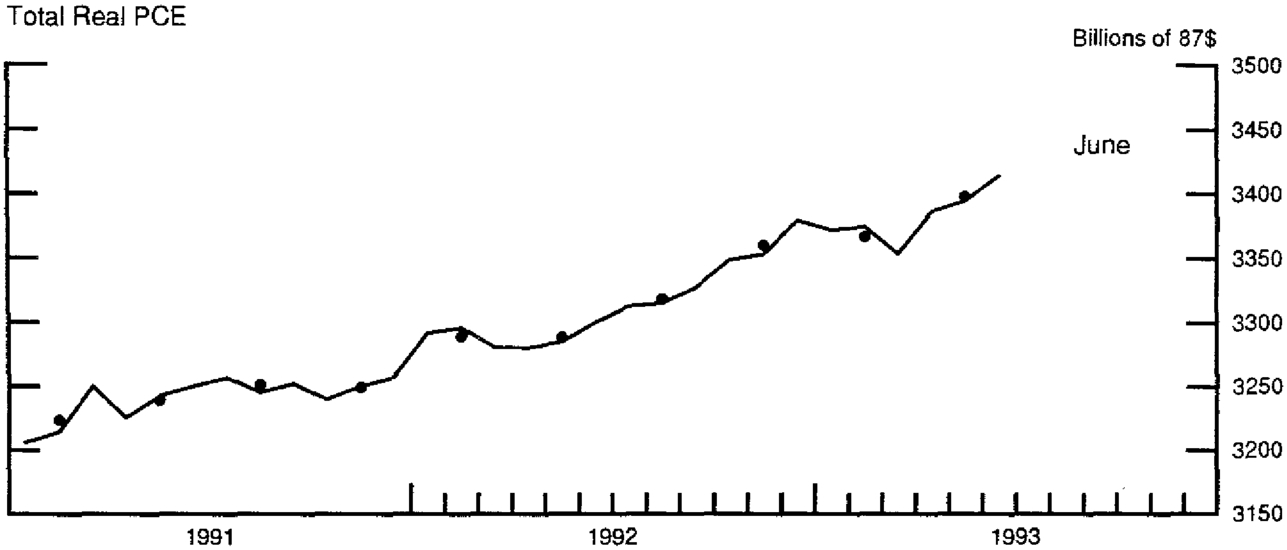
However, looming on the horizon are potentially sizable price increases for the 1994 models of foreign makes, particularly Japanese, as a result of recent movements in exchange rates. In addition, GM's recently announced price increases for its new models, which will average about 2 percent when the cost of enhanced safety and convenience equipment is excluded, are likely to boost average sticker prices about 7 percent. With regard to incentives, price breaks have been expanded further and are available on a wide range of makes and models--but discounts are not generally as deep as seen at the ends of some recent model years.

Real spending on durable goods other than motor vehicles advanced at a relatively brisk pace in the second quarter, rising 5-1/2 percent at an annual rate after growing at a 3-1/2 percent rate in the first quarter. Growth in this component of spending mainly reflects rising purchases of furniture and household equipment. Much of this spending is probably the result of the rising trend of home sales, but with household balance sheets in better shape, consumers may also be more willing to buy big-ticket items even if they must borrow to do so. From a longer perspective, spending on durables other than motor vehicles (as well as total durables) during the current expansion has risen as a share of total personal consumption expenditures but by substantially less than in earlier expansion periods.

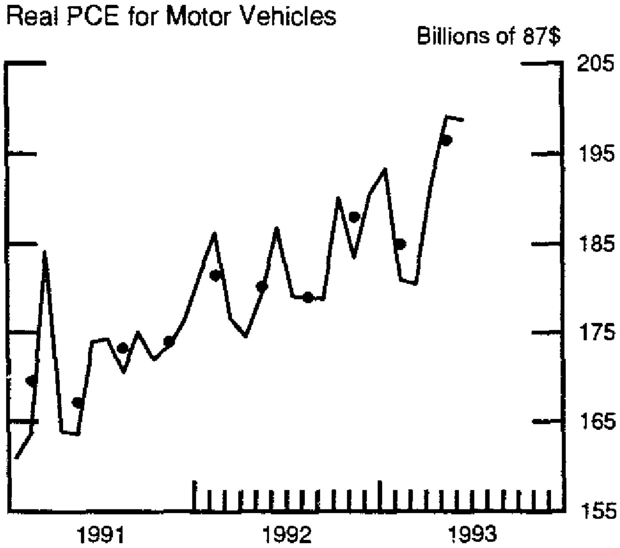
Real outlays for nondurable goods grew at a 2-1/2 percent annual rate in the second quarter after a first-quarter decline. Although spending on nondurable goods has bounced around a lot--even on a quarterly average basis--the level of outlays in the second quarter appeared to be back on the 2 percent (annual rate) trend that has prevailed since the latter part of 1991 (chart).

Personal Consumption Expenditures

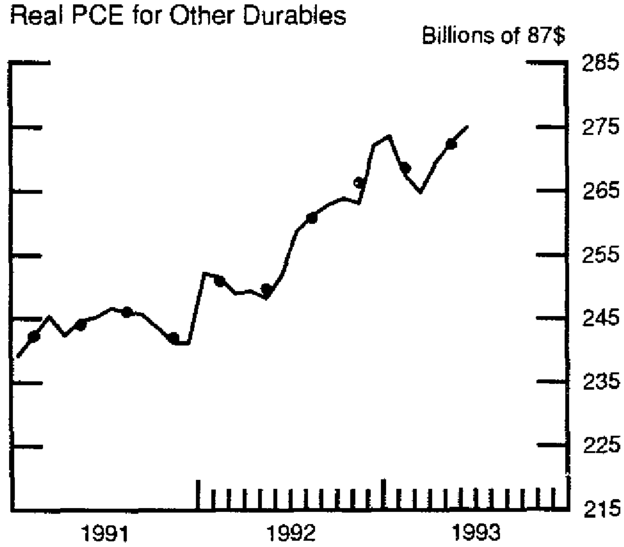
Total Real PCE



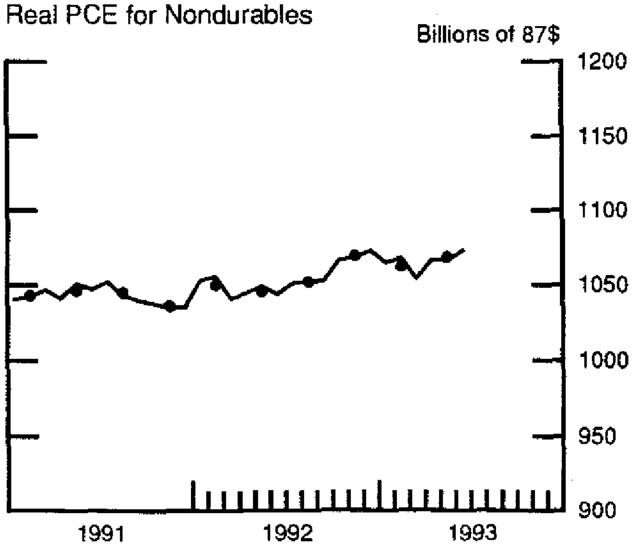
Real PCE for Motor Vehicles



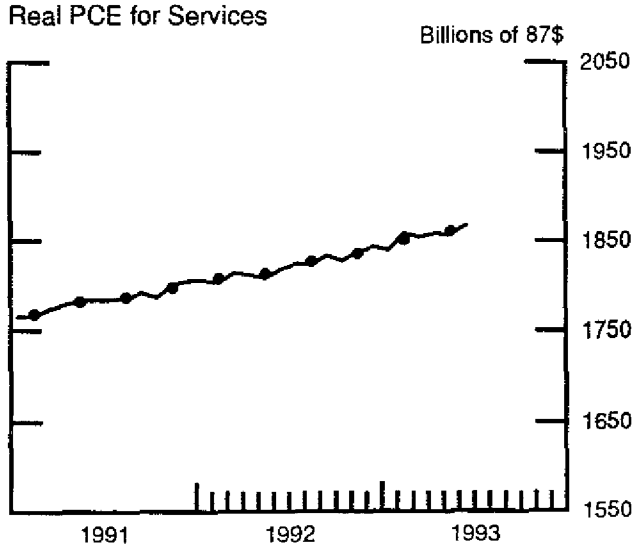
Real PCE for Other Durables



Real PCE for Nondurables

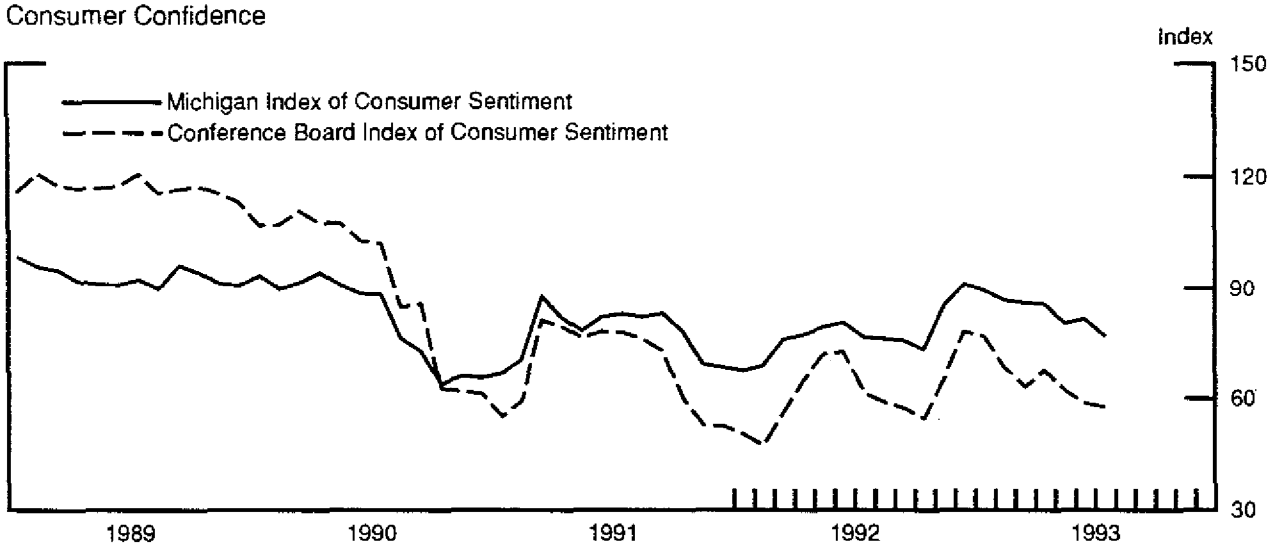


Real PCE for Services

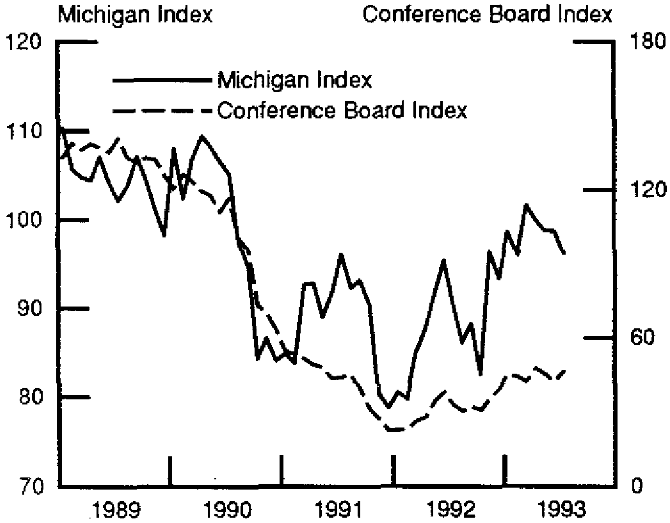


Indicators of Consumer Sentiment

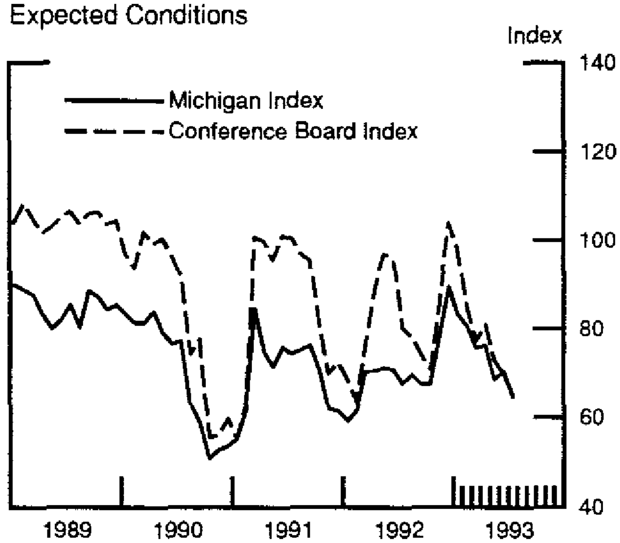
Consumer Confidence



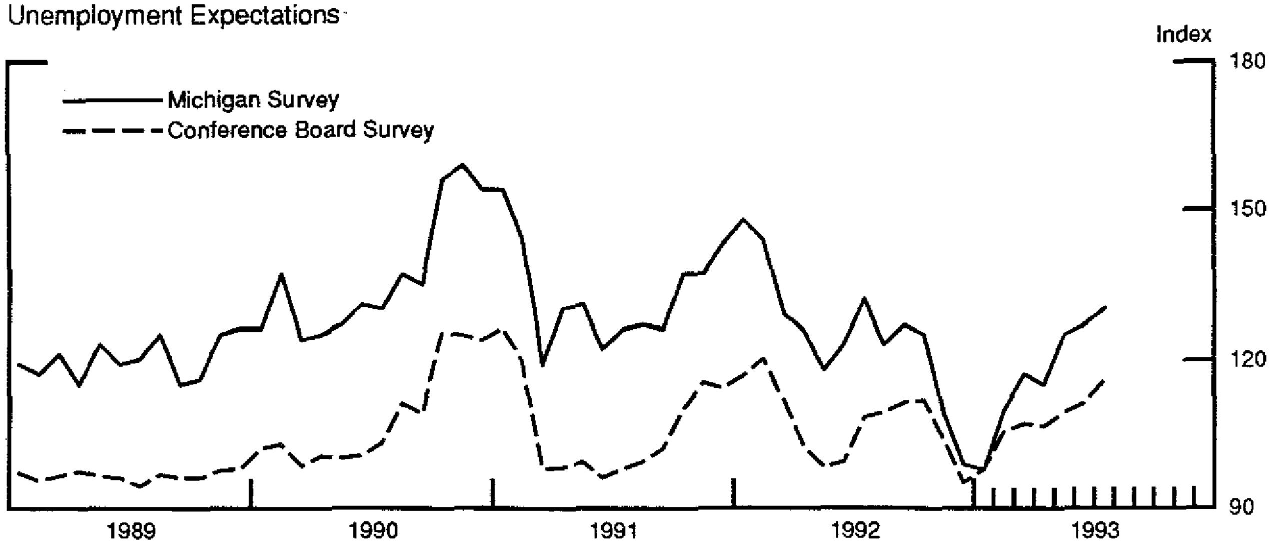
Current Conditions



Expected Conditions



Unemployment Expectations



Real expenditures on services grew at a 2-1/4 percent annual rate in the second quarter, held down by unusually low utilities bills; excluding energy, services spending grew at about a 2-3/4 percent annual pace, led by a surge in air travel. On balance, real consumption of services has been on a gradual 2-1/4 percent (annual rate) uptrend since early 1991.

Underpinning these spending developments has been moderate trend growth in real disposable personal income. Real DPI rose around 2-1/2 percent in 1992, and at about a 2 percent annual rate in the first half of 1993. Fluctuations in subsidy payments to farmers, and the timing of year-end bonus payments, have caused some volatility in the growth of real DPI in the last several quarters. Looking over a longer period, real labor income has grown at about a 2-1/4 percent annual rate since the fourth quarter of 1991. Further, the July employment report is consistent with continued growth in real labor income.

The recent increases in consumer spending have come about despite an ongoing erosion of consumer confidence. Both the Michigan and the Conference Board indexes of consumer sentiment continued to fall through July and are now back near the levels that prevailed before the onset of the post-election euphoria (chart). The deterioration of attitudes largely reflects increased pessimism about the prospects for the economy; assessments of current conditions have not shown much change since January. Likewise, responses regarding households' expectations for job market conditions, which are correlated with spending, have turned decidedly more pessimistic this year.

Housing Markets

Most housing sector indicators were up substantially in the second quarter compared with a year earlier, although they generally remained slightly below the highs reached in the fourth quarter of 1992. Protracted heavy rainfall in parts of the Midwest hampered construction in the second quarter, and the flooding that subsequently occurred likely will have a small effect on residential construction expenditures in July and in the third quarter.[1]

Total housing starts were unchanged in June, following an upward revision to a relatively robust May reading, and were well above the level in the first quarter and a year earlier. Starts in the dominant single-family sector decreased in June to an annual rate of 1.08 million units, after a strong increase in May; the June level is better aligned with the recent pace of construction permits and new home sales, relative to historical norms.

Sales of single-family homes also increased, on average, during the second quarter. Sales of new homes rose 11 percent in June to one of the highest levels in the past three-and-one-half years, and sales of existing homes increased slightly, both in June and for the second quarter as a whole. According to anecdotal reports from parts of the South and the Midwest, rising new home sales have outstripped the pace of new construction, shrinking the inventory of homes for sale and placing upward pressure on home prices.

Nationally, price increases for new and existing homes picked up during the second quarter, with special factors probably explaining some of the increases. Average selling prices of both new and existing homes rose about 2 percent from a year earlier; median prices increased somewhat more rapidly, at rates akin to those observed in the fourth quarter of 1992, when construction and sales activity were relatively strong. The constant-quality price index for new homes, which adjusts for compositional changes in house quality and the regional mix of sales, rose 5.8 percent from a

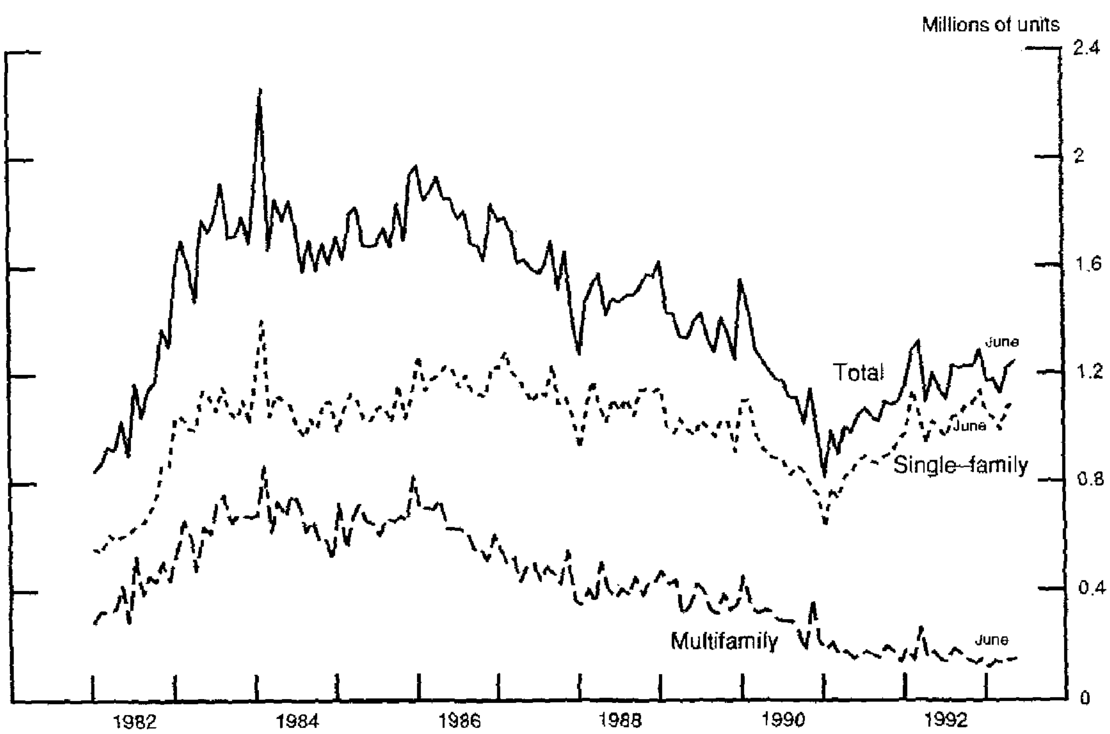
1. In the upper Mississippi valley, April-June 1993 was the wettest period since recordkeeping began ninety-nine years ago.

PRIVATE HOUSING ACTIVITY
(Millions of units; seasonally adjusted annual rates)

	1992	1992	1993		1993		
	Annual	Q4	Q1	Q2p	Apr.r	Mayr	Junep
All units							
Starts	1.20	1.25	1.16	1.24	1.21	1.25	1.25
Permits	1.11	1.16	1.11	1.11	1.10	1.12	1.11
Single-family units							
Starts	1.03	1.10	1.03	1.08	1.06	1.11	1.08
Permits	.92	.99	.93	.92	.93	.92	.93
Sales							
New homes	.61	.64	.60	.66	.70	.61	.68
Existing homes	3.52	3.87	3.54	3.59	3.45	3.62	3.69
Multifamily units							
Starts	.17	.15	.13	.16	.15	.14	.18
Permits	.19	.17	.18	.19	.18	.20	.18

p Preliminary. r Revised estimates.

PRIVATE HOUSING STARTS
(Seasonally adjusted annual rate)



year earlier, the largest increase in this series since late 1987; however, this rise may be exaggerated somewhat by an unrepresentative set of regional weights in the index.[2] Also, rising new home prices in some areas may reflect the cost of lumber acquired when mill prices temporarily rose sharply earlier this year owing to a perceived shortage.[3] In addition, a shortage of developed lots in some localities may be contributing to firming prices.

Several indicators suggest that the market for single-family homes continued to strengthen in July (chart). Responding particularly to continued declines in mortgage rates, consumer attitudes toward homebuying rose to one of the most positive levels on record. Also, an index of applications filed at mortgage bankers for loans to purchase a new or existing home remained high throughout July, and builders' ratings of new home sales improved substantially.

Despite the June pickup in the pace of multifamily housing starts to 175,000 units at a seasonally adjusted annual rate, these starts remain only slightly above their record low. Any lasting improvement in multifamily construction continues to be impeded by a persistent oversupply of rental apartments and the resulting restraint on rents.

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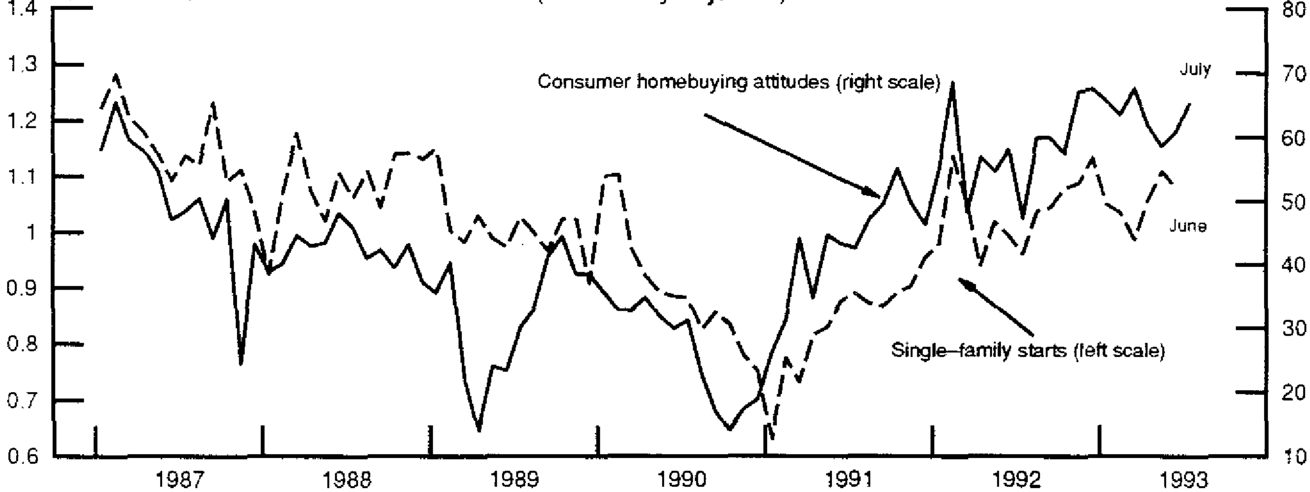
2. In 1993:Q2, the median new home transaction price for the Northeast rose 13.3 percent from the first-quarter level, compared with 0.7 percent for the unweighted median price for the nation. The constant-quality measure uses 1987 weights; thus, price changes in the Northeast are weighted more heavily than would be warranted by the current proportion of national new home sales in that region, owing to a sharp decline in sales there in recent years.

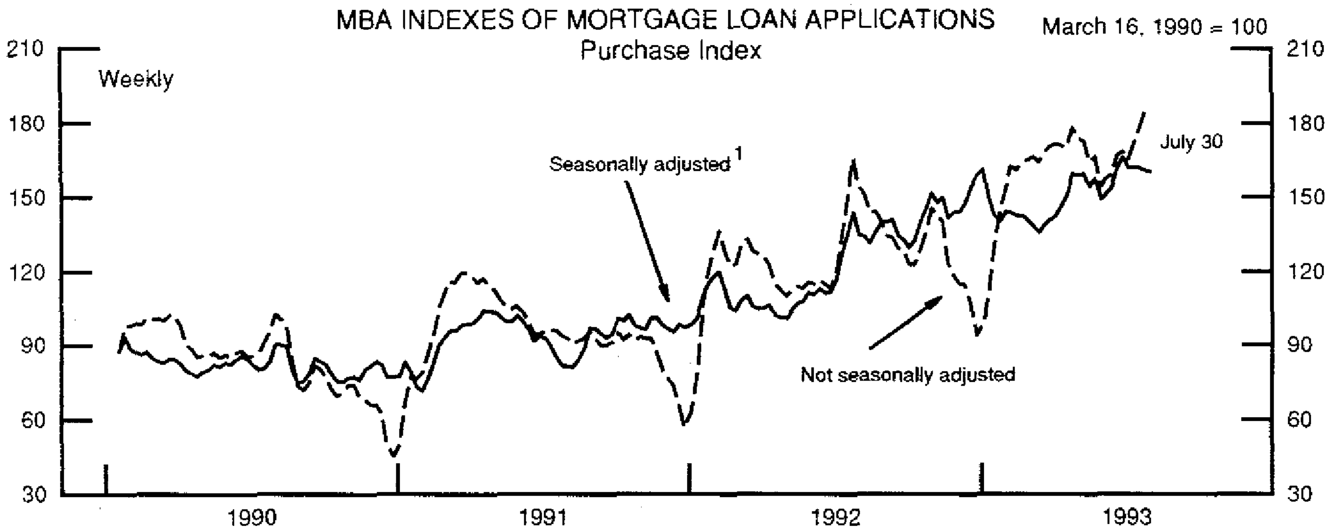
3. The mill price of lumber doubled during the winter, reaching a peak of nearly $475 per thousand board feet in the second half of March. Prices then plunged during the second quarter, to a low of $218 per thousand board feet in early July. More recently, prices have turned up, with the reading for the week ended August 6 at $280 per thousand board feet.

CONSUMER HOMEBUYING ATTITUDES[1]
(Seasonally adjusted)



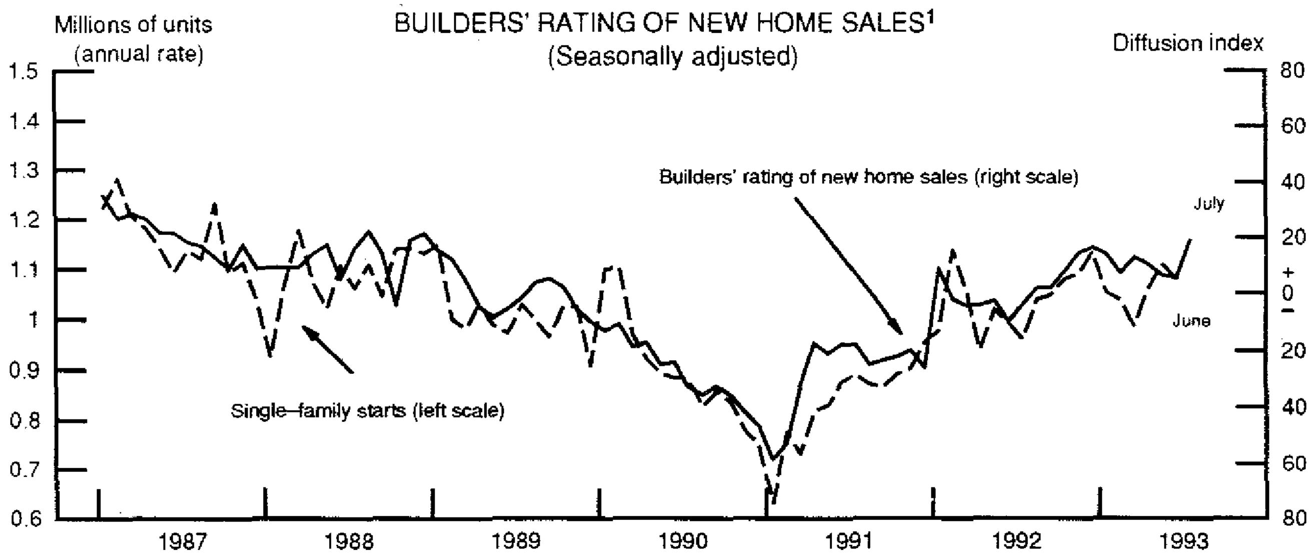
1 The homebuying attitudes index is calculated by the Survey Research Center (University of Michigan) as the proportion of respondents rating current conditions as good minus the proportion rating such conditions as bad.

MBA INDEXES OF MORTGAGE LOAN APPLICATIONS
Purchase Index



1. Seasonally adjusted by Federal Reserve Board Staff

BUILDERS' RATING OF NEW HOME SALES[1]
(Seasonally adjusted)



1 The index is calculated from National Association of Homebuilders data as the proportion of respondents rating current sales as good to excellent minus the proportion rating them as poor.

Business Fixed Investment

Real business fixed investment advanced 13 percent at an annual rate in the second quarter, a pace roughly similar to that of the first quarter.[4] Investment in nonresidential structures posted its largest advance in three years. On the equipment side, the nominal value of shipments of nondefense capital goods was flat in the second quarter, but rapid price declines for office and computing equipment boosted real spending; in addition, purchases of motor vehicles were strong. From the limited information available on the third quarter, the growth of equipment spending appears to be subsiding a bit.

Sales of heavy trucks in the second quarter were 12 percent above their first-quarter level. When these sales fell sharply between 1988 and 1991, the average age of trucks in use rose noticeably. The resulting increase in replacement demand, as well as ongoing technological improvements, likely have provided a sizable impetus to sales this year; indeed, both major heavy truck manufacturers, Navistar and Freightliner, are operating at or near capacity. Business purchases of automobiles and light trucks were also very high in the second quarter.

Business spending on office and computing equipment advanced at more than a 15 percent annual rate in the second quarter, after having increased at an annual rate of close to 100 percent in the first quarter. Although nominal orders and shipments of computers flattened in the second quarter, rapid price declines nonetheless led to a healthy increase in real expenditures. In the third quarter, however, the downtrend in computer prices may be sidetracked by repercussions of a fire that recently destroyed the

4. Data released since GDP data were released imply only a slight downward revision to second-quarter business fixed investment.

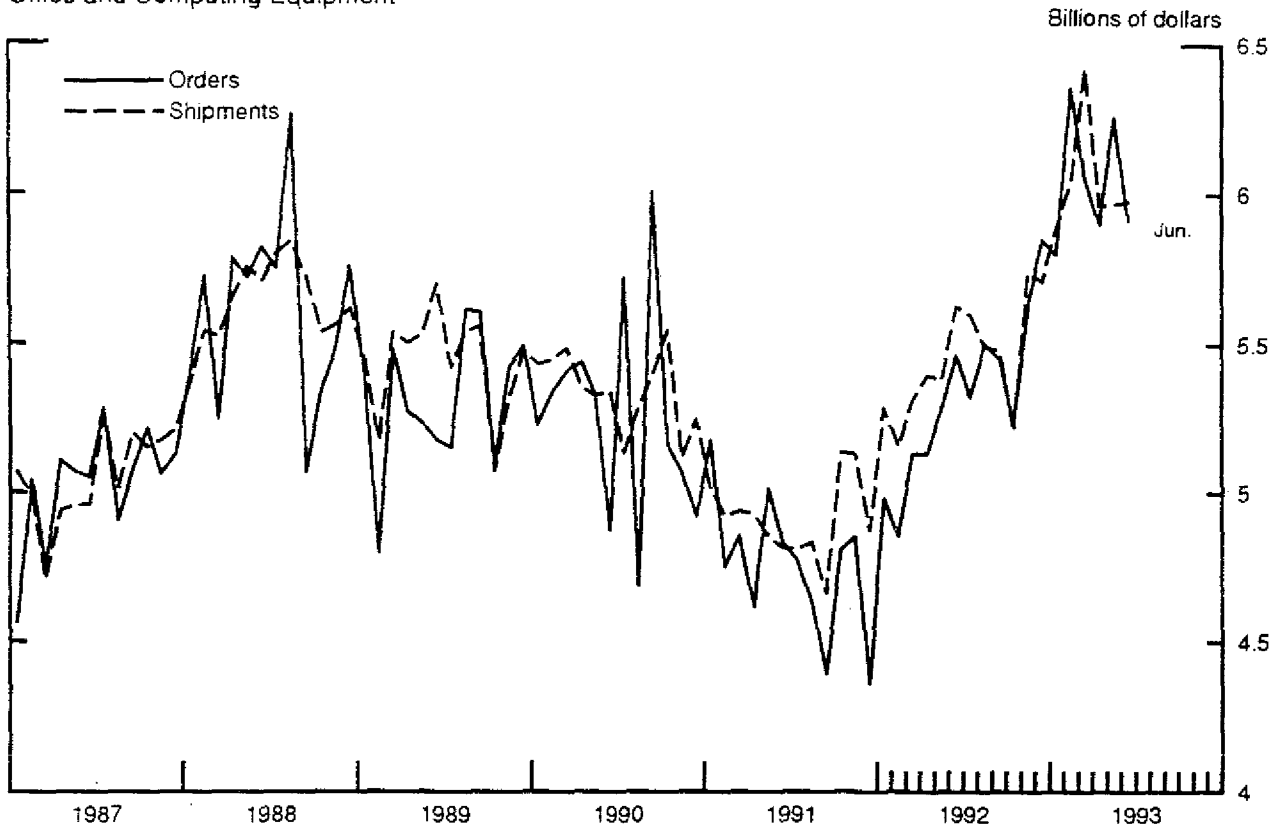
BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period;
based on seasonally adjusted data, in current dollars)

	1992	1993		1993		
	Q4	Q1	Q2	Apr.	May	June
Producers' durable equipment						
Shipments of nondefense capital goods	3.4	1.1	1.0	-3.8	1.5	2.2
Excluding aircraft and parts	2.6	3.3	.8	-3.8	1.4	.6
Office and computing	.6	10.1	-2.4	-7.1	.1	.2
All other categories	3.1	1.5	1.7	-2.8	1.8	.8
Shipments of complete aircraft[1]	4.9	21.5	n.a.	-15.3	-.8	n.a.
Sales of heavy weight trucks	6.8	3.1	11.8	4.1	-.2	2.7
Orders of nondefense capital goods	3.7	1.5	3.6	4.6	-1.7	11.5
Excluding aircraft and parts	4.2	4.4	.6	.4	-2.5	.9
Office and computing	2.6	9.0	-.7	-2.5	6.1	-5.5
All other categories	4.6	3.1	.9	1.2	-4.9	2.8
Nonresidential structures						
Construction put-in-place	1.4	.2	2.8	-.2	2.6	-.4
Office	-.3	-2.2	.0	3.3	.1	-3.8
Other commercial	2.8	4.9	2.3	1.8	.5	.7
Industrial	-1.2	6.2	-4.9	-12.0	3.3	-3.0
Public utilities	4.6	-4.3	4.1	1.5	1.6	2.3
All other	-1.2	-.4	8.6	2.8	6.3	-1.6
Rotary drilling rigs in use	14.5	-8.2	-5.3	1.9	2.6	6.6
Footage drilled[2]	10.5	2.5	-6.4	-5.0	22.4	9.7
Memo:						
Business fixed investment[3]	9.7	13.1	13.3	n.a.	n.a.	n.a.
Producers' durable equipment[3]	14.5	18.3	16.5	n.a.	n.a.	n.a.
Nonresidential structures[3]	-1.9	.0	4.8	n.a.	n.a.	n.a.

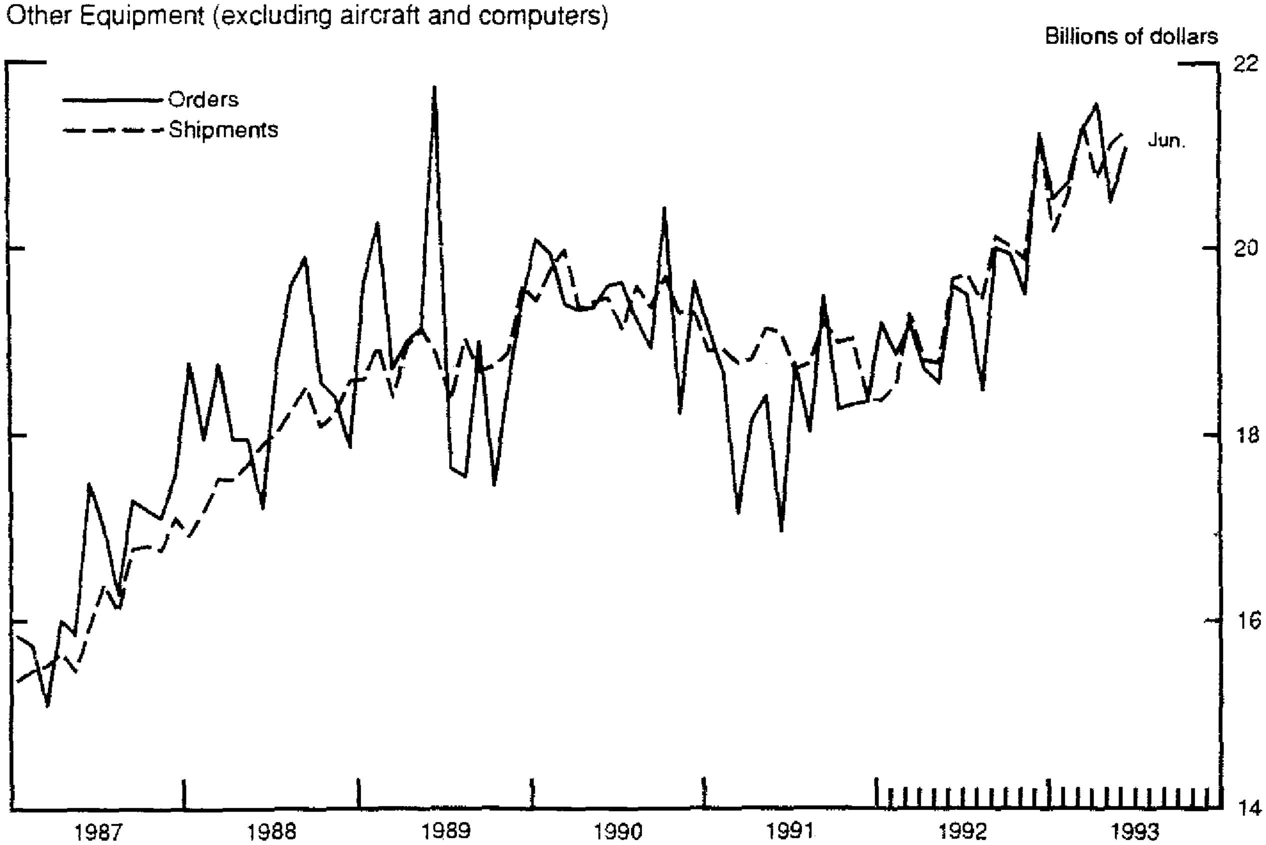
1. From the Current Industrial Report "Civil Aircraft and Aircraft Engines." Monthly data are seasonally adjusted using FRB seasonal factors constrained to BEA quarterly seasonal factors. Quarterly data are seasonally adjusted using BEA seasonal factors.
2. From Department of Energy.
3. Based on constant-dollar data; percent change, annual rate.
n.a. Not available.

RECENT DATA ON ORDERS AND SHIPMENTS

Office and Computing Equipment

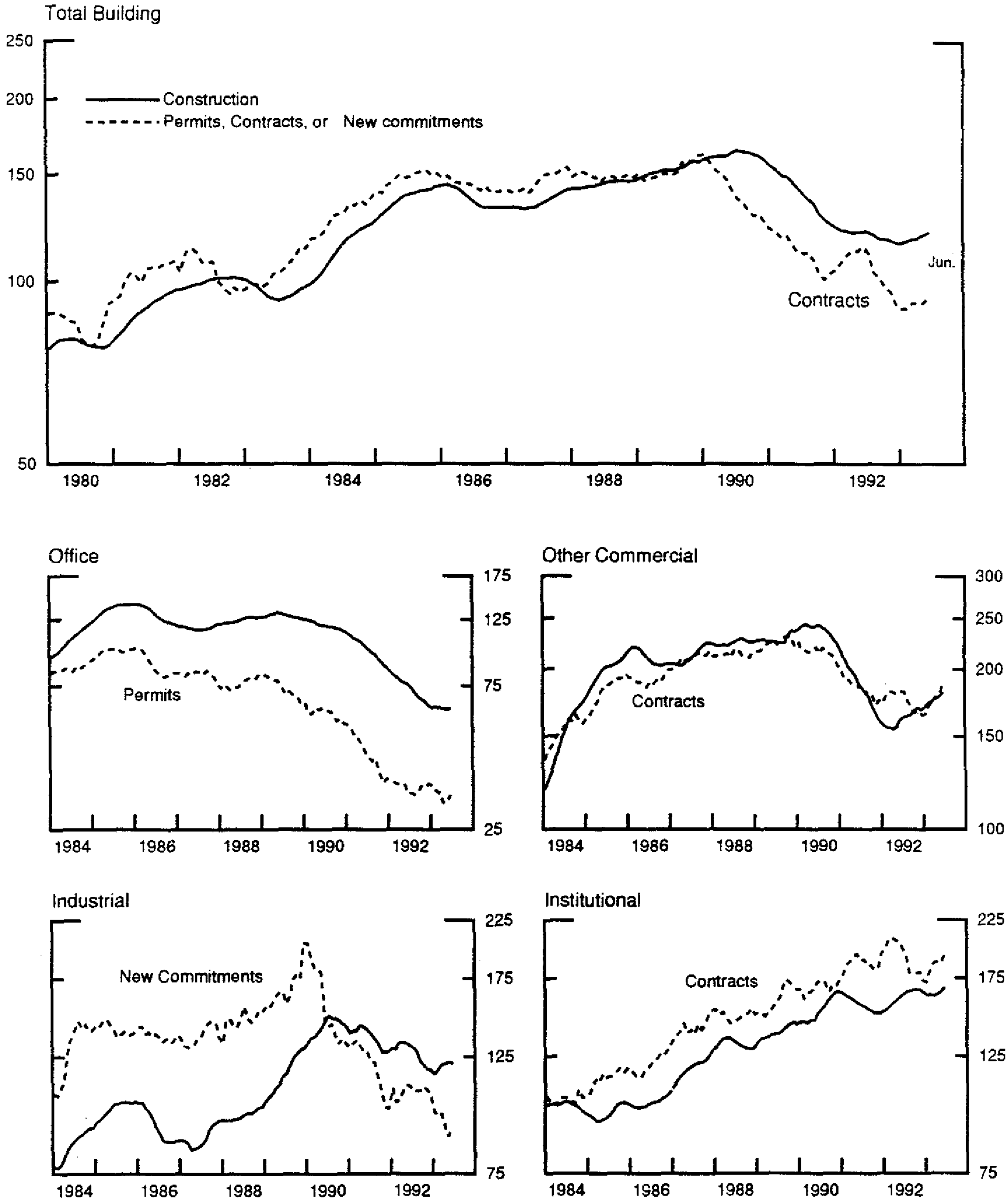


Other Equipment (excluding aircraft and computers)



NONRESIDENTIAL CONSTRUCTION AND SELECTED INDICATORS*

(Index, Dec. 1982 = 100, ratio scale)



*Six-month moving average for all series shown. For contracts, individual sectors include private & public buildings. All other include private only. New commitments are the sum of permits and contracts.

Sumitomo chemical plant in Japan. That plant produced 40 percent to 60 percent of the world's supply of Bakelite epoxy resin, a crucial ingredient in many semiconductors. Spot markets responded rapidly to the bad news in mid-July: Prices for computer memory chips (DRAMS) have doubled since the fire. The major computer manufacturers reportedly have large inventories of the affected components, but a scramble is nonetheless under way to find substitutes and alternative suppliers. Sumitomo has indicated that it has two months' supply of the resin and currently is talking with unnamed third parties about possibly assisting with stop-gap supplies. The total effect of these developments on computer output and prices remains uncertain, but further steep declines in computer prices in the third quarter appear unlikely, and some potential purchasers could be inclined to postpone spending.

Outlays for aircraft declined 23 percent at an annual rate in the second quarter, retracing some of the strong first-quarter advance. The news about this sector has been bleak for some time, and Boeing expects shipments for the remainder of the year to be 20 percent below the level for the same period last year. Continental Airlines' recent announcement of modernization plans, which include seventeen new orders for Boeing, will not affect shipments for two years or more. McDonnell-Douglas has received more cancellations than orders this year and is now encouraging past clients to refurbish older aircraft.

Business purchases of equipment excluding aircraft, computers, and motor vehicles posted a solid increase in the second quarter. Spurred by strong demand from automotive parts manufacturers, outlays for metalworking machine tools advanced notably in the second quarter and are now 16 percent above their level of a year ago. Outlays for industrial machinery, communications equipment, and construction machinery were all strong as well. On the structures side, second-quarter outlays rose 4.8 percent at an annual rate but remained depressed, at levels not seen since the late 1970s. Expenditures rose across a broad array of categories in the second quarter, with institutional and public utilities investment posting double-digit growth rates.

Looking forward, orders for capital goods excluding aircraft and computers rose 2-3/4 percent in June and have advanced steadily since early 1992. The demand for communications equipment from both domestic and foreign purchasers has been especially strong of late, advancing 19 percent in the second quarter. On the whole, the backlog of orders for other capital goods increased over the first half of 1993, and the growth rate for shipments of other capital goods should be healthy in the current quarter as shipments continue to catch up to orders. The limited data in hand are consistent with moderate growth in structures investment in the current quarter. Both permits and contracts were up substantially in June; over the first half of 1993, permits rose 5.5 percent and contracts were up 4.3 percent. Finally, the Baker-Hughes index of footage drilled jumped in July, likely in response to the strength of natural gas prices, suggesting that drilling activity is picking up after a pause in the first and second quarters.

Business Inventories

Business inventories expanded moderately during the second quarter. Stocks in manufacturing and trade rose at an annual rate of about $13 billion in constant-dollar terms in April and May, and Census surveys indicate that manufacturing and wholesale inventories rose $3.7 billion in current-cost terms in June.[5] These moderate

5. The second-quarter increases in manufacturing and wholesale inventories currently reported in Census surveys appear consistent with BEA's inventory assumptions underlying the advance GDP
(Footnote continues on next page)

buildups appear to have kept stocks broadly in line with sales.

The constant-dollar figures for April and May, as now reported, show smaller accumulations in manufacturers' stocks than did the estimates available at the time of the last FOMC meeting. BEA's revision to real factory inventories in April was particularly surprising because its direction was opposite that of the Census Bureau's revision to the current-cost inventory change (BEA's source data) in April; it also ran contrary to what BEA's "concurrent" seasonal adjustment for April would suggest. BEA analysts informed us that the downward revision was largely a result of new and higher inventory acquisition cost indexes for the manufacturing sector, reflecting updated estimates of monthly unit labor costs.

In manufacturing, stocks (in current costs) held by aircraft producers posted another sizable decline in June, continuing a two-year downtrend that likely reflects the weak market outlook for both the commercial airline industry and defense contractors. Outside of aircraft, manufacturers' inventory changes were mixed in June: Accumulations of stocks at producers of industrial machinery, food products, and apparel were partially offset by drawdowns in many other industries. By stage of processing, a sizable rise in factory shipments drew down finished goods inventories in June; work-in-process stocks expanded in June, while stocks of production materials and supplies were trimmed. The manufacturers' inventory-to-shipments ratio fell in June to 1.47 months, one of the lowest levels in recent years.

In the trade sector, wholesale inventories expanded moderately in June, with stocks held by distributors of motor vehicles,

(Footnote continued from previous page)

estimate. The Census retail inventory data for June will be released on August 13.

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars at annual rates;
based on seasonally adjusted data)

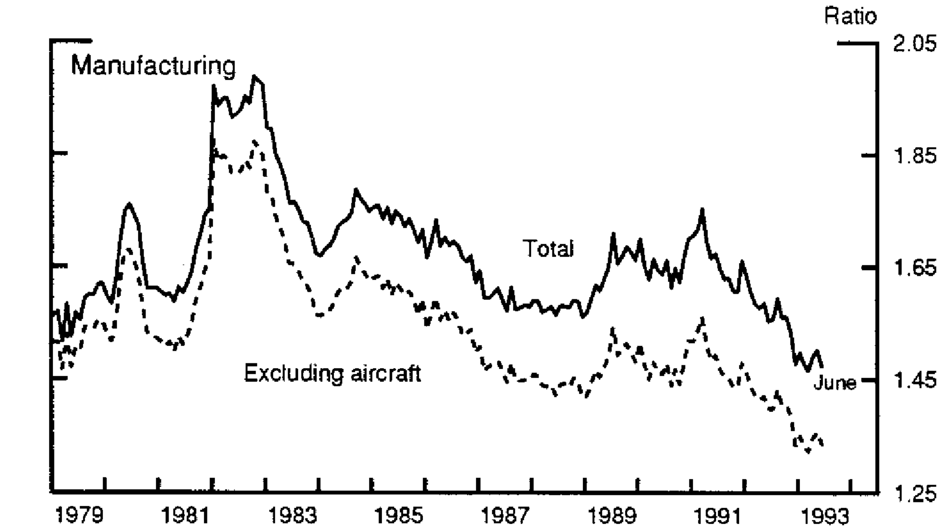
	1992	1993		1993		
	Q4	Q1	Q2	Apr.	May	June
Current-cost basis						
Total	20.4	39.9	n.a.	40.6	19.5	n.a.
Excluding auto dealers	11.7	20.6	n.a.	37.2	30.0	n.a.
Manufacturing	-19.1	1.2	7.3	9.2	15.4	-2.7
Defense aircraft	-2.0	-4.4	-.1	-2.0	3.1	-1.4
Nondefense aircraft	-2.8	.0	-3.1	-4.3	-1.1	-3.8
Excluding aircraft	-14.3	5.6	10.4	15.5	13.4	2.4
Wholesale	16.5	5.1	8.9	16.3	4.0	6.4
Retail	23.1	33.6	n.a.	15.1	.1	n.a.
Automotive	8.7	19.3	n.a.	3.4	-10.5	n.a.
Excluding auto dealers	14.4	14.3	n.a.	11.7	10.6	n.a.
Constant-dollar basis						
Total	7.1	22.4	n.a.	15.7	10.1	n.a.
Excluding auto dealers	5.0	5.6	n.a.	10.8	14.4	n.a.
Manufacturing	-14.5	1.8	n.a.	-2.4	6.0	n.a.
Wholesale	9.6	-4.1	n.a.	9.1	3.9	n.a.
Retail	12.0	24.7	n.a.	9.0	.2	n.a.
Automotive	2.1	16.8	n.a.	4.9	-4.3	n.a.
Excluding auto dealers	9.9	7.9	n.a.	4.1	4.5	n.a.

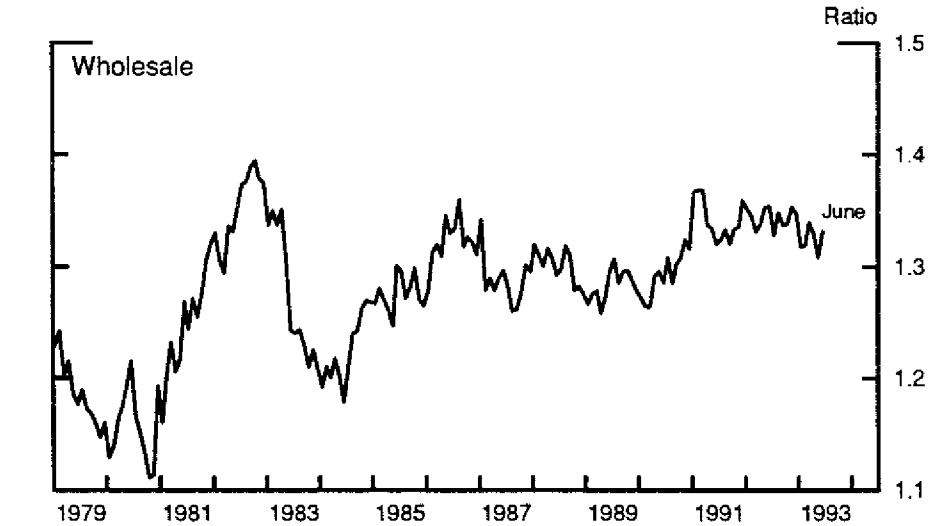
INVENTORIES RELATIVE TO SALES[1]
(Months supply; based on seasonally adjusted data)

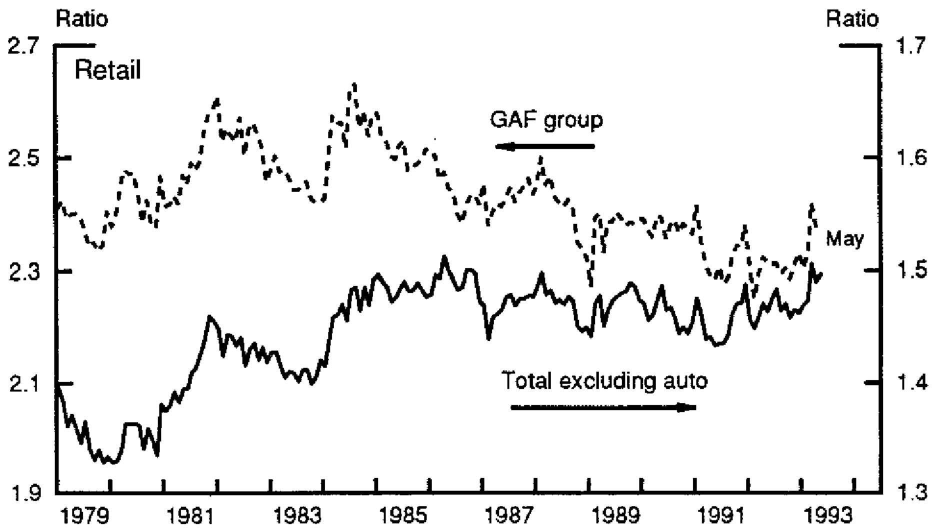
	1992	1993		1993		
	Q4	Q1	Q2	Apr.	May	June
Current-cost basis						
Total	1.48	1.47	n.a.	1.47	1.47	n.a.
Excluding auto dealers	1.46	1.44	n.a.	1.44	1.44	n.a.
Manufacturing	1.52	1.48	1.49	1.49	1.50	1.47
Defense aircraft	5.21	5.07	5.27	5.12	5.39	5.28
Nondefense aircraft	4.66	5.08	4.84	5.13	5.03	4.52
Excluding aircraft	1.37	1.34	1.35	1.35	1.36	1.34
Wholesale	1.35	1.33	1.33	1.33	1.31	1.33
Retail	1.55	1.60	n.a.	1.59	1.58	n.a.
Automotive	1.85	1.99	n.a.	1.94	1.89	n.a.
Excluding auto dealers	1.47	1.49	n.a.	1.49	1.50	n.a.
Constant-dollar basis						
Total	1.57	1.55	n.a.	1.57	1.56	n.a.
Excluding auto dealers	1.54	1.52	n.a.	1.53	1.53	n.a.
Manufacturing	1.63	1.59	n.a.	1.61	1.62	n.a.
Wholesale	1.41	1.38	n.a.	1.39	1.37	n.a.
Retail	1.62	1.66	n.a.	1.66	1.65	n.a.
Automotive	1.93	2.06	n.a.	2.04	2.00	n.a.
Excluding auto dealers	1.53	1.55	n.a.	1.55	1.55	n.a.

1. Ratio of end of period inventories to average monthly sales for the period.

RATIO OF INVENTORIES TO SALES
(Current-cost data)







FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis, billions of dollars, except where otherwise noted)

	Jun. 1992	Jun. 1993	Fiscal year to date FY1992	FY1993	Dollar change	Percent change
Outlays	117.1	117.5	1042.9	1059.5	16.6	1.6
Deposit insurance (DI)	1.4	-2.0	9.3	-20.5	-29.9	n.m.
Defense Cooperation account (DCA)	.0	.0	-5.2	.0	5.2	n.m.
Outlays excluding DI and DCA	115.7	119.5	1038.8	1080.1	41.3	4.0
National defense	25.9	24.8	226.1	218.8	-7.3	-3.2
Net interest	15.5	15.5	149.9	148.8	-1.1	-.7
Social security	27.2	28.7	215.1	227.9	12.9	6.0
Medicare and health	18.9	21.3	153.8	170.0	16.2	10.5
Income security	13.5	13.8	149.9	159.7	9.8	6.5
Other	14.8	15.4	144.0	154.9	10.9	7.6
Receipts	120.9	128.6	815.2	858.9	43.8	5.4
Personal income and social insurance taxes	91.5	94.9	666.1	699.3	33.2	5.0
Corporate income taxes	20.8	24.9	76.0	88.4	12.4	16.3
Other	8.6	8.8	73.1	71.3	-1.8	-2.4
Deficit(+)	-3.8	-11.1	227.8	200.6	-27.2	-11.9
Excluding DI and DCA	-5.2	-9.1	223.6	221.2	-2.4	-1.1

Details may not add to totals due to rounding.
n.m. - not meaningful

electrical goods, and machinery showing the largest increases. Despite declines in sales in June, inventory-to-sales ratios for most types of wholesale establishments remained well within their recent ranges. In retail trade, although the accumulation of nonauto inventories as a whole was moderate in April and May, stocks held by general merchandise, apparel, and furniture and appliance (GAF) stores have posted large increases since March. The inventory-to-sales ratio for GAF stores rose to the highest level since January 1991, with the exception of March of this year, when severe weather conditions distorted sales. However, GAF sales moved up moderately in June, according to the advance data from Census, and anecdotal reports indicate no significant imbalances in the retail sector in July.

Federal Sector

The deficit picture for FY93 continues to look brighter, though largely because of transitory developments such as reduced outlays for deposit insurance. In a preliminary midyear budget update last month, the Office of Management and Budget revised its deficit forecast down to $285 billion, about $35 billion lower than its April forecast. In addition to lower outlays for deposit insurance, the lower current figure reflects elimination of the "stimulus" outlays (except for the continuation of extended unemployment benefits) and the investment tax credit that were part of the President's April budget proposal. Through June, the deficit for the fiscal year was $200 billion, a decrease of $28 billion from the same period in the last fiscal year. Excluding deposit insurance and the defense cooperation account, though, the fiscal year deficit through June was $221 billion, nearly the same as last year.

Receipts for the fiscal year through June grew moderately overall, but corporate receipts showed particular strength, with a

16 percent increase over the same period last year. The increase in corporate receipts partly reflects stronger corporate profits, but it also reflects tightened provisions for payment of corporate estimated taxes, which require corporations to pay more of their estimated tax liability earlier in the year. Personal income and social insurance taxes together grew about 5 percent for the fiscal year through June, relative to the same period last year.

Outlays for Medicare and health programs are still rising rapidly, but the increases have been offset in part by falling interest payments and the continued decline in defense spending. Although spending in the Medicare and health category is up 10 percent for the fiscal year through June, the rate of growth continues to be much slower than it was in the two preceding fiscal years. Interest outlays through June are $1 billion lower than in the previous year. After a sharp plunge in the first quarter, nominal defense outlays rebounded in the second quarter, bringing outlays for the fiscal year to date in line with projections made for the year in the *Fiscal Year 1994 Budget*.

However, on an NIPA basis, real defense purchases declined only about $1 billion (annual rate) in the second quarter of 1993, after the sharp $19 billion drop in the first quarter.[6] Real nondefense purchases edged down in the second quarter and now are at the bottom of the range for this spending category since the end of 1991.

The main legislative news, discussed in detail in an appendix to this Greenbook, is the passage of a deficit-reduction bill by

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6. Although NIPA real defense purchases edged down between the first and second quarters of this year, defense outlays on a unified budget basis (converted to real terms using the NIPA defense deflator) rose. The reason for this discrepancy is that some of the higher unified defense outlays were progress payments for certain military procurement items that were not counted on a NIPA basis; the NIPA convention is to exclude such outlays until the items are completed and delivered.

the Congress and its signing by the President. In addition, both the House and the Senate have passed a bill providing $5.5 billion of relief to victims of the Midwestern flood. Of this, $2.4 billion is for agricultural subsidies, $1.1 billion is for the Federal Emergency Management Agency, and $0.5 billion is for guarantees of loans. In addition, $1.1 billion of contingency funds are available to be spent at the President's discretion.

State and Local Government Sector

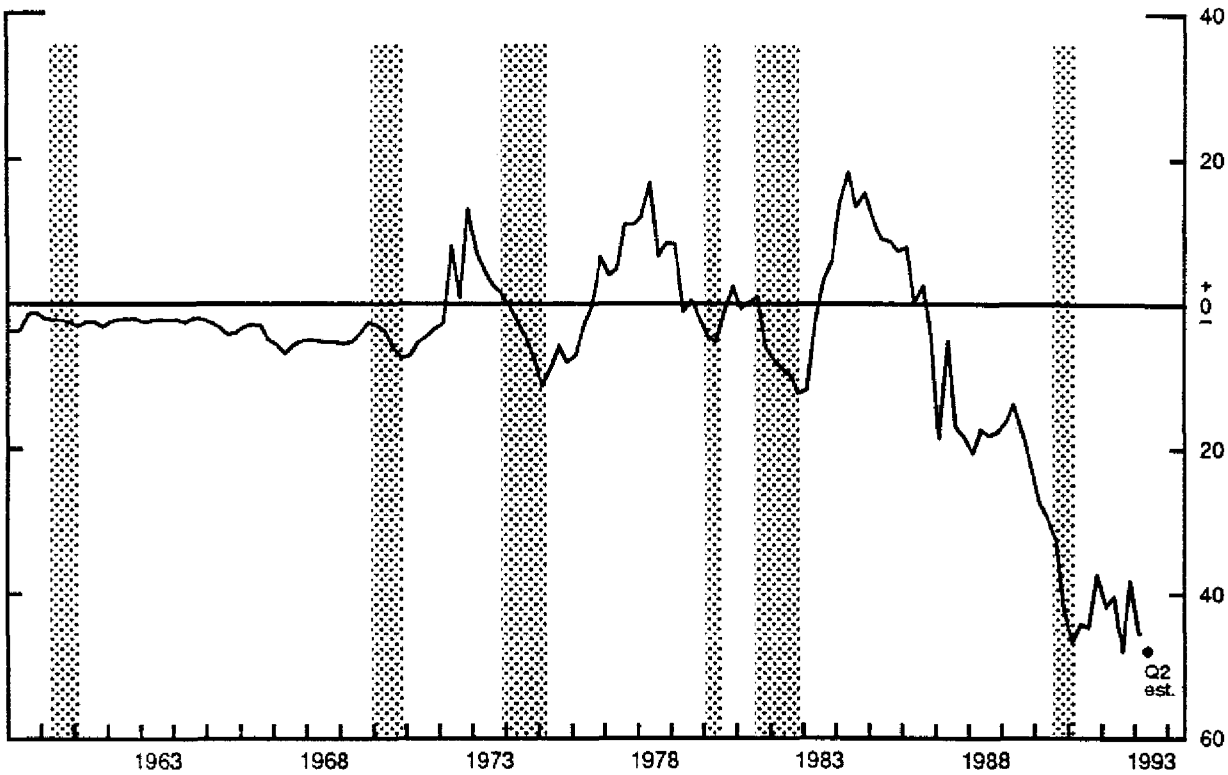
Real purchases of goods and services by the state and local government sector are estimated to have risen at a 2.3 percent annual rate in the second quarter, after having been about flat over the preceding four quarters. The rise was concentrated in construction outlays and is estimated to have held the sector's deficit on operating and capital accounts, excluding social insurance funds, in the $40 billion to $50 billion range that has prevailed since late 1990 (chart). Moreover, data available since the GDP release indicate that real construction spending was revised up in May and jumped 3.8 percent further in June, implying a likely upward revision to the second-quarter NIPA purchases figure.

Separate data on states and on local governments suggest that although the fiscal condition of states may be improving, cities continue to be plagued by shaky budgets. A recent survey of more than 1,600 cities with populations greater than 10,000 indicates that fiscal difficulties widened in FY93: Fifty-three percent of the cities reported that spending would exceed receipts during fiscal 1993, whereas 46 percent reported that spending had exceeded receipts in fiscal 1992 (chart). Factors contributing importantly to the budget problems included city employee health benefits, infrastructure needs, and unfunded federal and state mandates.

08/3/93

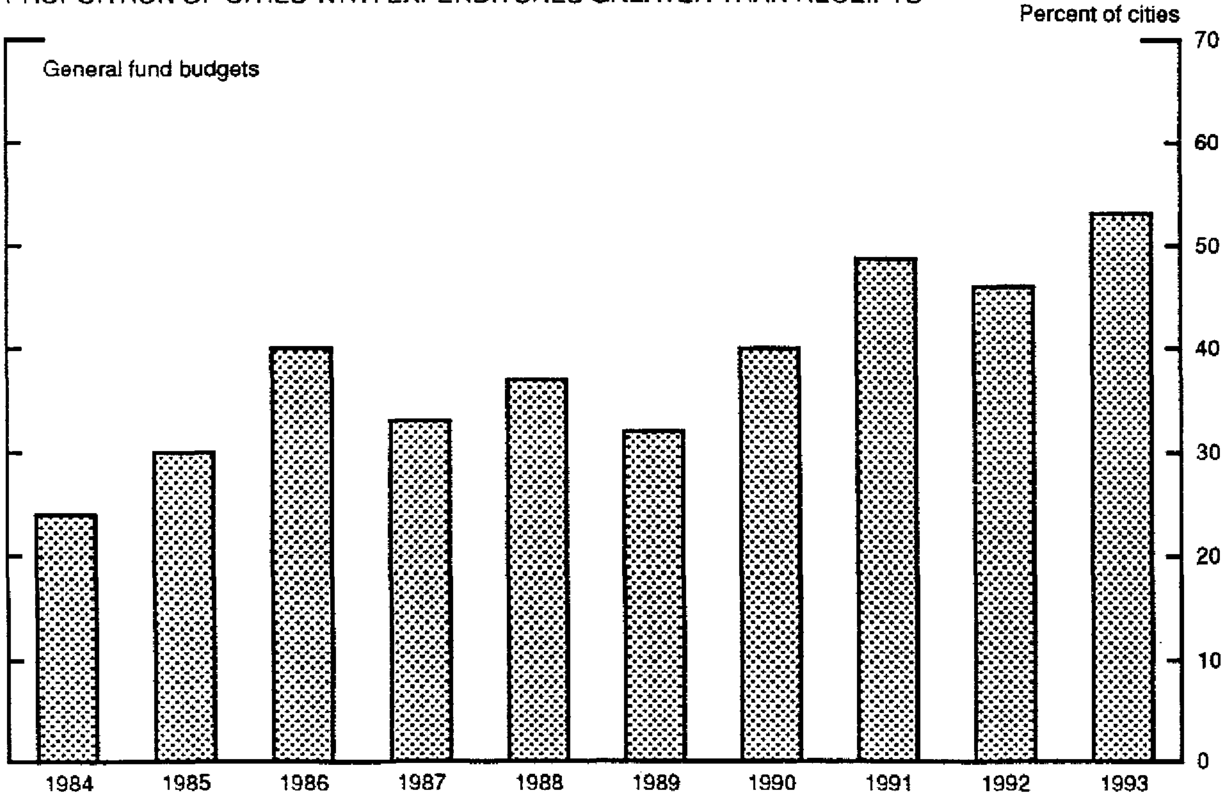
STATE AND LOCAL SECTOR

SURPLUS(DEFICIT)*



* Excludes social insurance funds; Q2 is a staff forecast.

PROPORTION OF CITIES WITH EXPENDITURES GREATER THAN RECEIPTS



Source: "City Fiscal Conditions in 1993," National League of Cities.

Disproportionately, cities in rural areas and in the Western and Midwestern census regions reported more difficulties.

Midwestern states and cities will no doubt be set back by the need to repair levees, roads, and other infrastructure after flooding subsides. Many local governments are expecting financial support from the states and, especially, the federal government, but it is too early to assess the cost of repairs. According to rating agencies, changes in the credit ratings of affected governments will be determined on a case-by-case basis. Credit ratings depend largely on long-term considerations, and downgrades could result if projected revenue streams, such as user fees generated by a utility, are adversely affected.[7] At this time, however, widespread downgradings are not expected.

Prices

In June, the overall consumer price index was unchanged, and the index excluding food and energy rose just 0.1 percent. This marked the second month of small increases, with the May CPI up just 0.1 percent. Over the second quarter (from March to June), the CPI rose just 2-1/4 percent at an annual rate, compared with 4 percent in the first quarter of the year.

Declines in prices of tobacco and apparel helped hold down both the overall CPI and the rate of core inflation in June. Tobacco prices fell 1-1/2 percent as price cuts announced in April were put in place by the cigarette manufacturers. Apparel prices fell at a 4-1/2 percent annual rate in the second quarter after moving up at an 8 percent rate in the first quarter. Among other goods, new car prices rose just 0.2 percent in June and have risen 2-1/4 percent

7. In late July, Fitch Investors Service Inc. upgraded Minnesota's general obligation rating to AAA, noting the state's healthy financial position; although analysts are anticipating some losses, they did not feel that the flood would have a major effect on the state's budget picture.

INFLATION RATES EXCLUDING FOOD AND ENERGY

	Percent change from six months earlier		
	Jun 1992	Dec 1992	Jun 1993
CPI	3.6	3.1	3.6
Goods	3.2	1.7	2.6
Alcoholic beverages	3.5	2.5	0.5
New vehicles	3.2	1.4	3.6
Apparel	2.8	-0.5	1.6
House furnishings	3.8	-0.7	0.7
Housekeeping supplies	.0	-0.5	2.8
Medical commodities	6.1	4.2	2.8
Entertainment	2.6	0.9	2.0
Services	3.8	3.8	4.2
Owners' equivalent rent	3.3	2.8	3.7
Tenants' rent	2.5	2.2	3.0
Other renters' costs	6.6	1.7	3.5
Airline fares	-12.5	29.9	11.2
Medical care	7.4	6.5	7.2
Entertainment	3.4	3.9	2.7
Auto financing	-10.9	-16.8	-3.7
PPI finished goods	2.7	1.2	2.4
Consumer goods	3.0	1.3	2.2
Capital goods, excluding computers	3.2	1.6	3.5
Computers	-17.7	-11.9	-16.7
PPI intermediate materials	1.8	0.5	2.1
PPI crude materials	10.1	2.0	17.4
Factors affecting price inflation			
ECI hourly compensation[1]	3.4	3.4	3.8
Goods-producing	4.0	3.5	4.7
Service-producing	3.1	3.2	3.3
Civilian unemployment rate[2,3]	7.6	7.1	6.8
Capacity utilization[2] (manufacturing)	78.6	79.8	80.3
Inflation expectations[3,4]			
Mean of responses	3.9	3.5	4.4
Median, bias-adjusted[5]	3.8	3.8	3.9
Non-oil import price[6]	0.8	0.8	1.4
Consumer goods, excluding autos, food, and beverages	2.6	1.7	1.3
Autos	-0.2	1.0	3.2

1. Private industry workers.
2. End-of-period value.
3. July values.
4. Michigan Survey one-year ahead expectations.
5. Median adjusted for average downward bias of 0.9 percentage points, relative to actual inflation, since 1978.
6. BLS import price index (not seasonally adjusted).

over the past twelve months. Increases in prices of services were also modest in June, with the CPI for services other than energy up just 0.2 percent. Owners' equivalent rent rose 0.4 percent, but this was offset by declines for out-of-town lodging, auto finance charges, and air fares.

Over the first six months of 1993, the CPI excluding food and energy rose 3.6 percent at an annual rate, the same as in the first six months of last year. Comparing these periods, price inflation for commodities other than food and energy was lower this year than last: 2-1/2 percent versus 3-1/4 percent. In contrast, prices of services other than energy rose 4-1/4 percent in the first half of 1993, compared with 3-3/4 percent in the first half of 1992. Within services, owners' equivalent rent is responsible for a sizable portion of the pickup, with prices increasing at a 3-3/4 percent annual rate over the first six months of the year, compared with a 3-1/4 percent annual rate in the first six months of 1992. Also, auto finance charges have not fallen as rapidly in 1993 as they did in 1992, because interest rate declines have been less pronounced this year. And, the deceleration of prices for medical care services stalled in the first part of 1993, with an increase of 7-1/4 percent at an annual rate in the first six months of the year, compared with 7-1/2 percent in the first six months of 1992. (By comparison, medical services prices had come down sharply in 1991 and 1992 from an increase of 10 percent in 1990.)

Energy prices in the CPI edged down 0.2 percent in June following a 1 percent drop in May. Gasoline prices fell 1 percent in June and are down 4-1/2 percent since February, owing mainly to an easing in crude oil costs. However, the CPI for natural gas posted a 1-1/2 percent increase in June, the fourth consecutive large monthly increase. Natural gas prices moved up sharply early

RECENT CHANGES IN CONSUMER PRICES
(Percent change; based on seasonally adjusted data)[1]

	Relative importance, Dec. 1992	1991	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June
				-----Annual rate------			-Monthly rate-	
All items[2]	100.0	3.1	2.9	3.2	4.0	2.2	.1	.0
Food	15.8	1.9	1.5	1.4	2.6	1.4	.4	-.4
Energy	7.3	-7.4	2.0	1.9	3.1	-3.8	-1.0	-.2
All items less food and energy	76.9	4.4	3.3	3.8	4.3	2.9	.2	.1
Commodities	24.7	4.0	2.5	1.5	4.6	.6	.0	-.1
Services	52.2	4.6	3.7	4.7	4.4	4.1	.3	.2
Memo:								
CPI-W[3]	100.0	2.8	2.9	3.2	4.1	2.0	.1	.0

1. Changes are from final month of preceding period to final month of period indicated.
2. Official index for all urban consumers.
3. Index for urban wage earners and clerical workers.

RECENT CHANGES IN PRODUCER PRICES
(Percent change; based on seasonally adjusted data)[1]

	Relative importance, Dec. 1992	1991	1992	1992 Q4	1993 Q1	1993 Q2	1993 May	1993 June
				-----Annual rate------			-Monthly rate-	
Finished goods	100.0	.1	1.6	-.3	3.9	1.0	.0	-.3
Consumer foods	22.4	-1.5	1.6	3.3	-2.2	1.9	-.1	-.9
Consumer energy	13.9	-9.6	-.3	-10.2	17.2	-4.0	-.6	-.5
Other finished goods	63.7	3.1	2.0	1.2	3.0	1.8	.2	-.1
Consumer goods	40.6	3.4	2.1	1.2	2.9	1.4	.2	-.3
Capital equipment	23.1	2.5	1.7	.6	3.4	2.2	.2	.2
Intermediate materials[2]	95.4	-2.7	1.1	-2.1	5.3	.7	.2	.3
Excluding food and energy	81.8	-.8	1.2	-.3	4.3	.0	.2	.1
Crude food materials	41.2	-5.8	3.0	5.1	1.1	-.8	.5	-3.1
Crude energy	39.5	-16.6	2.3	-17.8	-9.7	18.7	4.8	.2
Other crude materials	19.3	-7.6	5.7	1.9	25.0	10.2	.4	.2

1. Changes are from final month of preceding period to final month of period indicated.
2. Excludes materials for food manufacturing and animal feeds.

this year as reduced supplies after last winter's unusually cold weather combined with an ongoing increase in demand for natural gas for generation of electricity due to the requirements of the 1990 Clean Air Act. In recent months, natural gas futures prices have edged off their late winter highs but remain at an elevated level.

The CPI for food fell 0.4 percent in June, pulled down by a drop of nearly 6 percent in prices of fresh fruits and vegetables; prices of tomatoes and lettuce plunged 18 percent and 27 percent, respectively. The drop in fruit and vegetable prices more than reversed a sizable jump in May. So far this year, fruit and vegetable prices are down 2 percent, on net, helping to keep the index for food to a modest 2 percent annual pace, up only a little from the pace of 1991 and 1992.

Some pickup from this low rate of food price inflation may be in the offing, however, as the combination of flooding in the Midwest and drought in some other regions has led to widespread reports of crop damage and increased price volatility in a number of farm markets. The prices of corn and soybeans surged around midyear, and although much of the increase for corn has since been reversed, soybean prices, while also softening of late, remain considerably higher than they were before the weather problems set in. Crops such as peanuts and processed vegetables also have been hurt by bad weather in one region or another. With crops behind schedule in many areas, uncertainties about production and prices may persist for several more weeks. In the livestock sector, the futures prices for cattle dipped temporarily in mid-July, but they since have rebounded to levels slightly above those seen at midyear. Futures prices for hogs jumped in early July in response to a USDA report that showed herds to be smaller than traders had expected: additional price firming that took place later in July has been largely offset by price declines in recent trading sessions. Traders may be anticipating that pork producers will slow expansion plans until the remaining uncertainties about crop production and feed supplies are resolved.

FUTURES PRICES FOR FARM COMMODITIES[1]

Commodity and contract	Pricing date					
	May 13	June 30	July 7	July 15	July 30	Aug. 10
Corn, Dec	2.40	2.38	2.58	2.45	2.42	2.46
Soybeans, Nov.	6.01	6.59	7.15	7.12	6.88	6.73
Wheat, Dec.	3.05	2.96	3.17	3.08	3.13	3.15
Cattle, Oct.	74.90	75.12	75.07	73.15	75.20	75.62
Cattle, Apr.	75.05	76.45	76.57	76.10	76.65	77.10
Hogs, Oct.	43.47	40.30	44.12	43.30	45.72	44.82
Hogs, Apr.	43.10	40.25	43.72	43.80	44.85	43.20

1. The prices of corn, soybeans, and wheat are in dollars per bushel. The prices of cattle and hogs are in dollars per hundredweight.

Just how strongly food prices overall will be affected by the current problems in farming remains to be seen. In 1983 and 1988--two other recent years in which major crop damage occurred--food price inflation picked up noticeably, but with considerable variation in the speed at which initial price shocks made their way through to retail (table). During 1983, for example, food prices rose less rapidly than they had in the previous year, and acceleration in 1984 did not raise food price increases even to the level of core inflation. By contrast, the 1988 episode led to a quick acceleration of food price increases, and the rate of food price rise exceeded core inflation by a percentage point or so over an extended period. Even in the latter instance, however, food price acceleration was not so extreme as to dramatically alter the general inflation picture.

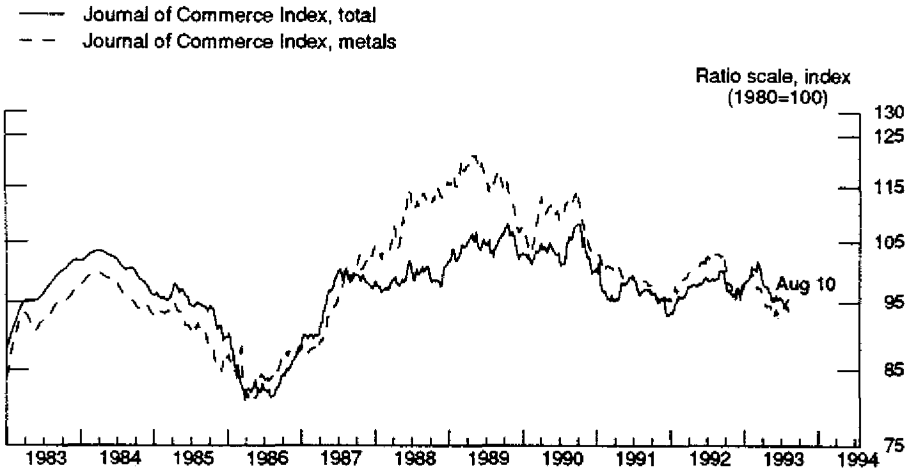
PATTERNS OF CHANGE IN FARM AND FOOD PRICES
IN YEARS OF POOR CROPS
(Percentage change, Q4 to Q4)

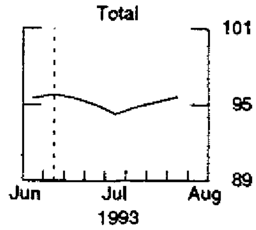
	1982	1983	1984
1983 drought:			
CPI for food	3.2	2.2	3.8
PPI for finished foods	1.8	2.1	3.3
PPI for crude foods	-1.1	7.4	-1.8
Prices received by farmers	-1.3	7.8	-1.2
Crops	-6.1	20.8	-5.3
Livestock	2.2	-1.2	2.7
MEMO:			
CPI excluding food and energy	5.2	4.2	5.0

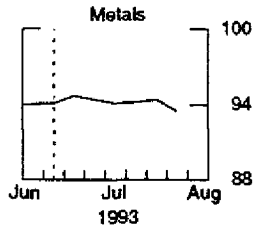
	1987	1988	1989
1988 drought:			
CPI for food	3.5	5.1	5.4
PPI for finished foods	.1	5.1	4.8
PPI for crude foods	1.4	15.2	.3
Prices received by farmers	5.5	11.4	2.1
Crops	13.0	18.2	-5.2
Livestock	0.0	6.0	8.5
MEMO:			
CPI excluding food and energy	4.3	4.5	4.4

Producer prices of finished goods fell 0.3 percent in June, following no change in May. Excluding food and energy, finished goods prices fell 0.1 percent in June, the best monthly outcome since last fall. A 6 percent drop in tobacco prices more than accounted for the decline, but apparel prices fell as well. Producer prices of apparel have fallen on net thus far this year, after rising 2 percent in 1992. Over the first six months of 1993, producer prices of finished goods other than food and energy rose 2.4 percent at an annual rate, compared with 2.7 percent over the first six months of last year. Prices of intermediate materials other than food and energy have risen at a 2.1 percent pace so far this year, compared with 1.2 percent for all of 1992 and 1.8 percent in the first six months of last year.

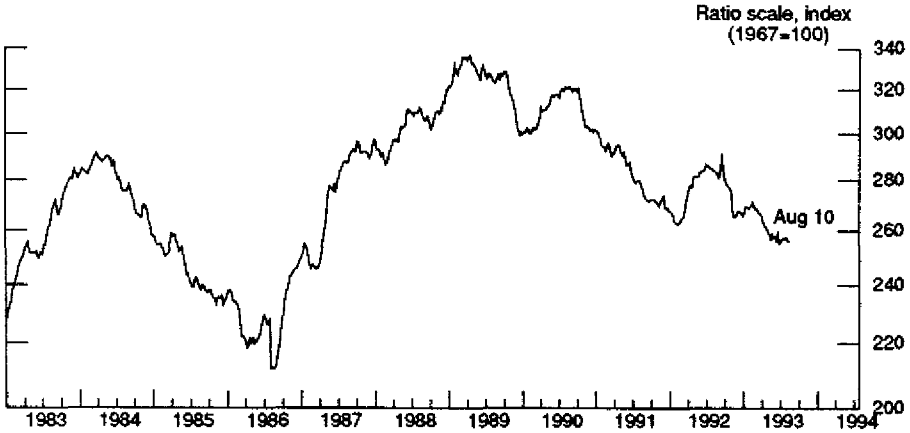
COMMODITY PRICE MEASURES *

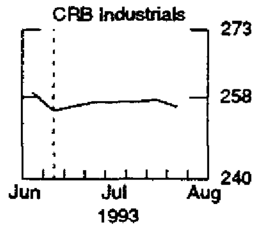




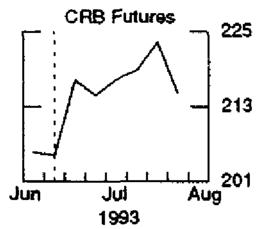


CRB Spot Industrials





CRB Futures



* Weekly data, Tuesdays; Journal of Commerce data monthly before 1985

Dotted lines indicate week of last Greenbook.

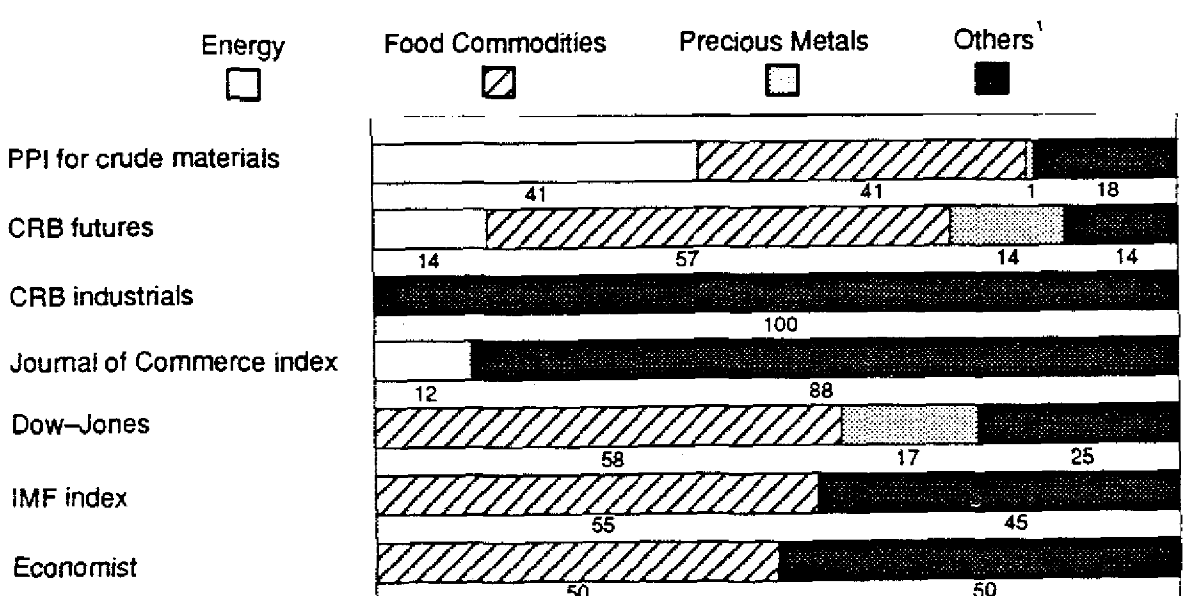
PRICE INDEXES FOR COMMODITIES AND MATERIALS[1]

	Last observ-ation	1991	1992	Dec 92 to Jun 29[3]	Jun 29 to date	Memo: Year earlier to date
		Percent change[2]				
1. PPI for crude materials	Jun	-11.6	3.3	3.6	n.a.	2.4
1a. Foods and feeds	Jun	-5.8	3.0	2.6	n.a.	-0.1
1b. Energy	Jun	-16.6	2.3	1.8	n.a.	1.4
1c. Excluding food and energy	Jun	-7.6	5.7	9.1	n.a.	9.5
1d. Excluding food and energy, seasonally adjusted	Jun	-7.7	6.0	8.3	n.a.	9.4
2. Commodity Research Bureau						
2a. Futures prices	Aug 10	-6.5	-2.9	1.6	4.9	7.6
2b. Industrial spot prices	Aug 10	-11.3	-0.7	-3.9	0.3	-9.7
3. Journal of Commerce industrials	Aug 10	-7.2	5.0	-2.1	-0.2	-2.9
3a. Metals	Aug 10	-7.1	1.9	-3.4	-0.6	-9.1
4. Dow-Jones Spot	Aug 10	-12.1	10.4	-0.9	3.8	6.9
5. IMF commodity index[4]	Jun	0.7	-2.6	-5.8	n.a.	-8.2
5a. Metals	Jun	-8.9	-3.1	-11.1	n.a.	-17.8
5b. Nonfood agricultural	Jun	1.3	2.4	-1.9	n.a.	-1.3
6. Economist (U.S. dollar index)	Aug 03	-9.1	1.6	-4.4	6.4	-1.2
6a. Industrials	Aug 03	-14.9	4.5	-8.9	5.8	-9.2

1. Not seasonally adjusted.
2. Change is measured to end of period, from last observation of previous period.
3. Week of the June Greenbook.
4. Monthly observations. IMF index includes items not shown separately.

n.a. Not available

Index Weights



1. Forest products, industrial metals, and other industrial materials

EMPLOYMENT COST INDEX OF HOURLY COMPENSATION
FOR PRIVATE INDUSTRY WORKERS

	1992			1993	
	June	Sep.	Dec.	Mar.	June
	-----Quarterly percent change------- (compound annual rate)				
Total hourly compensation:[1]	2.9	3.2	3.5	4.2	3.5
Wages and salaries	2.2	2.5	2.9	3.2	2.5
Benefit costs	4.8	5.5	5.0	7.0	5.9
By industry:					
Construction	4.0	5.1	2.5	3.9	3.9
Manufacturing	3.6	3.5	4.2	5.2	4.1
Transportation and public utilities	2.9	3.6	3.6	3.2	4.3
Wholesale trade	2.5	1.1	5.0	1.4	2.5
Retail trade	2.5	3.3	3.2	4.3	1.8
FIRE	-3.2	1.1	0.7	4.8	1.8
Services	5.0	3.8	4.5	3.4	3.7
By occupation:					
White-collar	2.9	3.2	2.8	5.3	3.1
Blue-collar	3.2	3.6	3.2	4.6	3.8
Service occupations	2.8	3.5	2.1	4.6	3.1
Memo:					
State and local governments	4.6	3.1	3.8	2.7	3.4
	-----Twelve-month percent change----				
Total hourly compensation:	3.7	3.4	3.5	3.5	3.6
Excluding sales workers	3.9	3.6	3.5	3.7	3.9
Wages and salaries	3.0	2.7	2.6	2.7	2.7
Benefit costs	5.5	5.2	5.2	5.6	5.8
By industry:					
Construction	2.9	3.5	3.5	3.9	3.8
Manufacturing	4.3	4.0	3.8	4.0	4.4
Transportation and public utilities	3.9	3.6	3.5	3.3	3.7
Wholesale trade	3.6	2.3	3.0	2.5	2.6
Retail trade	2.8	2.5	2.6	3.3	3.1
FIRE	1.2	1.3	1.2	0.8	2.1
Services	4.4	4.2	4.3	4.2	3.9
By occupation:					
White-collar	3.5	3.3	3.3	3.5	3.6
Blue-collar	4.0	3.7	3.6	3.6	3.8
Service occupations	3.9	3.5	3.1	3.3	3.3
Memo:					
State and local governments	3.3	3.5	3.7	3.6	3.4

1. Seasonally adjusted by the BLS.

The _Journal of Commerce_ index of industrial materials prices, which fell moderately during the first half of 1993, has changed little, on net, since the June Greenbook. Price changes for industrial metals have been mixed, with this week's price quotes for copper and steel scrap up a little from the midyear levels but prices of aluminum and tin down slightly. Flatness also has been evident in the CRB index of industrial materials prices. However, more substantial upward pressures have been evident in some other measures of commodity prices--notably the CRB futures index and the Dow-Jones spot price index. These measures, which give heavy weight to agricultural products and precious metals, were boosted in July by weather-related increases of the prices of farm crops and by sharp advances in the prices of gold and silver. With crop prices softening in early August and gold and silver off sharply, the two indexes have recently reversed a portion of the July increases.

Labor Costs

Increases in labor costs remained stable through mid-year. As measured by the employment cost index (ECI), hourly compensation for private industry workers rose at a 3.5 percent annual rate over the March to June period, little different from the average rate of increase during the preceding year. Overall trends in both the wage and salary and the benefit components of the index were little changed. Wages in manufacturing trended lower over the year ending in June, but the slowing was offset by a firming in wages in retailing and in finance, insurance, and real estate. The growth of employer costs for health care decelerated noticeably in the past year. However, the increase in costs of legally required benefits has accelerated; in particular, states have raised employer premiums for state unemployment insurance to reflect firms' experience ratings and to replenish low U.I. funds. Moreover, supplemental pay

EMPLOYMENT COST INDEX OF HOURLY WAGES AND SALARIES
FOR PRIVATE INDUSTRY WORKERS
(Twelve-month percent changes)

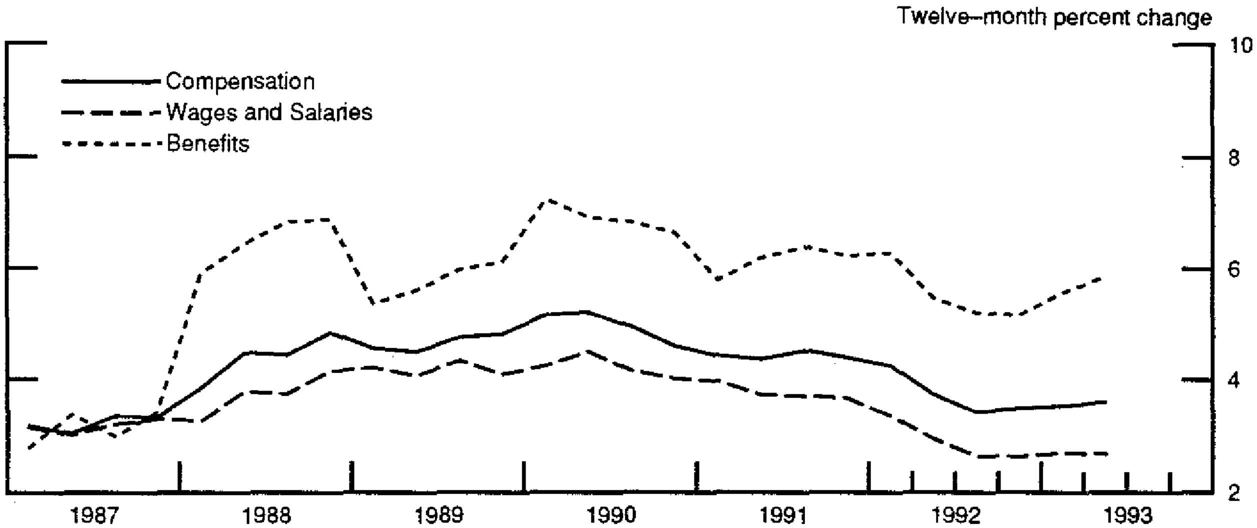
	1992			1993	
	June	Sep.	Dec.	Mar.	June
Hourly wages and salaries	3.0	2.7	2.6	2.7	2.7
By industry:					
Construction	1.9	2.3	2.0	2.1	2.3
Manufacturing	3.5	3.3	3.1	2.9	2.9
Transportation and public utilities	3.8	3.2	3.1	2.9	3.1
Wholesale trade	3.0	1.4	2.9	2.2	2.3
Retail trade	2.4	2.1	2.4	3.0	2.9
FIRE	0.1	0.2	-0.1	-0.2	1.0
Services	3.6	3.3	3.5	3.4	3.2
By occupation:					
White-collar	2.9	2.5	2.7	2.7	2.8
Blue-collar	2.9	2.9	2.6	2.6	2.5
Service occupations	3.0	2.5	2.1	2.1	2.2
Memo:					
State and local governments	3.0	2.7	3.0	3.0	2.8

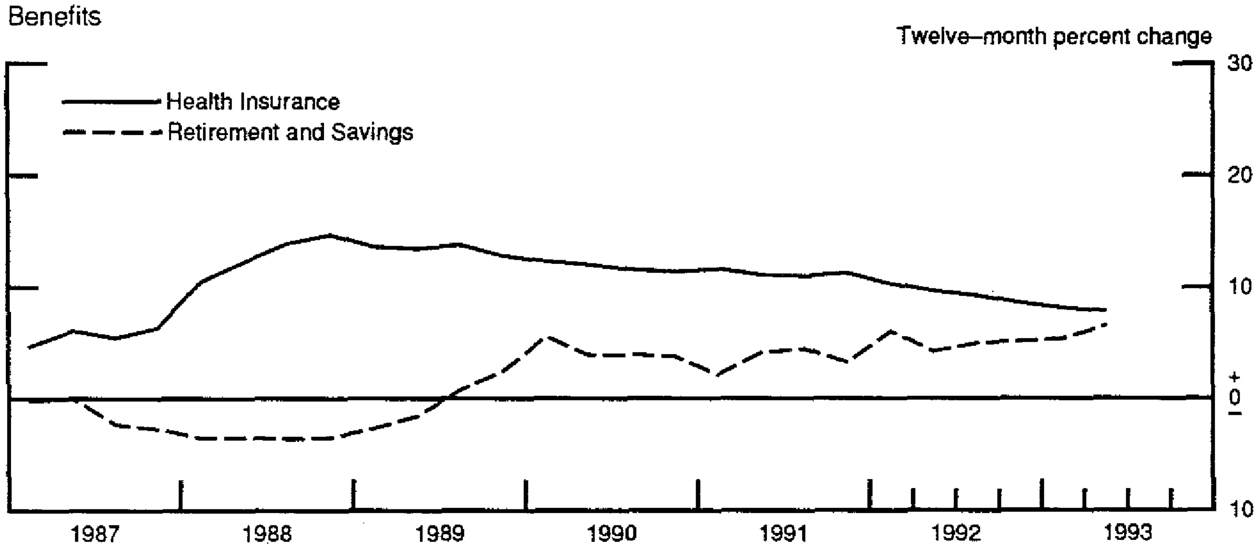
EMPLOYMENT COST INDEX OF HOURLY BENEFIT COSTS
FOR PRIVATE INDUSTRY WORKERS
(Twelve-month percent changes)

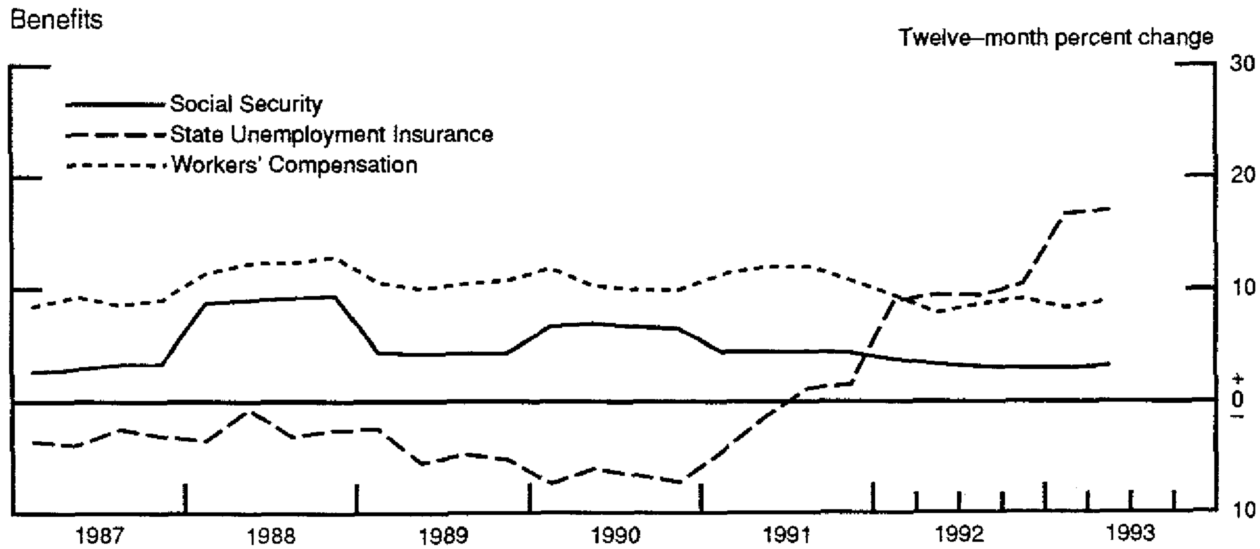
	1992			1993	
	June	Sep.	Dec.	Mar.	June
Hourly benefit costs[1]	5.5	5.2	5.2	5.6	5.8
Insurance costs	9.3	8.7	8.1	7.7	7.2
Health care	9.6	9.2	8.6	8.1	7.8
Supplemental pay	2.7	1.4	2.7	3.6	4.3
Retirement and savings	4.3	5.0	5.2	5.4	6.6
Paid leave	3.6	3.3	3.3	3.4	3.7
Legally required	4.8	4.8	4.8	4.9	5.3
By industry:					
Goods-producing	5.9	5.6	5.7	6.3	7.0
Service-producing	5.1	5.1	4.8	4.8	4.9
By occupation:					
White-collar occupations	4.9	4.9	4.8	5.3	5.4
Blue-collar occupations	6.1	5.5	5.6	5.7	6.3
Service occupations	6.2	6.2	5.8	6.4	6.3
Memo:					
State and local governments	4.3	5.1	5.4	4.8	4.4

1. The detail on benefit costs is from unpublished data from the BLS.

Employment Cost Index
(Private Industry Workers)

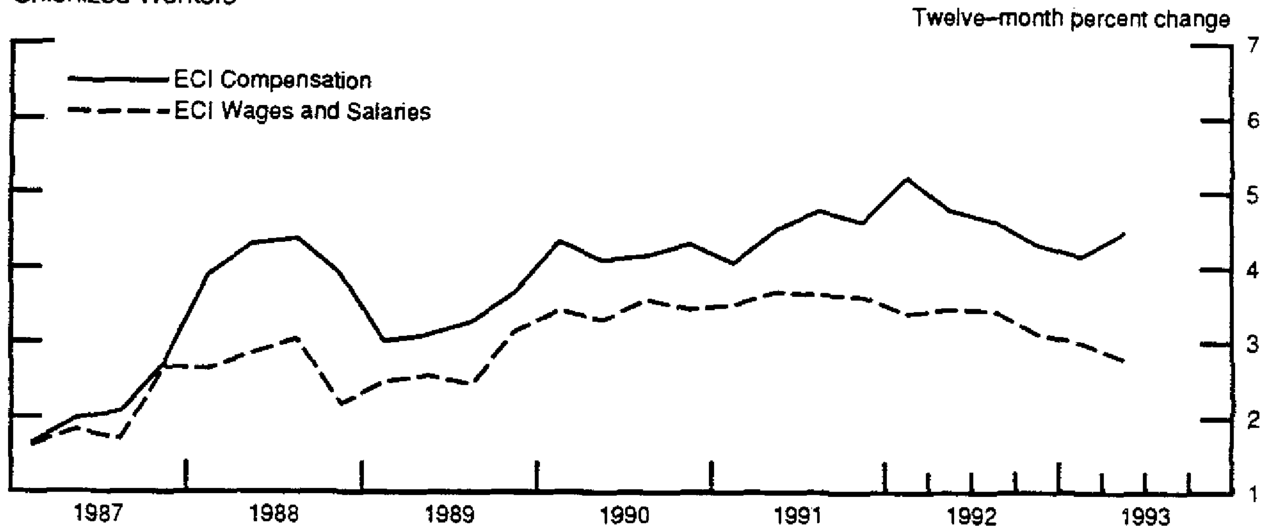






Compensation in Union Contracts

Unionized Workers



EFFECTIVE WAGE CHANGE IN MAJOR UNION CONTRACTS AND COMPONENTS OF CHANGE

	Total Effective Wage Change	Contribution of: Prior Settlements	New Settlements	COLAS
1988	2.6	1.3	.7	.6
1989	3.2	1.3	1.2	.7
1990	3.5	1.5	1.3	.7
1991	3.6	1.9	1.1	.5
1992	3.1	1.9	.8	.4
1992:Q2[1]	3.3	2.0	.9	.4
1993:Q2[1]	2.9	1.8	.7	.4

1. Changes over the four quarters ended this period.

CHANGES IN NEGOTIATED WAGE AND COMPENSATION RATES UNDER MAJOR COLLECTIVE BARGAINING SETTLEMENTS[1]
(Percent change)

	1991	1992	Q1	Q2	Q2 parties under prior settlements
Wage rate changes (all industries)[2]					
First-year changes	3.6	2.7	2.6	2.8	3.6
Average over life of contract	3.2	3.0	2.9	2.7	3.3
Workers affected (in thousands)	1790	1608	207	459	---
Compensation rate changes (all industries)[3]					
First-year changes	4.1	3.0	3.2	3.5	---
Average over life of contract	3.4	3.1	3.3	2.8	---
Workers affected (in thousands)	1179	919	117	202	---

1. Estimates exclude lump-sum payments and potential gains under cost-of-living clauses.
2. Contracts covering 1,000 or more workers.
3. Contracts covering 5,000 or more workers.

and contributions to retirement and savings plans have increased--the latter apparently because of the impact of low interest rates on those plans. The acceleration in these components of benefits appears to have had a differential impact on manufacturers, whose benefit costs rose more rapidly in the past year than in the preceding twelve months.

In the state and local sector, the ECI for hourly compensation increased a bit less rapidly than in private industry over the twelve months ended in June. Compensation growth slowed dramatically in the state and local sector in 1990 and 1991, but, as in private industry, it has leveled off thereafter.

By bargaining status, compensation increases for union workers outpaced gains by nonunion workers in the second quarter, continuing the pattern seen over the past few years. As with private industry workers as a whole, compensation costs for union workers have leveled off. Wages in the union sector, however, have continued to decelerate: The ECI for wages and salaries for union workers increased 2.8 percent over the twelve months ended in June, down from 3.5 percent over the preceding twelve-month period.

Separate data on major union settlements (covering 1,000 or more workers) also show continued deceleration in union wages. The effective wage change series--which is conceptually similar to the ECI--increased 2.9 percent over the four quarters ended in June, down from 3.3 percent over the previous four quarters. Deferred adjustments under prior settlements accounted for the majority of those overall union wage increases. Looking to the future, new second-quarter settlements called for wage adjustments averaging 2.7 percent annually over the life of the contract. This increase is somewhat less than the increases posted in the first quarter and in 1992, and is considerably less than when the same parties bargained two to three years ago.[8]

The only third-quarter labor cost data available are average hourly earnings of production or nonsupervisory workers, which rose 0.2 percent in July, reversing a similar decline in June. Over the past twelve months, average hourly earnings have increased 2.4 percent, virtually unchanged from the pace recorded over the preceding twelve-month period.

AVERAGE HOURLY EARNINGS
(Percent change; based on seasonally adjusted data)

	12 months ending in July			1993		
	1991	1992	1993	May	June	July
				--Monthly rate--		
Total private nonfarm	2.9	2.2	2.4	.5	-.2	.2
Manufacturing	3.2	2.2	2.4	.0	.0	.3
Services	3.7	3.0	2.1	.7	-.2	-.1
Finance, insurance, real estate	3.5	3.7	5.0	1.7	-.7	.5

8. Compensation rate changes in new settlements--for which data are collected only from contracts covering 5,000 or more workers--also were somewhat less than in contracts signed in the first quarter and in 1992.

APPENDIX

THE OMNIBUS BUDGET RECONCILIATION ACT OF 1993

President Clinton has signed the Omnibus Budget Reconciliation Act of 1993, which was passed by the Congress last week. The legislation implements much of the President's budgetary plan and is estimated to reduce the deficit by a cumulative $496 billion over the fiscal years 1994-1998. It is broadly consistent with the Budget Resolution passed last spring.

The Reconciliation Agreement and the Budget Outlook

The House and Senate Budget committees estimate that the reconciliation agreement will reduce the budget deficit by amounts that grow from $47 billion in fiscal 1994 to nearly $150 billion in fiscal 1998 (table 1). The deficit changes are measured relative to a baseline that incorporates the reductions in defense spending in President Bush's January 1992 budget request but that holds the rest of the budget at "current services" levels.[1] All told, the cumulative deficit reduction over the five years is projected to be $496 billion, comprising $190 billion from changes in spending (other than debt service), $241 billion from revenue increases, and $66 billion from savings in debt service (reflecting both the effects of lower levels of debt and changes in debt management policies).

After the savings from the reconciliation agreement are built in, the deficit is projected to drop steadily from $285 billion in fiscal 1993 to less than $200 billion in fiscal 1996 before moving up to about $230 billion by fiscal 1998.[2] By comparison, the baseline deficit is estimated to remain around $300 billion through fiscal 1996 and to rise appreciably thereafter, to about $380 billion in fiscal 1998.

Spending Provisions

The reconciliation agreement will bring about a shift in the composition of federal spending over the fiscal 1994-98 period and is projected to lower the rate of growth of spending, on average, about 1 percentage point per year. Relative to the baseline described above, the agreement is expected to achieve savings of $256 billion over this period: $102 billion is expected to come from caps on discretionary spending, $88 billion from reductions in

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1. The baseline deficit shown in table 1 is the Administration's mid-July preliminary update of its projection for the Mid-Session Review, which has been delayed to incorporate the reconciliation bill. Congressional projections of the deficit, which are based on baseline estimates prepared by the Congressional Budget Office (CBO) last March, differ slightly and are shown as a memo item in the table. Estimates of deficit reduction were prepared by CBO and the Joint Committee on Taxation (JCT).

2. In the main, the upward tilt in the deficit after the mid-1990s reflects the combination of continued large increases in outlays for health care and the slowing of real GDP growth in the underlying economic forecast. As President Clinton noted when he released his budgetary program last winter, he expects savings from health care reform to help keep the budget deficit on a downward track. Moreover, the President and several members of the Congress have agreed to consider further spending reductions later this year.

Table 1
BUDGET PROJECTIONS, BY FISCAL YEAR
(Billions of dollars)

	1993	1994	1995	1996	1997	1998
Baseline deficit	285	300	286	291	340	379
LESS						
Spending reductions (net)	...	19	26	35	48	62
Revenue increases (net)	...	26	44	52	61	59
Debt service savings	...	2	6	12	18	27
Total	...	47	76	98	127	148
EQUALS						
Post-reconciliation deficit	285	253	210	193	213	231
Memo						
Congressional deficit estimate	...	255	227	204	201	213

entitlement programs, and $66 billion from lower debt service costs (table 2).

With respect to discretionary (annually appropriated) spending, the reconciliation agreement reaffirms the caps specified by the 1990 budget act for fiscal 1994-95 and sets caps on spending for fiscal 1996-98. The new caps hold nominal spending at its fiscal 1993 level and imply an average decline in real spending of about 3 percent per year.[3]

Although the caps for the fiscal 1994-98 period apply to discretionary spending in total (separate caps for defense and other categories ended in fiscal 1993), with the actual programmatic changes to be worked out in yearly appropriations, defense is expected to account for virtually all of the savings. Notably, in *The Budget for Fiscal Year 1994*, President Clinton proposed to hold nondefense discretionary spending about even in real terms over the next five years, whereas defense spending was slated to fall by fiscal 1998 to a level about 12 percent below that proposed by President Bush in 1992. Such a level of defense spending in fiscal 1998 would be about 20 percent below that needed to maintain 1993's real funding level.

The reconciliation agreement also includes $88 billion in entitlement cuts over the five years, with around two-thirds of the reductions coming from Medicare. The savings in Medicare come primarily from restraints on payments to health care providers and, after 1995, from higher premiums for Supplementary Medical Insurance (SMI). The savings are expected to cumulate to $56 billion over the next five years, but Medicare outlays still are expected to grow approximately 10 percent per year, on average, over the period.

3. Because the nominal caps will be adjusted in future years for unanticipated changes in inflation, the agreement, in effect, establishes a path for real spending.

Table 2
KEY SPENDING PROVISIONS, CHANGES FROM BASELINE, BY FISCAL YEAR
(Billions of dollars)

	1994	1995	1996	1997	1998	Total
Total	-21	-32	-46	-67	-89	-256
Discretionary spending	-9	-15	-16	-26	-36	-102
Mandatory spending	-10	-11	-18	-22	-27	-88
Medicare	-2	-5	-12	-16	-20	-56
Medicaid	0	-1	-2	-2	-3	-8
Government retirement	0	-1	-3	-4	-4	-12
FCC spectrum auction	-2	-3	-2	-1	-1	-10
Student loans	-1	0	-1	-1	-1	-5
Expansion of EITC[1]	0	2	4	6	6	19
Debt service	-2	-6	-12	-18	-27	-66

1. Earned income tax credit. Outlay effect only; also entails a five-year revenue loss of $2 billion.

Other significant savings are estimated to come from reductions in Medicaid, changes in federal retirement policies (mainly by eliminating the "lump-sum" retirement option), the introduction of competitive bidding for the use of the telecommunications spectrum (the proceeds are treated as an offset to outlays), and reform of the student loan program. The student loan reforms will phase in the replacement of guaranteed student loans by direct government loans (until they account for half of new lending) and impose fees on banks and other institutions.

The agreement contains a substantial expansion of the earned income tax credit (EITC), which has been touted by the President as a first step in the reform of assistance to low-income families. The agreement also increases funding for food stamps and a variety of child welfare and health programs.

Revenue Provisions

According to congressional estimates, the changes to the tax laws are estimated to narrow the deficit, on net, $26 billion in fiscal 1994 and a cumulative $241 billion over the five years (table 3). The distribution of tax burdens also shifts appreciably: Upper-income individuals and businesses generally will face higher liabilities, while most middle- and low-income individuals will see little change in their overall tax payments.[4] In addition to new initiatives, the package extends several expiring provisions, but the extensions have only a small effect on the deficit.

4. According to the JCT, taxpayers earning $200,000 or more will see an increase in their total tax liabilities equal to 5.4 percent of their incomes while those earning less than $10,000 will see a decrease equal to 1.3 percent of income. Tax burdens of other groups are estimated to change by less than 1 percent of income. These calculations include the change to the outlay portion of the EITC.

Table 3
KEY REVENUE PROVISIONS, CHANGES FROM BASELINE, BY FISCAL YEAR
(Billions of dollars)

	1994	1995	1996	1997	1998	Total
Total	26	44	52	61	59	241
Provisions affecting individuals						
Upper-income tax rates	15	23	26	25	26	115
Tax up to 85 percent of social security benefits	2	5	5	6	7	25
Repeal of Medicare wage cap	3	6	6	7	7	29
Provisions affecting businesses						
Higher tax rate on large corporations	4	3	3	3	3	16
Smaller deduction for meals, entertainment	2	3	3	3	4	15
Estimated tax rules	2	0	0	4	1	8
Transportation fuels tax						
Increase, 4.3 cents per gallon	4	4	5	5	5	23
Extension of existing tax	0	0	3	3	3	8
Investment incentives						
Small business expensing	-2	-1	-1	0	0	-5
Extension of R&E credit	-2	-1	-1	0	0	-5
Empowerment zones[1]	0	0	-1	-1	-1	-2

1. Revenue effect only; also adds $1 billion to outlays over five years.

Upper-income individuals will pay higher income and social insurance taxes. The increase in income taxes is accomplished through (1) the addition of a fourth (36 percent) bracket for taxable incomes of more than $140,000 (joint returns) and $115,000 (single returns), (2) the imposition of a 10 percent surtax on the portion of taxable income that exceeds $250,000 (on both joint and single returns), (3) the permanent extension of provisions that limit the itemized deductions and phase out the personal exemptions claimed by high-income taxpayers, and (4) adjustments to the provisions concerning the alternative minimum tax.[5] These provisions change liabilities for 1993, but affected taxpayers will be able to pay this year's additional taxes in installments over the 1994-96 period. Moreover, beginning in 1994, the wage-base cap on Medicare taxes (currently $135,000) will be repealed. (Upper-income persons also will be affected by new limits on contributions to 401(k) and other

5. According to staff estimates, these changes are likely to affect only about 10 percent of individual returns reporting business income. Partnerships and Subchapter-S corporations account for about one-third of individually reported business income, and almost all of their income is reported on affected returns. The remaining two-thirds of individually reported business income is earned by sole proprietors; roughly one-fifth of sole-proprietorship income is on affected returns.

qualified retirement plans as well by higher rates on estate and gift taxes.)

All told, the marginal tax rate on the wage income of taxpayers with total taxable incomes of more than $250,000 rises from 31 percent under current law to 42.5 percent, taking account of both the higher rates of individual taxation and the combined employer and employee share of Medicare; the maximum statutory rate on realized capital gains, however, remains at 28 percent.[6]

In addition, beginning in 1994, a greater share of social security benefits will be subject to income tax. Currently, married taxpayers whose incomes (calculated as the sum of adjusted gross income plus tax-exempt interest income plus one-half of social security benefits) are at least $32,000 ($25,000 for single taxpayers) must include up to 50 percent of social security benefits (depending on income) in taxable income. The new law introduces a second test that raises the maximum share of benefits subject to tax to 85 percent. The provision will begin to bite for married taxpayers with incomes of $44,000 ($34,000 for single taxpayers); those with incomes below the new thresholds will be unaffected.

On the business side, the agreement raises the corporate tax rate from 34 percent to 35 percent on taxable incomes of more than $10 million; the higher liabilities begin in 1993, but payments will not be required until 1994. Also, beginning in January, the deductible portion of business meals and entertainment will be reduced from 80 percent to 50 percent; deductions for a variety of other items, including executive compensation in excess of $1 million, will be limited or eliminated.

The other key revenue-raising provision in the reconciliation agreement is a 4.3 cents per gallon increase in the tax on transportation fuels, including gasoline and diesel fuel, on October 1, 1993 (commercial aviation fuel will be exempt for two years). The agreement also extends the 2.5 cents per gallon portion of the current gasoline tax scheduled to expire on September 30, 1995.

Although the major investment incentives proposed by the President in February have been dropped, the reconciliation agreement contains numerous smaller initiatives. Notably, small businesses now will be able to expense up to $17,500 of expenditures on capital equipment each year (compared with $10,000 currently), and the research and experimentation (R&E) credit is extended. In addition, stockholders in certain new firms will be able to exclude 50 percent of capital gains on investments held at least five years; the five-year revenue loss from this provision is less than $1 billion.

Finally, the legislation provides funding for the creation of nine empowerment zones and ninety-five enterprise communities. Among other things, employees who work and live in the designated enterprise zones will receive credits equal to 20 percent of the first $15,000 of qualified wages, and businesses locating in these areas will be able to take advantage of favorable expensing provisions.

6. These calculations are approximate and do not take into account the limits on itemized deductions, deductibility of the employer share of Medicare taxes, and state income taxes.

Budget Process and Executive Orders

The Reconciliation Act extends the 1990 budget enforcement law through fiscal 1998 and contains provisions designed to facilitate sustained deficit reduction. As noted above, the act sets caps on discretionary spending through fiscal 1998 that are consistent with the Budget Resolution; it also continues the existing sequester mechanism and the pay-as-you-go (PAYGO) system governing mandatory spending and revenues. However, it adjusts the PAYGO structure to ensure that none of the deficit reduction in the reconciliation bill can be "spent" to finance increases in mandatory spending or reductions in taxes. Also, the President signed an executive order on August 4 creating a new Deficit Reduction Fund. A second order established procedures that the Administration will have to follow in the event that mandatory spending exceeds its projections; notably, the Administration will have to acknowledge the overrun and offer a plan for dealing with it.

DOMESTIC FINANCIAL DEVELOPMENTS

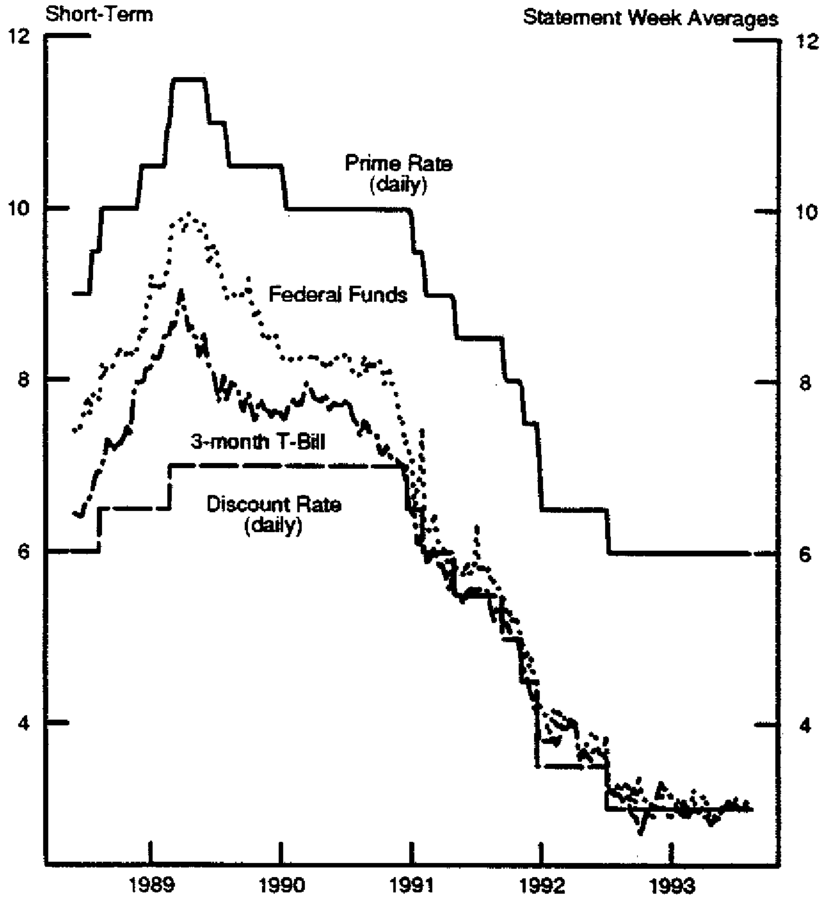
SELECTED FINANCIAL MARKET QUOTATIONS[1]
(Percent except as noted)

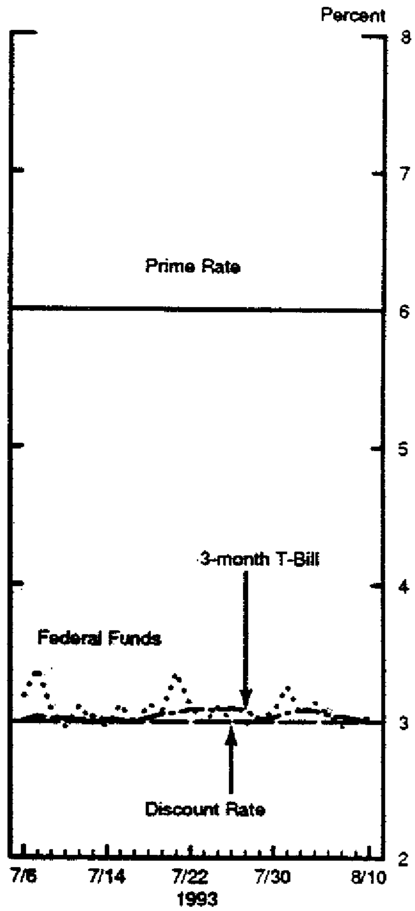
Instrument	1992 September 4	1993 FOMC, July 7	1993 Aug. 10	Change to Aug. 10, 1993 From Sept. 4	Change to Aug. 10, 1993 From FOMC, July 7
SHORT-TERM RATES					
Federal funds[2]	3.19	3.11	2.99	-.20	.12
Treasury bills[3]					
3-month	2.92	3.04	3.03	.11	.01
6-month	2.96	3.11	3.17	.21	.06
1-year	3.06	3.29	3.36	.30	.07
Commercial paper					
1-month	3.22	3.17	3.15	-.07	.02
3-month	3.22	3.20	3.21	-.01	.01
Large negotiable CDs[3]					
1-month	3.06	3.11	3.09	.03	.02
3-month	3.06	3.15	3.15	.09	.00
6-month	3.11	3.33	3.35	.24	.02
Eurodollar deposits[4]					
1-month	3.31	3.06	3.06	-.25	.00
3-month	3.31	3.19	3.13	.18	-.06
Bank prime rate	6.00	6.00	6.00	.00	.00
INTERMEDIATE- AND LONG-TERM RATES					
U.S. Treasury (constant maturity)					
3-year	4.38	4.38	4.48	.10	.10
10-year	6.40	5.80	5.82	-.58	.02
30-year	7.29	6.68	6.45	-.84	-.23
Municipal revenue[5] (Bond Buyer)	6.31	5.75	5.73	-.58	.02
Corporate--A utility, recently offered	8.06	7.48	7.21	-.85	-.27
Home mortgages[6]					
FHLMC 30-yr. fixed rate	7.84	7.23	7.21	-.63	-.02
FHLMC 1-yr. adjustable rate	5.15	4.58	4.55	-.60	-.03

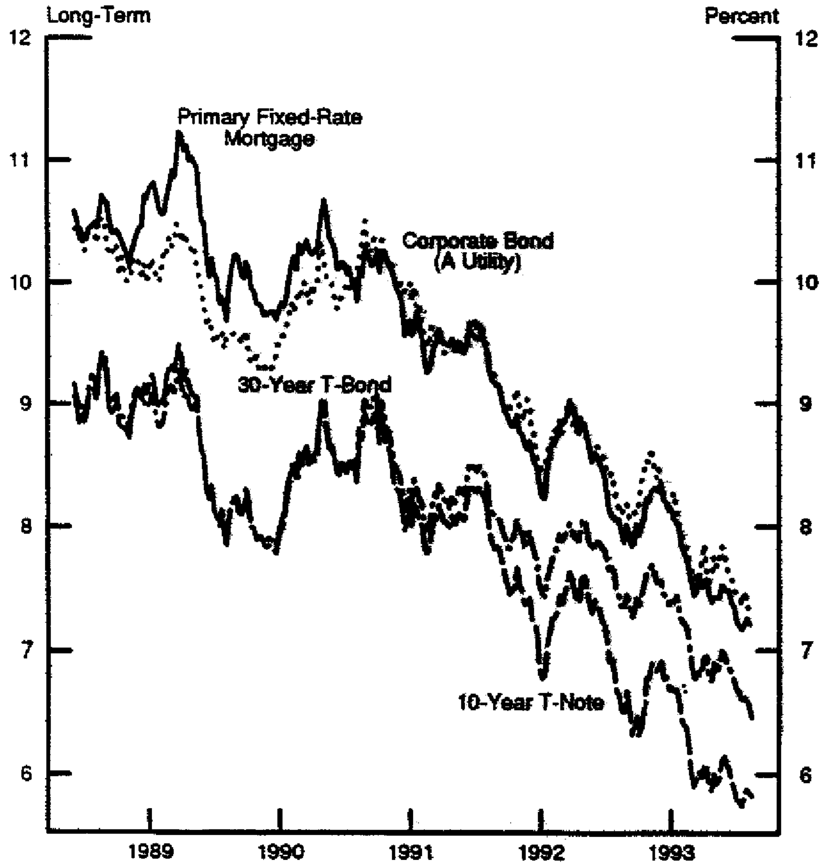
Stock exchange index	Record high Level	Record high Date	1989 Low, Jan. 3	1993 FOMC, July 7	1993 Aug. 10	Percentage change to Aug. 10 From record high	Percentage change to Aug. 10 From 1989 low	Percentage change to Aug. 10 From FOMC, July 7
Dow-Jones Industrial	3576.08	8/9/93	2144.64	3475.67	3572.73	-.09	66.59	2.79
NYSE Composite	251.36	3/10/93	154.00	245.68	249.63	-.69	62.10	1.61
AMEX Composite	440.95	6/4/93	305.24	431.79	439.19	-.40	43.88	1.71
NASDAQ (OTC)	718.49	8/9/93	378.56	698.79	717.08	-.20	89.42	2.62
Wilshire	4477.53	8/9/93	2718.59	4392.49	4469.27	-.18	64.40	1.75

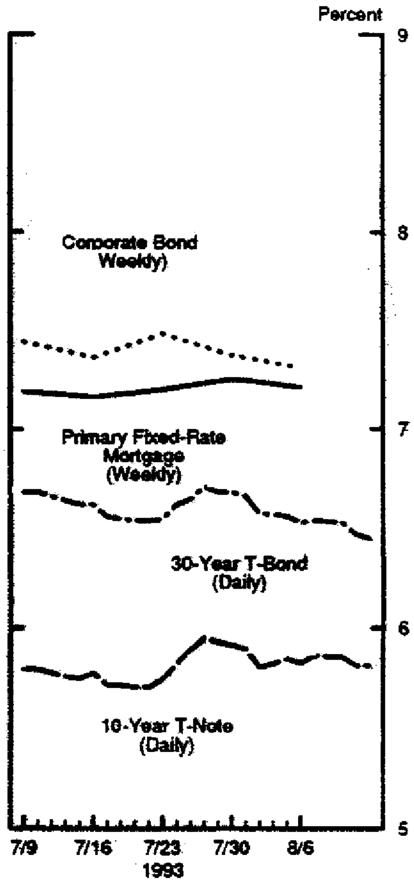
1. One-day quotes except as noted.
2. Average for two-week reserve maintenance period closest to date shown. Last observation is verage to date for maintenance period ending August 18, 1993.
3. Secondary market.
4. Bid rates for Eurodollar deposits at 11 a.m. London time.
5. Based on one-day Thursday quotes and futures market index changes.
6. Quotes for week ending Friday previous to date shown.

Selected Interest Rates*









* Friday weeks are plotted through Aug 6, statement weeks through Aug 4, 1993

Short- and intermediate-term interest rates have recorded only small changes on net since the July FOMC meeting. Rates generally backed up a bit as market participants perceived the Chairman's Humphrey-Hawkins testimony as signaling a greater likelihood of policy tightening. However, with economic data suggesting no accumulation of inflation pressures, and with the passage of the deficit-reduction package, rates have generally fallen back, especially long-term rates. Indeed, the thirty-year Treasury bond rate has dropped about 1/4 percentage point on net to a new record low below 6-1/2 percent. Most major stock price indexes have risen 1-1/2 percent to 3 percent over the intermeeting period.

Households apparently continued to shift their portfolios toward assets outside the monetary aggregates--particularly stock and bond mutual funds--and the growth of the broad monetary aggregates weakened slightly further in July. Bank credit presented a mixed picture: Consumer and real estate loans registered solid growth; however, business loans contracted after two months of expansion even as banks reportedly have become more willing to lend.

The pattern of financial flows has continued to reflect efforts of businesses to restructure balance sheets and to take advantage of low long-term interest rates. Firms continued to issue large volumes of bonds--some with unusually long maturities--and used the bulk of the proceeds to refinance existing debt, evidently including bank loans. As stock prices extended their ascent, equity issuance remained strong as well. Demand for mortgages to finance home purchases appears to have picked up, but loan originations have been dominated by another surge in refinancing activity. Paced by substantial increases in auto and revolving installment loans, overall consumer credit advanced at a moderate rate in the second

MONETARY AGGREGATES
(Based on seasonally adjusted data except as noted)

Aggregate or component	1992[1]	1993 Q1[2]	1993 Q2[2]	1993 May	1993 Jun.	1993 Jul. (pe)	1992:Q4 to Jul. 93 (pe)	Level (bil. $) Jun. 93
Aggregate	Percentage change (annual rate)							
1. M1	14.3	6.6	10.5	27.4	7.3	14	10	1073.3
2. M2	1.8	-1.9	2.1	10.5	2.1	1	1	3511.0
3. M3	0.3	-3.8	2.3	8.5	-1.3	-2	-½	4166.8
Selected components								
4. M1-A	13.7	6.2	13.0	26.5	7.3	14	11	675.4
5. Currency	9.1	9.5	9.7	10.4	11.1	11	10	306.8
6. Demand deposits	18.0	3.7	16.1	40.8	5.0	17	12	360.6
7. Other checkable deposits	15.4	7.3	6.3	28.9	7.3	13	8¾	397.9
8. M2 minus M1[3]	-2.6	-5.4	-1.4	3.3	-0.1	-4	-3	2437.8
9. Overnight RPs and Eurodollars, n.s.a.	1.8	-10.2	-17.0	-57.5	53.3	17	-6¼	70.6
10. General-purpose and broker-dealer money market funds	-5.2	-10.1	-0.7	17.4	-1.4	-1	-3½	336.1
11. Commercial banks	-0.1	-2.2	0.1	4.3	-0.1	-4	-1	1259.5
12. Savings deposits	14.5	1.6	4.6	14.0	6.4	0	3½	769.0
13. Small time deposits	-15.8	-7.6	-6.7	-10.3	-10.2	-12	-8	490.5
14. Thrift institutions	-5.5	-8.9	-4.8	2.5	-4.5	-5	-6	768.9
15. Savings deposits	14.8	-0.2	0.7	9.0	2.8	2	1	429
16. Small time deposits	-21.5	-19.0	-11.4	-5.6	-13.6	-15	-14¼	339
17. M3 minus M2[3]	-6.6	-13.0	3.5	-2.2	-19.1	-22	-8	655.7
18. Large time deposits	-16.3	-17.8	-1.3	-0.3	-13.2	-19	-10½	342.1
19. At commercial banks[4]	-15.4	-18.0	0.3	3.0	-14.1	-22	-10¼	278.3
20. At thrift institutions	-19.6	-17.5	-7.9	-14.7	-9.3	0	-10¾	63.8
21. Institution-only money market mutual funds	18.2	-14.1	0.4	14.4	-27.8	-19	-9	198.1
22. Term RPs, n.s.a.	7.9	9.9	29.5	-5.4	23.2	35	21¾	89.7
23. Term Eurodollars, n.s.a.	-22.6	0.0	32.3	38.2	-34.7	-76	¼	50.3
	Average monthly change (billions of dollars)							
Memo								
24. Managed liabilities at com'l. banks (lines 25 + 26)	-2.2	3.2	3.5	-2.8	4.3	12	...	697.0
25. Large time deposits, gross	-4.6	-3.6	-1.0	1.3	-3.7	-8	...	352.6
26. Nondeposit funds	2.4	6.8	4.5	-4.1	8.0	21	...	344.4
27. Net due to related foreign institutions	2.7	2.8	1.8	-5.1	1.3	11	...	84.9
28. Other[5]	-0.3	4.1	2.7	0.9	6.8	9	...	259.5
29. U.S. government deposits at commercial banks[6]	-0.5	-0.5	2.4	-5.1	7.0	4	...	26.1

1. "Percentage change" is percentage change in quarterly average from fourth quarter of preceding year to fourth quarter of specified year. "Average monthly change" is dollar change from December to December, divided by 12.
2. "Percentage change" is percentage change in quarterly average from preceding quarter to specified quarter. "Average monthly change" is dollar change from the last month of the preceding quarter to the last month of the specified quarter, divided by 3.
3. Seasonally adjusted as a whole.
4. Net of holdings of money market mutual funds, depository institutions, U.S. government, and foreign banks and official institutions.
5. Borrowing from other than commercial banks in the form of federal funds purchased, securities sold under agreements to repurchase, and other liabilities for borrowed money (including borrowing from the Federal Reserve and unaffiliated foreign banks, loan RPs, and other minor items). Data are partially estimated.
6. Treasury demand deposits and note balances at commercial banks.

quarter, and bank data for July point to a another solid gain last month.

In the public sector, state and local governments again issued large volumes of bonds, especially for refunding purposes. The Treasury has continued its reliance on shorter-term bill and coupon offerings and, as previously announced, inaugurated a semiannual schedule for auctions of thirty-year bonds. The Treasury is expected to borrow $54 billion during the third quarter, about on par with the pace through the first half of 1993.

Money and Bank Credit

Although temporarily obscured by special factors in May and June, the fundamental forces impeding the growth of the broad monetary aggregates in recent quarters became more apparent in July. M2 growth in July slowed to about 1 percent at an annual rate, placing it just below the new lower bound of its annual target range.[1] Despite a decline in long-term rates, households have continued to tilt the composition of their portfolios toward longer-term, higher-risk assets outside the monetary aggregates. Most notably, anecdotal reports suggest a repeat in July of the strong inflows to stock and bond funds of recent months. M3 contracted in July at a 2 percent pace as banks continued to meet additional funding needs largely by issuing liabilities that are not included in the monetary aggregates. More rapid growth of demand deposits,

1. The deceleration of M2 occurred despite a boost resulting from the acquisition of a primary dealer firm by a large bank. Currently, the primary dealership is structured as a subsidiary of the bank; ultimately, the bank is expected to place the dealer in its "Section 20" subsidiary of the bank holding company. Because the acquired dealer is, for the moment, part of the bank, its overnight and term RPs are included in the monetary aggregates. Estimates suggest that the inclusion of these RPs added $4-1/2 billion to the level of M2 and $5 billion to the level of M3 in July. On the asset side, the merger is estimated to have added about $7-1/4 billion to bank security holdings and another $3-1/2 billion to security loans last month. These increases will be reversed when the dealer becomes a separate subsidiary of the bank holding company.

COMMERCIAL BANK CREDIT AND SHORT- AND INTERMEDIATE-TERM BUSINESS CREDIT[1]
(Percentage change at annual rate, based on seasonally adjusted data)

Type of credit	Dec. 1991 to Dec. 1992	1993 Q1	1993 Q2	1993 May	1993 June	1993 July p	Level, July 1993 p ($billions)
	Commercial bank credit						
1. Total loans and securities at banks	3.6	2.8	7.3	8.6	9.6	7.8	3,036.3
2. Securities	13.0	11.6	10.7	4.4	12.7	5.0	888.5
3. U.S. government	17.5	13.1	12.2	4.2	16.6	5.6	706.8
4. Other	-1.1	6.1	5.1	4.6	-1.3	2.0	181.6
5. Loans	.2	-.7	5.9	10.2	8.2	9.1	2,147.9
6. Business	-3.2	-1.0	.9	6.9	3.9	-3.2	592.1
7. Real estate	2.1	.9	5.3	7.4	7.9	3.7	906.8
8. Consumer	-1.8	7.7	6.5	9.2	4.3	12.1	371.9
9. Security	18.4	-4.3	48.0	122.7	50.4	156.9	81.3
10. Other	1.1	-13.5	9.7	-1.3	16.3	10.5	195.8
	Short- and intermediate-term business credit						
11. Business loans net of bankers acceptances	-3.3	-1.6	.5	6.0	3.9	-4.3	582.9
12. Loans at foreign branches[2]	2.0	-33.1	-5.2	-5.1	-20.5	-20.9	22.6
13. Sum of lines 11 and 12	-3.1	-2.9	.4	5.6	3.2	-5.3	605.4
14. Commercial paper issued by nonfinancial firms	9.5	-9.3	15.8	17.5	-1.6	40.0	158.2
15. Sum of lines 13 and 14	-.8	-4.2	3.4	7.8	2.4	3.8	763.6
16. Bankers acceptances, U.S. trade-related[3,4]	-16.9	-10.4	-14.2	-16.1	-16.4	n.a.	21.7[5]
17. Finance company loans to business[4]	1.8	-5.1	-.4	.8	-1.2	n.a.	303.1[5]
18. Total (sum of lines 15, 16, and 17)	-.5	-4.6	2.0	5.3	1.0	n.a.	1,086.0[5]

1. Except as noted, levels are averages of Wednesday data and percentage changes are based on averages of Wednesday data; data are adjusted for breaks caused by reclassification; changes are measured from preceding period to period indicated.
2. Loans to U.S. firms made by foreign branches of domestically chartered banks.
3. Acceptances that finance U.S. imports, U.S. exports, and domestic shipment and storage of goods.
4. Changes are based on averages of month-end data.
5. June 1993.
p Preliminary.
n.a. Not available.

likely spurred by prepayments on mortgage-backed securities resulting from the latest refinancing surge, helped push M1 growth to a 14 percent pace in July.

Buoyed significantly by a bank's acquisition of a primary dealer firm, bank credit advanced at a 7-3/4 percent annual rate--down somewhat from the pace recorded in May and June but still well above the trend growth of the last three years. Excepting this merger, bank credit in July would have expanded at only about half that pace. Consumer and real estate loans were unaffected by the merger and showed genuine strength, advancing in July at 12 percent and 3-3/4 percent annual rates, respectively. Growth in real estate loans accorded with the pickup in home sales. Home equity loans declined in July, suggesting that households may have used some of the proceeds from mortgage refinancings to pay down home equity debt. In contrast to the upbeat tone in the consumer and real estate lending data, business loans declined in July at a 3-1/4 percent rate. In part, the decline in business loans may reflect substitution of capital market funding for bank loans by some businesses and perhaps a reduced need to finance inventories. Business loans at small banks declined in July, following a smaller runoff in June. Only foreign banks recorded any business loan growth last month. European banks, with ample capital and likely facing weak loan demand in their domestic market, accounted for most of the increase in business loans. Japanese banks, still facing capital pressures, continued to retrench.

Depository Institutions

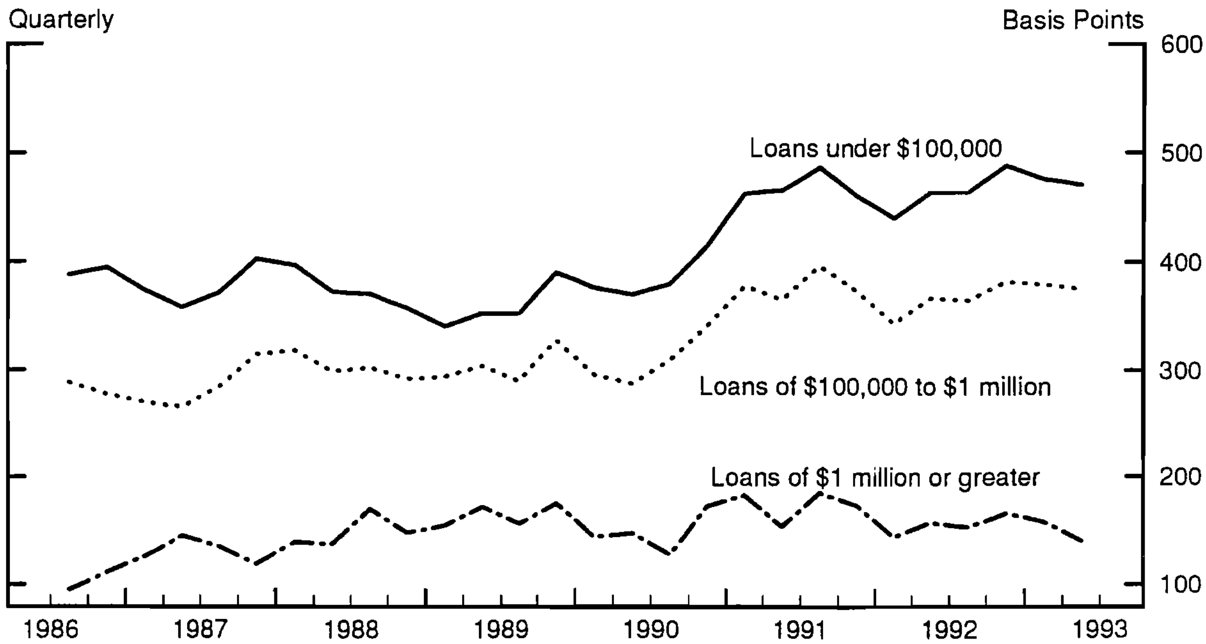
Banks continued to enjoy robust earnings in the second quarter. Partial information for the top twenty-five banking companies indicates that net interest margins, albeit still high, may have begun to narrow a bit. Profits remain substantial, augmented by gains from securities and foreign exchange trading and from fee generating activities. Shares of money center banks appeared to respond favorably to earnings reports, rising appreciably over the intermeeting period; share prices for other banks were little changed. Improved profitability, along with continued issuance of equity and subordinated debt, has boosted capital at most banks to levels well in excess of regulatory minimums. Some banks may be building extra capital in anticipation of future acquisitions, while others may still be responding to various regulatory and market incentives to maintain strong capital bases. However, there are signs that some banks may be beginning to deploy their excess capital by extending new loans. Indeed, preliminary information from the August Bank Lending Practices Survey (BLPS) indicates that banks which are comfortable with their capital position tend also to be pursuing loans more aggressively.[2]

Data on loan rates appear consistent with the view that banks are attempting to be more competitive in certain market sectors. For example, data from the Survey of Terms of Business Lending (chart) indicate that spreads on rates for large loans relative to the federal funds rate have narrowed in 1993. Similarly, data from other sources on the pricing of large syndicated loans also suggest that spreads have narrowed in 1993. The August BLPS indicates that a considerable number of banks have eased standards for approving new C&I loans, especially for large- and medium-sized credits, and a large share of the respondents reported easing of loan terms such as credit line fees and spreads.

Although a significant number of problem thrifts remain, anecdotal reports indicate that the profitability of the industry overall is gradually improving. The improved earnings of S&Ls have

2. A full analysis of the Bank Lending Practices Survey is included in a Greenbook supplement.

Spreads Between Business Loan Rates
and the Federal Funds Rate, By Loan Size



Note: Last observation is 1993 Q2.
Source: Survey of Terms of Bank Lending

been incorporated in their share prices, which generally have tracked the upward trajectory of bank stocks in recent months. Some S&Ls have opted to abandon their S&L charter in favor of a federal or state savings bank charter. The federal savings bank charter allows S&Ls to market themselves as FDIC-insured rather than SAIF-insured.[3] The move to a state savings bank charter has been popular among S&Ls chafing under the supervision of OTS--the FDIC is the primary federal regulator for state savings banks. Despite the lack of new funds from Congress, the RTC was able to resolve a few small institutions in May and June by tapping its reserve fund.

3. This is largely a marketing device--deposit insurance assessments for these institutions are split between BIF and SAIF on the basis of their status before the change in charter. Although there is not much difference between the deposit rates offered by S&Ls and those of savings banks, some S&Ls may find the change in charter allows them to attract or retain customers more easily.

GROSS OFFERINGS OF SECURITIES BY U.S. CORPORATIONS
(Monthly rates, not seasonally adjusted, billions of dollars)

	1991	1992	1993 Q1	1993 Q2[p]	1993 Apr.	1993 May[p]	1993 June[p]
Corporate securities - total[1]	32.14	40.81	55.99	45.44	40.55	43.11	52.66
Public offerings in U.S.	29.35	38.01	51.68	41.62	36.97	39.80	48.09
Stocks--total[2]	5.44	6.54	8.04	8.25	6.25	8.70	9.79
Nonfinancial	3.72	4.03	4.39	4.73	3.67	5.39	5.13
Utility	0.42	0.87	0.63	0.99	0.69	1.14	1.13
Industrial	3.30	3.16	3.76	3.75	2.98	4.25	4.01
Financial	1.72	2.51	3.66	3.52	2.58	3.31	4.66
Bonds	23.91	31.47	43.63	33.37	30.72	31.10	38.30
Nonfinancial	9.52	12.81	19.85	15.26	14.88	11.50	19.40
Utility	2.99	5.33	9.12	7.24	7.91	4.85	8.95
Industrial	6.54	7.47	10.73	8.03	6.98	6.65	10.45
Financial	14.39	18.67	23.78	18.11	15.84	19.60	18.90
By quality[3]							
Aaa and Aa	3.72	3.73	5.50	4.49	3.65	4.71	5.09
A and Baa	12.09	14.50	20.90	16.59	15.27	11.69	22.82
Less than Baa	1.03	3.10	4.92	4.45	4.04	4.11	5.19
No rating (or unknown)	0.02	0.08	0.05	0.07	0.03	0.08	0.09
Memo items:							
Equity-based bonds[4]	0.63	0.62	0.49	0.77	0.33	0.46	1.52
Mortgage-backed bonds	2.99	6.07	8.04	3.54	4.43	5.43	0.77
Other asset-backed	4.07	4.00	4.23	4.24	3.30	5.07	4.35
Variable-rate notes	0.84	1.89	2.04	2.63	2.37	3.00	2.52
Bonds sold abroad - total	2.33	2.30	3.79	3.37	3.20	3.00	3.90
Nonfinancial	1.00	0.84	0.64	1.08	1.45	0.80	1.00
Financial	1.33	1.46	3.15	2.28	1.75	2.20	2.90
Stocks sold abroad - total	0.46	0.50	0.53	0.45	0.37	0.31	0.67
Nonfinancial	0.38	0.39	0.37	0.27	0.30	0.28	0.24
Financial	0.08	0.11	0.16	0.18	0.07	0.03	0.42

1. Securities issued in the private placement market are not included. Total reflects gross proceeds rather than par value of original discount bonds.
2. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings.
3. Bonds categorized according to Moody's bond ratings, or to Standard and Poor's if unrated by Moody's. Excludes mortgage-backed and asset-backed bonds.
4. Includes bonds convertible into equity and bonds with warrants that entitle the holder to purchase equity in the future.
p Preliminary.

These small resolutions required only minor outlays of loss funds. It is still unclear whether Congress will approve additional funding for the RTC to complete the thrift cleanup.

Business Finance

The familiar pattern in business borrowing during recent quarters was again evident during the intermeeting period: Businesses continued to strengthen their balance sheets and cash flows by issuing large volumes of longer-term debt and equities, and using the proceeds to retire higher-cost outstanding debt. Issuers have moved to lock in funding costs for the long term as long maturity rates have fallen to twenty-year lows, and investors are continuing to "reach for yield" by lengthening the maturity of their portfolios and accepting greater risk.

In July, Walt Disney and Coca-Cola took the trend toward long-term debt issuance a step further, becoming the first firms in forty years to issue U.S. public bonds having hundred-year maturities. Yields on the bonds came in roughly 25 to 35 basis points higher than yields on thirty-year bonds issued by corporations with similar ratings. Disney and Coca-Cola were not alone in exploring the far frontier of the maturity spectrum. Also in July, Pacific Bell became the fifth corporation this year to sell a fifty-year bond. Indeed, during the first half of 1993, 36 percent of investment-grade bonds issued by nonfinancial corporations have had maturities of thirty years or longer, the highest percentage since 1987. Moreover, long-term debt offerings have not been limited to investment-grade bonds; Cablevision Systems (B2/B) issued a thirty-year bond in April, and Time Warner (Ba2/BBB-) issued a forty-year bond in July.

Investors' willingness to accept more risk in return for higher yields is evident in the strength of the junk bond market. Junk bond issuance remained strong in July, and if it continues at its current pace, junk bond volume in 1993 will exceed the $42 billion record set in 1986. The character of junk bond financing in the 1990s has generally differed from that in the 1980s. Companies have been using the proceeds from offerings primarily to pay down high coupon bonds and bank loans rather than to finance mergers and LBOs. Recently, however, junk quality appears to have deteriorated, as evidenced by a higher volume of subordinated offerings, a decline in the credit quality of new issuers, and a reemergence of relatively risky pay-in-kind and zero coupon structures.

Investors in the speculative-grade market have become more receptive to first-time issuers, which generally have smaller financing requirements than companies that had previously accessed the public bond market. Secondary market yields on many junk bonds have fallen below 10 percent, and spreads to Treasury securities are at their lowest level since early 1989, before the market collapsed.

After posting substantial declines during the early months of 1993, commercial paper has grown at nearly a 20 annual percent rate since May. Some corporate borrowers reportedly have issued commercial paper this year while awaiting still lower long-term rates. In addition, a portion of the growth in commercial paper during July owed to borrowing by the government of Denmark,

. Finally, some of the additional commercial paper issued may have been used for basic business purposes. Commercial paper issuers have found the markets receptive; yields spreads relative to Treasury bills are quite narrow, and spreads between A-2/P-2 and A-1/P-1 commercial paper have fallen to their narrowest point since the SEC proposed its amendment to rule 2a-7 three years ago.

Net equity issuance in July slipped only slightly from the very robust pace of the first half of 1993. The continued heavy flow of new equity issues likely owes to the buoyant stock market and perhaps to attempts by many businesses to secure a favorable market reception for new long-term debt issues. The staff estimates that net equity issuance by nonfinancial firms amounted to $32 billion (annual rate) in the second quarter, compared with $29 billion in the first quarter. The market for initial public offerings has remained robust; nonfinancial firms raised more than $1.5 billion in June and reportedly maintained that pace in July.

Municipal Securities

Gross issuance of long-term, tax-exempt bonds was strong again in July, with most issuance earmarked for refunding of existing debt. Through the first seven months of this year, long-term volume is on a pace that, if maintained, would exceed last year's record volume by almost 40 percent. Indeed, refunding issuance in 1993 has

GROSS OFFERINGS OF MUNICIPAL SECURITIES
(Monthly rates, not seasonally adjusted, billions of dollars)

			1993				
	1991	1992	Q1	Q2	May	June^p	July^p
Total offerings[1]	16.68	21.78	23.88	32.69	29.74	41.62	26.26
Total tax-exempt	16.26	21.21	23.37	31.77	28.67	40.45	25.88
Long-term	12.87	17.93	21.75	25.56	27.18	28.53	21.60
Refundings[2]	3.12	7.91	15.04	17.28	18.90	17.32	13.87
New capital	9.75	10.02	6.71	8.28	8.68	11.21	7.73
Short-term	3.39	3.28	1.62	6.21	1.49	11.92	4.28
Total taxable	.42	.57	.54	.92	1.07	1.17	.38

1. Includes issues for public and private purposes.
2. Includes all refunding bonds, not just advance refundings.
p Preliminary.

already established a new annual high. By contrast, new capital issuance has run well behind last year's pace.

Municipal bond yields have been subject to upward pressure since the last FOMC meeting. As a result, the ratio of the Bond Buyer's index of revenue bond yields to the thirty-year Treasury bond rate has jumped to its highest level since October of last year. The increase in the ratio has occurred despite substantial bond redemptions in July and the growing certainty of hikes in marginal tax rates under the deficit reduction package. Market participants report that investor demand, particularly from municipal bond funds, has abated somewhat, after being unusually heavy in May and June when purchasers sought to obtain bonds in anticipation of large redemptions in July.

Changes in credit ratings for long-term municipal bonds during the second quarter presented a mixed picture. At Standard and Poor's, the number of downgrades exceeded the number of upgrades by nearly a two-to-one margin, whereas at Moody's the number of upgrades outpaced the number of downgrades by a three-to-two margin. The difference between the two agencies stemmed partly from their disparate treatment of so-called "moral obligation" housing bonds. These are revenue bonds issued by state agencies for which the state is authorized, but not required, to appropriate funds from general revenues if needed to meet scheduled debt payments. Standard and Poor's downgraded a number of these bonds based on its perception that the will to meet the moral commitments had weakened in some states suffering from slow economic growth. Moody's attaches little weight to the moral obligation, so that firm's ratings for these issues were largely unchanged. Apart from this difference, both Moody's and Standard and Poor's reported deterioration in the credit quality of health care and hospital bonds, continued improvement among municipal utilities, and little change in general obligation issues.

The rating agencies have focused on two concerns in their initial evaluation of the credit ratings of local government units affected by the flooding in the Midwest. One is the availability of federal emergency funds to finance the reconstruction of roads, bridges, utility plants, and other public facilities damaged by the floods. Such losses generally are not covered by insurance, and the absence of adequate federal assistance could impair the financial condition of affected municipalities. The other concern is the longer-term impact of the flood on local tax bases. Municipal bond dealers indicate that yields on securities of issuers within the flood region have not yet shown any reaction. The rating agencies have not yet published any downgrades as a result of the flood.

California's 1994 budget received a vote of confidence last month as the rating agencies affirmed their earlier ratings of the state's bonds: double-A from Moody's and A-plus from Standard and Poor's. Although the state remains vulnerable to further economic setbacks, the agencies concluded that it had taken appropriate steps to keep the budget in balance and to generate funds necessary to eliminate the $2.8 billion deficit carried over from previous years. The city of Los Angeles received less favorable treatment; Moody's lowered its Aaa rating to Aa1 in late July. The downgrading reflected a number of factors including losses of tax revenues resulting from the depressed local economy.

<u>Treasury Financing</u>

The staff anticipates that the Treasury will finance a projected $63 billion third-quarter fiscal deficit by borrowing $48 billion in the market and by drawing down its cash balance by $13 billion. Nonmarketable borrowing is expected to be negligible; the lowering of guaranteed rates earlier this year has slowed savings bond growth, and state and local government series bonds (SLGS) have been running off as municipalities have increasingly invested the proceeds of advance refunding operations in eligible, higher-yielding instruments. The recently passed budget bill included a permanent increase in the debt ceiling to $4.9 trillion, thereby avoiding possible disruptions at the end of September when the temporary debt ceiling of $4.4 trillion was due to expire. At the end of July, debt subject to the limit totaled $4.3 trillion.

TREASURY FINANCING[1]
(Total for period; billions of dollars)

	1993				
	Q2	Q3[p]	July[e]	Aug.[p]	Sept.
Treasury financing					
Total surplus/deficit (-)	-17.8	-63.1	-42.0	-30.5	9.3
Means of financing deficit:					
Net cash borrowing from the public	61.1	47.9	1.2	50.0	-3.3
Marketable borrowings/ repayments (-)	53.6	50.0	5.2	48.7	-3.9
Bills	-.6	8.3	11.9	6.1	-9.7
Coupons	54.3	41.7	-6.7	42.6	5.8
Nonmarketable	7.4	-2.1	-4.0	1.3	.6
Decrease in the cash balance	-39.0	12.9	32.4	-8.9	-10.7
Memo: Cash balance at end of period	60.6	47.7	28.1	37.1	47.7
Other[2]	-4.2	2.4	8.4	-10.6	4.6

1. Data reported on a not seasonally adjusted, payment basis.
2. Includes checks issued less checks paid, accrued items and other transactions.
e--estimated.
p--projected.
Note: Details may not add to totals due to rounding.

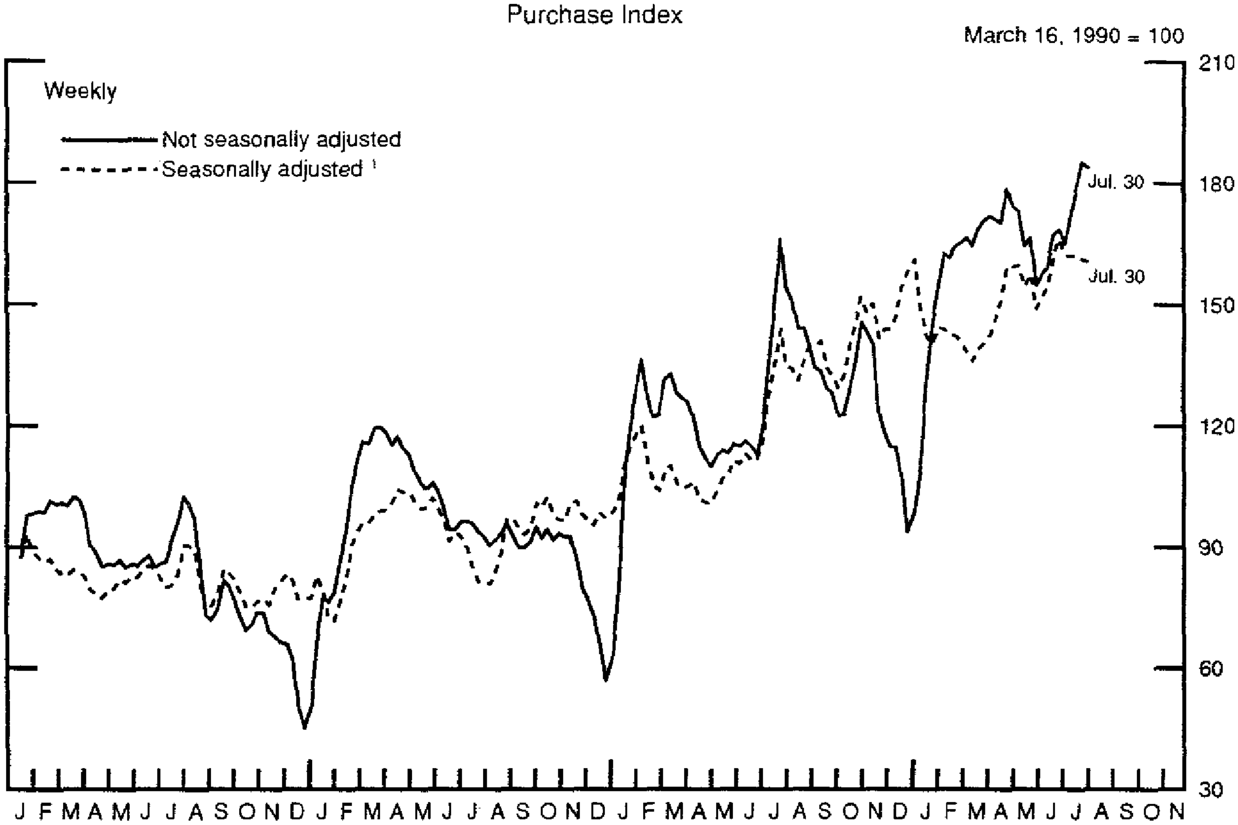
Most third-quarter marketable borrowing is expected to be in the coupon sector, with gross auction sizes generally unchanged to up \$500 million.[4] An exception to this pattern will be the gross size of the thirty-year bond auction. As part of its move to a semiannual auction schedule for thirty-year bonds, the Treasury auctioned \$11 billion of thirty-year bonds in the August midquarter refunding, up \$2-3/4 billion from the May auction; the next auction of thirty-year securities will be held in February, and the annual volume of bonds offered in the twice-yearly auctions is expected to be about 40 percent lower than the volume issued under the quarterly schedule. The August midquarter refunding, which also included \$16-1/2 billion of three-year notes and \$11 billion of ten-year notes, raised a total of about \$11.8 billion in cash. The gross size of the weekly Treasury bill auctions is expected to rise from the current level of \$24.4 billion to \$24.8 billion.

The Treasury completed the eleventh round of single-price auctions of two- and five-year notes in July. Thus far, the single-price auctions have resulted in an average markup of 1 basis point over when-issued rates; in comparison, the average markup of auction average rates for a sample of discriminating price auctions was about 1/2 basis point. Dealer awards as a fraction of total awards at single-price auctions have been little changed from that typical of discriminating-price auctions; evidently, single-price auctions have not yet significantly expanded the role of nondealers at Treasury auctions. The Treasury announced plans to continue the experiment with single-price auctions for another year to provide additional data for analysis and evaluation.

4. Of course, to finance the deficit, gross auction sizes are substantially larger than maturing issues.

MBA Indexes of Mortgage Loan Applications

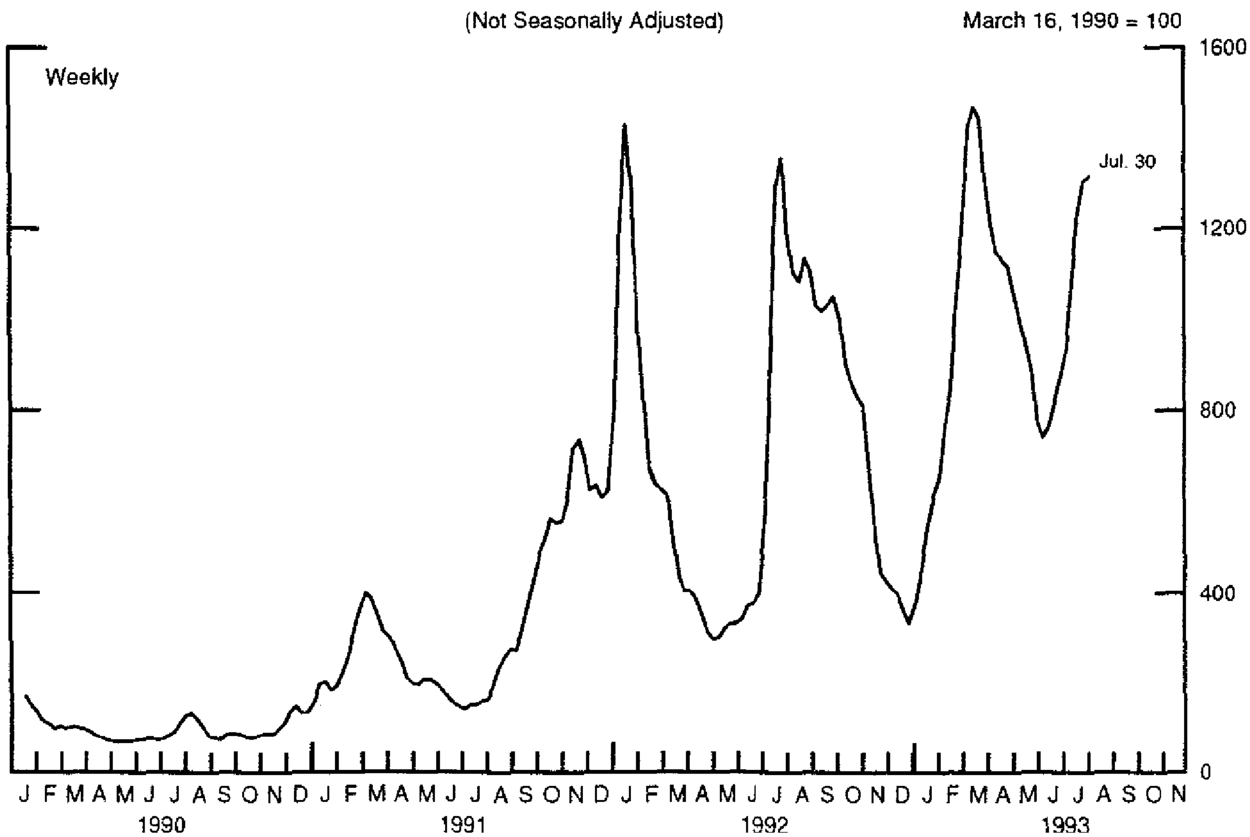
Purchase Index



1. Seasonally adjusted by Federal Reserve Board staff.

Refinancing Index

(Not Seasonally Adjusted)



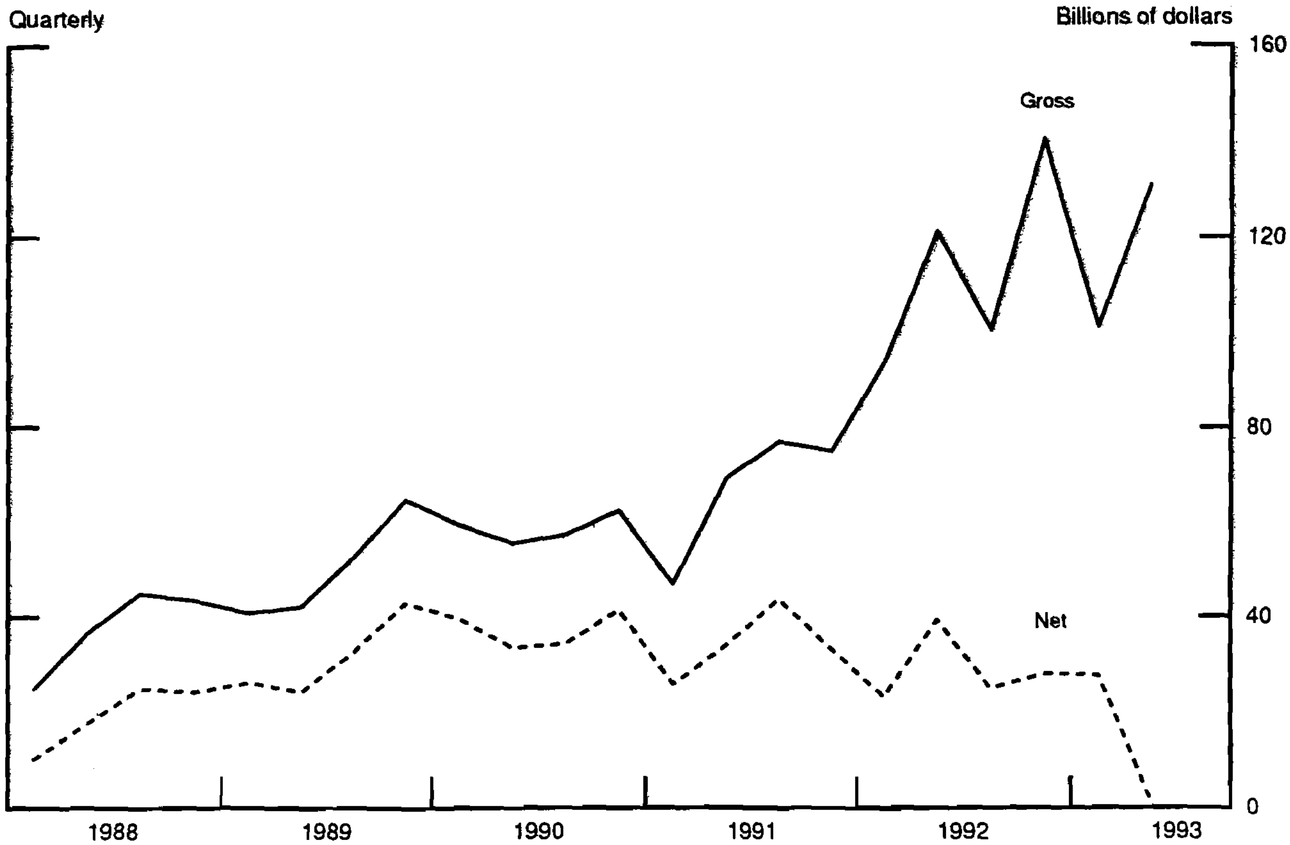
<u>Mortgage Markets</u>

As in other financial sectors, much of the activity in mortgage markets has been associated with the actions of households and businesses to refinance existing debt at lower rates. Interest rates on conventional thirty-year, fixed-rate mortgages, which generally track the ten-year Treasury note, were about unchanged since the last FOMC meeting; however, at about 7-1/4 percent, they remain twenty-five basis points below their average for the second quarter. The generally low level of rates has led to another surge of refinancings, with the Mortgage Bankers Association index of refinancing applications again approaching record highs in recent weeks (chart). Staff analysis suggests that households' efforts to reduce the interest costs of mortgage debt have been quite successful. Depending on various assumptions, estimates of total interest savings in 1993 range between $12 billion and $21 billion, with most of the savings associated with refinancing of fixed-rate mortgages.[5]

As a result of heavy refinancing of residential mortgages, gross issuance of agency pass-through securities returned to near-record levels in the second quarter, amounting to just over $130 billion on a not seasonally adjusted basis (chart). However, partly reflecting $23 billion of purchases by Fannie Mae and Freddie Mac for their own portfolios during the first half of 1993, gross issuance was barely enough to offset total retirements, resulting in net issuance for the quarter of only $1.5 billion. Fannie Mae and Freddie Mac have been able to boost their net interest income by expanding their portfolios over the past year. Combined with

5. Estimates of interest savings due to refinancings are based on expected total refinancings completed in 1993 and an estimate of the average interest rate reduction. Total interest savings also include an estimate of the impact of lower rates on existing adjustable rate mortgages.

Gross and Net Issuance of Agency Mortgage Pass-Through Securities
(Not seasonally adjusted)



Last observation is 1993:Q2

continued investor demand for assets with longer durations and higher yields, the lack of net new supply of pass-through securities has helped to keep secondary market yield spreads on current coupon pass-through securities relatively narrow.

<u>Consumer Credit</u>

Growth in consumer installment credit rebounded sharply in June to a seasonally adjusted annual rate of 12-1/4 percent after a small decline in May; growth for the second quarter as a whole was at a 4-1/2 percent rate, slightly below the revised first-quarter pace of 5 percent. Second-quarter growth was held down by the sale of a large portfolio of consumer loans by a finance company to an entity outside the scope of the consumer credit statistics. This transaction removed about $3 billion from the measured stock of installment credit in May; without that downward shift in outstanding credit, the rate of growth in the second quarter would have risen to about 6 percent. Total credit, which includes the small but volatile noninstallment credit component, expanded at a 3-1/2 percent pace in the the second quarter, about the same as in in the first quarter.

After softening over the previous three months, revolving credit grew at a 13 percent pace in June. Smoothing through the monthly volatility, revolving credit advanced at about an 8 percent pace through midyear. Stronger household balance sheets, as evidenced by reduced levels of scheduled debt service payments relative to income and by generally lower delinquency rates, have probably made people more comfortable about increasing the amount of their revolving debt. Sharply reduced interest rates in some segments of the credit card market and the promotion of several rebate-type incentive programs also have likely stimulated growth in revolving credit.

A pickup in sales at auto dealers has contributed to a turnaround in the growth of auto credit since late last year. Increased car sales have boosted new credit extensions well in excess of repayments on auto debt outstanding. Auto credit expanded at a 10 percent rate in June and has grown at a 5 percent annual rate since its trough in October 1992.

Auto credit growth this year has been damped somewhat by the growing popularity of leasing arrangements at the expense of traditional installment loans. According to industry estimates, approximately one in four new passenger cars acquired by individuals thus far in 1993 has been leased. The proportion of leased cars

CONSUMER CREDIT
(Seasonally adjusted)

	Percent change (Annual rate)							Memo: Outstandings[1] (Billions of dollars)
				1993				1993
	1990	1991	1992	Q1[r]	Q2[p]	May[r]	June[p]	June[p]
Installment	2.0	-.7	1.0	4.9	4.5	-1.2	12.3	758.5
Auto	-2.7	-8.4	-.5	4.2	5.9	10.0	10.0	266.2
Revolving	12.1	9.5	4.4	8.4	7.3	2.5	13.1	264.4
Other	-.8	-1.0	-.8	1.8	-.4	-18.3	13.9	227.9
Noninstallment	-4.6	-15.1	3.0	-8.5	-12.0	26.3	-96.0	49.5
Total	1.5	-1.8	1.2	4.0	3.4	0.6	5.0	808.0

1. Components may not sum to totals because of rounding.
r Revised. Reflects more complete information for savings institutions from March 1993 Call Report.
p Preliminary.

CONSUMER INTEREST RATES
(Annual percentage rate)

				1992	1993			
	1990	1991	1992	Nov.	Feb.	Apr.	May	June
At commercial banks[1]								
New cars (48 mo.)	11.78	11.14	9.29	8.60	8.57	...	8.17	...
Personal (24 mo.)	15.46	15.18	14.04	13.55	13.57	...	13.63	...
Credit cards	18.17	18.23	17.78	17.38	17.26	...	17.15	...
At auto finance cos.[2]								
New cars	12.54	12.41	9.93	9.65	10.32	9.61	9.51	9.45
Used cars	15.99	15.60	13.79	13.37	13.90	12.74	12.61	12.55

1. Average of "most common" rate charged for specified type and maturity during the first week of the middle month of each quarter.
2. For monthly data, rate for all loans of each type made during the month regardless of maturity.
Note: Annual data are averages of quarterly data for commercial bank rates and of monthly data for auto finance company rates.

grew fairly sharply from 1987 through 1991 and has edged a bit higher over the past several quarters. Auto manufacturers actively promoted car sales during the 1987-91 period by offering attractive lease terms (low implicit interest rates and high residual values), much as they offered below-market interest rates on loans in the early and mid-1980s. More recently, the scaling back of these special lease programs, along with historically low interest rates on bank and finance company loans, have slowed the shift to leasing.

INTERNATIONAL DEVELOPMENTS

Merchandise Trade

The merchandise trade deficit in May was $8.4 billion (seasonally-adjusted, Census-basis), much smaller than the deficits of March and April, but still above the levels recorded in the previous six months. Exports rose slightly from April to May, as increases in industrial supplies, machinery, and consumer goods offset declines in agricultural products, automotive vehicles and parts, and civilian aircraft. A drop in imports from April to May was attributable to a wide range of products, particularly automotive products, consumer goods, and oil.

U.S. MERCHANDISE TRADE: MONTHLY DATA
(Billions of dollars, seasonally adjusted, Census basis)

	Exports			Imports			
	Total	Ag.	NonAg.	Total	Oil	NonOil	Balance
1992-Jul	37.4	3.8	33.7	44.9	4.9	40.1	-7.5
Aug	36.4	3.6	32.8	45.1	4.6	40.4	-8.7
Sep	37.7	3.8	33.8	46.0	4.8	41.2	-8.3
Oct	38.9	4.0	34.9	46.1	5.0	41.1	-7.2
Nov	37.8	3.7	34.1	45.6	4.6	41.1	-7.8
Dec	39.2	3.7	35.5	46.1	4.1	42.0	-7.0
1993-Jan	37.5	3.5	34.0	45.2	4.2	40.9	-7.7
Feb	36.9	3.7	33.3	44.8	4.1	40.8	-7.9
Mar	38.9	3.6	35.3	49.3	4.5	44.9	-10.5
Apr	38.5	3.7	34.7	48.7	4.9	43.7	-10.2
May	39.0	3.6	35.4	47.3	4.6	42.8	-8.4

Source: U.S. Department of Commerce, Bureau of the Census.

For April/May combined, the trade deficit increased from the first quarter by over $11 billion at a seasonally adjusted annual rate (balance of payments basis). Both exports and imports rose substantially from first-quarter levels.

MAJOR TRADE CATEGORIES
(Billions of dollars, BOP basis, SAAR)

	Year	1992			1993		$ Change	
	1992	Q2	Q3	Q4	Q1	Q2-e	Q2e-Q2	Q2e-Q1
Trade Balance	-96.1	-99.2	-110.4	-103.8	-116.3	-127.9	-28.7	-11.6
Total U.S. Exports	440.1	433.2	438.0	456.0	446.5	456.8	23.6	10.3
Agric. Exports	44.0	42.6	44.7	45.5	43.4	44.0	1.4	0.6
Nonagric. Exports	396.1	390.6	393.3	410.4	403.1	412.8	22.2	9.8
Industrial Suppl.	101.8	100.9	102.3	104.5	102.7	105.6	4.8	3.0
Gold	4.5	3.5	3.6	7.2	6.4	9.3	5.8	2.9
Fuels	13.6	13.7	13.5	13.4	12.6	13.0	-0.8	0.3
Other Ind. Suppl.	83.7	83.6	85.2	83.8	83.6	83.4	-0.3	-0.3
Capital Goods	176.9	175.0	173.3	182.0	177.9	183.3	8.4	5.4
Aircraft & Parts	37.7	37.7	33.4	37.1	33.1	34.9	-2.8	1.8
Computers & Parts	28.8	28.7	28.8	30.0	28.8	28.4	-0.2	-0.4
Other Machinery	110.4	108.6	111.1	114.9	116.0	120.0	11.4	4.0
Automotive Goods	47.1	46.4	47.8	50.9	51.3	52.2	5.8	1.0
To Canada	23.8	23.8	24.2	25.6	26.4	27.1	3.3	0.7
To Other	23.2	22.6	23.6	25.4	24.9	25.1	2.5	0.2
Consumer Goods	50.4	49.0	51.0	53.3	51.5	52.4	3.5	0.9
Other Nonagric.	20.0	19.3	19.0	19.7	19.7	19.2	-0.2	-0.6
Total U.S. Imports	536.3	532.4	548.4	559.8	562.8	584.7	52.3	21.9
Oil Imports	51.6	52.4	57.2	54.9	51.0	57.0	4.6	6.0
Non-Oil Imports	484.7	480.0	491.2	505.0	511.8	527.7	47.7	15.9
Industrial Suppl.	88.6	88.1	88.3	93.5	94.1	99.4	11.4	5.3
Gold	3.8	3.6	2.7	6.7	5.3	10.1	6.5	4.8
Other Fuels	4.6	4.3	5.0	4.7	4.5	4.8	0.5	0.3
Other Ind. Suppl.	80.3	80.2	80.6	82.1	84.3	84.5	4.3	0.2
Capital Goods	134.2	131.8	137.8	141.8	142.7	147.6	15.9	4.9
Aircraft & Parts	12.6	13.3	12.3	13.0	10.6	10.9	-2.4	0.4
Computers & Parts	31.8	30.8	33.6	34.6	35.9	36.6	5.8	0.7
Other Machinery	89.8	87.6	91.9	94.2	96.2	100.1	12.4	3.8
Automotive Goods	91.8	91.2	91.8	95.1	100.1	101.9	10.7	1.8
From Canada	31.7	31.6	31.6	32.3	36.4	36.5	4.9	0.2
From Other	60.1	59.6	60.2	62.8	63.7	65.4	5.8	1.6
Consumer Goods	123.0	121.3	126.7	126.5	128.6	131.2	9.9	2.6
Foods	27.9	28.7	28.1	27.6	27.4	27.3	-1.5	-0.1
All Other	19.3	19.0	18.5	20.6	18.9	20.3	1.3	1.5

e--Average of first 2 months of quarter at an annual rate.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Exports for April/May combined recovered from a first-quarter decline, with the increase in exports consisting almost entirely of non-agricultural products. Most of the increase in exports went to Canada, and only part of this was automotive products. Exports to Japan fell slightly, while exports to the EC countries tumbled, reflecting those nations' slow growth and recessions. By product, the most notable increase in April/May was in exports of machinery; since the second quarter of last year, machinery exports have expanded about twice as fast as overall non-agricultural exports.

Imports in April/May were nearly 4 percent higher than in the first quarter. The increase was spread over most trade categories, with the largest rises in machinery and oil. Robust growth in U.S. investment expenditures has supported a steady expansion of imported machinery since the second quarter of last year. Imports of consumer goods and automotive products rose at a moderate pace in April/May. By area, non-oil imports from Canada (mostly non-automotive) and Europe accounted for most of the increase.

OIL IMPORTS
(BOP basis, seasonally adjusted annual rates)

	1992	1993		Months			
	Q4	Q1	Q2-e	Feb	Mar	Apr	May
Value (Bil. $)	54.85	51.02	56.97	48.92	53.33	59.15	54.80
Price ($/BBL)	17.89	16.42	17.27	16.35	16.86	17.20	17.34
Quantity (mb/d)	8.39	8.50	9.03	8.19	8.66	9.41	8.65

e--Average of first 2 months of quarter at an annual rate.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.

The value of imported oil increased in April/May, as prices increased slightly and the quantity imported jumped. Preliminary Department of Energy data suggest that the April/May gain in the

IMPORT AND EXPORT PRICE MEASURES
(percent change from previous period, annual rate)

	Year 1993-Q2 / 1992-Q2	Quarters 1992 Q4	1993 Q1	1993 Q2	Months 1993 May	Jun
		(Quarterly Average, AR)			(Monthly Rates)	
	--------------------BLS Prices--------------------					
Imports, Total	1.2	0.4	-5.1	3.7	0.4	-0.4
Foods, Feeds, Bev.	-0.3	2.8	-5.5	3.6	0.5	0.9
Industrial Supplies	0.1	-4.2	-9.2	5.2	-0.2	-1.8
Ind Supp Ex Oil	0.1	-0.5	-1.9	0.6	-0.3	-0.7
Capital Goods	1.3	-0.1	-4.4	1.8	0.7	0.2
Automotive Products	2.3	3.0	-2.8	5.1	0.6	0.0
Consumer Goods	1.8	2.9	-3.1	2.3	0.5	-0.1
Memo:						
Oil	-0.7	-11.4	-23.6	14.2	0.2	-3.5
Non-oil	1.3	1.5	-3.3	2.5	0.4	-0.1
Exports, Total	0.4	-1.0	1.2	1.6	0.3	-0.2
Foods, Feeds, Bev.	-3.0	-3.9	5.7	0.7	1.4	-2.8
Industrial Supplies	2.3	-2.7	1.9	4.7	0.5	-0.2
Ind Supp Ex Ag	--	--	1.6	5.6	0.6	-0.1
Capital Goods	0.1	-0.7	-0.7	0.2	-0.1	0.4
Automotive Products	1.4	2.5	1.2	0.5	0.1	-0.1
Consumer Goods	1.8	3.3	3.1	0.2	0.5	-0.6
Memo:						
Agricultural	-1.5	-2.7	5.6	-1.4	1.0	-2.9
Nonagricultural	1.0	-0.8	0.6	1.9	0.3	0.1
	------------Prices in the NIPA Accounts-----------					
Fixed-Weight						
Imports, Total	1.1	0.0	-5.2	3.6	--	--
Oil	-2.8	-14.0	-29.7	15.0	--	--
Non-oil	1.3	0.7	-2.4	2.9	--	--
Exports, Total	0.6	-0.4	0.7	1.8	--	--
Ag	-2.8	-6.0	4.9	-1.4	--	--
Nonag	1.1	0.0	0.7	1.8	--	--
Deflators						
Imports, Total	-1.6	-1.5	-7.7	0.8	--	--
Oil	-2.8	-12.7	-30.2	15.4	--	--
Non-oil	-1.5	-0.2	-5.1	-0.4	--	--
Exports, Total	-0.8	-1.1	-0.8	0.3	--	--
Ag	-0.1	4.1	5.1	-3.2	--	--
Nonag	-0.9	-1.5	-1.4	0.7	--	--

quantity of imported oil was associated with large increases in U.S. stocks, and that this pattern continued in June. For both April and May, imports amounted to more than half of U.S. consumption.

The price of imported oil averaged $17.27 per barrel in April/May, an increase of $0.85 per barrel from the first-quarter average, as OPEC reined-in production early in the second quarter. More recently, oil prices fell, on balance, as it appeared more likely that Iraq might begin oil sales under United Nations auspices. The apparent confusion within OPEC over a strategy for handling the return of Iraq to the world oil market also contributed to downward price pressure. Within the past two weeks, bickering between Saudi Arabia and Iran has kept prices low even as prospects for Iraqi sales have faded. Currently, the near-term futures contract for West Texas Intermediate is trading near $17.67 per barrel. Given contract and shipping lags, the oil import unit value should fall sharply, averaging roughly $15.60 per barrel in July.

Prices of Exports and non-Oil Imports

Non-oil import prices (BLS) declined slightly in June. For the second quarter as a whole, prices of non-oil imports rose by 2-1/2 percent at an annual rate, reversing the decline of the first quarter. Increases were recorded in prices of all major trade categories, with a notable rise in the price of imported automotive products.

Non-agricultural export prices rose by nearly 2 percent at an annual rate in the second quarter, led by strong increases in prices of industrial supplies, particularly building materials. Agricultural export prices fell, though not nearly enough to reverse the strong price increases of the first quarter.

U.S. International Financial Transactions

Foreign official reserve assets held in the United States rose by $17.6 billion in the second quarter (line 4 of the Summary of U.S. International Transactions table). An increase of over $14 billion in Japanese reserves, associated with exchange market intervention, dominated the picture. Spanish holdings fell by $5 billion, reflecting in part Spain's efforts to replenish its mark reserves.

In the second quarter, private foreigners purchased net $14.1 billion of corporate and U.S. agency bonds (line 2a), a substantial increase over the first quarter; about $8 billion were for U.S. agency bonds and $6 billion for corporates. European countries accounted for $4.7 billion of total net purchases ($3.9 billion for the U.K.) and residents of Japan for almost $3 billion. By contrast, private foreign net purchases of U.S. corporate stocks (line 2b) and U.S. Treasury obligations (line 3) were close to zero during the quarter.

U.S. residents continued their unprecedented net purchases of foreign stocks and bonds (line 2c). With a total of $21 billion in the second quarter, net purchases in the first half of 1993 ($49 billion) were nearly equal to the annual total for 1992 (a record $50.5 billion). Stock purchases accounted for over $13 billion of the second quarter total. As is typical, net stock purchases from the United Kingdom, at $3.6 billion, was the largest of the country totals; but significant net purchases from other countries were widespread. Net purchases from Canada were $1.3 billion, from Mexico almost $700 million, and from Japan just under $600 million. Net foreign bond purchases were concentrated in Europe, over $10 billion from residents of the United Kingdom; net bond purchases from Mexico continued high at $1.2 billion.

The net foreign position of banking offices in the United States changed little during the second quarter (line 1). In July,

SUMMARY OF U.S. INTERNATIONAL TRANSACTIONS
(Billions of dollars)

	1992	1992		1993		1993		
	Year	Q3	Q4	Q1	Q2	Apr.	May	June
Private Capital								
Banks								
1. Change in net foreign positions of banking offices[1] in the U.S. (+ = inflow)	39.2	37.2	-0.1	-9.4	-0.2	-1.1	-0.6	1.4
Securities								
2. Private securities transactions, net[2]	-19.4	-11.5	-5.3	-18.1	-6.7	-1.0	-0.4	-5.3
a) foreign net purchases (+) of U.S. corporate bonds[3]	34.8	6.6	8.7	5.8	14.1	4.4	3.7	6.0
b) foreign net purchases (+) of U.S. corporate stocks	-3.7	-3.8	4.2	3.9	0.4	-0.2	0.3	0.3
c) U.S. net purchases (-) of foreign securities	-50.5	-14.4	-18.1	-27.8	-21.2	-5.1	-4.5	-11.7
3. Foreign net purchases (+) of U.S. Treasury obligations	37.4	5.0	21.4	13.8	-0.3	2.8	1.5	-4.5
Official Capital								
4. Changes in foreign official reserves assets in U.S. (+ = increase)	38.1	-8.2	4.6	11.3	17.6	3.5	10.9	3.3
a) By area								
G-10 countries	4.8	3.8	-4.7	-1.9	17.5	4.9	7.3	5.3
OPEC	4.9	2.9	1.7	0.5	-1.7	-1.1	0.5	-1.1
All other countries	28.5	-14.9	7.5	12.7	1.8	-0.4	3.1	-0.9
b) By type								
U.S. Treasury securities	18.5	-0.3	-7.8	1.0	6.0	3.3	4.4	-1.7
Other[4]	19.7	-7.9	12.4	10.3	11.6	0.2	6.5	4.9
5. Changes in U.S. official reserve assets (+ = decrease)	3.9	2.0	1.5	-1.0	1.5	0.1	-0.2	1.5
Other transactions (Quarterly data)[5]								
6. U.S. direct investment (-) abroad	-34.8	-2.0	-11.5	-10.0	n.a.	n.a.	n.a.	n.a.
7. Foreign direct investment (+) in U.S.	2.4	1.0	3.1	5.8	n.a.	n.a.	n.a.	n.a.
8. Other capital flows (+ = inflow)[6]	11.8	-7.8	-5.3	23.8	n.a.	n.a.	n.a.	n.a.
9. U.S. current account balance	-66.4	-17.8	-23.7	-22.2	n.a.	n.a.	n.a.	n.a.
10. Statistical discrepancy	-12.2	2.1	15.3	6.0	n.a.	n.a.	n.a.	n.a.
MEMO:								
U.S. merchandise trade balance -- part of line 9 (Balance of payments basis, seasonally adjusted)	-96.1	-27.6	-26.0	-29.1	n.a.	n.a.	n.a.	n.a.

1. Includes changes in positions of all depository institutions, bank-holding companies, and certain transactions between brokers/dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements.)
2. These data have not been adjusted to exclude commissions on securities transactions and, therefore, do not match exactly the data on U.S. international transactions as published by the Department of Commerce.
3. Includes all U.S. bonds other than Treasury obligations.
4. Includes deposits in banks, commercial paper, acceptances, borrowing under repurchase agreements, and other securities.
5. Seasonally adjusted.
6. Includes U.S. government assets other than official reserves, transactions by nonbanking concerns, and other banking and official transactions not shown elsewhere. In addition, it includes amounts resulting from adjustments to the data made by the Department of Commerce and revisions to the data in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business.
*--Less than $50 million.
NOTE: Details may not add to total because of rounding.

INTERNATIONAL BANKING DATA
(Billions of dollars)

	1991				1992				1993			
	Mar.	June	Sept.	Dec.	Mar	June	Sept.	Dec.	Mar.	May	June	July */
1. Net Claims of U.S. Banking Offices (excluding IBFS) on Own Foreign Offices and IBFS	-23.8	-13.7	-14.1	-35.8	-41.4	-56.8	-58.0	-71.6	-77.1	-81.9	-79.0	-89.0
(a) U.S.-chartered banks	7.6	5.4	11.0	12.4	3.2	8.3	12.7	17.0	8.9	11.4	16.8	17.2
(b) Foreign-chartered banks	-31.3	-19.2	-25.2	-48.3	-44.6	-65.1	-70.9	-88.6	-86.0	-93.3	-95.8	-106.2
2. Credit Extended to U.S. Nonbank Residents by Foreign Branches of U.S. Banks	26.0	23.9	23.7	23.9	23.3	24.5	24.8	24.8	23.5	23.5	23.1	22.5
3. Eurodollar Holdings of U.S. Nonbank Residents 1/	114.6	105.8	100.8	102.9	100.3	91.2	86.3	90.0	89.5	87.7	86.1	81.8

1. Includes term and overnight Eurodollars held by money market mutual funds. Note: These data differ in coverage and timing from the overall banking data incorporated in the international transactions accounts. Line 1 is an average of daily data reported to the Federal Reserve by U.S. banking offices. Line 2 is an average of daily data. Line 3 is an average of daily data for the overnight component and an average of Wednesday data for the term component.

*/ Data through July 26.

however, monthly average data on the net claims of U.S. banking offices on their own foreign offices and IBFs indicate substantial inflows, particularly into foreign-chartered banks. (See lines 1 and 1b of the International Banking Data table.)

Foreign Exchange Markets

Since the July 7 FOMC meeting, the weighted-average dollar has risen about 1 percent. The dollar has declined nearly 4 percent versus the Japanese yen. The yen strengthened as the U.S.-Japan agreement on a framework for trade negotiations, reached on July 10, failed to reduce perceived tensions between the two countries over trade imbalances. The electoral defeat of the Liberal Democratic Party for the first time in 38 years, and the subsequent uncertainty over the formation of a new Japanese government, depressed the yen only temporarily. Near the end of the period, the dollar reached a record low of about ¥103.50 following news of a further widening of the Japanese trade surplus.

In contrast to its movement against the yen, the dollar has risen about 1/2 percent against the mark since the July FOMC meeting and substantially more against most other ERM currencies. Pressures on the ERM came to a head at the end of July, prompting a decision to greatly widen the margins of allowed currency movement around the central parities.

German short-term interest rates moved substantially lower during July, with three-month rates now 75 basis points lower than on July 7, however unfavorable news about the French economy fed expectations that French policymakers would try to reduce interest rates faster than the Bundesbank. During July, the French franc, as well as the Belgian franc, the Danish krone, and the Iberian currencies, came under downward pressure relative to the mark, forcing sharp increases in short-term interest rates in those countries. The Bank of France suspended its 5-to-10 day RP facility, replacing it with an overnight RP facility and raising the RP rate to 10 percent. Though that rate usually serves as a ceiling to overnight market rates, a shortage of eligible collateral limited banks' ability to borrow at the RP rate, and French overnight market rates rose well above 10 percent.

As ERM pressures increased, market expectations developed that the Bundesbank would respond by easing its monetary policy at a quicker pace. In particular, market participants expected the Bundesbank to lower its discount rate by 1/2 percentage point at its Council meeting on July 29, leaving room for reductions in the Bundesbank's RP rate during August. In fact, the Bundesbank left its discount rate unchanged, precipitating a sharp rise in pressures within the ERM.

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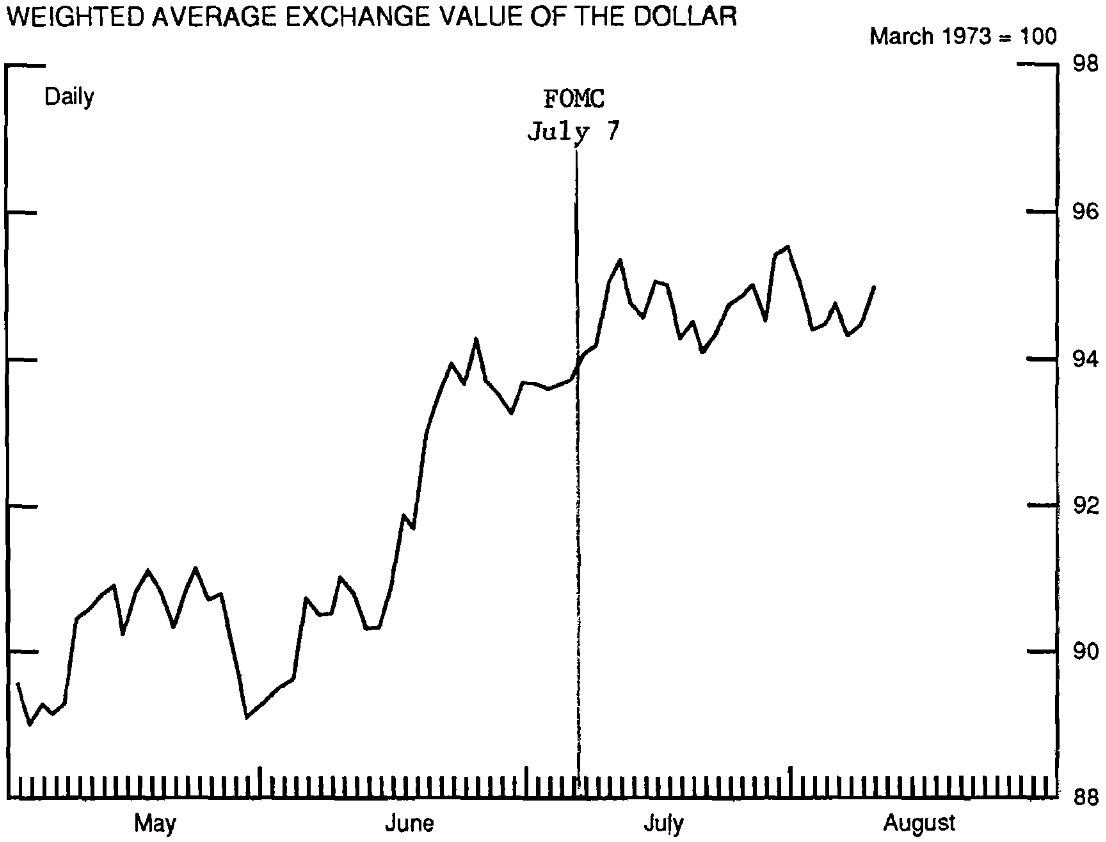
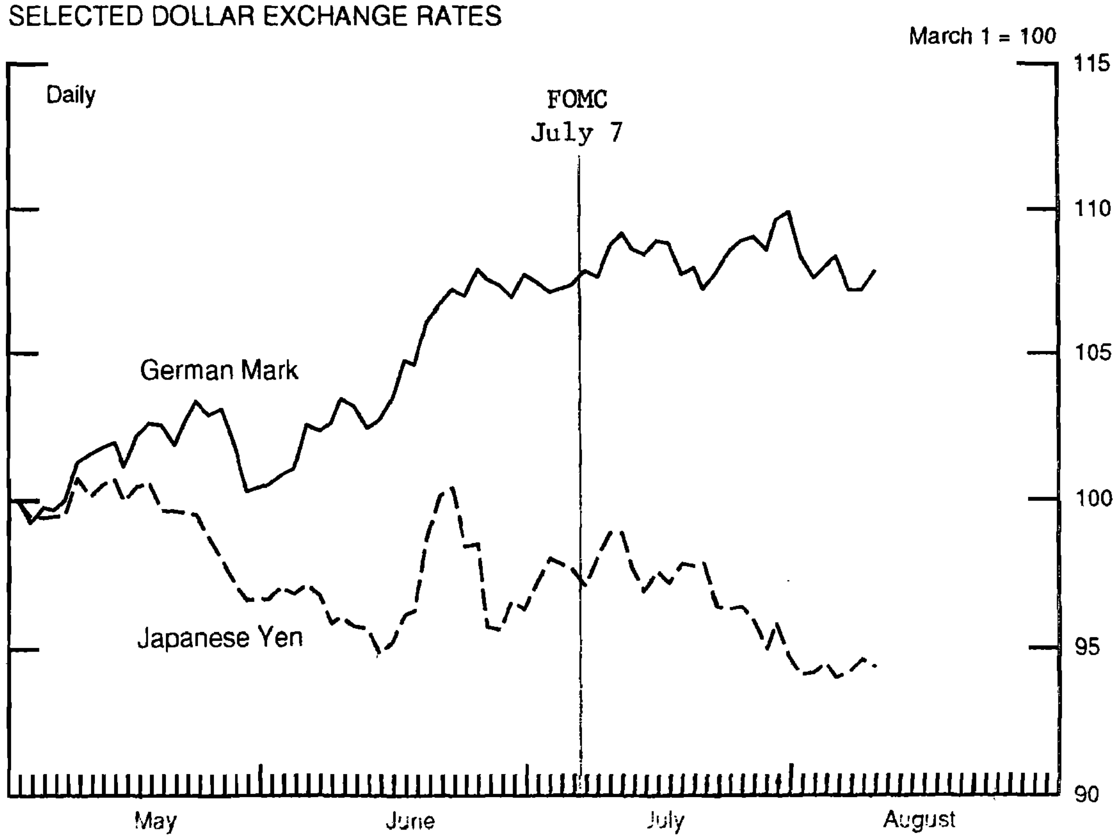
with the Bundesbank having indicated its unwillingness to alter its monetary policy to reflect external considerations, European officials met that weekend to consider ways to deal with the currency pressures. After intensive discussions, it was finally agreed that all the ERM currencies would be allowed to deviate as much as 15 percent from the central parities, as opposed to the prior allowed deviations of 2-1/4 percent for most ERM currencies and 6 percent for the Spanish peseta and the Portuguese escudo. In a side agreement, the German and Dutch central banks reestablished a 2-1/4 percent band between their two currencies.

On Monday, August 2, following the announcement of the new bands, the French franc, the Belgian franc, and the Danish krone each declined more than 2 percent below the bottom of their previous

WEIGHTED AVERAGE EXCHANGE VALUE OF THE DOLLAR



SELECTED DOLLAR EXCHANGE RATES



bands against the mark. Subsequently, the Belgian franc and the French franc have stabilized at 1-1/2 and 2-1/2 percent, respectively, below the bottom of the previous bands, while the Danish krone has moved down to about 4-1/2 percent below its previous lower limit. Those three central banks have kept official interest rates well above German interest rates in an attempt to regain exchange rate stability, though there has been some easing relative to the high levels reached at the height of the crisis. Market participants expect substantial easing of interest rates in those countries in the near future, as reflected in market interest rates of three and six month maturities. European stock and bond markets have rallied on the expectation of interest rate cuts. The French stock market has risen 7 percent since July 29 and French bond yields have declined about 35 basis points.

, with no intervention by U.S. authorities.

Developments in Foreign Industrial Countries

Real growth in the major foreign industrial countries was mixed in the second quarter. Output continued to decline in western Germany, while in Japan economic activity appears to have stalled after modest growth in the first quarter. In contrast, British real GDP continued to grow at a modest pace, and economic activity in Canada continued to move ahead, although more slowly than in the first quarter. French output appears to have been flat, or down slightly, in the second quarter after falling more steeply in the two previous quarters.

In recent months inflation in foreign industrial countries has been relatively steady. Inflation in western Germany and Japan has increased somewhat due to special factors lately, but slack in the

Italian and British economies has held inflation down in spite of sharp depreciations of the lira and pound following their exits from the ERM last September.

Recent budget developments suggest that fiscal policy is not likely to provide much additional boost to growth in the medium term. The Italian government recently presented a new FY1994 budget incorporating further tightening, and the FY1994 budget recently approved by the German cabinet is designed to hold the Federal deficit in Germany at this year's level. Lack of consensus on economic matters among the members of the new ruling coalition in Japan is likely to preclude a substantive change in fiscal policy in the short run. The French government recently proposed some modest new spending.

Individual Country Notes. In Japan, second-quarter data suggest that on balance economic activity slowed, although there have been signs of a pick-up toward the end of the quarter. Industrial production (s.a.) grew 1.3 percent in June after declining 2.5 percent in April and 2.6 percent in May. New car registrations (s.a.) rose 8.5 percent in June following a cumulative 20.3 percent slide in April and May, and housing starts (s.a.) ticked up 3.3 percent after declining 8.2 percent over the same two-month period. Among less positive signs, the index of leading indicators fell below the boom/bust demarcation line in May for the first time in five months, and new machinery orders (s.a.) in the second quarter were down 9.5 percent from their first-quarter average. The ratio of job offers to applicants declined from 0.81 in May to 0.74 in June, while the unemployment rate held steady at 2.5 percent.

Consumer prices in the Tokyo area ticked up in July, advancing 1.7 percent on a 12-month basis compared with 0.9 percent in June.

The July increase was attributed to higher fresh food prices resulting from poor weather; excluding perishables, Tokyo consumer prices rose 1.4 percent on a 12-month basis in July, only slightly above June's 1.3 percent rate. In part reflecting appreciation of the yen, wholesale prices continued to decline in June, falling 3.2 percent below their year-earlier level.

The trade surplus (customs basis, s.a.) edged down from $10 billion in May to $8.7 billion in June before rebounding to $11.2 billion in July, bringing the cumulative surplus for the first seven months of 1993 to $121 billion (a.r.) compared with $107 billion for 1992 as a whole. The June current account surplus (s.a.) declined to $9 billion from $11.1 billion in May; the cumulative surplus for the first half of 1993 was $136 billion (a.r.), up from $117 billion for all of 1992.

A newly formed coalition of opposition parties gained control of the Diet and on August 6 elected reformist politician Morihiro Hosokawa, a former LDP member and provincial governor, to be Japan's new prime minister. Hirohisa Fujii, a former Finance Ministry official and LDP member of the Diet's Upper House, will serve as Finance Minister. Because the anti-LDP coalition encompasses ideological positions ranging from ex-LDP, pro-business conservatives to the Socialists, it is considered unlikely to generate the consensus needed to change Japanese economic policy substantially in the near term.

Major economic indicators in western Germany point to a continued decline in real GDP in the second quarter following a drop of almost 6 percent (s.a.a.r.) in the first quarter. Industrial production fell 1.8 percent at an annual rate in the second quarter from an already low first-quarter level. Total orders (s.a.) edged up slightly in the second quarter from their first-quarter average.

REAL GDP AND INDUSTRIAL PRODUCTION IN MAJOR INDUSTRIAL COUNTRIES
(Percentage change from previous period, seasonally adjusted 1/)

	1991	1992	1992 Q3	1992 Q4	1993 Q1	1993 Q2	1993 FEB	1993 MAR	1993 APR	1993 MAY	1993 JUN	Latest three months from year ago 2/
JAPAN												
GDP	3.0	0.0	-0.5	-0.2	0.7	NA	*	*	*	*	*	-0.3
IP	-1.6	-7.7	0.1	-2.9	-0.1	-1.7	1.5	2.5	-2.5	-2.6	1.3	-4.5
WEST GERMANY												
GDP	2.0	0.4	-0.4	-0.8	-1.4	NA	*	*	*	*	*	-2.9
IP	0.1	-4.6	-1.4	-4.1	-2.9	-0.5	-1.3	1.5	-1.0	0.7	-1.5	-8.6
FRANCE												
GDP	1.1	0.7	0.1	-0.3	-0.5	NA	*	*	*	*	*	-0.6
IP	1.8	-2.3	-0.1	-2.6	-0.9	NA	2.4	-1.0	-0.5	0.2	NA	-3.7
UNITED KINGDOM												
GDP	-1.7	0.2	0.4	0.3	0.4	0.4	*	*	*	*	*	1.5
IP	-0.7	0.5	0.8	0.9	0.2	NA	1.6	-1.2	-0.1	2.0	NA	2.1
ITALY												
GDP	1.7	-0.2	-0.4	-0.4	-0.1	NA	*	*	*	*	*	-0.9
IP	-0.5	-3.2	-2.3	-0.7	1.2	NA	0.6	-1.5	-4.3	NA	NA	-5.1
CANADA												
GDP	-0.1	0.8	0.1	0.7	0.9	NA	*	*	*	*	*	1.7
IP	-1.1	2.6	0.7	1.6	1.9	NA	1.0	1.5	-0.9	-0.2	NA	5.0
UNITED STATES												
GDP	0.1	3.1	0.8	1.2	0.2	0.4	*	*	*	*	*	2.6
IP	-0.3	3.2	0.2	1.6	1.4	0.5	0.5	0.2	0.3	-0.0	-0.2	3.7

* Data not available on a monthly or quarterly basis.
1/ Yearly data are Q4 to Q4 percent change.
2/ For quarterly data, latest quarter from a year ago.

CONSUMER AND WHOLESALE PRICES IN MAJOR INDUSTRIAL COUNTRIES
(Percentage change from previous period 1/)

	1991	1992	1992 Q1	1992 Q2	1992 Q3	1992 Q4	1993 Q1	1993 Q2	1993 APR	1993 MAY	1993 JUN	1993 JUL	Latest month from year ago 2/
JAPAN													
CPI	3.2	0.9	-0.3	1.3	-0.1	0.0	0.0	1.1	0.6	0.4	-0.2	0.4	1.7
WPI	-1.7	-1.5	-0.4	0.0	-0.2	-0.9	-0.5	-1.4	-0.5	-0.3	-0.5	NA	-3.2
WEST GERMANY													
CPI	3.9	3.7	1.2	1.1	0.5	0.9	1.8	1.0	0.3	0.3	0.2	0.1	4.3
WPI	1.6	-1.9	0.4	0.5	-2.0	-0.8	0.7	0.1	-0.1	-0.1	0.2	NA	-1.8
FRANCE													
CPI	2.9	1.8	0.5	0.8	0.0	0.5	0.8	0.7	0.1	0.2	0.0	NA	2.0
WPI	-3.6	-2.1	0.2	0.4	-0.4	-2.3	0.0	NA	*	*	*	*	-2.3
UNITED KINGDOM													
CPI	4.2	3.1	0.5	2.2	-0.1	0.4	-0.7	1.6	0.9	0.4	-0.1	NA	1.2
WPI	4.9	3.4	1.4	1.1	0.4	0.5	1.7	1.3	0.5	0.2	0.1	NA	4.0
ITALY													
CPI	6.1	4.8	1.4	1.2	0.7	1.3	1.0	1.1	0.4	0.4	0.5	0.4	4.4
WPI	1.1	3.0	0.0	0.8	-0.5	2.8	1.6	NA	0.7	-0.3	NA	NA	4.9
CANADA													
CPI	4.1	1.8	0.4	0.5	0.4	0.4	0.7	0.2	0.0	0.2	0.1	NA	1.6
WPI	-3.2	3.3	0.5	0.6	0.8	1.2	1.2	-0.0	-0.2	-0.1	0.1	NA	2.9
UNITED STATES													
CPI (SA)	3.0	3.1	0.8	0.8	0.7	0.8	0.9	0.7	0.4	0.1	0.0	NA	3.0
WPI (SA)	-0.1	1.5	0.1	0.8	0.4	0.2	0.6	0.7	0.6	0.0	-0.3	NA	1.5

* Data not available on a monthly or quarterly basis.
1/ Yearly data are Q4 to Q4 percent change.
2/ For quarterly data, latest quarter from year ago.

TRADE AND CURRENT ACCOUNT BALANCES OF MAJOR INDUSTRIAL COUNTRIES 1/
(Billions of U.S. dollars, seasonally adjusted except where otherwise noted)

	1991	1992	1992 Q1	1992 Q2	1992 Q3	1992 Q4	1993 Q1	1993 Q2	1993 APR	1993 MAY	1993 JUN	1993 JUL
JAPAN												
TRADE	78.5	107.3	28.0	24.5	26.2	28.6	29.7	29.9	11.2	10.0	8.6	11.2
CURRENT ACCOUNT	73.1	117.2	28.6	28.8	28.1	31.7	36.0	31.8	11.7	11.1	9.0	NA
GERMANY												
TRADE (NSA)	13.6	21.4	4.4	3.4	8.6	5.0	5.9	NA	0.8	NA	NA	NA
CURRENT ACCOUNT (NSA)	-19.5	-26.0	-5.5	-6.6	-8.7	-5.2	NA	NA	NA	NA	NA	NA
FRANCE												
TRADE	-5.3	5.6	1.1	1.9	1.3	1.3	2.5	NA	1.4	NA	NA	NA
CURRENT ACCOUNT	-5.8	2.7	-1.3	1.1	0.1	2.9	NA	NA	*	*	*	*
UNITED KINGDOM												
TRADE	-18.3	-24.1	-5.4	-5.7	-6.2	-6.8	NA	NA	NA	NA	NA	NA
CURRENT ACCOUNT	-10.0	-20.6	-5.1	-5.6	-4.2	-5.8	NA	NA	NA	NA	NA	NA
ITALY												
TRADE	-13.0	-10.5	-2.2	-4.1	-2.3	-1.9	NA	NA	NA	NA	NA	NA
CURRENT ACCOUNT (NSA)	-21.4	-25.4	-9.0	-5.4	-6.4	-4.7	NA	NA	*	*	*	*
CANADA												
TRADE	4.3	7.4	1.3	1.4	1.7	2.9	2.5	NA	1.0	0.5	NA	NA
CURRENT ACCOUNT	-25.3	-23.0	-6.7	-6.1	-5.6	-4.6	-4.7	NA	*	*	*	*
UNITED STATES												
TRADE	-73.8	-96.1	-17.8	-24.8	-27.6	-26.0	-29.1	NA	-11.5	-9.8	NA	NA
CURRENT ACCOUNT	-8.3	-66.4	-6.7	-18.3	-17.8	-23.7	-22.2	NA	*	*	*	*

* Data not available on a monthly or quarterly basis.
1/ The current account includes goods, services, and private and official transfers.

JAPANESE ECONOMIC INDICATORS
(percent change from previous period except where noted, s.a.)

	1992		1993				
	Q3	Q4	Q1	Q2	Apr.	May.	Jun.
Machinery Orders	8.4	-14.8	16.0	-9.5	-23.3	16.8	-2.9
New Car Registrations	-1.9	-5.6	10.7	-11.8	-11.2	-10.2	8.5
Job Offers Ratio	-9.7	-7.8	-3.2	-12.5	-4.5	-3.6	-8.6
Business Sentiment*	-37	-44	-49	-49	--	--	--

* Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.

WESTERN GERMAN ECONOMIC INDICATORS
(percent change from previous period except where noted, s.a.)

	1992		1993				
	Q3	Q4	Q1	Q2	May	Jun.	Jul.
Total Orders	-2.3	-7.1	-0.9	0.2	2.7	-1.7	--
Capacity Utilization	-2.2	-3.1	-2.5	-0.3	--	--	--
Unemployment Rate (%)	6.7	7.2	7.6	8.1	8.1	8.2	8.3
Production Plans* (%)	-12.0	-33.3	-25.7	-21.7	-22.0	-19.0	--

* Percent of mining and manufacturing firms that expect to increase production minus those that expect to decrease it.

led by an increase in foreign orders. In July, the unemployment rate (s.a., as a percent of the dependent labor force) rose to 8.3 percent, up from 8.2 percent in June but below the 9.4 percent peak registered in 1983.

Consumer prices in western Germany increased 4.3 percent in July on a year/year basis, reflecting in part the higher value-added tax introduced at the beginning of January as well as increases in postal rates and a tax on insurance premiums that took effect in July. Underlying price pressures have remained moderate. Wholesale prices dropped 1.8 percent for the year ending in June, while producer prices declined 0.4 percent over the same period.

Through June, M3 in western and eastern Germany combined increased 7.1 percent (s.a.a.r.) relative to the fourth quarter of last year, a pace above Bundesbank's 1993 target range of 4-1/2 to

6-1/2 percent. The Bundesbank resumed its policy of gradual easing in early July when the discount and Lombard rates were reduced to 6-3/4 and 8-1/4 percent, respectively; on July 29, the Lombard rate was lowered again to 7-3/4 percent. During this period the repo rate also was cut several times.

The Federal budget for 1994 and medium-term financial plan were approved by the German cabinet earlier this summer and await passage by parliament this fall. The budget package would institute a number of expenditure-reducing measures, the most important of which is a sizable cut in unemployment benefits and a freeze on nominal wages of permanent public-sector employees. The Federal budget deficit would be held to about DM 68 billion in 1994, unchanged from the expected deficit for 1993. By 1995, the budget package is anticipated to hold the broad public-sector deficit to about 3 percent of all-German GNP, down from 5-1/2 percent registered in 1992.

In France, real GDP declined 2 percent (s.a.a.r.) in the first quarter after falling a revised 1.2 percent in the fourth quarter. Monthly indicators from the second quarter have been relatively flat. Industrial production (s.a.) rose 0.2 percent in May after declining 0.6 percent in April, and has recovered somewhat from low levels registered early in the year. An industry survey by the Bank of France indicates that industrial production probably was flat in June. The unemployment rate (s.a.) continued to rise in June, reaching 11.6 percent. Consumption of manufactured products (equal to 1/3 of total consumption) rose 0.3 percent (s.a.) in the second quarter, suggesting that consumption spending stabilized after falling in the first quarter.

Inflation has remained at a relatively low level. The consumer price index in June was only 2.0 percent above its year-earlier level, the same as in the previous month.

The French trade balance has continued to record large surpluses. In April, it registered a surplus (s.a.) of $1.4 billion after recording a surplus of $2.5 billion in the first quarter.

The government announced that later this year it will privatize Elf Aquitaine, an oil firm that is France's largest company; Rhone-Poulenc, a chemical company; and BNP, one of France's largest banks. In anticipation of the sale, the government issued special bonds ("Balladur bonds") that are convertible into shares of public enterprises when they are actually privatized. Proceeds from sale of these bonds will be used to finance a number of additional measures designed to stimulate growth.

Legislation granting independence to the Bank of France was approved recently by the French National Assembly and Senate. However, on August 4, the French constitutional court ruled that this legislation was not consistent with the clause in the French constitution giving the government responsibility for economic policy. The government responded that this setback was not serious because the necessary amendment to the constitution was contained in the Maastricht treaty. It stated that it would resubmit the legislation to the court when the treaty takes effect, probably this fall.

Provisional estimates suggest that real GDP in the United Kingdom increased 1.8 percent (s.a.a.r.) in the second quarter, the same rate of increase as occurred in the first quarter. Expanding manufacturing output appears to have continued to account for much of GDP growth. Unemployment (s.a.) stabilized at a rate of 10.4 percent in June.

In June, consumer prices (n.s.a.) fell 0.1 percent, and the 12-month inflation rate slowed to 1.2 percent. Excluding mortgage interest rates, consumer prices were 2.8 percent above their level of June 1992. Cost increases associated with the depreciation of sterling have been offset by continued moderation in labor costs. In June, input prices were 7.8 percent higher than a year earlier, mainly reflecting depreciation of the pound, compared with a decline of 1.6 percent in June 1992. The underlying rate of inflation in earnings was 3.8 percent in May, down considerably from 6.3 percent in May 1992.

The Maastricht Treaty was finally ratified in the United Kingdom on August 2 after Parliament approved the treaty (with an opt-out from the Social Chapter) in late July and a court challenge was dropped after being rejected in the High Court on July 30. However, Prime Minister Major reiterated that the United Kingdom would not return to the ERM in the near future, even with the new wider bands.

In Italy, economic activity remains weak. First-quarter real GDP fell 0.2 percent (s.a.a.r.) from the fourth quarter, and survey data suggest that second-quarter industrial production (s.a.) declined 0.2 percent from the first quarter. The unemployment rate (n.s.a.) in the second quarter stood at 10.5 percent, up 1.1 percentage point from the rate recorded in the first quarter.

Despite lira depreciation last year and earlier this year, consumer price inflation has remained restrained due largely to the weakness in economic activity. In the year to July, consumer price inflation averaged 4.4 percent (12-month basis), down from the 4.8 percent (Q4/Q4 rate) recorded in 1992.

On July 15, Parliament approved a 12.4 trillion lire (0.8 percent of GDP) supplementary budget reduction package for 1993.

The package was needed to prevent Italy's 1993 budget deficit from mushrooming beyond the target of 150 trillion lire (9.4 percent of GDP). On July 13, the Ciampi government released its outline for the 1994 budget that seeks to cut the projected 1994 budget deficit by 38.5 trillion lire (2.3 percent of GDP).

In Canada, recent indicators are consistent with a moderation of growth in the second quarter from its strong first-quarter performance. The average level of industrial production (s.a.) in April and May edged up 0.3 percent from its first-quarter level. During the same period GDP at factor cost (s.a.) rose 0.5 percent, factory shipments (s.a.) increased 0.7 percent, and retail sales (s.a.) were up 0.8 percent, but new orders (s.a.) dropped 3.3 percent. Relatively high real long-term interest rates may be contributing to continued weakness in the construction sector; housing starts (s.a.) rebounded 7 percent in the second quarter but remained near recession levels.

Slack persists in Canadian labor markets. Total employment (s.a.) grew 0.2 percent in the second quarter from its first-quarter average and 0.2 percent more in July, but the unemployment rate (s.a.) remained above 11 percent. Wage settlements averaged 0.6 percent in the first five months of the year, a record low. Accordingly, price inflation has remained moderate, despite depreciation of the Canadian dollar during the past year. The 12-month change in the targeted CPI excluding food and energy was 1.7 percent in June. The all-items CPI was up 1.6 percent over this period, and wholesale prices rose 2.9 percent.

Economic Situation in Other Countries

There are indications that growth slowed further in the second quarter in Mexico, Argentina, and Brazil. In Korea, however, growth recovered modestly. In China, an economic retrenchment program was instituted in July to help slow an overheated economy. In Taiwan, the infrastructure investment program is being cut by 22 percent. Inflation continued to slow in Mexico, falling to single-digit twelve-month rates in June and July for the first time since 1973, and in Argentina, where the lowest monthly increase in more than a decade was reached in July. Inflation remained very high in Brazil, increased in China, but slowed in Korea. Mexico's trade deficit has begun to narrow in line with slower GDP growth. Argentina's trade balance has shifted into deficit, owing mainly to the ongoing real appreciation of the peso. Brazil's trade surplus widened only slightly in the first half, despite sharply higher imports following the easing of monetary policy late last year. Korea's trade deficit is continuing to narrow, reflecting strong demand from China and Southeast Asian countries for its exports, while Taiwan's trade surplus fell in the face of weak world demand. In Russia, bank notes issued before 1993 have been demonetized.

Individual country notes. In Mexico, business comments and anecdotal evidence suggest that real GDP growth slowed further in the second quarter, reflecting tight fiscal and monetary policies and the inhibiting effect on investment of the growing uncertainty about the fate of the North American Free Trade Agreement in the U.S. Congress. As a result, the cumulative trade deficit through May, at $5.8 billion, was $160 million lower than in the same period last year, the first time since May 1990 that the cumulative trade deficit has been less than a year earlier. In January-May, imports were 7.6 percent higher than a year earlier, while exports were 10.9 percent higher. With large capital inflows from abroad continuing, international reserves rose further in April, reaching $24.5 billion, excluding gold, $5.6 billion more than at the end of 1992.

In June, the CPI was 9.9 percent higher than a year earlier. This was the first time since 1973 that the twelve-month inflation rate (as measured by the CPI) was less than 10 percent. In July, the twelve-month rate of increase fell to 9.7 percent. Interest rates fell further in July, mainly reflecting lower inflation expectations and the sluggish pace of economic activity. Further international reserve gains, only partially sterilized by the Bank of Mexico, also appear to have been a factor. At the auction of August 11, the twenty-eight-day Treasury-bill rate was 13.9 percent, down 186 basis points from the most recent high reached in mid-June.

The peso/dollar exchange rate is continuing to fluctuate in a narrow range. On August 10, it was 3.1095 pesos per dollar, little changed from a year earlier, and 5.25 percent above the lower limit of its band.

In Brazil, judging from anecdotal accounts, economic activity appears to have slowed over the second quarter. Monthly inflation was about 30 percent in July and is expected to remain at that level in August. The 1993 cumulative trade surplus through June was $6.6 billion, only slightly higher than in the same period a year ago. Exports were 15.8 percent higher, due in part to a large increase in shipments to Argentina. Imports were 25.2 percent higher, due to the rapid expansion in internal demand resulting from a loosening of monetary policies beginning in the fourth quarter of 1992.

In July, foreign commercial bank creditors agreed to reduce from $3.2 billion to $2.8 billion the amount of collateral that Brazil is required to provide for the first phase of the Brady-style rescheduling agreement. This reflects a downward revision from $44 billion to $39 billion in the estimated amount of bank loans to be restructured. Brazil hopes to secure an IMF agreement, in part to facilitate conclusion of the rescheduling package, but the continued absence of political support for fiscal and monetary reforms makes it unlikely that Brazil will qualify for an IMF program by November, the deadline for implementing the first phase of the rescheduling. As a result, the future of the package remains in doubt.

In Argentina, manufacturing production is growing more slowly this year than last year. Automobile production continued to expand rapidly during the first half of 1993, due to strong domestic demand and higher exports to Brazil. However, in other manufacturing industries, output has been dampened by real exchange rate appreciation and was only 1 percent higher in January-April than a year earlier. In July, consumer prices rose by 0.3 percent, the lowest monthly increase in more than a decade, and were 10.7 percent higher than a year earlier. This compares with an 18.6 percent increase over the twelve months ending in July 1992.

Merchandise imports during the first five months of 1993 were 8.4 percent higher than a year earlier, while merchandise exports were 7.1 percent higher. This resulted in a $71 million trade deficit over this period, compared with a tiny surplus during the same period last year. International reserves, excluding gold, have remained steady at around $10 billion during the first half of 1993.

In July, China began concerted efforts to slow its economy, as signs of overheating continued. In the first half of 1993, GDP was 13.9 percent higher than in the same period in 1992, led by fixed investment expenditures (including construction). In June, the urban cost-of-living index was 21.6 percent higher than a year earlier. This was the largest rise since before the last economic retrenchment in China, in 1988-89. The new stabilization efforts began in early July with the naming of Zhu Rongji, China's economics czar, as head of the central bank. This was followed by measures principally aimed at slowing credit growth at local levels, where state banks and non-bank financial institutions have channeled much of their loans to speculative real estate and stock market ventures, neglecting infrastructure projects. Interest rates were raised for the second time in two months on July 11, but nominal rates continue to lag current inflation. In mid-July, a forced sale of Treasury bonds to urban workers was needed to place the full amount on offer. , the yuan strengthened in the Shanghai swap market in late July. It stood at 8.766 yuan per dollar on August 10, about 20 percent above its July 23 all-time low. A black market premium on foreign exchange continues to exist.

In Taiwan, real GDP was 6.1 percent higher in the first quarter than a year earlier, after recording a 6.3 percent increase in the fourth quarter of 1992 compared with a year earlier. The somewhat slower growth reflected weaker world demand for Taiwan's exports.

The 1993 cumulative trade surplus through July was $4 billion, $1.4 billion less than in the same period of 1992. Exports were 5.1 percent higher in value terms, down from a 7.5 percent growth in all of 1992, while imports were 9.2 percent higher, down from a 14.5 percent rise in all of 1992. The current account surplus fell to $1.7 billion in the first quarter from $2.4 billion a year earlier.

Price pressures remain moderate. Consumer prices were 3.2 percent higher in July than in July 1992.

The government announced in July that it would cut the size of Taiwan's ambitious $310 billion infrastructure program by about 22 percent. The program, which was launched in 1991, was scheduled originally to be completed by mid-1997.

In Korea, real GNP was 4.5 percent higher in the second quarter than in the same period of 1992. This was a modest recovery from the low of 2.8 percent recorded in the fourth quarter of 1992, compared with a year earlier. But it was still less than half the average annual growth rate of the past ten years. Domestic demand appears to have picked up in response to a lowering of interest rates in the first quarter and the removal of some restrictions on construction activity. Strong export growth, mainly to China and Southeast Asian countries, also contributed to the improved GNP performance. Exports were 6.6 percent higher in the first half than in the same period of 1992. This export growth and a 1.5 percent contraction in imports produced a narrowing of the current account deficit to $1 billion in the first half from $4.5 billion in the same period last year. However, a major labor dispute at the Hyundai Group dampened exports in June and resulted in a nearly $600 million current account deficit for that month.

Consistent with the relatively slow economic activity (by historical standards), price pressures have continued to ease. The CPI was 4.3 percent higher in July than a year earlier, after a rise of 6.6 percent in the twelve months ending in July 1992.

On June 29, the Korean government released a detailed summary of the third (and final) stage of its blueprint for financial reform. The "third stage blueprint" contains a comprehensive plan to deregulate by 1997 virtually all interest rates except on demand deposits. It also calls for additional liberalization of foreign exchange market transactions and reduced restrictions on capital flows, seeks to curtail the use of policy loans, and proposes to reform substantially the conduct of monetary policy by shifting toward a primary reliance on such traditional instruments as open market operations rather than direct credit controls.

Hong Kong's foreign exchange holdings were published in July for only the second time since a longstanding policy of secrecy was reversed a year ago. They totaled $35.2 billion at the end of 1992, up $6 billion from the end of 1991.

On July 24, a Saturday, the Central Bank of Russia announced that all ruble bank notes issued before 1993 were no longer legal tender effective the following Monday. Individuals were given two weeks to exchange up to 35,000 rubles in pre-1993 currency (about $35 at the official exchange rate) for new bills. Amounts in excess of this amount were to be deposited in six-month saving deposits. The action, which was announced while President Yeltsin and Finance Minister Federov were away from Moscow, was criticized from all sides and, on July 26, President Yeltsin issued a decree that raised the conversion limit to 100,000 rubles ($100) per person and extended the conversion period till the end of August.

This action will have little direct impact in Russia because the 100,000 ruble limit on individual conversions is not expected to be binding on most Russians. Nonetheless, the currency reform has undermined the credibility of Russian policymakers.

After the Russian central bank announcement, both Georgia and Azerbaijan declared that the Russian ruble was no longer legal tender. However, the ruble had already largely been replaced in those countries by local substitute currencies. Pre-1993 rubles will continue to circulate in the seven other former-Soviet-Union states that are still in the ruble zone until they can be replaced, probably through the introduction of new national currencies.