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[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

[2] A two-step process was used. An advanced optimal character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

Confidential (FR) Class III FOMC

June 28, 1995

RECENT DEVELOPMENTS

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

DOMESTIC NONFINANCIAL DEVELOPMENTS

Economic activity will likely decline a bit this quarter, primarily reflecting a slowing in homebuilding and an inventory correction centered in the motor vehicle industry. Consumer spending has remained sluggish, and growth in business fixed investment appears to be moderating from the very rapid pace of recent quarters. There are indications that consumer and producer price inflation may be slowing, after picking up earlier this year.

Labor Market Developments

Recent data indicate a substantial weakening in labor demand. Most notably, nonfarm payroll employment fell 101,000 in May, after posting a slight decline in April.[1] As noted in the last Greenbook, the Board staff and the BLS believe that the April data were depressed somewhat by seasonal adjustment problems associated with the timing of the survey week. However, even adjusting for this problem, employment gains in April were small. And, while we are skeptical that the May decline in payrolls is a good representation of trends in the labor market, apart from some minor weather-related disruptions in construction, we can identify no major special factors affecting the data for that month.

The deterioration in the labor market has been especially marked in the goods-producing sector. Manufacturing payrolls dropped 81,000 over the past two months; employment in nearly every major industrial category declined, on net, over the April-May period. In addition, the factory workweek fell from an average of

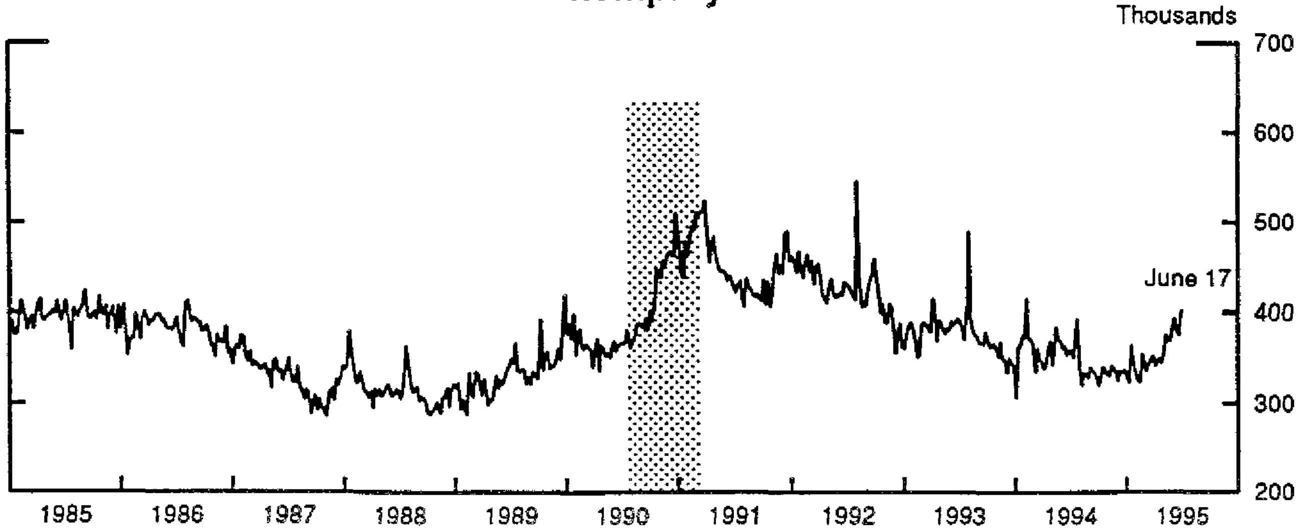
1. The BLS also revised previous data to reflect the 1994 benchmark to unemployment insurance tax records (ES-202 program). These revisions raised the level of nonfarm employment by 789,000 in March 1994 (the benchmark month). At the same time, however, BLS lowered their estimates of employment growth by roughly 25,000 per month after March 1994 to reflect more recent information available from the ES-202 program. As a result, the level of employment was 486,000 higher as of February 1995.

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

	1993	1994	1994 Q3	1994 Q4	1995 Q1	1995 Mar.	1995 Apr.	1995 May
	-----------Average monthly changes[1]-----------							
Nonfarm payroll employment[2]	235	294	273	287	226	179	-7	-101
Private	215	273	238	283	216	172	-6	-79
Strike-adjusted	215	274	246	277	216	172	-7	-79
Manufacturing	4	30	19	39	18	2	-25	-56
Durable	3	25	18	31	20	11	-4	-29
Nondurable	0	5	1	8	-2	-9	-21	-27
Construction	24	30	24	30	30	43	-19	-57
Trade	57	75	69	81	20	-22	17	-17
Finance, insurance, real estate	19	4	-1	-4	2	9	-19	-3
Services	100	117	116	115	130	120	35	60
Personnel supply services	26	27	24	22	4	-28	-27	5
Total government	20	21	35	4	10	7	-1	-22
Private nonfarm production workers	194	242	205	243	194	187	-50	-35
Manufacturing production workers	10	31	21	38	16	-1	-13	-43
Civilian labor force	119	236	251	145	262	203	226	-926
Total employment[3]	209	326	336	309	235	149	-202	-753
Nonagricultural	219	289	297	268	179	107	-98	-516
Unemployment	-90	-90	-85	-164	27	54	428	-173
	-----------------Levels-----------------							
Labor force participation rate	66.2	66.6	66.5	66.6	66.9	66.9	67.0	66.5
Unemployment rate	6.8	6.1	6.0	5.6	5.5	5.5	5.8	5.7
Average workweek (hours)[2]	34.5	34.7	34.7	34.7	34.7	34.6	34.6	34.3
Manufacturing (hours)	41.5	42.0	42.0	42.1	42.1	42.0	41.5	41.5
Manufacturing overtime (hours)	4.2	4.7	4.7	4.8	4.8	4.7	4.5	4.3
Memo:								
Aggregate hours of private production workers (percent change)	0.3	0.4	0.3	0.3	0.1	0.1	0.2	-1.1

1. From final month of preceding period to final month of period indicated.
2. Survey of establishments.
3. Survey of households. Data after 1993 are not directly comparable with earlier years because of a redesign of the CPS in January 1994.

Initial Claims for Unemployment Insurance



Note. Includes EUC adjustment.

42.1 hours per week in the first quarter to 41.5 hours per week in April and May. Most of this decline appears to reflect reductions in the use of overtime hours, which fell from 4.8 hours in the first quarter to 4.3 hours in May. Employment also declined in the construction industry in April and May. The BLS indicated that some of the dropback in construction jobs can be attributed to heavy rains and floods in the South during the May survey week.

In the service-producing sector, overall employment has continued to rise in recent months, but the pace of hiring has slowed. In the services industry, payrolls rose by an average of 47,000 in April and May, well below the average pace of growth during the first quarter. Business services posted no gain over the latest two months, as a downturn in employment at temporary help agencies offset small gains elsewhere; meanwhile, net hiring in the health care industry slowed to about half its first-quarter pace. Employment in wholesale and retail trade was unchanged, on balance, in April and May, while the number of jobs in finance, insurance, and real estate fell.[2]

The combination of the decline in employment and a shortening of the average workweek in most sectors left the level of aggregate hours of production or nonsupervisory workers thus far this quarter 1 percent below the first-quarter average. Even if June shows a sizable increase in aggregate hours, as seems likely, aggregate

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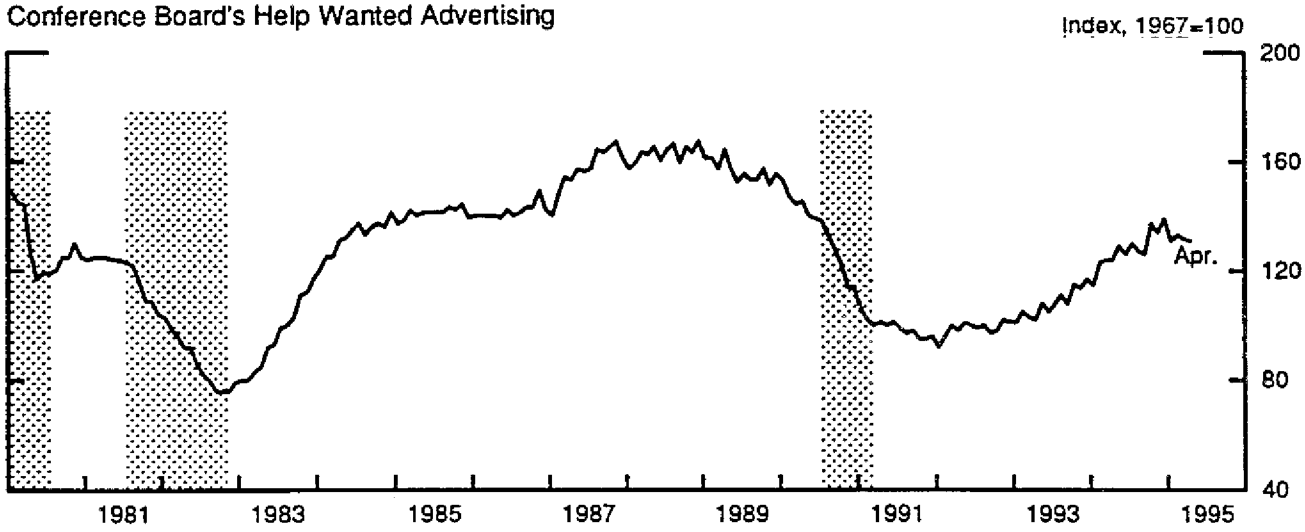
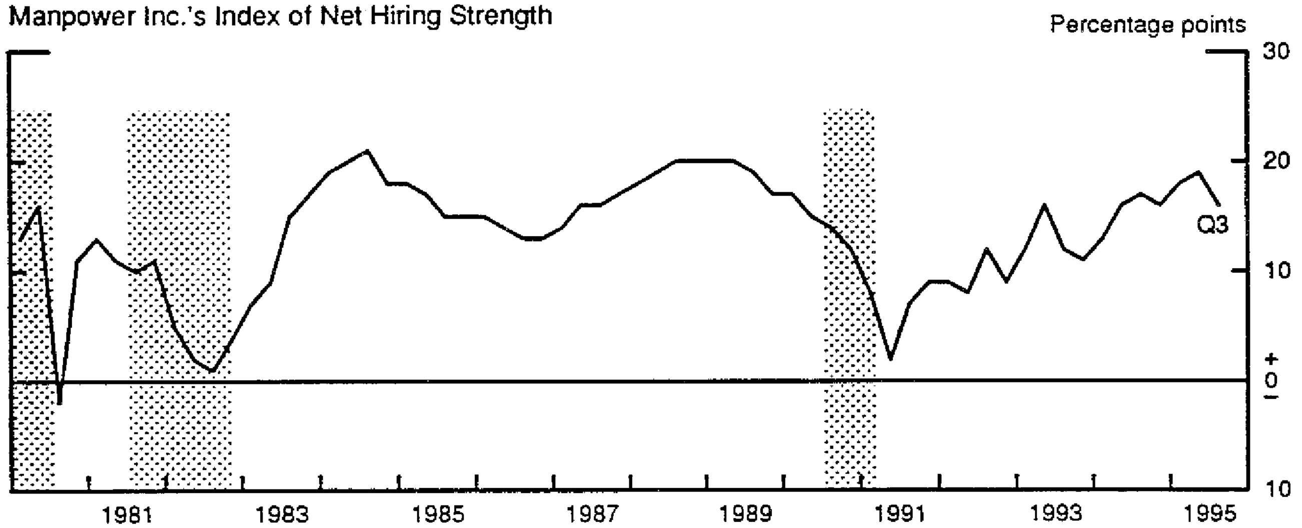
2. The federally funded summer jobs program, which was targeted for cuts in the House version of the rescissions bill earlier this year, appears to be proceeding normally. The final version of the rescissions package, which contained cuts in summer jobs only for future years, was vetoed by President Clinton. As a result, we expect the program to fund about 600,000 youth jobs this summer, about the same as in 1994.

Surveys of Labor Demand

Conference Board's Help Wanted Advertising



Manpower Inc.'s Index of Net Hiring Strength

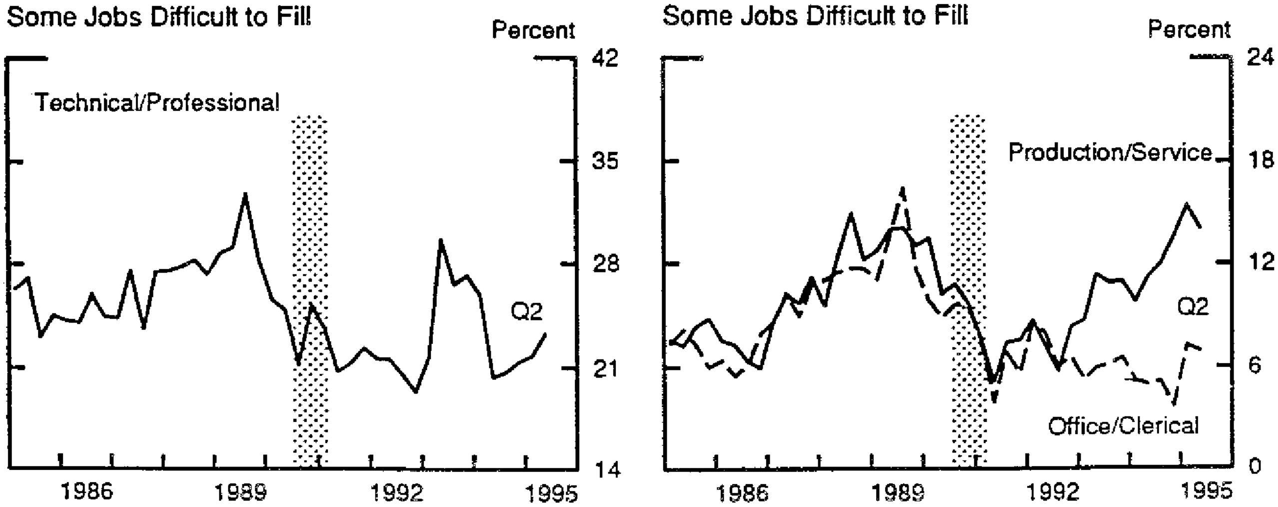


Note. Percentage of firms planning an increase minus percentage planning a decrease.

Bureau of National Affairs' Survey of Personnel Executives

Some Jobs Difficult to Fill

Some Jobs Difficult to Fill



Note. Seasonally adjusted by FRB.

hours for the second quarter as a whole will probably show a decline.[3]

Data from the household survey also indicate a weakening in labor demand. The unusually sharp declines in household employment in April and May--which totaled nearly 1 million--most likely reflect seasonal adjustment problems associated with the timing of survey weeks and the end of the school year. Such problems often afflict the household data at this time of year, and we would not be surprised to see at least a partial offset in the June or July data.[4] Nonetheless, the unemployment rate--which is less affected by these timing issues--has moved up in recent months, to around 5-3/4 percent. Increased joblessness among teenagers has accounted for part of the rise in the overall unemployment rate. However, jobless rates for adult men and adult women also have increased.

Other labor market data also suggest that growth in labor demand has slowed, but the weakness implied by these series is not so profound as the drop in the employment numbers would suggest. Initial claims for unemployment insurance have moved up in recent weeks to the 400,000 range, but even that level of claims has historically been consistent with no change or a small increase in payroll employment rather than an outright decline. Moreover, the decline in the Conference Board's index of help-wanted advertising--about 5 index points from its peak in December--left the series in April at a level about equal to that in the second half of last

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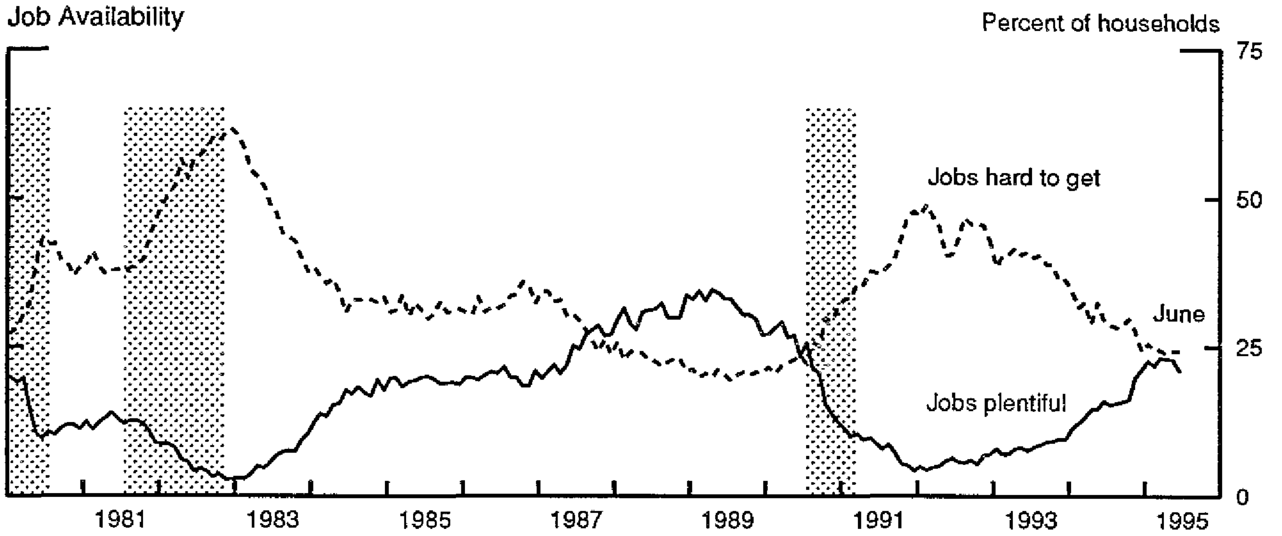
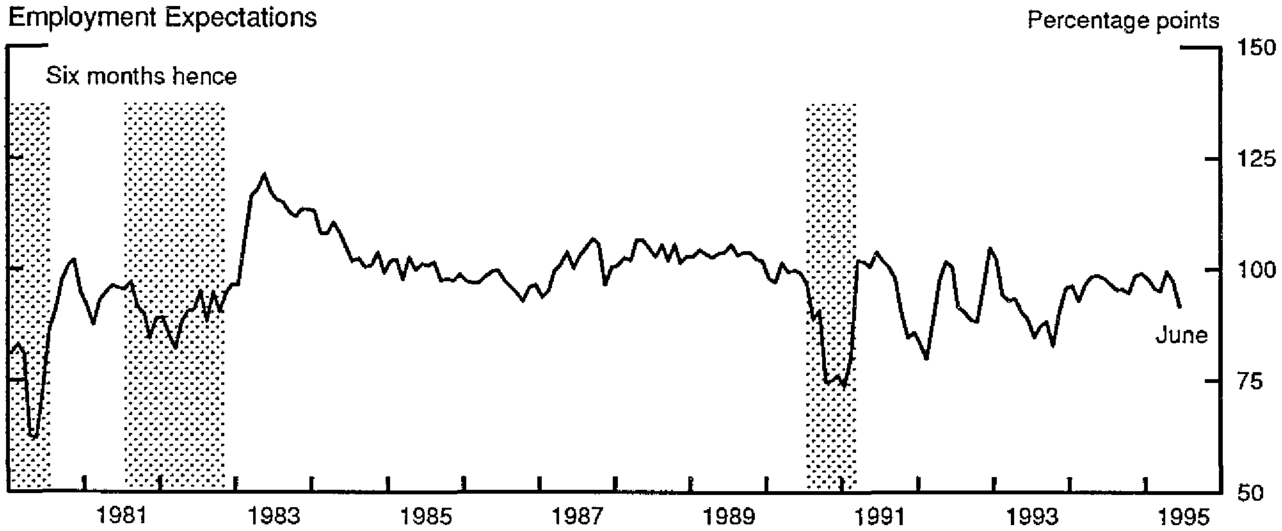
3. Payroll employment in June may be artificially boosted by the same type of seasonal adjustment problem that depressed the April data. Because the May and June survey periods were separated by five weeks this year instead of the usual four, the reported June employment change could be elevated by about 100,000 jobs.

4. The difficulty is caused by the large numbers of seasonal workers who enter the labor force following the end of the school year. This year, the May survey week was early in the month, and it is likely that many college students were still in school, leading to underestimates of both employment and the labor force.

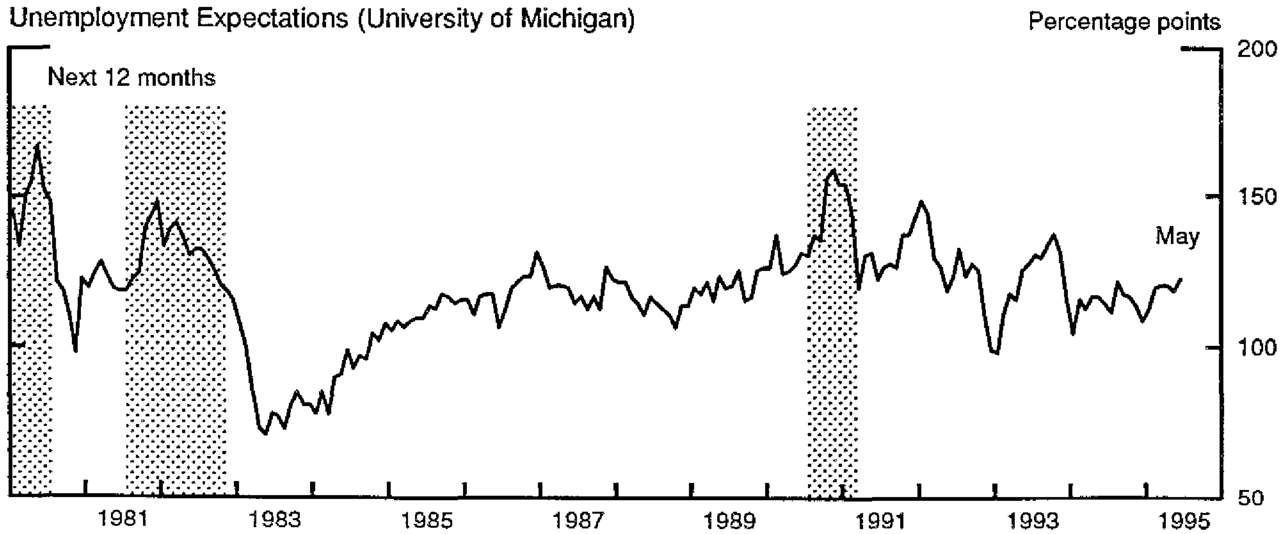
Consumer Surveys of Labor Market Conditions

Conference Board Survey except as noted





Note. Percentage of households responding "more jobs" minus percentage responding "fewer jobs" plus 100.



Note. Percentage expecting "more" minus percentage expecting "less" plus 100.

year. Similarly, the most recent reading from the Manpower index of net hiring strength--which refers to employers' hiring plans in the third quarter--showed a decline that about offset the increases posted in the previous two quarters. Finally, the Bureau of National Affairs' survey of personnel executives indicated that employers continued to have some difficulty in the second quarter in filling production/service and technical/professional jobs; however, the survey also reported that fewer employers are planning workforce expansions in the third quarter than in recent quarters.

Despite the generally negative tone of the recent labor market indicators, workers have remained relatively upbeat about job prospects. The Conference Board's June indexes on current job availability indicated that roughly a quarter of the respondents believed that jobs were hard to get, a bit greater than the fraction reporting that jobs were plentiful. Although the balance deteriorated slightly from readings earlier this year, those readings had been the most favorable since 1990. With regard to future job prospects, recent readings from both the Conference Board's employment expectations index and the Michigan Survey's index of unemployment expectations have generally held in the range seen over the past couple of years.

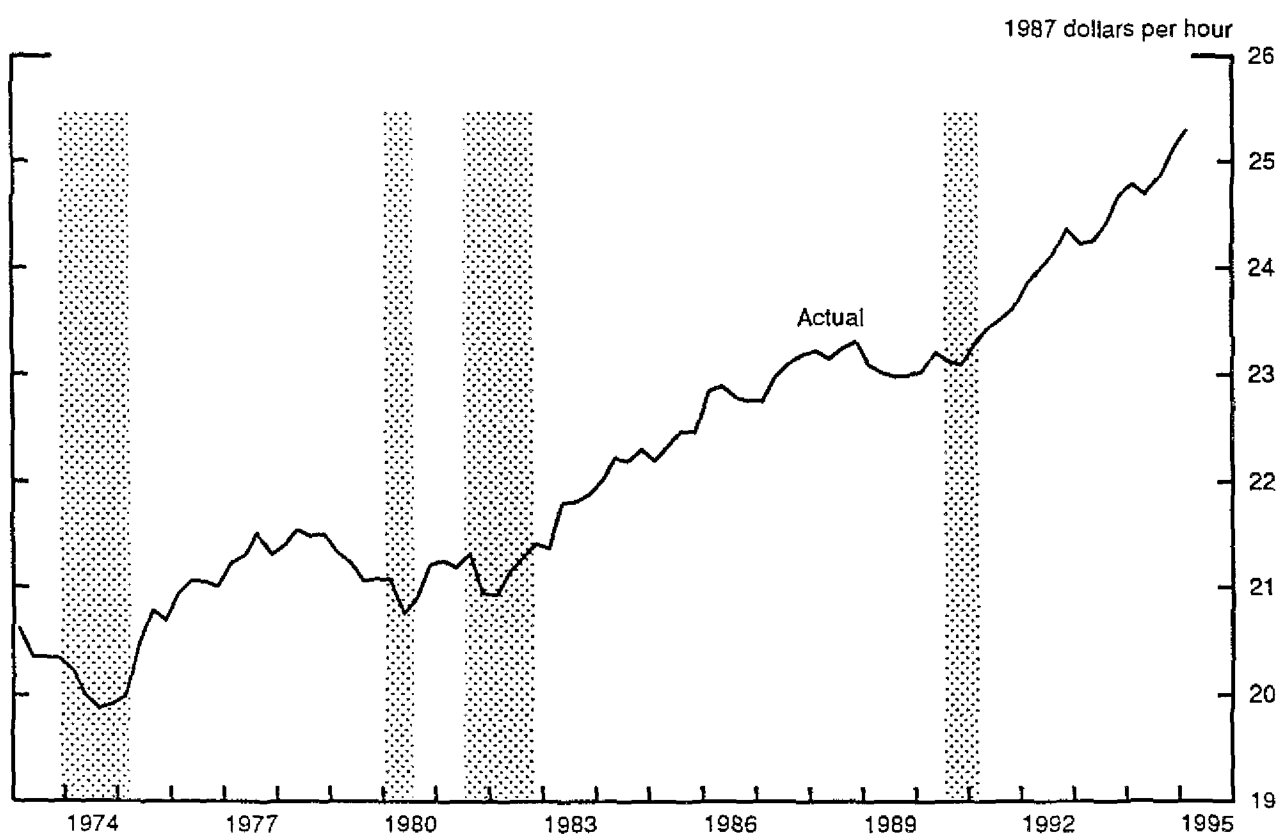
Output per hour in the nonfarm business sector rose 2.7 percent in the first quarter, bringing the growth in labor productivity over the past year to 2.0 percent. Part of the recent surge in productivity--which seems somewhat surprising in light of the deceleration in GDP--results from the fact that the income-based

LABOR PRODUCTIVITY
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

	1993[1]	1994[1]	1994 Q2	1994 Q3	1994 Q4	1995 Q1	1994:Q1 to 1995:Q1
Output per hour							
Total business	1.4	2.0	-1.4	3.2	4.3	2.2	2.1
Nonfarm business	1.3	1.8	-1.4	2.7	4.3	2.7	2.0
Manufacturing	2.6	4.2	4.3	3.4	3.7	3.4	3.7
Nonfinancial corporations[2]	2.3	1.6	-.8	1.6	3.4	1.8	1.5

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, finance and insurance companies; the sector accounts for about two-thirds of business employment.

Nonfarm Business Sector Productivity



measure of output used by BLS to calculate productivity has been rising faster than the product-based measure.[5]

Industrial Production

Industrial production slid another 0.2 percent in May and has declined nearly 1.0 percent from its peak in February. Weekly production data received so far in June (covering about 17 percent of total IP) indicate further weakening in IP this month. Manufacturing output registered its fourth consecutive decline in May as the production of motor vehicles and parts moved down sharply and production in most other industries remained sluggish. The factory operating rate fell to 83.0 percent in May, 2.2 percentage points below its beginning-of-year high but still 1.7 percentage points above the 1967-94 average.

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

	1995					
	Apr.	May	June	Q1	Q2	Q3
			Planned		--Planned--	
U.S. production	12.1	11.5	11.9	12.9	11.8	12.1
Autos	6.5	6.1	6.2	7.1	6.3	6.3
Trucks	5.6	5.4	5.7	5.7	5.6	5.9
Days' supply						
Autos	84.4	74.4		72.3		
Light Trucks	73.6	68.4		62.9		

Note. Components may not sum to totals because of rounding.

The output of motor vehicles and parts dropped 8.0 percent from March to May, directly accounting for about one-half of the decline in total IP over that two-month period; perhaps another quarter of

5. This divergence is reflected as a sharp decline in the value of the statistical discrepancy in the national income and product accounts--from $25.5 billion in the first quarter of 1993 to -$60.4 billion in the first quarter of 1995. BLS plans to convert its productivity series to a product-side concept (by adding the statistical discrepancy) in late 1995 or early 1996.

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

	Proportion in total IP 1994:Q4	1994 Q4	1995 Q1	1995 Mar.	1995 Apr.	1995 May
		-Annual rate-		----Monthly rate----		
Total index	100.0	5.9	5.0	-.2	-.5	-.2
Previous		5.9	4.6	-.3	-.4	
Total index excluding motor vehicles and parts	94.3	5.1	4.6	-.1	-.3	.0
Major Market Groups:						
Products, total	60.1	4.5	4.4	-.3	-.6	-.2
Consumer goods	27.5	2.8	4.5	-.8	-.8	-.2
Durable	5.8	6.4	6.6	-1.8	-1.9	-2.1
Excluding autos and trucks	3.9	.5	.9	-1.6	-.4	-.3
Nondurable	21.7	1.8	3.9	-.5	-.5	.3
Intermediate products	14.2	5.7	1.7	-.2	-1.0	-.3
Construction supplies	5.5	8.1	3.1	-.5	-1.3	-.6
Business supplies	8.8	4.3	.8	.0	-.8	-.1
Equipment	18.4	6.2	6.4	.4	-.1	.0
Business equipment	15.2	8.6	8.3	.7	-.2	.1
Excluding autos and trucks	13.9	7.7	7.7	.9	.3	.5
Defense and space equipment	2.4	-2.8	-4.7	-.2	-.4	-1.1
Materials	39.9	8.1	6.1	.0	-.4	-.3
Durable	22.4	12.6	8.8	.1	-.3	-.2
Nondurable	8.8	6.9	1.2	-.2	-1.0	-.4
Energy	8.7	-1.7	4.1	-.1	.0	-.4
Major Industry Groups:						
Manufacturing	86.8	7.7	5.0	-.1	-.6	-.3
Manufacturing excluding motor vehicles and parts	81.1	6.9	4.4	.0	-.4	.0
Motor vehicles and parts	5.7	20.6	12.9	-1.4	-4.3	-3.9
Mining	6.1	-3.4	4.1	-.7	-.2	-1.0
Utilities	7.2	-6.0	7.0	-.1	.5	.6

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

	1988-89 High	1967-94 Avg.	1994 Q4	1995 Q1	1995 Feb.	1995 Mar.	1995 Apr.	1995 May
Total industry	84.9	82.0	84.9	85.2	85.3	84.9	84.2	83.7
Manufacturing	85.2	81.3	84.5	84.7	84.7	84.3	83.5	83.0
Primary processing	89.0	82.5	89.5	89.6	89.4	89.1	88.4	87.9
Advanced processing	83.5	80.7	82.5	82.8	82.8	82.4	81.5	81.0

the decline can be traced to indirect effects of motor vehicle production on related industries. Though the makers' schedules call for some increase in motor vehicle assemblies in June, the weekly output data suggest that production in June will remain roughly unchanged at May levels.

Industrial production excluding motor vehicles and parts was essentially unchanged in May, after declining 0.3 percent in April. Production of consumer goods fell 0.2 percent in May as an increase in the production of nondurables, such as chemical and paper products, offset some of the auto-related decline in the production of durables. Output of other durable consumer goods, which sank 4.5 percent between January and April, edged down another 0.2 percent in May. Production of construction supplies fell 0.6 percent in May, for a total drop of 3.4 percent since January. Production of business equipment edged up a bit in May after falling 0.2 percent in April.

Downturns in IP of the dimension recently experienced have often occurred in the midst of continuing expansions; but, of course, they have also been the early phase of a recession or a precursor of a near-term cyclical downswing. The historical relationship between declines in manufacturing output and recessions suggests that, given the 1.2 percent reduction in manufacturing IP between January and May, there is a roughly 44 percent chance that the economy will be in recession as of November (table).[6]

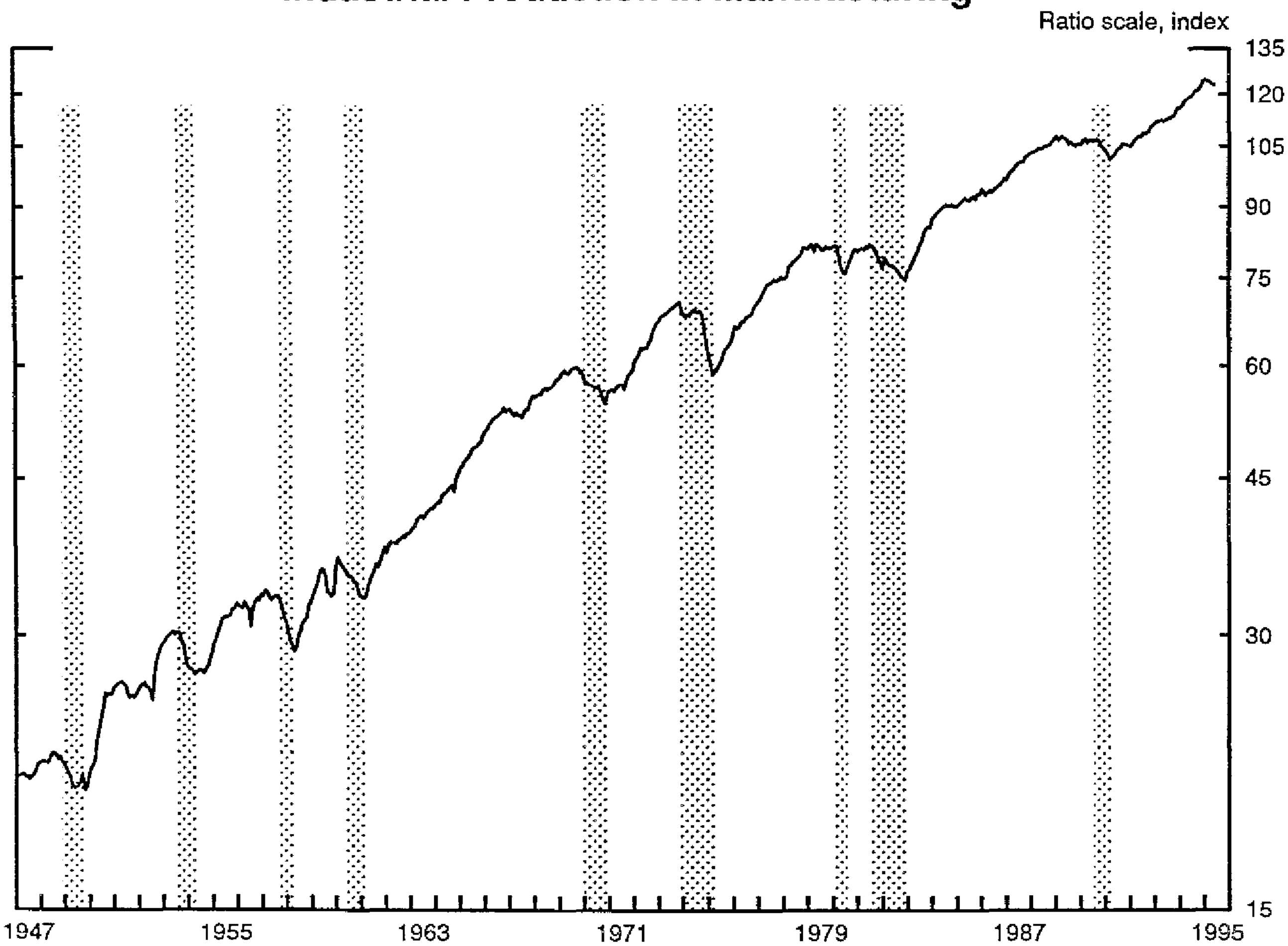
6. The table groups months from January 1947 to June 1994 by the magnitude of the percent change in manufacturing output over the preceding four-month period. In order to examine the relationship between output declines and the probability of <u>entering</u> a recession, the analysis excludes output changes that occur in the midst of a recession. Recession months are defined as months on or after a business cycle peak and on or before the subsequent business cycle trough. Peaks and troughs are dated by the National Bureau of Economic Research.

INDUSTRIAL PRODUCTION AS AN INDICATOR OF RECESSIONS

Four-month percentage change in factory output	Number of months	Percent of months leading into a recession[1]
Above 2	215	7
1 to 2	99	14
0 to 1	75	31
-1 to 0	35	40
-2 to -1	16	44
Below -2	25	68

Note. Analysis based on manufacturing IP, 1947-1994.
1. To be counted in the last column as an episode "leading into recession," the economy must be in a recession at the end of the four-month change in IP or within the subsequent six months.

Industrial Production in Manufacturing



Motor Vehicles

Sales of new light vehicles rebounded in May to a 14.8 million unit annual rate from the 13.3 million unit rate in April (FRB seasonals). Sales of foreign autos spurted to 2.1 million units at an annual rate.

Last month's increase in sales of domestic vehicles reflects, at least in part, the broadening and deepening of incentives that were introduced earlier in response to the weaker-than-expected first-quarter demand. Even with the increase in incentives, sales plunged in April, and despite the rebound in May, purchases so far this quarter are running well below the pace of the first quarter. Much of this decline reflects weakness in sales to consumers (including leases). Fleet sales in April were also low, with most of the decrease attributable to a planned shift in the timing of sales from April to December of last year; in May, fleet sales returned to more normal levels. (Information on retail and fleet sales is based on confidential data from industry sources.)

Consumption and Personal Income

The data received since the last Greenbook indicate that real consumer spending has remained sluggish. Nominal retail sales increased only 0.2 percent in May, to a level essentially unchanged from the first-quarter average. Retail sales have been held back this quarter by a contraction in spending at building material stores and by the April dip in sales at automotive dealers. In the retail control category, nominal spending grew 0.4 percent in May. Among the components of retail control, sales of apparel and furniture and appliances revived a bit in May after persistent weakness in both categories for much of 1995. The retail sales data, in combination with the latest reports on consumer prices and on unit sales of motor vehicles, suggest that real spending for

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

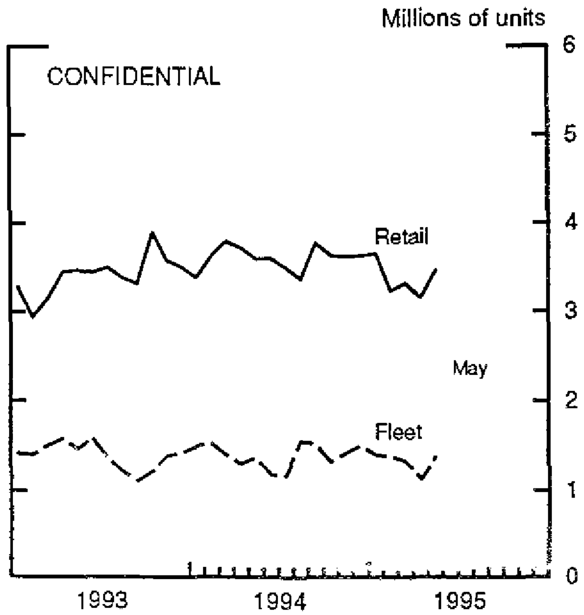
	1993	1994	1994 Q3	1994 Q4	1995 Q1	1995 Mar.	1995 Apr.	1995 May
Total	13.9	15.0	15.1	15.3	14.9	15.0	13.3	14.8
(BEA seasonals)	13.9	15.0	14.6	15.4	14.9	15.1	13.8	14.5
Autos	8.7	9.2	9.3	9.2	8.9	9.0	7.9	9.0
Light trucks	5.2	5.8	5.8	6.1	6.0	6.1	5.3	5.8
North American[2]	11.7	12.9	12.8	13.2	12.9	13.0	11.5	12.7
Autos	6.7	7.3	7.2	7.3	7.1	7.2	6.3	7.1
Big Three	5.5	5.7	5.6	5.8	5.6	5.5	4.9	5.5
Transplants	1.3	1.5	1.6	1.6	1.5	1.7	1.4	1.6
Light trucks	5.0	5.7	5.6	5.9	5.8	5.9	5.2	5.6
Foreign produced	2.1	2.1	2.2	2.0	2.0	2.0	1.8	2.1
Autos	2.0	2.0	2.0	1.8	1.8	1.8	1.6	2.0
Light trucks	.2	.2	.2	.2	.2	.2	.2	.2
Memo: Domestic name-plate market share								
Total	.74	.73	.71	.74	.74	.73	.74	.73
Autos	.65	.63	.61	.64	.63	.62	.63	.62

Note. Data on sales of trucks and imported autos for the most recent month are preliminary and subject to revision.

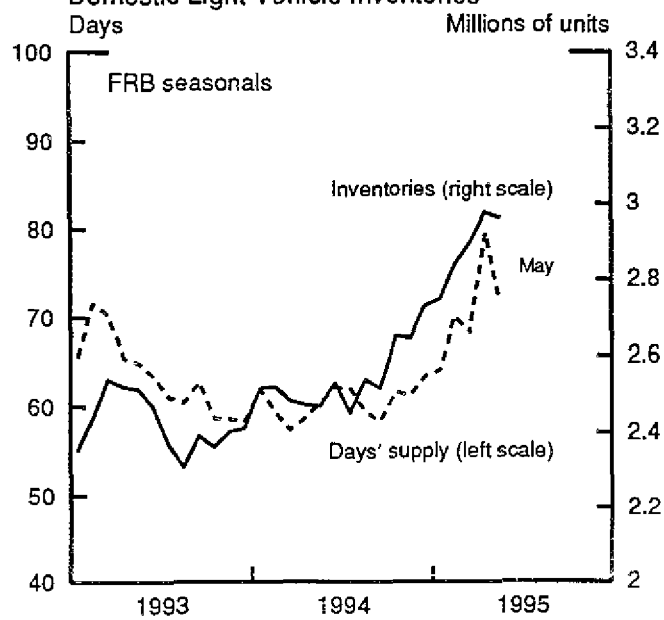
1. Components may not add to totals because of rounding.

2. Excludes some vehicles produced in Canada that are classified as imports by the industry; before January 1994, some vehicles produced in Mexico were also excluded.

GM and Ford Fleet and Retail Auto Sales



Domestic Light Vehicle Inventories



Consumer Spending

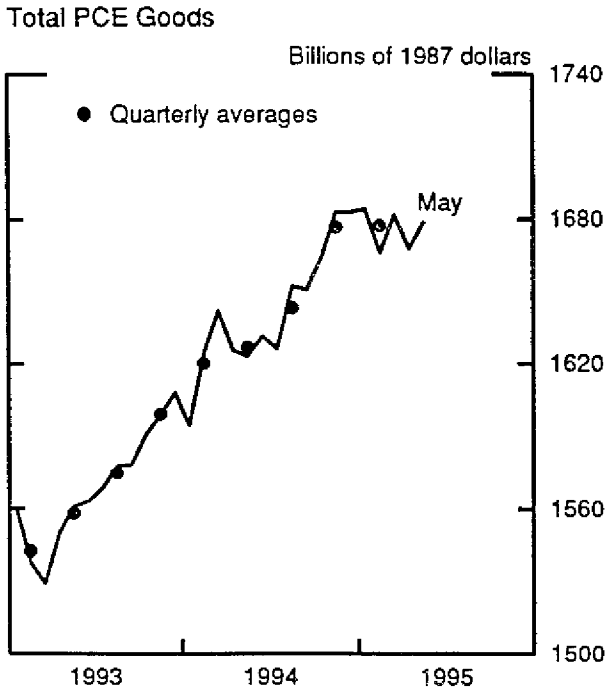
Retail Sales

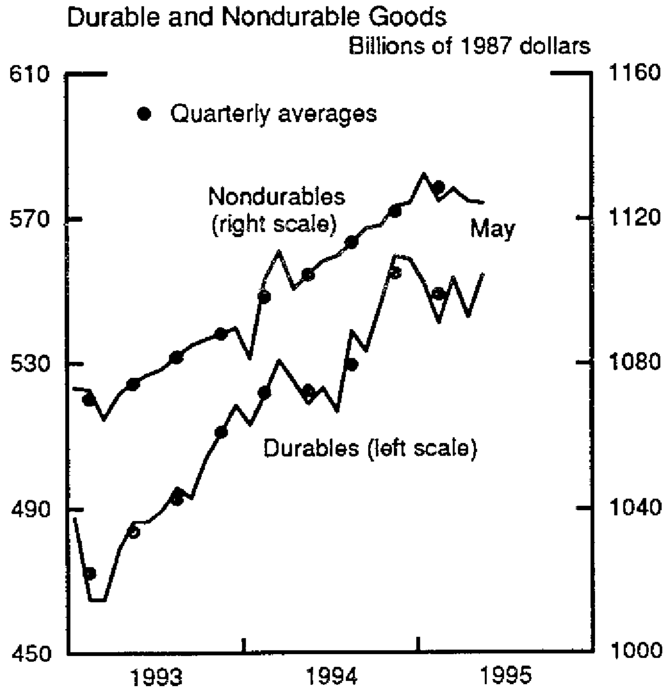
(Percent change from preceding period, seasonally adjusted)

		1994 [1]	1994 Q4 [2]	1995 Q1 [2]	1995 Mar.	1995 Apr.	1995 May
1.	Total sales	1.9	2.4	.4	.7	-.3	.2
2.	*(Previous)*			*(.5)*	*(.8)*	*(-.4)*	
3.	Building materials and supplies	2.2	2.1	-1.3	1.1	-2.3	-1.7
4.	Automotive dealers	3.2	6.0	-.5	1.6	-1.4	.5
5.	Retail control [3]	1.4	1.3	.9	.4	.2	.4
6.	*(Previous)*			*(1.0)*	*(.6)*	*(.3)*	
7.	Nondurables	1.2	1.1	1.0	.4	.1	.2
8.	Apparel	.7	1.8	-1.1	1.9	-4.2	1.5
9.	Durables	2.8	2.3	.0	.0	.6	.3
10.	Furn. & appliances	3.7	5.3	-.6	-.6	-1.2	1.4
MEMO:							
11.	Sales of light vehicles [4]	15.1	15.4	14.9	15.1	13.8	14.5

1 Average quarterly growth rate over the year.
2. Percent change of quarterly averages.
3. Total excluding auto dealers and building material and supply stores, except auto and home supply stores.
4. Millions of units, annual rate; BEA seasonals.

Real PCE Goods

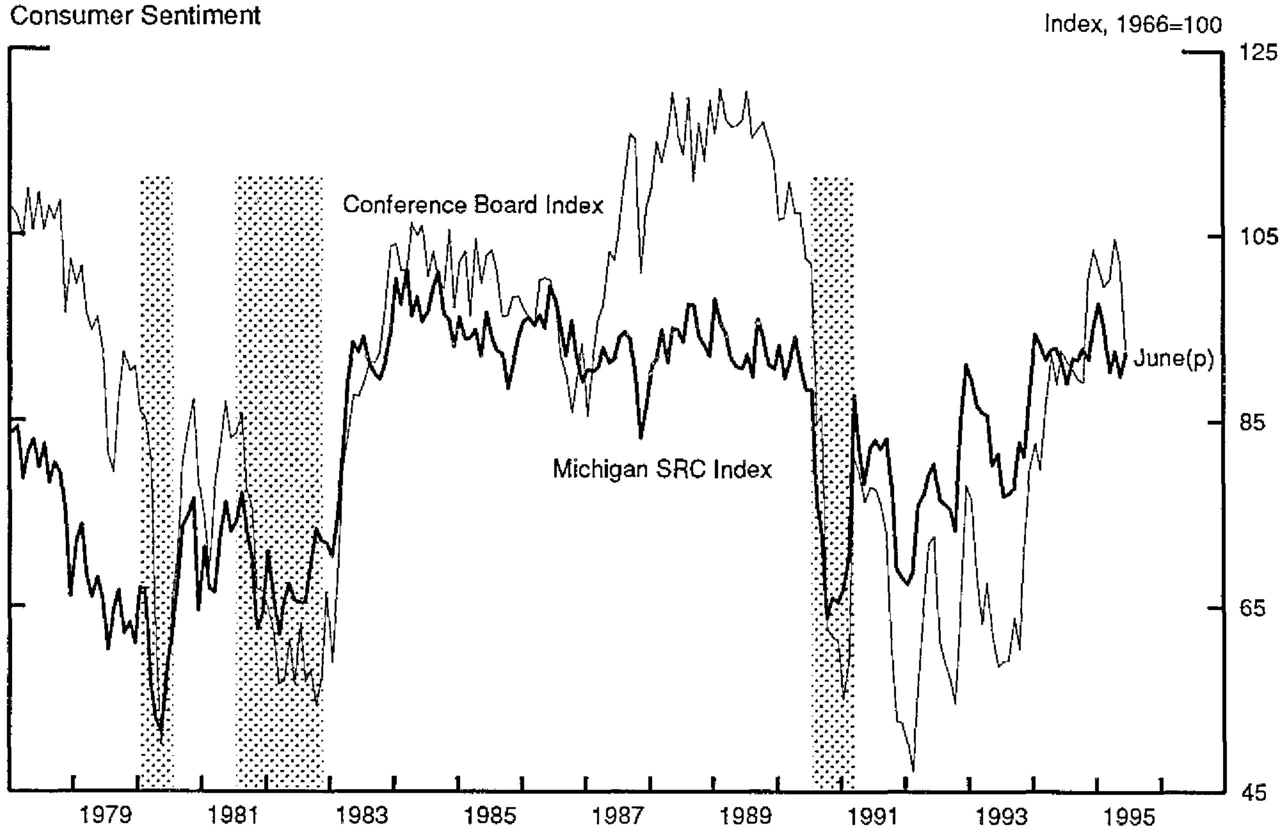




Note. March, April, and May are staff estimates.

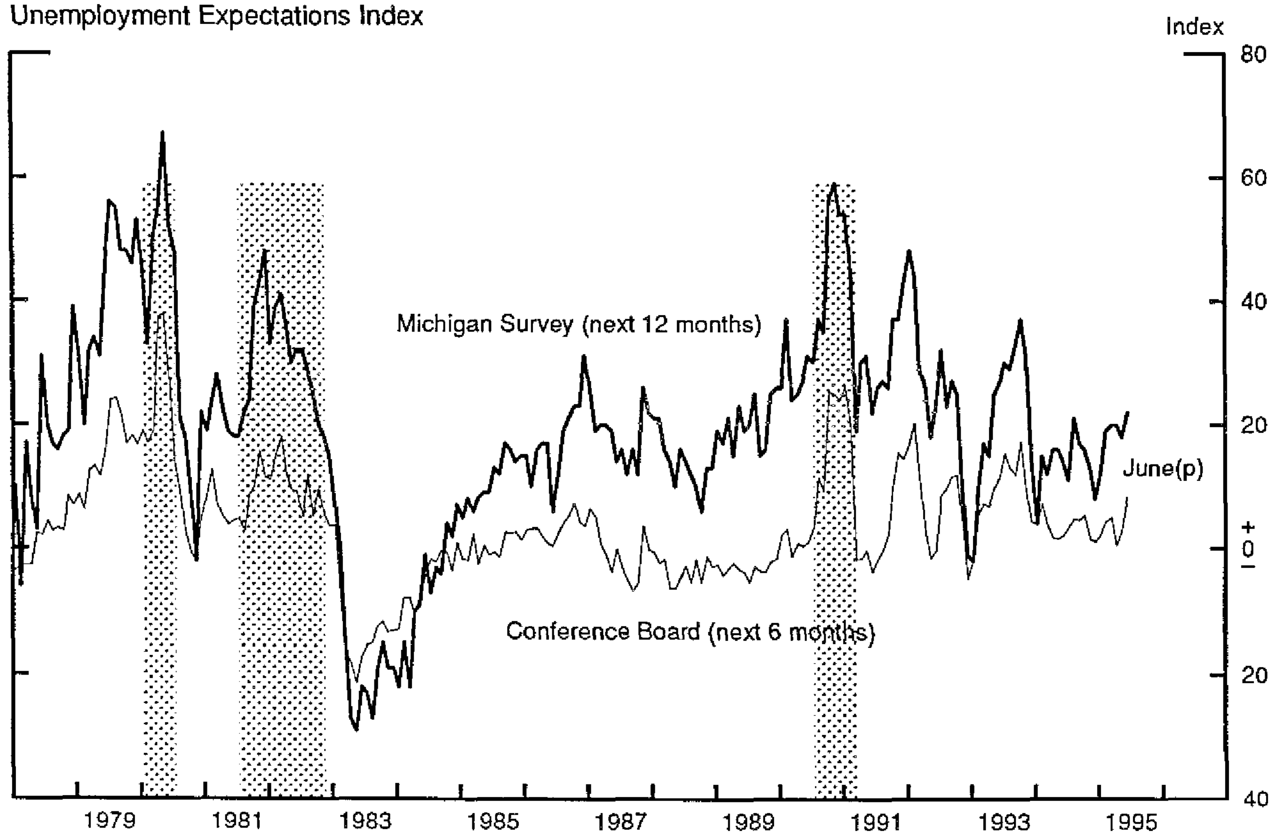
Consumer Surveys

Consumer Sentiment



p = Preliminary.

Unemployment Expectations Index



p = Preliminary.

Note. The unemployment expectations index is defined as the proportion of households that believe unemployment will rise in the near term, minus the proportion who believe unemployment will fall.

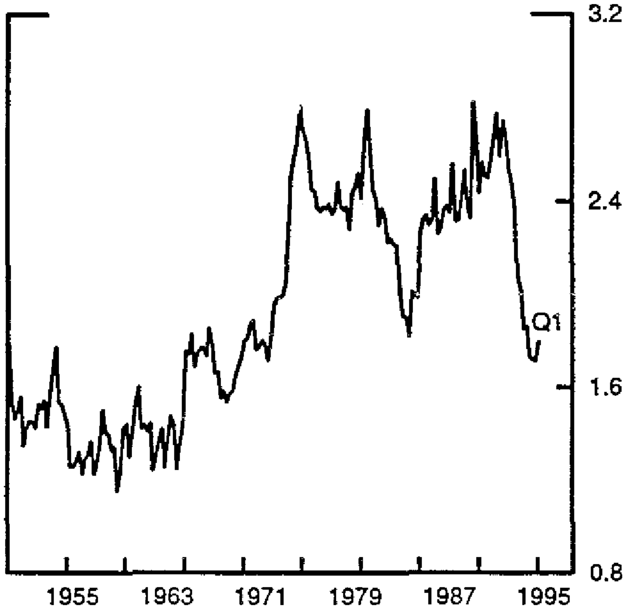
goods has been essentially constant since the fourth quarter of last year.

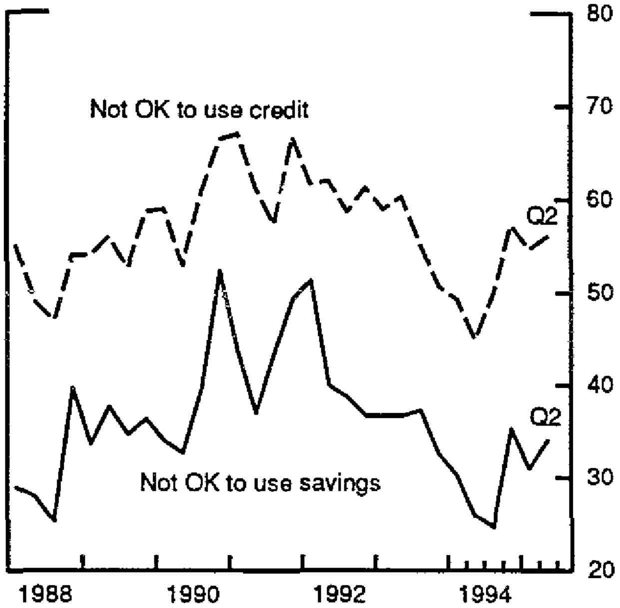
This slowdown in consumption growth has occurred in an environment of weakening income growth. After growing at an average monthly rate of 0.6 percent (annual rate of 7.5 percent) in the fourth quarter of 1994, real disposable income decelerated to an average monthly increase of 0.4 percent in the first quarter of 1995. In April, real DPI fell 1.1 percent. Although private wages and salaries grew moderately in April, DPI was depressed by a $50 billion increase in personal taxes--reflecting the second installment of the OBRA-93 tax increase on high-income households. Even though the level of personal taxes fell back in May, hours worked and average hourly earnings declined, so real DPI likely remained weak.

Recent readings on consumer sentiment have been mixed. According to the preliminary estimate, the University of Michigan SRC index rose slightly in June. Although down somewhat from the peak in January 1995, recent monthly readings on this index have remained well within the range that has prevailed since early 1994. In contrast, the Conference Board index moved down substantially in June to a level distinctly below the buoyant readings that had prevailed since late last year. Despite the slippage over the first half of 1995, both sentiment indexes remain at levels that have been consistent in the past with moderate consumption growth. Furthermore, both of the unemployment expectations indexes, which are more highly correlated with spending than are the overall indexes, also have remained in a relatively favorable range.

The overall financial condition of households remains good, but some small signs of financial stress may be emerging. Delinquency rates for both mortgages and most other consumer loans remain low,

Indicators of Household Financial Conditions





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

	1994	1994 Q3	1994 Q4	1995 Q1	1995 Mar.	1995 Apr.
Total personal income	30.6	31.2	38.4	36.9	31.4	17.3
Wages and salaries	17.3	14.4	19.4	14.7	5.4	19.9
Private	15.4	13.1	17.7	12.3	4.2	19.3
Other labor income	1.7	1.8	1.6	3.6	1.5	1.4
Proprietors' income	1.0	1.2	6.2	5.1	12.9	-15.3
Farm	-1.1	-.8	3.7	4.3	12.9	-14.8
Rent	-.4	.0	-2.2	-.9	-1.9	-1.2
Dividend	1.7	1.8	1.9	.7	1.0	1.1
Interest	7.1	8.9	8.7	7.7	7.4	7.2
Transfer payments	3.9	4.1	4.0	8.4	5.8	5.6
Less: Personal contributions for social insurance	1.7	1.1	1.1	2.4	.5	1.5
Less: Personal tax and nontax payments	3.9	2.8	3.4	6.7	4.3	53.8
Equals: Disposable personal income	26.7	28.3	34.9	30.2	27.1	-36.5
Memo: Real disposable income	13.2	12.2	22.8	14.2	16.5	-41.8

but auto-loan and credit-card delinquency rates rose in the first quarter of 1995.[7] Debt service payments are also rising relative to income, although again from very low levels. There is no evidence, however, that banks have started to restrict credit or that consumers have reduced their credit demand. Responses to the Michigan survey, for example, show that consumers are still quite willing to use savings or credit to finance big-ticket purchases. In addition, the recent stock market rally has added several hundred billion dollars to the net worth of households, although the effects of this addition to wealth on consumption are likely to be spread over a considerable period of time.

Housing Markets

Housing starts edged down in May. In the single-family segment of the market, starts fell 4 percent, although permit issuance was somewhat stronger. Flooding in some areas of the country may have been a factor in the weakness of starts.

Sales of new homes remained soft through April. Sales of existing homes, most of which are recorded a month or two after a contract has been signed, bounced back in May, but only to their relatively low first-quarter pace. Selling prices of new and existing homes have been subdued in their latest readings. But these monthly statistics are fairly noisy indicators and likely have been depressed by shifts in the mix of sales, as suggested by the continued increases in the constant-quality price indexes.

More recent surveys, available through early June, suggest that improvement in starts and sales may be at hand. The recent decline

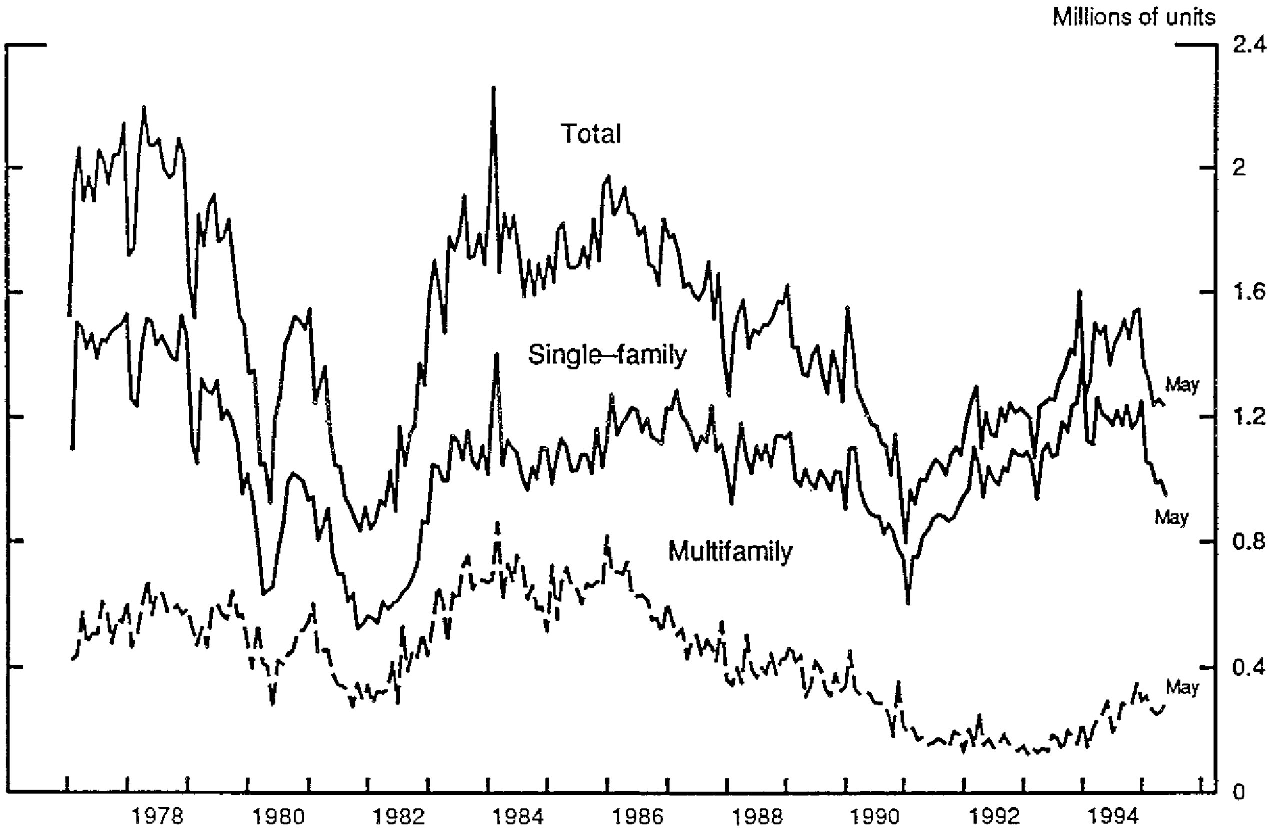
7. Recent data give a mixed picture of the extent of the delinquency problem. Data from the American Bankers Association show a steep rise in credit-card delinquencies, but data from the Call Report registered only a small increase in the first quarter. Similarly, delinquencies on auto loans at the captive auto finance companies rose in the first quarter, while those at banks continued to trend down.

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

	1994				1995	1995		
	Annual	Q2	Q3	Q4	Q1	Mar.[r]	Apr.[r]	May[p]
All units								
Starts	1.46	1.44	1.47	1.51	1.31	1.24	1.26	1.24
Permits	1.37	1.37	1.39	.39	1.27	1.24	1.24	1.25
Single-family units								
Starts	1.20	1.19	1.21	1.20	1.03	.99	1.00	.95
Permits	1.07	1.08	1.06	1.06	.94	.91	.91	.93
New-home sales	.67	.66	.66	.66	.60	.60	.58	n.a.
Existing-home sales	3.95	4.08	3.91	3.76	3.55	3.62	3.39	3.55
Multifamily units								
Starts	.26	.25	.26	.31	.28	.25	.26	.29
Permits	.31	.29	.33	.33	.33	.32	.34	.32

Note. p Preliminary. r Revised. n.a. Not available.

Private Housing Starts
(Seasonally adjusted annual rate)

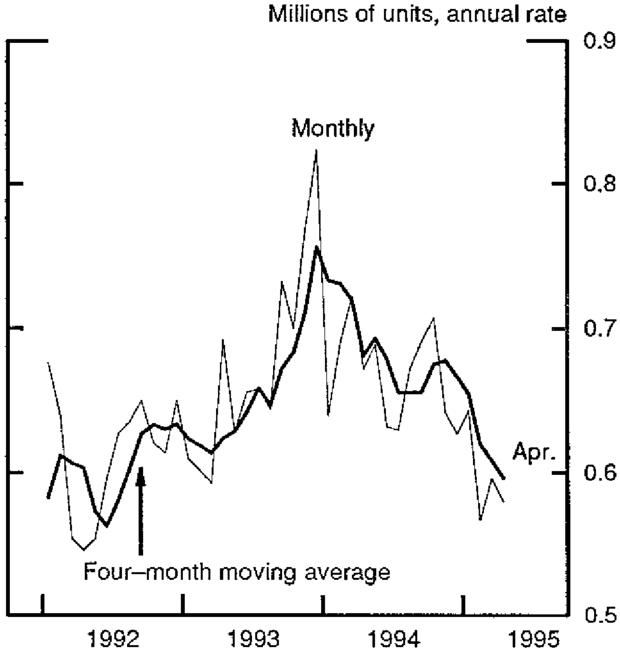


Single–Family Homes

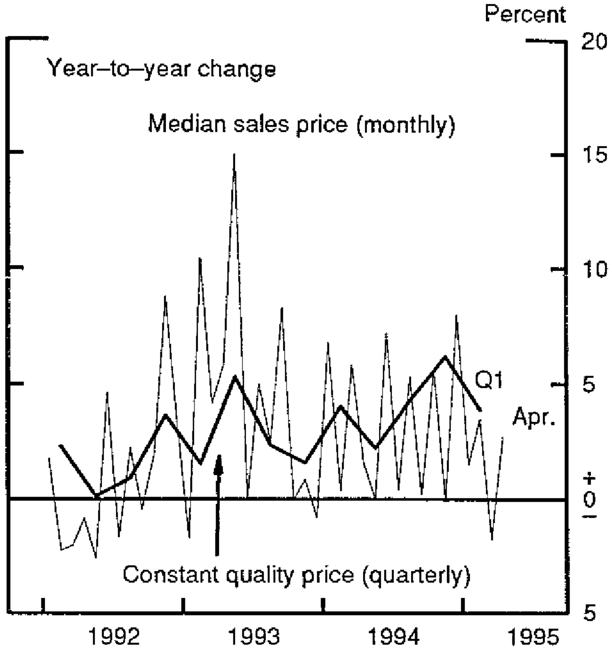
6/26/95

New Homes

Sales

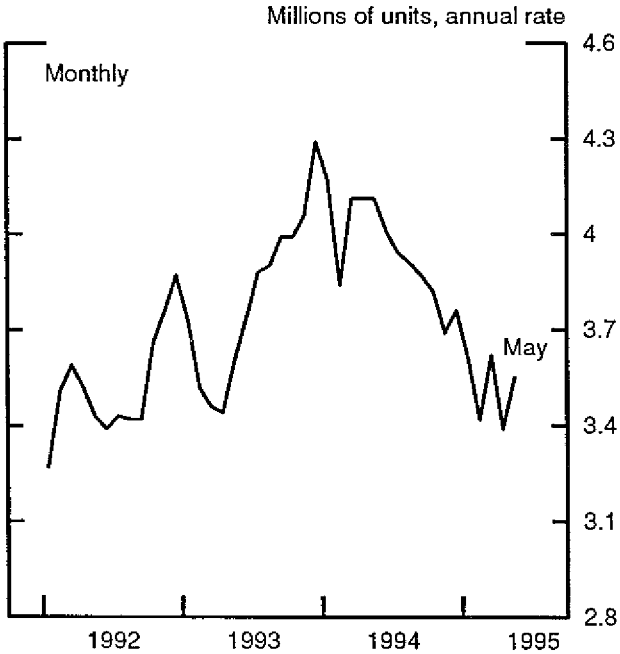


Prices

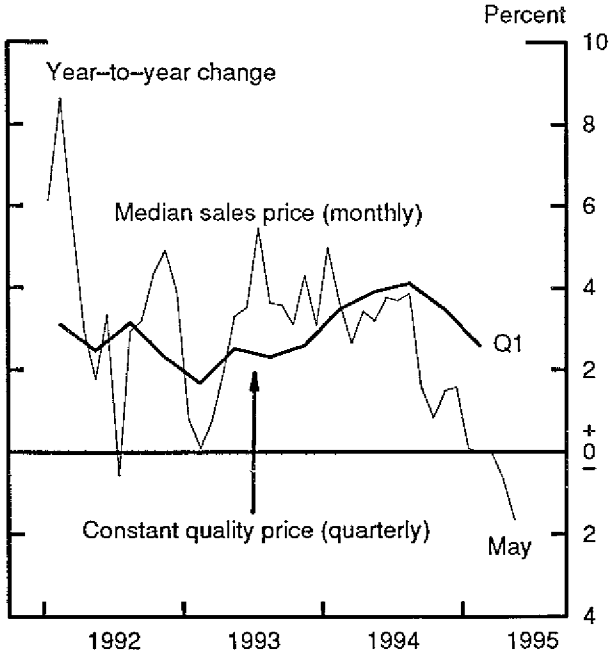


Existing Homes

Sales

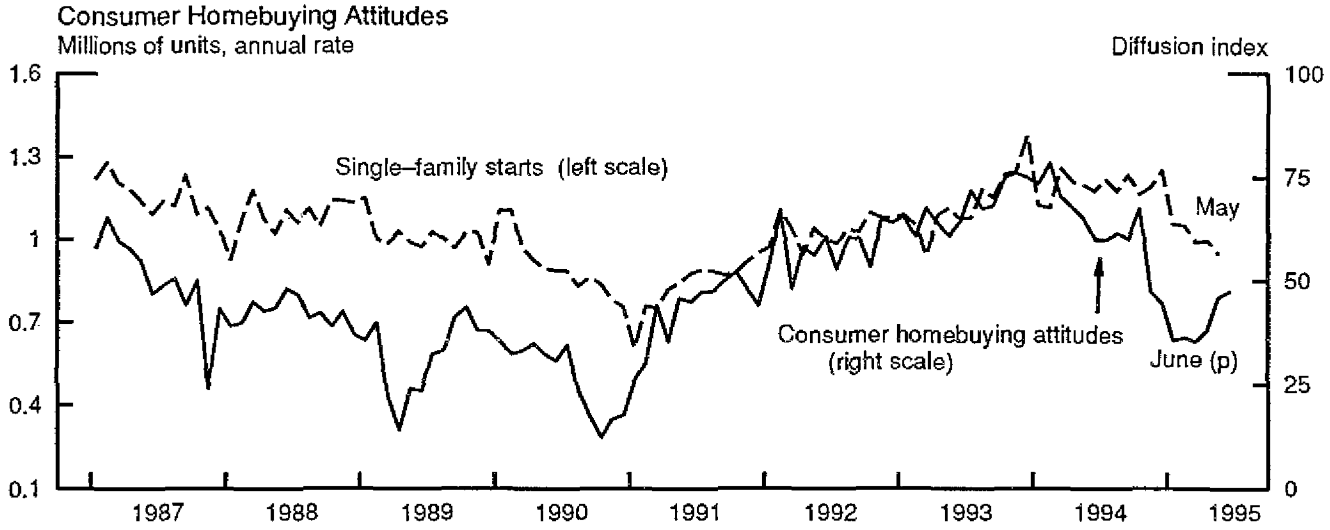


Prices

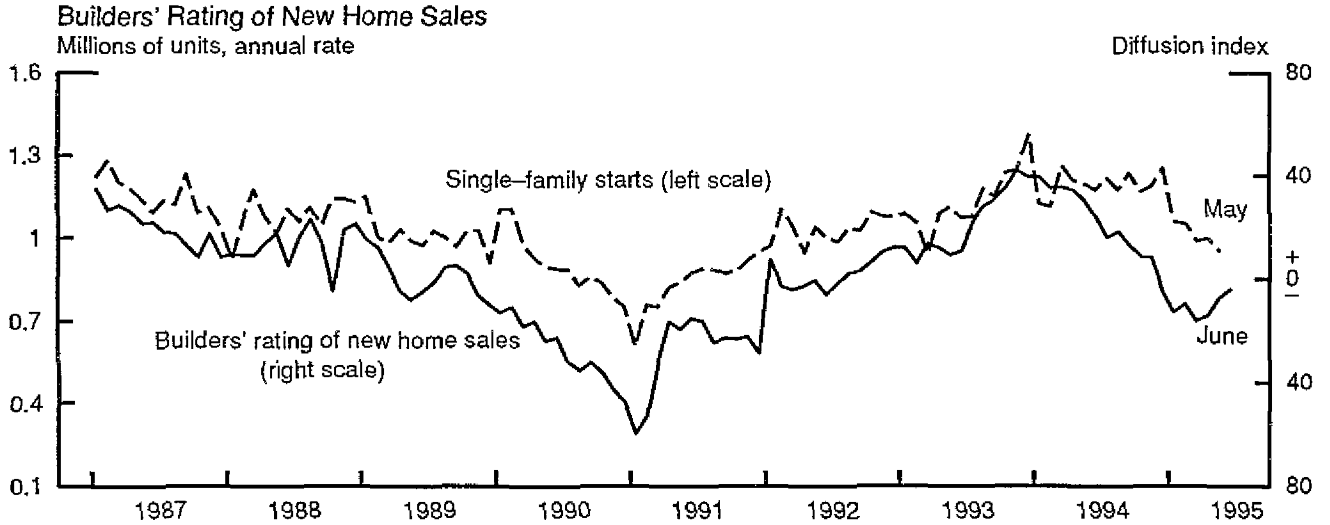


Indicators of Housing Demand

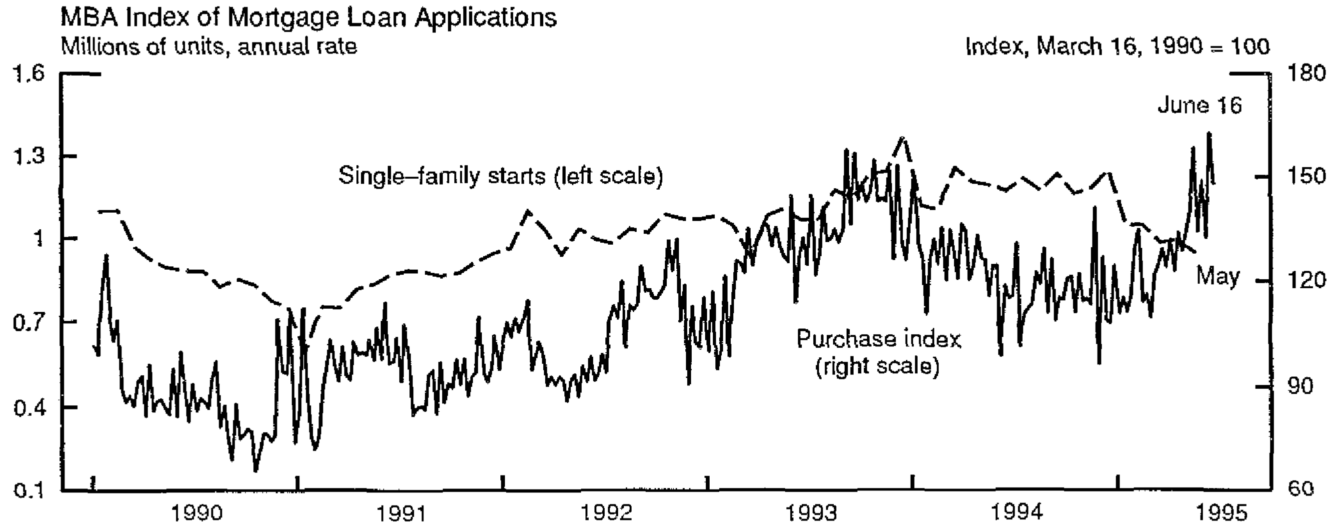
(Seasonally adjusted; FRB seasonals except starts)



Note. 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.



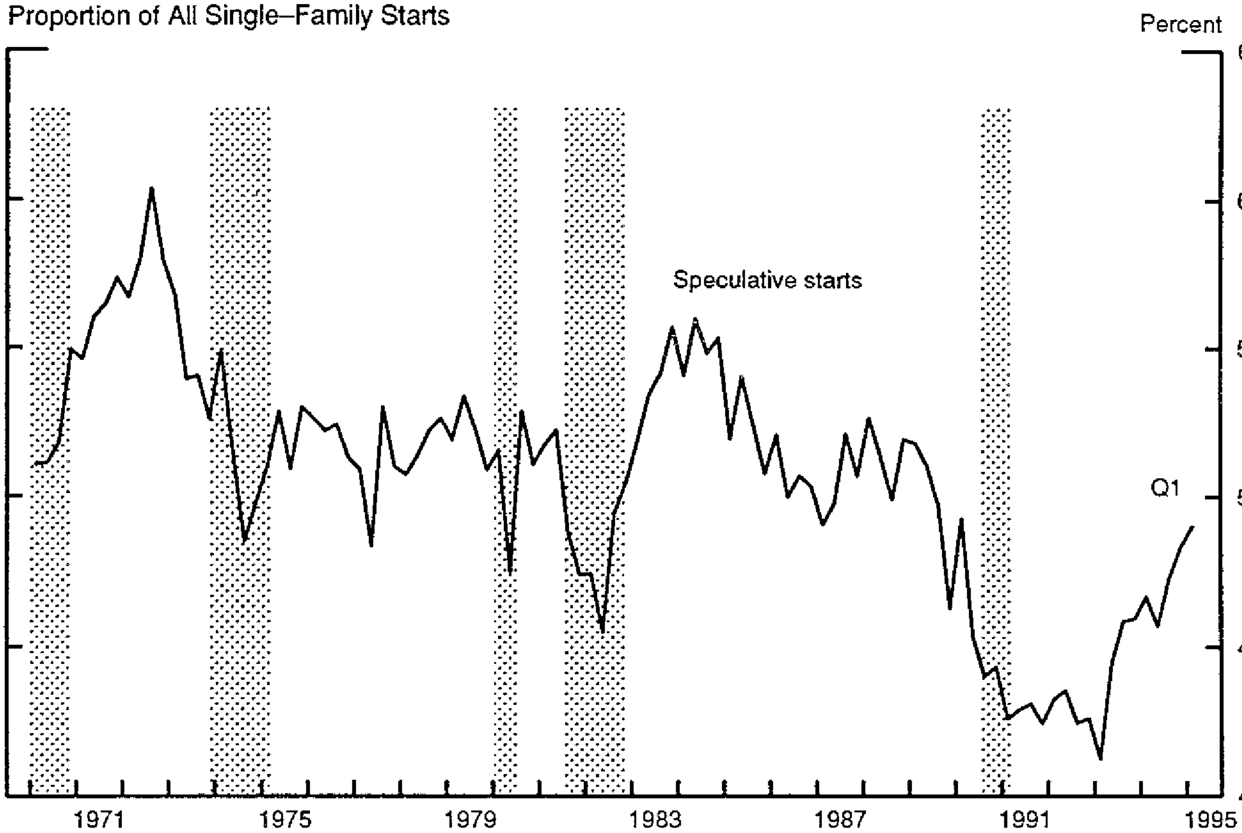
Note. The index is calculated from National Association of Homebuilders data as the proportion of respondents rating current sales as good to excellent minus the proportion rating them as poor



Single–Family Housing

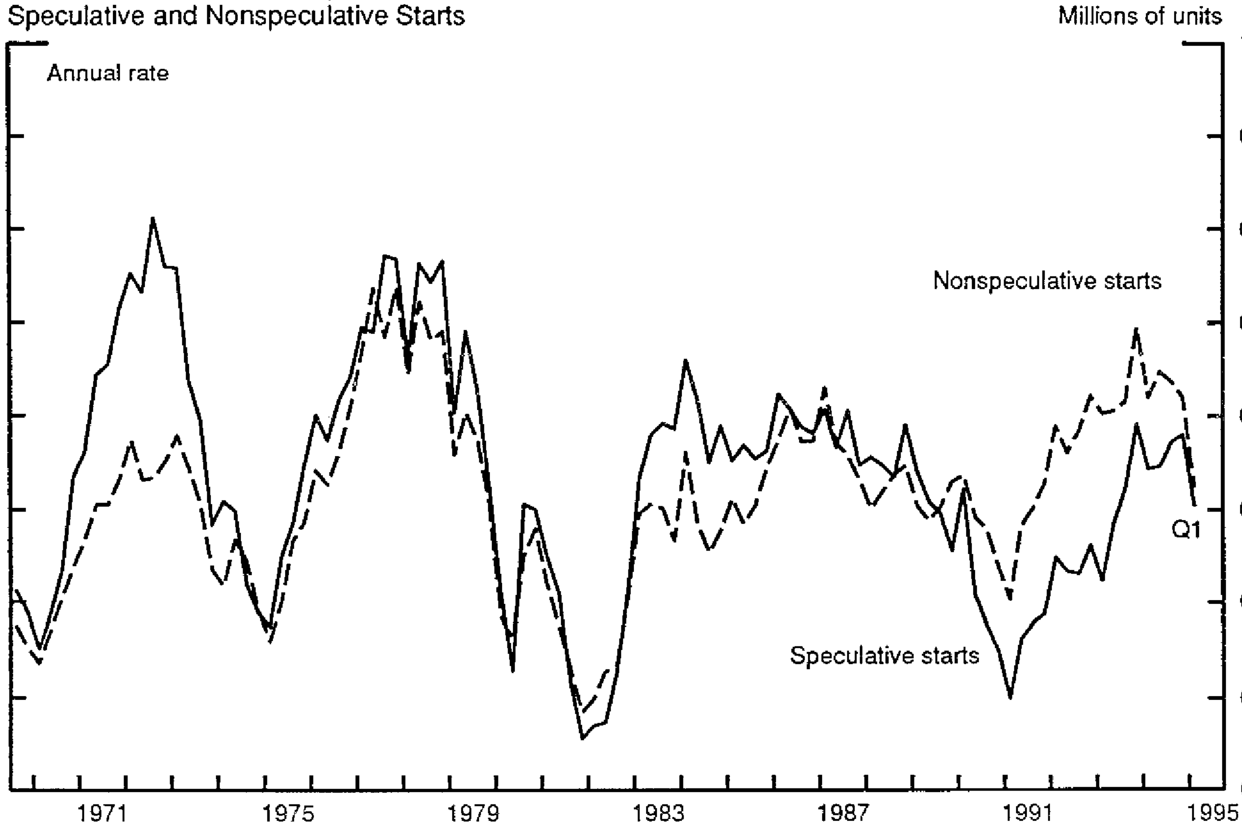
(Seasonally adjusted)

Proportion of All Single–Family Starts



Note. Units started before sale plus units built to be rented.

Speculative and Nonspeculative Starts



in interest rates has buoyed consumer homebuying attitudes and reduced the cash-flow burden of homeownership (based on fixed-rate mortgages) to near the twenty-five-year low set late in 1993. Builders rate their current sales more positively than they did earlier in the spring, and mortgage loan applications appear to be up.

If housing demand is firming, the response of builders may be tempered to a degree by the substantial inventory of unsold new homes. At the end of April, the stock of unsold units was at a five-year high, having trended up both absolutely and relative to sales for more than two years. During this period the speculative share of all single-family starts rose considerably from its record low at the beginning of 1993, as builders and their lenders became more willing to initiate projects prior to having a customer under contract. In the second half of last year, even as demand (measured by nonspeculative starts) was softening, builders were still increasing their speculative construction, contributing to the overhang of unsold new homes.

Multifamily starts rose in May to their highest monthly pace since January. The increase is consistent with the level of permit issuance in recent months and with various indicators of gradual firming in this long-depressed segment of the housing market.

Business Fixed Investment

The available monthly indicators suggest that equipment investment advanced at a brisk pace in the second quarter, although growth has moderated from the still more rapid clip of the previous year or so. Spending for nonresidential structures appears to be headed for another large gain in the second quarter, consistent with an improvement in market fundamentals in this sector.

Shipments of nondefense capital goods excluding aircraft--an important indicator of near-term equipment spending--increased 2.5 percent in May, more than retracing the April decline. The average level of these shipments during the first two months of the quarter was 2-1/4 percent above the first-quarter average; in contrast, during the previous four quarters, these shipments advanced at an average quarterly pace of 4-1/2 percent. New orders for these goods rose 4.1 percent in May, after a 5-1/2 percent decline in April. Cutting through the monthly ups and downs, these orders have continued to increase in recent months, but at a more moderate pace than in 1994.

Computer shipments have been especially robust in recent months. The level of shipments in May was 13-1/2 percent higher than the average reading in the fourth quarter of last year. This strength would seem to defy anecdotal reports that computer shipments have been crimped in recent months by shortages of parts and peripherals. [8]

Overall, the fundamentals for investment are consistent with a moderation in equipment spending later this year. The accelerator effect, which econometric relations suggest is best captured by long lags of changes in business output--with a mean lag of seven quarters--has been waning gradually during the past couple of years, and in the first quarter of this year was about neutral for investment. After large increases early in 1994, the underlying trend in real cash flow has moderated since last fall. The cost of capital for equipment was boosted last year by the rise in interest rates, and, given the estimated lag relationships, that increase

8. While the list of items reported to be on short supply is fairly long (memory chips, CD-ROM drives, monitors, and hard disk drives), industry contacts have indicated that these are mainly spot shortages of the sorts that have nagged most major producers at one time or another during the past couple of years.

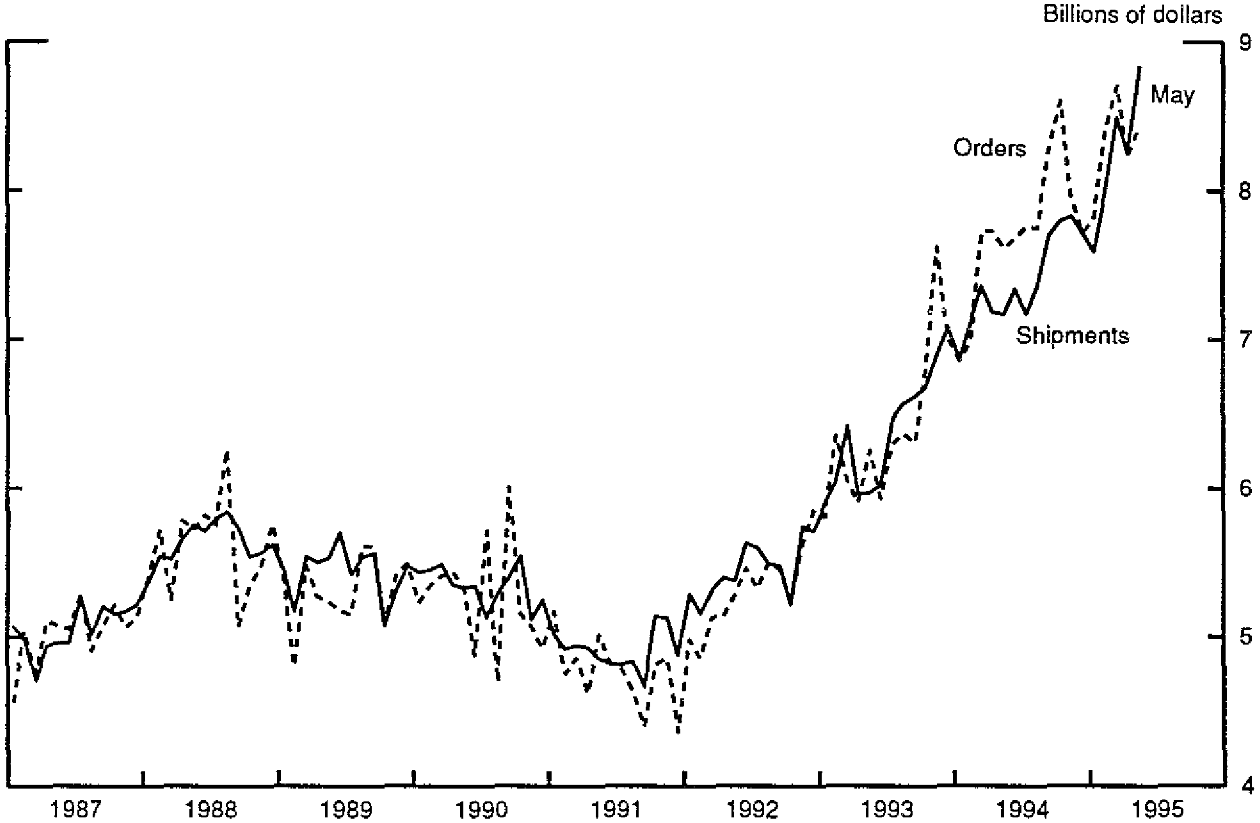
BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period; based on seasonally adjusted data, in current dollars)

	1994		1995	1995		
	Q3	Q4	Q1	Mar.	Apr.	May
Producers' durable equipment						
Shipments of nondefense capital goods	3.4	2.7	5.3	1.1	.0	.7
Excluding aircraft and parts	3.2	3.3	4.8	1.7	-.9	2.5
Office and computing	2.5	4.9	3.1	6.3	-2.8	6.9
All other categories	3.4	2.9	5.2	.3	-.3	1.1
Shipments of complete aircraft[1]	24.0	-12.8	12.5	2.0	-3.7	n.a.
Sales of heavy trucks	1.3	8.2	8.8	-3.5	-2.6	3.7
Orders of nondefense capital goods	3.3	3.4	8.3	1.4	-5.9	6.8
Excluding aircraft and parts	3.4	2.7	6.4	3.8	-5.6	4.1
Office and computing	3.3	2.0	2.8	3.6	-5.4	2.3
All other categories	3.5	2.9	7.4	3.8	-5.7	4.7
Nonresidential structures						
Construction put-in-place	2.4	5.0	1.1	.7	3.4	n.a.
Office	2.8	9.6	3.1	-3.4	.4	n.a.
Other commercial	1.9	4.2	7.7	5.9	.6	n.a.
Institutional	-1.3	1.9	-.1	-4.0	3.5	n.a.
Industrial	3.5	6.9	3.2	-1.8	5.8	n.a.
Public utilities	5.4	4.5	-8.1	4.0	6.9	n.a.
Lodging and miscellaneous	-4.6	6.8	9.9	-5.9	.7	n.a.
Rotary drilling rigs in use	-2.1	-5.3	-1.7	-3.2	4.8	.2
Memo:						
Business fixed investment[2]	14.1	17.6	20.7	n.a.	n.a.	n.a.
Producers' durable equipment[2]	18.1	19.6	22.5	n.a.	n.a.	n.a.
Nonresidential structures[2]	1.6	11.0	14.3	n.a.	n.a.	n.a.

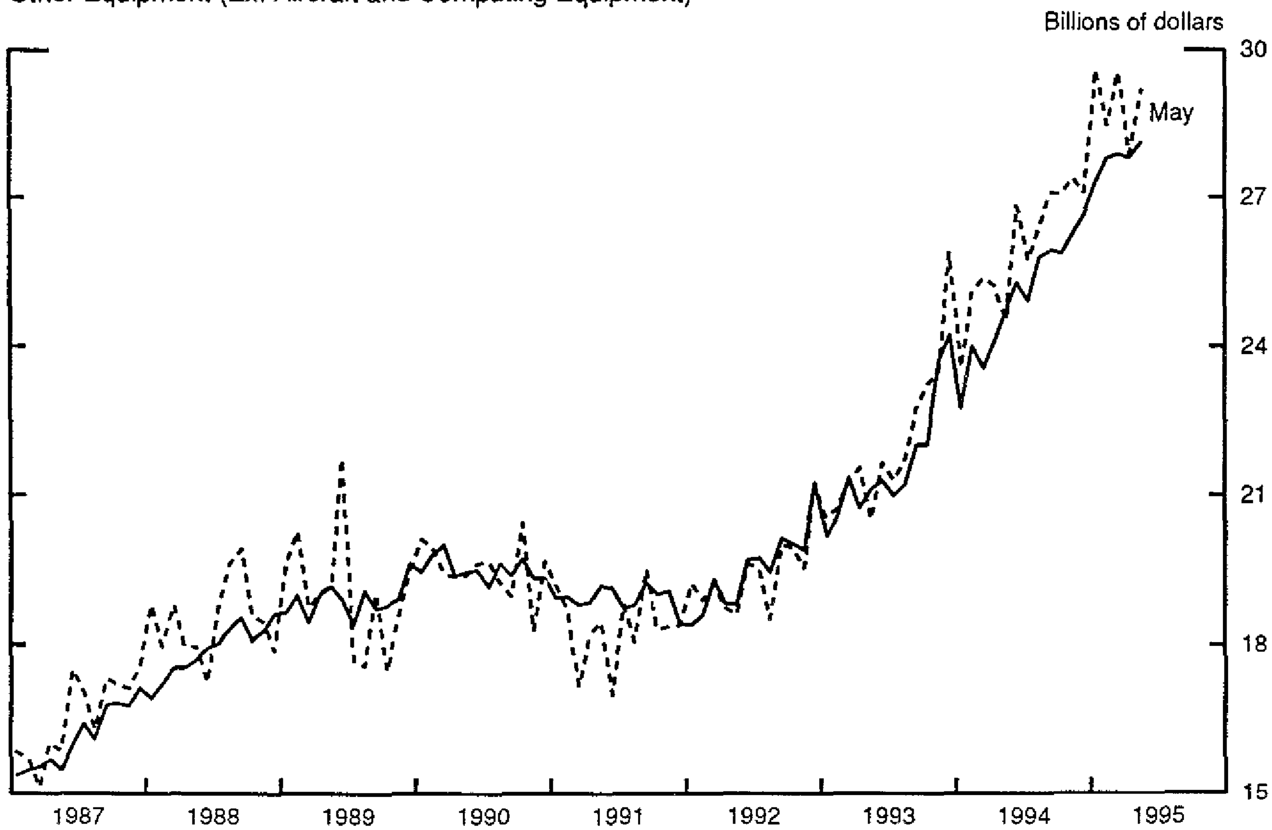
1. From the Current Industrial Report "Civil Aircraft and Aircraft Engines." Monthly data are seasonally adjusted using FRB seasonal factors constrained to BEA quarterly seasonal factors. Quarterly data are seasonally adjusted using BEA seasonal factors.
2. Based on constant-dollar data; percent change,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

Orders and Shipments of Nondefense Capital Goods

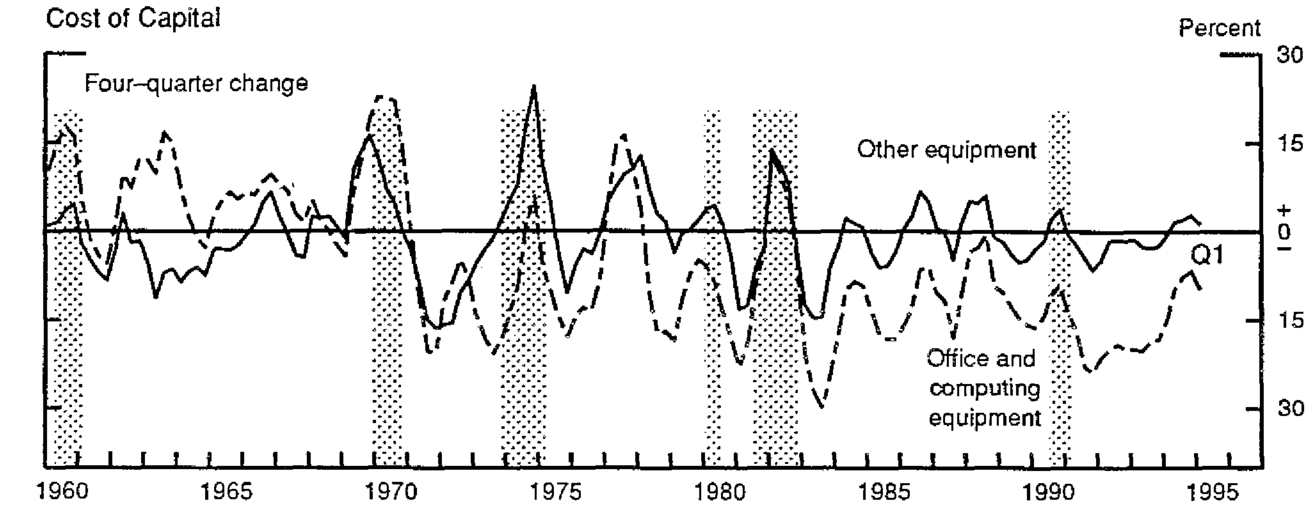
Office and Computing Equipment

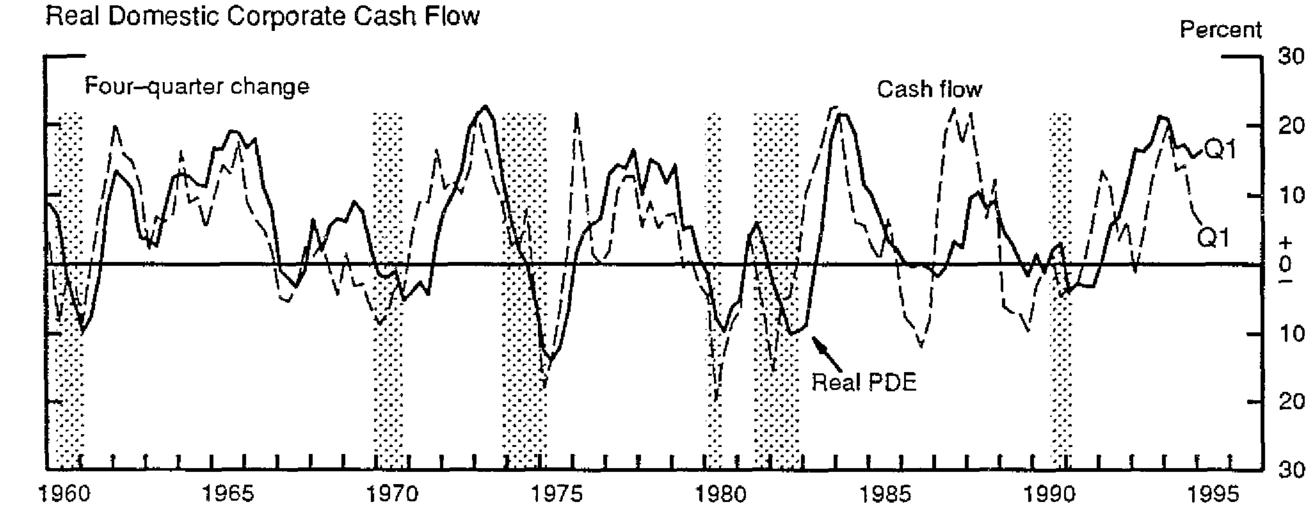


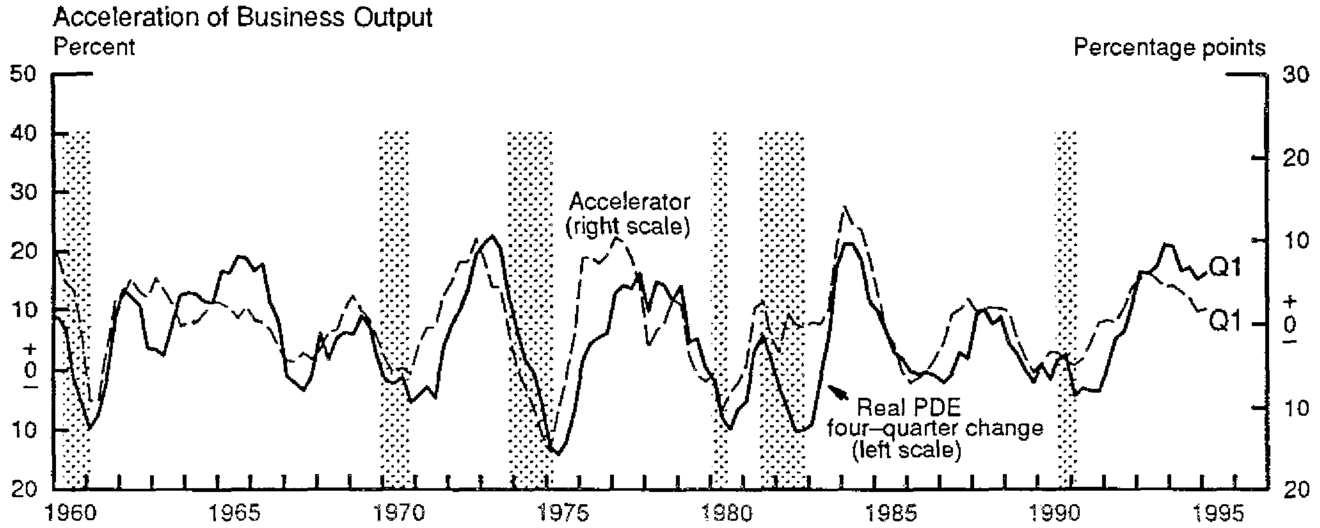
Other Equipment (Ex. Aircraft and Computing Equipment)



Fundamental Determinants of Equipment Spending







Note. The accelerator is the eight-quarter percent change in business output less the year-earlier eight-quarter percent change.

should exert its greatest effect on PDE during the first half of this year. Looking ahead, the rallies in the stock and bond markets so far this year have lowered the cost of capital; all else equal, this should have a positive influence on spending later this year and early in 1996.

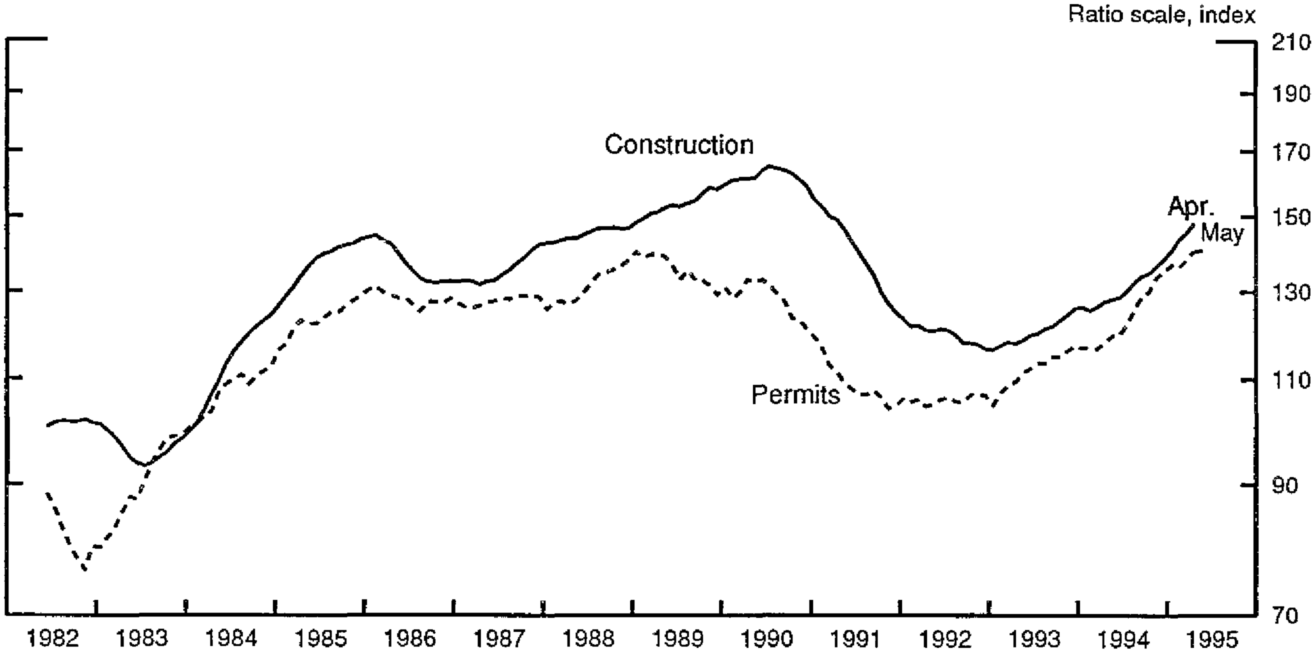
Outlays for nonresidential structures have been on a solid uptrend since the spring of 1994. Spending for these structures advanced at a 14-1/4 percent annual rate in the first quarter, reflecting widespread gains among the various components. Monthly data on construction put-in-place through April point to another healthy increase early in the second quarter. Permits for nonresidential structures, which tend to lead construction by a few months, still are trending up, especially sharply in the industrial sector.

Indicators of market conditions in the nonresidential construction sector have continued to improve. According to CB Commercial, vacancy rates for office buildings declined to 15.1 percent in the first quarter, down 1-3/4 percentage points from a year earlier. Downtown markets have seen a dramatic improvement during the past couple of years, although the first-quarter vacancy reading, 15.6 percent, still is a few percentage points above the typical estimate of equilibrium. While the growth of construction spending has been quite rapid, the level of activity is still extremely low. For example, only 1.9 million square feet of completed office space were added to markets in the first quarter, and much of this space was pre-leased or build-to-suit for a corporate owner. This is up from the pace in 1993 and 1994, when new supply averaged about 1 million square feet each quarter, but in 1985, the peak year for new supply, 131.5 million square feet were completed, and most of this space was not pre-leased. In the

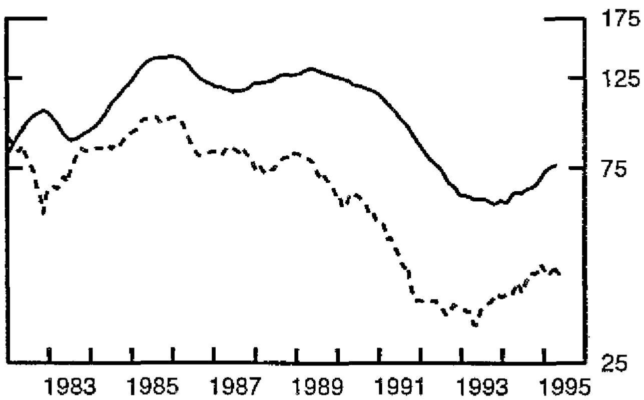
Nonresidential Construction and Permits

(Six–month moving average)

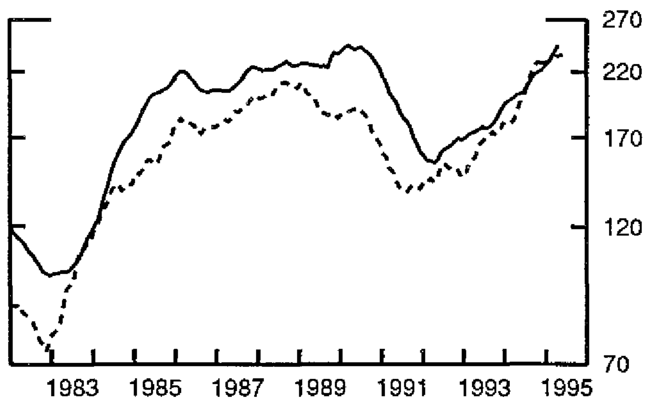
Total Building



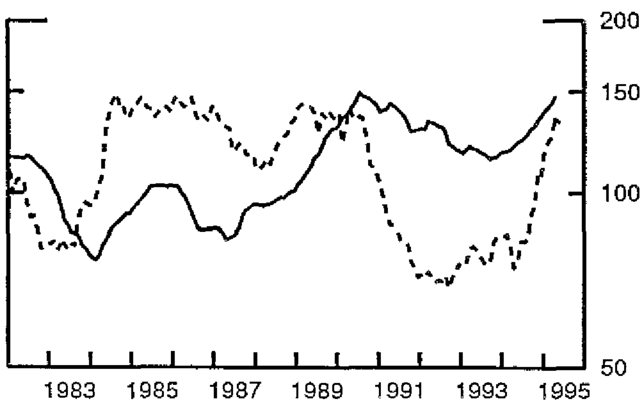
Office



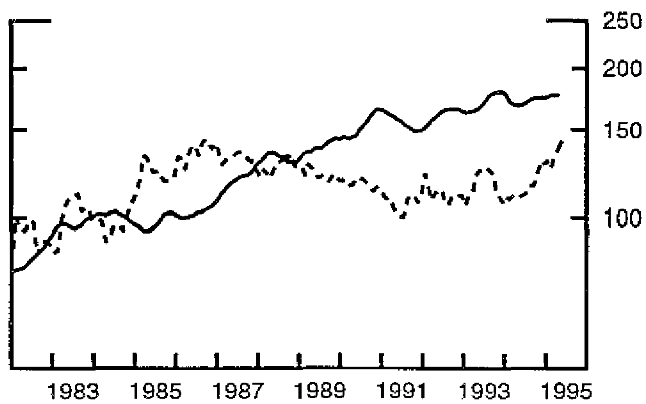
Other Commercial



Industrial



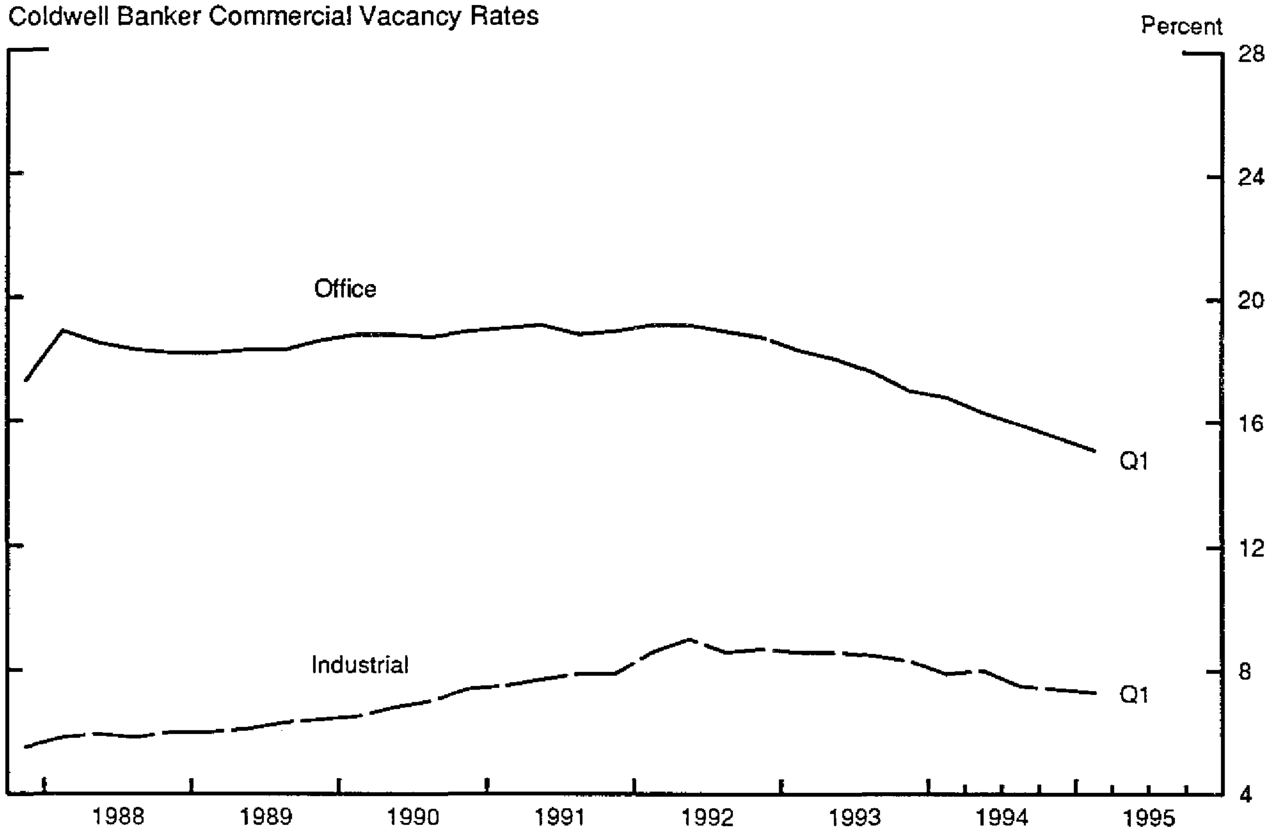
Institutional



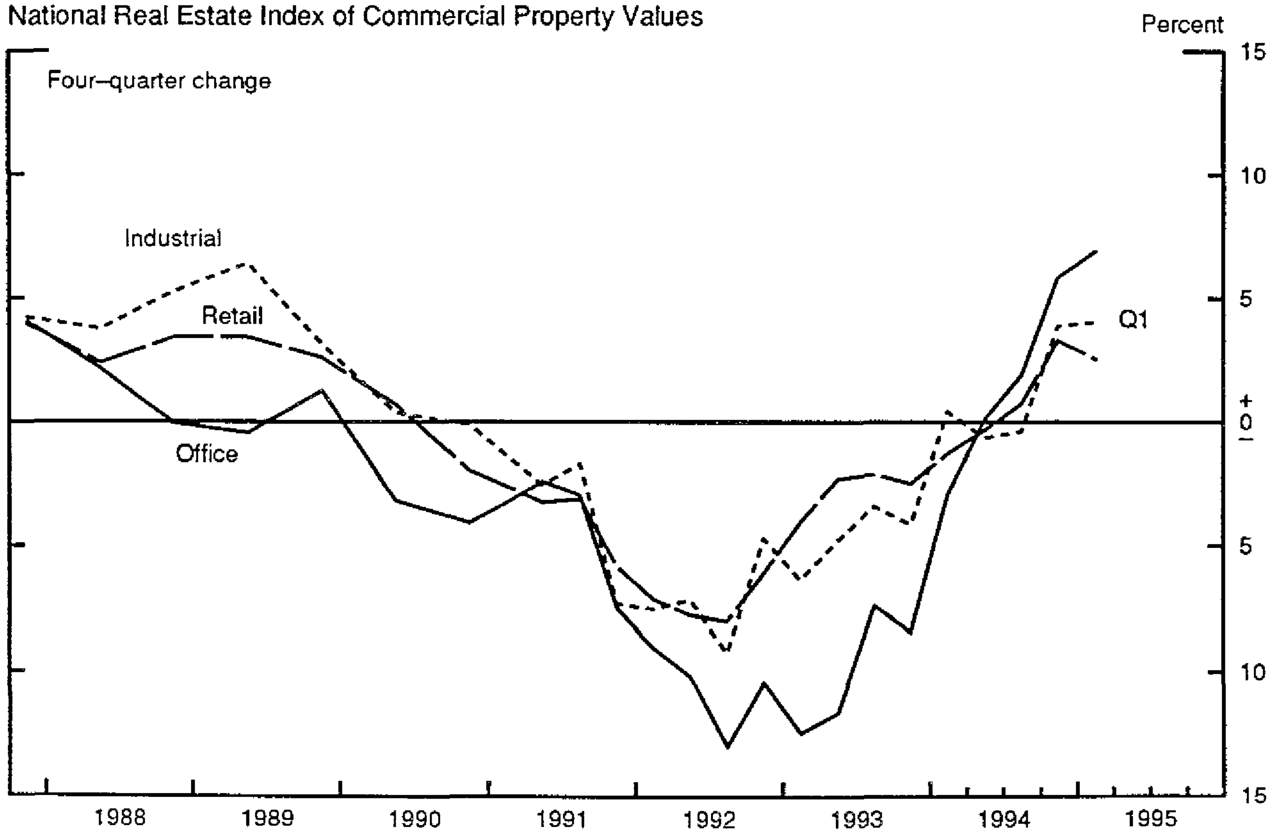
Note. The underlying monthly data were indexed to Dec. 1982 = 100; a six–month moving average was applied to the indexed data.

Nonresidential Structures Indicators

Coldwell Banker Commercial Vacancy Rates



National Real Estate Index of Commercial Property Values



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

	1994		1995	1995		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Total	68.9	57.7	104.8	89.0	79.8	90.3
Excluding wholesale and retail motor vehicles	51.9	55.2	75.2	67.0	61.8	71.7
Manufacturing	13.7	21.1	41.1	43.5	28.3	35.3
Wholesale	22.0	25.5	35.0	25.1	37.2	34.8
Excluding motor vehicles	22.3	25.9	28.9	18.3	38.1	27.2
Retail	33.2	11.1	28.7	20.4	14.4	20.1
Automotive	17.3	2.9	23.4	15.2	19.0	10.9
Excluding auto dealers	15.9	8.2	5.3	5.3	-4.6	9.2
Constant-dollar basis						
Total	39.6	33.8	43.2	34.8	41.7	n.a.
Excluding motor vehicles	31.6	22.7	29.5	19.9	19.5	n.a.
Manufacturing	4.5	4.1	14.1	11.8	7.4	n.a.
Wholesale	15.2	14.1	19.5	11.3	20.4	n.a.
Excluding motor vehicles	15.9	14.9	14.5	5.4	22.0	n.a.
Retail	19.9	15.6	9.6	11.7	13.8	n.a.
Automotive	7.9	11.8	8.5	9.4	21.7	n.a.
Excluding auto dealers	12.0	3.8	1.0	2.3	-7.9	n.a.

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

	1994		1995	1995		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Total	1.40	1.38	1.40	1.39	1.40	1.41
Excluding wholesale and retail motor vehicles	1.37	1.36	1.36	1.35	1.36	1.38
Manufacturing	1.36	1.35	1.35	1.34	1.35	1.37
Wholesale	1.31	1.31	1.33	1.30	1.33	1.34
Excluding motor vehicles	1.29	1.29	1.30	1.27	1.31	1.31
Retail	1.53	1.51	1.54	1.54	1.54	1.55
Automotive	1.76	1.68	1.81	1.79	1.80	1.85
Excluding auto dealers	1.46	1.46	1.46	1.46	1.46	1.46
Constant-dollar basis						
Total	1.46	1.44	1.44	1.44	1.45	n.a.
Excluding motor vehicles	1.50	1.49	1.48	1.48	1.49	n.a.
Manufacturing	1.41	1.39	1.38	1.38	1.38	n.a.
Wholesale	1.40	1.40	1.42	1.40	1.43	n.a.
Excluding motor vehicles	1.40	1.39	1.40	1.37	1.42	n.a.
Retail	1.57	1.55	1.57	1.57	1.57	n.a.
Automotive	1.63	1.62	1.71	1.68	1.72	n.a.
Excluding auto dealers	1.55	1.53	1.53	1.54	1.52	n.a.

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

industrial sector the vacancy rate declined to 7.3 percent in the first quarter, down 1/2 percentage point from a year earlier and 1-3/4 percentage points below its peak in mid 1992.

The National Real Estate Index, which is based on transactions prices for commercial properties, has also improved markedly during the past year or so. Office prices, which fell the furthest earlier in the 1990s, have turned around most abruptly. Prices for warehouses and for other commercial properties also have rebounded.

Inventories

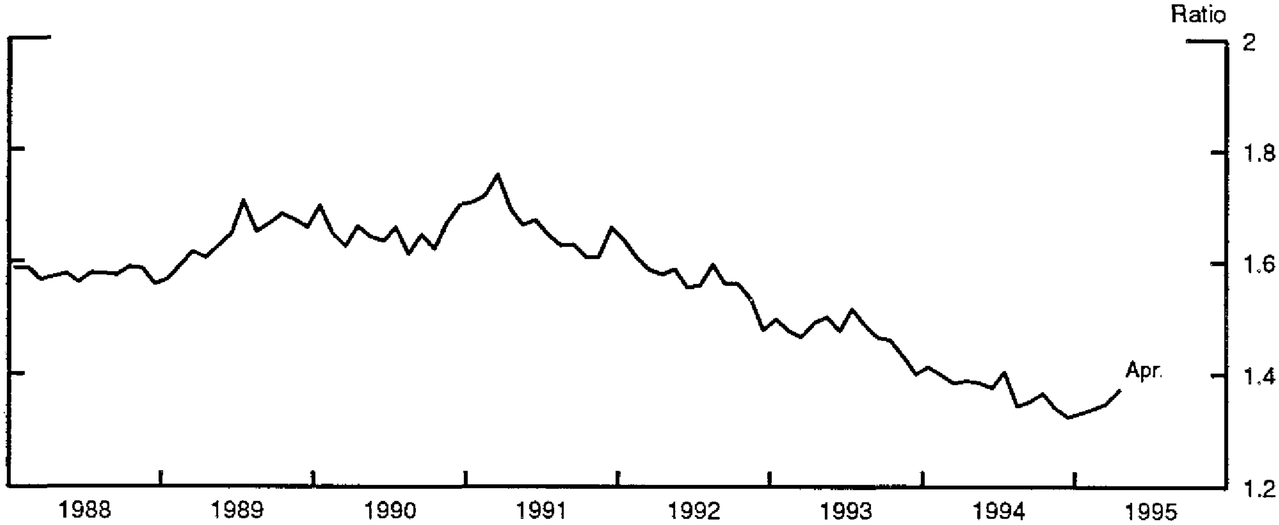
After a significant buildup in the first quarter, business inventories continued to expand at a fairly brisk pace in April. Although the information in hand suggests that serious inventory imbalances exist in only a few sectors, surveys indicate that businesses are watching their stock levels very closely and are poised to adjust orders and production if demand weakens further. Other than motor vehicle inventories, no data are yet available on stockbuilding in May and June, but there are a few hints that the pace of inventory investment may have slowed. Industrial production declined further in May--with part of the weakness stemming from production adjustments in sectors with excessive stocks. In addition, the growth in shorter-term business credit--particularly C&I loans and commercial paper--which often is used to finance inventories, slowed in May and turned negative in early June; this could, however, reflect debt restructuring, as bond issuance is up sharply.

For all manufacturing and trade, the book value of inventories rose at an annual rate of $90 billion in April--down from the $105 billion accumulation in the first quarter. Excluding motor vehicles, stocks were up at a $72 billion annual rate in April--about the same rate as in February and March but well below the

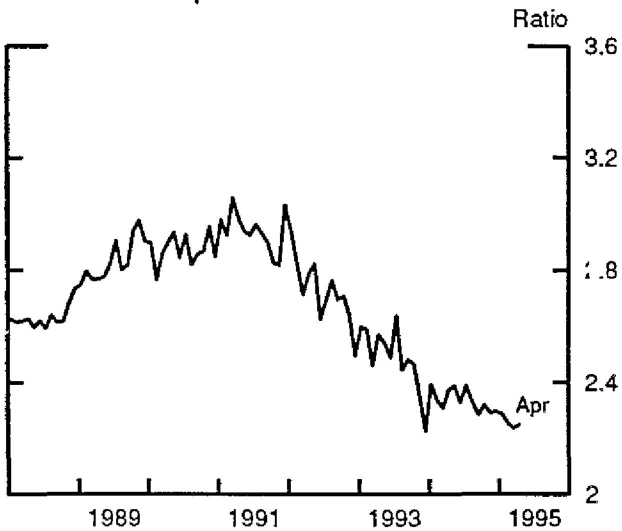
Inventory–Sales Ratios in Manufacturing by Market Category

(Book value)

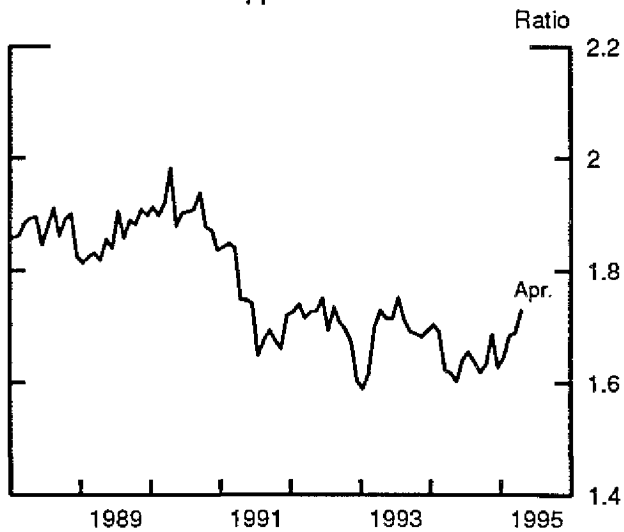
Total



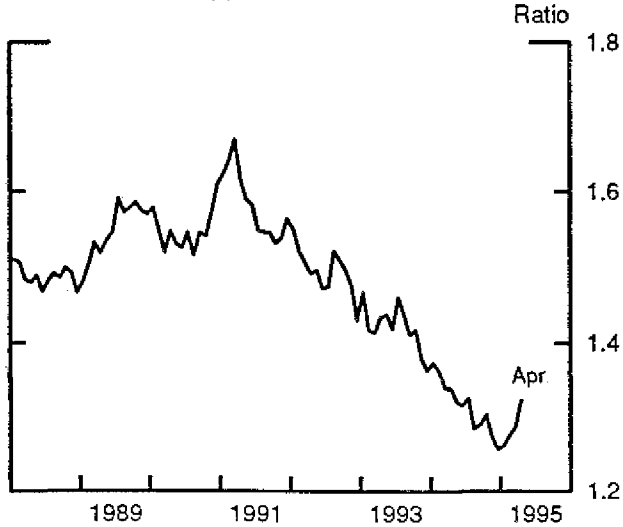
Nondefense Capital Goods



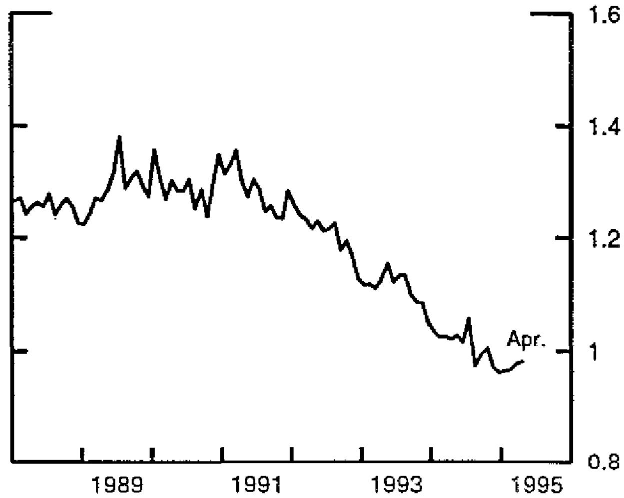
Home Goods and Apparel



Materials and Supplies

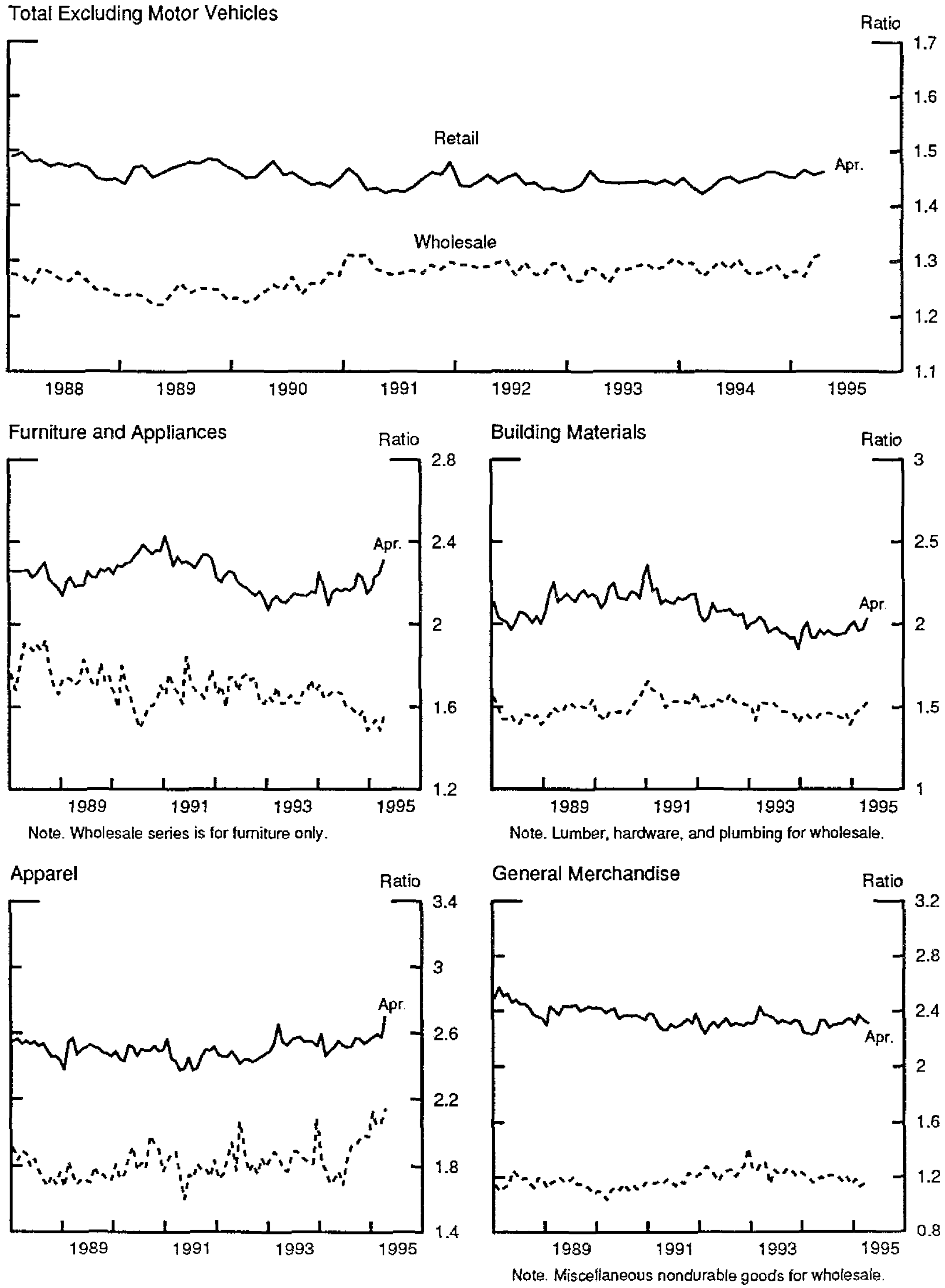


Defense Products, Consumer Staples, and Miscellaneous Goods



Inventory–Sales Ratios in the Non–Auto Trade Sector

(Book value)



blistering pace of $97 billion in January. As a result of these increases, stock-to-sales ratios in manufacturing and trade (excluding motor vehicles) moved up to the high end of the recent range.

In manufacturing, inventories rose at a $35 billion annual rate in April--somewhat above the pace in March. Stocks held by producers of materials and supplies have continued to rise despite the cutbacks in production. Among industries producing finished goods, the picture is mixed. Although stocks rose further in industries producing capital goods--particularly manufacturers of computing and telecommunications equipment--demand for these products appears to have held up through the spring. In contrast, the buildup in inventories of apparel and goods for the home has taken place in the context of weakness in sales, and inventories now seem high in these areas.

In wholesale trade, stocks rose at a $35 billion annual pace in April--matching the gain in the first quarter. Stocks of motor vehicles continued to build, likely reflecting an uptick in imported vehicles. Significant stock accumulations also occurred outside of autos, and the inventory-sales ratio in this segment jumped to the highest level in four years. The accumulation of stocks was greatest among distributors of machinery, other durable goods, and apparel. Import penetration ratios are high for these goods as well, suggesting that some of the adjustment in production will occur abroad.

Inventory investment was more moderate at retail establishments. Outside of auto dealers, retail trade inventories rose $9 billion in April, and inventory-to-sales ratios generally seem to be in line with the current pace of sales. The notable exceptions are in stocks of apparel, where retailers have consistently been surprised this year by the dearth of demand, and in inventories of furniture, appliances, and home furnishings.

Federal Sector

The federal government recorded a budget surplus, on a unified basis, of $11 billion in April and May, compared with a $15 billion deficit a year ago. However, after adjusting for differences in the timing of some payroll and benefits payments and excluding deposit insurance, the April-May deficit improvement from last year was $16 billion; adjusted outlays were up 6-1/4 percent and receipts were up 14 percent.[9]

Personal nonwithheld taxes in April and May were up 41 percent ($22 billion) from last year. These payments were boosted this year by a change in "safe-harbor provisions" that allowed some high-income individuals to delay a larger share of payments on 1994 liability to the April 17 due date for final payments.[10] It is likely that this tax law change accounted for most, if not all, of the growth in personal nonwithheld taxes.[11]

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9. Because April 1 fell on a Saturday, some outlays for defense payroll, veterans benefits, and supplemental security income benefits were accelerated into March. No such payment shift occurred last April.

10. Under current law, taxpayers with adjusted gross income (AGI) in 1993 of less than $150,000 can avoid IRS penalties for late payments of 1994 taxes if payments in 1994 (including the estimated payment in January 1995) were at least as great as the lesser of 90 percent of 1994's tax liability or 100 percent of 1993's tax liability (the so-called "previous year's safe harbor"). For higher-income taxpayers, the previous year's safe harbor is 110 percent of their 1993 tax liability. These provisions are looser than the law that applied to estimated and final payments on 1993 liabilities. Under that law, taxpayers were denied the option of the previous year's safe harbor if their AGI was greater than $75,000, or had jumped more than $40,000, or if they had paid estimated taxes or penalties for underpayment of estimated taxes in any of the previous three years.

11. There has been some speculation in the press that lower mortgage interest deductions, derived from 1993 mortgage refinancing, led to the jump in April and May tax payments. However, as of May, cumulative 1994 individual income tax payments were not unexpectedly high, given income growth and estimates of the incremental liabilities legislated in OBRA-93. Similarly, refunds were not unexpectedly low.

ADJUSTED[1] FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis; billions of dollars, except where otherwise noted)

	April and May		Fiscal year to d.te			
	1994	1995	FY1994	FY1995	Dollar change	Percent change
Outlays	239.5	250.9	966.0	1009.3	43.3	4.5
Deposit insurance (DI)	1.7	-1.8	-5.1	-12.4	-7.3	144.9
Outlays excluding DI	237.8	252.7	971.1	1021.7	50.6	5.2
National defense	44.0	42.6	183.7	176.7	-7.0	-3.8
Net interest	34.8	40.3	133.9	153.8	19.9	14.9
Social security	53.2	56.0	209.1	219.7	10.5	5.0
Medicare and health	40.2	45.1	163.7	178.5	14.9	9.1
Income security	36.8	41.4	149.8	153.8	3.9	2.6
Other	29.0	27.3	130.8	139.3	8.4	6.4
Receipts	224.9	255.8	801.3	870.2	68.9	8.6
Personal income	84.4	106.2	346.4	381.0	34.6	10.0
Withheld	70.7	75.9	311.0	339.5	28.6	9.2
Nonwithheld	52.6	73.7	105.8	118.4	12.6	11.9
Refunds	38.9	43.3	70.3	77.5	7.2	10.2
Social insurance	96.9	102.0	306.3	326.9	20.7	6.7
Corporate	23.4	25.7	77.1	82.7	5.6	7.3
Other	20.2	21.9	71.6	80.0	8.4	11.7
Deficit(+)	14.6	-4.9	164.7	139.1	-25.6	-15.5
Excluding DI	12.9	-3.1	169.8	151.5	-18.3	-10.8
Memo:						
Unadjusted deficit(+)	14.6	-10.8	164.7	133.2	-31.5	-19.1
Excluding DI	12.9	-9.0	169.8	145.6	-24.2	-14.2
Refunds + EITC	41.0	49.7	80.9	91.8	10.9	13.5

1. 1995 outlay numbers for defense, income security, and the other category are adjusted up to account for shifting of official outlays from April 1995 to March 1995 and from October 1994 to September 1994.

Note. Components may not sum to totals because of rounding.

Payments of individual refunds and the EITC (scored as an outlay) were up 21 percent in April and May, owing in part to increased IRS scrutiny that delayed payments ordinarily made during the first quarter. After adjusting for timing effects, about $9 billion of refund/EITC payments were shifted into the second quarter.[12] Much of the payment shift was from February (down about $6 billion) to May (up about $6 billion), especially the last week of May (up about $4 billion).

For the first eight months of the fiscal year, the deficit was $133 billion, $32 billion less than last year. Excluding deposit insurance, and adjusting for timing shifts, the deficit reduction this year was $18 billion, very close to the deficit improvement for April and May alone. Adjusted outlays excluding deposit insurance rose at a 5-1/4 percent pace, as rapid growth in spending for net interest (15 percent) and health programs (9 percent) was offset by modest growth for adjusted income security spending (2-1/2 percent) and negative growth for payday-adjusted defense spending (-3-1/2 percent). Over the first eight months of the fiscal year, receipts grew at an 8-1/2 percent pace, with all major categories contributing strongly.

A House-Senate conference committee has agreed on a seven-year budget resolution that projects budget balance in fiscal 2002. Relative to CBO's April baseline, the agreement cuts spending $1271 billion and decreases taxes $245 billion. About 50 percent of the spending reductions are for mandatory programs, primarily Medicare (21 percent of reductions) and Medicaid (14 percent). In addition, the plan calls for a $441 billion decrease in discretionary spending. The agreement includes procedural rules designed to

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12. Refund/EITC payments are bunched on Fridays, and the last Friday of the first quarter fell on March 31; payments made on the corresponding Friday of last year fell on April 1 and were included in the second-quarter numbers.

CONFERENCE AGREEMENT DEFICITS COMPARED TO CBO BASELINE

	1996	1997	1998	1999	2000	2001	2002	1996-2002
CBO Baseline Deficit	210	230	232	266	299	316	349	1902
Changes:								
Discretionary	-18	-29	-40	-59	-75	-99	-121	-441
Mandatory	-20	-45	-66	-90	-117	-139	-168	-645
Health	-11	-25	-42	-62	-82	-104	-125	-451
Other	-9	-20	-24	-28	-35	-35	-43	-194
Debt Service	-1	-6	-12	-20	-32	-47	-67	-185
Deficit (reduction from baseline)	-39	-80	-118	-169	-224	-285	-356	-1271
Memo:								
Maximum Tax Cut	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	50	245
Financing:								
Fiscal Dividend	3	7	14	23	32	41	50	170
Other	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0	75

Note. The conference agreement assumes the fiscal dividend will occur if the spending reductions are enacted. The fiscal dividend is based on CBO's April 1995 document *An Analysis of the President's Budgetary Proposals for Fiscal Year 1996*.

n.a. Not applicable.

ensure that the spending targets are met before any tax cuts are enacted. Tax cuts are limited to $245 billion over seven years and $50 billion in fiscal 2002, and are paid for by an assumed $170 billion fiscal dividend derived from lower interest rates and $75 billion in additional budget cuts to be agreed upon later.

The conference agreement calls for far more deficit reduction than does the ten-year budget balance plan released by the President on June 13. The President's plan reaches balance in fiscal 2005 only under economic and technical assumptions that are more optimistic than the CBO assumptions used in the conference agreement. Using CBO's assumptions, the policies in the President's plan would keep the deficit close to $200 billion over the next ten years.

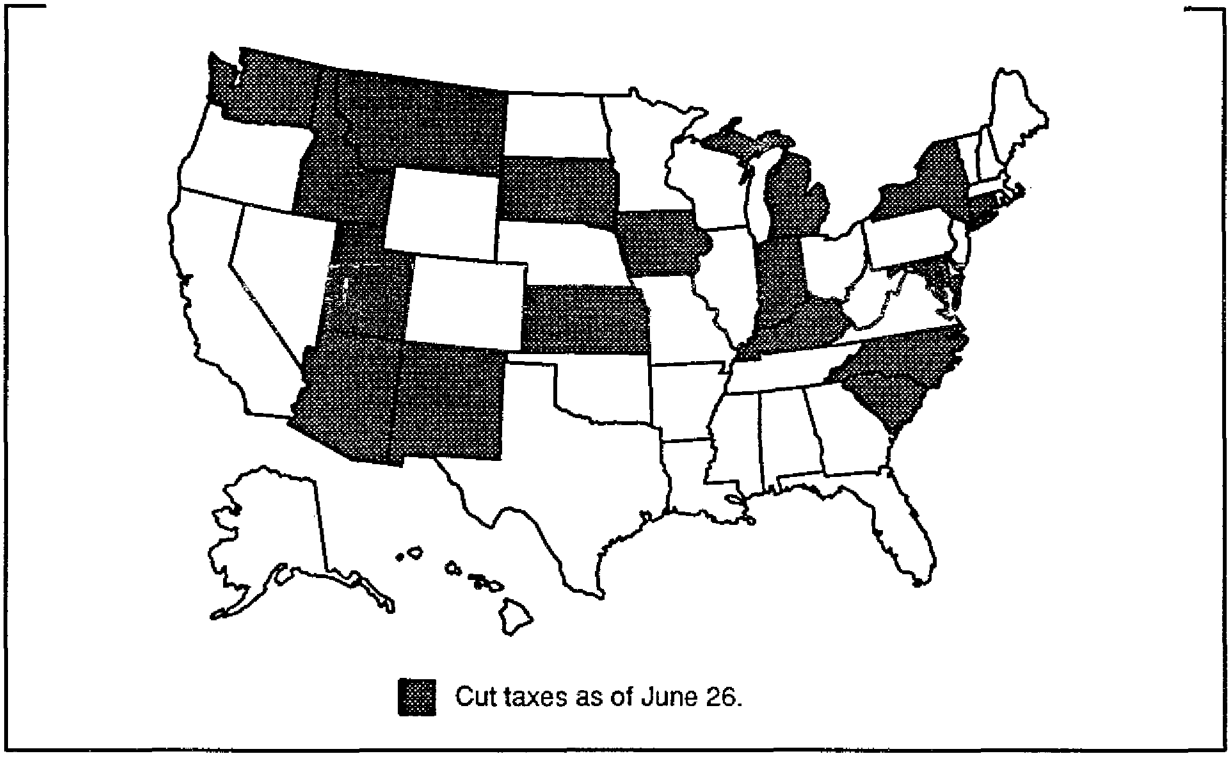
State and Local Government Sector

Indicators of state and local government spending so far in the second quarter have been mixed, with employment basically flat over the first two months of the quarter and construction up in April. Employment fell 16,000 in May, reversing most of the April increase. All of the May weakness was in employment of noneducation workers. Real construction spending rose 1 percent at a monthly rate in April, about twice the monthly average during the first quarter. Construction of schools and other buildings (the category that includes prisons) registered strong gains.

State governments are currently finalizing their fiscal 1996 budgets, if they haven't done so already, as the new fiscal year for all but four states starts July 1. Most states should end the current year in relatively good shape financially. At the start of the fiscal year, the states as a group were assuming that general fund revenue would increase 3.8 percent over the year. For the first three quarters of the fiscal year, the level of receipts from

States Cutting Taxes

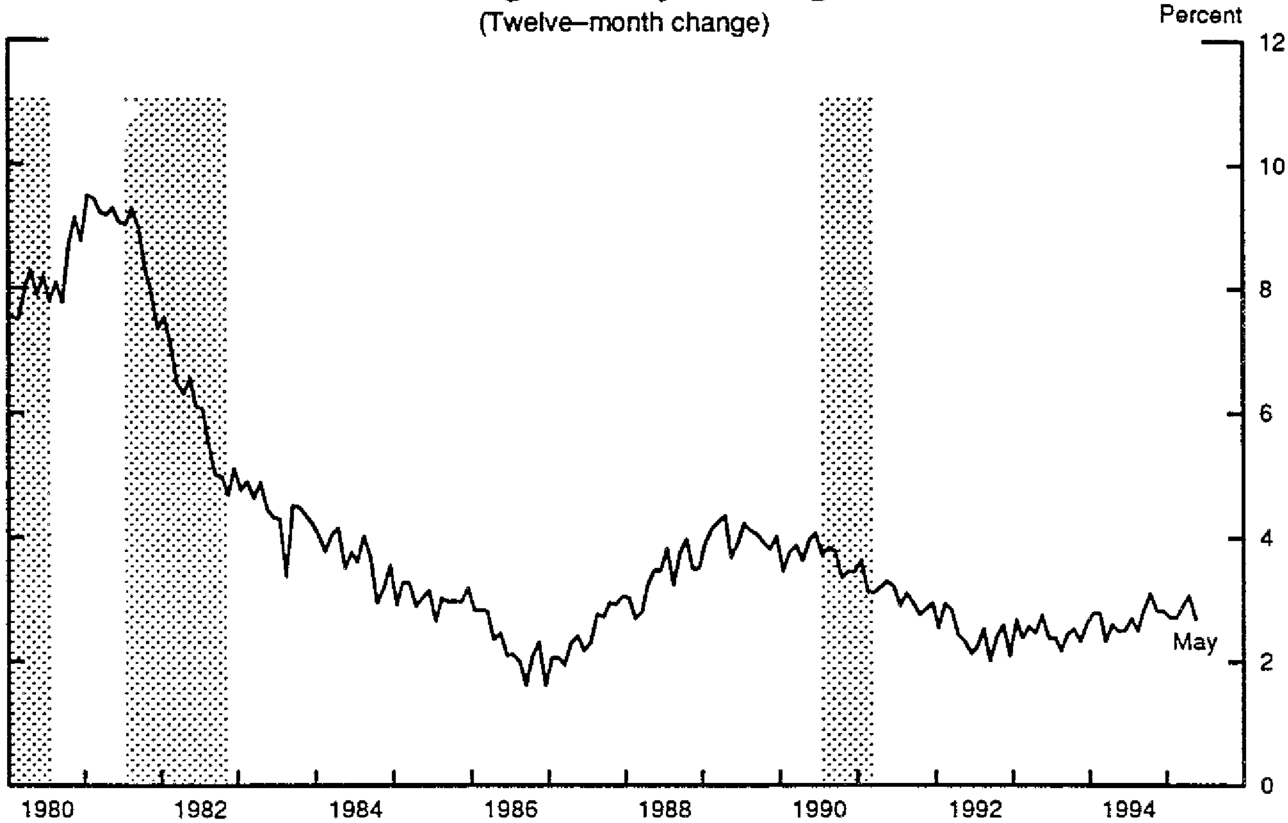
(Effective after June 30, 1995)



taxes and fees for all state and local governments had already risen 4.0 percent. Even so, with tax revenue in recent months coming in below expectations in some states and concern mounting about potential, but as yet unknown, federal reductions in grants, many state legislatures have been reluctant to pass the generous tax-cut measures requested by their governors earlier in the year. Indeed, gubernatorial tax cuts have been rejected, or are likely to be, in seven states this year: California, Massachusetts, Mississippi, Nebraska, Oklahoma, Virginia, and Vermont. And, although seventeen states have cut taxes this year, with several more likely to do so, these tax cuts have tended to be smaller than first proposed. Generally, states cutting taxes this year are states with relatively strong economies, with Republican governors, or with tax hikes earlier in the decade.

While states, which account for about half of the sector's spending, have been reporting improved fiscal conditions this year, many local governments are still struggling financially. After considerable improvement in 1993 and 1994, more than half of cities are estimating that they will run current-year deficits in their general fund accounts in fiscal 1995. In addition, school districts have been in deficit since the school-year ending in 1990, after running surpluses during the mid-to-late 1980s; the reported deficits reflect imbalances in operating accounts as well as a step-up in school construction early in the 1990s. And, in a recent survey, nearly 65 percent of counties said they were either having difficulty maintaining services or were reducing discretionary programs; 4 percent characterized their fiscal position as in a crisis. Cities, school districts, and counties make up the bulk of local governments.

Average Hourly Earnings
(Twelve–month change)



LABOR COSTS
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

	1993[1]	1994[1]	1994 Q2	1994 Q3	1994 Q4	1995 Q1	1994:Q1 to 1995:Q1
Compensation per hour							
Total business	2.3	3.2	.9	3.1	3.6	4.0	2.9
Nonfarm business	1.9	3.2	1.4	2.7	3.8	4.3	3.0
Manufacturing	1.7	1.7	-1.8	2.4	3.8	4.7	2.3
Nonfinancial corporations[2]	1.3	2.6	.6	2.9	3.2	3.8	2.6
Unit labor costs							
Total business	.8	1.2	2.3	-.1	-.7	1.8	.8
Nonfarm business	.5	1.4	2.8	.0	-.4	1.6	1.0
Manufacturing	-.9	-2.4	-5.8	-1.0	.1	1.3	-1.4
Nonfinancial corporations[2]	-1.0	1.0	1.4	1.2	-.3	2.0	1.1

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, finance and insurance companies; the sector accounts for about two-thirds of business employment.

Wages and Prices

Wage inflation has remained in check to date. Average hourly compensation in the nonfarm business sector accelerated to a 4.3 percent rate of increase in the first quarter, but in large part this pickup reflected developments that are likely to be reversed in the second quarter.[13] Over the twelve months ended in March, this measure rose 3 percent, about 1/2 percentage point more than the change over the previous year.[14] More recent data on average hourly earnings showed a 0.5 percent increase in April, followed by a 0.2 percent decline in May. This measure of wage change has risen 2.7 percent over the past twelve months, 0.2 percentage point more than during the comparable period of a year ago.

Price inflation abated in the most recent data, after an uptick in early 1995. Excluding food and energy, consumer prices increased 0.2 percent in May--as compared with the roughly 0.4 percent average pace in the first four months of the year. Over the past twelve months, the core CPI has increased 3.1 percent--0.3 percentage point more than in the preceding year. Prices for finished producer goods excluding food and energy rose 0.3 percent in May, about the same as in the previous month. However, price increases for producer goods at earlier stages of production slowed considerably. Prices for industrial commodities have been mixed, and most commodity price indexes continue to show only modest increases or slight declines in prices for industrial materials.

Prices for consumer commodities excluding food and energy were flat in May. Apparel prices fell 0.3 percent, probably reflecting

13. In particular, the first-quarter increase was boosted by an increase in overtime hours, mix-shifts toward higher-wage industries, a lump-sum payment by GM to its pension plan, and the increase in the wage ceiling for social security taxes.

14. The employment cost index for private industry workers showed an almost identical change in hourly compensation--2.9 percent over this same period.

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

	Relative importance, Dec. 1994	1993	1994	1994 Q3	1994 Q4	1995 Q1	1995 Apr.	1995 May
				-----Annual rate------			-Monthly rate-	
All items[2]	100.0	2.7	2.7	3.6	1.9	3.2	.4	.3
Food	15.8	2.9	2.9	5.1	3.9	.0	.7	.1
Energy	7.0	-1.4	2.2	9.2	.4	-1.1	.4	.5
All items less food and energy	77.2	3.2	2.6	2.6	2.0	4.1	.4	.2
Commodities	24.1	1.6	1.4	.9	.3	2.6	.2	.0
Services	53.1	3.9	3.2	3.6	2.6	4.8	.4	.3
Memo:								
CPI-W[3]	100.0	2.5	2.7	3.9	2.2	3.6	.3	.2

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. 1994	1993	1994	1994 Q3	1994 Q4	1995 Q1	1995 Apr.	1995 May
				-----Annual rate------			-Monthly rate-	
Finished goods	100.0	.2	1.7	1.9	2.2	2.6	.5	.0
Consumer foods	22.8	2.4	1.1	1.9	9.2	-1.8	-.2	-.6
Consumer energy	13.6	-4.1	3.5	3.2	.0	9.1	2.3	-.2
Other finished goods	63.7	.4	1.6	1.8	.3	2.6	.3	.3
Consumer goods	40.2	-.4	1.4	1.7	.6	2.6	.3	.4
Capital equipment	23.5	1.8	2.0	2.1	-.3	2.4	.3	.2
Intermediate materials[2]	95.6	.8	4.8	6.2	7.2	9.9	.8	.3
Excluding food and energy	82.9	1.6	5.2	6.8	8.3	9.8	.7	.2
Crude food materials	40.4	7.2	-9.4	-13.5	-1.2	-5.0	-.9	-3.0
Crude energy	34.5	-12.3	-.1	-19.2	-7.6	-3.9	5.3	1.6
Other crude materials	25.1	10.7	17.3	20.3	27.9	20.0	1.2	-.3

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

larger inventories of clothing and weaker demand. New car prices rose only slightly in May, and prices for used cars fell 0.7 percent, the first monthly decline in over three years. The CPI for services other than energy rose 0.3 percent in May, somewhat less than in the last two months. Automobile finance charges decreased 1.3 percent, the first decline since 1993, indicating that earlier interest rate hikes are now fully reflected in consumer charges.[15] Airfares rose a modest 0.4 percent in May, slowing substantially from their pace over the last three months. Owners' equivalent rent and tenants' rent increased 0.4 percent and 0.3 percent, respectively.

The CPI for food was about flat in May. Vegetable prices fell sharply, after rising in April owing to the California floods. However, much of that decline was offset by increases in prices for fresh fruits. Prices for food excluding fruits and vegetables were little changed in May, held back by declines in prices for beef, pork and poultry.

Energy prices rose 0.5 percent in May, largely owing to a 2.0 percent increase in gasoline prices at the pump. This increase in gas prices reflected the pass-through of crude oil costs earlier in the year and some supply bottlenecks stemming from the introduction of reformulated gasoline in some parts of the country. Natural gas prices fell sharply as stocks have been high in the wake of a mild winter.

Prices at earlier stages of processing point to some easing of inflationary pressures over the next few months. The PPI for intermediate materials excluding food and energy rose 0.2 percent in May, sharply lower than the 0.7 percent average monthly pace in the

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15. Finance costs have risen 26 percent in the last twelve months, adding 0.2 percentage points to the twelve-month change in core inflation.

INFLATION RATES EXCLUDING FOOD AND ENERGY

	Percent change from twelve months earlier		
	May 1993	May 1994	May 1995
CPI	3.4	2.8	3.1
Goods	2.3	1.3	1.5
Alcoholic beverages (2.0)[1]	1.4	1.3	1.6
New vehicles (6.6)	2.5	3.6	2.8
Apparel (6.6)	1.2	0.2	-2.0
House furnishings (4.5)	0.1	1.9	-0.4
Housekeeping supplies (1.4)	1.4	0.5	3.4
Medical commodities (1.7)	3.5	3.0	1.6
Entertainment (2.5)	1.4	2.4	1.4
Tobacco (2.1)	8.5	-7.3	2.1
Used cars (1.7)	9.1	4.9	14.4
Services	4.0	3.5	3.8
Owners' equivalent rent (26.3)	3.3	3.2	3.3
Tenants' rent (7.5)	2.5	2.3	2.5
Other renters' costs (2.8)	4.1	3.5	4.4
Airline fares (1.3)	13.4	3.3	5.0
Medical care (7.7)	6.9	5.0	5.2
Entertainment (3.1)	2.8	4.1	3.4
Auto financing (0.8)	-9.7	2.9	26.4
Tuition (3.4)	8.4	6.8	5.9
PPI finished goods	1.8	0.3	2.0
Consumer goods	1.8	-0.9	2.1
Capital goods, excluding computers	2.5	2.5	1.9
Computers	-15.2	-7.5	-9.9
PPI intermediate materials	1.6	1.5	7.8
PPI crude materials	9.6	6.5	18.8
<u>Factors affecting price inflation</u>			
ECI hourly compensation[2]	3.5	3.3	2.9
Goods-producing	4.0	3.2	2.9
Service-producing	3.2	3.4	2.9
Civilian unemployment rate[3,4]	6.9	6.1	5.7
Capacity utilization[3] (manufacturing)	80.5	83.2	83.0
Inflation expectations[5,6]			
Michigan Survey	4.8	4.1	3.7
Conference Board	4.7	4.2	4.2
Non-oil import price[7]	1.6	1.7	5.4
Consumer goods, excluding autos, food, and beverages	2.0	0.6	2.1
Autos	2.8	3.3	3.8

1. Relative importance weight in CPI excluding food and energy.
2. Private industry workers, periods ended in March.
3. End-of-period value.
4. Data after 1993 are not directly comparable with earlier values because of a redesign of the CPS in January 1994.
5. One-year-ahead expectations.
6. Latest reported value: June.
7. BLS import price index (not seasonally adjusted).

preceding twelve months, and prices for industrial commodities have risen modestly since the last Greenbook. The Journal of Commerce Industrial price index has increased 1.2 percent. Prices for steel scrap have slipped slightly, reversing their mild uptick in the last Greenbook. Aluminum prices seem to have stabilized at levels about ten percent below their late-1994 highs, as aluminum supply has increased recently. Demand for aluminum has also eased, due to the slowdown in economic activity and some substitution away from aluminum by can manufacturers. On the other hand, copper prices have surged in recent weeks, and are about 13 percent higher than at the time of the last Greenbook, as copper traders appear to be nervous about short-run supplies. Stocks of copper in London Mercantile Exchange warehouses have been dropping rapidly and now stand at only a four weeks' supply. The Chinese reportedly are taking advantage of the price surge to sell off their strategic copper reserve: Chinese exports of copper rose 200 percent in the first quarter.

Agricultural Conditions

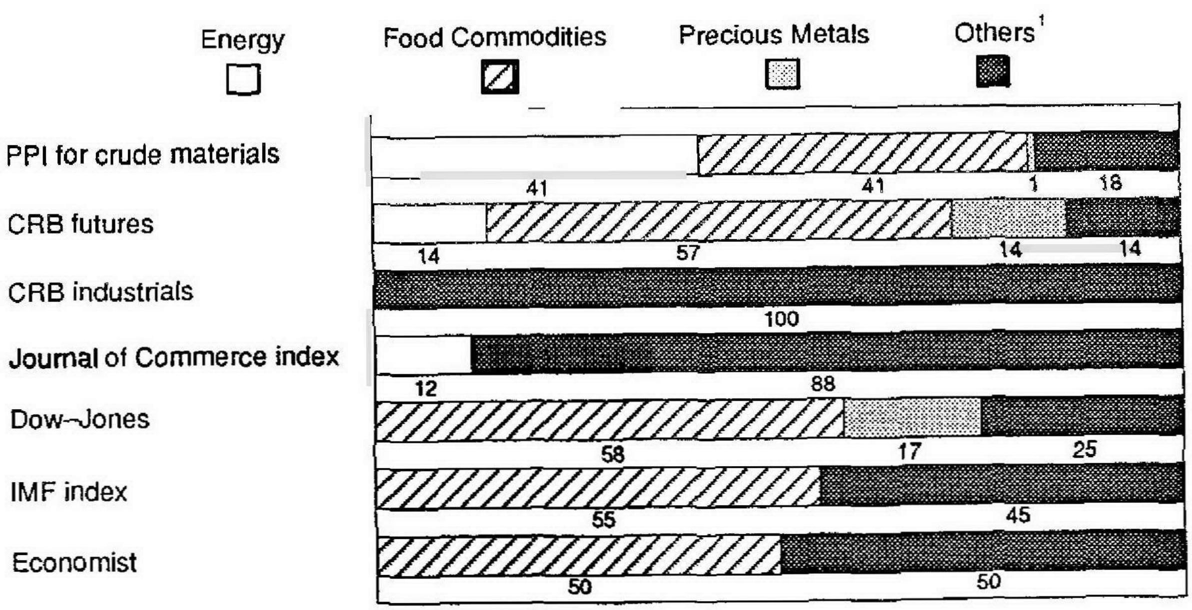
Prices for agricultural commodities have been volatile in the weeks since the last Greenbook, reflecting weather-related uncertainty. Both cash and futures prices for corn, wheat, and soybeans have risen since the last Greenbook, and it looks like harvest prices will be significantly higher than last year's levels. Prices for cotton in the cash market have fluctuated widely, as traders are concerned about short-run supply problems before the harvest of the U.S. crop; futures markets for cotton have been about steady since the last Greenbook. Prices for livestock, both cattle and hogs, have firmed modestly, but are likely to show little increase over the next six months, except for seasonal fluctuations.

COMMODITY PRICE INDEXES

	Last observ- ation	Percent change[1] 1993	1994	Dec. 94 to May 16[2]	May 16[2] to date	Memo: Year earlier to date
PPI for crude materials[3]	May.	0.1	-0.5	3.0	n.a.	0.5
Foods and feeds	May.	7.2	-9.4	-2.1	n.a.	-9.3
Energy	May.	-12.3	-0.1	6.0	n.a.	1.0
Excluding food and energy	May.	10.7	17.3	6.8	n.a.	18.8
Excluding food and energy, seasonally adjusted	May.	10.5	17.6	5.5	n.a.	18.6
Commodity Research Bureau						
Futures prices	Jun. 27	11.6	4.8	-1.9	1.2	1.8
Industrial spot prices	Jun. 20	-0.0	29.1	2.6	0.7	20.7
Journal of Commerce industrials	Jun. 27	-2.9	22.1	0.7	1.2	14.0
Metals	Jun. 27	-1.8	31.9	-3.4	4.1	22.8
Dow-Jones Spot	Jun. 27	5.1	14.8	1.5	2.8	8.5
IMF commodity index[3]	May.	2.4	15.2	18.6	n.a.	30.7
Metals	May.	-14.4	39.1	-8.1	n.a.	16.3
Nonfood agricultural	May.	0.2	14.8	11.3	n.a.	18.1
Economist (*U.S. dollar index*)	Jun. 20	9.1	31.0	-1.7	-1.2	8.5
Industrials	Jun. 20	4.4	38.6	-1.6	-1.4	13.6

Note. Not seasonally adjusted. Copyright for Journal of Commerce data is held by CIBCR, 1994.
1. Change is measured to end of period, from last observation of previous period.
2. *Week of the May Greenbook.*
3. Monthly observations. IMF index includes items not shown separately.
n.a. Not available.

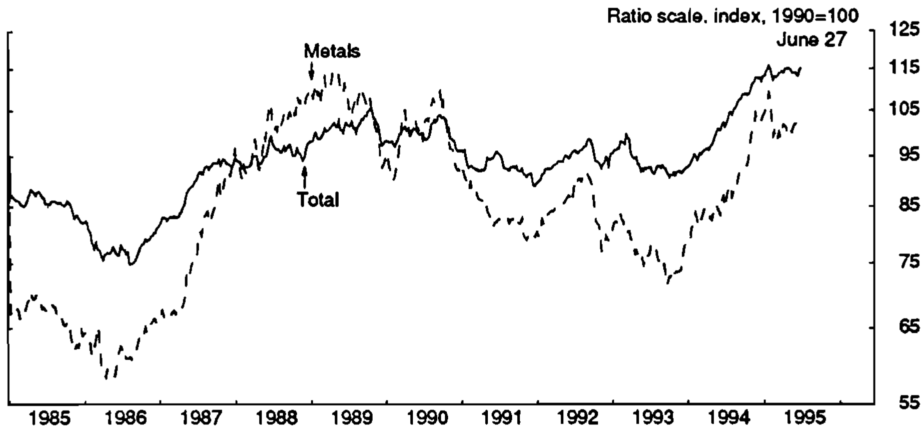
Index Weights

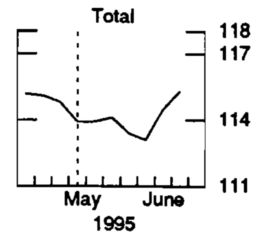


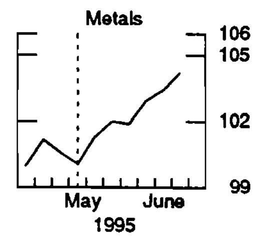
1. Forest products, industrial metals, and other industrial materials.

Commodity Price Measures

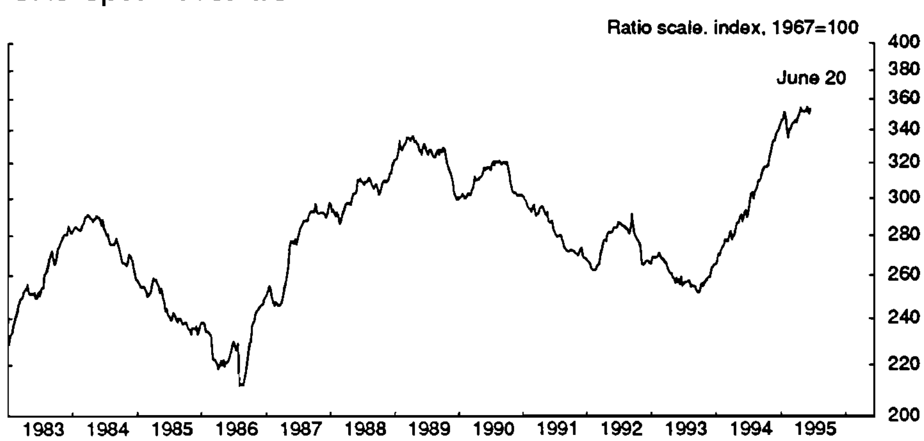
Journal of Commerce Index

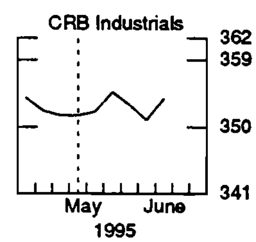




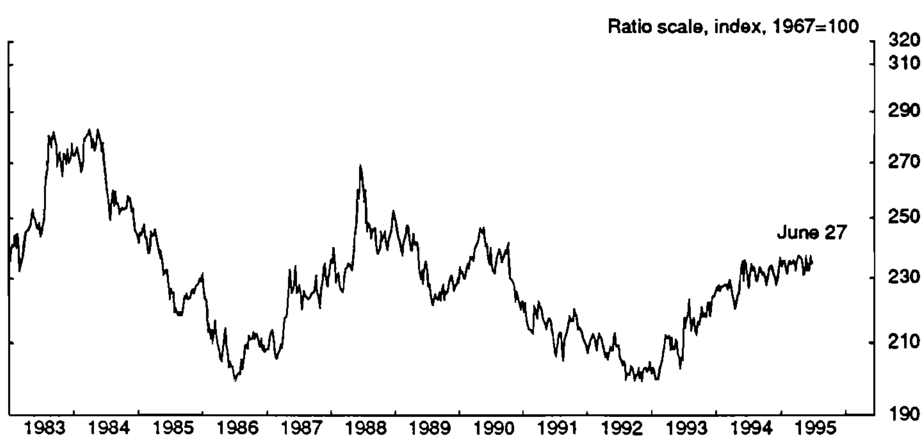


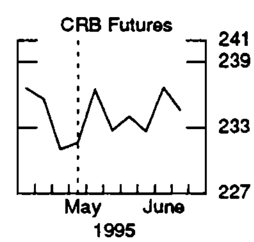
CRB Spot Industrials





CRB Futures





Note. Weekly data, Tuesdays. Vertical lines on small panels indicate week of last Greenbook. The Journal of Commerce index is based almost entirely on industrial commodities, with a small weight given to energy commodities, and the CRB spot price index consists entirely of industrial commodities, excluding energy. The CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities, and precious metals. Copyright for Journal of Commerce data is held by CIBCR, 1994.

SPOT PRICES OF SELECTED COMMODITIES

	Current price ($)	Percent change[1]: 1993	1994	To May 16[2]	May 16[2] to June 27	Memo: Year earlier to date
	INDUSTRIAL COMMODITIES					
Metals						
Copper (lb.)	1.470	-19.0	64.9	-7.8	13.1	32.4
Steel scrap (ton)	140.500	46.8	2.9	-.7	-1.4	26.0
Aluminum, London (lb.)	.805	-10.7	73.5	-8.9	1.7	24.1
Lead (lb.)	.417	3.0	20.7	-.6	.7	17.4
Zinc (lb.)	.515	-7.5	23.6	-2.4	-8.5	6.2
Tin (lb.)	4.441	-14.1	21.4	-1.0	13.0	22.8
Textiles and fibers						
Cotton (lb.)	1.056	19.6	38.5	19.0	3.2	44.3
Burlap (yd.)	.303	8.2	10.2	1.0	2.5	10.0
Miscellaneous materials						
Hides (lb.)	.890	1.3	14.2	9.7	-10.1	.6
Rubber (lb.)	.788	-7.3	75.4	15.9	-13.5	35.2
	OTHER COMMODITIES					
Precious metals						
Gold (oz.)	389.400	16.6	-1.7	.7	1.4	.7
Silver (oz.)	5.320	38.8	-5.0	13.7	-2.3	.3
Platinum (oz.)	442.500	8.0	7.5	4.2	2.4	11.0
Forest products						
Lumber (m. bdft.)	214.000	75.8	-37.1	-19.9	-8.5	-36.7
Plywood (m. sqft.)	345.000	-6.3	1.5	.6	3.9	7.1
Petroleum						
Crude oil (barrel)	16.910	-25.0	15.6	20.3	-9.9	-.5
Gasoline (gal.)	.548	-31.0	32.4	35.4	-17.6	2.5
Fuel oil (gal.)	.471	-22.4	12.7	2.0	-6.4	-6.2
Livestock						
Steers (cwt.)	63.000	-7.3	-3.4	-10.0	.0	4.1
Hogs (cwt.)	46.000	.6	-12.9	8.5	19.5	5.7
Broilers (lb.)	.559	6.1	-4.9	7.7	5.9	10.0
U.S. farm crops						
Corn (bu.)	2.585	41.7	-23.2	11.8	4.9	2.8
Wheat (bu.)	4.900	5.8	11.4	-4.6	17.9	45.6
Soybeans (bu.)	5.735	24.5	-19.6	-.3	3.1	-14.7
Other foodstuffs						
Coffee (lb.)	1.415	-2.3	153.1	-1.2	-12.2	-16.4
Memo:						
Exchange value of the dollar (March 1973=100)	81.673	3.4	-5.5	-7.0	-2.4	-8.8
Yield on Treasury bill, 3-month[3]	5.420	-14	247	16	-27	124

1. Changes, if not specified, are to the last week of the year indicated and from the last week of the preceding year.
2. Week of the May Greenbook.
3. Changes are in basis points.

The Agriculture Department's estimates of crop production for 1995 indicate much lower supplies of corn and wheat, as planting delays earlier in the year led to a downward revision in production estimates for both crops. The real value of output from the twelve major crops is now projected to decline about 11 percent. If these projections were to turn out to be accurate, stocks at the end of 1995 would be much lower than the average in recent years, indicating higher prices for these commodities. Projections of cotton production, on the other hand, indicate about a 7 percent rise in 1995. While output of crops will be lower this year, higher prices will offset some of the loss to farmers.

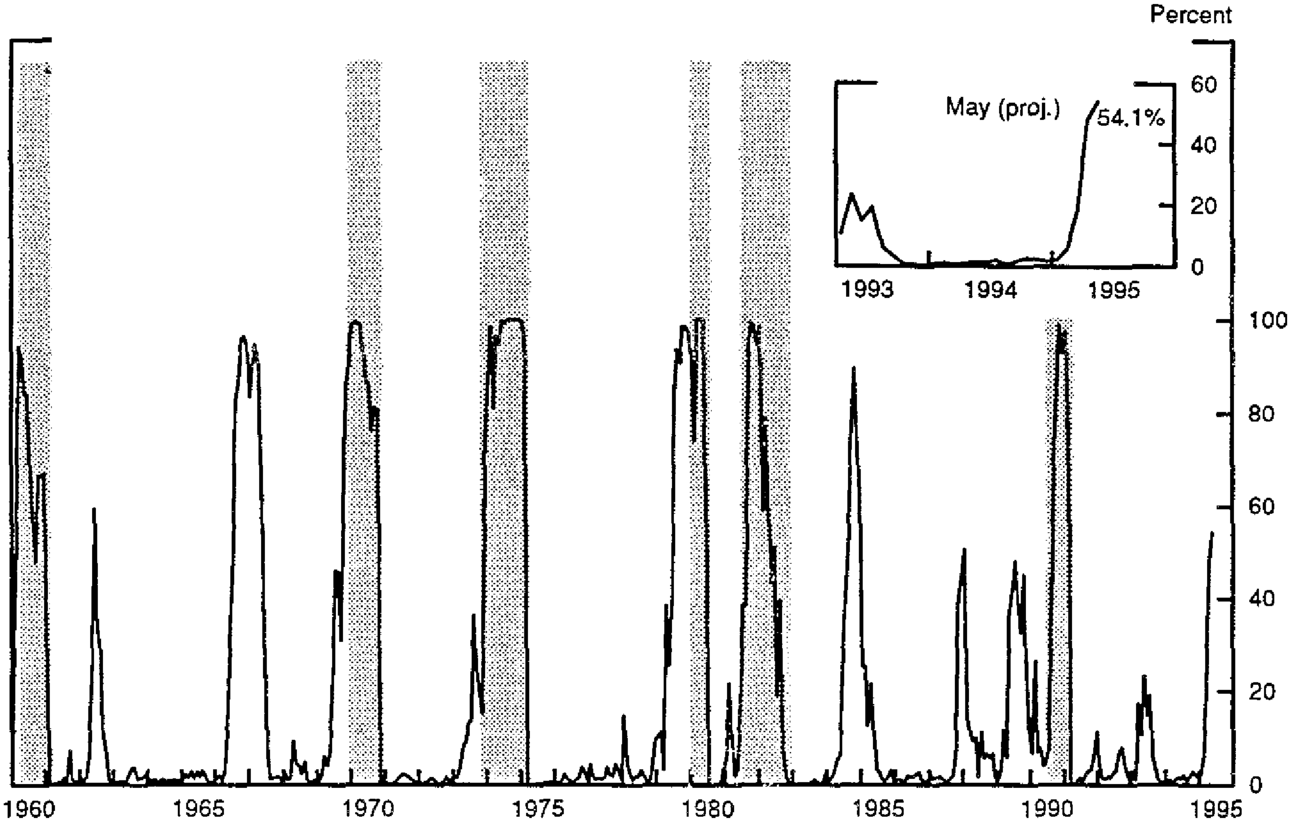
U.S. CROP PRODUCTION[1]

	1992	1993	1994	Date of USDA projections for 1995: May 12	Date of USDA projections for 1995: June 12
	Billions of bushels				
Corn	9.48	6.34	10.10	8.60	7.90
Soybeans	2.19	1.87	2.56	2.20	2.21
Wheat	2.46	2.40	2.32	2.32	2.26
Sorghum	.88	.53	.66	.56	.56
Oats	.29	.21	.23	.20	.20
Barley	.46	.40	.38	.38	.38
	Billions of hundredweight				
Rice	.18	.16	.20	.18	.18
	Millions of bales				
Cotton	16.22	16.13	19.66	21.00	21.00
	Billions of 1987 dollars				
Memo: Value, 12 crops[2]	47.03	38.62	49.67	45.42	44.22
BEA crop output	79.80	72.89	81.10		

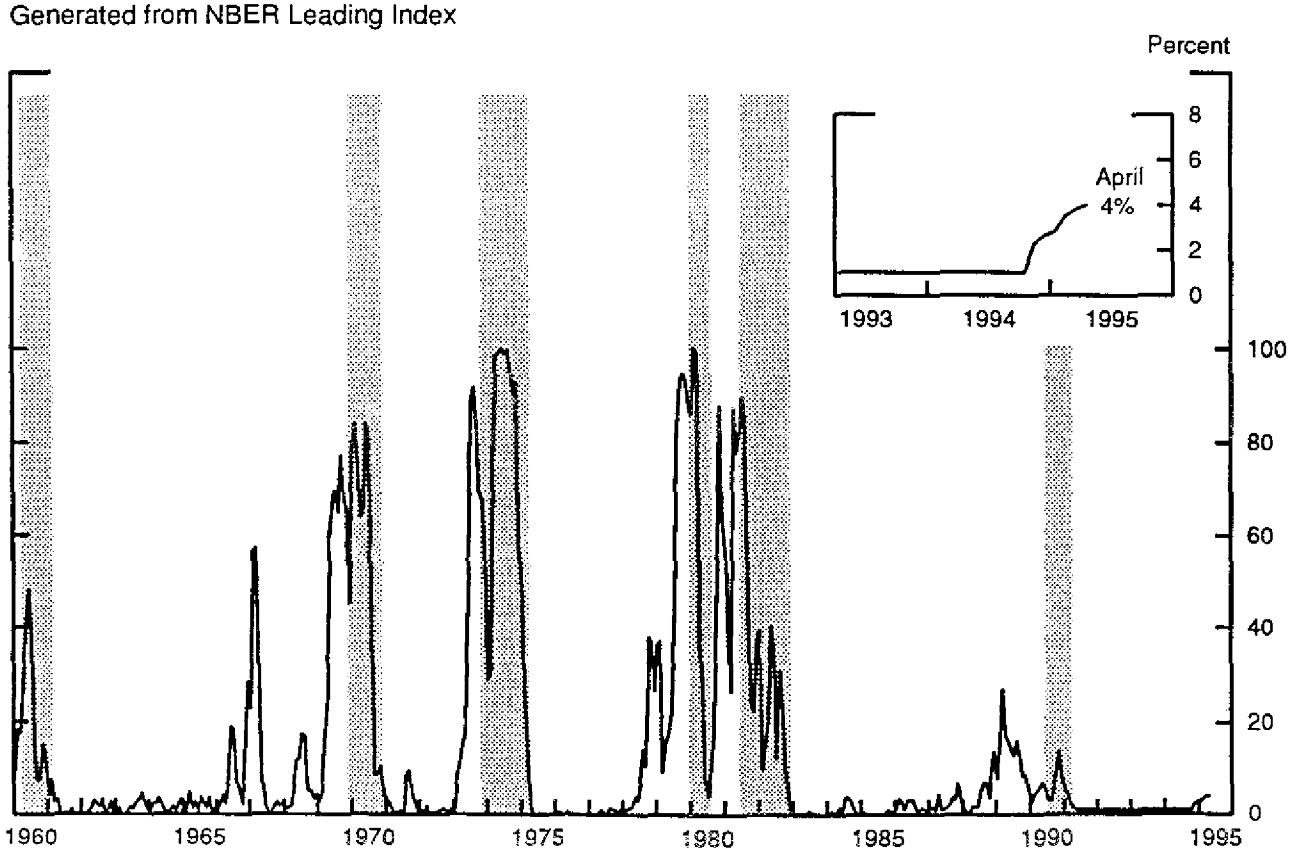
1. Data are from the U.S. Department of Agriculture.
2. Calculated by the staff from USDA data. The twelve crops include those listed above, plus four crops for which USDA has not yet projected production: peanuts, tobacco, sugar beets and sugar cane.

Probability of a Recession

Generated from Commerce Leading Index



Generated from NBER Leading Index



Note. Each probability represents the likelihood that a recession will begin during the next six months.

Recession Probabilities

The latest readings on recession probability measures based on indexes of leading economic indicators are mixed. The measure based on the Commerce Department's April index of leading economic indicators (LEI) puts the probability of a recession starting during the April-September period at 48 percent. Based on the available data for May, the staff expects the LEI to fall about 0.2 percent and the probability of recession (over the May-October period) to rise to 54 percent.

In contrast, the April reading on the National Bureau of Economic Research (NBER) measure, which gives a heavier weight to financial variables, put the probability of recession at only 4 percent.

As may be seen in the charts, these leading indicator measures have been far from infallible. At this point, they certainly don't provide any clear reading on whether the recent weakness in the economy is the beginning of a downturn of recession proportions or just another of the brief pauses that have occurred in the midst of previous expansions.

DOMESTIC FINANCIAL DEVELOPMENTS

SELECTED FINANCIAL MARKET QUOTATIONS [1]

(Percent except as noted)

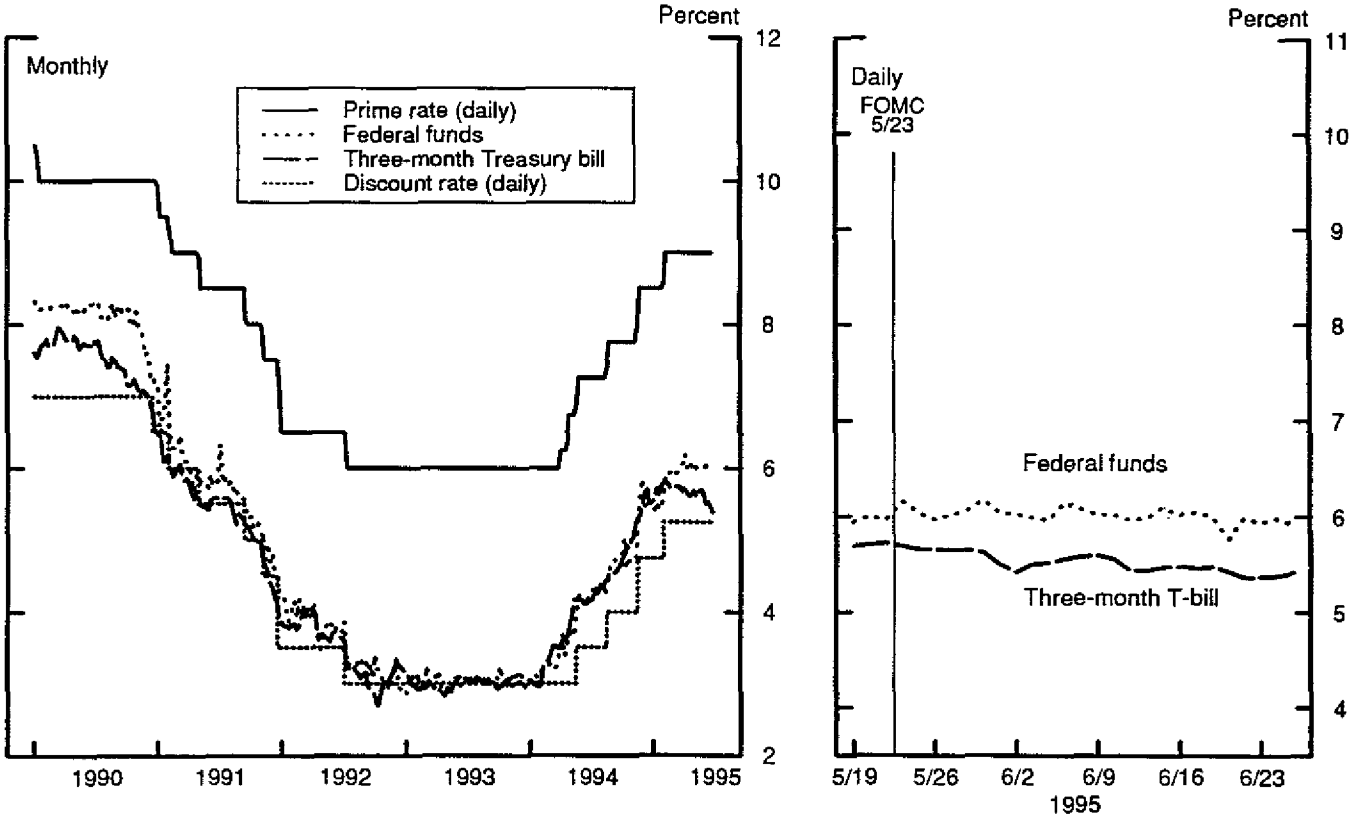
Instrument	1994 Feb 3	1994 High	1995 FOMC, May 23	1995 Jun 27	Change to Jun 27, 1995: From 1994 Feb 3	From 1994 high	From FOMC, May 23
SHORT-TERM RATES							
Federal funds [2]	3.07	5.66	5.99	5.96	2.89	.30	-.03
Treasury bills [3]							
3-month	3.13	5.78	5.73	5.42	2.29	-.36	-.31
6-month	3.27	6.38	5.69	5.37	2.10	-1.01	-.32
1-year	3.52	6.84	5.63	5.32	1.80	-1.52	-.31
Commercial paper							
1-month	3.16	6.13	6.05	6.07	2.91	-.06	.02
3-month	3.25	6.32	6.06	5.92	2.67	-.40	-.14
Large negotiable CDs [3]							
1-month	3.11	6.10	5.99	6.01	2.90	-.09	.02
3-month	3.25	6.39	6.03	5.92	2.67	-.47	-.11
6-month	3.41	6.89	6.07	5.79	2.38	-1.10	-.28
Eurodollar deposits [4]							
1-month	3.06	6.06	6.00	5.97	2.91	-.09	-.03
3-month	3.25	6.38	6.03	5.84	2.59	-.54	-.19
Bank prime rate	6.00	8.50	9.00	9.00	3.00	.50	.00
INTERMEDIATE- AND LONG-TERM RATES							
U.S. Treasury (constant maturity)							
3-year	4.60	7.82	6.22	5.80	1.20	-2.02	-.42
10-year	5.81	8.04	6.57	6.15	.34	-1.89	-.42
30-year	6.31	8.16	6.87	6.56	.25	-1.60	-.31
Municipal revenue [5] (Bond Buyer)	5.49	7.37	6.15	6.05	.56	-1.32	-.10
Corporate--A utility, recently offered	7.35	9.05	7.83	7.55	.20	-1.50	-.28
Home mortgages [6]							
FHLMC 30-yr. fixed rate	6.97	9.25	7.83	7.53	.56	-1.72	-.30
FHLMC 1-yr. adjustable rate	4.12	6.79	6.10	5.84	1.72	-.95	-.26

Stock exchange index	Record high Level	Record high Date	1989 Low, Jan. 3	1995 FOMC, May 23	1995 Jun 27	Percentage change to Jun 27: From record high	From 1989 low	From FOMC, May 23
Dow-Jones Industrial	4589.64	6/22/95	2144.64	4436.44	4542.61	-1.02	111.81	2.39
NYSE Composite	294.93	6/22/95	154.00	283.80	290.75	-1.42	88.80	2.45
NASDAQ (OTC)	940.09	6/22/95	378.56	879.64	919.56	-2.18	142.91	4.54
Wilshire	5400.87	6/22/95	2718.59	5172.35	5318.65	-1.52	95.64	2.83

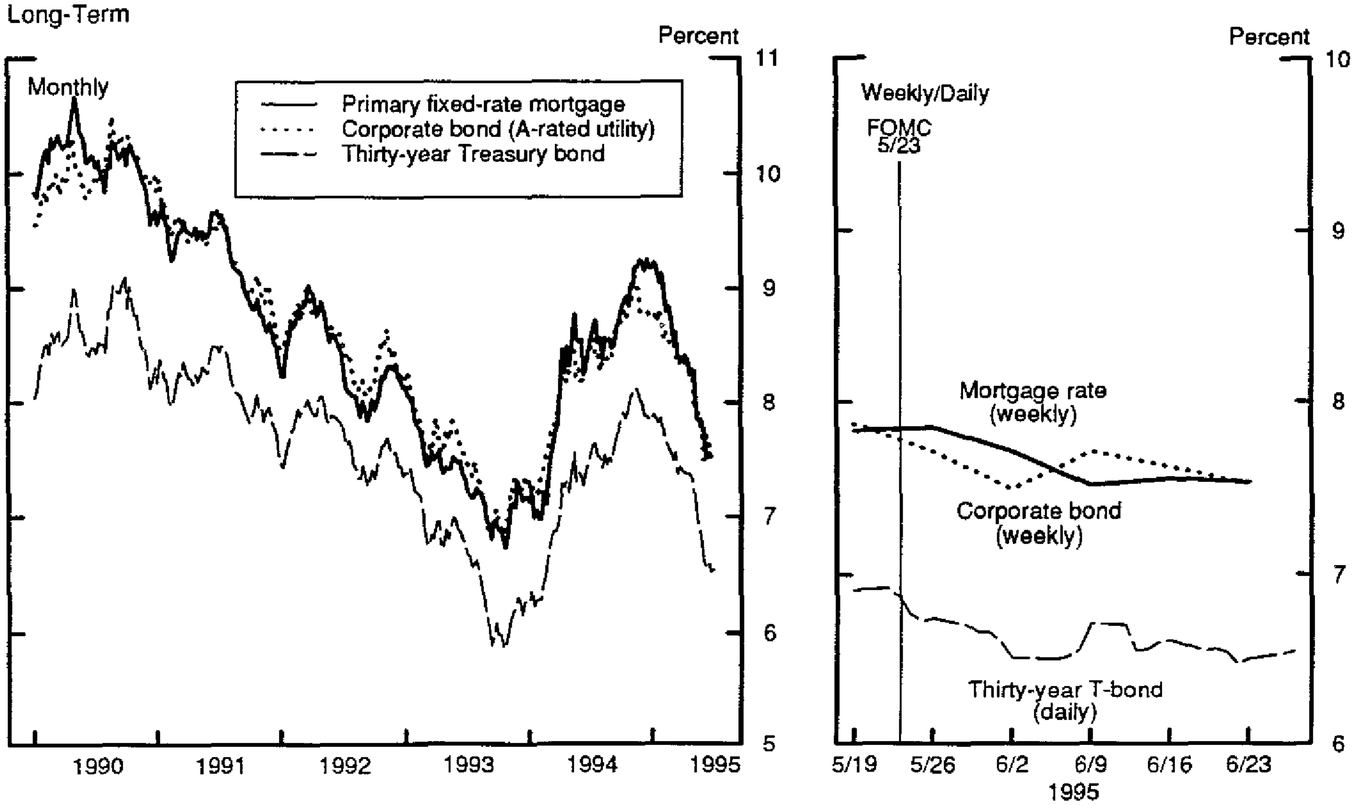
1. One-day quotes except as noted.
2. Average for two-week reserve maintenance period closest to date shown. Last observation is average to date for maintenance period ending July 5, 1995.
3. Secondary market.
4. Bid rates for Eurodollar deposits at 11 a.m. London time.
5. Most recent observation based on one-day Thursday quote.
6. Quotes for week ending Friday previous to date shown.

Selected Interest Rates

Short-Term



Long-Term

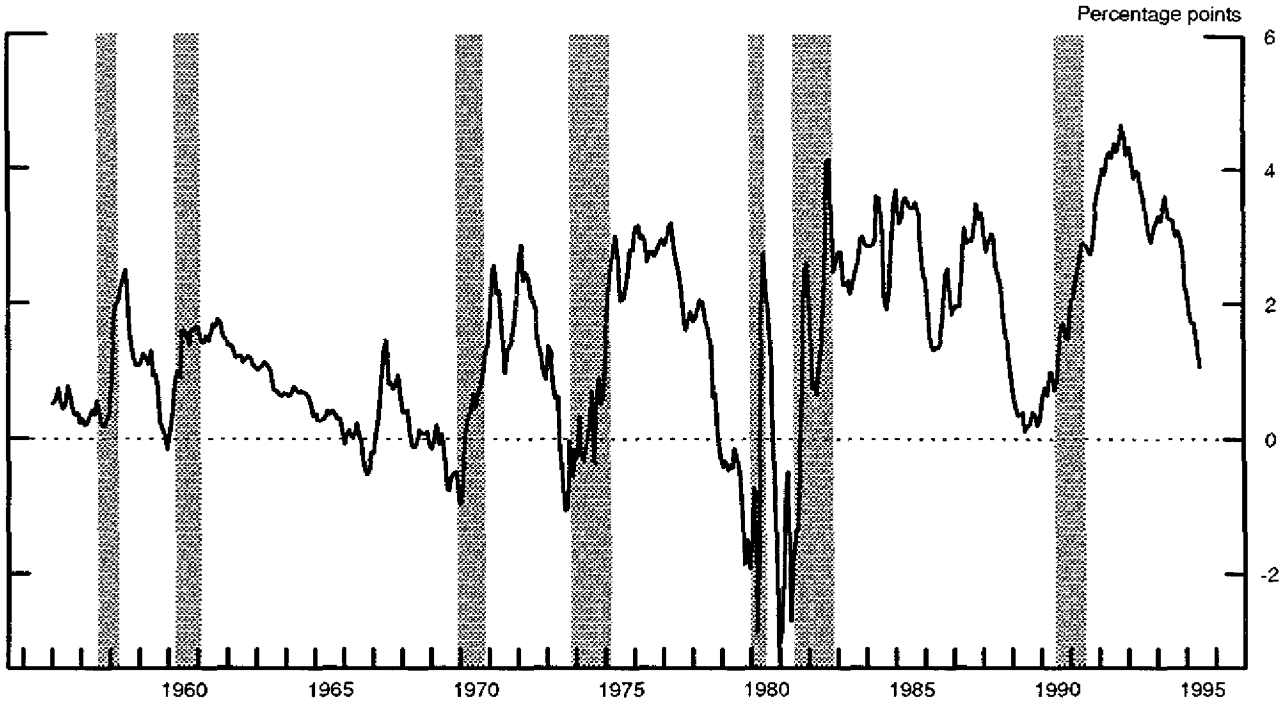


Market interest rates have declined substantially in recent weeks on evidence of economic weakness and hints in remarks by System officials that an easing of monetary policy might be at hand. On balance, Treasury yields moved down 30 to 40 basis points since the May 23 FOMC meeting, with the largest declines at intermediate maturities. Declines in private-market interest rates have been slightly smaller than those on Treasuries. But if that relative movement reflected concern about the financial strength of firms in a softer economy, such sentiment did not seem to weigh heavily on the equity markets: Major stock market indexes have posted gains of about 2-1/2 percent during the intermeeting period, with most setting all-time highs.

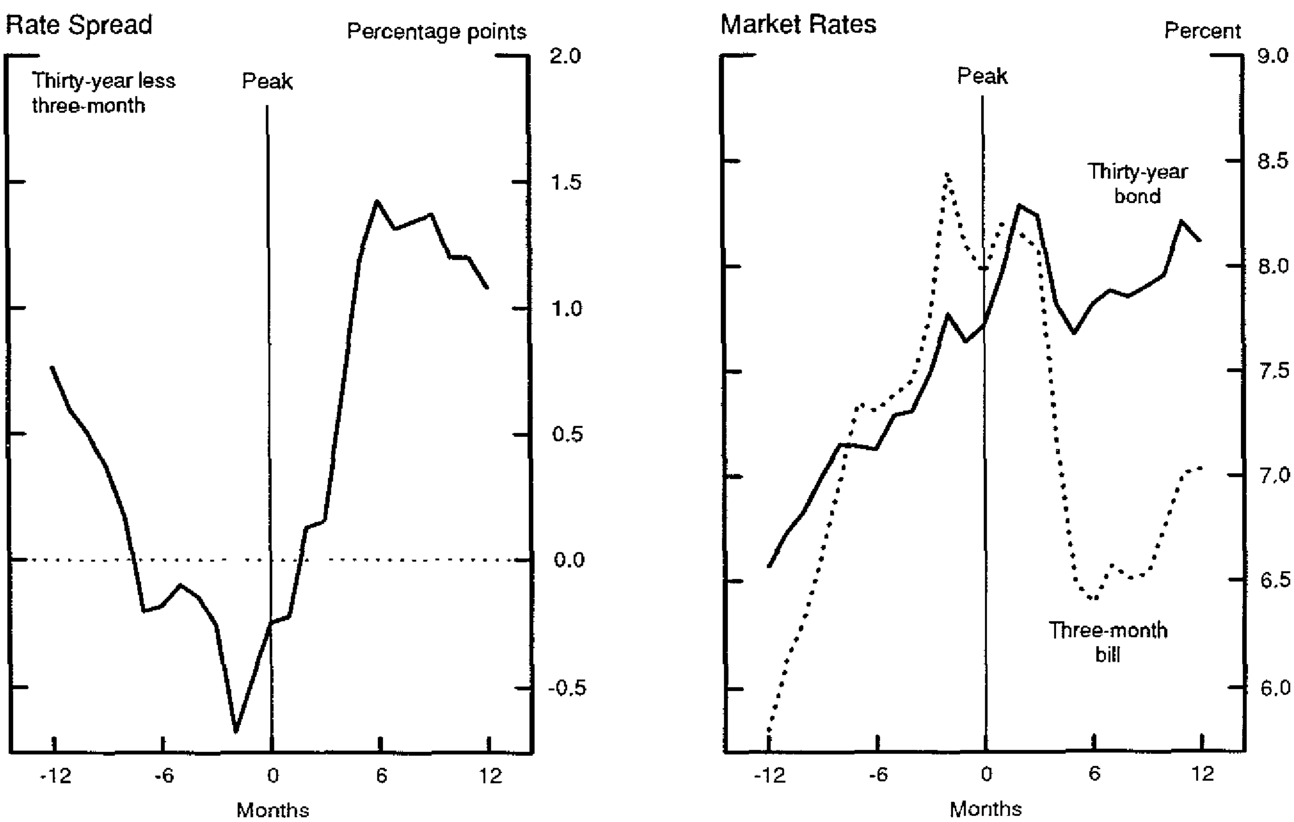
Credit demands of the federal and state and local governments have slackened in the second quarter, but borrowing by the private sector has remained strong. Nonfinancial businesses jumped back into the bond market in May and June and lifted gross issuance to the highest volume in more than a year. Business borrowing from banks was also brisk early in the period, but appears to have tapered off in the past several weeks, and commercial paper has contracted since early May. The shift toward bond issuance has lessened demands on banks and the paper market, but the back-off in shorter-term credit could also be signalling a reduction in financing for inventory investment. In the household sector, data beyond April are scant, but it is likely that overall borrowing has remained moderate in the second quarter.

M2 and M3 accelerated in May and appear to be expanding at double-digit rates in June. The former has moved to the upper portion of its annual range, while the latter has climbed further

Spread Between the Thirty-Year Treasury Yield and the Three-Month Bill Rate



Average Experience around Peaks of the Business Cycle



Note. Twenty-year Treasury rate used before April 1977 Bottom panels show the average level of a variable across the seven NBER peaks since 1955.

above the upper bound of its growth cone. In contrast, narrow monetary measures, such as total reserves and M1, have remained weak, though that pattern has been exaggerated to a degree by the spread of sweep facilities.

Rate Expectations and Yield Curves

Just prior to the May 23 FOMC meeting, quotes on futures contracts for shorter-term interest rates were essentially flat over both intermediate and near-term periods; with due allowance for term premia, this pattern suggested an expectation that policy might ease by the fall. At present, futures prices anticipate a substantial easing by that time.

The flattening of the yield curve beyond the near term has been substantial. Indeed, at times of late an investor had to go to maturities beyond seven years to find a Treasury yield above the 6 percent intended federal funds rate. Nonetheless, the spread of the thirty-year bond rate over the three-month bill rate (chart) is still around 115 basis points. This spread is a good deal wider than is typical before an economic recession. In the average experience around the peaks of the seven business cycles since 1955, the yield curve generally began to flatten as much as one year prior to the onset of recession, and the spread moved distinctly into negative territory well before the economic peak (chart). Moreover, the inversion of the yield curve observed before recessions generally occurred because long-term rates rose by less than short-term rates, whereas the flattening that has occurred since early this year has come from a rally at the long end of the market.

Monetary Aggregates and Bank Credit

M2 grew at an annual rate above 5 percent in May and appears to have strengthened further to an 11 percent pace in June, placing the aggregate above the midpoint of its annual range of 1 percent

MONETARY AGGREGATES
(Based on seasonally adjusted data)

Aggregate or component	1994	1995 Q1	1995 Q2 (pe)	1995 Apr.	1995 May	1995 June (pe)	1994:Q4 to June 95 (pe)	Level (bil. $) May 95
Aggregate	Percentage change (annual rate)[1]							
1. M1	2.3	0.0	-1	2.0	-7.1	0	-¾	1142.9
2. M2	1.0	1.6	4¼	4.1	5.2	11	3¾	3657.9
3. M3	1.4	4.4	6¾	5.9	8.0	12	6¼	4408.7
Selected components								
4. Currency	10.2	8.2	8¼	10.6	7.9	-1	7½	368.1
5. Demand deposits	0.4	0.6	-¾	-6.3	-1.9	19	1½	380.6
6. Other checkable deposits	-2.1	-7.7	-10¼	0.9	-26.2	-17	-10½	385.0
7. M2 minus M1	0.4	2.4	6½	5.2	10.8	16	6	2515.0
8. Savings deposits	-4.5	-15.7	-9¾	-13.7	0.6	9	-10	1081.9
9. Small time deposits	2.4	22.9	24½	25.3	18.2	12	23¼	909.8
10. Retail money market funds	7.3	7.9	17½	15.7	28.2	56	18	405.3
11. Overnight RPs, n.s.a.	14.1	14.4	-8¼	-30.4	4.3	0	2¾	84.9
12. Overnight Eurodollars, n.s.a.	42.2	24.5	-34	-23.5	-4.0	12	-4	30.0
13. M3 minus M2	3.6	18.9	19¾	14.8	22.0	16	19¾	750.8
14. Large time deposits, net[2]	7.1	14.4	13¾	3.2	18.1	7	14	384.5
15. Institution-only money market mutual funds	-8.2	10.0	26¾	24.8	11.8	64	23¼	194.8
16. Term RPs, n.s.a.	6.6	31.4	27¼	33.1	51.9	1	29	120.6
17. Term Eurodollars, n.s.a.	16.1	29.6	33	31.7	19.3	-4	28½	63.2
Memo								
18 Monetary base	8.4	6.3	6½	7.6	7.3	-1	5¾	430.7
19. Household M2[3]	0.5	1.0	5	5.8	5.6	12	4	3149.7
	Average monthly change (billions of dollars)[4]							
Memo								
20. Managed liabilities at commercial banks (lines 21 + 22)	14.3	27.9	11	19.1	17.2	-12	. . .	1136.9
21. Large time deposits, gross	2.1	5.1	5½	0.0	8.8	5	. . .	400.9
22. Nondeposit funds	12.1	22.8	5½	19.1	8.4	-17	. . .	736.0
23. Net due to related foreign institutions	7.5	9.4	-2¼	-6.4	5.1	3	. . .	240.0
24 Other[5]	4.6	13.4	7¾	25.4	3.4	-21	. . .	496.1
25. U.S. government deposits at commercial banks	0.0	-0.8	¾	2.6	2.3	1	. . .	20.5

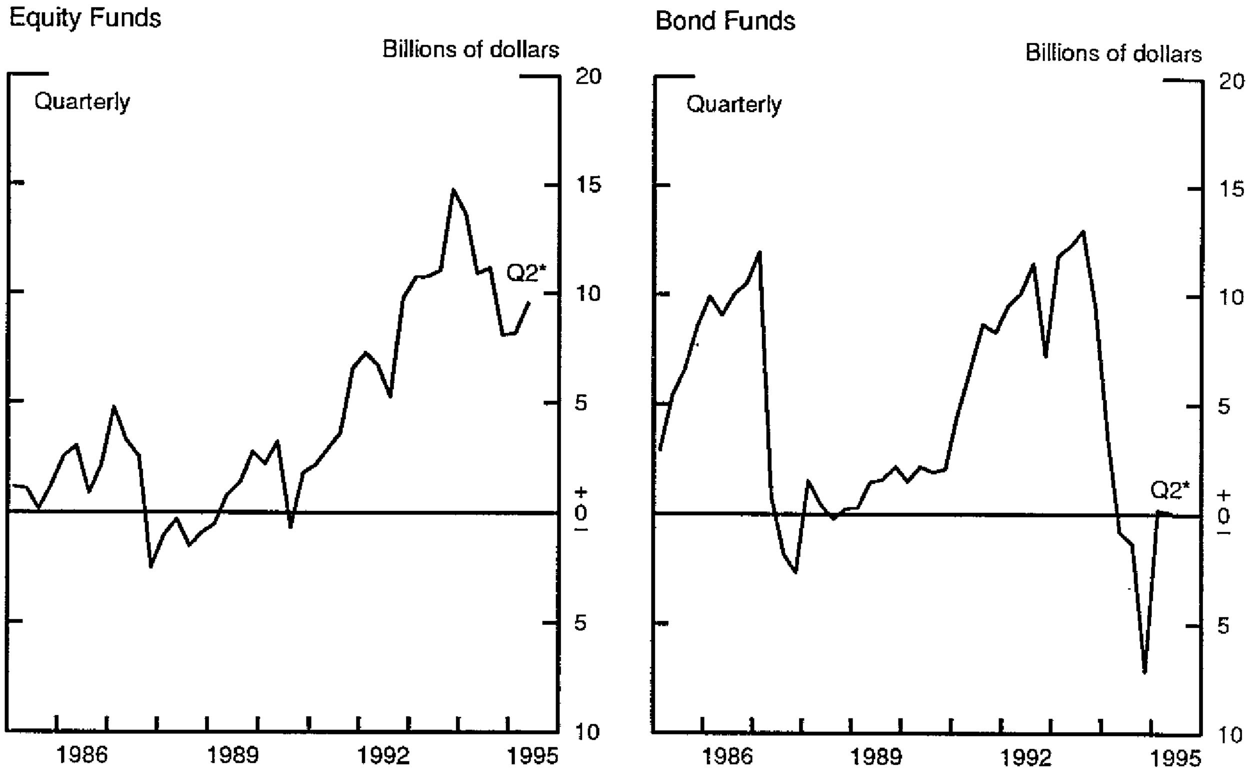
1. For the years shown, fourth quarter-to-fourth quarter percent change. For the quarters shown, based on quarterly averages.
2. Net of holdings of depository institutions, money market mutual funds, U.S. government, and foreign banks and official institutions.
3. Sum of seasonally adjusted currency, retail money funds, and other checkable, savings, and small time deposits.
4. For the years shown, "average monthly change" is the fourth quarter-to-fourth quarter dollar change, divided by 12. For the quarters shown, it is the quarter-to-quarter dollar change, divided by 3.
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.
pe Preliminary estimate. n.s.a. Not seasonally adjusted.

to 5 percent. M3 growth also picked up in May, to an 8 percent pace, and remained well above the upper bound of its annual range of 0 percent to 4 percent. Available data for June suggest that M3 growth will be a brisk 12 percent for the month, owing primarily to a surge of flows into institution-only money market mutual funds. This volatile and interest-sensitive component was likely boosted by the decline in money market rates that made money funds relatively more attractive. Given the pickup in M2 and M3 and the likely prospects for nominal income in the second quarter, the velocities of the broad aggregates appear to have fallen for the first time in more than four years. Meanwhile, M1 is expected to be about flat in June after having contracted in May, as implementation of sweep programs in May and early June reduced other checkable deposits. The sweep programs have no effect on M2, however.

The staff believes that the recent pickup in M2 relative to nominal income primarily reflects portfolio reallocations, in part responding to declines in market rates relative to returns available on M2 assets. The strength in M2 over the past two months has been driven by inflows to retail money market mutual funds and small time deposits. Money funds grew at a 28 percent pace in May and are estimated to have surged to more than a 50 percent growth rate in June. When market rates fall sharply, as they have in recent months, returns on money funds lag and thus become attractive relative to other short-term investments. Indeed, with the front end of the yield curve currently inverted, money funds are paying returns above the rates that banks offer on five-year certificates of deposit. The competition from money funds may also account for some of the recent weakness in net noncompetitive tenders at Treasury auctions, which appear to be averaging less than $1 billion

Net Sales of Equity and Bond Mutual Funds

(Monthly rate, not seasonally adjusted)



* Value for 1995:Q2 is a staff estimate.

NET SALES OF MUTUAL FUNDS CLASSIFIED BY TYPE
(Billions of dollars, monthly rate, not seasonally adjusted)

	1994	1995				Memo:
	Q4	Q1	Q2[e]	May	Jun.[e]	May Assets
Total stock	8.1	8.2	9.5	9.0	8.6	1,025.4
International	2.0	.4	1.3	1.3	.5	175.0
Domestic	6.1	7.8	8.2	7.7	8.1	850.4
Total bond	-7.1	.2	.0	2.4	-2.8	743.9
GNMA	-1.2	-.7	-.1	-.1	-.3	54.7
Government	-2.0	-.6	-.6	-.5	-.6	87.7
High-yield	.0	1.0	.5	.9	-.3	52.9
Tax-exempt	-3.2	.3	-.6	.9	-1.9	246.1
Income	.2	.8	.8	1.2	.5	241.1
Other	-.9	-.6	.0	.0	-.2	61.4
Total money fund	9.8	7.7	16.6	20.0	26.7	675.8
Taxable	9.4	6.7	16.3	17.8	25.3	556.9
Tax-exempt	.4	1.0	.3	2.2	1.4	118.9

e Staff estimate

Source. Investment Company Institute.

at a monthly rate this quarter, compared with a six-year high of nearly $4 billion a month in the first quarter.

Small time deposits continue to register strong growth, at an 18 percent pace in May and at a 12 percent rate in May. Rates paid on these deposits have fallen less than those on Treasury securities of comparable maturities and remain well above rates paid on liquid deposits. Even so, growth of small time deposits is below the nearly 25 percent pace of earlier in the year.

Outside of the monetary aggregates, flows into long-term mutual funds picked up in the second quarter (chart). Net purchases of equity mutual funds shares eased slightly in May and June but remained above their pace during the first quarter. Net flows into bond funds remained weak in May after outflows last year and a flat first quarter. Municipal and income funds grew modestly, but much of the rise in assets in these funds likely reflects reinvested dividends rather than new money from investors. Inflows into high-yield bond funds continued in May. More recently, municipal and high-yield funds have reversed these gains, and, on balance, bond funds posted modest outflows over the first three weeks of June.

Growth of bank credit softened in May and appears to have eased further in June. The decline in growth in May was attributable to a contraction in holdings of securities, as the marking to market of derivatives contracts reduced reported holdings in the other securities category.

Loan expansion remained robust in May, at a 14 percent pace, but slackened over the month, and appears to have slowed in June. The softening is particularly pronounced in business loans, which had increased near a 15 percent pace in April and May. Real estate loans in May posted their smallest advance of the year, and their

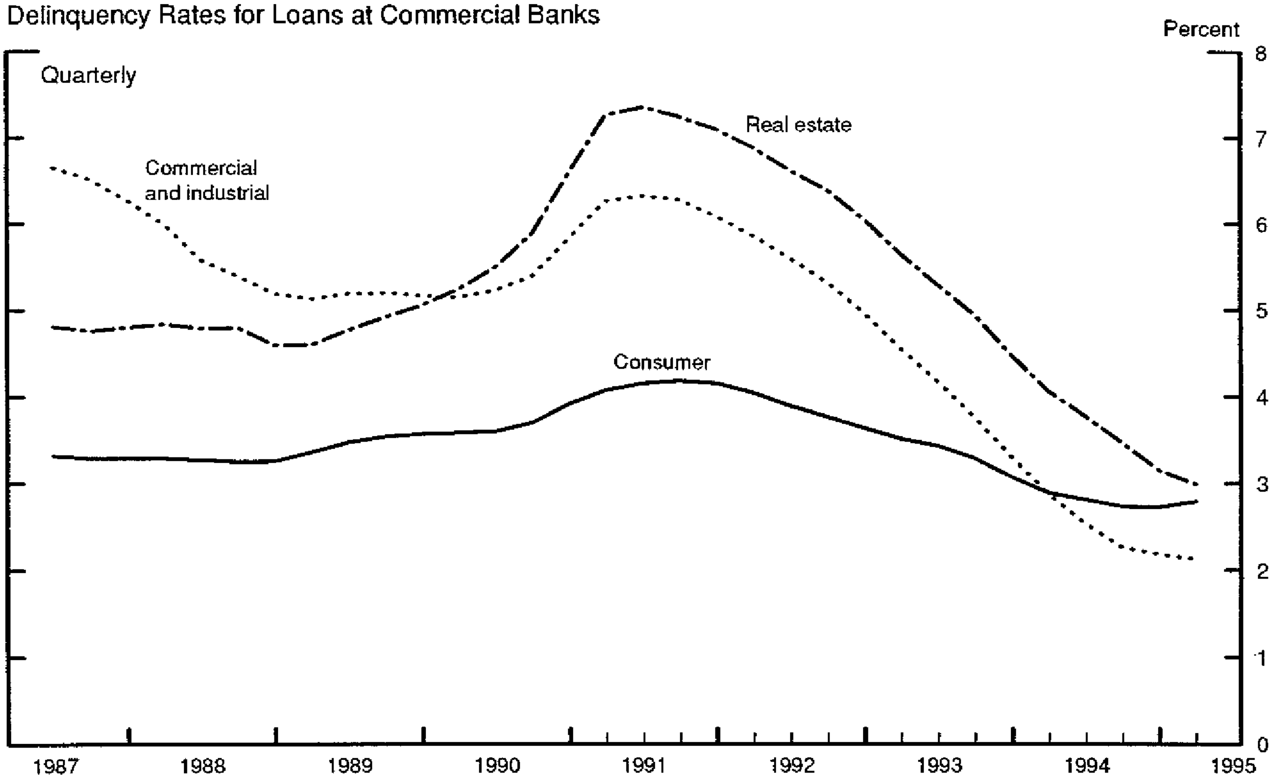
Commecial Bank Credit and Short- and Intermediate-Term Business Credit
(Percentage change; seasonally adjusted annual rate)[1]

Type of credit	1994	1994 Q4	1995 Q1	1995 Mar	1995 Apr	1995 May	Level, May 1995 (billions of $)
	Commercial bank credit						
1. Total loans and securities	6.8	4.0	7.8	8.3	14.1	9.2	3,452.1
2. Securities	4.9	-7.4	-5.0	3.3	16.5	-3.8	949.9
3. U.S. government	0.0	-11.2	-6.1	-20.8	0.0	4.8	707.3
4. Other	23.8	5.2	-1.8	80.5	66.3	-28.0	242.6
5. Loans	7.6	8.8	13.0	10.2	13.2	14.2	2,502.2
6. Business	9.2	10.3	17.1	6.3	16.0	14.6	690.4
7. Real estate	6.5	7.8	12.0	6.7	8.9	5.1	1,040.5
8. Consumer	15.2	16.4	12.7	14.4	15.2	4.3	472.6
9. Security	-17.2	-20.0	-9.1	33.6	60.3	185.2	84.5
10. Other	3.3	3.4	13.4	23.9	5.7	21.1	214.3
	Short- and intermediate-term business credit						
11. Business loans net of bankers acceptances	9.4	10.9	18.2	7.1	15.5	16.0	683.9
12. Loans at foreign branches[2]	5.1	-3.5	17.6	-5.0	45.6	19.5	25.0
13. Sum of lines 11 and 12	9.3	10.6	18.1	6.6	16.5	16.1	708.9
14. Commercial paper issued by nonfinancial firms	1.2	25.0	22.1	20.4	36.7	20.8	181.6
15. Sum of lines 13 and 14	7.6	13.3	18.9	9.4	20.6	17.1	890.5
16. Bankers acceptances, U.S. trade-related[3,4]	-8.3	-25.7	-21.2	20.2	-6.6	n.a.	18.0[5]
17. Loans at finance companies[4]	12.2	17.0	20.6	17.7	14.2	n.a.	376.6[5]
18. Total (sum of lines 15, 16, and 17)	8.6	13.7	18.8	12.0	18.3	n.a.	1,272.6[5]

1. Except as noted, levels are averages of Wednesday data and percentage changes are based on averages of Wednesday data. For years, "percentage change" is percentage change in quarterly average from fourth quarter of preceding year to fourth quarter of specified year. For quarters, it is the percentage change in quarterly average from preceding quarter to specified quarter, annualized. Data are adjusted for breaks caused by reclassification.
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. Levels and changes are based on averages of month-end data.
5. April 1995.
n.a. Not available.

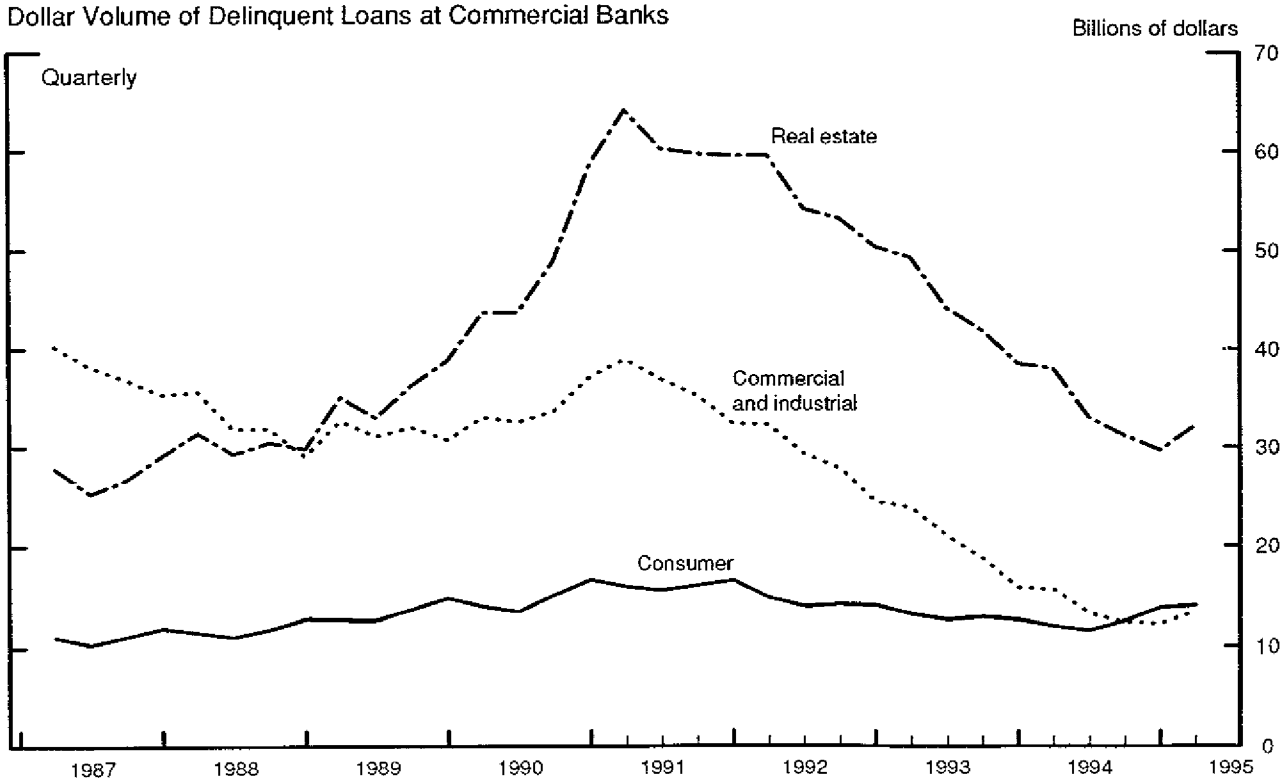
Loan Quality at Commercial Banks

Delinquency Rates for Loans at Commercial Banks



Note. The data are seasonally adjusted. Data for 1995:Q1 are preliminary.

Dollar Volume of Delinquent Loans at Commercial Banks



Note. The data are not seasonally adjusted. Data for 1995:Q1 are preliminary.

GROSS OFFERINGS OF SECURITIES BY U.S. CORPORATIONS[1]
(Billions of dollars; monthly rates, not seasonally adjusted)

Type of security	1993	1994	1994 Q4	1995 Q1	1995 Mar.	1995 Apr.p	1995 Mayp
All U.S. corporations	52.89	40.61	32.27	39.71	40.21	29.59	46.34
Stocks[2]	9.12	5.50	4.04	3.83	3.23	3.59	5.34
Bonds	43.77	35.11	28.23	35.88	36.98	26.00	41.00
Nonfinancial corporations							
Stocks[2]	5.04	3.14	3.02	2.78	2.44	2.71	3.24
Sold in U.S.	4.64	2.92	2.79	2.51	2.13	2.61	2.95
Utility	1.05	.37	.23	.38	.22	.19	.36
Industrial	3.82	2.55	2.56	2.13	1.91	2.42	2.59
Sold abroad	.40	.22	.23	.27	.31	.10	.30
Bonds	16.19	7.35	5.41	6.65	5.75	6.33	12.71
Sold in U.S.	15.55	6.44	4.30	5.35	4.68	5.70	11.00
Utility	7.34	2.19	1.09	1.31	1.63	1.77	5.10
Industrial	8.21	4.26	3.21	4.04	3.05	3.94	5.90
Sold abroad	.64	.90	1.11	1.30	1.07	.63	1.71
By quality[3]							
Aaa and Aa	2.56	.58	.58	.69	.48	.78	2.08
A and Baa	8.70	3.82	2.59	3.38	3.37	3.98	6.08
Less than Baa	4.17	2.01	1.13	1.24	.73	.93	2.73
Unrated or rating unknown	.09	.01	n.a.	.01	.01	.00	.10
Financial corporations							
Stocks[2]	4.08	2.36	1.02	1.05	.79	.88	2.10
Sold in U.S.	3.83	2.11	.99	1.04	.79	.88	2.10
Sold abroad	.25	.25	.04	.01	.00	.00	.00
Bonds	27.58	27.76	22.82	29.23	31.23	19.67	28.29
Sold in U.S.	25.02	23.98	19.12	23.16	28.08	16.30	23.00
Sold abroad	2.56	3.78	3.70	6.08	3.14	3.37	5.29
By quality[3]							
Aaa and Aa	1.78	3.72	2.69	3.95	4.37	2.14	2.92
A and Baa	9.01	9.02	7.73	10.83	10.06	7.72	11.27
Less than Baa	.49	.31	.20	.04	.04	.15	.00
Unrated or rating unknown	.08	.10	.28	.05	.08	.34	.08

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 & Poor's if unrated by Moody's. Excludes mortgage-backed and asset-backed bonds.
p Preliminary.

growth in June appears moderate as well. In contrast, consumer lending at banks has continued to be brisk. The rise in May was at only a 4-1/2 percent pace, but it was held down by a spate of securitizations. Adjusting for loans that were removed from banks' books puts consumer loan growth in May at an 11 percent rate, and growth in June appears higher. The volatile security loan category jumped in May, as dealers' financing needs likely rose with the pickup of underwriting activity in corporate securities.

Data from the March Call Report indicate that delinquency rates for business and real estate loans at banks continued to fall while those on consumer loans flattened (chart). In terms of dollar volume, delinquent loans touched bottom last year and have ticked up since (chart).

Business Finance

Net borrowing by nonfinancial corporations remained sizable in May and June, primarily owing to a sharp pickup in bond issuance after a prolonged period of quiescence. With long-term yields down to their lowest levels since February 1994 and the term structure relatively flat, firms found it attractive to lock in bond rates. The resurgence in gross public offerings was broad based, encompassing investment-grade and junk issues in all maturity ranges.

Quality spreads on bonds increased a bit as the market absorbed the hefty volume of new issues, but spreads remained narrow by historical standards. Spreads on junk bonds widened somewhat more than those on investment-grade bonds. Even so, the overall climate for junk issuance has remained favorable.

A portion of the proceeds from long-term debt issues has been used to repay nonfinancial commercial paper, and outstandings fell steadily through May and early June. The paydowns reflected, in part, a substitution to longer-term bond funding of mergers and acquisitions that were completed in late 1994 and earlier this year. Given the large volume of commercial paper issued for mergers and acquisitions, further paydowns are expected in coming months.

Nonfinancial merger activity has continued to be strong. Several large mergers have been announced since late May, led by IBM's $3.5 billion acquisition of the Lotus Corporation and Kimberly-Clark's $7.1 billion merger with Scott Paper. Consistent with the pattern over the past year, most recent deals have been nonhostile, strategic alliances between firms in a single industry. In addition, the form of payment has continued to be split fairly evenly between stock swaps and cash. IBM is expected to tap its large liquid reserves to finance its cash payment to Lotus shareholders; financing for the other cash transactions has not yet been announced.

ITT stated in mid-June that it would split into three separate publicly traded companies. ITT stock traded up substantially to reach a fifteen-year high on the announcement. In addition to ITT, twenty-five other spinoffs have been announced thus far this year, up from last year's pace that eventually totaled forty-five transactions valued at a record $17.8 billion.

Gross public equity issuance by nonfinancial corporations, both initial and seasoned offerings, was up slightly in May over the slow pace earlier this year. As has been the case since the beginning of the year, most of the initial public offerings have involved technology firms and, mirroring the recent strength among semiconductor and software stocks, demand for these offerings has been strong. Seasoned issuance was bolstered by a large offering by DuPont to finance its repurchase of shares from Seagram. Excluding DuPont, seasoned offerings have remained light. Despite the new highs touched by major stock indexes, issuance has been damped by price-to-earnings measures that remain well below those prevailing earlier in the expansion. Analysts' forecasts of earnings through 1996 have continued to hold up fairly well on balance, though the estimates for companies serving the domestic consumer sector appear to have been pared somewhat.

Municipal Securities

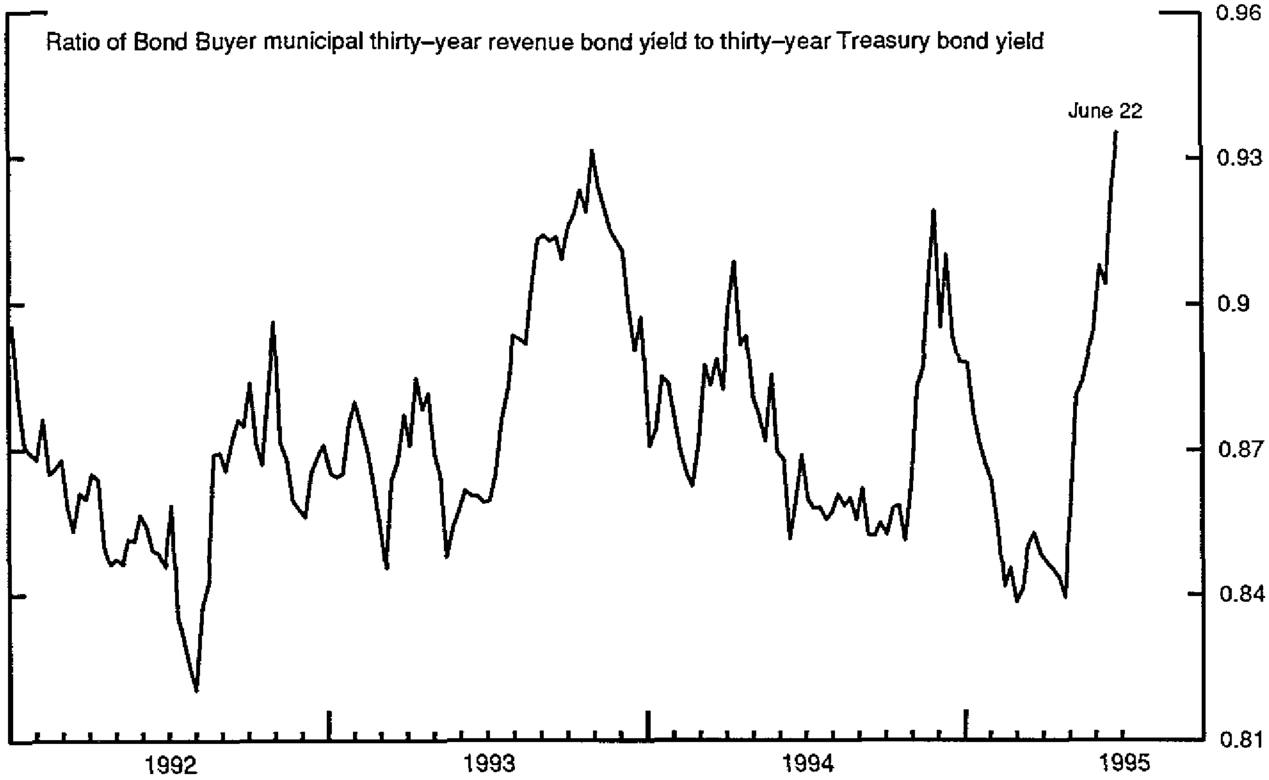
Yields on tax-exempt bonds have changed little over the intermeeting period despite appreciable declines in long-term Treasury rates. Investors have become increasingly concerned that the Congress might alter income tax laws in a way that would reduce or eliminate the value of the tax exemption of interest received from such securities. The yield ratio for thirty-year tax-exempt to Treasury bonds rose to 93 percent in mid-June, its highest since November 1989 (chart). At shorter maturities, the tax-exempt to taxable yield ratio has remained about unchanged at 70 percent, presumably because any revamping of the tax code is expected to be some way off in the future.

The narrowing of the long-term spread has occurred even as retirements have outpaced gross issuance, reducing the outstanding level of long-term municipal debt by an estimated $24 billion thus far this year. Gross issuance of long-term tax-exempt debt picked up a bit during May and June, in part owing to refunding activity. However, such activity is not expected to rise appreciably further, even in the event of additional declines in interest rates, because little debt remains eligible after the wave of advance refundings in 1993.[1] During May, short-term tax-exempt issuance continued to be light, and outstandings fell about $1-1/4 billion; however, in recent weeks there has been a seasonal pickup in issuance.

1. The 1986 Tax Reform Act restricts state and local governments to only one refinancing of a tax-exempt debt issue.

Ratio of Tax-Exempt to Treasury Yields

(Weekly data)



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

	1993	1994	1994 Q4	1995 Q1	1995 Mar.	1995 Apr.	1995 May p
Total tax-exempt	27.2	16.1	12.6	10.9	14.6	9.6	12.6
Long-term	23.3	12.8	10.9	9.0	11.8	8.6	11.8
Refundings[1]	15.7	4.0	1.7	1.7	1.3	2.1	3.4
New capital	7.6	8.8	9.1	7.3	10.5	6.5	8.4
Short-term	3.9	3.3	1.7	1.9	2.8	1.0	.8
Total taxable	.7	.7	1.1	.4	.5	.7	.4

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

Market participants continue to focus on developments in Orange County, California. On June 27, Orange County voters overwhelmingly rejected a 1/2 percentage point increase in the county's sales tax, making it almost certain the county will default on about $800 million in debt. Defeat of the measure was widely anticipated and appeared to have little immediate impact on prices of other insured municipal debt. Meanwhile, investors balked at buying $155 million in bonds the county offered on the same day, despite a bank letter of credit that guarantees repayment of the debt. Underwriters of the bonds ended up absorbing the bulk of the securities.

Federal Finance

The inflow of federal tax receipts has been heavier than expected and is anticipated to produce a budget surplus of $35 billion in the second quarter. These tax proceeds have caused the Treasury's cash balance to surge even as its marketable borrowing has slowed from $74 billion in the first quarter to $23 billion in the second quarter. By quarter's end, the Treasury plans to have paid down $14 billion in bills; but auction sales of coupon securities will net $37 billion.

Given the high level of the cash balance now, the Treasury likely will have enough room within its current debt authority of $4.9 trillion to operate until late October, although the cash balance will be on the lean side in early September.

Net borrowing by government-sponsored enterprises (GSEs) in the second quarter appears to have picked up slightly from the sluggish pace of the preceding three months. Gross issuance of debt has risen as the enterprises refunded callable securities carrying rates above those currently available. Yield spreads on the new debt issues remain tight, in the neighborhood of 20 basis points over Treasury rates.

TREASURY FINANCING
(Billions of dollars; total for period)

Item	1995 Q1	Q2[p]	Apr.	May	June[p]
Total surplus/deficit (-)	-71.3	35.4	49.7	-39.0	24.7
Means of financing deficit					
Net cash borrowing and repayments (-)	65.7	21.6	-27.6	44.7	4.5
Nonmarketable	-8.8	-1.5	.7	-0.7	-1.5
Marketable	74.4	23.2	-28.3	45.4	6.0
Bills	22.6	-13.6	-21.3	15.4	-7.8
Coupons	51.8	36.8	-7.0	30.0	13.8
Decrease in cash balance	8.5	-44.1	-20.0	11.8	-36.0
Other[1]	-2.8	-13.0	-2.1	-17.6	6.8
Memo:					
Cash balance, end of period	18.1	62.2	38.1	26.2	62.2

Note. Data reported on a payment basis. Details may not sum to totals because of rounding.
p Projected.
e Estimate.
1. Accrued items, checks issued less checks paid, and other transactions.

NET CASH BORROWING OF GOVERNMENT-SPONSORED ENTERPRISES
(Billions of dollars)

Agency	Q1	1995 Feb.	Mar.	Apr.	May
FHLBs	4.5	-2.1	4.5	1.9	6.5
FHLMC	8.4	6.4	0.3	4.8	1.3
FNMA	1.4	5.3	2.9	-0.5	4.8
Farm Credit Banks	0.8	-1.7	0.1	-0.3	0.4
SLMA	1.2	1.1	1.0	n.a.	n.a.

Note. Excludes mortgage pass-through securities issued by FNMA and FHLMC.
n.a. Not available.

Global bonds are becoming a bigger source of funds for agencies. The bonds can be settled on a variety of clearing systems and they trade in relatively liquid secondary markets. In June, the Tennessee Valley Authority--an agency on the federal budget--joined the GSEs in tapping this market, raising about $2 billion. The TVA deal, the largest single issue ever by a company owned or sponsored by the U.S. government, was well received. Indeed, the issue size was doubled because of investor demand.

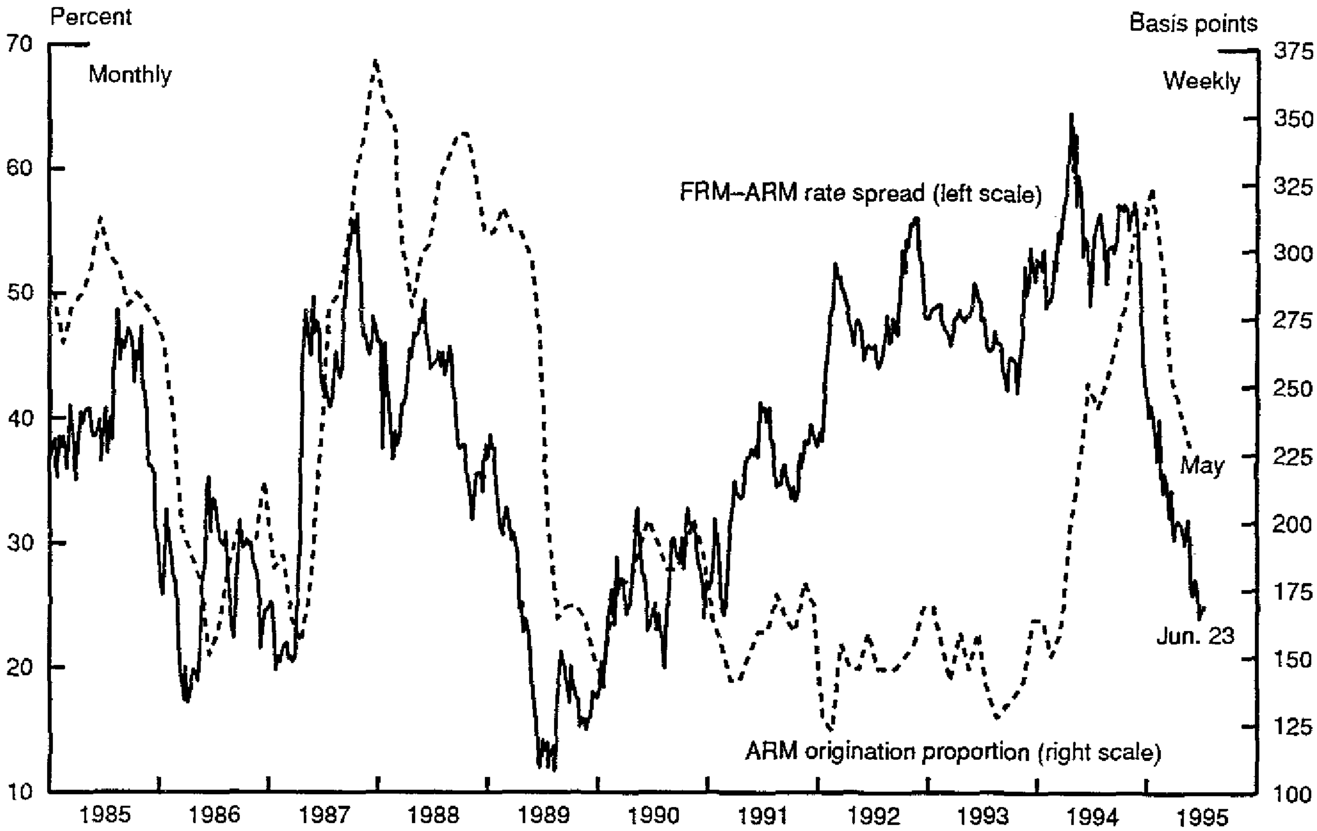
Mortgage Markets

The average contract rate on conventional fixed-rate mortgage loans has fallen roughly 30 basis points on net since the May FOMC meeting. At about 7-1/2 percent, the rate has returned to the levels that prevailed in early March 1994. Rates on adjustable-rate mortgages indexed to one-year Treasuries have declined somewhat less over the period; at 169 basis points, the initial rate advantage of these ARMs is the narrowest since mid-December 1990. With the large drop in FRM rates, thirty-year fixed-rate loans have become more popular among homebuyers, and the ARM share of conventional mortgage originations has declined (chart). According to the Federal Housing Finance Board, the ARM share of originations declined in May for the fourth consecutive month to 38 percent, down from 59 percent in January. This measure is based on loan closings rather than applications and thus reflects interest rate developments with some lag; a further rise in the FRM proportion seems likely.

The downtrend in mortgage interest rates has sparked a pickup in borrowing activity, especially refinancings. The Mortgage Bankers Association (MBA) indexes of loan applications and new indexes constructed by J.P. Morgan (chart) provide timely signals of potential market activity based on the number of applications at

ARM Origination Proportion and FRM–ARM Spread

(Not seasonally adjusted)

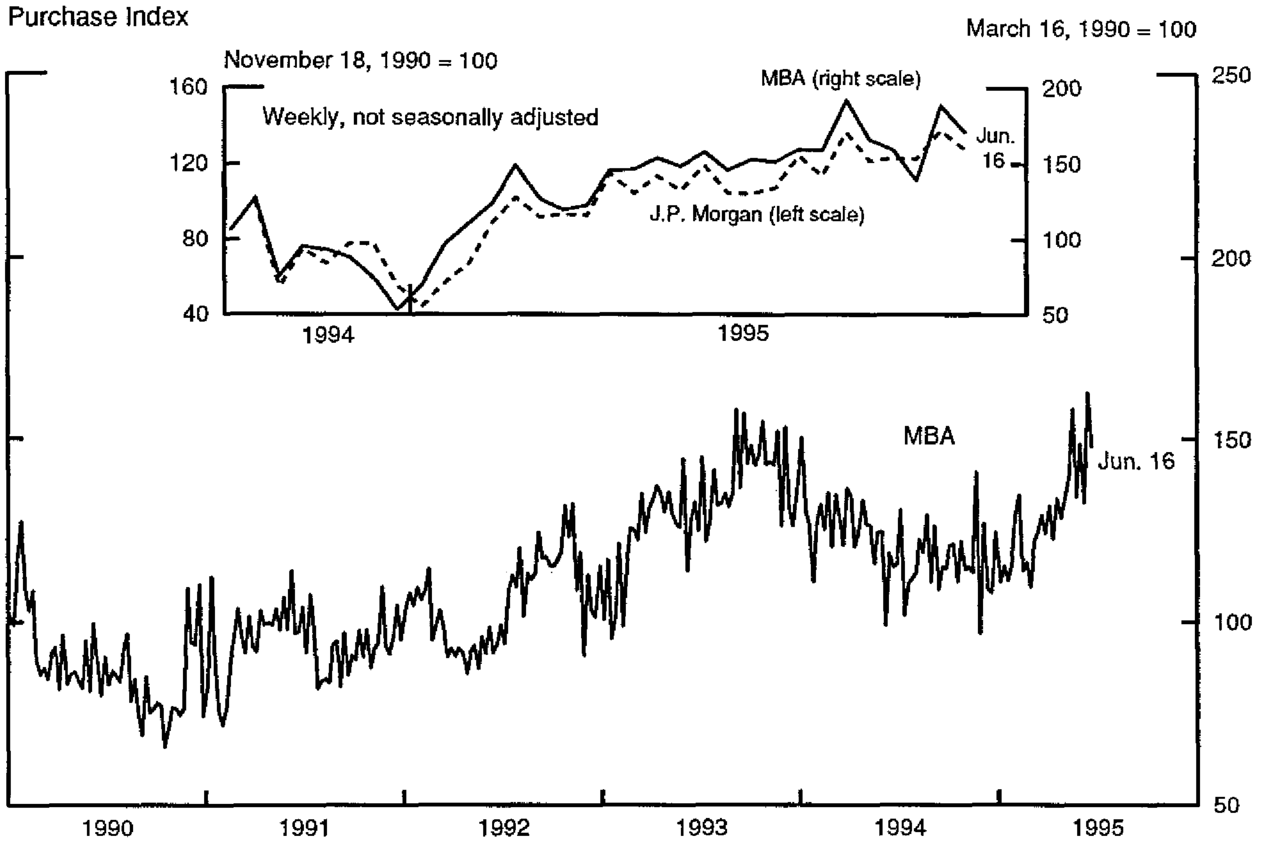


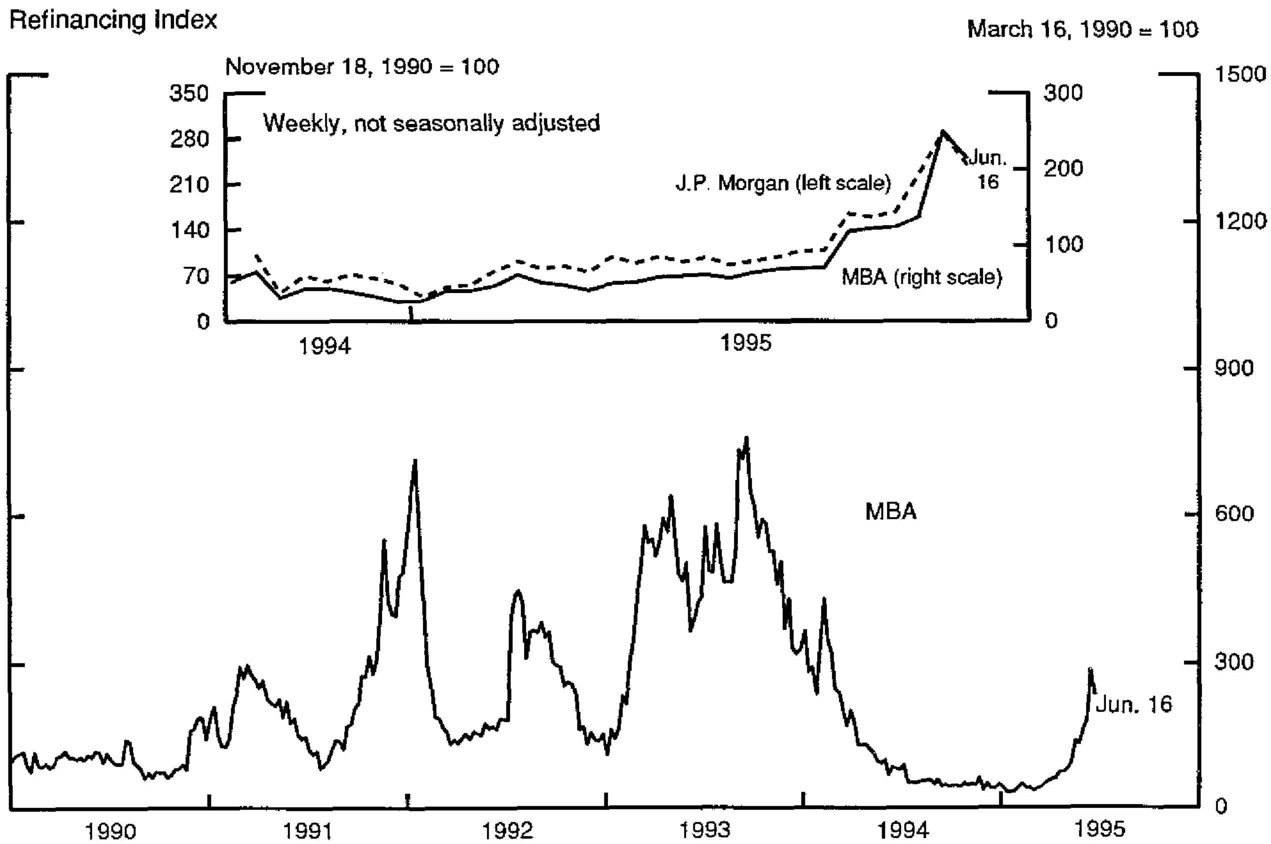
survey respondents.[2] Since late April the J.P. Morgan purchase index has increased about 11 percent, while the MBA purchase index is up roughly 18 percent on net. Both surveys indicate that the refinancing share of total applications has increased. Despite the sizable increase in the indexes, the longer MBA series indicates that aggregate refinancing is currently less than one-third of the peak levels of 1993. Most market participants expect that, in the absence of a further significant drop in interest rates, refinancing is unlikely to approach those earlier levels. According to data on home mortgages securitized by agencies, the proportion of

2. J.P. Morgan and the MBA collect information from leading mortgage lenders on the number of new applications each week. The lenders surveyed by the MBA account for about 40 percent of all home mortgage originations. Those surveyed by J.P. Morgan cover about 50 percent of all originations.

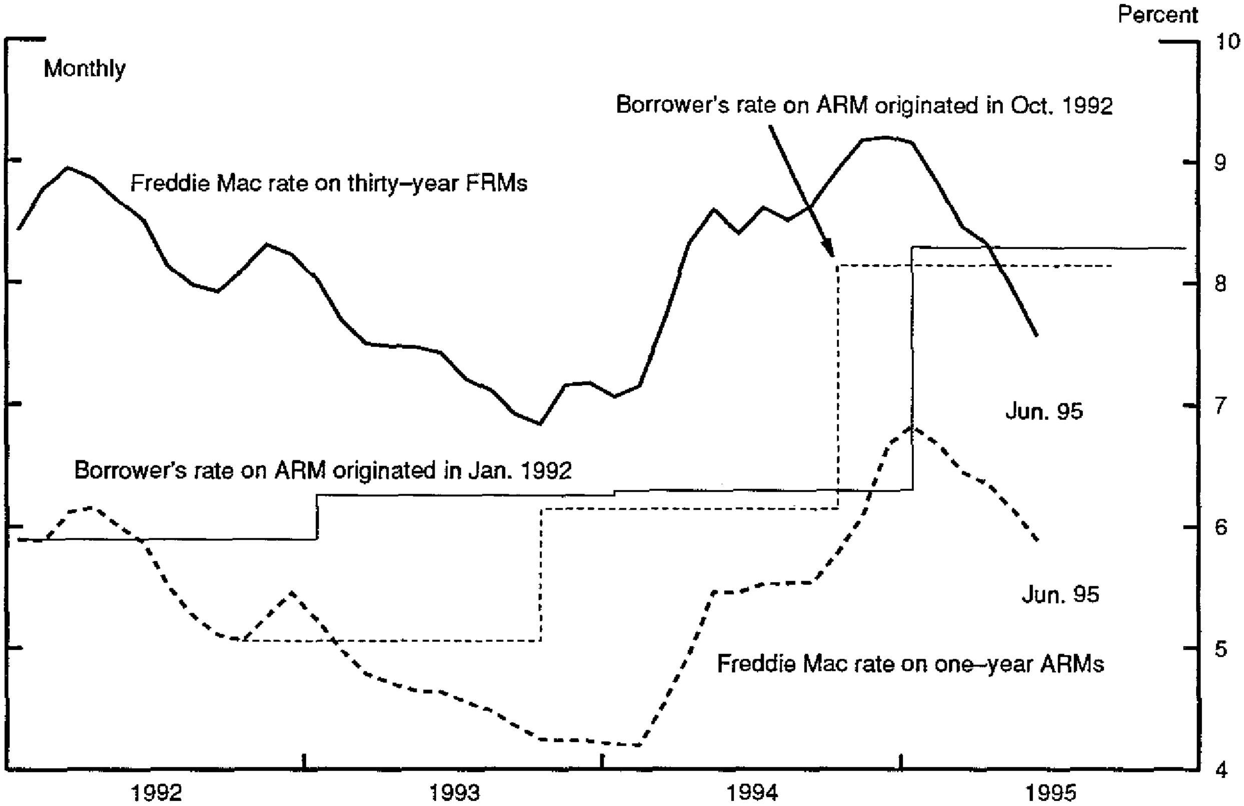
Mortgage Application Indexes

(Seasonally adjusted)



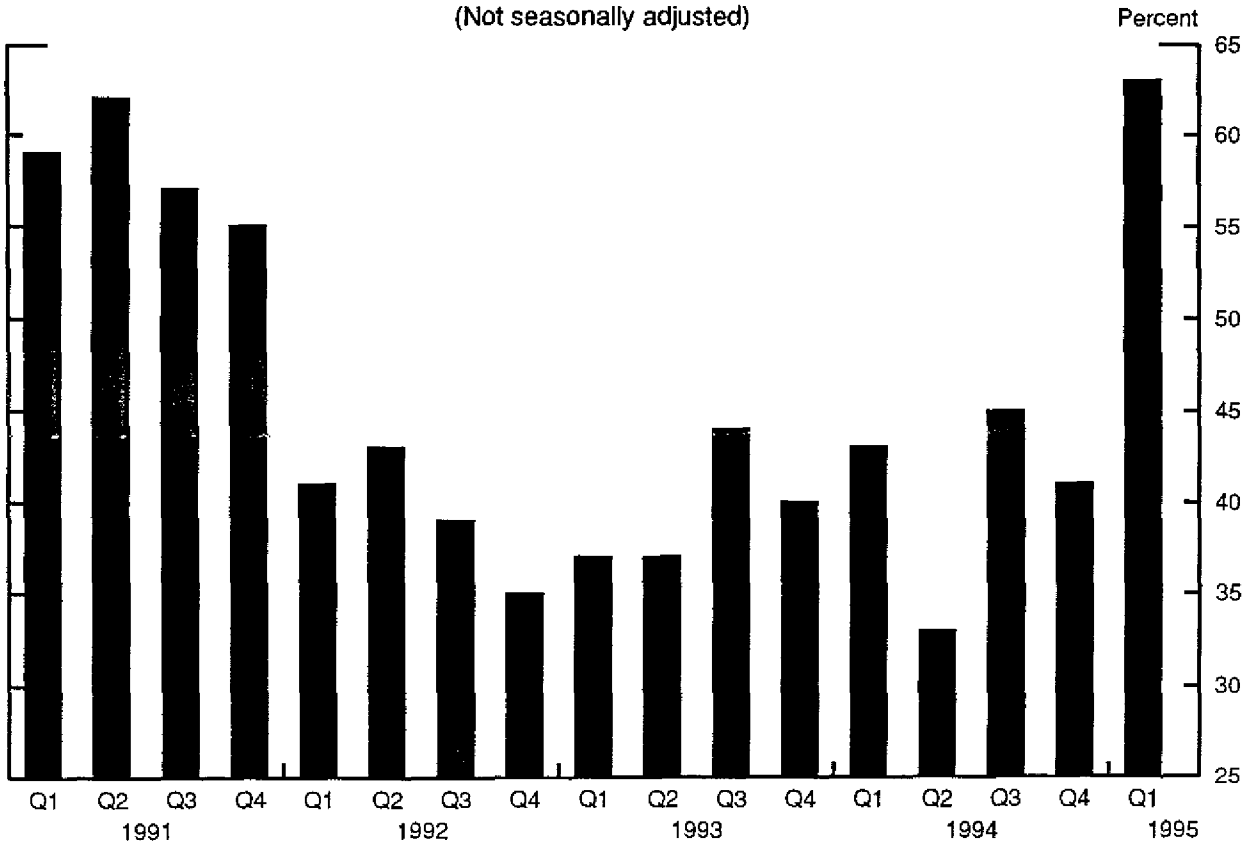


Recently Adjusted ARM Rates Compared to FRM Rates



ARM Borrowers Refinancing to Fixed Rate Loans

(Not seasonally adjusted)



Source. Freddie Mac

outstanding fixed-rate loans that are considered good candidates for refinancing at current interest rates is considerably less than in the 1992-93 episode.

Much of the current refinancing is probably by borrowers who purchased homes in the past year or so, when FRM rates were near 8-3/4 percent on average, and by borrowers holding ARMs that are adjusting upward. Treasury-based ARMs originated during 1992 or early 1993 would now have rates well in excess of current contract rates on FRMs (chart). Data from Freddie Mac show that more than 60 percent of conventional ARMs that were refinanced in the first quarter were replaced by an FRM (chart).

The pickup in origination of FRMs has contributed to a slight increase in issuance of agency pass-through securities, and issuance is likely to be somewhat higher in the next several months as recent FRM originations make their way to the secondary market. Issuance also will be boosted by the settlement of a record $6.4 billion swap of payment-capped ARM loans for pass-throughs between Freddie Mac and Home Savings of America, the nation's largest thrift.

Consumer Credit

Growth in consumer installment credit retreated somewhat in April from the strong advance in March, but at 14 percent was a shade above the pace of the first quarter as a whole. The still-brisk consumer borrowing is broadly consistent with the pattern of durable goods sales over the same period. Although outlays for durables have been flat this year, they had climbed sharply in the second half of 1994. The level of spending is still high enough to generate a large volume of loan originations, but with repayments continuing to rise in lagged response to growth in the stock of credit outstanding over the past few years, the net flow of credit should begin to moderate gradually.

GROWTH OF CONSUMER CREDIT
(Percent change; seasonally adjusted annual rate)

Type of credit	1993	1994	1994 Q4	1995 Q1 r	1995 Mar. r	1995 Apr. p	Memo: Outstanding Apr. 1995 (billions of dollars)
Installment	8.6	14.7	14.3	13.5	18.3	14.1	953.2
Auto	9.5	15.1	11.9	7.0	9.0	9.1	332.7
Revolving	11.9	17.3	18.4	21.9	23.0	21.8	362.6
Other	3.8	11.0	11.8	10.7	23.8	9.7	257.9
Noninstallment	-4.9	-4.9	-7.7	-27.6	.2	-38.5	45.6
Total	7.7	13.5	13.2	11.4	17.4	11.6	998.8

r Revised.
p Preliminary.

INTEREST RATES ON CONSUMER LOANS
(Annual percentage rate)

Type of loan	1993	1994	1994 Nov.	1995 Feb.	1995 Mar.	1995 Apr.	1995 May
At commercial banks[1]							
New cars (48 mo.)	8.1	8.1	8.8	9.7	n.a.	n.a.	9.8
Personal (24 mo.)	13.5	13.2	13.6	14.1	n.a.	n.a.	14.0
Credit cards	16.8	16.2	n.a.	n.a.	n.a.	n.a.	n.a.
Credit cards[2]							
All accounts	n.a.	n.a.	15.7	16.1	n.a.	n.a.	16.2
Accounts assessed interest	n.a.	n.a.	15.8	15.3	n.a.	n.a.	16.2
At auto finance cos.[3]							
New cars	9.5	9.8	10.5	11.9	12.0	11.7	n.a.
Used cars	12.8	13.5	14.2	15.1	15.1	15.0	n.a.

Note. Annual data are averages of quarterly data for commercial bank rates and of monthly data for auto finance company rates.

1. Average of "most common" rate charged for specified type and maturity during the first week of the middle month of each quarter.

2. The rate for *all accounts* is the stated APR averaged across all credit card accounts at all reporting banks. The rate for *accounts assessed interest* is the annualized ratio of total finance charges at all reporting banks to the total average daily balances against which the finance charges were assessed (excludes accounts for which no finance charges were assessed).

3. For monthly data, rate for all loans of each type made during the month regardless of maturity.

n.a Not available.

Increased use of credit cards for transactions has continued to boost installment credit and may have softened the downward pull resulting from the slowdown in the growth of outlays for durable goods. Revolving credit, which is now close to 40 percent of installment credit, remains the fastest growing component, with recent gains in excess of 20 percent at an annual rate. In addition to rebate programs and other incentives, credit card use has been stimulated by the expanding range of opportunities for using cards, such as for grocery store purchases.

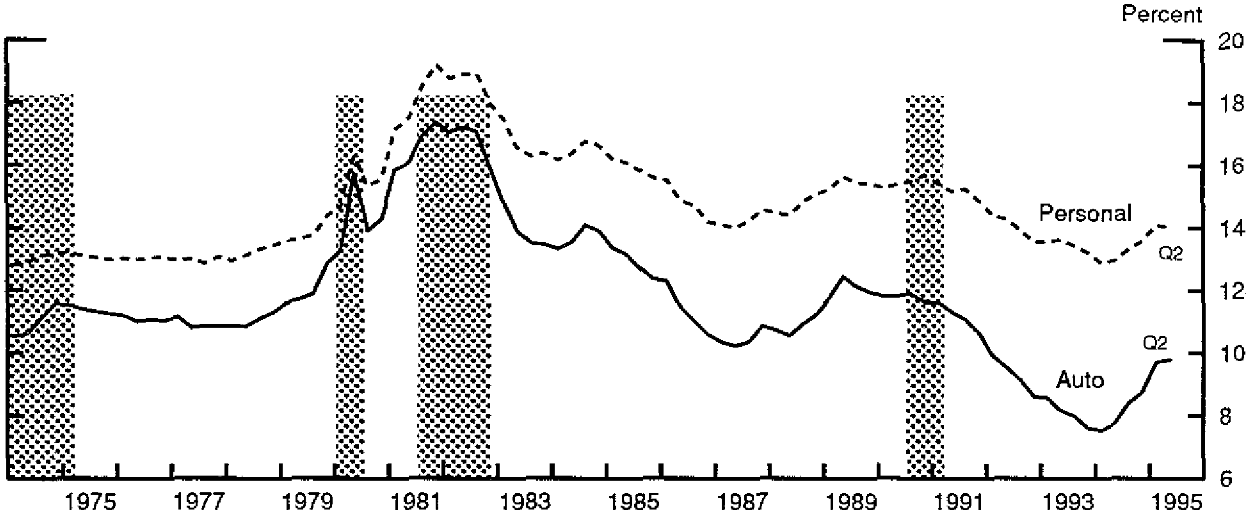
The cost to consumers of financing credit card debt apparently declined on balance last year even as interest rates rose on other types of consumer credit. Insofar as more than half of all credit card accounts now pay adjustable-rates, the increases in short-term market rates between early last year and early this year were presumably giving an upward push to credit card rates. However, balance transfer programs featuring low initial rates and other promotions have tended to pull down average rates paid. The Board's new series on average rates paid on accounts that are assessed finance charges showed a slight drop between November and February but rebounded in May.

In contrast, the average "most common" rate on a forty-eight month new-car loan at banks jumped sharply between November and February and edged up slightly further on net in the May survey (chart). Rates on personal loans followed a similar path. Because yields on Treasury securities of comparable maturity fell between February and May, spreads over Treasuries for the two consumer loan rates rose. The auto loan spread has risen to about the middle of its ten-year range after being unusually low most of last year. Historically, most of the large swings in such spreads have mirrored

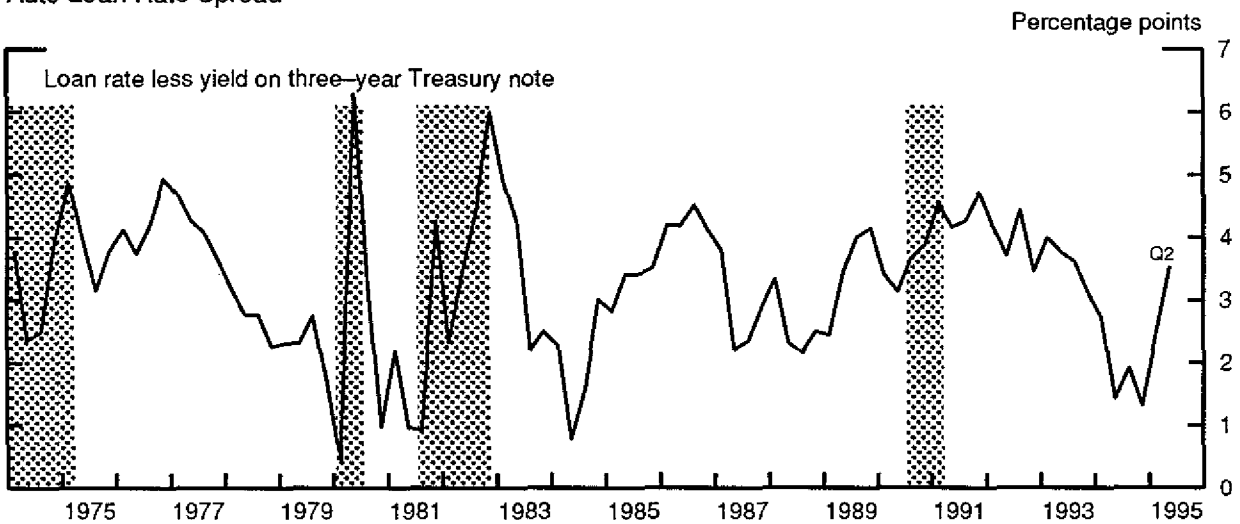
Interest Rates on Consumer Loans at Commercial Banks

(Quarterly; not seasonally adjusted)

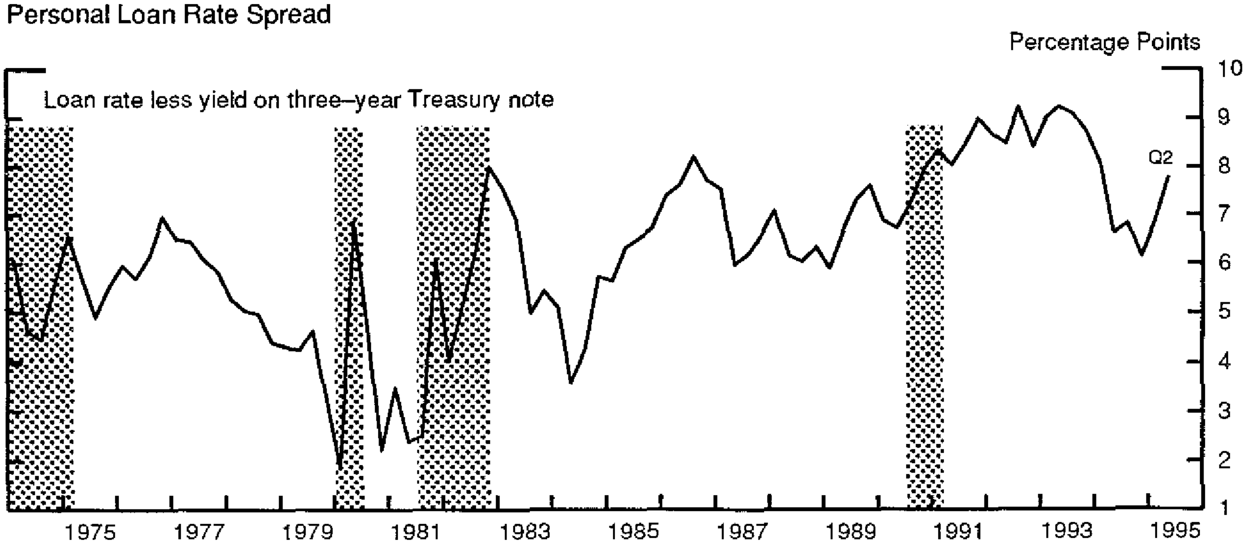
Loan Rates



Auto Loan Rate Spread



Personal Loan Rate Spread



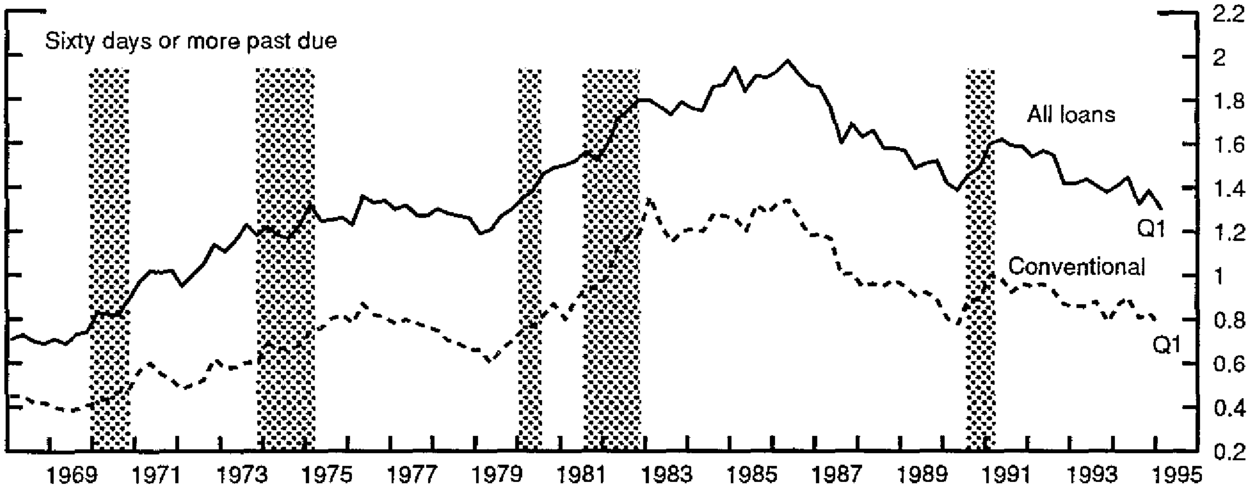
changes in Treasury rates; movements in consumer loan rates lag changes in Treasury yields, and they tend to be more gradual.

Delinquency rates on household debt presented a mixed picture during the first quarter (chart). Most series on home mortgage delinquencies registered declines and were at very low levels. Some series for consumer loans were also at low levels, but others, such as auto loan delinquencies at the auto finance companies, have climbed fairly sharply over the past two quarters or so. The American Bankers Association (ABA) has reported a particularly steep rise in credit card delinquencies at banks since 1994:Q3, as measured by the proportion of accounts that are past due. Calculations from Call Report data on dollar balances also show increases in the fourth and first quarters, but the rise was much smaller than reported by the ABA. Delinquencies on closed-end consumer loans increased slightly in the first quarter, according to the ABA, but the previous quarter's past-due ratio was the lowest in more than twenty years.

Household Credit Quality

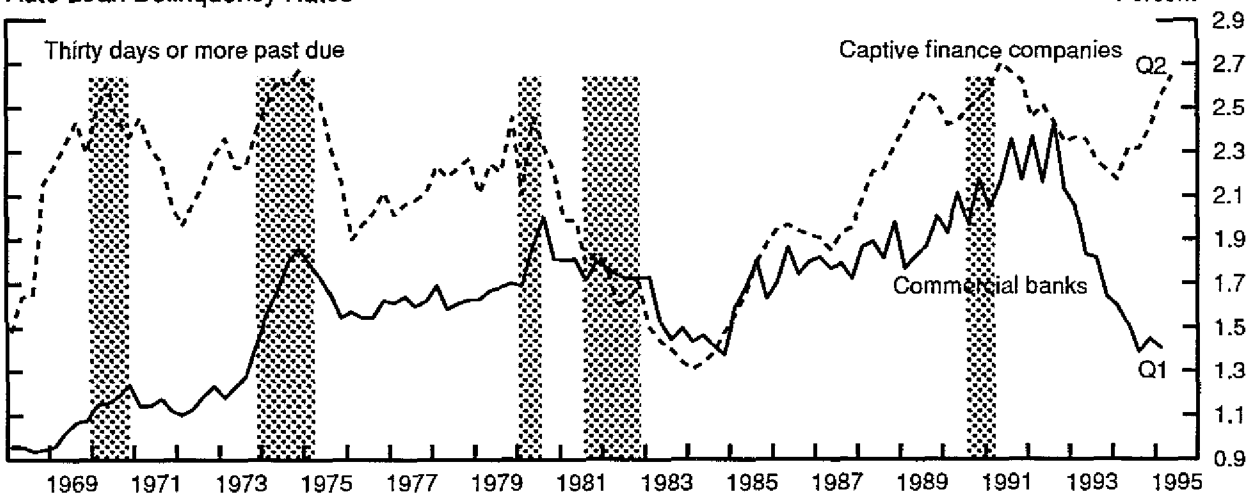
(Quarterly, seasonally adjusted)

Home Mortgage Delinquency Rates at All Lenders



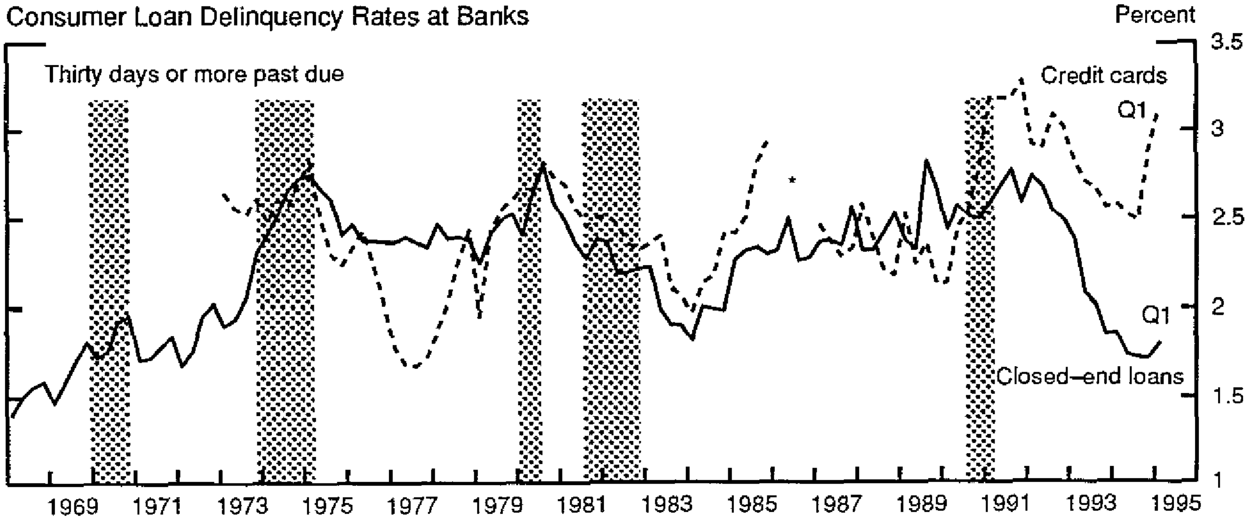
Source. Mortgage Bankers Association

Auto Loan Delinquency Rates



Sources. Federal Reserve Board, American Bankers Association

Consumer Loan Delinquency Rates at Banks



* Break in series between 1985 and 1987

Source. American Bankers Association

INTERNATIONAL DEVELOPMENTS

U.S. International Trade in Goods and Services

In April, the U.S. trade deficit in goods and services was substantially larger than in March. Exports, which had jumped in March, edged down in April. Imports, which had surged in March, advanced at a modest pace in April.

NET TRADE IN GOODS & SERVICES
(Billions of dollars, seasonally adjusted)

	Year	Quarters			Months		
	1994	94Q3	94Q4	95Q1	Feb	Mar	Apr
		(annual rates)			(monthly rates)		
Real NIPA 1/							
Net Exports of G&S	-110.0	-117.0	-107.1	-120.0	--	--	--
Nominal BOP							
Net Exports of G&S	-105.8	-113.4	-109.9	-120.1	-9.6	-9.8	-11.4
Goods, net	-165.6	-176.7	-174.0	-180.2	-14.4	-14.7	-16.5
Services, net	59.9	63.3	64.1	60.1	4.8	4.9	5.1

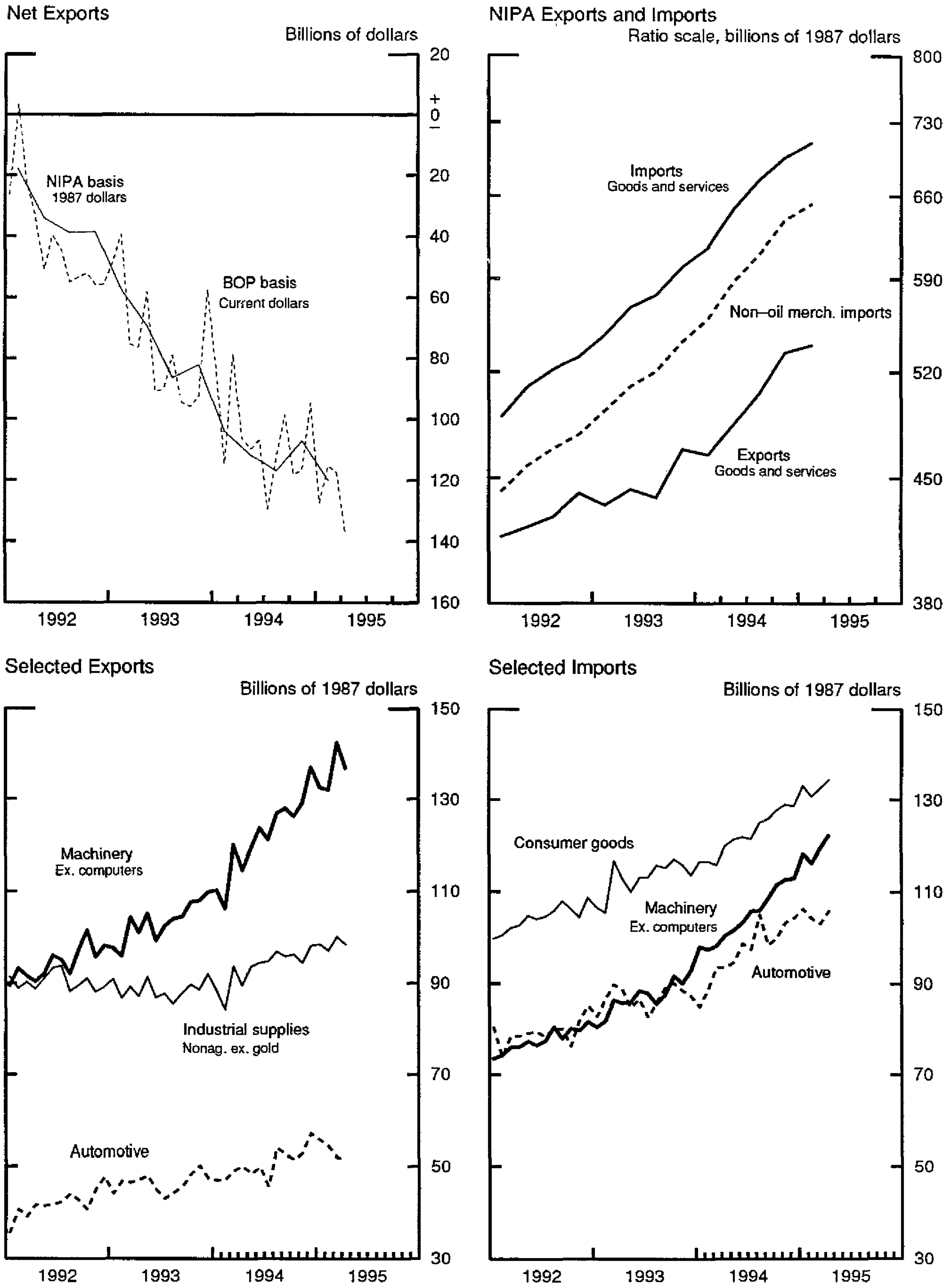
1/ In billions of 1987 dollars, SAAR.
Source: U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

The level of exports of goods and services for April was modestly higher at an annual rate than the first-quarter level. Increases in exports of aircraft and industrial supplies were partially offset by declines in exports of automotive products to Canada and Mexico. The change in exports was largely in quantity; the exception was exports of industrial supplies, where virtually all of the increase was in prices.

Imports of goods and services in April were about 3 percent higher at an annual rate than the first-quarter level, about the same rate of increase as those seen in the past two quarters. Increases were posted in all major import categories except food and services. Imports of industrial supplies and consumer goods continued to expand at a healthy pace. A drop in imports of automotive products from Canada and Mexico about offset a jump in

U.S. International Trade in Goods and Services

(Seasonally adjusted annual rate)



U.S. EXPORTS AND IMPORTS OF GOODS AND SERVICES
(Billions of dollars, SAAR, BOP basis)

	Levels				Amount Change 1/			
	Quarters		Months		Quarters		Months	
	94Q4	95Q1	Mar	Apr	94Q4	95Q1	Mar	Apr
Exports of G&S	739.5	755.6	777.8	767.7	24.6	16.1	32.7	-10.1
Goods Exports	535.7	552.2	573.7	563.1	24.4	16.5	27.9	-10.6
Agricultural	54.2	56.1	57.9	55.9	7.6	1.9	2.0	-2.0
Gold	3.4	5.6	10.1	6.8	-1.2	2.2	6.6	-3.4
Computers	35.8	36.3	36.7	35.9	1.8	0.5	0.0	-0.7
Other Goods	442.3	454.2	468.9	464.5	16.2	11.9	19.3	-4.5
Aircraft & Pts	29.4	25.2	30.4	32.1	0.9	-4.2	3.1	1.7
Semiconductors	27.7	30.0	32.5	30.4	2.1	2.3	3.5	-2.0
Other Cap Gds	122.0	125.0	130.7	127.0	3.3	3.0	9.6	-3.7
Automotive	61.7	62.1	59.8	59.6	3.7	0.4	-2.9	-0.1
to Canada	34.9	35.8	32.2	32.7	3.3	0.9	-4.0	0.5
to Mexico	8.5	6.0	5.7	4.7	0.9	-2.5	-0.2	-0.9
to ROW	18.3	20.4	21.9	22.2	-0.5	2.1	1.2	0.3
Ind Supplies	116.7	125.6	128.5	129.4	5.6	8.9	4.2	0.8
Consumer Goods	63.7	63.1	64.3	63.3	2.7	-0.6	0.6	-1.0
All Other	21.1	23.2	22.9	22.6	-2.1	2.1	5.1	-0.2
Services Exports	203.8	203.4	204.2	204.6	0.2	-0.4	4.8	0.5
Imports of G&S	849.4	875.7	895.4	904.2	21.0	26.3	34.9	8.9
Goods Imports	709.7	732.4	749.8	761.1	21.6	22.8	30.9	11.3
Petroleum	51.1	52.3	55.5	53.5	-9.5	1.2	3.4	-2.0
Gold	2.7	4.4	9.7	9.6	-0.2	1.7	8.0	-0.1
Computers	50.7	50.8	51.3	51.8	3.1	0.2	1.3	0.6
Other Goods	605.2	624.9	633.4	646.2	28.2	19.7	18.2	12.8
Aircraft & Pts	11.8	10.5	12.3	11.1	2.1	-1.3	2.4	-1.3
Semiconductors	30.2	32.0	32.7	34.3	3.1	1.8	1.6	1.7
Other Cap Gds	107.2	112.5	114.4	118.0	3.6	5.4	3.1	3.6
Automotive	127.1	129.8	128.1	132.4	4.5	2.7	-1.6	4.3
from Canada	47.5	48.3	46.6	42.9	2.9	0.8	-1.8	-3.7
from Mexico	17.1	17.8	19.3	16.6	3.2	0.6	2.2	-2.7
from ROW	62.5	63.8	62.2	72.9	-1.6	1.3	-2.0	10.7
Ind Supplies	117.1	122.8	126.5	130.2	6.3	5.7	7.3	3.7
Consumer Goods	154.2	159.1	159.8	163.0	6.0	4.9	2.2	3.2
Foods	31.9	34.1	34.8	32.8	-0.1	2.2	1.4	-2.0
All Other	25.7	24.0	24.7	24.4	2.7	-1.7	1.6	-0.3
Services Imports	139.7	143.2	145.5	143.1	-0.6	3.5	4.0	-2.5
Memo:								
Oil Qty (mb/d)	9.21	8.95	9.37	8.48	-1.10	-0.26	0.52	-0.89

1/ Change from previous quarter or month.
Source: U.S. Dept. of Commerce, Bureaus of Econ. Analysis and Census

automotive imports from other countries; the jump was partly attributable to the introduction of some new models, and imports from Japan accounted for about half of the increase. As with exports, most of the increase in imports was in quantity.

The total quantity of oil imported in April fell on higher domestic production and a contra-seasonal decline in inventories. Preliminary Department of Energy statistics indicate that in May seasonal inventory accumulation has set in and we estimate that imports rose.

The price of imported oil rose sharply in April, just over $1.00 per barrel. Oil prices rose on increased tension between the United States and both Iran and Iraq, a relatively tight gasoline market in the United States, and seasonally lower production in the North Sea. During May, spot oil prices (West Texas Intermediate - WTI) averaged slightly less than in April, as prices eased at the end of the month given the impending suspension of the month-long Brazilian oil workers strike.

Currently, spot WTI is trading at around $18 per barrel, compared with an April-May average of $19.80 per barrel. Oil prices fell sharply in mid-June on concern over prospective higher OPEC production due to comments by an OPEC leader that the cartel may suspend quotas to regain market shares.

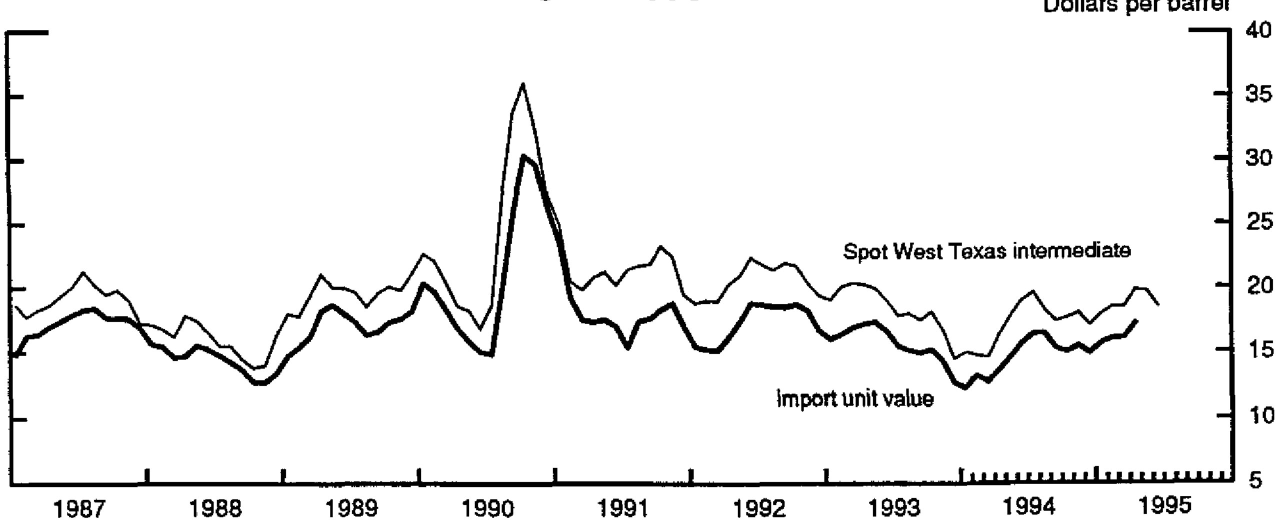
Prices of Merchandise Non-oil Imports and Exports

The price of U.S. non-oil imports rose 1/2 percent in April. This rate of increase was much faster than the increases seen in the first quarter and a bit larger than those seen in the last half of 1994. Most of the April increase was in prices of imported capital goods and industrial supplies. The price of imported food, which has been quite volatile in recent months, fell 2-1/2 percent in April, reflecting weaker prices for vegetables and coffee.

PRICES OF U.S. IMPORTS AND EXPORTS
(percent change from previous period)

	Quarters			Months		
	94Q3	94Q4	95Q1	Feb	Mar	Apr
	(annual rates)			(monthly rates)		
	--BLS Prices--					
Merchandise Imports	7.7	3.8	4.3	0.7	0.5	1.2
Oil	36.1	-10.9	15.4	2.7	2.1	6.2
Non-Oil	5.3	5.5	3.1	0.5	0.4	0.5
Foods, Feeds, Bev.	38.4	7.9	-0.4	-1.9	2.5	-2.6
Ind Supp Ex Oil	8.5	15.2	15.0	1.2	0.8	1.3
Computers	-8.7	-6.2	-4.2	-0.3	-1.4	-0.3
Capital Goods Ex Comp	4.3	2.6	0.6	0.5	0.4	1.2
Automotive Products	2.4	6.2	0.4	0.3	0.1	0.6
Consumer Goods	1.0	1.6	1.1	0.5	0.0	0.5
Memo:						
Oil Imports ($/bbl)	16.09	15.19	16.01	16.08	16.20	17.26
Merchandise Exports	2.1	5.9	8.8	0.7	0.5	0.8
Agricultural	-14.4	7.0	12.1	0.5	1.6	1.7
Nonagricultural	4.5	5.9	8.3	0.7	0.4	0.7
Ind Supp Ex Ag	17.1	18.8	23.5	1.5	0.9	1.7
Computers	-11.3	-6.3	-5.8	-0.5	-0.5	0.3
Capital Goods Ex Comp	0.4	0.0	3.0	0.2	0.3	0.3
Automotive Products	1.0	2.3	0.9	0.3	-0.4	0.0
Consumer Goods	-0.6	1.2	1.7	0.5	0.2	0.3
	--Prices in the NIPA Accounts--					
Fixed-Weight						
Imports of Gds & Serv.	9.1	3.2	3.8	--	--	--
Non-oil Merch Ex Comp	6.2	5.4	3.2	--	--	--
Exports of Gds & Serv.	2.9	6.9	9.3	--	--	--
Nonag Merch Ex Comp	6.1	7.1	9.6	--	--	--

Oil Prices



The price of U.S. exports posted another strong increase in April, somewhat faster than the already robust rate of increase seen in the first quarter. The bulk of the increase was in prices of exported agricultural products (primarily soybeans and wheat) and industrial supplies.

Price data for U.S. merchandise trade for May will be released June 28 and will be included in the Greenbook supplement.

U.S. Current Account in 1995:Q1

In the first quarter of 1995, the U.S. current account deficit was $11 billion SAAR smaller than in the fourth quarter of 1994. Decreased net payments of investment income and a seasonal drop in unilateral transfers more than offset a widening in the trade deficit for goods and services.

Decreased net payments of investment income were attributable to an increase in net direct investment receipts (mostly manufacturing) of $8-1/2 billion. Net payments on portfolio capital

U.S. CURRENT ACCOUNT
(Billions of dollars, seasonally adjusted annual rates)

	Goods & Services Balance	Investment Income, net	Transfers net	Current Acct Balance
Years				
1993	-74.8	9.0	-34.1	-99.9
1994	-106.2	-9.3	-35.8	-151.2
Quarters				
1993-1	-54.3	14.8	-30.1	-69.5
2	-75.2	8.3	-30.4	-97.3
3	-88.0	12.8	-32.9	-108.1
4	-82.0	0.1	-42.9	-124.7
1994-1	-92.1	0.5	-29.5	-121.1
2	-107.7	-9.1	-35.1	-151.9
3	-115.2	-10.1	-33.5	-158.9
4	-109.9	-18.3	-45.0	-173.1
1995-1	-120.1	-10.8	-31.1	-162.0
Memo:				
$ Change				
Q1-Q4	-10.2	7.5	13.9	11.1

Source: U.S. Department of Commerce, Bureau of Economic Analysis rose by $1-1/2 billion in the quarter, largely attributable to a further deterioration of the net portfolio position.

U.S International Financial Transactions

Capital inflows through both foreign official sources and private purchases of U.S. securities slowed between March and April. These smaller inflows were more than offset by a swing in private banking flows from large net outflows in March to large net inflows in April. U.S. net purchases of foreign securities slowed between March and April, but remained near the modest first-quarter pace.

The reduction in foreign official inflows in April reflected smaller intervention purchases of dollars by foreign industrial countries. Intervention purchases by Japan in April, although much smaller than in March, remained substantial, and increases in Japanese reserves in the United States account for most of the increase in total official reserves (line 1 of the Summary of U.S. International Transactions table). Official reserves held by Mexico, Chile, and Russia also increased in April.

. Partial data for May from the FRBNY show modest official inflows.

Foreign net purchases of U.S. securities slowed to $8-1/2 billion in April from $12-1/2 billion in March (line 4). Foreign purchases of both Treasuries and corporate bonds fell off in April. New Eurobond issues by U.S. corporations picked up in May. Foreigners on net purchased a small amount of corporate stocks in April--the first month of net purchases since November of last year.

U.S. private net purchases of foreign securities fell slightly from March to April, but remained above the weak first-quarter pace (line 5). Nearly all of the decline in net purchases was concentrated in Latin America and the Caribbean.

SUMMARY OF U S. INTERNATIONAL TRANSACTIONS
(Billions of dollars, not seasonally adjusted except as noted)

	1993	1994	1994			1995		
			Q2	Q3	Q4	Q1	Mar.	Apr.
Official capital								
1. **Change in foreign official reserve assets in U.S. (increase, +)**	70.4	37.2	9.0	19.2	-1.1	21.7	14.9	9.8
a. G-10 countries	30.1	28.9	15.8	8.9	-6.1	16.9	15.8	8.6
b. OPEC countries	-5.1	-3.3	4.7	3.3	.4	.4	.2	.4
c. All other countries	45.5	11 7	-2.0	7 0	4.6	4.4	-1.1	.9
2. **Change in U.S. official reserve assets (decrease, +)**	1.4	5.3	-.1	3.5	-.2	-5.3	-.7	-1.2
Private capital								
Banks								
3. **Change in net foreign positions of banking offices in the U.S.**[1]	13.7	110.4	35.7	9.8	24.8	-15.9	-18.5	16.1
Securities[2]								
4. **Foreign net purchases of U.S. securities (+)**	105.7	94.4	5.8	20.6	36.6	45.8	12.5	8.5
a. Treasury securities[3]	24.8	34.5	-7.1	5.6	26.1	29.8	7.6	3.7
b. Corporate and other bonds[4]	61.4	55.5	14.8	14.0	12.9	19.6	7.4	4.0
c. Corporate stocks	19.6	4.4	-1.9	1.0	-2.4	-3.5	-2.5	.8
5. **U.S. net purchases (-) of foreign securities**	-143.1	-52.7	-10.8	-10.2	-15.2	-7.5	-4.8	3.0
a Bonds	-80 4	-5.9	1.7	-3.3	-6.1	-3.4	2.0	-.9
b. Stocks	-62.7	-46.8	-12.5	-6.8	-9.2	-4.1	2.8	-2 1
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-72.6	-49.4	-7.8	-10.1	-11.9	-18.4	n.a.	n.a.
7. Foreign direct investment in U.S.	41.1	49.4	5.9	19.7	19.6	9.8	n.a.	n.a.
8. Other (inflow, +)[5]	50.1	-29.1	2.9	-0.7	-23.0	-9.1	n.a.	n.a.
U.S. current account balance (s.a.)	-99.9	-151.2	-38.0	-39.7	-43.3	-40.5	n.a.	n.a.
Statistical discrepancy (s.a.)	36.0	-14.3	-2.6	-12.1	13.7	19.4	n.a.	n.a.

Note The sum of official capital, private capital, the current account balance, and the statistical discrepancy is zero. Details may not sum to totals because of rounding.

1. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements) Includes changes in custody liabilities other than U.S. Treasury bills.

2 Includes commissions on securities transactions and therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. Includes Treasury bills

4 Includes U.S. goverment agency bonds.

5 Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business.

n.a. Not available. * Less than $50 million.

INTERNATIONAL BANKING DATA[1]
(Billions of dollars)

	1991 Dec.	1992 Dec.	1993 Dec.	1994 June	1994 Dec.	1995 Mar.	1995 Apr.	1995 May
1. Net claims of U.S. banking offices (excluding IBFs) on own foreign offices and IBFS	-35.8	-71.6	-122.1	-175.4	-224.0	-242.7	-239.0	-243.2
a. U.S.-chartered banks	12.4	17.0	4.2	-29.9	-70.1	-88.6	-85.5	-89.7
b. Foreign-chartered banks	-48.3	-88.6	-126.3	-145.5	-153.9	-154.1	-153.5	-153.6
2. Credit extended to U.S. nonbank residents								
a. By foreign branches of U.S. banks	23.9	24.8	21.8	22.2	23.1	23.5	24.3	25.2
b. By Caribbean offices of foreign-chartered banks	n.a.	n.a.	90.9	81.0	78.4	80.3	n.a.	n.a.
3. Eurodollar holdings of U.S. nonbank residents								
a. At all U.S.-chartered banks and foreign-chartered banks in Canada and the United Kingdom	102.9	90.0	77.8	77.5	85.6	90.5	91.0	92.7
b. At the Caribbean offices of foreign-chartered banks	n.a.	n.a.	79.2	81.1	86.0	96.2	n.a.	n.a.
MEMO: Data as recorded in the U.S. international transactions accounts								
4. Credit extended to U.S. nonbank residents	182	195	202	202	198	n.a.	n.a.	n.a.
5. Eurodeposits of U.S. nonbank residents	236	235	230	242	260	n.a.	n.a.	n.a.

1. Data on lines 1 through 3 are from Federal Reserve sources and sometimes differ in timing from the banking data incorporated in the U.S. international transactions accounts.

Lines 1a, 1b, and 2a are averages of daily data reported on the FR 2950 and FR 2951.

Lines 2b and 3b are end-of-period data reported quarterly on the FFIEC 002s.

Line 3a is an average of daily data (FR 2050) supplemented by the FR 2502 and end of quarter data supplied by the Bank of Canada and the Bank of England. There is a break in the series in April 1994.

Lines 4 and 5 are end-of-period data estimated by BEA on the basis of data provided by the BIS, the Bank of England, and the FR 2502 and FFIEC 002s. It includes some foreign-currency denominated deposits and loans. Source: SCB

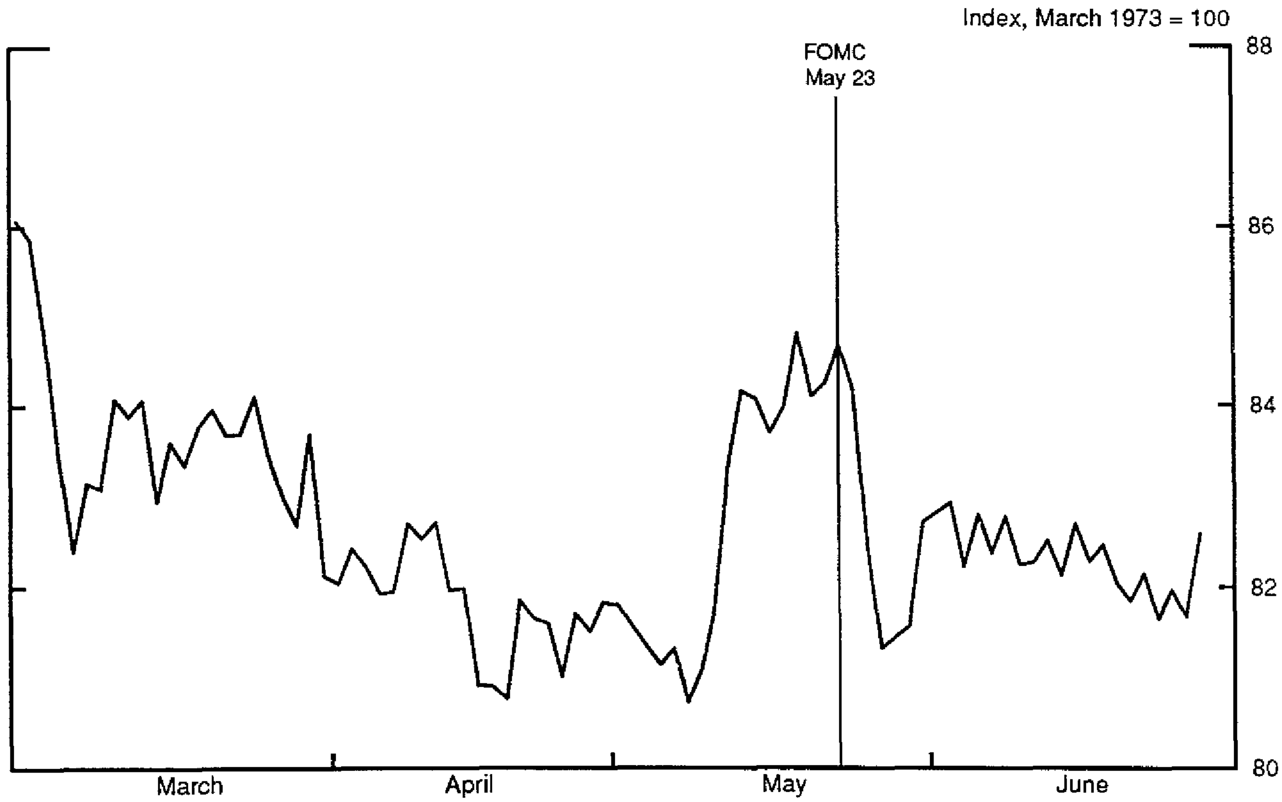
The huge outflow recorded for private banking transactions in March was largely reversed in April (line 3). On a monthly average basis, data on banks' transactions with their own foreign offices and IBFs do not show these sharp swings (line 1 of the International Banking Data table). In fact, these data show continuing net Eurodollar borrowing by banks through May, accompanied by rising deposits of U.S. residents at offshore banking offices (line 3).

Balance of payments data for the first quarter recorded large outflows through U.S. direct investment abroad and relatively small inflows from foreign direct investment in the United States. As with the banking data for the first quarter, the direct investment flow data are likely distorted by temporary factors. The U.S. offices of both domestic and foreign-based financial firms lent large sums to their foreign affiliates, which is recorded as a direct investment outflow. Data on mergers and acquisitions in the first quarter would indicate a larger inflow of direct investment than that which was recorded. The statistical discrepancy in the first quarter was a positive $19 billion, indicating a substantial unrecorded inflow. Only part of the unrecorded inflow in the first quarter can be accounted for by large increases in foreign holdings of U.S. currency.

<u>Foreign Exchange Markets</u>

The weighted-average dollar has declined 2-1/2 percent on balance since the May 23 FOMC meeting as the dollar has depreciated 3-1/3 percent against the mark and 1-3/4 percent against the yen. The dollar declined sharply early in the intermeeting period and then rebounded somewhat due to concerted intervention by G-10 countries on May 31. In June, the dollar's oscillations in a fairly narrow range have been driven mostly by technical factors as most market participants reportedly have been hesitant to open new positions before the future courses of monetary policy in the United States and Germany, and to a lesser extent, Japan,

Weighted Average Exchange Value of the Dollar
(Daily data)



Interest Rates in Major Industrial Countries

	Three-month rates			Ten-year bond yields		
	May 23	June 28	Change	May 23	June 28	Change
Germany	4.45	4.50	0.05	6.80	6.81	0.01
Japan	1.33	1.15	-0.18	3.26	2.83	-0.43
United Kingdom	6.50	6.88	0.38	8.05	8.40	0.35
Canada	7.58	6.90	-0.68	8.09	7.87	-0.22
France	7.12	6.88	-0.24	7.41	7.53	0.12
Italy	10.50	11.00	0.50	12.21	12.46	0.25
Belgium	4.90	4.64	-0.26	7.47	7.43	-0.04
Netherlands	4.40	4.18	-0.22	6.87	6.93	0.06
Switzerland	3.31	3.13	-0.18	4.76	4.63	-0.13
Sweden	9.05	9.45	0.40	10.72	10.82	0.10
Weighted-average foreign	4.88	4.75	-0.13	6.89	6.80	-0.09
United States	6.03	5.90	-0.13	6.57	6.13p	-0.44

Note. Change is in percentage points. p Preliminary become more apparent. On June 28, the dollar rose 1-1/2 percent against the yen, and 1/2 percent on a weighted-average basis, following the announcement that U.S. and Japanese negotiators had reached agreement in the auto trade talks.

The dollar's precipitous drop in the days immediately following the May 23 FOMC meeting reflected U.S. data releases on May 25 that showed a sharp decline in durable goods orders in April and a large increase in initial jobless claims in the second week of May. Both of these releases were seen as evidence that economic activity in the United States was decelerating faster than the market had expected, thereby increasing the likelihood that the Federal Reserve would ease monetary policy in the near term. The dollar recouped nearly half its losses when central banks in the G-10 countries surprised the market on May 31 with concerted intervention purchases of dollars. The Desk purchased $500 million against yen and $500 million against marks for the accounts of the System and the Treasury.

Since May 31, the dollar has traded in a fairly narrow range. There appears to be little interest to buy the dollar due to the weakness of recent economic indicators in the United States. In addition, there are a number of factors that reportedly have made many market participants unwilling to open new positions. In early June, there reportedly was little desire to open new positions ahead of the G-7 summit meeting on June 15-17 although most market participants did not expect the announcement of any major economic policy packages at that meeting. Since the conclusion of the G-7 meeting, this hesitancy among most market participants to open new positions has continued due to uncertainty surrounding the auto trade talks between the United States and Japan, which were successfully concluded on June 28, and to the upcoming meetings of the Bundesbank Council on June 29 and July 13, and the FOMC on July 5-6.

Within Europe, DM cross rates have been generally stable over the intermeeting period. However, the British pound has declined 3 percent against the mark due in part to renewed intra-party squabbling within the ruling Conservative Party over European integration. In addition, the resignation on June 22 of John Major as leader of the Conservative Party, which will force the party to choose a new leader and hence, prime minister, has weighed on the pound. Sterling's weakness has contributed to the 2 percent decline of the Irish punt. The Swedish krona has depreciated 2 percent due in part to rising inflation in Sweden and market expectations that the upcoming Swedish budget will not go far enough in correcting that country's fiscal woes. The French franc has strengthened 1 percent as market uncertainty over the economic policies of the newly elected Chirac government has dissipated.

Short-term interest rates in the United Kingdom jumped 1/4 percentage point following the resignation of John Major as Conservative Party leader. Following monetary tightening by the Bank of Italy and the Swedish Riksbank, short-term rates in Italy and Sweden have risen. In contrast, monetary easing in Belgium and the Netherlands has provided scope for short-term rates in those countries to decline. French short-term rates have drifted lower as pressure on the French franc has subsided. In Canada, short-term rates have fallen as the Bank of Canada has reduced its target range for the Canadian overnight rate by 50 basis points since the May 23 FOMC meeting.

In contrast to the marked decline in long-term interest rates in the United States over the intermeeting period, long-term rates in most European countries have remained about unchanged. Long-term rates in the United Kingdom backed up following John Major's resignation, and renewed political uncertainty in Italy, initiated by former-Prime Minister Berlusconi's call for general elections in October, has contributed to the rise in Italian long-term rates. In Japan, long-term rates have declined due to the weakness of the Japanese economy and as investors continue to shift funds from the depressed Japanese stock market, which on June 13 reached its lowest point since August 1992, to the bond market. Since May 23, the Japanese stock market has declined 8 percent due to the weakness of the Japanese economy and to heightened concerns about the fragility of the banking system.

The Mexican peso has depreciated 5 percent against the dollar during the intermeeting period as peso-denominated short-term interest rates have fallen 7 to 8 percentage points. Mexican stock prices are about unchanged on balance, and the interest rate spread of Mexican Brady bonds against U.S. Treasury securities of similar maturity has widened 1/2 percentage point. Mexican banks have continued to repay their FOBAPROA loans as outstanding balances have declined by $800 million since May 23 to $1.5 billion.

Developments in Foreign Industrial Countries

After expanding rapidly last year, economic activity appears to have moderated in the first half of this year in most major foreign industrial countries. The slowdown has been particularly sharp in Canada, where all components of demand except inventory accumulation were flat or declined in the first quarter and recent indicators suggest output may be falling in the second quarter. The economic expansion also appears to have moderated to a lesser extent in the major European countries, except Italy, which had a stagnant fourth quarter. Growth in Japan was anemic in the first quarter after falling in the fourth quarter and appears to have remained weak in the second quarter.

Consumer price inflation has slowed in the major foreign industrial countries with currencies that have strengthened, especially in Japan, where prices have declined. On the other hand, inflation has picked up somewhat in countries with currencies that have depreciated, especially in Italy.

Individual country notes. Japanese real GDP increased 0.3 percent (SAAR) in the first quarter of 1995, after falling a revised 3.9 percent in the fourth quarter of 1994. Personal consumption was nearly flat, but government consumption grew strongly because of the earthquake relief effort. Growth in private corporate investment and housing was offset by steep declines in government investment.

JAPANESE REAL GDP
(Percent change from previous period, SAAR)[1]

	1993	1994	1994			1995
			Q2	Q3	Q4	Q1
GDP	-0.5	0.5	0.7	3.7	-3.9	0.3
Total Domestic Demand	0.5	0.9	0.7	3.9	-2.7	0.4
Consumption	1.8	1.1	-0.9	4.3	-2.6	0.3
Investment	-1.4	1.1	1.9	3.7	-5.0	-1.8
Government Consumption	0.9	2.3	0.1	6.6	0.4	9.2
Exports	-2.3	5.3	14.2	0.7	10.0	-0.1
Imports	5.0	8.0	13.6	4.4	18.7	0.6
Net Exports (contribution)	-1.0	-0.3	0.1	-0.5	-0.3	-0.0

1. Annual changes are Q4/Q4.

Data for the second quarter point to continued weakness in private-sector activity. Industrial production fell in April and May, but the April-May average remained 0.8 percent higher than the first-quarter average. New car registrations, an important indicator of durable consumption and machinery orders, have declined considerably so far in the second quarter. The unemployment rate worsened in April but improved slightly in May. However, the job offers/applicants ratio deteriorated in both April and May, suggesting that the labor market may have deteriorated further. In May, the government announced fiscal measures totaling 0.5 percent of Japan's GDP to cope with the recent appreciation of the yen. Recently, it was announced that a larger fraction of planned spending will occur in the next several months.

In the Bank of Japan's May Tankan survey, the index of business sentiment of major manufacturing firms registered -16, less negative than the previous survey taken in February. This was the fifth consecutive increase after more than four years of decline. However, firms predicted a fall in investment of 8.3 percent in the fiscal year that began in April 1995, worse than the 5.6 percent drop predicted in February.

JAPANESE ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994		1995				
	Q3	Q4	Q1	Q2	Mar	Apr	May
Industrial Production	1.7	1.6	1.6	n.a.	1.4	-0.2	-0.3
Housing Starts	-2.6	-0.1	-1.9	n.a.	-7.8	n.a.	n.a.
Machinery Orders	19.3	-1.7	5.1	n.a.	-3.8	-3.9	n.a.
New Car Registrations	6.0	-4.0	10.9	n.a.	8.7	-19.0	5.9
Unemployment Rate (%)	3.0	2.9	3.0	n.a.	3.0	3.2	3.1
Job Offers Ratio[1]	0.63	0.64	0.66	n.a.	0.66	0.65	0.63
Business Sentiment[2]	-39	-29	-21	-16	--	--	--
Wholesale Prices[3]	-1.5	-1.2	-0.9	n.a.	-1.1	-1.5	-1.8

1. Level of indicator.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.
3. NSA; percent change from previous year.

The yen's appreciation has contributed to deflationary pressures. Falling wholesale prices have fed through to a decline in consumer prices; nationwide consumer prices in April were down 0.2 percent from a year earlier. Furthermore, price indices using sales at selected supermarkets show 12-month deflation of over 4 percent.

Recent information on Germany is limited as the conversion of data on orders, production, and sales to new EU methods has delayed the publication of these series and impaired their comparability with previous data. However, some slowing in the economy from last year's rapid pace appears to have occurred. In western Germany, industrial production fell 4.1 percent in the first quarter, but much of this decline has been attributed to the changeover in statistical methods. Meanwhile, first-quarter capacity utilization showed another strong gain. However, the unemployment rate has remained constant at 8.2 percent since late last year. The pan-German volume of retail sales rose 1 percent in April from a year earlier after falling in the first quarter from their previous-year level.

WEST GERMAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994	1995					
	Q4	Q1	Feb	Mar	Apr	May	June
Industrial Production	2.5	-4.1	2.1	-3.0	n.a.	n.a.	n.a.
Capacity Utilization	84.2	85.2	--	--	--	--	--
Unemployment Rate (%)[1]	8.2	8.2	8.2	8.2	8.2	8.2	n.a.
Production Plans[2]	17.8	13.7	14	11	3	5	n.a.
Orders	4.1	n.a.	1.6	n.a.	n.a.	n.a.	n.a.
Consumer Prices[3]	2.8	2.3	2.4	2.3	2.3	2.2	2.3

1. Total labor force, including the self-employed.
2. Percent of manufacturing firms planning to increase production in the next six months less those planning to decrease production.
3. NSA; percent change from previous year. June figure is preliminary.

Production plans have been lowered sharply in the wake of the appreciation of the DM that has occurred this year. The net percentage of firms that expect to increase production over the next six months averaged 4 percent in April and May after peaking near 20 percent late last year. Firms' assessment of their inventory situation also worsened slightly between January and May.

The appreciation of the DM has helped restrain inflation recently, as import prices fell in each of the three months ending in April. Western German consumer price inflation dropped to 2.2 percent on a 12-month basis in May, its lowest level in over six years. However, preliminary data indicate that inflation increased to 2.3 percent in June, contrary to expectations of further deceleration. There were some special factors affecting the preliminary inflation data, including oil price increases. However, some of the rise was in the service sector and is thought to reflect the relatively high wage settlements that have occurred this year.

In eastern Germany, production rose 2.1 percent in the first quarter. However, these data are affected by the same problems as the western German data. The unemployment rate in May was 13.3 percent, about two percentage points below its year-ago level.

EAST GERMAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994		1995				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	0.0	4.9	2.1	13.0	-7.3	n.a.	n.a.
Orders	6.5	4.8	n.a.	7.9	n.a.	n.a.	n.a.
Unemployment Rate (%)[1]	14.5	13.3	14.5	14.7	14.2	13.9	13.3

1. Total labor force, including the self-employed.

In France, real GDP growth was 2.9 percent (SAAR) in the first quarter, down slightly from the rate registered in the fourth quarter. This slowing was more than accounted for by a negative contribution from inventories. Investment growth picked up, but consumption remained relatively weak after declining in the fourth quarter. Net exports made a substantial positive contribution to growth as import growth dropped sharply.

Monthly indicators for the second quarter have been mixed. In April, capacity utilization in manufacturing and investment intentions remained unchanged from January according to a quarterly business survey by INSEE, the French statistics institute. The June INSEE survey of

FRENCH REAL GDP
(Percent change from previous period, SAAR)[1]

	1993	1994	1994 Q2	1994 Q3	1994 Q4	1995 Q1
GDP	-1.0	4.0	5.5	3.6	3.2	2.9
Total Domestic Demand	-2.4	4.6	3.1	4.5	2.2	1.1
Consumption	-0.1	1.5	3.9	2.5	-0.2	1.5
Investment	-5.7	4.7	5.2	7.8	3.8	6.1
Government Consumption	2.7	0.8	1.0	1.8	1.3	2.0
Inventories (contribution)	-1.7	2.5	-0.5	1.0	1.3	-1.4
Exports	3.0	7.5	16.7	0.7	15.8	6.7
Imports	-2.6	9.7	7.3	3.6	11.7	0.3
Net Exports (contribution)	1.5	-0.6	2.3	-0.8	1.0	1.8

1. Annual changes are Q4/Q4.

business confidence indicated that businessmen expect production to weaken. It also showed that orders declined, while inventories rose slightly. On the other hand, consumption of manufactured products (equal to one-third of total consumption) rebounded strongly in April and May.

Consumer prices in May were 1.6 percent above their year-earlier level. This good inflation performance was partly due to relatively moderate wage inflation. Hourly wages in the first quarter were 2.2 percent above their year-earlier level, up slightly relative to the increase registered in the fourth quarter.

Prime Minister Juppé presented the new French government's mini-budget for 1995 on June 22. The budget seeks to fulfill President Chirac's promise to reduce unemployment and maintain progress towards meeting the Maastricht budget criterion. The budget contains significant job creation measures but, on balance, shifts fiscal policy toward a more restrictive stance. Although it leaves the 1995 central government budget deficit target unchanged at 4.6 percent of GDP, it

FRENCH ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994		1995				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	2.0	-0.0	1.6	0.2	0.9	n.a.	n.a.
Unemployment Rate (%)[1]	12.5	12.4	12.1	12.3	11.7	11.6	n.a.
Consumption of Manufactured Products	1.6	-0.2	-0.7	1.0	-0.6	0.4	1.3
Consumer Prices[2]	1.6	1.6	1.7	1.7	1.8	1.6	1.6

1. Break in series starting in March due to annual benchmark revision. Historical data are not yet available.
2. NSA; percent change from previous year.

increases taxes significantly in order to prevent a projected overshooting of the target. In particular, the VAT was increased by 2 percentage points to 20.6 percent, and the corporate income tax was increased by over 3 percentage points to 36.6 percent.

Growth in the United Kingdom continued to slow in the first quarter from its rapid pace last year. Total real GDP grew 2.7 percent (SAAR), but GDP excluding oil and gas extraction grew only 2.3 percent. Every component of domestic demand fell in the first quarter, while net exports expanded rapidly.

Activity in the second quarter appears to have continued to expand moderately. Industrial production fell in April but was 0.4 percent higher than the first-quarter average. After falling in the first quarter, retail sales continued to be weak in April and May, leaving average April-May sales about 0.3 percent higher than the first-quarter average. Since late last year, consumer expenditure has been diverted from retail sales by overwhelming participation in the new national lottery; the introduction of the lottery is estimated to have reduced retail sales so far this year by about 2 percentage points. As participation in the lottery stabilizes, retail sales growth should pick

UNITED KINGDOM REAL GDP
(Percent change from previous period, SAAR)[1]

	1993	1994	1994			1995
			Q2	Q3	Q4	Q1
GDP	2.6	4.3	6.1	3.7	2.8	2.7
Total Domestic Demand	3.1	3.0	0.5	1.8	5.5	-2.3
Consumption	3.3	2.4	2.4	3.2	3.4	-0.6
Investment	1.7	2.1	-10.6	-0.9	6.2	-0.8
Government Consumption	2.0	0.6	1.4	-0.2	-0.6	-0.1
Inventories (contribution)	0.3	1.0	0.7	0.0	2.4	-1.8
Exports	4.4	10.5	11.8	9.7	10.5	3.3
Imports	4.1	7.0	-5.5	3.0	20.4	-13.0
Net Exports (contribution)	0.0	0.7	4.7	1.7	-2.6	5.0
Non-oil GDP	2.3	3.9	5.3	3.6	2.7	2.3

1. Annual changes are Q4/Q4.

up. Unemployment stabilized in May at 8.3 percent after falling rapidly last year. In the second quarter, production plans fell back from their first-quarter peak but remained quite strong. Over the same period, however, consumer confidence dropped to its lowest level in 2-1/2 years.

UNITED KINGDOM ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994		1995				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	1.3	0.4	0.2	0.3	0.9	-0.3	n.a.
Retail Sales	0.7	0.3	-0.2	1.3	-0.2	-0.1	0.2
Unemployment Rate (%)	9.3	8.8	8.5	8.5	8.4	8.3	8.3
Consumer Prices[1]	2.2	2.2	2.7	2.7	2.8	2.6	2.7
Producer Prices[2]	2.1	2.5	3.6	3.6	3.8	4.2	4.2

1. Retail prices excluding mortgage interest payments. NSA; percent change from previous year.
2. NSA; percent change from previous year.

In Italy, monthly indicators suggest that economic activity increased moderately in the first quarter and gathered strength in the second quarter. After a small increase in the first quarter, industrial production rose in April to a level 2.2 percent higher than the first-quarter average. In addition, a survey of industrial output conducted by Confindustria, the national employers organization, indicated that output increased in the second quarter at a pace significantly above that in the first quarter. The April business confidence survey by ISCO, a government-sponsored research institute, showed a modest improvement in production plans relative to the first quarter and relatively stable orders. The ISCO consumer survey showed that consumer confidence rebounded in April and May. Unemployment fell somewhat in the second quarter to 12 percent from its peak in the first quarter.

Inflation has risen sharply in Italy. In June, data from the eight largest Italian cities pointed to an increase in consumer prices of 5.8 percent relative to their year-earlier level. This rise in measured inflation reflects the effects of the depreciation of the lira, which has pushed up intermediate goods prices, as wage increases have remained modest. Hourly wages in both April and May were 2.8 percent above their year-earlier level; in contrast, wholesale prices in April were 11.3 percent above their year-earlier level.

ITALIAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994	1995					
	Q4	Q1	Q2	Mar	Apr	May	June
Industrial Production	1.5	0.3	n.a.	1.3	0.9	n.a.	n.a.
Cap. Utilization (%)	77.6	78.2	n.a.	--	--	--	--
Unemployment Rate (%)	11.9	12.2	12.0	--	--	--	--
Consumer Confidence[1]	112.7	112.2	n.a.	106.4	109.7	114.8	n.a.
Bus. Sentiment[2] (%)	20	30	n.a.	28	29	n.a.	n.a.
Consumer Prices[3]	3.8	4.4	5.5	4.9	5.2	5.5	5.8
Wholesale Prices[3]	4.6	7.5	n.a.	9.3	11.3	n.a.	n.a.

1. Level of index, NSA.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.
3. NSA; percent change from previous year. June CPI is preliminary.

On May 31, Prime Minister Dini proposed reducing the central government budget deficit from an estimated 7 1/2 percent of GDP this year to 3 percent of GDP in 1998, thus allowing Italy to satisfy the Maastricht budget deficit criterion by 1999. The planned deficit-reduction measures are conditional on optimistic growth and interest rate assumptions. Dini also stated that the government will consider rejoining the ERM in the autumn.

In Canada, real GDP expanded only 0.7 percent (SAAR) in the first quarter, while final domestic demand (not shown) decreased 0.4 percent. Business inventory accumulation rose sharply, contributing 3.9 percent to the quarter's growth. Statistics Canada attributed the sharp deceleration in activity to the combined effects of rising interest rates, strikes in the transportation sector, and a weakening U.S. economy.

CANADIAN REAL GDP
(Percent change from previous period, SAAR)[1]

	1993	1994	1994			1995
			Q2	Q3	Q4	Q1
GDP	3.1	5.4	5.9	5.7	4.7	0.7
Total Domestic Demand	3.6	2.7	3.6	0.1	3.3	3.5
Consumption	1.9	3.3	1.8	1.6	3.9	0.2
Investment	4.7	6.1	10.9	-0.2	8.3	-2.1
Government Consumption	-0.4	-1.8	-3.3	0.0	-1.4	-0.2
Inventories (contribution)	1.6	-0.2	1.0	-0.8	-0.4	3.9
Exports	11.0	20.4	25.6	25.5	30.7	5.3
Imports	11.5	13.0	17.9	10.0	25.0	11.2
Net Exports (contribution)	-0.4	2.4	2.1	5.0	1.8	-2.2

1. Annual changes are Q4/Q4.

Preliminary indicators suggest that activity has weakened in the second quarter. Retail sales picked up slightly in April but remained 0.6 percent below the first-quarter average. Manufacturers' shipments and new orders fell further in April to well below first-quarter averages. Employment was unchanged in May, the sixth consecutive month with little employment growth. Housing starts in May fell to their slowest pace in 13 years. However, consumer price inflation increased further in May to near the top of the Bank of Canada's target band for the end of 1995. The increase in 12-month inflation between February and May reflects in part the removal of the beneficial effects of tax reductions last year.

CANADIAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1994		1995				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	2.3	1.9	0.8	-0.6	-0.7	n.a.	n.a.
Manufacturing Survey:							
Shipments	4.7	5.1	3.3	-1.7	-0.8	-1.1	n.a.
New Orders	6.0	4.1	3.1	-2.1	-0.3	-2.6	n.a.
Housing starts	-6.5	-8.7	-10.0	-5.4	-18.7	5.0	-10.4
Retail Sales	0.8	2.1	-0.1	-0.4	-1.0	0.2	n.a.
Employment	0.9	0.7	0.3	-0.1	0.1	0.0	0.0
Unemployment Rate (%)	10.2	9.7	9.7	9.6	9.7	9.4	9.5
Consumer Prices[1]	0.2	0.0	1.6	1.8	2.2	2.5	2.9

1. Percent change from year earlier.

EXTERNAL BALANCES
(Billions of U.S. dollars, seasonally adjusted)

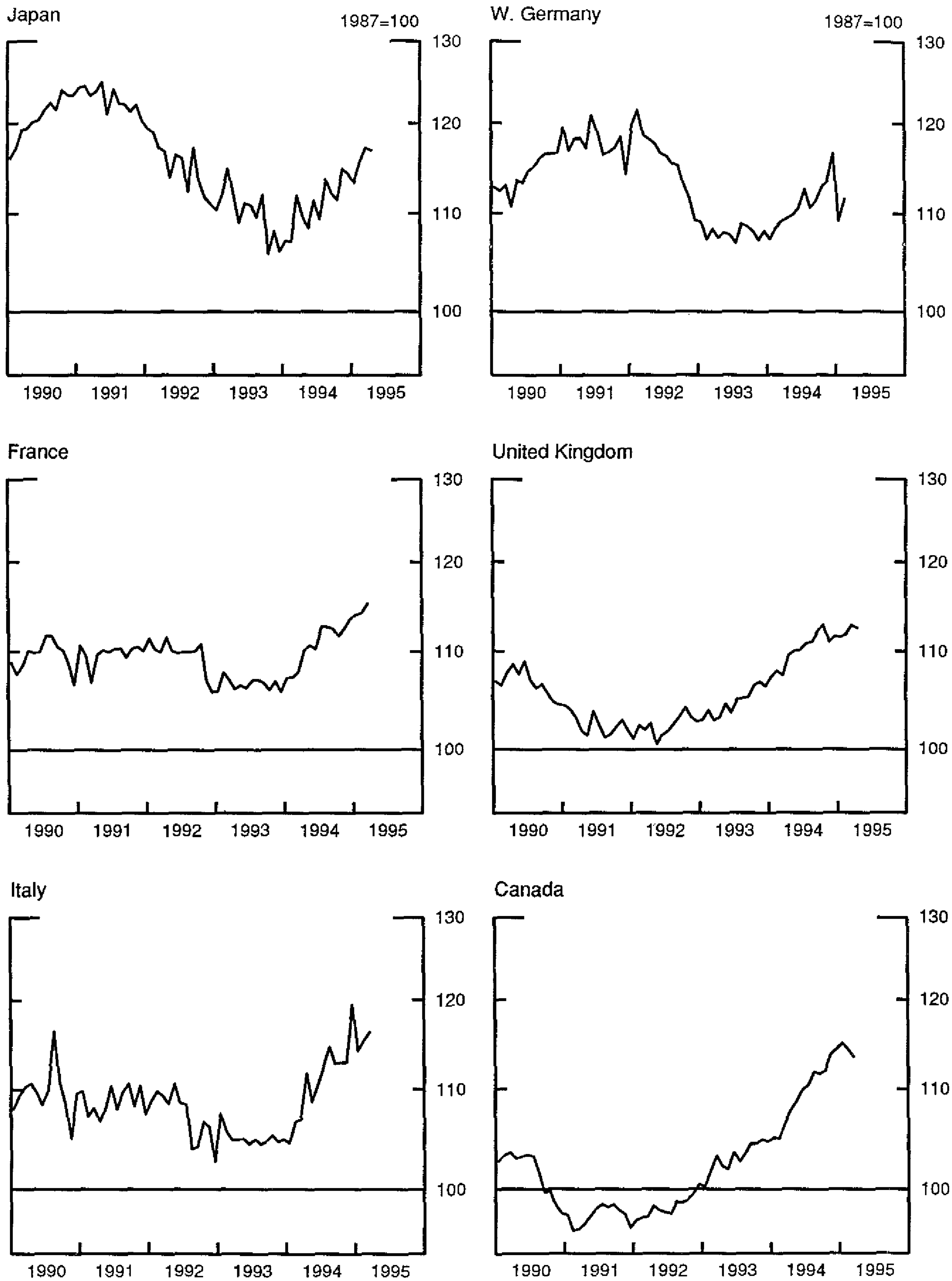
	1994	1994		1995				
		Q3	Q4	Q1	Feb	Mar	Apr	May
Japan: trade	120.9	28.4	30.3	27.4	10.5	9.4	11.1	10.4
current account	129.5	32.0	29.5	29.6	10.4	9.4	8.2	n.a.
Germany: trade	46.0	10.2	14.4	14.2	4.0	4.4	n.a.	n.a.
current account[1]	-22.7	-12.7	-6.5	-2.1	-1.8	0.3	n.a.	n.a.
France: trade	15.5	3.8	5.1	6.1	2.2	2.3	2.7	n.a.
current account[1]	0.8	2.8	3.4	n.a.	--	--	--	--
U.K.: trade	-16.2	-2.8	-4.7	-3.1	-1.1	-0.8	n.a.	n.a.
current account	-2.5	0.7	-0.8	-0.6	--	--	--	--
Italy: trade	21.8	5.4	3.6	n.a.	1.1	n.a.	n.a.	n.a.
current account[1]	15.6	5.0	4.8	-0.6	1.1	0.0	-0.9	n.a.
Canada: trade	11.0	3.5	4.0	4.1	1.4	1.3	1.3	n.a.
current account	-16.3	-3.3	-2.9	-2.8	--	--	--	--

1. Not seasonally adjusted.
-- Data not available on a monthly basis.

6-28-95

Industrial Production in Selected Industrial Countries

(Monthly data; seasonally adjusted; ratio scale, index)



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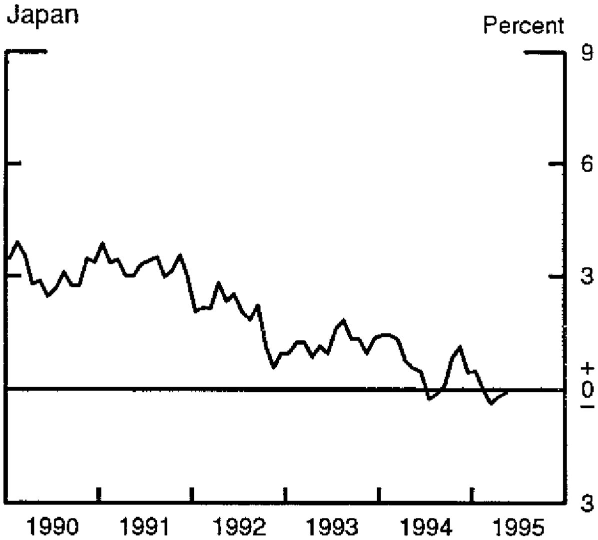
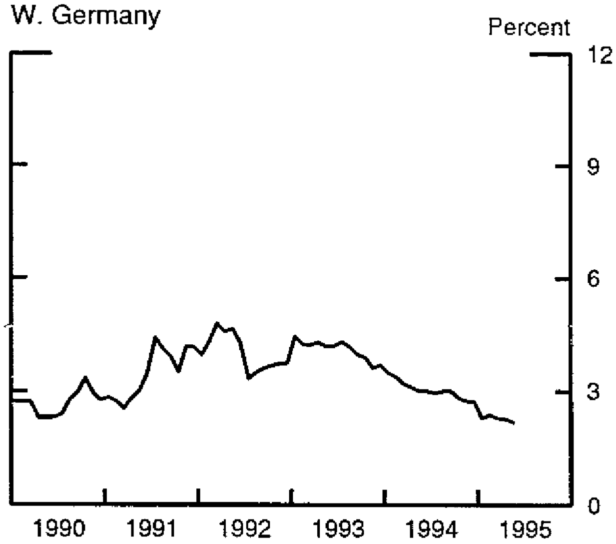
Consumer Price Inflation in Selected Industrial Countries
(12-month change)

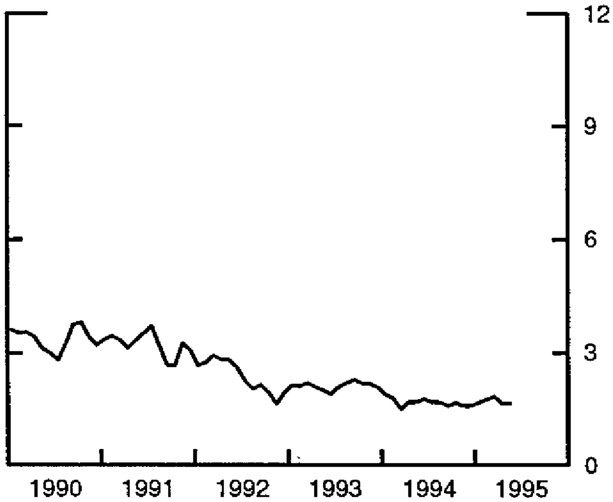
Japan



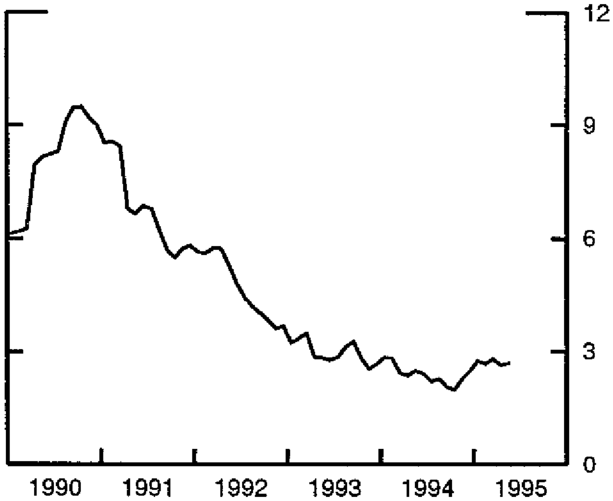
W. Germany



France

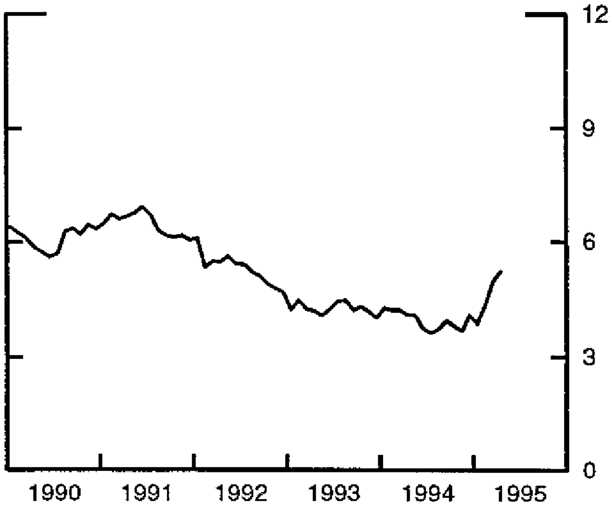


United Kingdom

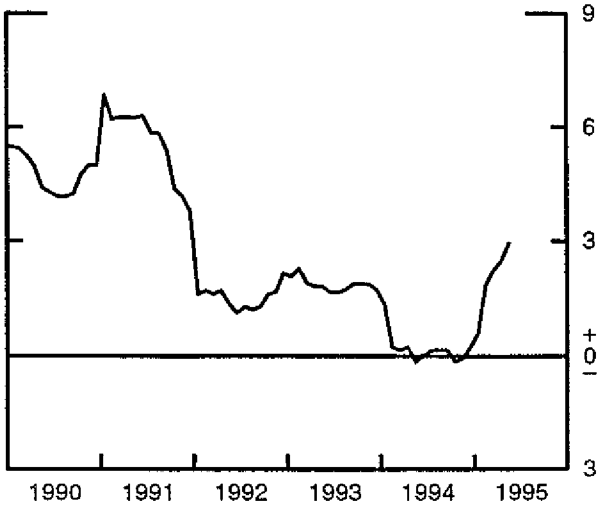


Note: Excludes mortgage interest payments.

Italy



Canada



Economic Situation in Other Countries

Economic activity in Mexico, Argentina, and Venezuela is sluggish, and mounting evidence suggests that Brazil's economy has slowed. The Asian developing countries, in contrast, continue to grow robustly. During the first quarter, real GDP expanded by 9.9 percent in Korea and 7 percent in Taiwan from year-earlier levels. Chinese industrial value added during the first five months of 1995 was 14 percent higher than during the same period last year.

Exports from many developing countries have expanded rapidly in 1995. Through May, exports were up by about 50 percent in China and Argentina and by over 30 percent in Mexico. Import growth has varied widely, contracting in Mexico and Venezuela, while almost doubling in Brazil.

Selected Developing Countries: Export and Import Growth
(January-May 1995, percent change from year-earlier period)

	Mexico	Brazil	Argentina	Venezuela 1/	China	Taiwan	Korea 1/
Exports	31	5	50	16	49	23	33
Imports	-8	93	0	-2	16	24	36

1/ Data through April

Since the last Greenbook, the stripped spread on Argentina's Brady bonds has increased by over 300 basis points, partially reflecting concerns about the country's fiscal situation and whether the currency's dollar parity is sustainable. The stripped spreads on Mexican and Brazilian bonds have also increased, rising 40 basis points and 150 basis points, respectively.

Individual Country Notes. In Mexico, the economy continues its rapid adjustment to the devaluation of the peso and the tightening of fiscal and monetary policy, amid mounting evidence that economic activity is contracting sharply. Industrial production (s.a.) rose 1.3 percent in March from February, but output for the first quarter was 0.7 percent below its year-earlier level. Real domestic demand (GDP less net exports) declined by 10.3 percent in the first quarter of 1995 from its year-earlier level, a much steeper decline than in real GDP and industrial production, reflecting the sharp improvement in Mexican trade performance. Of the components of domestic demand, gross fixed investment fell 18.4 percent, private consumption fell 8.7 percent, but government consumption declined by only 1.9 percent. The urban unemployment rate (n.s.a.) rose to 6.3 percent in April.

MEXICAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q1	Feb	Mar	Apr	May
Real GDP (s.a.)	3.5	-0.6	--	--	--	--
Industrial Production (s.a.)	3.8	-0.7	-1.1	-4.1	--	--
Unemployment Rate (%)	3.2	5.2	5.3	5.7	6.3	--
Consumer Prices[1]	7.0	14.5	4.2	5.9	8.0	4.2
Current Account[2]	-$28.9	-$1.2	--	--	--	--
Trade Balance[2]	-$18.5	$0.5	$0.4	$0.5	$0.8	$0.6

1. Percentage change from previous period.
2. Billions of U.S. dollars, n.s.a.

The (preliminary) merchandise trade balance in May registered a $600 million surplus, compared with a $1.5 billion deficit in May 1994. Exports during the January-May period were 31 percent above their year-earlier level, while imports were down 8 percent. Largely as a result of the improved trade performance, the current account deficit declined to $1.2 billion in the first quarter of 1995, from $6.7 billion in the first quarter of 1994. Mexico's gross international reserves increased to $10.4 billion as of June 23, from $6.9 billion at the end of March. This increase reflects likely continued improvement in the current account performance during the second quarter, moderation of pressures in financial markets leading to an improvement in Mexico's capital account position, and drawings on international support packages.

Consumer prices rose 4.2 percent in May, down from March and April. April's inflation spike partially reflected an April 1 increase in the value-added tax. The decline in May inflation from its March rate also reflects some strengthening of the peso, from an average of about 6.7 pesos per dollar during March to about 6.2 pesos per dollar in recent trading. During the first half of June, consumer prices were 1.7 percent higher than in the second half of May, suggesting a further decline in inflation.

On May 30, Mexico announced the buyout of ailing Mexican financial group Probursa by Spain's Banco Bilbao Vizcaya, which will increase its holdings from 20 percent to 70 percent of Probursa shares. To support the arrangement, which was made possible by a liberalization of laws on foreign ownership of banks earlier this year, the Mexican government will purchase a portion of Probursa's loan portfolio with interest-bearing bonds at its estimated market value, thereby limiting risk to investors. On June 13, it was announced that Mexico's third largest bank, Banco Serfin, would be recapitalized by its shareholders, with the government again providing support by purchasing part of Serfin's loan portfolio but, in this case, without interest-bearing instruments. The government hopes that such arrangements will help recapitalize the Mexican banking system, which is burdened by large amounts of non-performing loans and weak capital-asset ratios.

On June 30, the IMF Executive Board is scheduled to review Mexico's performance under its stand-by arrangement. Waivers for some end-June performance criteria are expected to be granted. The Board is also expected to approve a disbursement schedule for the remaining $10 billion equivalent of Mexico's stand-by.

In Brazil, economic activity was very strong through the first quarter of 1995, but recent evidence suggests that the economy has slowed. First-quarter real GDP was 10.5 percent higher than a year earlier. In April, however, industrial production (s.a.) fell by 1.7 percent. The number of consumers and firms experiencing debt repayment difficulties has also risen sharply in recent months. Since the enactment of the exchange rate-based stabilization program in July 1994, monthly inflation has remained relatively low, registering 2.5 percent in May 1995.

On June 22, the Central Bank adjusted its exchange rate band, moving the *real*-dollar band from 0.88-0.93 to 0.91-0.99. The *real* had been near the mid-point of the previous band, with little intervention by the Central Bank since March. The realignment was motivated by concerns about the external position. Specifically, Brazil continued to record large trade deficits in April and May 1995, bringing the trade deficit to $3.5 billion over the January-May period, reflecting a near doubling in imports; a trade surplus of $5.7 billion was recorded over the same period last year. Surprisingly, the Central Bank announced that international reserves (liquidity concept) rose from $31.8 billion at end-April to $33.7 billion at end-May 1995.

Central Bank President Arida unexpectedly resigned on June 1. Former Central Bank President Gustavo Loyola (previously in office November 1992-April 1993) is his replacement. On June 1, in response to evidence that the economy is slowing, the Central Bank lowered the overnight rate on federal government securities from 65 percent a year to 61 percent a year and relaxed reserve requirements. On June 21, the Central Bank also moved to ease the consumer debt burden by allowing banks to reschedule consumer debts that were delinquent as of May 31.

In Argentina, industrial production in May was 3.6 percent below its 1994 level. The recent slowdown in economic activity has contributed to a rapid turnaround in Argentina's trade deficit during the last three months, leading to a surplus of $770 million in May, reflecting a 50 percent increase in exports and no growth in imports from a year earlier.

Gross international reserves stood at $13.5 billion as of mid-June, of which $2.1 billion was in dollar-denominated Bonex bonds. The monetary base was $11.1 billion, leaving $2.4 billion in excess reserves. May consumer prices increased by 4.4 percent from a year earlier.

Argentina's fiscal situation remains difficult. Tax revenues during May were 6 percent below the government's forecasts, due to the weakness in economic activity. Concerns that Argentina will not achieve the fiscal objectives outlined in its IMF program (perhaps necessitating a waiver of program requirements), coupled with political conflicts between Finance Minister Cavallo and Cabinet Chief Bauza, have led to sharp price declines in Argentina's financial markets. Between June 6 and June 9, the Merval stock index and Argentina's Brady bond prices each fell by more than 10 percent. Asset prices have since recovered only slightly. In an effort to meet IMF fiscal requirements, Argentina brought forward a wealth tax payment that was due later in the year and postponed payments to government employees from the last week of June to the first weeks of July.

Banking sector reform has progressed little since the May presidential election, possibly due to government concerns that rapid reform would further increase unemployment. Bank deposits have remained stable at $39 billion.

In Venezuela, a continuing recession has led to an increase in the unemployment rate from 7.8 percent in December 1994 to 11.4 percent in March, according to official figures. Private sector analysts, however, estimate that the jobless rate may have reached 15 percent. Venezuela registered a trade deficit of $341 million in April, up from a deficit of $191 million in March. Total reserves excluding gold were an estimated $7.9 billion at the end of May, almost unchanged from the end of April. Monthly consumer price inflation was 4.9 percent in May, up from 4.1 percent in April. During the first five months of 1995, consumer prices increased by 18.9 percent, similar to the same period last year.

In late May, the government reached preliminary agreement on an anti-inflation pact with business and labor; a formal pact is expected to be signed by the end of June. The government has promised increased fiscal and monetary discipline in exchange for moderation in private sector wage and price increases.

In China, industrial value added during the first five months of 1995 was 14 percent higher than a year earlier, compared with 18 percent growth for all of 1994. Consumer prices in May were 20 percent higher than a year earlier.

In the first five months of 1995, China ran a trade surplus of $10.3 billion, sharply improved from a $2 billion deficit during the same period of 1994. Through May, exports jumped 49 percent and imports rose 16 percent from the year-earlier period. According to Chinese trade statistics, exports have been strong to all major trading partners. In the first four months of 1995 (the latest period for which detailed data are available), Chinese exports rose 58 percent to Japan, 45 percent to the European Union, and 37 percent to the United States. The export surge may be slowing, however, as exports increased by 64 percent in the first quarter, but by 35 percent in April and May.

Equity markets in China continue to be volatile. The Shanghai stock market rose nearly 60 percent in three days during mid-May, for example, after the authorities banned the sale of treasury bond futures. The market then fell 17 percent when the authorities announced that they were considering allowing new stock listings in 1995.

In Taiwan, real GDP rose 7 percent in the first quarter of 1995 from the year-earlier period. Consumer prices at the end of May were 3.3 percent higher than a year earlier. In the first five months of 1995, Taiwan ran a trade surplus of $2.3 billion, similar to the $2 billion surplus during the same period last year. Through May, exports rose 23 percent and imports increased 24 percent from a year earlier. Foreign exchange reserves less gold reached $100 billion at the end of May 1995, up $8 billion from the end of 1994.

Real output in Korea increased by 9.9 percent during the first quarter of 1995 from its level a year earlier, despite the adoption of a less accommodative monetary policy during the second half of 1994. Thus far, the strong growth experienced during the recent cyclical upturn has been consistent with a moderate level of consumer price inflation. Consumer prices in May were 5.1 percent higher than a year earlier.

Korea's exports expanded at the most rapid pace in nearly a decade during the early months of 1995, due in part to the appreciation of the Japanese yen and continued strong demand for Korea's technologically sophisticated manufactured goods. Exports in the first four months of 1995 increased by 33 percent from their year-earlier level in dollar terms. However, imports increased by 36 percent over the same period due to rapid growth in investment demand and to rising import prices. This contributed to a widening of the current account deficit to $4.6 billion during the first four months of the year, compared with a deficit of $2.4 billion a year earlier.

In Russia, the ruble continued to appreciate against the dollar, rising by 3 percent during May and 10 percent during the first four weeks of June. The ruble's recent strength reflects declining inflationary expectations and subsequent increases in demand for ruble-denominated assets. In mid-June, the Central Bank of Russia (CBR) reduced its refinance rate from 16.3 percent to 15 percent a month, in an attempt to stem the ruble's appreciation. The CBR has also sold rubles frequently in the foreign exchange market. This effort to limit the ruble's appreciation (while allowing the Central Bank to replenish its official reserves) has caused Russia's monetary aggregates to grow rapidly. Broad money, after expanding by less than 10 percent during the first quarter, jumped by 15 percent during April and another 7 percent during May. As a result, inflation has remained stubbornly high. Consumer prices increased by 8 percent in May, little changed from the 8.5 percent increase in April and the 9 percent increase in March. Russia's IMF stand-by arrangement anticipates monthly inflation of one percent during the last six months of 1995, which seems increasingly unrealistic.

The budget deficit through May registered 4 percent of GDP, consistent with the IMF program. A number of fiscal problems, however, are emerging: revenue collection is less than projected, the growth of tax arrears is accelerating, and the government has not fully implemented the tax increases on the energy sector outlined in the stand-by. In addition, seasonal pressures to fund the harvest and provide credits to the Northern Regions will increase demand for fiscal expenditures in coming months.

The decline in economic activity continues to slow. During the first five months of 1995, real GDP was 3 percent below its year-earlier level and industrial production was down by 4 percent. During the first five months of 1994, by contrast, industrial production plunged 25 percent and real GDP declined 17 percent from a year earlier.

On May 26, the IMF Executive Board approved the first $550 million equivalent monthly disbursement under Russia's stand-by arrangement. The Executive Board is scheduled to consider the second disbursement on July 14.