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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).

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Confidential (FR) Class III FOMC

Part 2

November 6, 1996

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

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

Confidential (FR) Class III FOMC

November 6, 1996

RECENT DEVELOPMENTS

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DOMESTIC NONFINANCIAL DEVELOPMENTS

The pace of economic expansion slowed considerably in the third quarter, and early indications point to only moderate growth this quarter. Although unemployment has remained low and anecdotal reports suggest competition for labor, official data show wage increases to have been subdued in recent months; meanwhile, there has been no discernible change in the trend of core consumer price inflation.

Real GDP

According to BEA's advance estimate, real GDP rose 2.2 percent at an annual rate in the third quarter after increasing 4.7 percent in the second quarter. The slowdown in growth was concentrated in final sales, which edged up just 0.3 percent after increasing more than 4 percent during the second quarter. Residential investment, government purchases, and net exports all declined last quarter, and personal consumption expenditures were little changed.

In contrast, business investment spending advanced at a brisk pace. Real outlays for business fixed investment increased nearly 15 percent, led by strong purchases of transportation and information-processing equipment. Inventory investment also rose sharply, with some firms perhaps rebuilding stocks that had become too lean when sales surged in the first half; the rise in inventory investment contributed nearly 2 percentage points to overall GDP growth last quarter.

REAL GDP AND SELECTED COMPONENTS IN 1996:Q3
(Percent change; annual rate)

	BEA advance	Staff estimate
Real GDP	2.2	2.5
Final sales	.3	.5
Business fixed investment	14.7	16.2
Producers' durable equipment	18.9	19.7
Nonresidential structures	3.3	6.5
Residential structures	-5.7	-6.6
State and local government	.2	1.7

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

	1994	1995	1996 Q1	1996 Q2	1996 Q3	1996 Aug.	1996 Sept.	1996 Oct.
	Average monthly changes							
Nonfarm payroll employment[2]	318	185	205	262	160	280	-35	210
Private	295	176	189	245	129	158	32	250
Manufacturing	33	-12	-29	6	-22	24	-59	6
Durable	28	5	-15	24	-7	31	-35	-2
Transportation equipment	5	-3	-13	16	-1	18	-13	-10
Nondurable	5	-17	-14	-19	-15	-7	-24	8
Construction	25	9	39	20	15	10	8	10
Trade	91	54	22	82	56	19	37	81
Finance, insurance, real estate	-3	4	15	12	12	12	4	26
Services	134	110	126	113	70	84	56	119
Business services	54	33	32	43	30	44	8	2
Total government	23	9	16	17	31	122	-67	-40
Private nonfarm production workers[2]	267	152	157	213	102	122	-10	195
Manufacturing production workers	34	-10	-30	5	-15	12	-38	7
Total employment[3]	261	32	390	153	253	171	313	259
Nonagricultural	225	51	336	188	202	253	198	336
Memo:								
Aggregate hours of private production workers (percent change)[2]	.4	.1	.3	.5	.1	.6	.9	-.9
Average workweek (hours)[2]	34.6	34.5	34.3	34.4	34.4	34.4	34.7	34.3
Manufacturing (hours)	41.9	41.6	40.9	41.7	41.7	41.7	41.8	41.6

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

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

	1994	1995	1996 Q1	1996 Q2	1996 Q3	1996 Aug.	1996 Sept.	1996 Oct.
Civilian unemployment rate (16 years and older)	6.1	5.6	5.6	5.4	5.2	5.1	5.2	5.2
Teenagers	17.6	17.3	17.4	16.3	16.4	17.2	15.6	16.1
20-24 years old	9.7	9.1	9.8	9.3	8.9	8.3	8.7	8.8
Men, 25 years and older	4.8	4.3	4.3	4.1	3.9	3.8	4.0	3.8
Women, 25 years and older	4.9	4.4	4.3	4.3	4.2	4.1	4.1	4.1
Full-time workers	6.1	5.5	5.5	5.3	5.1	4.9	5.1	5.1
Labor force participation rate	66.6	66.6	66.7	66.7	66.8	66.7	66.8	66.9
Teenagers	52.7	53.5	52.6	52.5	51.6	50.1	52.4	52.5
20-24 years old	77.0	76.6	76.9	77.0	76.4	75.6	77.0	77.4
Men, 25 years and older	76.0	76.0	76.0	76.1	76.4	76.5	76.2	76.3
Women, 25 years and older	58.1	58.3	58.4	58.6	58.9	58.9	58.8	58.8

Since the publication of the BEA estimate, additional source data have become available. Notably, manufacturing inventories and construction put in place turned out to be stronger in September than BEA had assumed. All else equal, the new data would point to a third-quarter increase in GDP of about 2-1/2 percent. The estimates of third-quarter spending discussed in the remainder of this section incorporate the new data; the new estimates are summarized in the table on II-1.

Labor Market Developments

Payroll employment increased 210,000 last month after falling in September. On a moving average basis, payroll growth has moderated since midyear but has remained substantial. Employment gains in the household survey have been hefty, too, and the unemployment rate has moved down to 5.2 percent in recent months even as labor force participation has moved up.

Other indicators also appear consistent with a relatively strong labor market. New claims for state unemployment insurance have averaged 331,000 over the past four weeks, about equal to the average in September and only slightly higher than the cyclical low. The Conference Board index of help-wanted advertising edged up in September to the high end of the narrow range that has held since early 1995. The Michigan Survey of unemployment expectations inched higher in October but remained at a quite optimistic level. Similarly, although the Conference Board's consumer survey showed a mild decline in perceived job availability conditions last month, the index remained at a relatively favorable level.

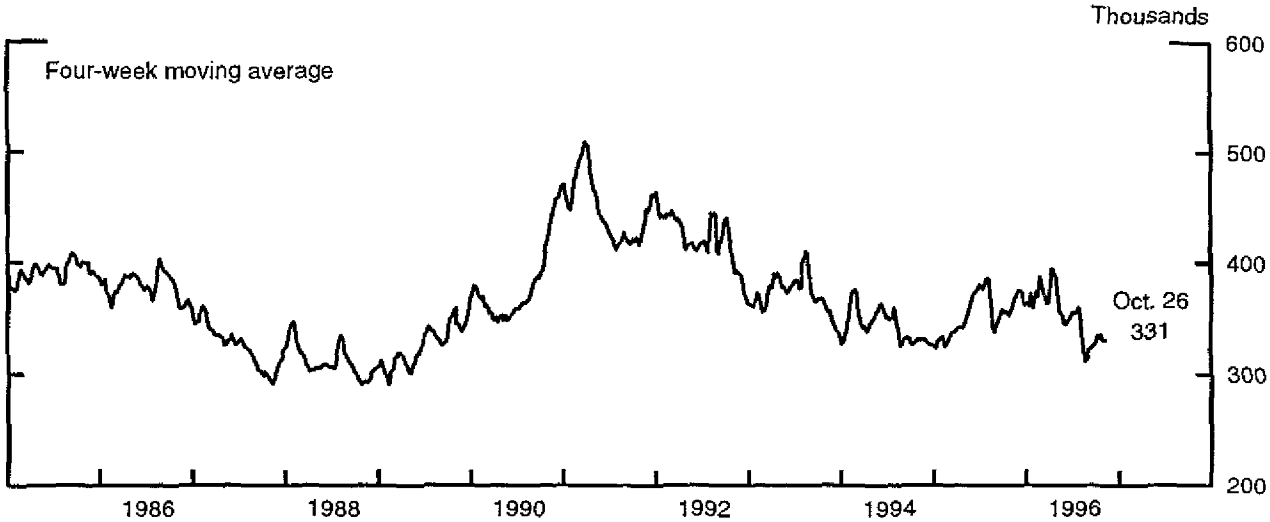
The rebound in productivity growth registered earlier this year apparently came to a halt in the third quarter. The official estimates that will be released tomorrow likely will show that output per hour in the nonfarm business sector edged down about 1/2 percent in the third quarter after rising at a 1.2 percent annual rate in the first half.

Industrial Production

On the basis of production-worker hours and limited data on physical output, we believe that industrial activity fell appreciably in October after rising about 0.2 percent per month on average during the third quarter. Much of the slackening is attributable to labor disruptions in the motor vehicles sector.

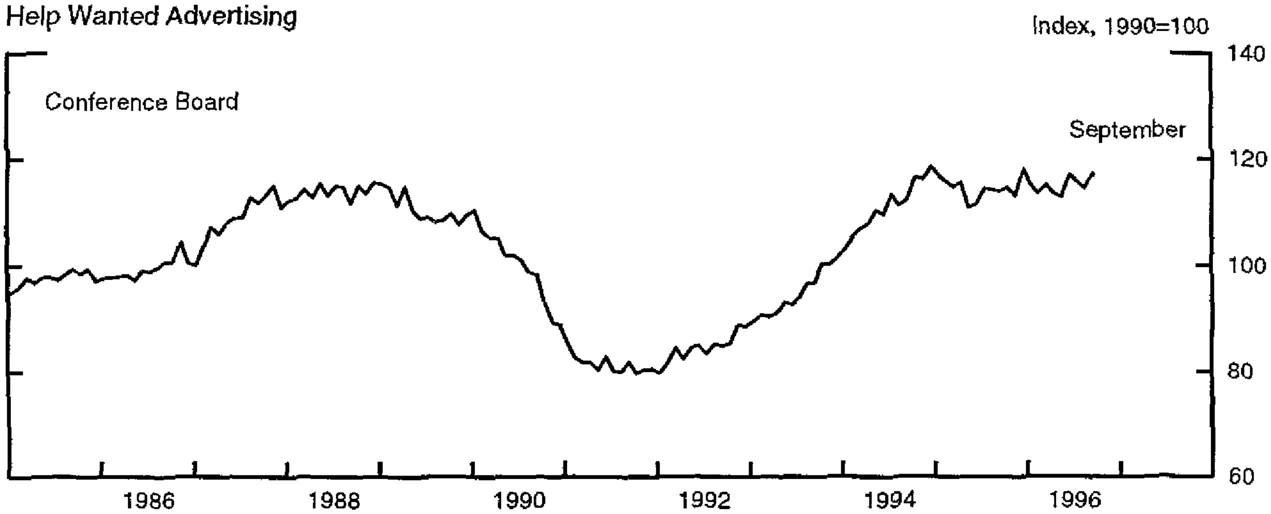
Labor Market Indicators

Initial Claims for Unemployment Insurance



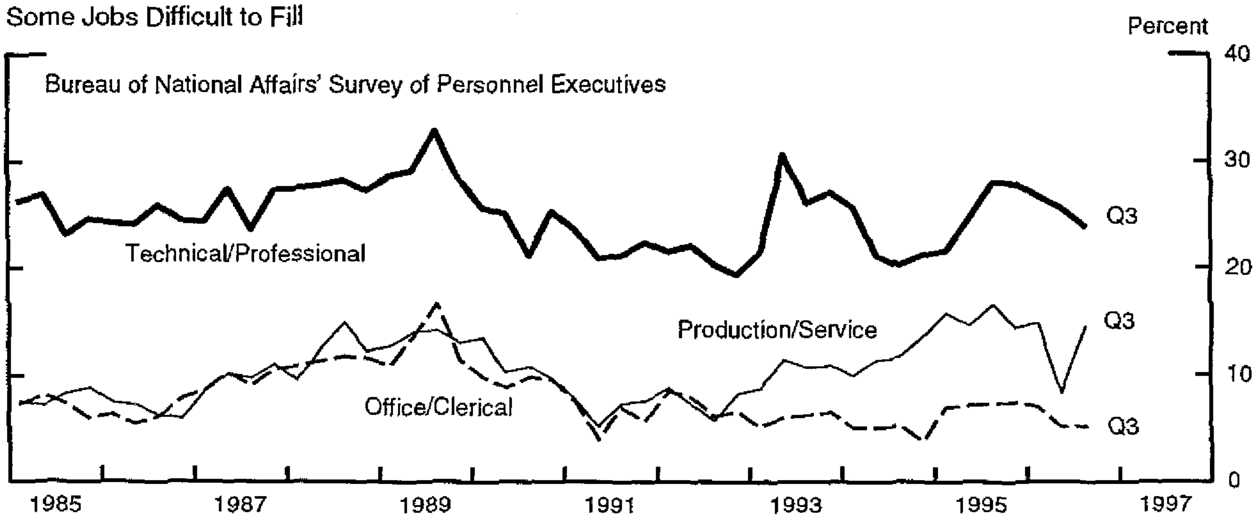
Note. State programs, includes EUC adjustment.

Help Wanted Advertising



Note. Series has been adjusted to take account of various structural and institutional changes, including consolidation of the newspaper industry and a tendency toward increased hiring through personnel supply agencies.

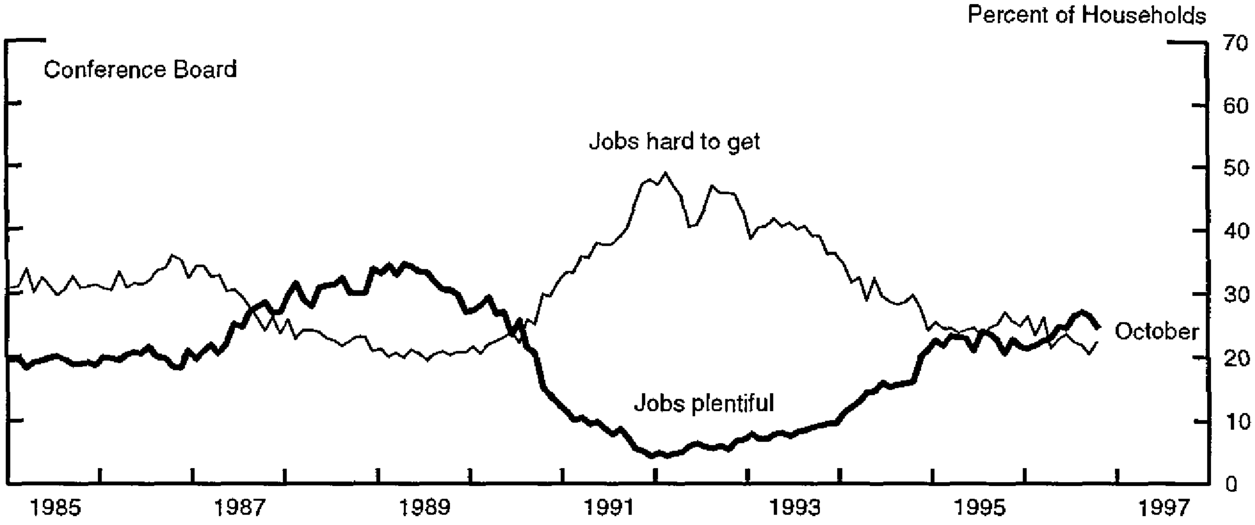
Some Jobs Difficult to Fill



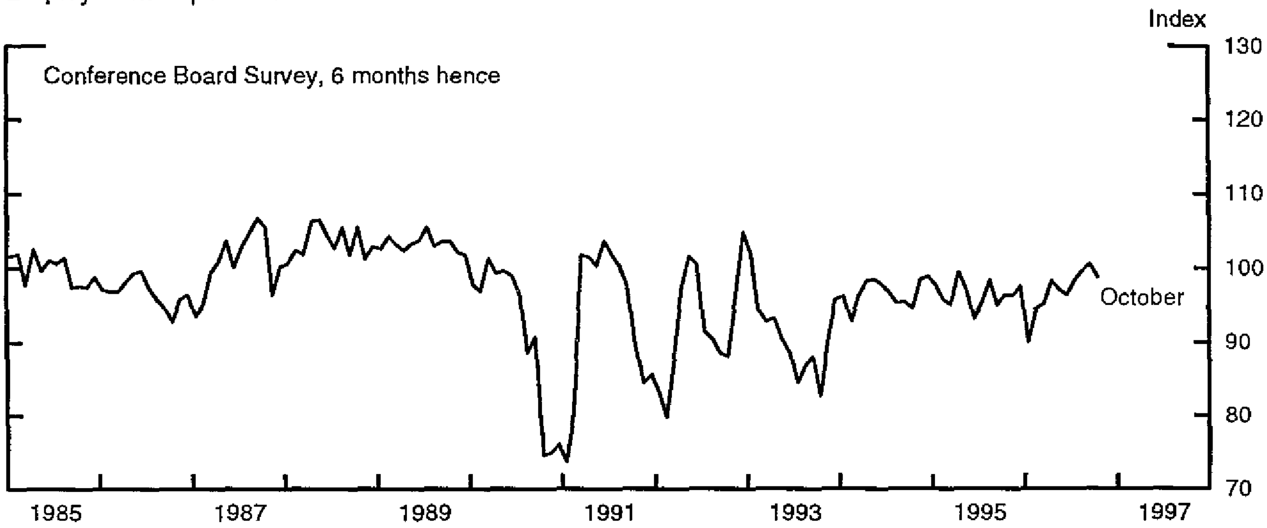
Seasonally adjusted by FRB staff.

Consumer Surveys of Labor Market Conditions

Job Availability

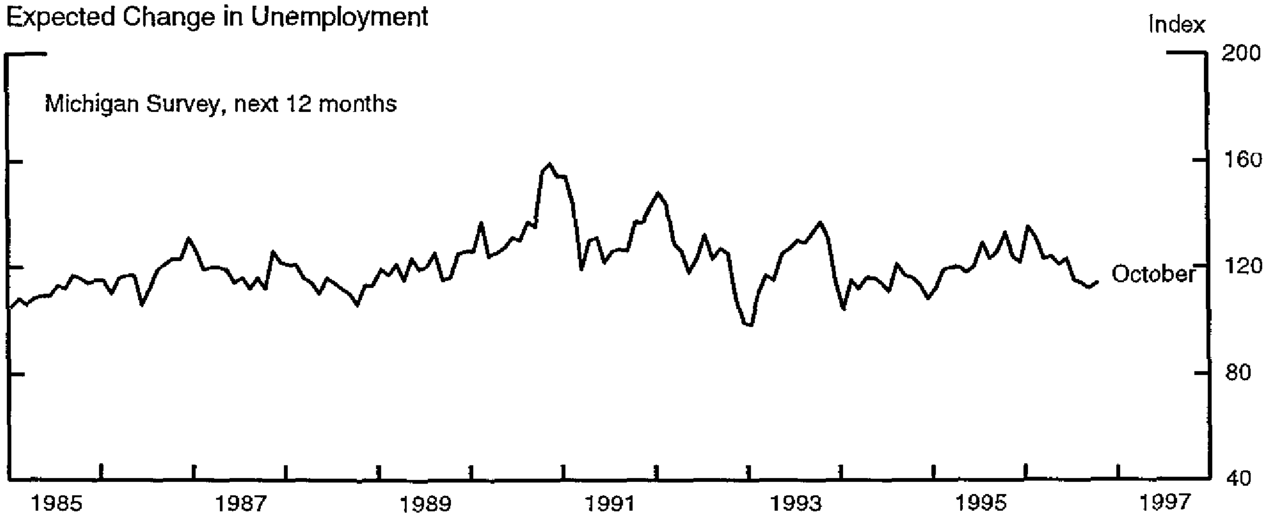


Employment Expectations



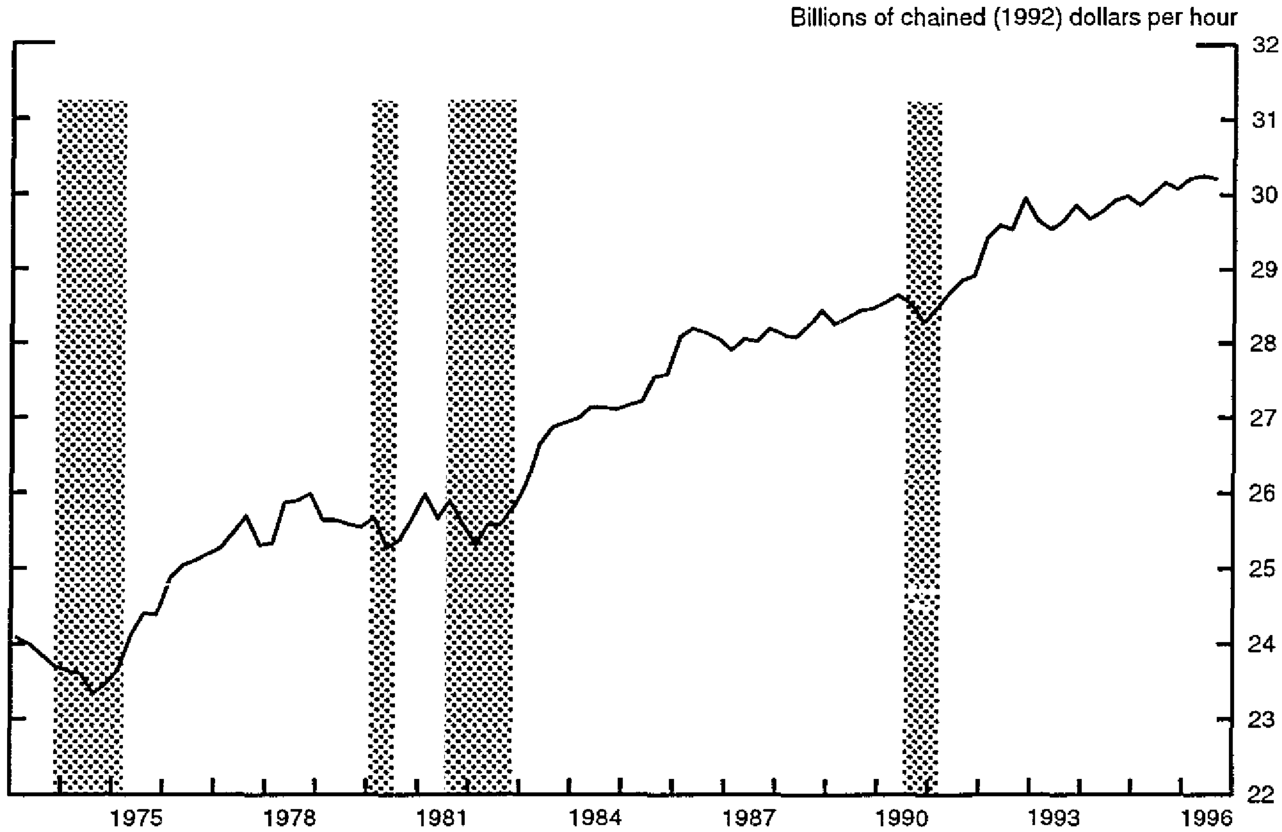
Note. Percentage of households responding "more jobs" minus percentage responding "fewer jobs" plus 100.

Expected Change in Unemployment



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

Productivity in the Nonfarm Business Sector



1996 Q3 data are unpublished BEA data.

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

	Proportion 1995:Q4	1995[1]	1996 Q1	1996 Q2	1996 Q3	1996 July	1996 Aug.	1996 Sept.
			----Annual rate	-----		--Monthly rate	---	
Total index	100.0	1.6	3.0	6.7	4.4	.0	.4	.2
Previous		1.6	3.0	6.7		.0	.4	
Manufacturing	86.5	1.4	2.4	7.1	5.4	.3	.1	.2
Motor veh. and parts	5.5	-2.6	-20.7	46.6	15.3	3.9	-2.0	-2.3
Aircraft and parts	1.7	-17.1	64.0	15.4	22.6	2.2	1.5	3.3
Manufacturing excluding motor vehicles, aircraft, and parts	79.2	2.2	3.0	4.6	4.3	.0	.2	.4
Consumer goods	23.1	.1	.2	.4	1.7	.3	-.5	.3
Durables	3.7	-.4	-5.4	8.2	-1.8	-2.4	-.8	-1.0
Nondurables	19.4	.2	1.2	-1.0	2.3	.8	-.4	.6
Business equipment	13.6	7.7	13.9	8.1	8.1	.2	.9	.9
Office and computing	3.1	36.2	48.4	45.5	41.0	3.0	2.7	2.3
Industrial	4.3	3.5	4.1	-3.7	-3.1	-.3	.4	.0
Other	6.1	.8	4.9	-3.5	-1.8	.0	.2	-.1
Defense and space equipment	1.7	-7.3	-1.7	6.1	10.6	1.5	1.3	-.6
Construction supplies	5.3	-.4	.6	7.7	6.2	-1.3	.7	.2
Materials	28.7	3.4	3.6	6.4	4.7	.1	.5	.0
Durables	20.3	6.3	7.1	4.1	5.7	-.2	1.1	.0
Nondurables	8.2	-2.8	-5.0	12.6	2.6	.9	-.8	.0
Mining	6.0	-1.8	1.9	10.5	7.0	-1.3	2.4	-.2
Utilities	7.5	6.2	8.9	1.3	-7.5	-2.7	1.7	.4
Memo:								
Information-related products[2]	11.2	21.4	21.6	20.1	16.6	.9	1.6	1.0

1. From the final quarter of the previous period to the final quarter of the period indicated.
2. Includes computer equipment, computer parts, semiconductors, communications equipment, and selected instruments.

NEW ORDERS FOR DURABLE GOODS
(percent change from preceding period, seasonally adjusted)

	Share 1996 H1	1996 Q2	1996 Q3	1996 July	1996 Aug.	1996 Sept.
Total durable goods	100.0	1.6	1.9	1.4	-3.6	4.9
Nondefense aircraft	4.0	-28.1	18.5	29.6	-39.7	126.8
Adjusted durable goods orders[1]	68.0	2.0	1.8	2.3	-2.6	.7
Office & computing machines	5.0	1.6	4.9	3.0	-.3	-2.6
Nondefense capital goods excluding aircraft and computers	17.0	-2.7	2.0	3.9	-6.3	4.2
Chain-weighted real adj. orders[2]		2.7	2.2	2.5	-2.5	.7

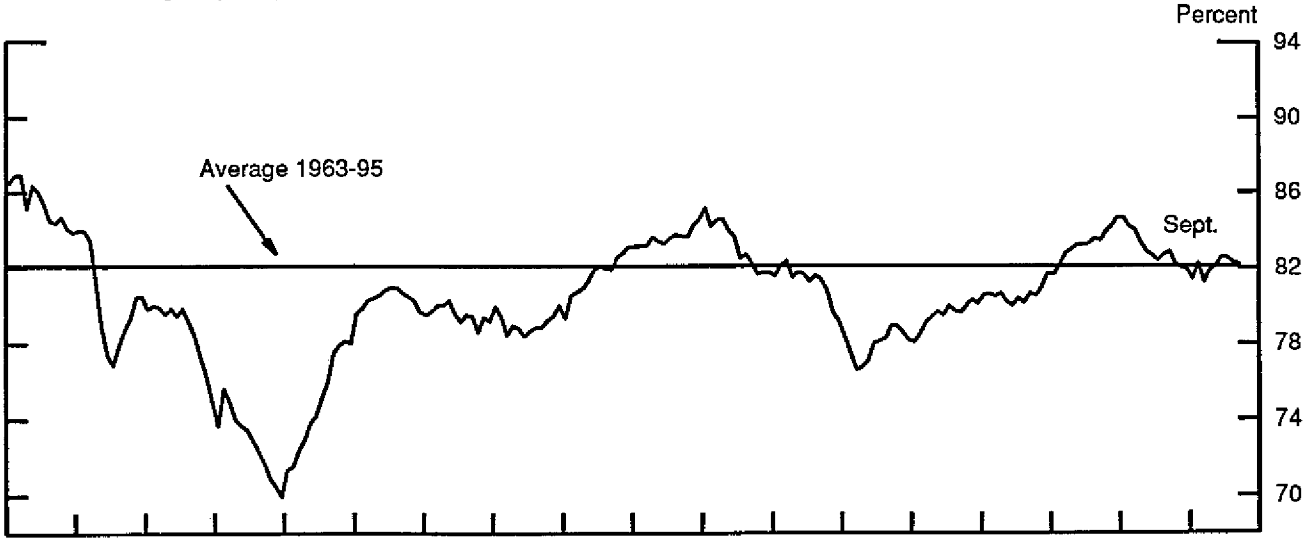
1. Orders excluding defense capital goods, nondefense aircraft, and motor vehicle parts.
2. Nominal adjusted durable goods orders were split into two components, computers and all other. These components were deflated and then aggregated in a chain-weighted fashion.

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

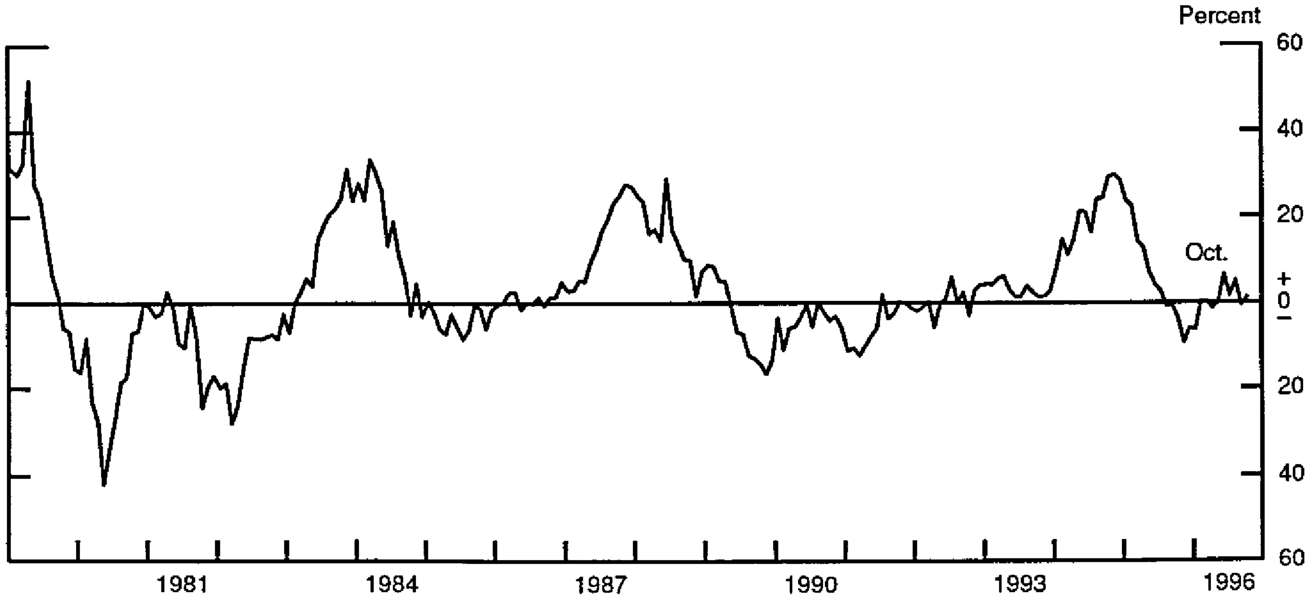
	1988-89	1963-95	1995	1996		1996		
	High	Avg.	Q3	Q2	Q3	July	Aug.	Sept.
Manufacturing	85.2	82.1	82.6	82.2	82.4	82.5	82.3	82.2
Primary processing	89.0	83.4	86.6	86.1	86.4	86.6	86.3	86.2
Advanced processing	83.5	81.5	80.9	80.5	80.7	80.8	80.7	80.5

Manufacturing Sector

Manufacturing Capacity Utilization



Vendor Performance*



*Percent of respondents in the purchasing managers survey reporting slower supplier deliveries minus those reporting faster deliveries, seasonally adjusted.

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

	1996				
	Aug.	Sept.	Oct.	Q3	Q4 (Sched.)
U.S. production	12.6	12.1	11.2	12.7	11.7
Autos	6.7	6.5	5.6	6.7	5.9
Trucks	5.9	5.6	5.6	6.0	5.8
Days' supply					
Autos	60.5	62.3	61.2	62.3	...
Light trucks	67.2	75.8	71.5	75.8	...

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

After registering a hefty 12-3/4 million unit annual pace in the third quarter, initial plans for motor vehicle production in the fourth quarter showed assemblies dropping back to a 12.1 million unit annual rate. In October, assemblies evidently ran at only an 11.2 million unit annual rate, with about three-fourths of the decline from the third-quarter pace attributable to the disruptions caused by last month's Canadian Auto Workers strike (see discussion below). On balance, the drop in output of motor vehicles and parts is expected to directly shave 0.3 percentage point off October IP growth.

Production also apparently declined slightly last month outside of the motor vehicles sector. Manufacturing production-worker hours (excluding motor vehicles and parts, FRB seasonals) dropped 0.3 percent in October. Hours in most durable goods industries were down, with the exception of lumber, instruments, and stone, clay, and glass. Among the nondurable goods industries, the picture was mixed, with aggregate hours up in food, leather, textiles, and paper but down in apparel, petroleum, rubber and plastics, and chemicals. In industries for which physical output data are available, the production of steel and lumber declined in October, while output of home appliances posted its first gain in four months. Mining output declined in October; electricity generation edged down but remained in its normal range for the season.

Forward-looking indicators of industrial activity provide further evidence of a slowing in manufacturing production growth in the current quarter. Real adjusted durable goods orders increased 0.7 percent in September, only partially offsetting a 2.5 percent drop in August. The November reading on new orders from the

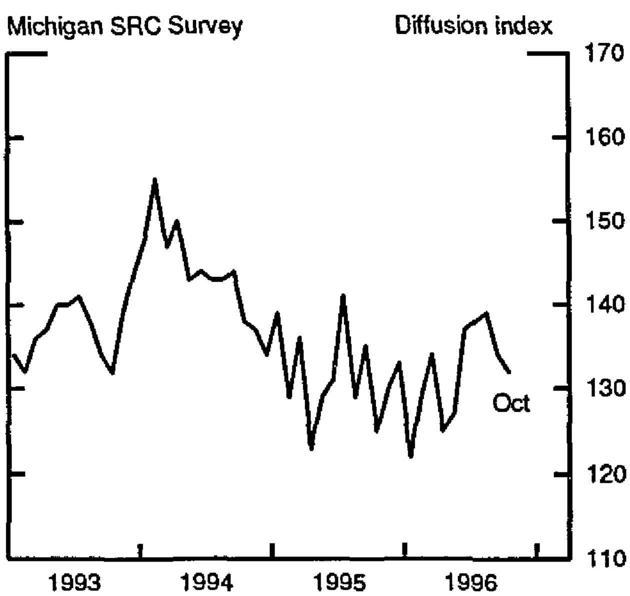
SALES OF AUTOMOBILES AND LIGHT TRUCKS
(Millions of units at an annual rate; FRB seasonals)

			1996			1996		
	1994	1995	Q1	Q2	Q3	Aug.	Sept.	Oct.
Total	15.0	14.7	15.2	15.1	14.9	15.7	14.9	14.8
Adjusted[1]	15.0	14.6	15.3	15.1	15.0	15.6	14.9	14.9
Autos	9.0	8.6	8.6	8.8	8.5	8.8	8.6	7.9
Light trucks	6.1	6.1	6.5	6.3	6.4	6.9	6.3	7.0
North American[2]	12.9	12.8	13.5	13.4	13.3	14.0	13.2	13.2
Autos	7.3	7.1	7.3	7.5	7.3	7.5	7.3	6.6
Big Three	5.7	5.4	5.4	5.6	5.2	5.3	5.2	4.8
Transplants	1.5	1.7	1.9	1.9	2.1	2.3	2.1	1.8
Light trucks	5.7	5.7	6.1	5.9	6.0	6.4	5.9	6.5
Foreign produced	2.1	1.9	1.7	1.7	1.7	1.7	1.7	1.7
Autos	1.7	1.5	1.3	1.3	1.2	1.3	1.3	1.2
Light trucks	.4	.4	.4	.5	.4	.5	.4	.4

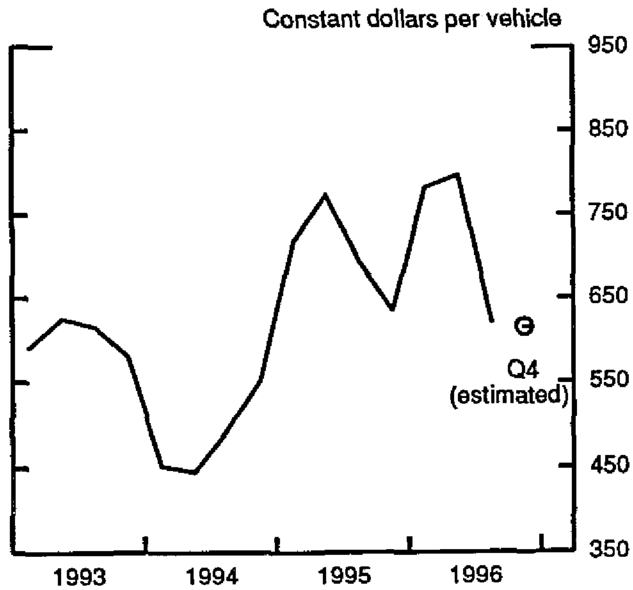
Note. Components may not add to totals because of rounding. Data on sales of trucks and imported autos for the most recent month are preliminary and subject to revision.

1. Excludes the estimated effect of automakers' changes in reporting periods.
2. Excludes some vehicles produced in Canada that are classified as imports by the industry.

Buying Conditions for New Vehicles



Marketing Incentives for Light Vehicles
(FRB seasonals)



Note. Data from J.D. Powers, deflated by CPI for new motor vehicles.

National Purchasing Managers also is consistent with a fourth-quarter deceleration in manufacturing activity. Anecdotal reports in the Beige Book, as well as business contacts maintained by Board staff, suggest that industrial output is growing moderately.

The factory operating rate fell further in October from 82.2 percent in September; it currently stands about 3 percentage points below its high for the current expansion, achieved in December 1994. The average factory operating rate in primary-processing industries is still well above its historical average, but in advanced-processing industries utilization rates are close to their long-run averages.

In mid-December we should be releasing the annual revisions of industrial production, capacity, and capacity utilization. The revisions will incorporate updated source data for recent years and will feature a change in the method of constructing aggregate indexes. From 1977 onward, the value-added proportions used to weight individual series will be updated annually rather than quinquennially and will be aggregated using a Fisher formula rather than a linked-Laspeyres formula. The new aggregation methods will lower both IP growth and capacity growth, reflecting the smaller weight that will be applied, on average, to the fast-growing computer industry; on net, the effect of the reaggregation on overall capacity utilization should be small.

Motor Vehicles

Sales of new light vehicles in October were about 14.8 million units at an annual rate, down slightly from the September level.[1] Sales at General Motors actually increased a bit from their level in September, as a surge in purchases of light trucks more than offset a sharp drop in car sales in the wake of the disruptions to supplies caused by the Canadian Auto Workers (CAW) strike. This strike lasted almost three weeks, with CAW employees returning to work on October 24.[2] The effect of the strike on GM dealers' stocks was twofold. First, most of GM's vehicles produced in Canada are sold in the United States. Second, the strike forced GM to shut down several domestic assembly lines because of shortages of parts produced in Canada. Based on sales data for other producers, it

1. A shift in reporting periods by Toyota held down overall reported sales in October by about 0.1 million units.

2. In the United States, the UAW has reached agreements with General Motors, Ford, and Chrysler. Meanwhile, in Canada the CAW has signed an agreement with Chrysler and today reached a tentative agreement with Ford.

does not appear that the other firms picked up many sales last month as a result of GM's supply problems. Thus, with stocks having been run down, production and sales at GM may be shifted from the current quarter to early next year. We expect GM to shift a greater portion of its sales to retail customers (and to reduce the share allocated to its fleet customers) until its supply problems ease.

GM's labor woes did not end with the settlement with the CAW. On October 29, the UAW struck a light truck assembly plant and a key parts plant. Although the strikes were settled within a week, production of GM's full-size pickups and sport utility vehicles was disrupted, with losses estimated to be about 30,000 units (not at an annual rate).

Production at GM's North American plants is expected to be back to normal by next week. However, inventories are likely to remain lean for a few months. Because of capacity constraints, only about 0.2 million of the 0.6 million units (annual rate) of Canadian production lost during October are expected to be made up this quarter; most of the rest should be made up during the first quarter of next year. On the domestic front, losses related to the CAW stoppage in October are estimated to be about 0.75 million units at an annual rate, and the output losses associated with the UAW strike are estimated at about 0.4 million units.[3] At this point, we expect less than one-fourth of these domestic output losses to be made up by the end of the year, delaying the bulk of the catch-up until the first quarter of next year.[4]

The underlying demand for light vehicles still seems to be relatively strong. Sales have eased only a bit from the high level of the first half, and other indicators have remained quite healthy. For example, the latest readings on consumers' attitudes toward car buying conditions edged down in October but still were in the middle of the range that has prevailed so far this year. In addition, increases in the effective prices of new cars have been relatively modest. Owing to the strength of the dollar this year, price

3. Start-up problems associated with new models (unrelated to the CAW strike) further reduced GM's production by another 0.25 million units or so last month.

4. Capacity contraints, particularly for GM's full-size pickups and sport utility vehicles, will make it difficult for GM to completely recapture this production by the end of the first quarter. In addition, a small amount of the lost production in both the U.S. and Canada is unlikely to be made up at all, as inventories for a few of the models affected by the strike were excessive prior to the work stoppages.

increases for Japanese vehicles have been small, putting pressure on the Big Three automakers to hold down buyers' costs for domestic vehicles as well. Also, the average level of incentives in the current quarter appears likely to be little changed from the third quarter. Although below the levels of the first half of the year, the current incentives are still relatively generous by historical standards.

Personal Income and Consumption

After expanding briskly over the first half of the year, real personal consumption expenditures increased at only a 0.4 percent annual rate in the third quarter, and the saving rate moved up to its highest level in more than three years. The sharp slowing in consumption growth was evident across a wide range of goods and services and occurred despite continued high consumer confidence and robust real income and wealth gains. Lenders did tighten their lending standards a bit in the third quarter, but even so, credit still appears to have been amply available to most consumers.

In the third quarter, real outlays for durable goods excluding motor vehicles rose at a 2.7 percent annual rate, reflecting higher spending on electronic equipment, including computers, and on household furnishings such as floor coverings, clocks, and lamps. In contrast, real outlays for furniture and household appliances declined. Real expenditures on nondurable goods fell marginally, reflecting sharp declines in outlays for food and gasoline, and modest gains for apparel and other items.

Outlays for real energy services fell nearly 10 percent at an annual rate in the third quarter, reflecting a cooler than average summer. Available weather data so far in the fourth quarter show temperatures closer to seasonal norms. If this pattern holds, the rise in energy expenditures should provide a small boost to PCE growth in the current quarter.

Non-energy services increased at a 1.7 percent annual rate in the third quarter. Real outlays for medical and transportation services moved higher, and there was a healthy gain in recreational services, owing in part to the Olympics. In contrast, the midsummer lull in the stock market contributed to a sizable decline in brokerage services (a component of personal business services); data for September, however, indicate that some reversal of this weakness is in train.

PERSONAL INCOME
(Average monthly percent change)

	1994	1995	1996 Q1	1996 Q2	1996 Q3	1996 Aug.	1996 Sept.
Total personal income	.3	.5	.4	.6	.4	.5	.6
Wages and salaries	.1	.4	.4	.8	.5	.8	.8
Private	.1	.5	.5	.9	.5	.9	.9
Other labor income	.4	.5	-.1	.4	.3	.3	.3
Less: Personal tax and nontax payments	.3	.6	1.0	1.2	.7	1.1	.8
Equals: Disposable personal income	.3	.4	.3	.6	.4	.5	.6
Memo:							
Real disposable income[1]	.1	.3	.1	.4	.2	.4	.4
Saving Rate (percent)	3.8	4.7	4.8	4.3	5.4	5.2	5.7

1. Derived from billions of chained (1992) dollars.

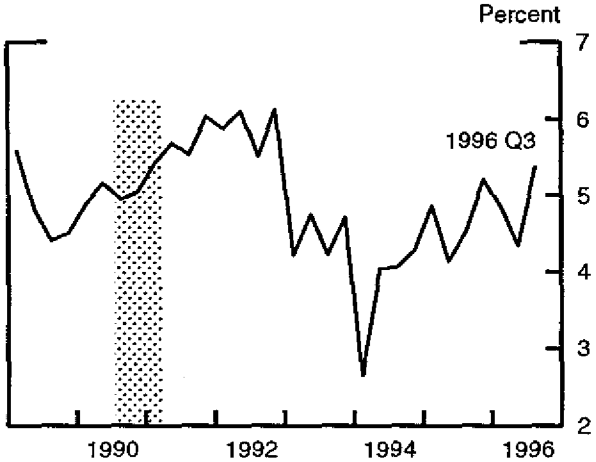
REAL PERSONAL CONSUMPTION EXPENDITURES[1]
(Percent change from the preceding period)

	1994	1995	1996 Q1	1996 Q2	1996 Q3	1996 Aug.	1996 Sept.
			- - - Annual rate		- - -	Monthly rate	
PCE	3.1	1.9	3.5	3.4	.4	.5	-.1
Durables	7.0	1.3	8.2	11.4	-.8	3.1	-1.4
Motor vehicles	1.8	-3.8	6.7	3.0	-6.5	5.9	-2.9
Computers	31.8	52.3	50.8	113.6	29.5	2.4	2.4
Other durable goods	9.1	.4	4.2	5.6	-1.7	1.4	-1.2
Nondurables	3.5	1.1	3.7	1.3	-.3	.1	.1
Gas and oil	2.1	1.9	-3.8	6.2	-3.8	-1.9	2.6
Clothing and shoes	7.1	.7	8.4	10.1	1.6	1.5	-.1
Other nondurables	2.9	1.1	3.4	-1.2	-.5	.0	-.1
Services	2.0	2.4	2.4	2.7	1.1	.1	.1
Energy	-5.3	5.4	7.3	8.8	-9.8	2.8	-1.7
Non-energy	2.3	2.3	2.2	2.4	1.7	.0	.1
Housing	2.4	1.8	1.6	1.5	1.4	.1	.1
Personal business	-1.3	2.5	5.9	-1.1	-4.4	-1.0	1.2
Personal care	1.5	2.4	2.6	2.6	2.6	.2	.2
Recreation	4.1	2.8	.8	5.8	4.1	-1.4	.5
Transportation	5.3	3.2	5.6	1.8	4.3	.3	.5
Medical	1.9	2.5	-.1	2.9	2.4	.3	.2
Other	4.4	2.1	2.9	5.6	4.3	.6	-1.2

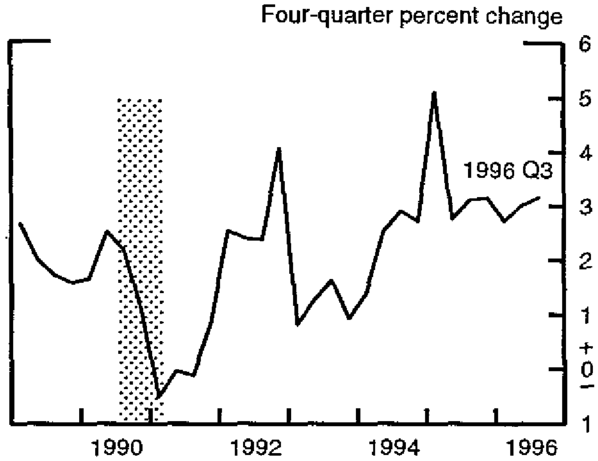
1. Derived from billions of chained (1992) dollars.

Savings and Consumer Attitudes

NIPA Personal Saving Rate

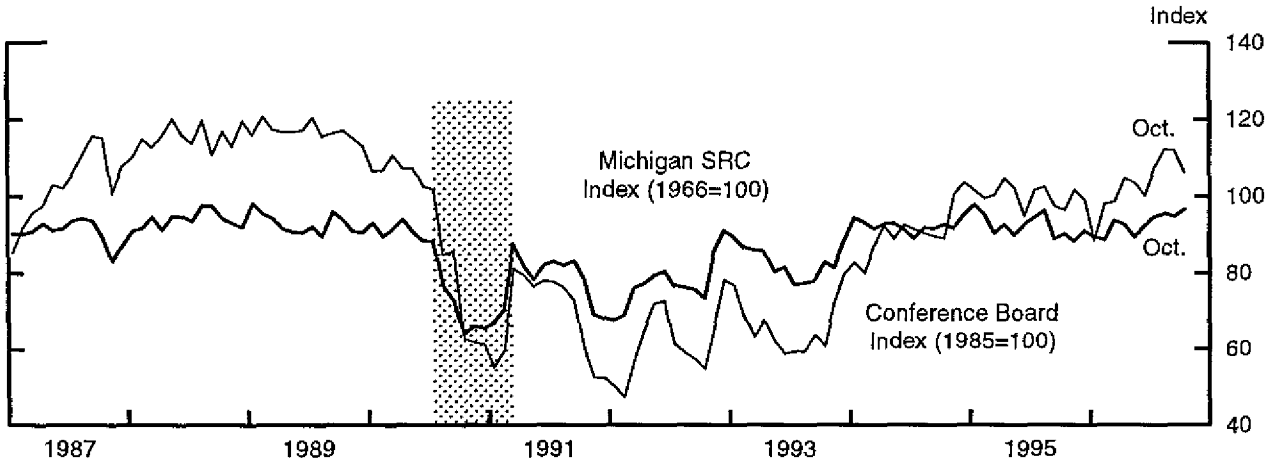


Real Disposable Personal Income

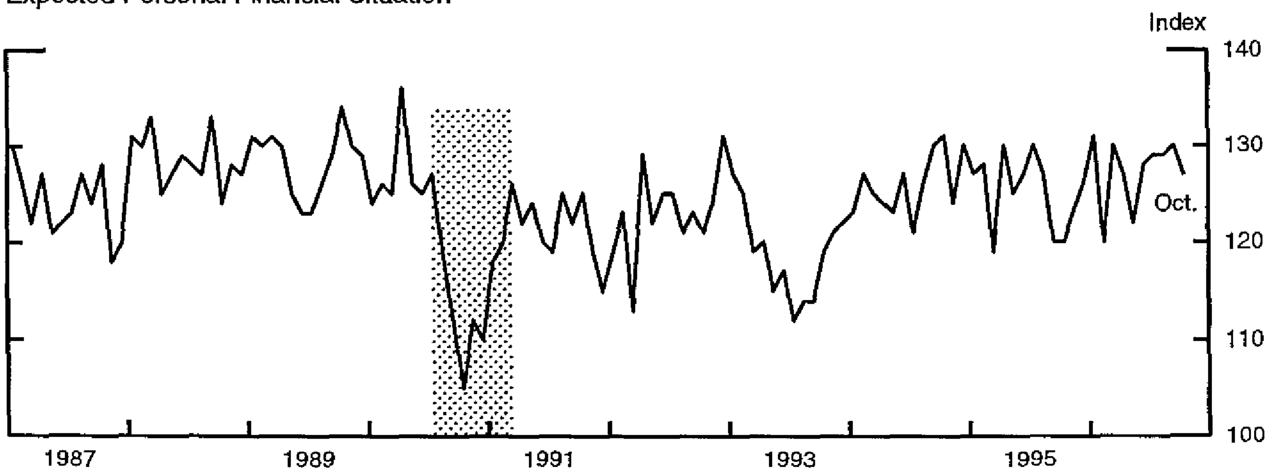


Michigan Survey

Consumer Sentiment



Expected Personal Financial Situation*



* Percent reporting expected situation in 12 months as better less percent who report worse, plus 100.

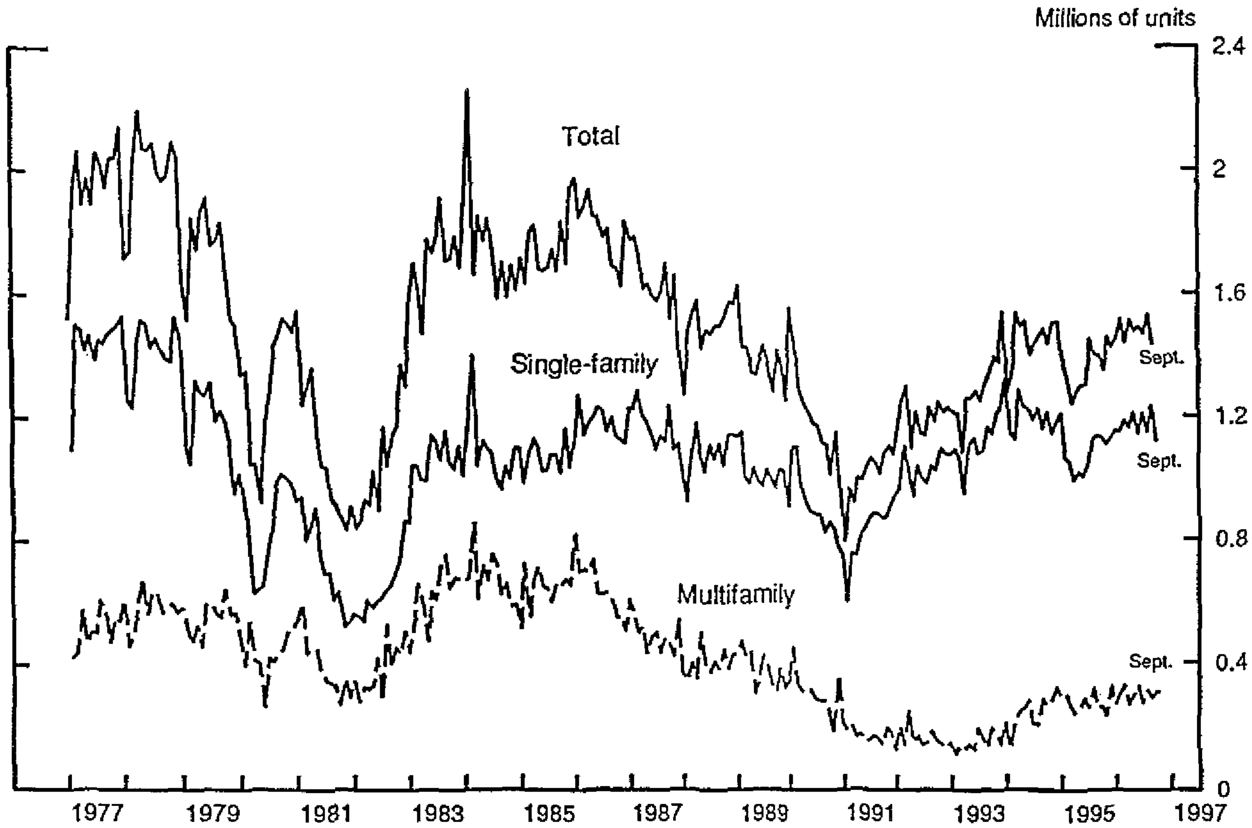
Private Housing Activity
(Millions of units; seasonally adjusted annual rate)

	1995	Q1	Q2r	Q3p	Julyr	Aug.r	Sept.p
All units							
Starts	1.35	1.47	1.49	1.48	1.47	1.53	1.44
Permits	1.33	1.41	1.44	1.42	1.46	1.42	1.38
Single-family units							
Starts	1.08	1.16	1.19	1.17	1.15	1.23	1.12
Permits	1.00	1.08	1.10	1.06	1.07	1.08	1.04
New home sales	0.67	0.75	0.74	0.81	0.79	0.82	0.82
Existing home sales	3.80	3.95	4.21	4.10	4.15	4.14	4.02
Multifamily units							
Starts	0.28	0.31	0.31	0.31	0.32	0.30	0.32
Permits	0.33	0.33	0.34	0.36	0.38	0.35	0.34
Mobile homes							
Shipments	0.34	0.35	0.37	n.a.	0.37	0.37	n.a.

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

Private Housing Starts

(Seasonally adjusted annual rate)



Outside of motor vehicles, we have few firm data on fourth-quarter consumer spending. However, the fundamentals underlying consumer demand appear supportive of a rebound in coming months. Income growth remained on a solid upward trend in the third quarter, with real disposable personal income up almost 5 percent at an annual rate. Part of the large advance in third-quarter disposable income was due to the timing of personal tax payments,[5] but wage and salary income also advanced at a healthy clip. The recent employment report suggests that estimated labor income in October will be weak, but we anticipate a recovery in November with a bounceback in the average workweek and a resumption of growth in hourly earnings.

In addition, consumer sentiment has remained upbeat. Although the Conference Board index dropped back a bit in October, the readings on this index from July through October were the highest posted over the current expansion. Similarly, the Michigan SRC index moved up in October to the top of the relatively favorable range that has prevailed since early 1994--buoyed largely by decidedly more positive views of current conditions (expected conditions changed little). Although a hefty 60 percent of SRC respondents in October expected interest rates to rise, this did not appear to have much of an adverse influence on their views of expected unemployment, business conditions, or their personal financial situation. Moreover, the SRC survey suggests that the third-quarter rise in the saving rate was not fueled by heightened precautionary motives: The index of expected unemployment change fell last quarter to its lowest level in almost two years, and respondents' views of their expected personal financial situation remained quite favorable--rising to the highest level of the current expansion.

<u>Housing</u>

As has been the case for some months now, indicators of housing sector activity have moved in divergent directions of late, making it difficult to gauge the effects of this year's backup in mortgage

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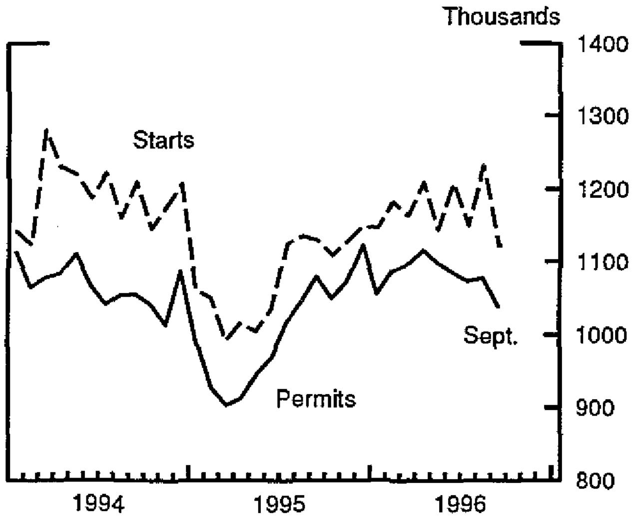
5. Payment of the third and final installment of tax liabilities resulting from OBRA-93 temporarily depressed second-quarter disposable income. In the third quarter, tax payments fell back to more normal levels--providing a commensurate boost to disposable income.

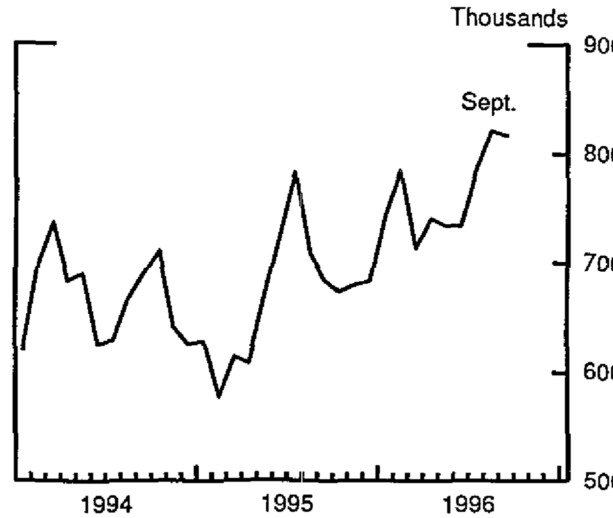
Indicators of Single-Family Housing Demand

(Seasonally adjusted)

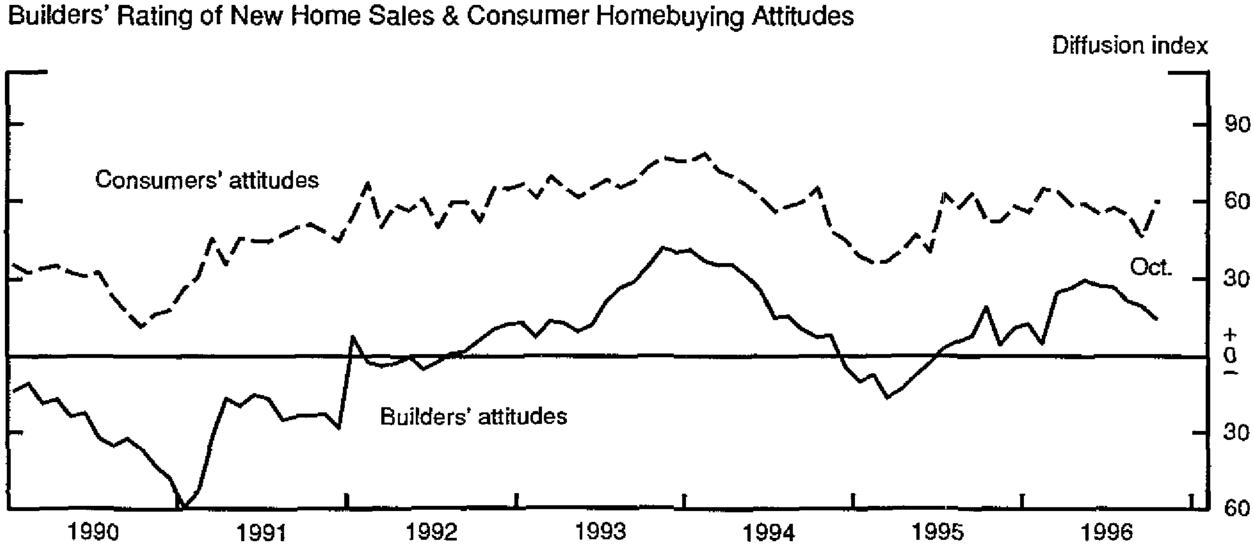
Permits and Starts



New Home Sales

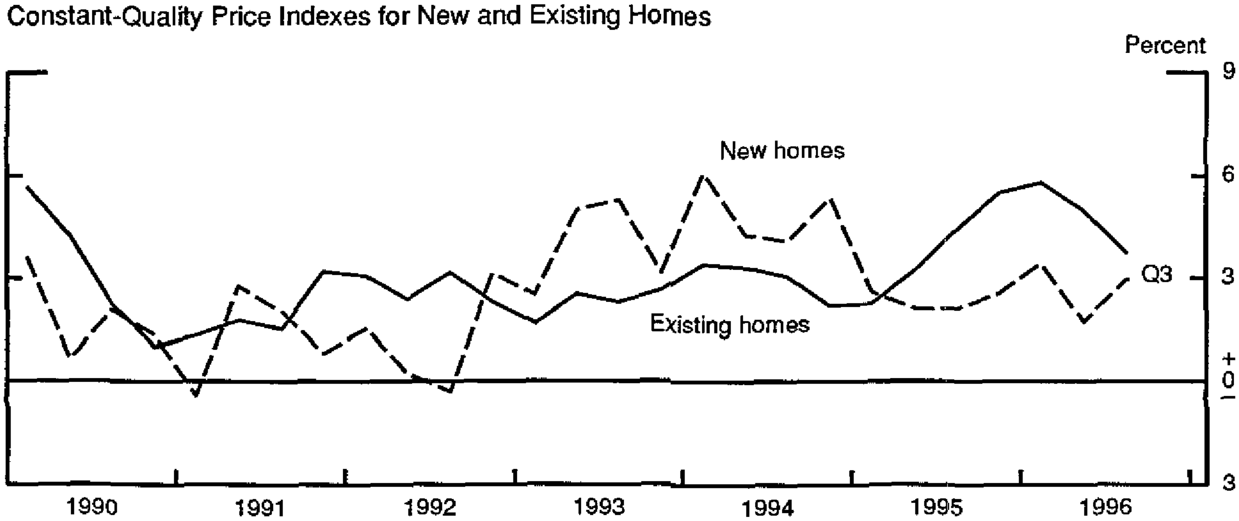


Builders' Rating of New Home Sales & Consumer Homebuying Attitudes



Note. The first index is calculated from the National Association of Homebuilders and the second from the Survey Research Center.

Constant-Quality Price Indexes for New and Existing Homes



Note. Percent change from a year earlier. The index for existing homes is the repeat sales index published by Freddie Mac and Fannnie Mae; the index for new homes is published by the Census Bureau.

rates.[6] On the production side, starts of single-family houses, which shot up in August, fell back in September to the lowest level seen so far this year. And permits for single-family structures, which are less volatile than starts, have shown a discernible downdrift since last spring.

In contrast, new home sales edged down in September but remained well above the average pace during the first half of this year--and at a level typically consistent with higher starts than observed in the past couple of months. Furthermore, the Michigan Survey's index of consumer homebuying attitudes, which had eroded earlier this year, snapped back in October to a level similar to that seen last spring. A survey of home builders' assessments of current sales, which historically has been correlated with the Commerce Department's new home sales series, has trended down since last spring, but applications for mortgages to purchase homes (both new and existing) remained flat, on net, through mid-October, in the neighborhood of the relatively strong level that has prevailed since early this year. All told, the available information suggests that the single-family sector probably has softened in recent months, but only a bit.

The index of prices of similar-quality existing homes was up 3-3/4 percent in the third quarter from its year-earlier reading, according to Freddie Mac and Fannie Mae. This price index accelerated considerably from the middle of 1995 through the first quarter of this year but has moderated since then. The Census Bureau's constant-quality price index for new homes rose about 3 percent during the past year, about the same as the average pace seen during the previous two years.

Multifamily housing starts rose to a 316,000 unit annual rate in September, reversing most of the August decline. From a longer perspective, the level of multifamily starts in the third quarter was up 12 percent from the 1995 average; building permits for these units also have moved higher this year. One factor that may hold back further construction in this sector is the rising inventory of unoccupied units. Vacancy rates for apartments rose to 9-1/2 percent in the third quarter, 1/2 percentage point more than the average reading during the previous two years. Thus far, however, rents do not appear to have suffered as a result: The

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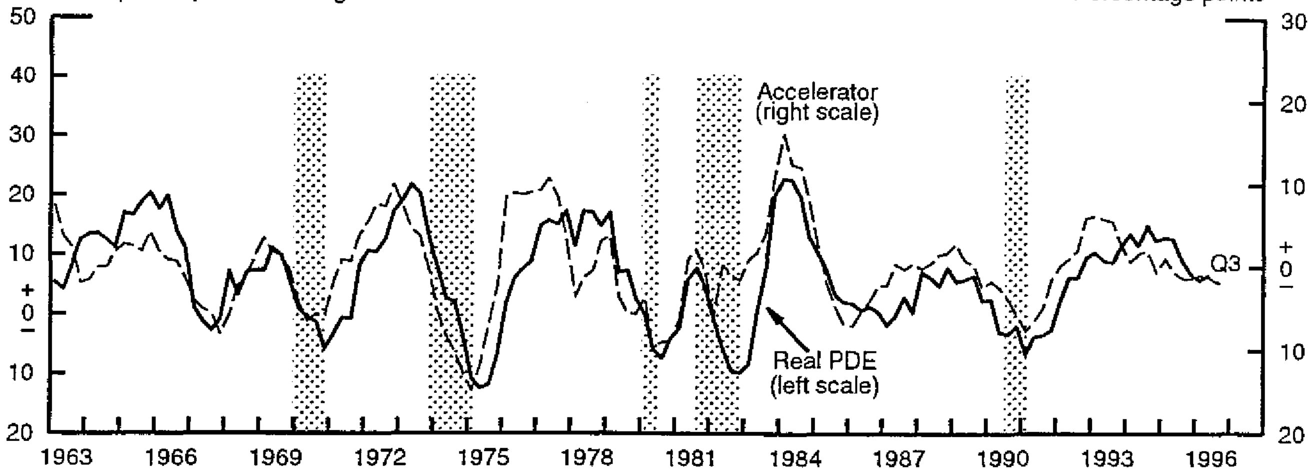
6. Although mortgage rates have moved down about 50 basis points since early September, they still are about 75 basis points above their levels of early this year.

Fundamental Determinants of Equipment Spending

Acceleration of Business Output

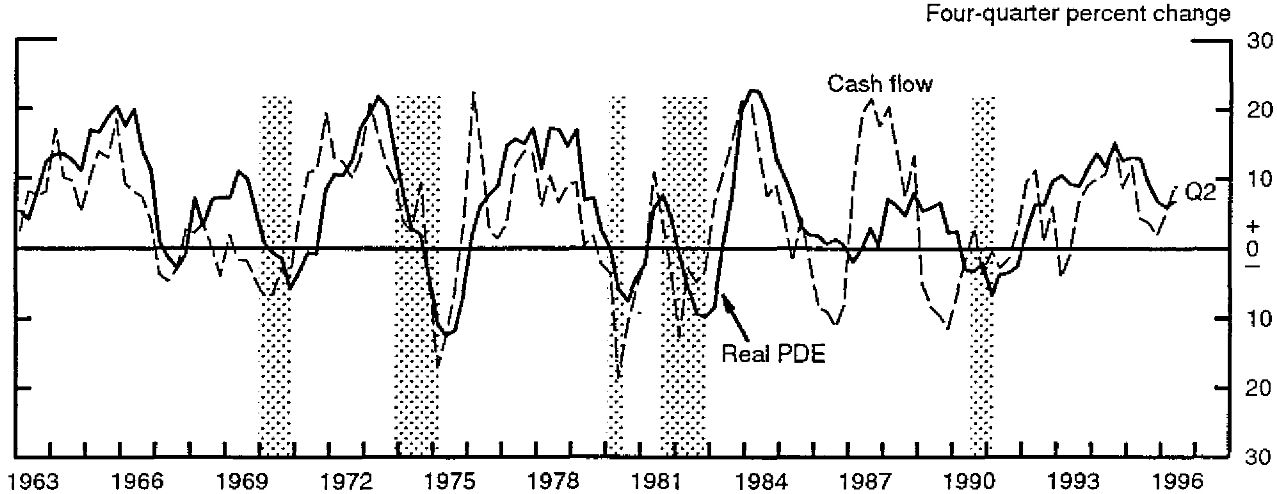
Four-quarter percent change | Percentage points



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

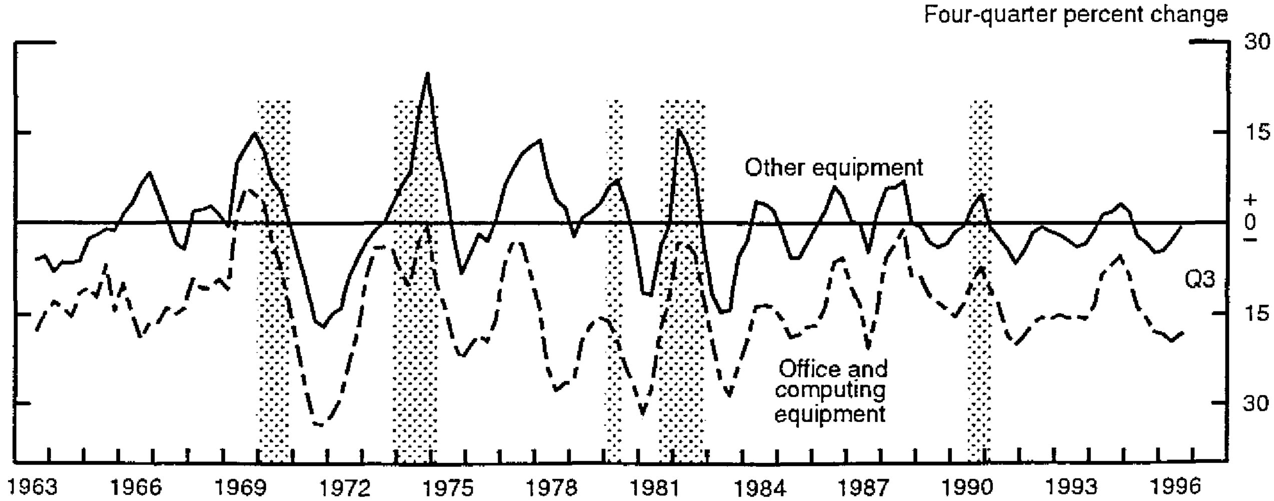
Real Domestic Corporate Cash Flow

Four-quarter percent change



User Cost of Capital

Four-quarter percent change



consumer price index for rental units rose 2-3/4 percent during the twelve months ended in September, about 1/2 percentage point more than its pace over the previous year.

Business Fixed Investment

Real business fixed investment accelerated sharply, to about a 16-1/4 percent annual rate, in the third quarter, but the fundamental determinants of investment point to less rapid gains in the near term. Increases in cash flow should continue to provide some impetus to spending, but the effect of the acceleration of business output should now be about neutral, and the rate of decline in the user cost of capital has slowed. Nonetheless, user costs remain quite favorable for the fast-growing office and computing category.

The third-quarter advance in PDE of close to 20 percent (annual rate) was led by a sharp increase in real expenditures on office and computing equipment. Anecdotal reports tend to confirm the strength implied by the recent spending data, with a number of computer industry leaders reporting favorable third-quarter results. For example, Compaq Computer's earnings per share grew 40 percent relative to a year ago, nearly twice analysts' expectations. Intel's 45 percent increase relative to the same period last year outpaced market forecasts by an even wider margin. Microsoft registered a solid gain, and even Apple Computer earned a small profit. Our contacts in the computer industry report that sales to businesses, especially of high-end servers, represent an important part of recent performance.

In a further mark of very strong demand for computer equipment, Intel Corporation announced in late October that it has been unable to meet manufacturers' needs for 200 MHz Pentium Pro processors used in high-end servers. Indeed, investment may be constrained somewhat in the fourth quarter if what systems vendors describe as "a serious shortage" of these processors persists.

Growth of real investment in communications equipment jumped more than 30 percent at an annual rate in the third quarter. In addition, orders for communications equipment were up a hefty 7 percent, a rise that should sustain fairly rapid growth in spending in this sector over the near term. On September 27, the U.S. Court of Appeals granted a temporary stay to the implementation of rules opening the local phone monopolies to competition. This development and the threat of lengthy legal delays introduces

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

	1996			1996		
	Q1	Q2	Q3	July	Aug.	Sept.
Producers' durable equipment						
Shipments of nondefense capital goods	-.5	2.9	1.8	-1.6	2.4	1.8
Excluding aircraft and parts	.8	1.5	1.5	-2.3	1.1	2.3
Office and computing	3.7	-.8	4.5	-.8	4.6	1.1
Communications equipment	-.3	4.7	4.8	-1.5	-1.0	4.5
All other categories	.0	1.7	-.5	-3.1	.3	2.3
Shipments of complete aircraft[1]	1.4	12.2	n.a.	2.7	50.5	n.a.
Sales of heavy trucks	-2.2	1.2	n.a.	.1	-.2	n.a.
Orders of nondefense capital goods	3.1	-6.5	4.9	7.0	-10.4	15.6
Excluding aircraft and parts	3.1	-1.7	2.7	3.7	-4.9	2.5
Office and computing	2.1	1.6	4.9	3.0	-.3	-2.6
Communications equipment	8.7	-8.5	7.1	15.1	-14.0	1.6
All other categories	2.2	-1.2	.9	1.2	-4.3	4.8
Nonresidential structures						
Construction put-in-place	1.0	.0	2.6	-1.3	3.6	1.1
Office	-6.6	8.3	8.1	-3.3	.5	1.4
Other commercial	3.0	-1.0	1.8	-.9	8.7	-2.5
Institutional	-2.9	1.2	8.1	-.8	7.2	2.2
Industrial	-1.6	-8.0	-1.8	-.5	-5.4	7.6
Public utilities	4.5	3.1	-1.0	-.7	4.4	-.4
Lodging and miscellaneous	10.6	.0	4.9	-2.4	4.5	1.7
Rotary drilling rigs in use	6.6	12.4	-4.7	-2.3	-.1	-4.9
Memo:						
Business fixed investment[2]	11.6	3.8	14.7	n.a.	n.a.	n.a.
Producers' durable equipment[2]	13.1	6.7	18.9	n.a.	n.a.	n.a.
Nonresidential structures[2]	7.7	-3.8	3.3	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 1992 chain-weighted data; percent change, annual rate.
n.a. Not available.

additional uncertainty into the outlook for investment in the telecommunications industry. However, rapid technological improvements and rising demand for services are likely to sustain growth of expenditures even in the absence of deregulation.

Spending on motor vehicles increased at a 21 percent annual rate in the third quarter. Auto fleet sales were strong but are expected to weaken in the fourth quarter as GM diverts sales to retail customers in the wake of its recent production disruptions. Sales of heavy trucks continued to drift lower, reflecting the ongoing weakness in orders. Domestic expenditures on aircraft rebounded to a level above that in the first quarter. Demand for aircraft continues to be robust; the value of orders received by Boeing rose in August, with all the increase coming from domestic customers.

Expenditures on other capital goods were up at a mere 1-1/4 percent pace in the quarter. Orders for these types of equipment also were up only slightly in the quarter after having fallen in the second quarter. The leveling off of new orders after two years of rapid increases suggests that investment growth in this category will remain sluggish in the current quarter.

Real expenditures on nonresidential structures firmed in the third quarter, more than reversing the second-quarter decline. Incorporating the likely revisions to the third-quarter data, spending has risen at a 3-1/4 percent annual rate so far this year, down from the 5 percent increase in 1995. Data on the value of contracts for private nonresidential buildings now look more in line with this pattern of slower growth in spending on structures. Large upward revisions to the contracts data for the first half of this year have lifted the path of this series considerably, eliminating much of the inconsistency that had existed between the spending data and the earlier reports that contracts were falling; a six-month moving average now shows a plateau since early 1995.

Business Inventories

Following a modest rate of accumulation in the second quarter, the pace of business inventory investment picked up considerably over the summer. Although the lull in consumer spending undoubtedly was a factor, the accelerated inventory buildup could well have reflected in part desires of some businesses to replenish stocks that had been drawn down sharply in late spring and early

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

	1996			1996		
	Q1	Q2	Q3	July	Aug.	Sept.
Book value basis						
Total	16.7	13.2	n.a.	61.0	56.5	n.a.
Excluding wholesale and retail motor vehicles	25.0	6.0	n.a.	39.1	39.3	n.a.
Manufacturing	12.3	-6.2	13.1	6.9	14.9	17.4
Excluding aircraft	6.3	-10.7	10.4	6.3	12.5	12.5
Wholesale	7.3	11.3	n.a.	-1.9	14.6	n.a.
Excluding motor vehicles	7.3	7.6	n.a.	-4.2	13.0	n.a.
Retail	-2.9	8.2	n.a.	56.0	27.1	n.a.
Auto dealers	-8.4	3.5	n.a.	19.7	15.6	n.a.
Excluding auto dealers	5.5	4.6	n.a.	36.3	11.5	n.a.
Chained (1992) dollars basis						
Total	-5.4	7.9	n.a.	56.4	26.0	n.a.
Excluding motor vehicles	17.5	1.9	n.a.	46.0	27.2	n.a.
Manufacturing	12.0	-3.9	n.a.	13.7	5.6	n.a.
Wholesale	3.8	6.5	n.a.	1.5	15.9	n.a.
Excluding motor vehicles	4.0	3.3	n.a.	-.4	14.4	n.a.
Retail	-21.7	5.2	n.a.	41.5	4.5	n.a.
Auto dealers	-23.6	2.0	n.a.	10.5	-2.7	n.a.
Excluding auto dealers	3.0	3.2	n.a.	31.0	7.3	n.a.

INVENTORIES RELATIVE TO SALES
(Months' supply; based on seasonally adjusted data)

	1996			1996		
	Q1	Q2	Q3	July	Aug.	Sept.
Book value basis						
Total	1.43	1.40	n.a.	1.39	1.40	n.a.
Excluding wholesale and retail motor vehicles	1.40	1.37	n.a.	1.36	1.37	n.a.
Manufacturing	1.45	1.40	1.39	1.39	1.39	1.39
Excluding aircraft	1.34	1.29	1.28	1.28	1.28	1.28
Wholesale	1.32	1.31	n.a.	1.28	1.30	n.a.
Excluding motor vehicles	1.30	1.28	n.a.	1.25	1.26	n.a.
Retail	1.49	1.49	n.a.	1.51	1.52	n.a.
Auto dealers	1.66	1.70	n.a.	1.74	1.76	n.a.
Excluding auto dealers	1.44	1.42	n.a.	1.43	1.45	n.a.
Chained (1992) dollars basis						
Total	1.38	1.36	n.a.	1.35	1.35	n.a.
Excluding motor vehicles	1.36	1.33	n.a.	1.32	1.33	n.a.
Manufacturing	1.39	1.35	n.a.	1.34	1.35	n.a.
Wholesale	1.35	1.34	n.a.	1.31	1.33	n.a.
Excluding motor vehicles	1.33	1.31	n.a.	1.28	1.30	n.a.
Retail	1.37	1.37	n.a.	1.38	1.39	n.a.
Auto dealers	1.54	1.57	n.a.	1.56	1.54	n.a.
Excluding auto dealers	1.34	1.33	n.a.	1.34	1.35	n.a.

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

summer.[7] Despite the substantial inventory investment in these two months, stocks held by most types of firms were fairly well aligned with sales at the end of August. In addition, preliminary September data for manufacturing suggest that the situation was little changed in that sector in the latter part of the third quarter. The general picture regarding inventory-sales ratios depicted by the Census data is consistent with reports from other sources, such as the recent Purchasing Managers Surveys and anecdotal reports from the latest Beige Book.

MANUFACTURERS' RECENT INVENTORY INVESTMENT
By stage of processing and market grouping
(Book value, billions of dollars at annual rate)

	1996					
	Q1	Q2	Q3	July	Aug.	Sept.
Total manufacturing	12.3	-6.2	13.1	6.9	14.9	17.4
By stage of processing						
Materials and supplies	2.0	-10.4	2.5	7.5	-5.2	5.2
Work-in-process	7.4	5.9	3.4	.8	9.2	.3
Finished goods	2.9	-1.7	7.1	-1.3	10.9	11.8
By market grouping						
Producers' dur. equip.	9.9	.6	12.0	18.0	14.4	3.7
Information equip.	2.3	-1.3	1.0	4.1	.3	-1.5
Industrial equip.	-.4	-2.1	2.4	7.6	1.8	-2.1
Transportation equip.	7.1	3.1	5.7	6.7	5.7	4.8
Other equipment	.2	.9	2.9	-.4	6.6	2.6
Household durables	.4	-.3	1.7	-2.4	4.6	2.8
Home goods & apparel	-1.0	-1.7	1.4	-1.9	3.1	2.9
Other	3.0	-4.8	-2.0	-6.8	-7.3	8.0

Manufacturing inventories expanded further in August and September. As in July, a substantial portion of the August-September buildup was in stocks of capital goods. However, the latest accumulation also comprised consumer goods--household durables, home goods, and apparel--for the first time since February. On the whole, manufacturers' inventories were reasonably balanced at the end of the third quarter, with stock-shipments ratios for most industries and market groupings still hovering near

7. For most types of non-auto retail establishments, inventory-sales ratios reached their most recent lows in May of this year; for manufacturers and wholesale distributors, the recent troughs occurred in July.

SELECTED INVENTORY-SALES RATIOS
(Months' supply, based on Census book-value data, seasonally adjusted)

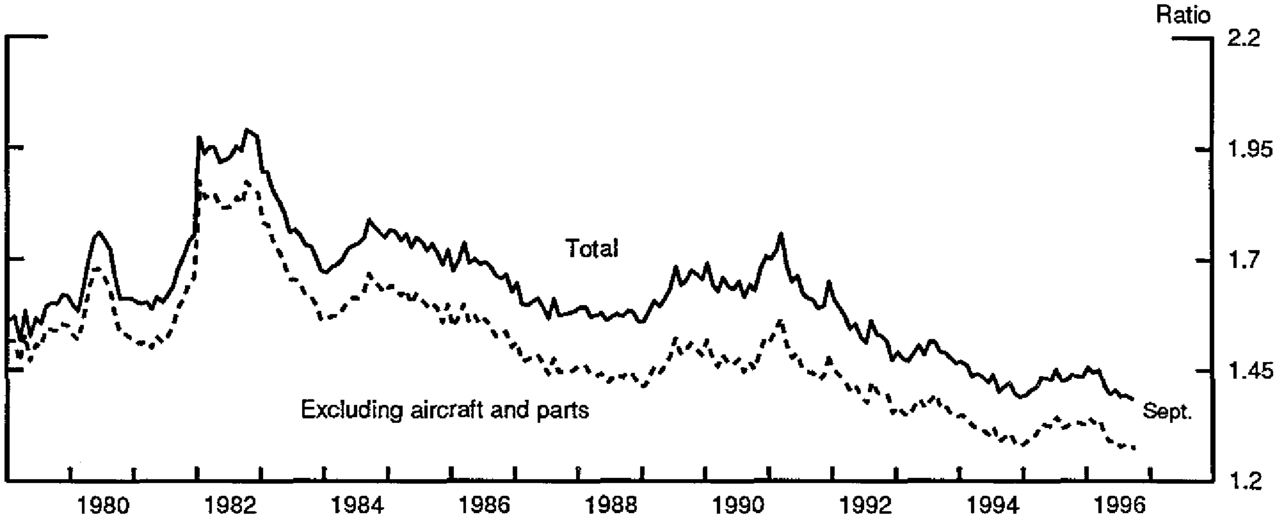
	Cyclical reference points		Most recent 12-month range		August/ September 1996[1]
	1990-91 High	1994-95 Low	High	Low	
Manufacturing and trade	1.58	1.40	1.45	1.39	1.40
Less wholesale and retail motor vehicles	1.57	1.40	1.44	1.39	1.37
Manufacturing	1.75	1.39	1.46	1.39	1.39
Primary metals	2.08	1.45	1.62	1.55	1.61
Nonelectrical machinery	2.48	1.88	1.94	1.84	1.81
Electrical machinery	2.08	1.52	1.60	1.52	1.51
Transportation equipment	2.94	1.59	1.87	1.65	1.65
Motor vehicles	.97	.53	.67	.56	.55
Aircraft	5.85	4.42	5.95	4.89	5.14
Nondefense capital goods	3.09	2.33	2.58	2.38	2.39
Textile	1.71	1.44	1.66	1.49	1.55
Petroleum	.94	.88	.92	.80	.80
Home goods & apparel	1.96	1.70	1.89	1.70	1.72
Merchant wholesalers	1.36	1.28	1.34	1.28	1.30
Less motor vehicles	1.31	1.26	1.31	1.25	1.26
Durable goods	1.83	1.54	1.64	1.58	1.61
Nondurable goods	.96	.98	1.03	.97	.98
Retail trade	1.61	1.46	1.56	1.48	1.52
Less automotive dealers	1.48	1.42	1.48	1.41	1.45
Automotive dealers	2.21	1.60	1.82	1.64	1.76
General merchandise	2.43	2.21	2.34	2.20	2.26
Apparel	2.56	2.47	2.66	2.35	2.44
G.A.F.	2.44	2.24	2.37	2.23	2.27

1. September 1996 ratios for manufacturing; August 1996 ratios for wholesale and retail trade.

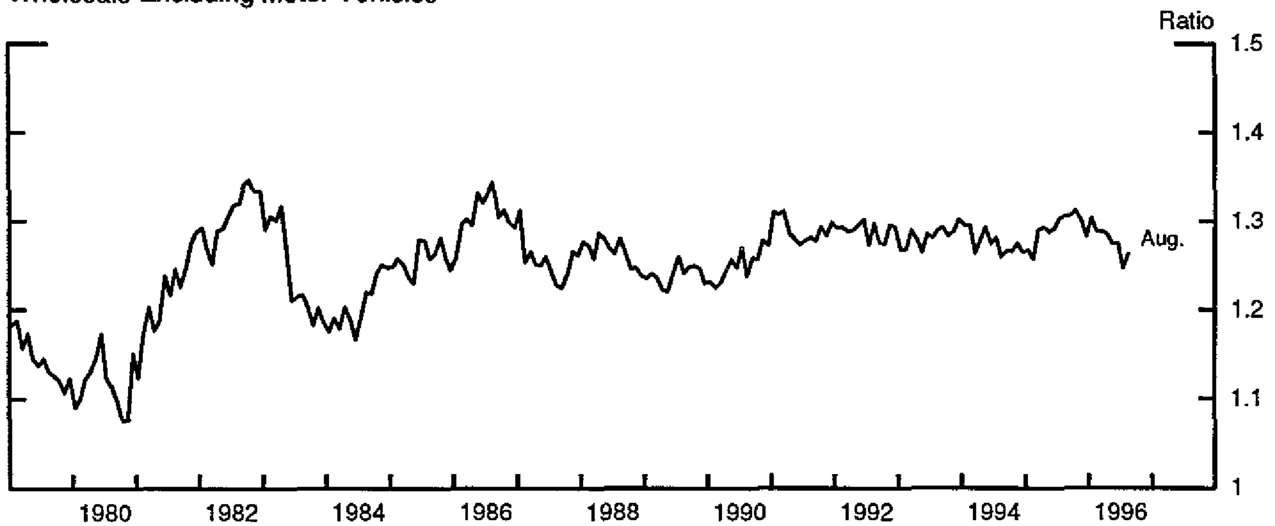
Inventory-Sales Ratios, by Major Sector

(Book value)

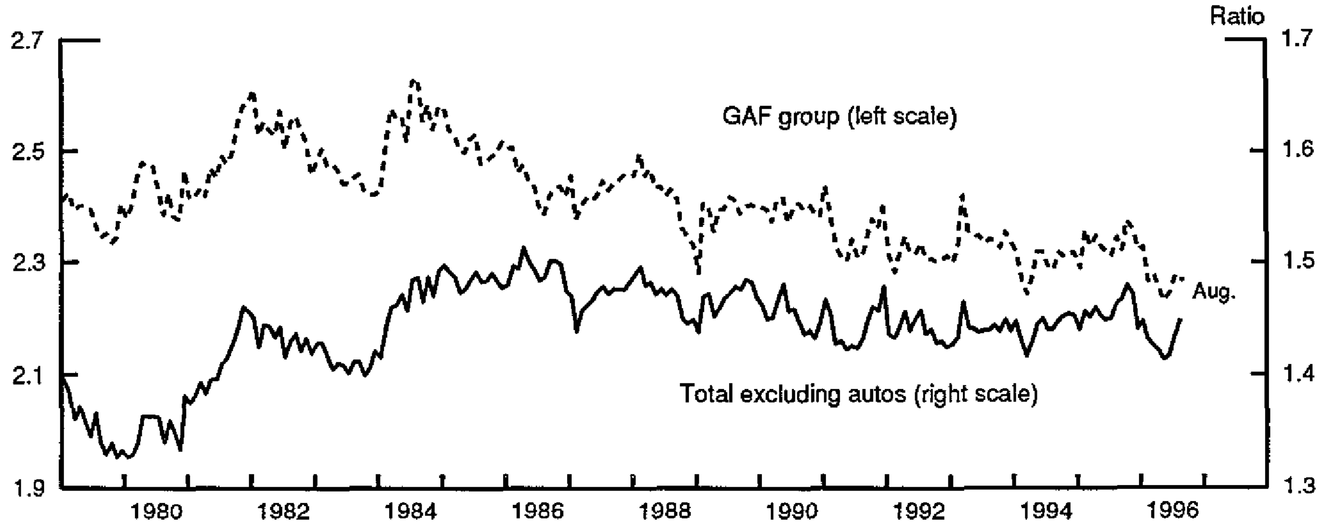
Manufacturing



Wholesale Excluding Motor Vehicles



Retail



FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis; billions of dollars except as noted)

	September		Fiscal year totals			
	1995	1996	1995	1996	Dollar change	Percent change
Outlays	136.1	122.3	1515.4	1560.1	44.7	2.9
Deposit insurance (DI)	.4	-.7	-17.8	-8.3	9.5	-53.3
Spectrum auction (SA)	.0	-.1	-7.6	-.3	7.3	-95.5
Other	135.7	123.1	1540.9	1568.8	27.9	1.8
Receipts	143.3	157.7	1351.5	1452.8	101.3	7.5
Deficit (+)	-7.2	-35.4	163.9	107.3	-56.6	-34.5
	Adjusted for payment timing shifts[1] and excluding DI and SA					
Outlays	128.6	130.9	1540.9	1576.6	35.7	2.3
National defense	23.6	22.4	272.1	268.1	-4.0	-1.5
Net interest	18.9	19.2	232.2	241.1	9.0	3.9
Social security	28.2	29.1	335.8	349.7	13.8	4.1
Medicare	13.3	14.1	159.9	175.8	16.0	10.0
Medicaid	7.4	7.7	89.1	92.0	2.9	3.3
Other health	2.1	2.3	26.0	26.9	.9	3.3
Income security	18.2	15.7	220.4	227.3	6.9	3.1
Other	16.8	20.2	205.4	195.7	-9.7	-4.7
Receipts	143.3	157.7	1351.5	1452.8	101.3	7.5
Individual	60.9	68.7	590.2	656.4	66.3	11.2
Withheld	36.3	39.5	499.9	533.1	33.2	6.6
Nonwithheld	27.2	30.6	175.8	212.2	36.4	20.7
Refunds (-)	2.6	1.5	85.6	88.9	3.3	3.8
Social insurance taxes	39.9	43.4	484.5	509.4	24.9	5.1
Corporate	33.0	35.1	157.1	171.8	14.7	9.4
Other	9.5	10.5	119.8	115.1	-4.7	-3.9
Deficit(+)	-14.7	-26.7	189.4	123.8	-65.6	-34.6

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

1. A shift in payment timing occurs when the first of the month falls on a weekend or holiday. The monthly and fiscal year to date outlays for defense, Medicare, income security, and "other" have been adjusted to account for this shift.

the low end of their recent ranges and considerably below the previous cyclical peak observed during the 1990-91 downturn.

Downstream in retail trade, the bulk of the inventory buildup since midyear has been at general merchandisers, apparel outlets, and at stores in the "miscellaneous" consumer goods category.[8] Although inventory-sales ratios for most types of non-auto retailers have been edging up since May, at the end of August they were still well below their recent highs observed in the autumn of 1995. Wholesale inventories, excluding motor vehicles and the volatile farm products series, also expanded in July and August. However, stocks held by distributors of some consumer goods--in particular, apparel and electrical appliances--fell in July and August, leaving inventory-sales ratios for these wholesale establishments relatively low.

Federal Sector

Total real federal purchases decreased at a 4 percent annual rate in the third quarter, pulled down by a 5 percent decline in real defense purchases. Real federal nondefense purchases were down almost 2 percent (annual rate). The drop in federal purchases for the third quarter reversed the positive growth seen in the previous two quarters and brings purchases back closer to their underlying trend rate of decline.

The unified budget deficit for fiscal 1996 was $107 billion, about $10 billion below the projections made by OMB and CBO last summer and $57 billion below the deficit posted in fiscal 1995.[9] Receipts climbed to a level 7-1/2 percent above that of the previous fiscal year, while outlays increased about 3 percent.[10]

The jump in federal receipts was led by an 11 percent increase in individual income tax payments. Preliminary data on 1995 individual tax returns have thus far been made available only to Treasury and CBO. CBO Director O'Neill recently stated that neither CBO nor OMB knows what has caused the jump in individual receipts but said that the agencies will continue to analyze the data over

8. These "miscellaneous" goods include cameras and other home photographic equipment, jewelry, books, toys, bicycles, and sporting goods.

9. Adjusted for calendar payment shifts and excluding deposit insurance and spectrum auction proceeds, an "adjusted" deficit came in at $124 billion for fiscal 1996, $66 billion below the adjusted deficit for last fiscal year.

10. Adjusted for calendar payment shifts, deposit insurance, and spectrum auction proceeds, "adjusted" outlays increased about 2 percent in fiscal 1996.

the next few months to determine the likely source of this strength.[11] The rise in social insurance taxes, a more subdued 5 percent, is about in line with the growth in wages and salaries. Corporate receipts increased about 9-1/2 percent, consistent with the growth in corporate profits.

In addition to closing out the fiscal year, September unified budget data also contained one of the four "due dates" for estimated individual tax payments, which normally provide useful information about total tax liabilities for the current tax year. Individual nonwithheld tax payments for September were approximately 13 percent higher than a year earlier, and gross corporate tax payments rose 8 percent, suggesting that the strong tax liabilities seen last year are persisting this tax year.

On the outlay side, developments in health-related programs were mixed in fiscal 1996. The 10 percent rise in Medicare outlays, after adjustment for payment timing shifts, is consistent with its recent trend growth. In contrast, Medicaid grew at an historically low 3 percent rate. Declines in welfare program enrollments, state-level reforms that continued the shift in Medicaid payments toward managed-care arrangements, a decline in disproportionate-share payments, and relatively small increases in overall health costs all appear to have contributed to the restrained growth in Medicaid spending. Nominal defense outlays, adjusted for payment timing shifts, continued their decline, falling 1-1/2 percent compared with last year. Adjusted nondefense outlays, excluding the major entitlement programs (social security, income security, and health) and net interest, were down almost 5 percent, primarily reflecting the restraint imposed on programs funded by the past fiscal year's annual appropriations.

In sharp contrast to last year's budget battle, seven regular appropriations bills and a final omnibus appropriations bill, covering programs ordinarily included in the remaining six regular appropriations bills, were all completed before the start of fiscal 1997. Legislated budget authority for discretionary spending programs climbed $9 billion, from $493 billion in fiscal 1996 to

11. "Lower 1996 Deficit Raises Key Questions For Budget Writers About Future Trends," Daily Report for Executives, Bureau of National Affairs, No. 209, October 29, 1996.

$502 billion in fiscal 1997.[12] However, CBO estimates that total discretionary outlays will increase less than $2 billion in fiscal 1997. This is partly a consequence of a $3 billion offset to outlays (but not budget authority) resulting from a provision of the omnibus appropriations bill that imposes a special levy on thrift institutions to recapitalize the Savings Association Insurance Fund.[13]

RECENT BUDGET APPROPRIATIONS
(Billions of dollars, fiscal years)

	1995	1996	1997
Budget authority			
Total	498.1	493.2	502.4
Defense	262.4	264.8	265.8
Nondefense	235.7	228.3	236.6
Outlays			
Total	548.0	535.5	537.2
Defense	270.2	264.2	264.9
Nondefense	277.8	271.4	272.4

Note. Scored by the Congressional Budget Office.

State and Local Governments

Total real state and local government consumption and investment spending now appears to have risen about 1-3/4 percent in the third quarter. Real consumption expenditures were up at a 1.5 percent annual rate after a 5.6 percent jump in the second quarter. The unusual pattern reflects gyrations in real compensation associated with the snowstorms last winter, as many educational employees who lost days during the storm made them up in the second quarter; in the third quarter, the level of compensation returned to trend. Taking into account expected revisions associated with the September construction data, real investment spending probably rose 2-1/2 percent in the third quarter. Employment of state and local government workers, the only data available for the fourth quarter, fell 32,000 in October after a

12. Budget authority in fiscal 1997 is approximately the same as the President's request in the fiscal 1997 budget and is $5 billion more than planned in the fiscal 1997 congressional budget resolution.

13. To raise SAIF's reserve ratio to the statutorily mandated minimum of 1.25 percent from the June level of 0.55 percent, the legislation calls for a one-time special assessment on most SAIF deposits of 68 basis points. After the assessment, SAIF premiums could then be allowed to fall to a level near that for BIF deposits.

drop more than twice as large in September. The two declines came after unusually large gains in previous months and likely reflect, at least in part, seasonal adjustment difficulties. In October, the big drop was concentrated in state education workers, unlike in previous months when the large swings were among local government education workers.

States cut taxes, on net, during their 1995 and 1996 legislative sessions, the first reductions since 1985. In both years, the cuts ($3.3 billion in 1995 and $4 billion in 1996) were about 1 percent of the previous year's general fund collections. The focus both years was on personal income taxes. In 1996, the largest reductions were in New York, Ohio, Connecticut, Massachusetts, and New Jersey, with smaller cuts in eleven other states. In addition, fifteen states reduced corporate income taxes, and twenty states cut sales taxes. The reductions are scheduled to take effect during fiscal year 1997, which began July 1 for most states. Meanwhile, nine states had a variety of tax initiatives on the November 5 ballot, most limiting taxes: Four of five states passed initiatives that would impose a requirement for voter or legislative approval of new or increased taxes; the result of the initiative in Oregon is too close to call. Two of five initiatives limiting property taxes passed.

Most states have been working to develop welfare programs that must be in place by July 1, 1997, to comply with the federal Temporary Assistance for Needy Families Act passed in August. So far, thirty-three states have submitted plans to the Department of Health and Human Services. Federal aid to states under the new block grant is tied to the caseload count in the 1992-94 period. Because caseloads have fallen in all but three states (Alaska, Hawaii, and Minnesota) in recent years, most states would receive more money this year under the block grant program than under the original entitlement program. Thus, states have a strong incentive to submit their plans early, as the federal government will not disburse funds on the block grant basis until the plans are declared complete.[14] The extent to which states will pick up costs for immigrants and others who lose under the legislation is unclear. So far, Maryland has indicated it may make aid available to the children of immigrants, and New Jersey, Utah, and Nebraska would use

14. HHS has declared eight plans complete, and another five are expected to be declared complete in the near future.

some state money to help noncitizens. In contrast, the governor of California is not likely to support the use of state funds to replace federal aid. Meanwhile, some local governments likely will step up aid: For example, more than a half-dozen counties in Northern California have announced that they will continue to provide prenatal care to illegal immigrant women if state aid is cut off.

Labor Costs

Although recent data point to more subdued compensation increases than in the first half of this year, the underlying trend in labor cost growth still appears to be upward. In the third quarter, the employment cost index (ECI) for private industry workers rose 2.5 percent at an annual rate compared with 3.2 percent in the second quarter. However, the recent quarterly movements in the ECI have been buffeted by fluctuations in the commissions earned by sales workers; on a twelve-month basis, the ECI was up 2.9 percent, slightly more than the 2.6 percent rise posted over the same period a year ago. Other measures of labor costs, such as preliminary estimates of compensation per hour in the nonfarm business sector and average hourly earnings also suggest a gradual acceleration over the past year.

The acceleration in the ECI has been concentrated in wages and salaries, which rose 3.3 percent over the year ended September 1996, compared with 2.8 percent in the preceding twelve months. Benefit costs again helped to moderate overall compensation growth, rising 1.8 percent on a twelve-month basis, 0.3 percentage point below the twelve-month change a year ago. This year's deceleration in benefit costs was largely in pensions, unemployment insurance, and workers' compensation.

An additional factor restraining benefit cost inflation has been the continued slow growth of employer costs for health insurance, which in the ECI rose just 0.7 percent over the twelve-month period ending in September. Although this increase is a bit higher than a year ago, it is well below the 7 percent pace of the early 1990s. The result of this sharp deceleration is that health care costs are now adding only about 0.1 percentage point per year to overall ECI growth, down from a contribution of almost 1 percentage point per year in the late 1980s.

EMPLOYMENT COST INDEX OF HOURLY COMPENSATION
FOR PRIVATE INDUSTRY WORKERS

	1995		1996		
	Sept.	Dec.	Mar.	June	Sept.
	-----Quarterly percent change------- (compound annual rate)				
Total hourly compensation[1]	2.6	2.6	2.9	3.2	2.5
Wages and salaries	3.0	2.6	4.3	3.6	2.6
Benefit costs	2.4	2.1	-0.3	2.7	2.7
By industry					
Construction	3.0	3.0	2.6	2.3	1.0
Manufacturing	2.2	3.2	1.9	3.8	3.4
Transportation and public utilities	4.2	3.2	1.9	2.5	2.5
Wholesale trade	5.2	3.5	1.6	4.1	2.8
Retail trade	2.7	2.3	6.0	-1.0	4.6
FIRE	3.0	1.3	4.6	5.9	1.3
Services	1.9	1.9	3.4	3.7	2.5
By occupation					
White-collar	2.9	2.5	3.5	3.1	3.4
Blue-collar	2.3	2.6	2.2	3.2	1.6
Service occupations	1.9	0.3	1.3	2.6	2.6
Memo:					
State and local governments	2.2	2.8	2.5	2.8	1.8
	-----Twelve-month percent change----				
Total hourly compensation	2.6	2.6	2.7	2.9	2.9
Excluding sales workers	2.5	2.6	2.6	2.8	2.9
Wages and salaries	2.8	2.8	3.2	3.4	3.3
Excluding sales workers	2.7	2.8	3.1	3.2	3.4
Benefit costs	2.1	2.2	1.6	1.7	1.8
By industry					
Construction	1.4	2.2	2.6	2.7	2.3
Manufacturing	2.3	2.6	2.5	2.8	3.1
Transportation and public utilities	3.8	3.7	3.1	3.0	2.6
Wholesale trade	4.6	4.5	3.5	3.6	3.0
Retail trade	1.8	2.2	3.0	2.5	2.9
FIRE	3.5	3.5	3.6	3.7	3.3
Services	2.4	2.2	2.5	2.7	2.9
By occupation					
White-collar	2.8	2.8	3.0	3.0	3.2
Blue-collar	2.3	2.4	2.5	2.6	2.4
Service occupations	2.4	1.9	1.9	2.0	2.2
Memo:					
State and local governments	3.0	2.9	2.8	2.6	2.5

1. Seasonally adjusted by the BLS.

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

	1995		1996		
	Sept.	Dec.	Mar.	June	Sept.
Hourly wages and salaries	2.8	2.8	3.2	3.4	3.3
By industry					
Construction	1.9	2.4	3.0	3.4	3.1
Manufacturing	2.9	2.9	2.9	2.9	3.4
Transportation and public utilities	3.4	3.4	2.8	2.5	2.4
Wholesale trade	4.2	4.7	4.3	4.3	3.7
Retail trade	2.1	2.4	3.5	2.9	3.2
FIRE	3.7	3.7	4.2	4.2	3.6
Services	2.5	2.4	3.0	3.5	3.5
By occupation					
White-collar	2.8	2.9	3.4	3.5	3.6
Blue-collar	2.8	2.9	2.9	3.0	2.9
Service occupations	2.7	2.2	2.3	2.5	2.7
Memo:					
State and local governments	3.1	3.2	2.8	2.8	2.8

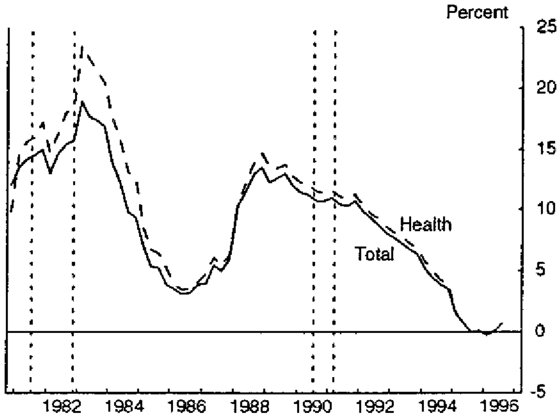
EMPLOYMENT COST INDEX OF HOURLY BENEFIT COSTS
FOR PRIVATE INDUSTRY WORKERS
(Twelve-month percent changes)

	1995		1996		
	Sept.	Dec.	Mar.	June	Sept.
Hourly benefit costs[1]	2.1	2.2	1.6	1.7	1.8
Insurance costs	0.0	0.1	-0.3	0.1	0.7
Health care	-0.1	0.1	-0.3	0.1	0.7
Supplemental pay	1.4	3.6	-0.5	2.2	1.7
Retirement and savings	7.8	4.7	4.7	3.3	3.5
Paid leave	3.3	3.4	3.3	3.4	3.6
Legally required	0.9	1.2	1.2	0.9	0.6
By industry					
Goods-producing	1.0	1.7	1.3	2.0	1.9
Service-producing	2.7	2.4	1.7	1.6	1.8
By occupation					
White-collar occupations	2.9	2.6	1.8	1.8	2.1
Blue-collar occupations	1.1	1.7	1.4	1.9	1.6
Service occupations	1.1	1.0	0.5	0.5	0.4
Memo:					
State and local governments	2.5	2.6	2.7	2.2	1.9

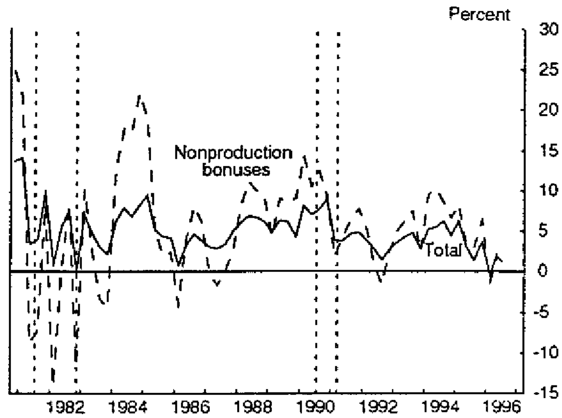
1. The detail on benefit costs is from unpublished data from the BLS.

Components of ECI Benefits Costs
(Private industry workers; twelve-month percent change)

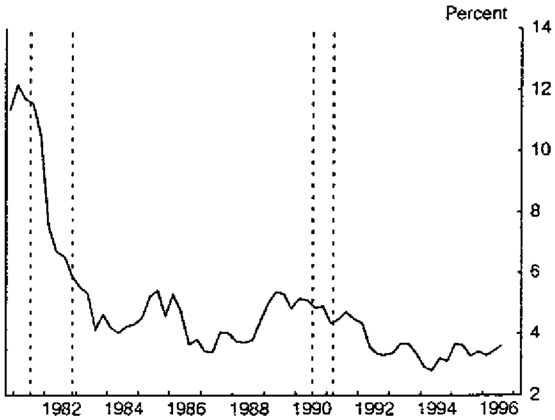
Insurance Costs



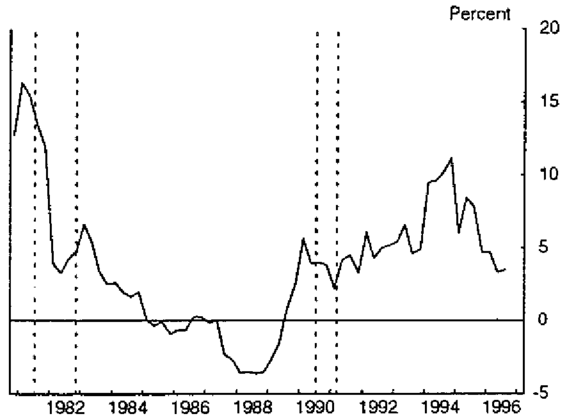
Supplemental Pay



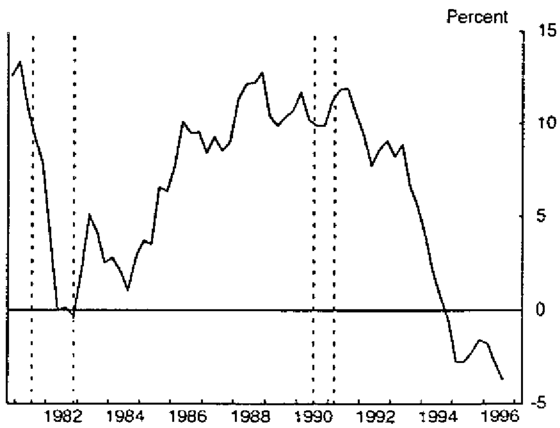
Paid Leave



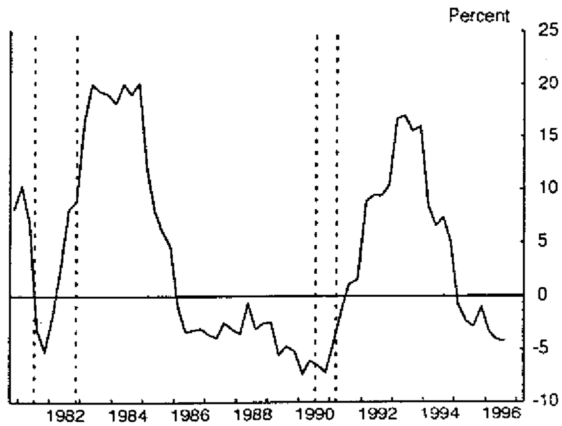
Retirement and Savings



Workers' Compensation Insurance



State Unemployment Insurance



Several recent surveys of firm benefit programs suggest four main reasons for the slowdown.[15] First, recent years have seen a tremendous shift from traditional fee-for-service plans to managed care and preferred-provider plans, with the number of workers in traditional plans falling from more than 70 percent in 1988 to around 25 percent in 1995. Second, over the same period, the proportion of workers and dependents covered by employer-provided health care fell from 78 percent to 74 percent. Third, employers have passed along an increasing share of premium costs to the workers. The fraction of full-time workers who pay no premium has declined about 10 percentage points since 1988, and the average fraction of the premium paid by workers rose from 25 percent to 33 percent in 1995 alone. Fourth, increases in total health care premiums have dropped sharply for all types of insurance plans. In part, this drop reflects an increase in deductibles and co-payments paid by insurees. However, price increases for health care services also have slowed sharply, with the PCE price index for medical care services excluding insurance premiums up about 2 percent over the past year, compared with increases in the 3-1/2 to 4 percent range in the previous few years.

Other measures of labor costs also show a modest uptick in compensation inflation. BEA estimates that compensation per hour in the nonfarm business sector rose almost 4-1/2 percent in the third quarter, up from 3.8 percent in the previous quarter. On a four-quarter-change basis, this measure of compensation has been up at a 3-3/4 percent to 4 percent pace since mid-1995. This higher rate of growth in compensation costs, coupled with relatively weak productivity gains, has led to a pickup in the growth of unit labor costs to about 3-3/4 percent over the same period. Average hourly earnings of production and nonsupervisory workers--the only wage data available for the fourth quarter--were unchanged in October. This series has been quite volatile in recent months, with twelve-month changes fluctuating between 3 percent and 3-1/2 percent. Nonetheless, the underlying trend in this series appears to be one of gradual acceleration, broadly in line with the trends shown by the ECI for wages of production workers.

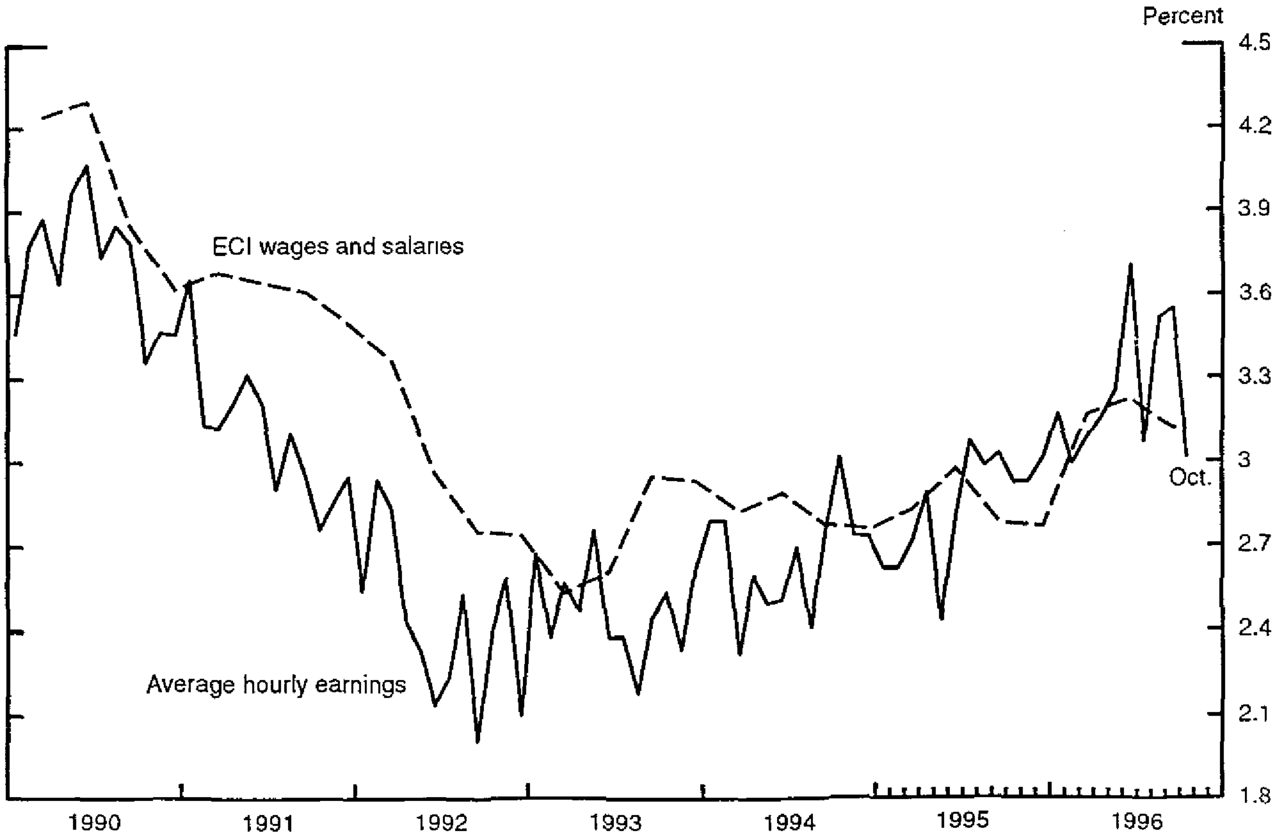
15. The information summarized here comes chiefly from three sources: the 1996 Hay/Huggins Benefits Report, the KPMG Peat Marwick 1996 Health Benefits Survey, and The American Hospital Association's final report on recent trends in employer health insurance coverage and benefits for 1996.

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

	1994[1]	1995[1]	1995 Q4	1996 Q1	1996 Q2	1996 Q3	1995:Q3 to 1996:Q3
Nonfarm Business Sector							
Output per hour	.5	.3	-1.1	1.8	.5	-.4	.2
Compensation per hour	2.5	4.1	4.1	3.3	3.7	4.4	3.8
Unit labor costs	2.0	3.8	5.2	1.5	3.2	4.8	3.6

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. 1996 Q3 data are unpublished BEA estimates.

Earnings of Production or Nonsupervisory Workers
(Twelve-month change)



Prices

The incoming data on consumer price inflation have remained favorable. Although the CPI excluding food and energy rose 0.3 percent in September, this followed an increase of only 0.1 percent in August. The overall CPI also was up 0.3 percent in September. The energy component, however, is likely to add noticeably to the overall CPI in coming months.

The CPI for energy was flat in September after declining in the preceding three months. Heating oil prices were up sharply in September owing both to low inventory levels and the run-up in crude oil prices since early that month. However, motor fuel prices were about flat. We would have expected the increase in crude oil prices to show up in retail gasoline prices by now; but according to the Lundberg survey, gasoline prices were just beginning to rise in late October. Gasoline margins--for both marketers and refiners--now stand at extremely low levels, and margins on heating oil also are on the low side. The low gasoline margins seem to be, in part, the result of ongoing price wars around Los Angeles, which have left gasoline prices about 15 cents per gallon lower than elsewhere in California. Such low margins probably cannot be maintained very long, however, and unless crude oil prices drop substantially, outsized energy price increases are likely in coming months.

Consumer food prices have continued to play out the effects of rising grain prices earlier in the year. The CPI for food rose another 0.5 percent in September and is up at about a 5 percent annual rate over the past six months. High prices for feed grains earlier in the year continued to boost prices for dairy products, meats, poultry, and eggs in September. But grain prices have come down sharply since midsummer, and this drop should lead to smaller increases in consumer food prices by year-end.

The September data showed no sign of a pickup in the trend of core inflation: In the absence of a few special factors, core CPI inflation probably would have registered an increase of 0.2 percent rather than the 0.3 percent published figure. Prices of new vehicles rose 0.6 percent in September, owing in part to a larger-than-usual share of new-model-year vehicles in the September

CPI AND PPI INFLATION RATES
(Percent change)

	From twelve months earlier		1996		1996	
	Sept. 1995	Sept. 1996	Q2	Q3	Aug.	Sept.
			-Annual rate-		-Monthly rate-	
CPI						
All items (100.0)[1]	2.5	3.0	3.9	2.3	0.1	0.3
Food (15.8)	2.7	3.8	4.3	5.6	0.4	0.5
Energy (6.7)	-1.8	5.2	18.4	-7.4	-0.6	.0
CPI less food and energy (77.5)	2.9	2.7	2.7	2.4	0.1	0.3
Commodities (23.9)	1.5	1.2	0.6	0.1	-0.1	0.4
New vehicles (5.0)	1.8	2.3	2.4	3.2	0.1	0.6
Used cars (1.3)	7.6	0.3	-5.8	-4.1	.0	0.3
Apparel (5.0)	-1.3	-1.3	-1.8	-4.8	-1.5	0.5
Services (53.6)	3.6	3.3	3.6	3.6	0.2	0.2
Owners' equivalent rent (19.7)	3.2	3.0	2.8	2.7	0.1	0.2
Tenants' rent (5.8)	2.3	2.8	2.6	3.0	0.1	0.2
Medical care (6.1)	5.0	3.3	3.1	3.3	0.2	0.2
Auto finance charges (0.6)	11.4	-0.9	0.3	13.7	1.8	0.9
PPI						
Finished goods (100.0)[2]	1.8	2.9	2.8	1.5	0.3	0.2
Finished consumer foods (23.4)	3.0	4.2	2.4	8.6	1.0	0.2
Finished energy (13.4)	-0.8	7.1	13.1	-7.4	0.7	0.2
Finished goods less food and energy (63.2)	2.0	1.4	0.9	1.2	-0.1	0.3
Consumer goods (38.5)	2.2	1.6	1.4	1.1	.0	0.2
Capital equipment (24.7)	1.6	1.1	0.1	1.2	-0.1	0.3
Intermediate materials (100)[3]	4.8	0.5	1.8	-1.1	0.2	0.3
Intermediate materials less food and energy (82.6)	6.1	-1.6	-1.3	-0.6	0.1	0.1
Crude materials (100)[4]	2.8	10.2	17.5	2.2	0.2	-1.5
Crude food materials (44.7)	7.4	14.6	40.7	16.7	-0.3	-3.8
Crude energy (31.4)	-5.5	20.9	11.4	-8.0	0.7	0.6
Crude materials less food and energy (23.9)	7.2	-10.3	-11.0	-8.2	0.1	0.6

1. Relative importance weight for CPI, December 1995.
2. Relative importance weight for PPI, December 1995.
3. Relative importance weight for intermediate materials, December 1995.
4. Relative importance weight for crude materials, December 1995.

sample.[16] In addition, apparel prices rose 0.5 percent on a seasonally adjusted basis after larger declines in preceding months; this monthly pattern apparently owes to the late introduction of fall clothing lines this year. Finally, airfares jumped nearly 3 percent in September following the re-introduction of a 10 percent tax on airfares in late August. This tax is temporary, and Congress failed to renew it before recess; if Congress does not renew the tax when it reconvenes after the election, the tax will expire again in January.

BROAD MEASURES OF INFLATION
(Four-quarter percent changes)

	1993 Q3	1994 Q3	1995 Q3	1996 Q3
Product prices				
GDP chain price index	2.6	2.4	2.5	2.1
GDP deflator	2.6	2.3	2.6	1.9
Nonfarm business chain price index[1]	2.6	2.5	2.1	1.7
Expenditure Prices				
Gross domestic purchases chain price index	2.3	2.5	2.3	2.0
Less food and energy	2.6	2.4	2.5	1.8
PCE chain price index	2.5	2.7	2.1	2.2
Less food and energy	2.9	2.7	2.4	1.8
PCE deflator	2.5	2.6	2.2	2.0
Less food and energy	2.9	2.7	2.3	1.7
CPI	2.8	2.9	2.7	2.9
Less food and energy	3.3	2.9	3.0	2.7
Median CPI	2.8	3.1	3.2	2.9

1. Excluding housing.

The quiescence of the CPI data was paralleled by the slow growth of PCE prices, which rose at a 1.6 percent rate in the third quarter. Indeed, over the past four quarters, the PCE chain price

16. The Big Three announced prices for 1997 cars that are about 1-1/2 percent above prices for comparably equipped 1996 models--about 1 percentage point smaller than last year's price increases. Of course, some of these price increases reflect quality improvements. On November 13, the BLS plans to report its estimates of quality changes for 1997-model vehicles.

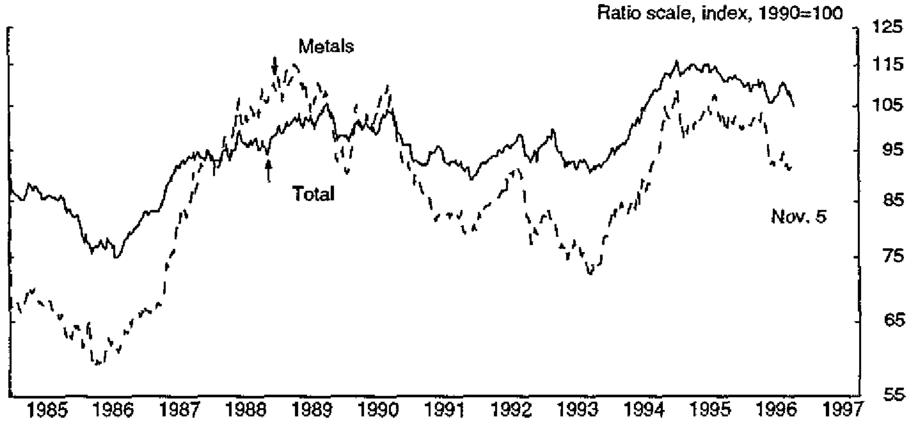
SPOT PRICES OF SELECTED COMMODITIES

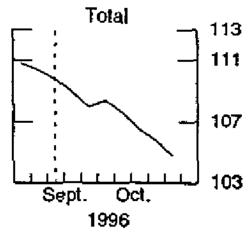
	Current price ($)	Percent change[1]: 1994	1995	Dec. 26 to Sept. 17[2]	Sept. 17[2] to Nov. 05	Memo: Year earlier to date
Metals						
Copper (lb.)	.990	64.9	-3.5	-32.4	7.6	-29.3
Steel scrap (ton)	126.500	2.9	-6.6	1.9	-7.3	-5.9
Aluminum, London (lb.)	.636	73.5	-12.9	-17.1	1.4	-16.0
Precious metals						
Gold (oz.)	379.300	-1.7	1.7	-1.0	-1.1	-1.4
Silver (oz.)	4.795	-5.0	7.2	-1.9	-4.9	-10.0
Forest products						
Lumber (m. bdft.)	431.000	-37.1	-14.4	73.2	-.5	71.0
Plywood (m. sqft.)	324.000	1.5	-6.1	18.4	-11.7	1.9
Petroleum						
Crude oil (barrel)	21.890	15.6	16.8	21.1	-.8	30.1
Gasoline (gal.)	.665	32.4	7.7	16.5	8.1	34.2
Fuel oil (gal.)	.653	12.7	22.6	8.6	-.5	28.7
Livestock						
Steers (cwt.)	71.000	-3.4	-5.7	9.1	-1.4	6.0
Hogs (cwt.)	53.500	-12.9	27.5	20.4	-1.8	30.5
Broilers (lb.)	.606	-4.9	10.7	15.5	-3.4	4.2
U.S. farm crops						
Corn (bu.)	2.510	-23.2	57.4	-6.6	-22.5	-22.9
Wheat (bu.)	4.455	11.4	24.0	-14.9	-3.2	-15.3
Soybeans (bu.)	6.645	-19.6	29.0	11.7	-17.4	-1.8
Cotton (lb.)	.702	38.5	-8.1	-5.9	-5.6	-17.3
Other foodstuffs						
Coffee (lb.)	1.270	153.1	-39.1	31.7	-3.1	2.4
Memo:						
JOC Industrials	104.800	22.1	-1.7	-1.3	-4.6	-6.2
JOC Metals	90.900	31.9	-1.8	-9.6	-1.1	-11.8
KR-CRB Futures	236.130	4.8	3.3	.2	-3.4	-3.4
KR-CRB Spot	328.330	29.1	-3.5	3.7	-4.2	-3.2

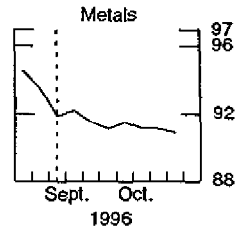
1. Changes, if not specified, are from the last week of the preceding year to the last week of the period indicated.
2. Week of the September Greenbook.

Commodity Price Measures

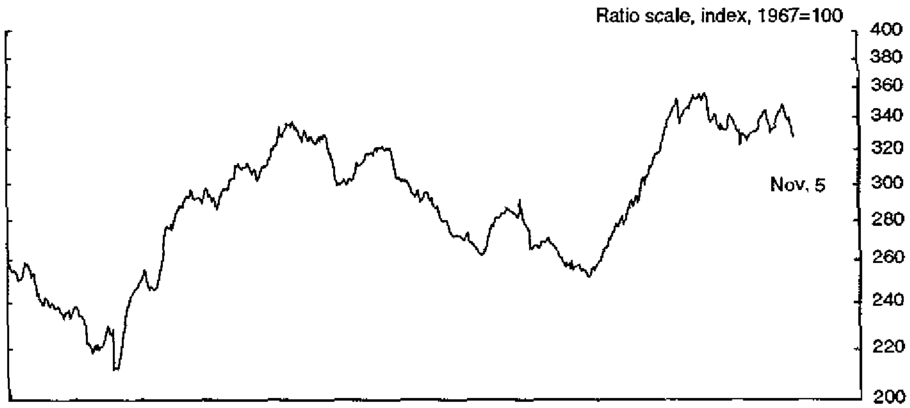
Journal of Commerce Index

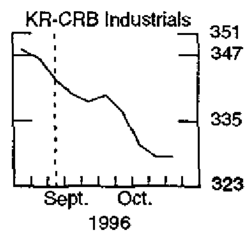




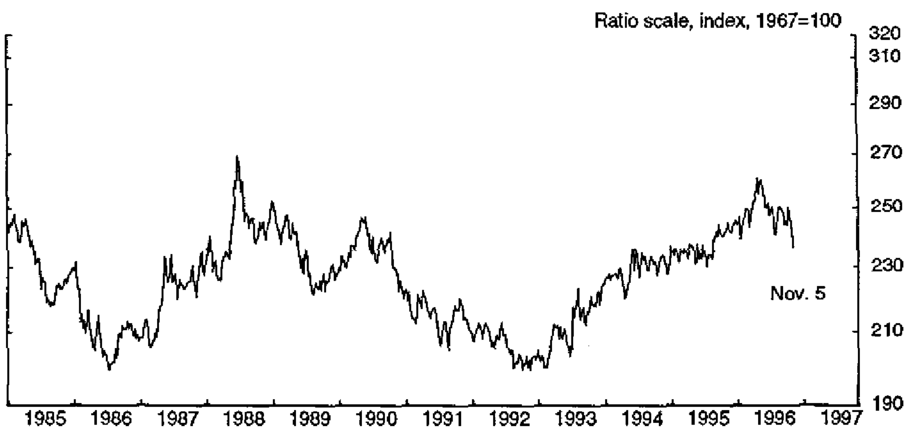


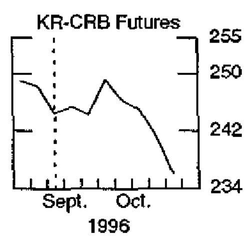
KR-CRB Spot Industrials





KR-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 KR-CRB spot price index consists entirely of industrial commodities, excluding energy. The KR-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.

index excluding food and energy increased only 1.8 percent, 1/2 percentage point less than over the preceding four quarters. By contrast, increases in the overall PCE chain price index, like the overall CPI, have remained about constant, reflecting the energy price increases earlier in the year. Product prices--which include energy but with a much smaller weight than in expenditure prices--also have continued to decelerate over this period.

In contrast to the situation with labor costs, there appear to be few price pressures coming from materials. The Journal of Commerce industrial materials index has declined 4-1/2 percent since the last Greenbook and remains below its year-ago level. As noted above, farm commodity prices have come down considerably in recent months. Prices of steel scrap and plywood also have come down since the last Greenbook. The PPI for crude materials less food and energy moved up in September but remained 10 percent below its year-earlier level.

DOMESTIC FINANCIAL DEVELOPMENTS

Selected Financial Market Quotations[1]
(Percent except as noted)

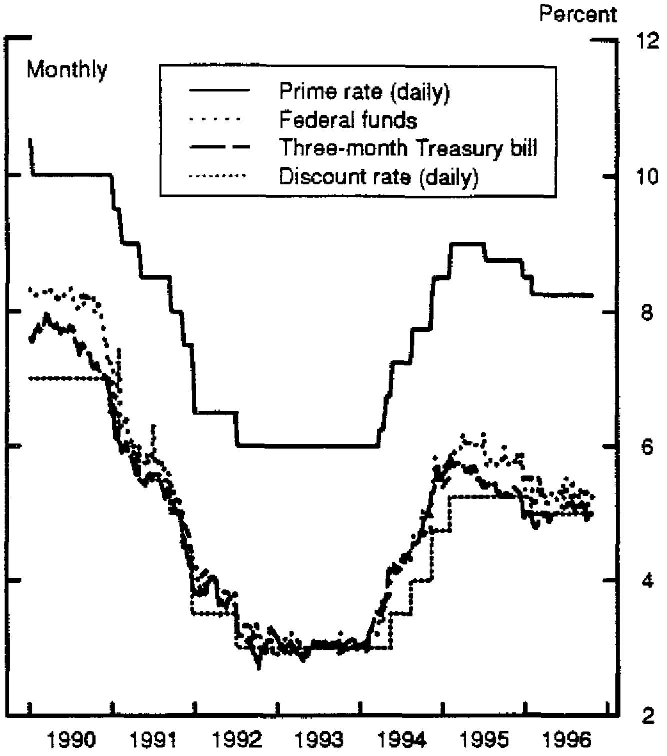
Instrument	1996 Feb. low	1996 July high	1996 FOMC,* Sep. 24	1996 Nov. 5	Change to Nov. 5, from: Feb. low	Change to Nov. 5, from: July high	Change to Nov. 5, from: FOMC, Sep. 24
Short-term rates							
Federal funds[2]	5.15	5.39	5.23	5.32	0.17	-0.07	0.09
Treasury bills[3]							
3-month	4.76	5.21	5.15	5.03	0.27	-0.18	-0.12
6-month	4.67	5.40	5.30	5.07	0.40	-0.33	-0.23
1-year	4.55	5.64	5.52	5.14	0.59	-0.50	-0.38
Commercial paper							
1-month	5.27	5.50	5.52	5.37	0.10	-0.13	-0.15
3-month	5.12	5.59	5.59	5.41	0.29	-0.18	-0.18
Large negotiable CDs[3]							
1-month	5.21	5.44	5.45	5.28	0.07	-0.16	-0.17
3-month	5.12	5.59	5.55	5.38	0.26	-0.21	-0.17
6-month	4.99	5.83	5.74	5.44	0.45	-0.39	-0.30
Eurodollar deposits[4]							
1-month	5.13	5.38	5.38	5.25	0.12	-0.13	-0.13
3-month	5.13	5.56	5.50	5.38	0.25	-0.18	-0.12
Bank prime rate	8.25	8.25	8.25	8.25	0.00	0.00	0.00
Intermediate- and Long-term Rates							
U.S. Treasury (constant maturity)							
3-year	4.98	6.62	6.40	5.86	0.88	-0.76	-0.54
10-year	5.58	7.06	6.83	6.28	0.70	-0.78	-0.55
30-year	6.02	7.19	7.02	6.60	0.58	-0.59	-0.42
Municipal revenue (Bond Buyer)[5]	5.67	6.24	6.10	5.94	0.27	-0.30	-0.16
Corporate-A utility, recently offered	7.18	8.23	8.08	7.65	0.47	-0.58	-0.43
High-yield corporate[6]	9.57	10.36	9.95	9.82	0.25	-0.54	-0.13
Home mortgages[7]							
FHLMC 30-yr fixed rate	6.94	8.42	8.14	7.78	0.84	-0.64	-0.36
FHLMC 1-yr adjustable rate	5.19	6.01	5.83	5.60	0.41	-0.41	-0.23

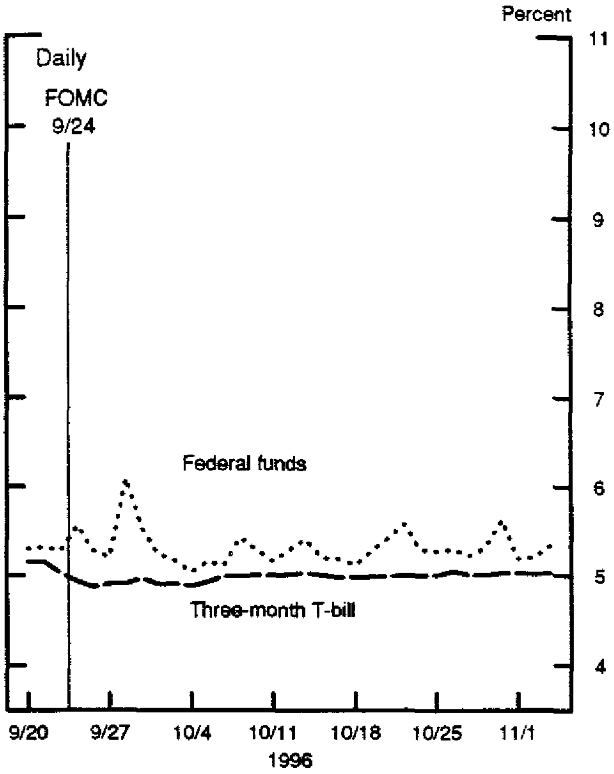
Stock exchange index	Record high Level	Record high Date	1996 July low	1996 FOMC, Sep. 24	1996 Nov. 5	Percentage change to Nov. 5, from: Record high	Percentage change to Nov. 5, from: July low	Percentage change to Nov. 5, from: FOMC, Sep. 24
Dow-Jones Industrial	6094.23	10/18/96	5346.55	5894.74	6081.18	-0.21	13.74	3.16
NYSE Composite	378.43	11/5/96	336.07	365.51	378.43	0.00	12.60	3.53
S&P 500 Composite	710.14	11/5/96	626.65	686.48	714.14	0.56	13.96	4.03
NASDAQ (OTC)	1258.10	10/15/96	1042.37	1211.47	1229.07	-2.31	17.91	1.45
Wilshire 5000	6943.80	10/18/96	6099.34	6723.87	6920.29	-0.34	13.46	2.92

1. One-day quotes except as noted.
2. Average for two-week reserve maintenance period closest to date shown. Last observation is the average to date November 6, 1996.
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 and futures market index changes.
6 Merrill Lynch MasterII high bond index composite.
7. Quotes for week ending Friday previous to date shown.
* Figures cited are as of the close on Septmeber 23.

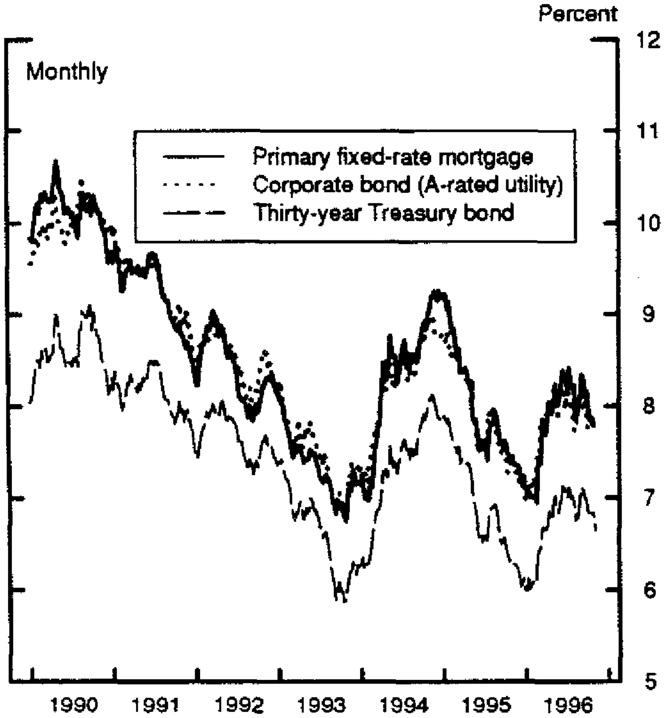
Selected Interest Rates

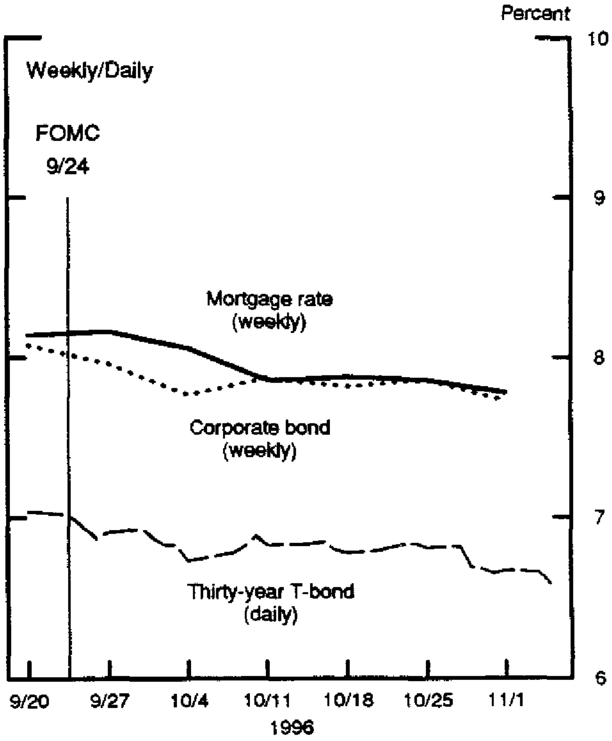
Short-Term





Long-Term





The FOMC's decision at its September meeting to keep the federal funds rate at 5-1/4 percent triggered a rally in most financial markets, with money market interest rates falling about 10 basis points and long-term rates edging lower. Subsequently, intermediate- and long-term interest rates have declined further as incoming data have generally confirmed the view that economic growth has slowed and inflation has remained subdued. Currently, the thirty-year Treasury bond rate is 6.6 percent, down about 40 basis points from the September meeting. Allowing for typical term premia, the prevailing structure of rates suggests that market participants have mostly ruled out System tightening in the months ahead.

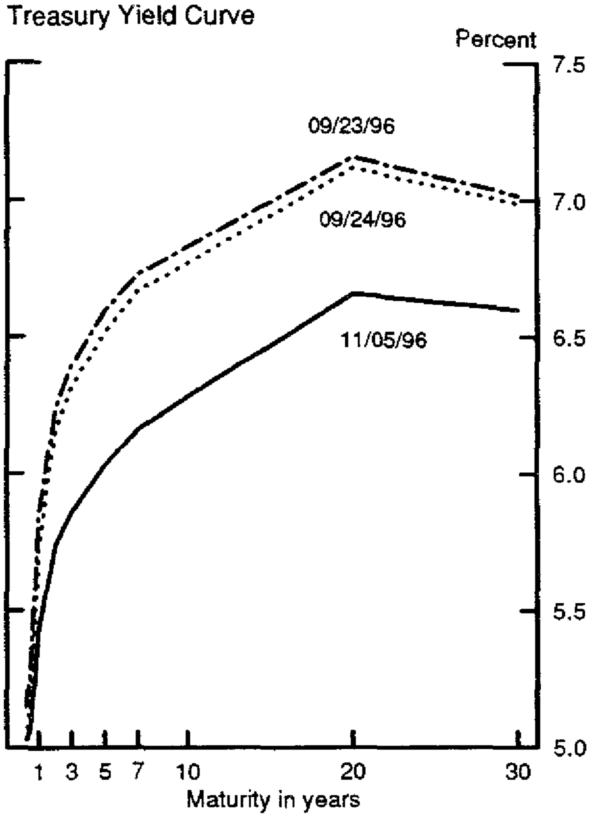
The rally in bond markets was accompanied by further price increases in the equity markets. The Dow and S&P 500 indexes have risen 3 percent to 4 percent since the previous FOMC meeting, bringing their cumulative gains from the end of 1995 to 19 percent and 16 percent respectively. In contrast, the NASDAQ index (which had recorded larger gains in August and September) has risen less than 1-1/2 percent since the September meeting; still, it is up 17 percent on the year.

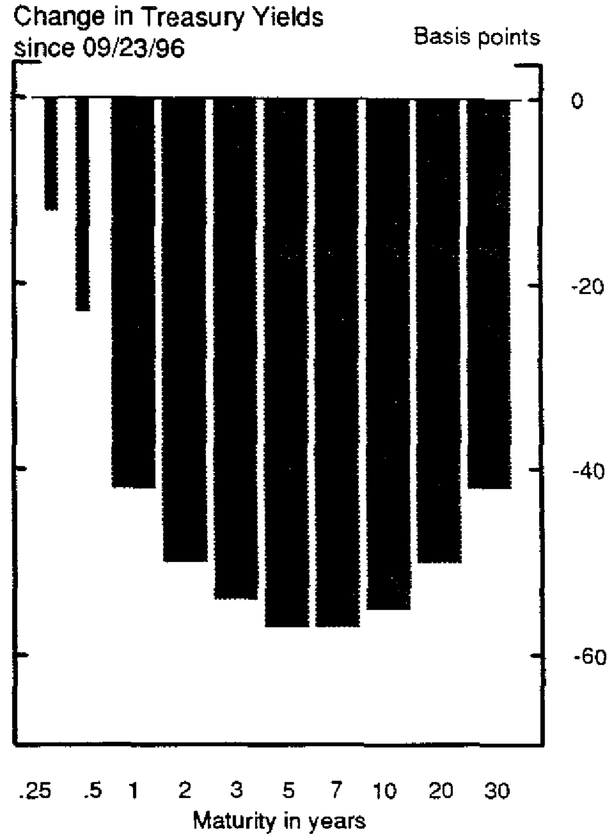
Overall growth of credit appears to have remained moderate in recent months. Business borrowing from banks and in the bond market picked up in September and October after a lull in the summer; the pickup was offset in part, however, by a sizable runoff of commercial paper. Growth of household debt evidently has slowed a bit, reflecting a further deceleration in consumer credit and some slowing of mortgage borrowing from its first-half pace. State and local government debt contracted in the third quarter, while borrowing by the federal government picked up more than seasonally from its weak second-quarter pace. Stronger expansion of bank credit in the past two months has been funded with wholesale liabilities, boosting M3 growth markedly relative to that of M2.

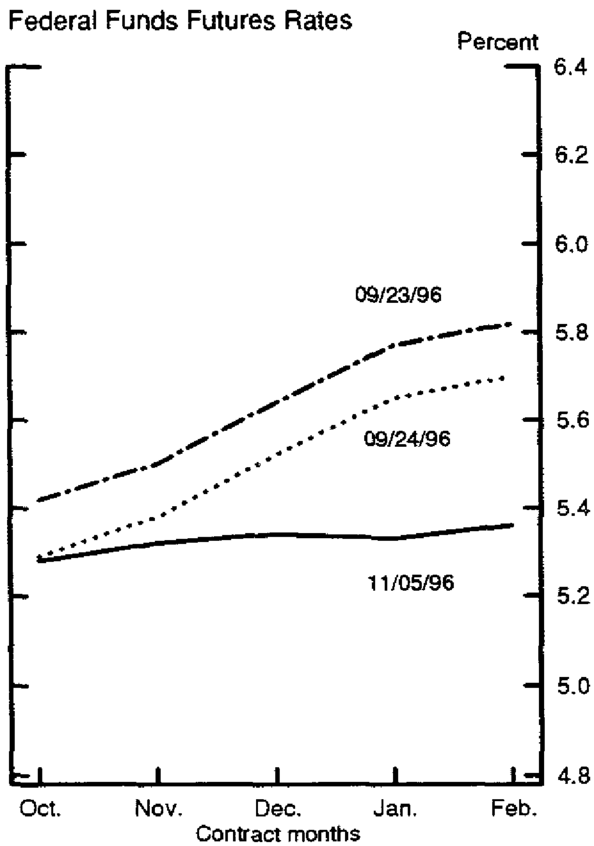
Bank Credit and the Monetary Aggregates

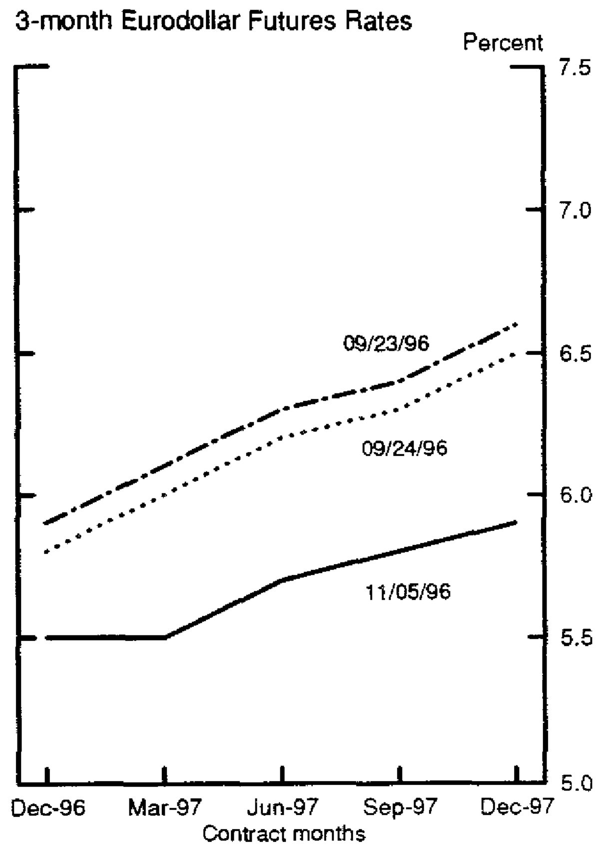
The growth of bank credit picked up a percentage point in October but, adjusted for mark-to-market accounting effects, was, at

Treasury Yield Curve and Selected Short-Term Futures Rates









Note. Changes are taken from levels of the day before the previous FOMC meeting.

6-3/4 percent, little changed from September.[1] Expansion in both months was entirely accounted for by loan growth. Business loans were up at an annual rate of more than 14 percent in October after rising at a 22-1/2 percent annual rate in September. Reasons for the huge surge in business lending at banks have been elusive, although it followed a couple of months of anemic expansion when external financing needs likely were rising with a buildup of inventories. The increase has been widespread among large, small, and foreign banks, and while linking the gain to specific types of business spending is not possible, some of the increase in September appears to be attributable to unusually strong demands to finance mergers and acquisitions. In addition, preliminary results from the November Senior Loan Officer Opinion Survey suggest that banks have continued to ease standards and terms for business loans since August.[2]

Growth in real estate loans at banks was weak in October, as it has been for most of this year, apparently reflecting the tendency of banks to securitize home mortgages. The home equity component of real estate loans, however, has grown much more rapidly of late, averaging around a 13 percent annual rate in September and October. Meanwhile, the retrenchment in consumer lending became more pronounced as loans held by banks contracted slightly in October; even after adding back loans that had been securitized, bank consumer loans grew at an annual rate of only about 1-1/4 percent last month.

The recent growth in bank loans has been funded in large part with wholesale deposits. M3, bolstered by substantial increases in large time deposits, expanded at a 10-1/2 percent annual rate in October, after a 7-1/4 percent rise in September. The recent strength in M3 has pushed this aggregate to the top of its 2 percent to 6 percent annual growth range for the year. M2 growth stayed at 3-1/4 percent in October, again reflecting some runoff in liquid deposits, which internalize shifts of funds related to sweep accounts. The volume of new retail sweeps set a record in October of nearly $15 billion.

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1. Bank credit has been adjusted to remove the effects of accounting rules that require the booking of changes in the market value of certain bank securities and the booking of revaluation gains in derivative portfolios.
2. Results of the Senior Loan Officer Opinion Survey are discussed in more detail in the appendix.

Commercial Bank Credit
(Percentage change; seasonally adjusted annual rate)

Type of credit	1995	1996 Q2	1996 Q3	1996 Aug	1996 Sep	1996 Oct p	Level, Oct 1996 p (billions of $)
1. Bank credit - reported	8.8	2.6	1.3	-1.8	5.0	6.0	3,711.9
2. - adjusted[1]	7.1	4.0	2.0	-0.8	7.0	6.8	3,654.5
3. Securities - reported	4.1	-2.7	-6.4	-13.5	-6.8	-2.1	967.6
4. - adjusted[1]	-2.2	2.4	-4.3	-10.3	0.1	0.5	910.3
5. U.S. government	-3.3	1.0	-2.3	-10.0	2.4	-6.8	699.7
6. Other[2]	28.8	-11.5	-17.0	-22.5	-30.4	10.8	268.0
7. Loans[3]	10.8	4.6	4.1	2.4	9.3	8.9	2,744.2
8. Business	11.6	5.1	6.7	2.6	22.4	14.2	766.9
9. Real estate	8.5	3.2	3.2	7.3	1.8	2.4	1,113.8
10. Home equity	5.2	-0.5	3.0	9.0	10.5	16.3	82.1
11. Other	8.7	3.5	3.3	7.2	1.2	1.2	1,031.6
12. Consumer - reported	10.7	4.9	5.8	3.3	9.3	-0.7	517.7
13. - adjusted[4]	17.6	9.2	7.8	5.1	8.4	1.2	673.4
14. Other[5]	17.5	7.7	-1.1	-14.8	4.7	33.5	345.9

Note. Adjusted for breaks caused by reclassifications. Monthly levels are *pro rata* averages of weekly (Wednesday) levels. Quarterly levels (not shown) are simple averages of monthly levels. Annual levels (not shown) are levels for the fourth quarter. Growth rates shown are percentage changes in consecutive levels, annualized but not compounded.

1. Adjusted to remove effects of mark-to-market accounting rules (FIN 39 and FASB 115).
2. Includes securities of corporations, state and local governments, and foreign governments and any trading account assets that are not U.S. government securities.
3. Excludes interbank loans.
4. Includes an estimate of outstanding loans securitized by commercial banks.
5. Includes security loans, loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.

MONETARY AGGREGATES
(Based on seasonally adjusted data)

Aggregate or component	1995	1996 Q2	1996 Q3	1996 Aug.	1996 Sept	1996 Oct. (p)	1995:Q4 to Oct. 96 (p)	Level (bil. $) Oct. 96 (p)
Aggregate	Percentage change (annual rate)[1]							
1. M1	-1.8	-0.7	-6.9	-9.6	-8.4	-18.1	-5.2	1075.3
2. M2[2]	3.9	3.8	2.7	3.8	3.3	3.3	4.0	3775.2
3. M3	5.8	5.1	4.0	4.8	7.2	10.4	6.0	4809.5
Selected components								
4. Currency	5.4	3.7	7.9	7.5	7.5	8.7	5.4	390.2
5. Demand deposits	1.4	10.6	-2.0	-8.8	-5.9	-26.6	2.2	396.5
6. Other checkable deposits	-11.1	-18.5	-30.2	-31.7	-32.9	-42.5	-24.0	280.2
7. M2 minus M1[3]	6.6	5.7	6.9	9.5	8.1	12.0	8.1	2700.0
8. Savings deposits	-3.3	11.2	8.0	10.8	7.0	15.8	12.0	1247.8
9. Small time deposits	15.0	-3.0	1.9	4.9	4.5	5.8	0.8	941.1
10. Retail money market funds	18.9	9.3	13.7	14.9	17.4	14.5	13.3	511.0
11. M3 minus M2[4]	14.5	10.2	8.7	8.6	22.4	37.4	14.2	1034.3
12. Large time deposits, net[5]	15.5	13.8	15.7	9.6	22.6	53.1	17.7	481.1
13. Institution-only money market mutual funds	23.1	8.8	18.5	20.4	25.7	7.8	19.0	264.4
14. RPs	4.6	11.6	-16.4	-8.0	18.1	34.9	1.7	187.3
15. Eurodollars	12.0	2.9	4.6	21.4	22.2	65.5	13.8	104.4
Memo								
16. Monetary base	4.1	2.1	5.8	6.2	4.6	-0.5	3.0	445.6
17. Household M2[6]	4.1	3.0	3.5	6.0	3.7	6.8	4.2	3378.7
	Average monthly change (billions of dollars)[7]							
Memo								
Selected managed liabilities at commercial banks:								
18. Large time deposits, gross	5.5	6.6	8.0	9.7	10.6	21.7	...	519.6
19. Net due to related foreign institutions	3.5	-4.8	-3.2	-5.4	1.1	-1.0	...	243.6
20. U.S. government deposits at commercial banks	-0.1	0.0	1.7	-3.7	3.0	-3.4	...	17.9

1. For the years shown, fourth quarter-to-fourth quarter percent change. For the quarters shown, based on quarterly averages.
2. Sum of seasonally adjusted M1, retail money market funds, savings deposits, and small time deposits.
3. Sum of retail money funds, savings deposits, and small time deposits, each seasonally adjusted separately.
4. Sum of large time deposits, institutional money funds, RP liabilities of depository institutions, and Eurodollars held by U.S. addressees, each seasonally adjusted separately.
5. Net of holdings of depository institutions, money market mutual funds, U.S. government, and foreign banks and official institutions.
6. M2 less demand deposits
7. 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.
p--Preliminary.

Net Sales of Selected Mutual Funds
(Billions of dollars; quarterly and annual data at monthly rate)

			1996					Memo:
	1994	1995	H1	Q3	Aug.	Sept.	Oct.[e]	Sept. assets
Stock funds	11.0	12.2	23.9	14.2	18.3	19.8	13.4	1621.6
Domestic[1]	7.2	11.1	18.9	11.5	14.8	16.5	10.3	1359.3
Aggressive growth	2.2	3.2	6.0	3.3	4.6	4.9	3.2	264.1
Growth	2.0	3.5	5.1	2.6	4.0	4.4	1.7	446.1
Growth & income[2]	4.2	4.4	7.7	5.6	6.0	7.5	5.8	643.8
International	3.8	1.2	5.0	2.7	3.5	3.3	3.0	262.3
Bond funds	-1.4	2.0	3.8	2.6	2.0	4.9	1.0	854.1
High-yield	0.2	0.9	1.0	1.6	2.0	1.6	0.8	72.5
Income	2.2	1.7	2.9	1.6	1.3	2.9	1.5	330.2
Other	-3.8	-0.6	-0.1	-0.6	-1.3	0.4	-1.3	451.4

1. Includes precious metals funds, not shown elsewhere.
2. Calculated as the sum of "Growth and income" and "Income equity" in the ICI data.
e Estimate.
Source. Investment Company Institute.

Even as M2 growth continued to be subdued in October, net sales of mutual fund shares slowed. Inflows to equity funds declined following a pickup in activity in August and September; nonetheless, net sales amounted to $13-1/2 billion, about the same rate of inflow as in the third quarter as a whole. In October, investors' demand for all types of equity funds was down from the previous month, but the dropoff was greatest for the more speculative types of funds. Net sales of bond mutual funds were $1 billion in October, down from the $2-1/2 billion monthly rate in the third quarter. Sales of all major types of bond funds weakened last month.

Although data are incomplete, commercial banks apparently recorded another increase in profits in the third quarter. Reports from forty-five of the top fifty bank holding companies indicate that net income rose about 3-1/2 percent from a year earlier, a marked slowdown from the 13 percent year-over-year expansion for the top fifty bank holding companies recorded in the third quarter of 1995. Profits were held down in the third quarter by the one-time assessment required of those banks with deposits insured by the Savings Association Insurance Fund (SAIF).[3] On the other hand, the shift by banks toward loans and away from securities provided a boost to net interest margins. Banks also continued to score gains in fee income, a major source of profit growth over the past several years. A number of banks increased loss provisions, although the ratio of nonperforming loans to total loans actually fell at many banks from their year-earlier levels.

Business Finance

Gross bond offerings by nonfinancial corporations rebounded in the second half of September and strengthened further in October (table). In part, the recent increases have reflected the typical seasonal pickup that occurs after Labor Day, but the decline in long-term interest rates since mid-September also appears to have encouraged more bond funding. Indeed, roughly one-fourth of October's strong issuance came in the final three days as long-term rates shed nearly 20 basis points. Meanwhile, commercial paper of nonfinancial firms declined in October for the fourth straight month (chart, lower left panel). A number of issuers have paid down commercial paper debt with proceeds from asset sales, while others have used repatriated profits that had accumulated in Puerto Rico.[4]

Gross equity issuance by nonfinancial firms, which slowed in response to the market correction in July and remained low in August and September, posted a sharp increase in October (table). The rebound in equity issuance reflected the recent gains in stock prices as well as renewed interest in initial public offerings. First-day price changes for IPOs in September rebounded to about

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3. The total assessment of $4.7 billion applies to all institutions holding SAIF-insured deposits. Commercial banks will bear about $1.2 billion of the total assessment. The after-tax cost will be somewhat less because the assessment reduces banks' taxable income. Overall, the SAIF assessment appears to have lowered bank profits about 6 percent in the third quarter, and thus could account for a significant part of the slowdown in the four-quarter growth of commercial bank profits. The payment is due November 29, but it had to be booked as a third-quarter expense.

4. Many large U.S. corporations invested profits from their Puerto Rican operations in a fund created to support Puerto Rican economic development; these investments were encouraged largely by tax credits. The favorable tax treatment was eliminated, however, in the minimum wage bill enacted in late August. Since then, some firms have withdrawn their Puerto Rican funds and used the cash to pay down commercial paper liabilities.

20 percent, double the average increases in the previous two months (chart, lower right panel).

Merger activity continues at a record-setting pace and involves deals in a wide range of industries. Although pending mergers will rely heavily on stock swaps for financing, the sheer magnitude of ongoing activity will keep equity retirements relatively high. These retirements plus the continued brisk pace of share repurchases will almost certainly cause nonfinancial firms to continue to retire equity on net in the near term.[5]

Stock prices have increased since the September FOMC meeting, with the Dow and S&P 500 indexes up 3 percent to 4 percent to record highs and the NASDAQ Composite up about half as much (chart, upper panel). It appears that the stock market's continued strong performance has been supported by the perception that because inflation remains subdued and economic growth is moderating, the likelihood that monetary policy will be tightened in the near term is low. In addition, earnings have continued to be healthy. Earnings of firms in the S&P 500 were up about 8 percent from four quarters earlier, decelerating from the 10 percent to 12 percent range over the preceding several quarters. Nonetheless, the twelve-month-forward price-to-earnings ratio for the S&P 500 continued to climb and, at just under 16 in October, eclipsed its 1987 high (middle panel).

News on the credit quality of nonfinancial corporations remains largely favorable. Even though the rate of business failures among nonfinancial firms edged up in the third quarter, it remains quite low (lower left panel). Moreover, estimated defaults on junk bonds in the third quarter were at the historically low rate of less than 1 percent (lower right panel), and spreads on junk bonds remain very narrow, although they increased sharply on a handful of lower-rated junk bond issues following the release of disappointing third-quarter earnings reports for those companies. The value of junk debt upgraded by Moody's in the third quarter exceeded the value of that downgraded by better than two-to-one, and the value of

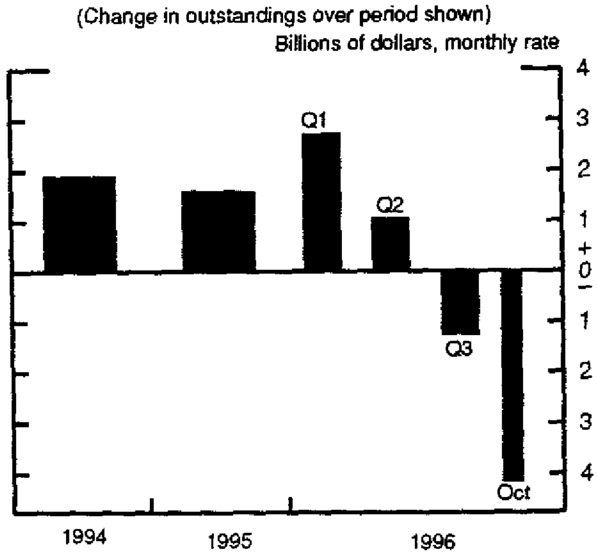
5. The recently announced acquisition of MCI by British Telecommunications alone results in domestic equity share retirements of around $26 billion. Even though a large portion of the deal involves a stock swap, the acquisition by a foreign company implies that domestic nonfinancial equity is retired, with foreign equity used as payment. The MCI share retirements probably will not occur before the second half of 1997, as the merger will be subject to an extensive review by regulators in the United States.

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

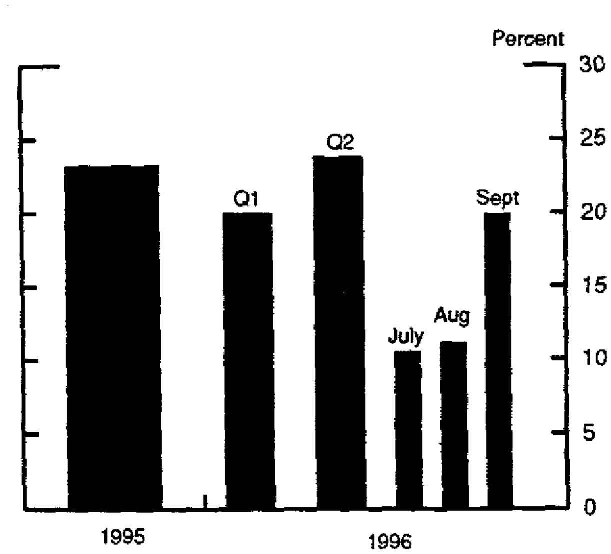
Type of security	1994	1995	1996 Q2	1996 Q3	1996 Aug.	1996 Sept.	1996 Oct.[p]
All U.S. corporations	41.29	47.64	64.87	48.48	44.43	60.58	60.20
Stocks[2]	5.49	6.10	13.91	6.76	5.73	6.70	11.97
Bonds	35.80	41.54	50.96	41.73	38.70	53.88	48.23
Nonfinancial corporations							
Stocks[2]	3.10	4.39	10.33	4.60	3.40	4.23	8.06
Initial public offerings	1.14	1.70	4.45	1.97	1.94	2.41	4.46
Seasoned offerings	1.96	2.69	5.88	2.63	1.46	1.82	3.60
Bonds	7.99	10.73	13.77	10.57	10.36	11.43	16.83
By rating, bonds sold in U.S.[3]							
Investment grade	4.41	6.45	6.31	5.65	5.25	5.07	9.34
Speculative grade	2.65	3.02	5.57	3.65	4.11	4.31	5.53
Public	2.01	1.95	3.26	1.81	2.25	1.77	2.10
Rule 144A	.63	1.07	2.31	1.84	1.86	2.55	3.43
Financial corporations							
Stocks[2]	2.39	1.71	3.59	2.16	2.34	2.48	3.91
Bonds	27.81	30.81	37.20	31.16	28.34	42.45	31.40

Note. Components may not sum to totals because of rounding.
1. These data include speculative-grade bonds issued privately under Rule 144A. All other private placements are excluded. 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.

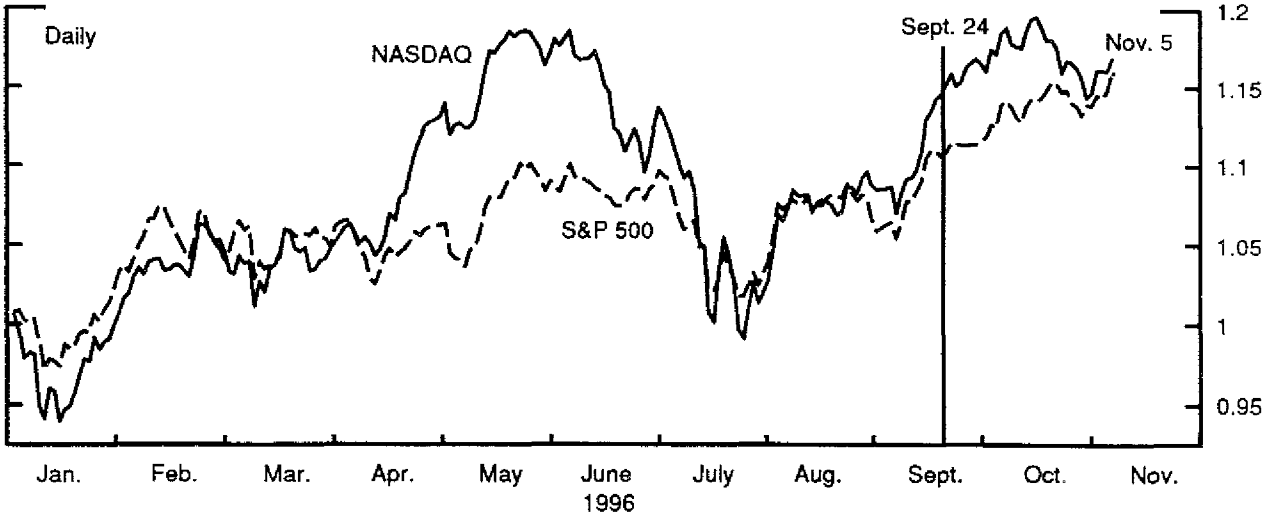
Commercial Paper Issued by Nonfinancial Firms
(Change in outstandings over period shown)



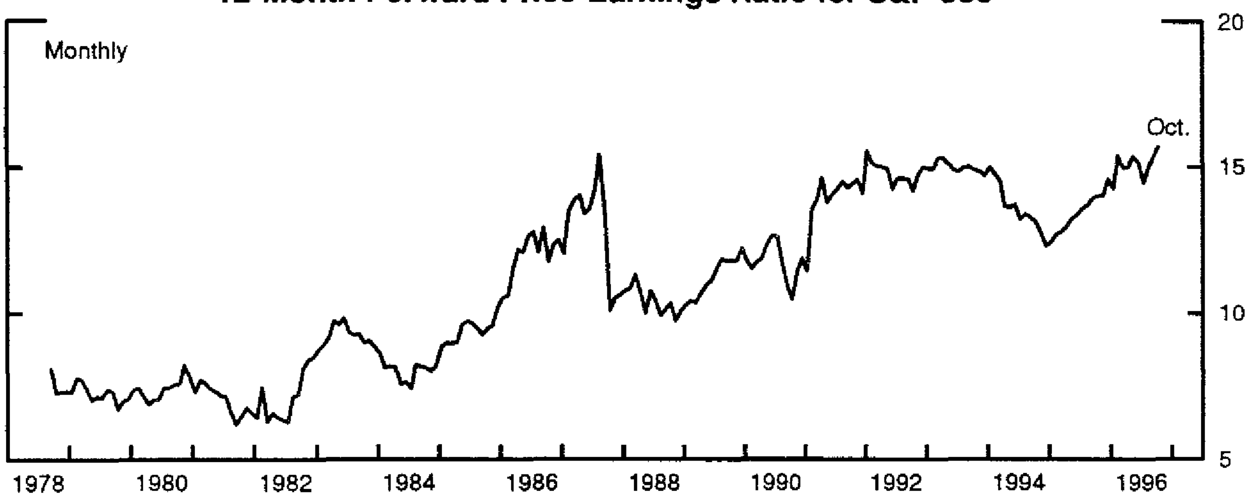
Average First-Day Price Change of IPOs



Selected Stock Indexes

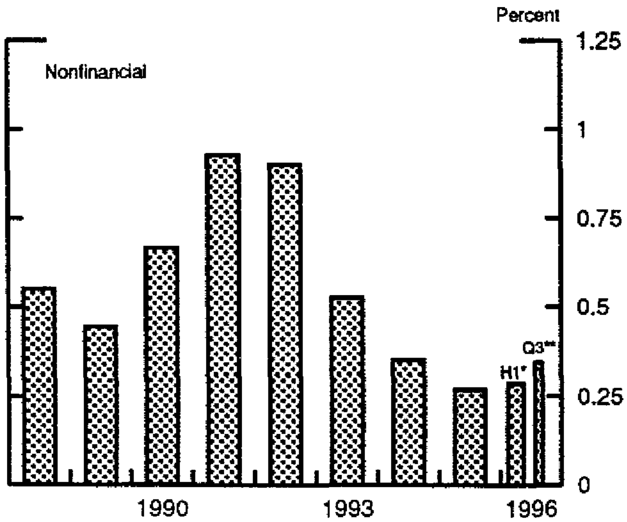


12-Month Forward Price-Earnings Ratio for S&P 500



Failed-Business Liabilities

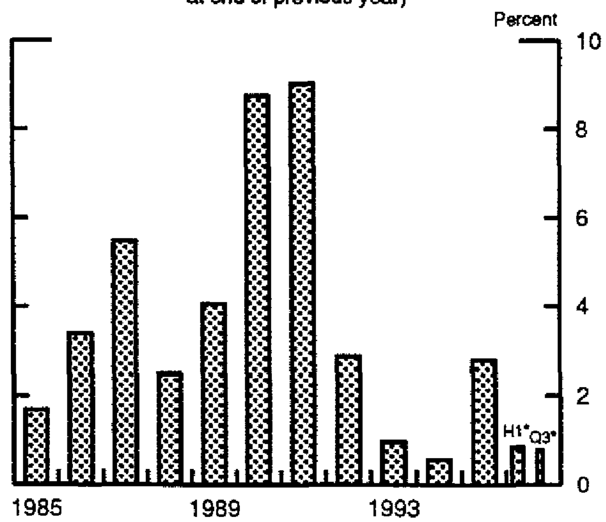
(As a percentage of total liabilities)



*At an annual rate.
**Based on data through August and at an annual rate.
Source. Dun & Bradstreet.

Default Rate on Junk Bonds

(Ratio of junk bond defaults to junk bonds outstanding at end of previous year)



*At an annual rate.
Source. Edward Altman, CS First Boston.

junk debt currently under review for possible upgrades exceeds that under review for possible downgrades by more than three-to-one. Finally, upgrades predominated among merger-related ratings changes in the third quarter, suggesting that Moody's continues to view recent mergers as value-enhancing rather than leading to credit quality problems.

Household Sector Finance

Total household borrowing appears to have slowed in the third quarter, reflecting a moderating pace in the growth of both mortgage and consumer credit. Preliminary indications are that total consumer credit contracted slightly in September, reducing third-quarter growth to a 5 percent annual rate. Growth in revolving credit slowed to just under a 10 percent rate during the quarter, while the nonrevolving forms of consumer credit were up only about 2 percent on balance.

Data available for the third quarter suggest that growth in mortgage borrowing slowed marginally from its first-half pace. Although growth in real estate loans at commercial banks slowed substantially in September, the increase for the third quarter as a whole, at a 3-1/4 percent rate, was about the same as in the second quarter. However, net issuance of federally related mortgage securities in the third quarter declined somewhat from its strong second-quarter pace, and direct portfolio holdings of Fannie Mae and Freddie Mac were unchanged.

In response to increased delinquency and charge-off rates on consumer loans this year, commercial banks generally tightened credit availability to consumers a notch during the third quarter. About half of the respondents to the Senior Loan Officer Opinion Survey in early November said that they had tightened approval standards for credit cards, and a fourth said they had done so for other types of consumer loans. A small net fraction of banks indicated that they were less willing to make consumer loans in November than they had been in August (chart). In contrast to the tighter stance toward consumer loans, banks on balance had eased standards for home equity loans and kept standards about unchanged for other home mortgage loans.

Although comprehensive data on delinquency and charge-off rates for the third quarter are not yet available, it appears that the delinquency experience on consumer loans may have begun to stabilize. In their third-quarter earnings commentaries, some banks

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

Type of credit	1994	1995	1996 Q1[r]	1996 Q2[r]	1996 Q3[pe]	1996 Aug.[r]	1996 Sep.[pe]	Memo: Outstanding Sep., 1996 (billions of dollars)[pe]
Total	14.5	14.2	12.0	7.6	5	5.2	-2-1/2	1,173
Auto	13.4	10.7	8.8	9.4	5-1/2	2.2	-3	372
Revolving	18.2	22.0	16.9	12.8	9-1/2	6.7	2-1/2	456
Other	11.8	9.1	9.5	-.6	-1-1/2	6.3	-9	345

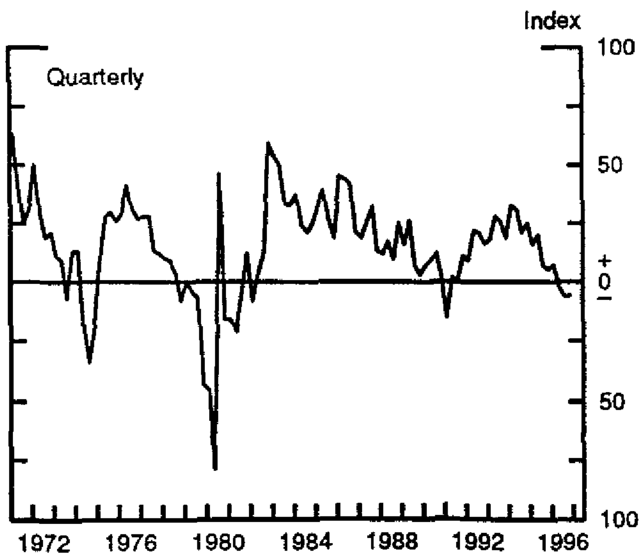
r Revised.
pe Preliminary estimate.

INTEREST RATES ON CONSUMER LOANS
(Annual percentage rate)

Type of loan	1994	1995	1995 Nov.	1996 Feb.	1996 May	1996 July	1996 Aug.	1996 Sep.
At commercial banks[1]								
New cars (48 mo.)[1]	8.1	9.6	9.4	9.1	8.9	n.a.	9.1	n.a.
Personal (24 mo.)[1]	13.2	13.9	13.8	13.6	13.5	n.a.	13.4	n.a.
Credit cards[2]	n.a.	16.0	15.8	15.8	15.4	n.a.	15.7	n.a.
At auto finance cos.[3]								
New cars	9.8	9.8	10.8	9.9	9.4	9.8	10.5	10.5
Used cars	13.5	13.5	14.0	13.3	13.3	13.8	13.9	13.9

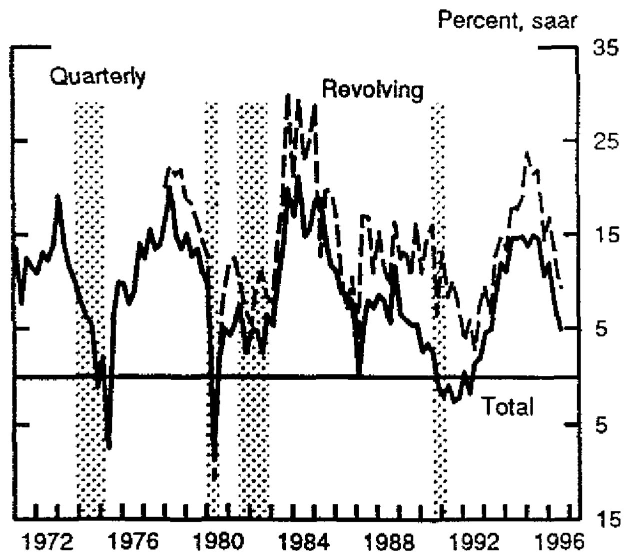
1. Average of "most common" rate charged for specified type and maturity during the first week of the middle month of each quarter.
2. Stated APR averaged across all credit card accounts at all reporting banks.
3. Average rate for all loans of each type made during period, of any maturity.
n.a. Not available.

Bank Willingness to Lend



Note. Weighted responses of banks more willing to make consumer loans minus those less willing.

Consumer Credit Growth Rate



reported that credit card losses had leveled off, and several large bank issuers of credit cards reported sizable earnings increases. MBNA, the second largest bank-card issuer, achieved a 33 percent year-over-year gain in net income; credit card specialists First USA, Capital One, and Advanta all had double-digit percentage increases in earnings. Each reported a charge-off rate that was higher than in the year-ago quarter but little changed from the previous quarter. The gains in earnings in the face of relatively high charge-offs were generally attributed to strong loan growth and, in some cases, to the repricing of receivables upon expiration of low introductory interest rates.

Treasury and Agency Financing

The staff anticipates that the Treasury will finance the projected $55 billion fourth-quarter fiscal deficit by borrowing about $39 billion from the public and by drawing down its cash balance by around $14 billion. About a quarter of the funds raised this quarter will be from weekly bill auctions. Although the size of these auctions has been increasing, the Treasury will also likely need to issue three cash management bills before year-end. One of these bills, for $13 billion, will be auctioned in conjunction with the midquarter refunding, which includes $18.5 billion of three-year notes, $10 billion of ten-year notes, and $10 billion of thirty-year bonds. The overall package will raise the average maturity of the debt slightly. Since the Treasury's announcement of its intention to shorten the average maturity of public debt in May 1993, the average has fallen from 73 months to about 62 months most recently.

On September 25, the Treasury provided details of the new indexed securities program. A ten-year note will be issued in January 1997, and other maturities will be added in quarterly auctions in April, July, and October. The Treasury will offer indexed securities through a uniform price auction. The structure of the securities is similar to that of the Canadian Real Return Bonds. That is, the value of the principal will be adjusted for inflation using the not-seasonally-adjusted consumer price index, and every six months the security will pay interest equal to a fixed percentage of the inflation-adjusted value of the principal. The bonds will be eligible for the STRIPS program as of the first issue date.

Issuance of debt by government-sponsored enterprises continued at a subdued rate in September, compared with the brisk pace earlier

TREASURY FINANCING
(Billions of dollars; total for period)

Item	1996 Q2	Q3	Q4[p]	Oct.[e]	Nov.[p]	Dec.[p]
Total surplus/deficit (-)	53.7	-33.3	-55.1	-34.0	-40.7	19.7
Means of financing deficit						
Net cash borrowing and repayments (-)	-23.5	39.4	38.5	12.5	40.6	-14.6
Nonmarketable	2.1	-1.0	3.7	3.7	0.0	0.0
Marketable	-25.6	40.3	34.8	8.8	40.6	-14.6
Bills	-38.3	-12.4	10.4	-1.7	36.5	-24.5
Coupons	12.7	52.7	24.3	10.4	4.0	9.9
Decrease in cash balance	-16.2	-6.2	14.4	18.6	5.0	-9.1
Other[1]	-14.0	0.1	2.2	2.9	-4.8	4.1
Memo:						
Cash balance, end of period	38.0	44.2	29.8	25.6	20.7	29.8

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

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

Agency	1996 Q2	Q3	July	Aug.	Sep.
FHLBs	10.0	5.7	1.9	2.7	1.1
FHLMC	19.1	3.6	3.2	2.2	-1.8
FNMA	1.6	10.8	2.1	1.9	6.8
Farm Credit Banks	2.8	-2.1	-1.9	-0.1	-0.1
SLMA	-1.0	0.2	1.3	0.4	-1.5

Note. Excludes mortgage pass-through securities issued by FNMA and FHLMC.

in the year. Spreads of GSE-issued securities over comparable Treasury securities remain stable, at about 15 basis points for five-year notes and around 25 basis points for ten-year notes.

Legislation was enacted on September 30 permitting the Student Loan Marketing Association (Sallie Mae) to reorganize, after shareholder approval, into a private, state-chartered holding company. Sallie Mae management must develop a privatization plan that would transfer existing financial assets to a GSE subsidiary of the new holding company; this GSE subsidiary must be dissolved no later than September 30, 2008. Loans made after the reorganization plan is in effect would become assets of a non-GSE subsidiary. The status of the current outstanding debt obligations of Sallie Mae would not be affected by the privatization.

Municipal Financing

Gross offerings of long-term municipal debt rose in October from the pace in September, reflecting a sharp pickup in new capital issuance from the seasonal lull in the third quarter; refunding volume fell slightly (table). Trade reports indicate that yields on long-term revenue bonds would need to fall about 50 basis points, to around 5-1/2 percent, before there would be a sizable increase in refunding volume from the low October level.

The ratio of yields on long-term tax-exempt bonds to comparable Treasuries edged up in October from the relatively low levels in August and September. The yield ratio may have been boosted

GROSS OFFERINGS OF MUNICIPAL SECURITIES
(Billions of dollars; monthly rates, not seasonally adjusted)

	1993	1994	1995	1996			
				Q2	Q3	Sept.	Oct.
Total tax-exempt	27.2	16.1	14.9	20.4	17.1	15.7	18.9
Long-term	23.3	12.8	12.1	15.6	11.9	11.6	15.7
Refundings[1]	15.7	4.0	3.6	4.5	3.9	3.8	3.0
New capital	7.6	8.8	8.5	11.1	8.0	7.8	12.7
Short-term	3.9	3.3	2.8	4.8	5.2	4.1	3.2
Total taxable	.7	.7	.7	.6	.6	.2	.5

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

slightly by the heavier issuance volume in October, but it remains fairly low because of diminished concerns that federal tax reform would adversely affect the tax-exempt status of municipal bonds.

Thus far, enactment of federal welfare reform has not hurt the credit ratings of states despite fears expressed by some analysts that the new law would impose a heavy fiscal burden on the states. In the view of Standard and Poor's, the transition period is long enough to provide time for most states to implement the changes outlined in the legislation without severely straining their fiscal situation. Nonetheless, states with large immigrant populations--notably New York, California, Texas, and Florida--may face serious strains because the new legislation will reduce federal support for legal immigrants.

APPENDIX

THE NOVEMBER SENIOR LOAN OFFICER OPINION SURVEY ON BANK LENDING PRACTICES

The November 1996 Senior Loan Officer Opinion Survey on Bank Lending Practices posed questions about bank lending standards and terms, loan demand by businesses and households, and credit-scoring models used in credit card lending operations.

The survey results show some continued easing of credit supply for businesses, but some pullback for households. Several banks reduced standards on business loans and many eased terms. However, a large number of banks raised standards for credit card lending, and many tightened standards for other consumer lending. Only a few banks tightened standards on home mortgage applications, while several eased standards on home equity loans. Terms on consumer loans were also firmed by many banks.

The survey found a moderation in demand for credit from both businesses and households. Banks reported little change in demand for commercial and industrial loans, although many experienced an increase in demand for commercial real estate loans. Several banks reported weaker demand from households, including demand for mortgages and for consumer loans.

Special questions on the survey examined banks' use of credit-scoring models for credit card lending. The responses suggest banks use these models to assist in many aspects of their lending process, from targeting solicitations to setting terms. The models are designed to predict a variety of events, including delinquencies, defaults, and expected profitability. However, the majority of respondents said their models had been too optimistic over the past year, predicting better outcomes than had actually been realized.

Lending to Businesses

The survey found a slight easing of lending standards for business loans (chart). As in August, about 5 percent of the domestic respondents eased standards over the past three months for loans to large firms. A similar fraction of foreign branches and agencies, which typically lend to large firms, eased standards. Around 10 percent of the domestic respondents eased standards for loans to middle-market firms and to small firms, larger fractions than in August. The fractions of banks that said they had eased terms are also larger than in August: Forty percent of the domestic respondents reported narrowing spreads over base rates and lowering costs of credit lines for large firms; about 30 percent reported narrowing spreads for smaller borrowers. Smaller fractions eased other terms, including size of credit lines, loan covenants, and collateralization requirements. About a third of the foreign respondents reported easing terms. Most of those banks that eased their standards or terms for business loans said they did so because of more aggressive competition from other banks and from nonbank lenders. Furthermore, between 20 percent and 40 percent of the respondents reported greater sensitivity to changes in terms at their banks of their loan demand from large, middle-market, and small firms, with the largest fraction reporting increased sensitivity for middle-market firms.

A special question asked banks why spreads of lending rates over base rates on smaller loans remained elevated relative to their levels in the late 1980s whereas spreads on larger loans were not so elevated. Banks offered a wide variety of explanations for the wider spreads, but by far the most popular was that the pricing of these loans has become more accurate and now reflects more fully the costs and risks associated with them. Many respondents also said that banks are now willing to lend to a riskier class of borrower than they were in the late 1980s. Several respondents said making small business loans is now more costly, in part because of increased regulation. Those that cited increased regulation pointed most commonly to Community Reinvestment Act requirements as the source of the higher costs.

Despite the rapid growth in commercial and industrial loans at all commercial banks registered in September and October, reporting banks said that demand for these loans was little changed over the past three months. On net, a couple of the respondents, less than 5 percent of the sample, reported increased demand from large and from small firms, and one bank, on net, reported decreased demand from middle-market firms. About one-fourth of the foreign respondents, however, reported stronger demand. In August, between 10 percent and 20 percent of the domestic respondents indicated they had experienced increased demand. Banks attributed changes in demand to variations in their customers' investment in plant and equipment, inventory financing needs, and, for larger customers, merger and acquisition financing needs.

Domestic and foreign respondents indicated little change in standards for construction and land development loans. About 15 percent of the domestic respondents and 30 percent of the foreign respondents experienced an increase in demand for these loans.

Lending to Households

The survey found slight evidence of tightened standards for home mortgage applications over the past three months, as about 5 percent of the banks, on net, indicated tighter standards (chart). Twelve percent of the banks reported weaker demand for these loans. The August survey also had found little evidence of a change in standards, but about twice as many banks indicated reduced demand.

The survey found continued evidence of more stringent consumer lending practices. More than half the banks tightened their standards for approving credit card applications, and a quarter tightened standards for other consumer loans, similar fractions to those found on the August survey. About 5 percent of the banks said they were less willing to make consumer installment loans than they were three months ago, the third consecutive survey showing a slight net fraction indicating a decline in willingness. Several banks also tightened terms on their credit cards over the past three months: About one-third of the respondents lowered credit limits, and about one-fifth raised spreads over market rates. Banks reported no change in the minimum fractions of outstanding balances required to be repaid. Banks also reported no change in terms on other consumer loans, including maximum maturities, spreads of loan rates over market rates, and minimum required down payments. Ten percent of the respondents reported weaker demand for consumer loans over the past three months.

The evidence of tighter standards and terms as well as the weaker demand for consumer loans found by the survey is consistent with the pronounced slowdown in the growth of consumer credit that occurred in the second half of this year. At the same time, nearly 20 percent of the respondents said they had eased standards for home equity, an area of household credit that has grown significantly in recent months.

Credit-Scoring Models and Credit Card Lending

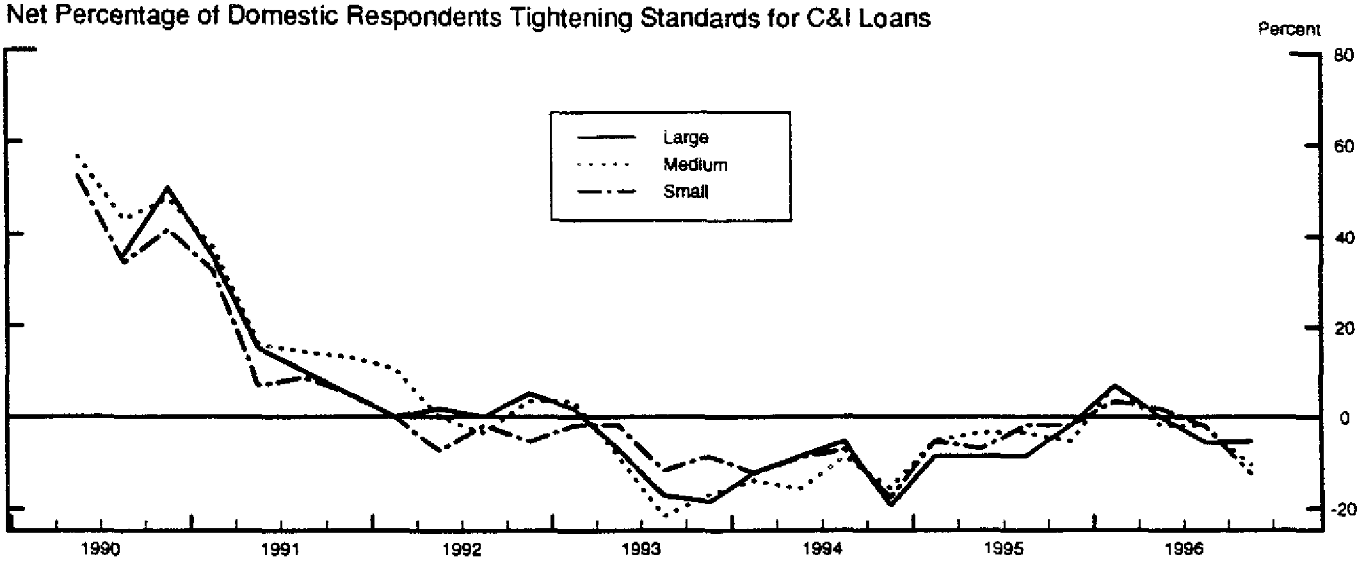
A series of special questions asked about banks' use of credit-scoring models in their credit card lending operations.

Banks most commonly use the models to select candidates for credit card solicitations and to approve applications, with fewer banks using the models to set or adjust terms on accounts. More than half the respondents said they have not tightened terms on existing accounts that are current on payments because of a worsened credit score. Nearly half, however, said they have lowered credit limits on such accounts, although not below existing balances, and about one-fourth had raised interest rates. Only a few banks had lowered credit limits below existing balances, forcing repayments, on an account in good standing with a worsened credit score.

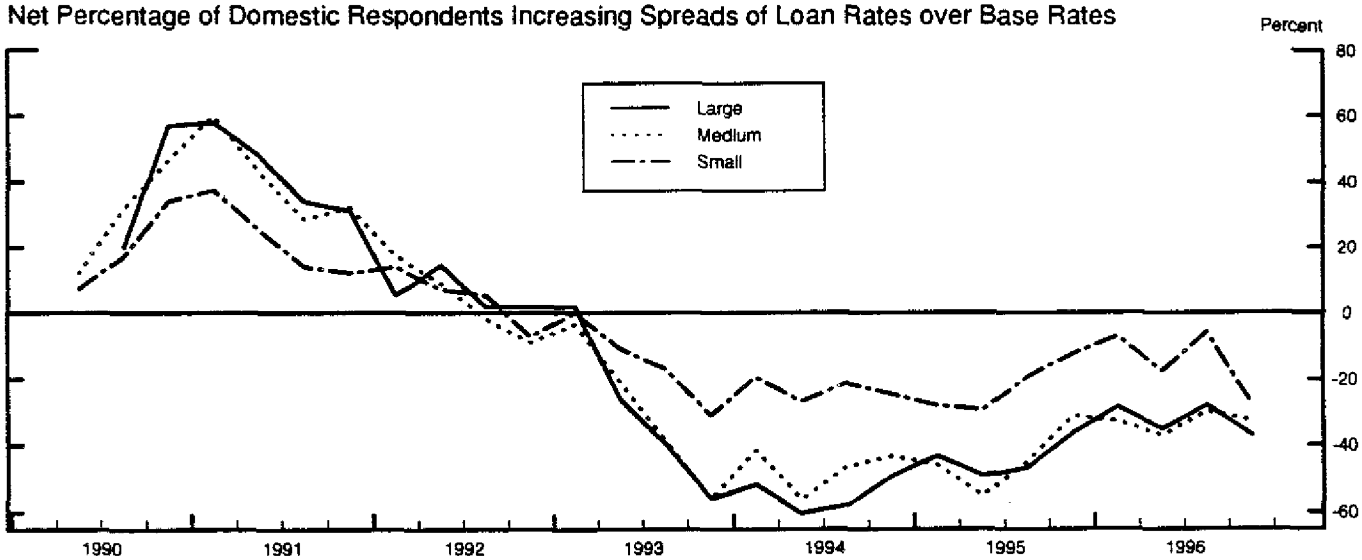
The models are designed to predict a variety of events: Most of the models predict delinquencies or defaults, although some models predict bankruptcy or expected profitability. Nearly two-thirds of the respondents indicated that their models had been too optimistic over the past year, predicting better outcomes than actually occurred. Many respondents attributed these failures to the short time period over which the models were estimated and to an increase in consumers' willingness to declare bankruptcy. In response to the recent poor performance of their models, banks most commonly raised cutoff scores necessary to qualify for credit and placed more weight on other sources of information. About half the banks experiencing poor predictions reestimated or redefined their models. Finally, over the past three months nearly 60 percent of the banks that use credit-scoring models to approve credit card applications tightened the score necessary to qualify.

Measures of Supply and Demand for C&I Loans, by Size of Firm Seeking Loans

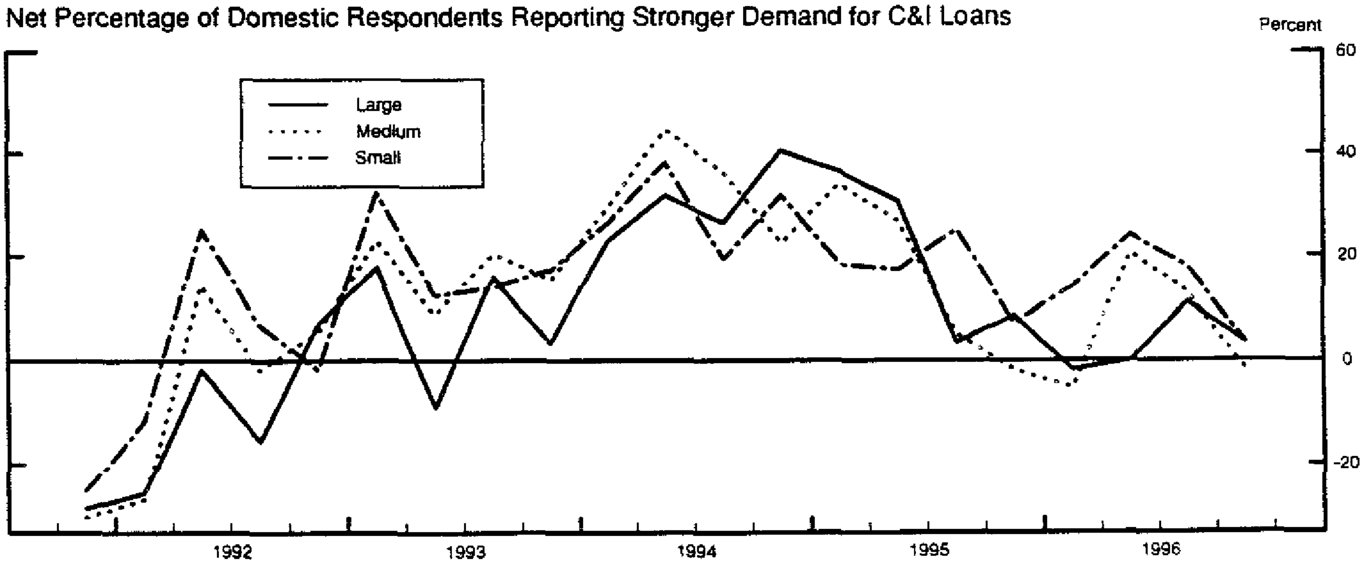
Net Percentage of Domestic Respondents Tightening Standards for C&I Loans



Net Percentage of Domestic Respondents Increasing Spreads of Loan Rates over Base Rates

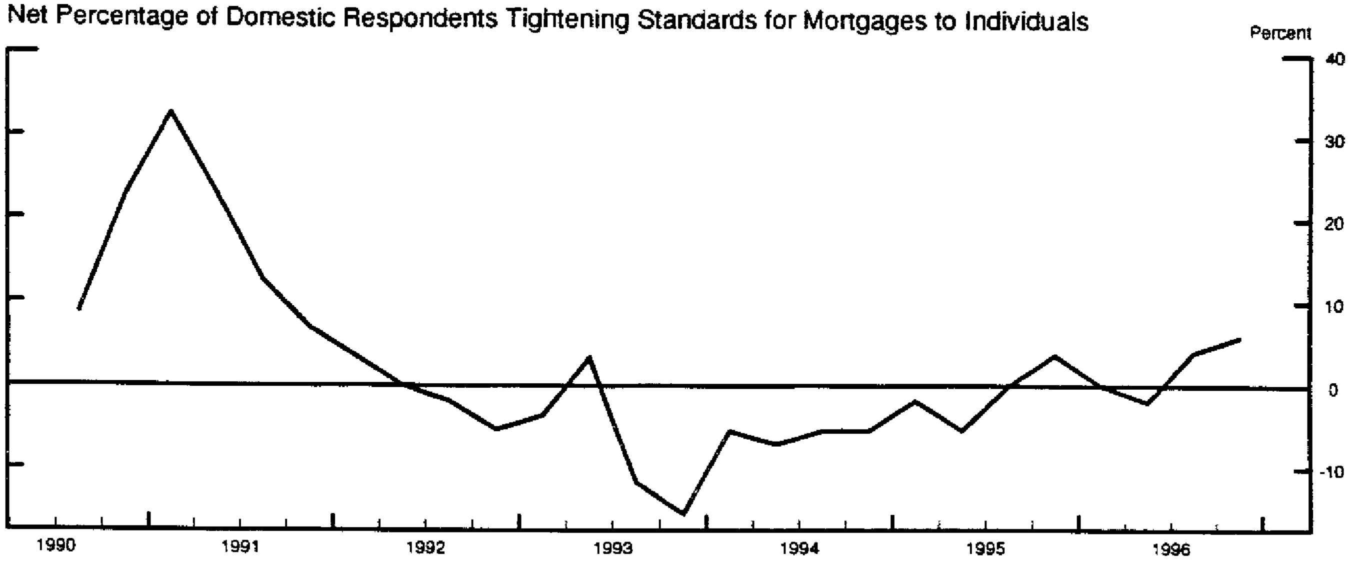


Net Percentage of Domestic Respondents Reporting Stronger Demand for C&I Loans

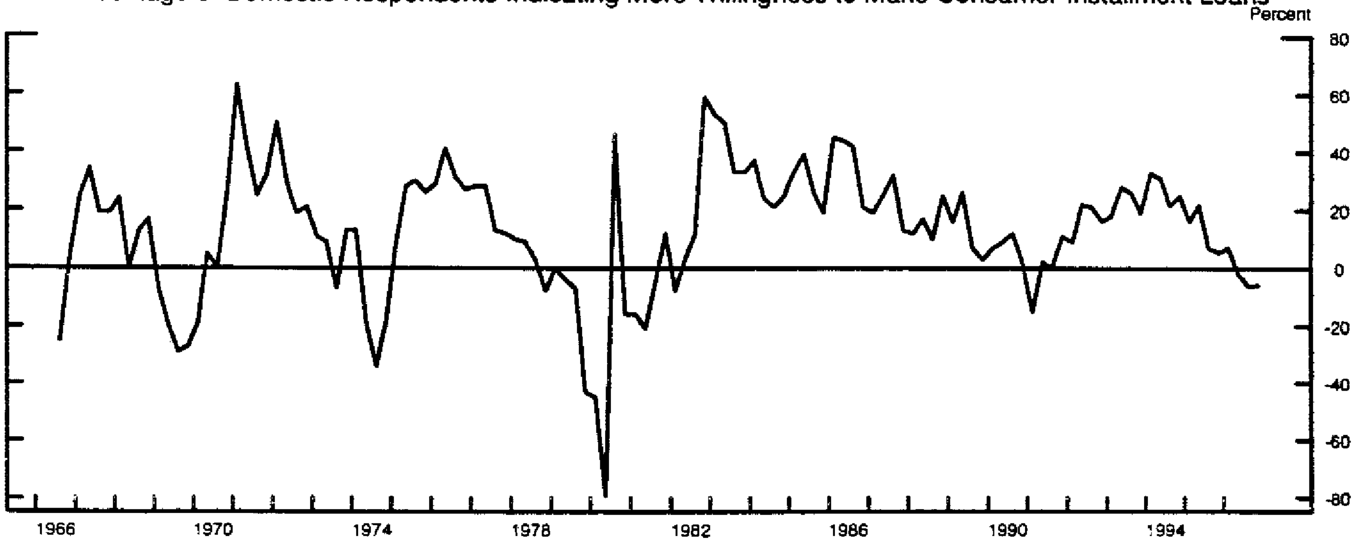


Measures of Supply and Demand for Loans to Households

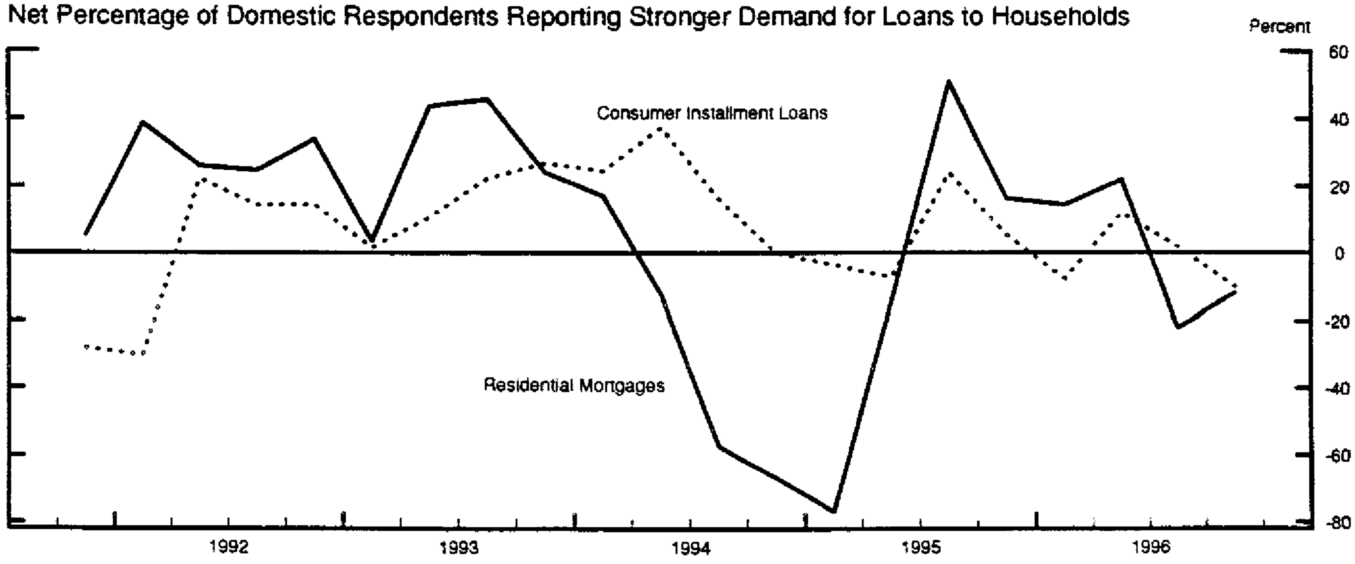
Net Percentage of Domestic Respondents Tightening Standards for Mortgages to Individuals



Net Percentage of Domestic Respondents Indicating More Willingness to Make Consumer Installment Loans



Net Percentage of Domestic Respondents Reporting Stronger Demand for Loans to Households



INTERNATIONAL DEVELOPMENTS

U.S. International Trade in Goods and Services

In August, the deficit in U.S. international trade in goods and services was somewhat less than in July, as exports rose twice as fast as imports. For July-August combined, however, the deficit (at an annual rate) was significantly larger than the second-quarter level.

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

	1995	Annual rates 1996 Q1	Q2	Q3e/	Monthly rates 1996 Jun	Jul	Aug
Real NIPA 1/							
Net exports of G&S	-107.6	-104.0	-114.7	-132.2	...	...	...
Nominal BOP							
Net exports of G&S	-105.1	-96.9	-112.2	-134.6	-8.2	-11.6	-10.8
Goods, net	-173.4	-170.9	-188.0	-206.9	-14.6	-17.5	-17.0
Services, net	68.4	74.0	75.8	72.3	6.4	5.9	6.2

1. In billions of chained (1992) dollars.
e. BOP data are two months at an annual rate.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

For July-August combined, exports were 2 percent less than in the second quarter. Three-fourths of the drop was in nonmonetary gold and aircraft. Exports of machinery and automotive products in July-August were at about the same levels as recorded in the second quarter. For July-August combined, imports were only marginally higher than in the second quarter. Increases in imported industrial supplies, consumer goods, and automotive products were offset by a drop in imports of semiconductors and nonmonetary gold.

Oil Imports

The quantity of oil imported during July and August averaged about the same rate as observed during May and June, but was slightly above the 1996Q2 pace. Seasonally strong consumption helped maintain imports at a high rate. Preliminary Department of Energy statistics indicate that oil imports declined significantly in September from their July-August pace. Weaker oil consumption and significant deliveries of oil from the Strategic Petroleum Reserve contributed to the decline in oil imports.

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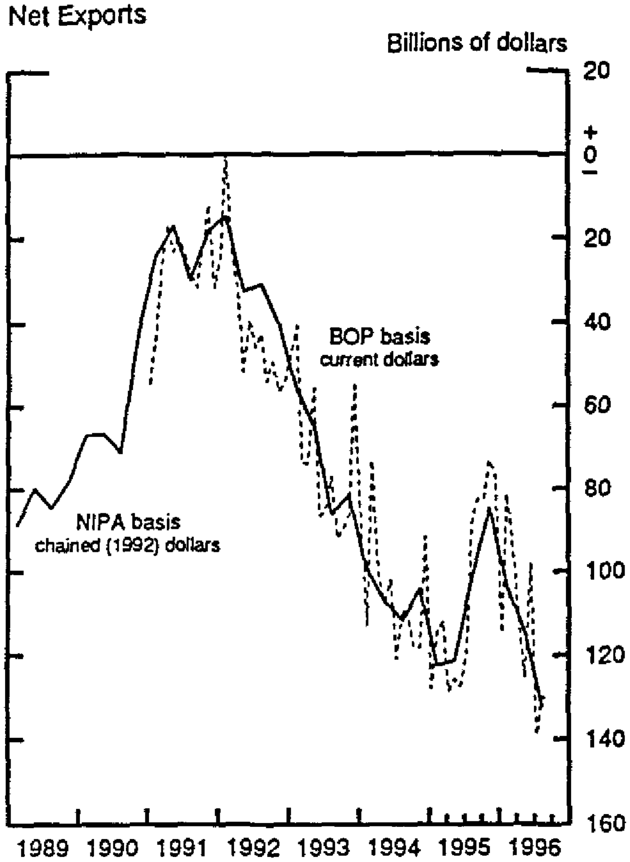
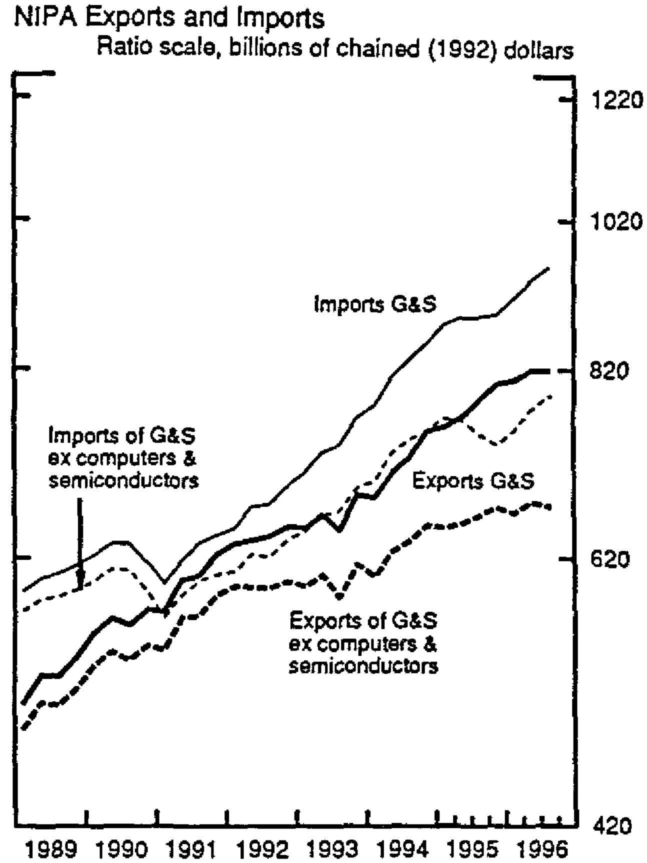
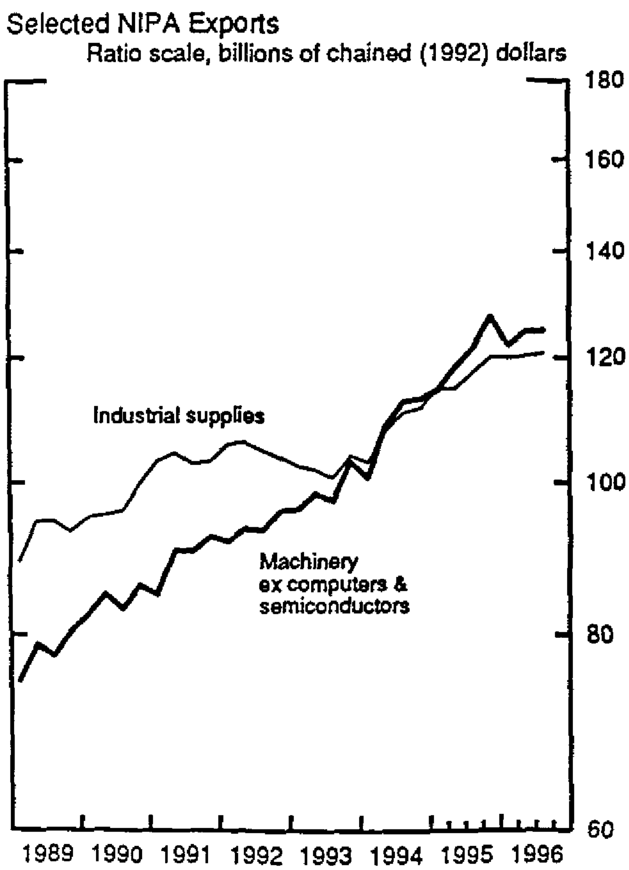
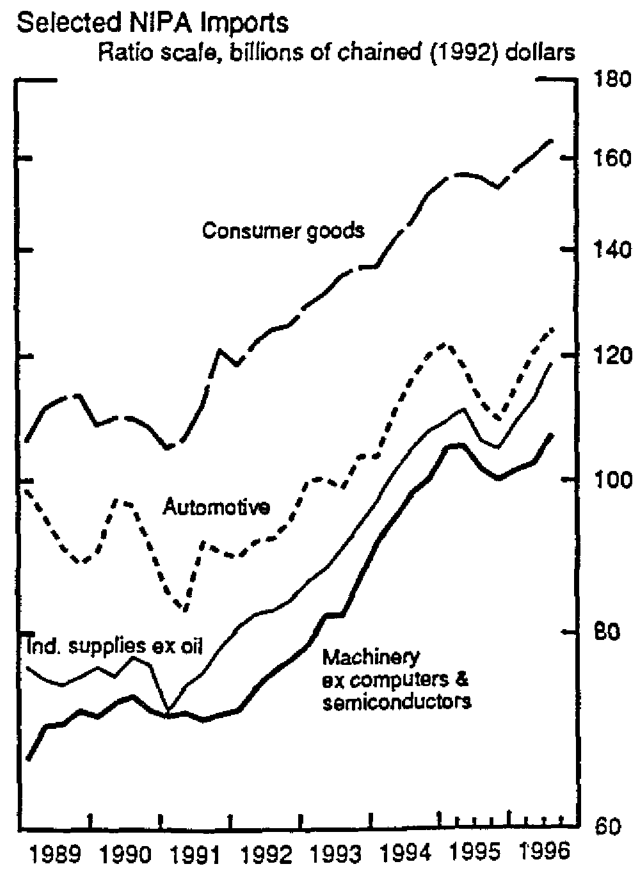
U.S. International Trade in Goods and Services

(Seasonally adjusted annual rate)









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

	Levels				Amount Change 1/			
	1996		1996		1996		1996	
	Q2	Q3e/	Jul	Aug	Q2	Q3e/	Jul	Aug
Exports of G&S	836.4	819.7	807.7	831.8	15.8	-16.7	-29.1	24.1
Goods exports	612.4	596.6	585.3	607.9	12.3	-15.7	-26.3	22.6
Agricultural	60.2	60.9	60.0	61.9	-3.0	0.7	1.3	1.9
Gold	12.5	5.6	4.7	6.5	6.2	-6.9	-5.7	1.8
Other goods	539.7	530.1	520.6	539.6	2.3	-9.5	-21.9	18.9
Aircraft & pts	33.4	28.2	23.9	32.4	6.9	-5.2	-8.4	8.5
Computers	43.2	43.0	41.9	44.0	-2.2	-0.3	-0.2	2.1
Semiconductors	34.9	33.4	33.0	33.8	-2.6	-1.5	-1.6	0.8
Other cap gds	140.2	141.2	140.6	141.8	1.7	1.0	0.7	1.1
Automotive	63.0	63.4	62.2	64.6	1.0	0.4	-4.1	2.4
to Canada	34.6	34.6	34.3	35.0	1.5	0.0	-2.2	0.7
to Mexico	7.9	7.1	6.9	7.3	0.3	-0.8	-1.5	0.4
to ROW	20.5	21.7	21.1	22.4	-0.7	1.2	-0.4	1.3
Ind supplies	129.3	127.1	124.9	129.3	0.4	-2.2	-5.8	4.4
Consumer goods	70.5	68.1	66.5	69.6	2.6	-2.4	-4.8	3.1
All other	25.2	25.8	27.6	24.0	1.3	0.6	-5.0	-3.5
Services exports	224.0	223.1	222.3	223.8	3.5	-0.9	-2.8	1.5
Imports of G&S	948.6	954.3	946.8	961.8	31.1	5.7	11.8	14.9
Goods imports	800.4	803.5	795.3	811.8	29.3	3.1	8.1	16.5
Petroleum	70.1	69.6	72.2	66.9	14.1	-0.5	4.7	-5.3
Gold	14.6	7.5	5.4	9.6	7.8	-7.1	-4.4	4.2
Other goods	715.7	726.4	717.6	735.2	1.8	10.7	7.9	17.6
Aircraft & pts	12.7	13.1	12.5	13.7	1.7	0.4	-2.0	1.1
Computers	60.5	61.5	61.4	61.6	-1.7	1.1	3.9	0.2
Semiconductors	37.0	33.1	32.9	33.4	-6.7	-3.9	-1.6	0.6
Other cap gds	115.5	116.9	116.7	117.1	-1.2	1.4	-0.0	0.3
Automotive	131.1	136.4	133.6	139.2	6.1	5.3	4.2	5.5
from Canada	49.2	51.7	49.6	53.8	3.5	2.5	0.5	4.2
from Mexico	24.1	22.9	21.3	24.5	1.3	-1.2	-2.7	3.2
from ROW	57.8	61.8	62.7	60.9	1.3	4.0	6.4	-1.8
Ind supplies	126.9	130.8	129.0	132.6	2.7	3.9	2.8	3.5
Consumer goods	166.3	170.1	166.9	173.2	3.0	3.7	0.7	6.4
Foods	35.9	35.8	35.2	36.5	1.7	-0.1	0.0	1.2
All other	29.7	28.6	29.3	28.0	1.7	-1.0	-0.1	-1.2
Services imports	148.2	150.8	151.6	150.0	1.7	2.6	3.6	-1.6
Memo:								
Oil qty (mb/d)	9.83	9.97	10.48	9.46	1.08	0.15	0.56	-1.02
Oil price ($/bbl)	19.53	19.11	18.85	19.37	1.97	-0.42	0.23	0.52

1. Change from previous quarter or month. e. Average of two months.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

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

	Annual rates 1996			Monthly rates 1996		
	Q1	Q2	Q3	Jul	Aug	Sep
	----------BLS prices (1990=100)----------					
Merchandise imports	2.4	1.5	-2.7	-0.1	0.1	0.8
Oil	47.4	41.0	-1.4	2.0	2.1	5.0
Non-oil	-1.2	-2.3	-3.0	-0.4	-0.1	0.3
Foods, feeds, bev.	-4.5	11.6	-10.7	-1.4	-0.8	1.9
Ind supp ex oil	-3.1	-5.0	-5.0	-0.9	0.0	0.6
Computers	-8.1	-16.7	-10.4	-0.3	-0.7	-1.2
Capital goods ex comp	-0.4	-4.4	-2.7	-0.2	-0.4	0.1
Automotive products	-0.8	-0.3	0.5	0.2	0.0	0.3
Consumer goods	1.2	-0.9	-0.9	-0.1	0.0	0.2
Merchandise exports	1.0	2.6	-3.7	-0.5	-0.2	-0.8
Agricultural	13.8	31.4	-18.1	-1.9	-0.2	-7.3
Nonagricultural	-0.9	-1.2	-1.0	-0.2	-0.2	0.1
Ind supp ex ag	-3.6	-4.8	-3.2	-0.6	-0.5	0.6
Computers	-9.2	-7.5	-11.8	-1.7	-0.9	-1.3
Capital goods ex comp	2.3	1.7	0.2	-0.2	0.0	0.0
Automotive products	-0.1	0.2	0.4	-0.1	0.2	0.0
Consumer goods	2.3	1.5	0.1	0.0	0.0	0.2
	---Prices in the NIPA accounts (1992=100)--					
Fixed-weight						
Imports of gds & serv.	0.0	0.7	-2.0	...	...	...
Non-oil merchandise	-3.1	-3.8	-3.1	...	...	...
Exports of gds & serv.	0.3	1.4	-1.7	...	...	...
Nonag merchandise	-2.2	-2.6	-1.5	...	...	...

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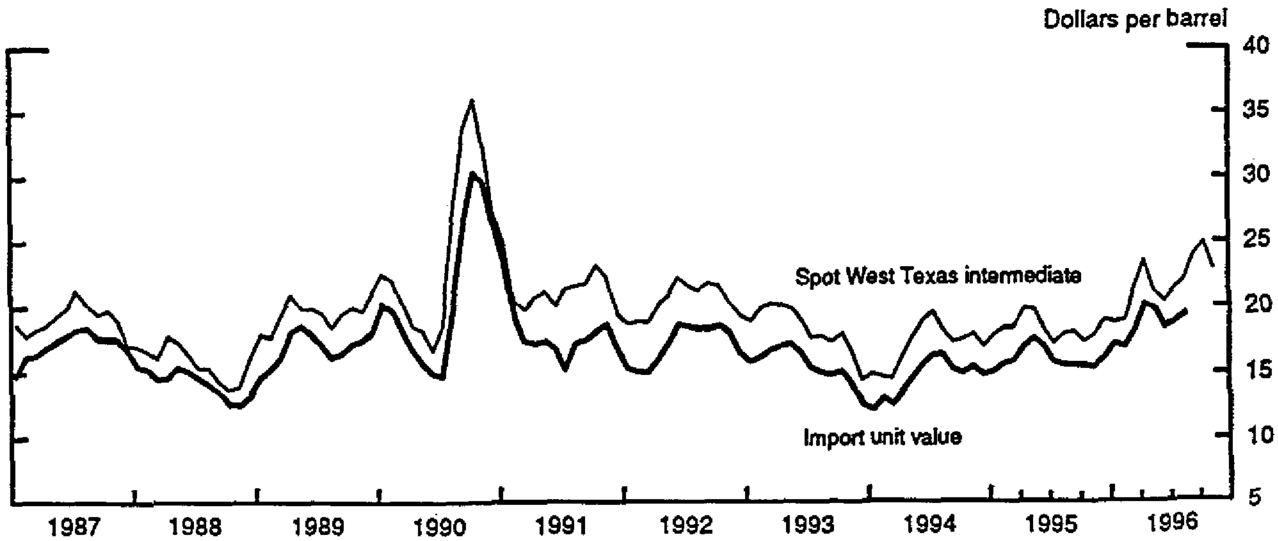
Oil Prices



Oil Prices

The price of imported oil increased by roughly 2 percent in July and again in August and then jumped up 5 percent in September. These increases follow substantial price declines during May and June. The price of imported oil now stands 24 percent above its September 1995 level. Spot WTI rose more than $2 per barrel in September, averaging $23.99 per barrel, and rose another $0.90 per barrel in October. Fighting in the Kurdish region of Northern Iraq and concern over the level of heating oil stocks in the United States and Europe helped push prices up. The announcement of a settlement of the dispute among the Kurds has resulted in a decline of nearly $2 per barrel during the last few days. Spot WTI is still quite volatile and is trading in the $22-24 per barrel range.

Prices of Non-oil Imports and Exports

Prices of non-oil imports decreased during the third quarter, at a somewhat faster pace than in recent quarters. Prices of imported capital goods and industrial supplies continued to fall sharply. Prices of imported foods also fell in the third quarter, nearly reversing a substantial increase in the second quarter.

Prices of exports also fell in the third quarter, with the bulk of the decline due to rapidly falling agricultural prices (especially grains). On balance, prices of non-agricultural exports fell, with continued declines seen in prices of computers and industrial supplies.

U.S. International Financial Transactions

Private foreign purchases of U.S. Treasury securities slowed markedly in August from the extraordinary pace in July. (See line 4.a of the Summary of U.S. International Transactions table.) Most of this slowing is attributable to offshore financial centers, which recorded small net sales in August following net purchases of more than $25 billion in July. Outside of these financial centers, there was a slowing in treasury purchases from the United Kingdom and a pickup from Japan. Private foreign purchases of other securities picked up only modestly in August, leaving total foreign net purchases of U.S. securities about $26 billion smaller in August than in July.

The smaller capital inflow through securities purchases in August was largely offset by smaller outflows through banking transactions (line 3). Bank outflows in July were swollen by RP lending made to finance the huge foreign purchases of treasuries. In August, there was little RP lending and bank outflows declined.

Foreign official reserves in the United States increased $4-1/2 billion in August, only slightly faster than in July (line 1). However, partial data from FRBNY indicate foreign official reserves in the United States rose by almost $20 billion in September. Large increases were reported by Spain, developing countries in Asia, Japan, and Saudi Arabia.

U.S reserve assets declined almost $8 billion in August (line 4), largely reflecting Mexico's medium-term swap repayments to the U.S. Treasury.

U.S. net purchases of foreign securities slowed slightly in August (line 5), as smaller net purchases of foreign equities were only partly offset by larger net purchases of foreign bonds.

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

	1994	1995	1995 Q3	1995 Q4	1996 Q1	1996 Q2	1996 Jul	1996 Aug
Official capital								
1. **Change in foreign official reserve assets in U.S. (increase, +)**	38.0	109.9	39.8	10.6	52.2	13.3	3.1	4.5
a. G-10 countries	28.9	33.1	5.6	-3.9	28.5	3.5	-2.6	3.6
b. OPEC countries	-3.3	4.3	6.2	-2.1	-.8	5.3	.6	.7
c. All other countries	12.4	72.5	27.7	16.7	24.5	4.5	5.1	.2
2. **Change in U.S. official reserve assets (decrease, +)**	5.3	-9.7	-1.9	.2	*	-.5	-.2	7.8
Private capital								
Banks								
3. **Change in net foreign positions of banking offices in the U.S.**[1]	102.8	-33.1	-8.4	10.7	-25.9	-11.4	-30.6	-12.8
Securities[2]								
4. **Foreign net purchases of U.S. securities (+)**	92.9	190.7	69.8	23.5	48.6	61.0	46.3	20.8
a. Treasury securities[3]	34.7	99.9	37.4	1.8	12.0	31.3	38.2	7.0
b. Corporate and other bonds[4]	53.9	82.6	27.0	17.7	32.8	23.4	9.5	10.6
c. Corporate stocks	4.3	8.2	5.3	4.0	3.8	6.3	-1.4	3.2
5. **U.S. net purchases (-) of foreign securities**	-57.3	-98.8	-35.7	-32.5	-34.5	-20.0	-7.0	-6.3
a. Bonds	-9.2	-48.5	-13.6	-18.7	-12.0	-2.6	-3.4	-5.2
b. Stocks	-48.1	-50.3	-22.1	-13.8	-22.5	-17.5	-3.6	-1.1
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-54.5	-95.5	-18.0	-44.1	-23.2	-23.0	n.a	n.a
7. Foreign direct investment in U.S.	49.8	60.2	25.0	14.8	28.7	10.7	n.a	n.a
8. Other (inflow, +)[5]	-14.9	-7.0	8.6	17.8	-15.1	1.1	n.a	n.a
U.S. current account balance (s.a.)	-148.4	-148.2	-37.7	-30.4	-34.9	-38.8	n.a	n.a
Statistical discrepancy (s.a.)	-13.7	31.5	-41.5	29.4	4.1	7.6	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)

	1994 Dec.	1995 Dec.	1996 Mar.	Jun.	Jul.	Aug.	Sep.	Oct.**
1. Net claims of U.S. banking offices (excluding IBFs) on own foreign offices and IBFs	-224.0	-260.0	-260.1	-245.0	-245.8	-240.4	-246.3	-240.8
a. U.S.-chartered banks	-70.1	-86.1	-84.1	-77.2	-72.3	-70.7	-72.5	-70.1
b. Foreign-chartered banks	-153.9	-173.9	-176.0	-167.8	-173.5	-169.7	-173.8	-17[illegible].7
2. Credit extended to U.S. nonbank residents								
a. By foreign branches of U.S. banks	23.1	26.5	27.3	28.8	28.9	28.6	29.2	30.3
b. By Caribbean offices of foreign-chartered banks	78.4	86.3	90.0	85.4	n.a	n.a	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	85.6	91.2	95.7	101.0	100.1	101.1	101.4	106.1
b. At the Caribbean offices of foreign-chartered banks	86.0	92.3	96.6	97.7	n.a	n.a	n.a.	n.a.
MEMO: Data as recorded in the U.S. international transactions accounts								
4. Credit extended to U.S. nonbank residents	172.6	207.3	212.7	n.a	n.a	n.a.	n.a.	n.a.
5. Eurodeposits of U.S. nonbank residents	243.8	276.9	290.0	n.a	n.a	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 FR2951.
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. They include some foreign-currency denominated deposits and loans. Source: SCB
**Data for October are thru October 21.

Foreign Exchange and Foreign Financial Markets

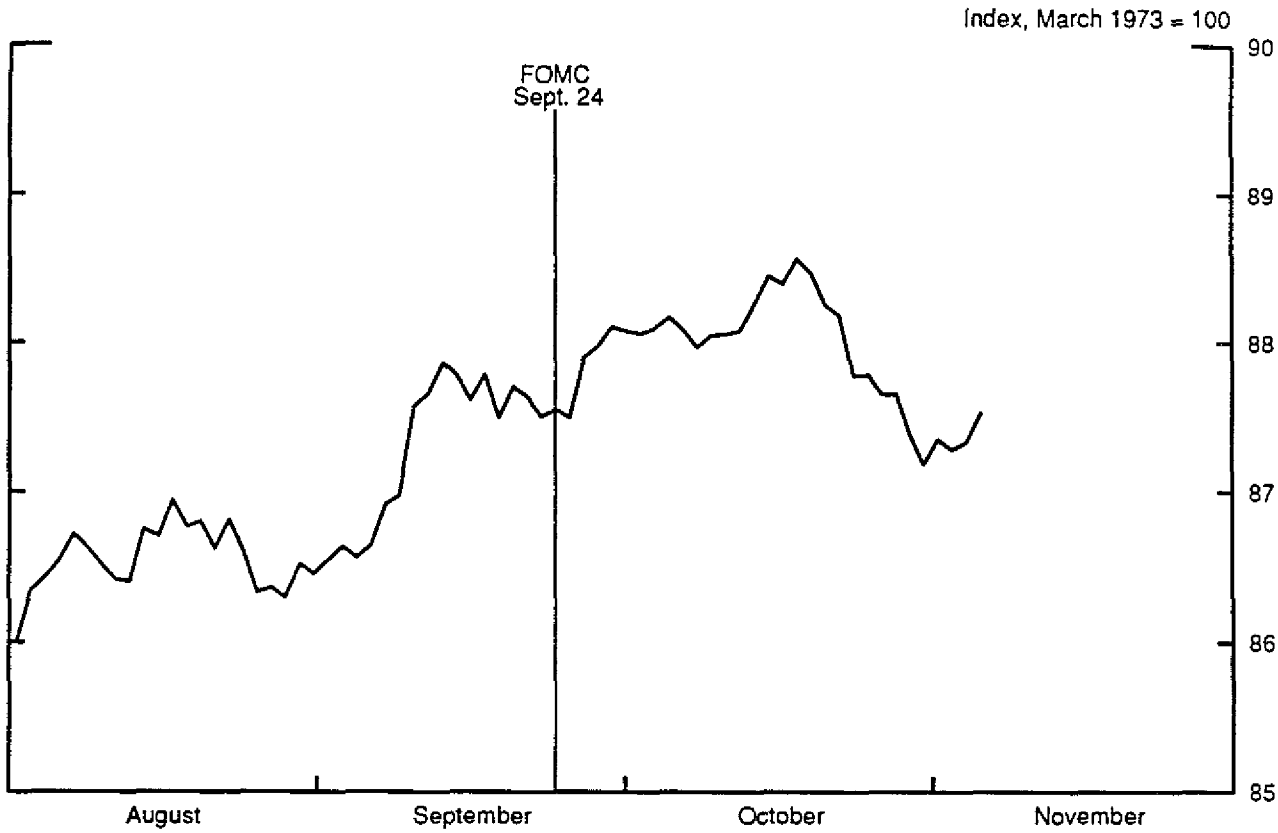
The weighted-average value of the dollar against the currencies of the major industrial countries has changed little on balance since the September FOMC meeting. Over this period, U.S. long-term interest rates have fallen 50 basis points in the absence of any move by the Federal Reserve to raise interest rates and on weaker than expected incoming data on U.S. economic activity. Foreign long-term rates have come down about 40 basis points on average since mid-September.

The dollar's movements against individual currencies have been unusually diverse. The dollar has been strongest against the yen, appreciating nearly 4 percent since the September FOMC meeting. The yen has weakened as market participants have appeared to scale back their expectations as to the size of a supplemental fiscal stimulus package this year. First, the fiscally conservative Liberal Democratic Party emerged from the October 20 general election with a near majority, and then had difficulty finding coalition partners, raising questions about its ability to take any fiscal action. In addition, recent indicators on Japanese economic activity have on balance seemed relatively weak, generating renewed uncertainty as to the strength of the recovery and appearing to push off further into the future any move by the Bank of Japan toward tighter monetary policy.

The dollar has been weakest over the intermeeting period relative to the pound, depreciating 5 percent. The pound strengthened in early October, aided by what market commentary judged a successful Conservative Party conference, appreciated further on stronger than expected activity data, and was given an added boost on October 30 by the surprise decision to raise the Bank of England's minimum lending rate by 25 basis points to 6 percent.

The dollar has depreciated 2-1/2 percent against the Canadian dollar. The Canadian currency's continued strength has been aided by low inflation data and a favorable report on the Canadian fiscal situation by Finance Minister Martin, including a forecast of a small federal budget surplus in the fiscal year after next. The Bank of Canada responded to the strength of the Canadian dollar in

Weighted Average Exchange Value of the Dollar
(Daily data)



Interest Rates in Major Industrial Countries

	Three-month rates			Ten-year bond yields		
	Sept. 24	Nov. 6	Change	Sept. 24	Nov. 6	Change
Germany	3.00	3.08	0.08	6.18	5.92	-0.26
Japan	0.53	0.51	-0.02	2.85	2.54	-0.31
United Kingdom	5.78	6.22	0.44	7.81	7.66	-0.15
Canada	4.12	3.09	-1.03	7.33	6.16	-1.17
France	3.50	3.33	-0.17	6.21	5.87	-0.34
Italy	8.38	7.56	-0.82	8.81	7.66	-1.15
Belgium	3.02	3.02	0.00	6.35	6.05	-0.30
Netherlands	2.72	2.90	0.18	6.02	5.79	-0.23
Switzerland	1.56	2.00	0.44	3.86	3.78	-0.08
Sweden	4.75	4.53	-0.22	7.62	7.24	-0.38
Weighted-average foreign	3.63	3.53	-0.10	6.23	5.80	-0.43
United States	5.57	5.37[p]	-0.20	6.77	6.28[p]	-0.49

Note. Change is in percentage points. [p] Preliminary.

the context of continued low inflation and moderate growth by lowering its band for the overnight rate three times by a total of 75 basis points to a range of 3 percent to 3-1/2 percent.

The dollar has appreciated slightly on balance against the mark since mid-September. The dollar-mark rate has remained firm in the face of statements by Bundesbank officials appearing to suggest that the outlook for German growth is relatively favorable and that further Bundesbank easing is not to be expected. The currencies of most other EC countries have strengthened slightly against the mark recently, despite statements by German officials warning that European Monetary Union should not proceed unless proposed members strictly adhere to prescribed economic criteria. On October 12, it was announced that the Finnish markka was joining the EUs Exchange Rate Mechanism. Italian Prime Minister Prodi indicated that he hopes to have the lira join the ERM by the end of the year.

Since the September FOMC meeting, short-term interest rates in major foreign industrial countries have generally moved lower, registering a weighted-average decline of 10 basis points. While short-term interest rates in Japan and Germany have remained little changed, several European countries have reduced money market intervention rates and/or official lending rates. Within the EU, the Bank of Italy cut its discount rate 75 basis points, the Swedish Riksbank lowered its repo rate four times by a total of 55 basis points, the Spanish central bank lowered its intervention rate by 50 basis points, and the Bank of France reduced its intervention rate by 5 basis points. The Swiss National Bank lowered its discount rate 50 basis points to 1.00 percent, citing what it considered the excessive strength of the Swiss franc as an important factor motivating the reduction.

Long-term interest rates have moved lower in all of the foreign G-10 countries since mid-September. The largest declines abroad have been in Canada and Italy (both about 115 basis points), while long-term rates have eased 25 basis points in Germany and 30 basis points in Japan.

The Mexican peso has depreciated 5 percent since mid-September, moving from about the 7-1/2 pesos per dollar level to just under 8 pesos per dollar. There does not appear to have been any one factor behind the peso's decline. The peso may have been depressed by the decision to sell only a minority share in the state oil company's petrochemical business, possibly calling into question the government's commitment to privatization, and the ongoing political difficulties of the ruling PRI party.

. The Desk did not intervene for U.S. monetary authorities during the period.

Developments in Foreign Industrial Countries

Recent indicators from the major foreign industrial countries suggest moderate expansion of economic activity in the third quarter. In Japan, industrial production grew strongly after declining slightly in the second quarter. German industrial production and manufacturing orders rose on balance albeit at a slower pace than the rapid growth recorded in the second quarter. U.K. real GDP grew 3 percent (SAAR) as retail sales continued at a brisk pace. French consumption of manufactured products advanced strongly in the third quarter, primarily owing to a temporary surge in car sales. In Canada, recent indicators have been mixed, but on balance point to a pickup in the pace of economic activity.

High unemployment rates persist, especially in France, Italy, Germany, and Canada, contributing to subdued wage and price pressures abroad. Recent 12-month rates of consumer-price inflation have been near zero in Japan and have averaged about 1-1/2 percent in Germany, France, and Canada. Italian consumer-price inflation continued on its steep downward trend, falling to 3 percent in October (from double that rate about a year ago). Underlying year-over-year inflation ticked up in the United Kingdom to a bit below 3 percent in September.

The recent rise in U.K. inflation pressures prompted the government to raise official interest rate by 25 basis points on October 30. In contrast, in both Canada and Italy moderating inflation as well as continued concerns about the pace of economic activity prompted monetary authorities to lower official interest rates by 75 basis points since the September FOMC meeting.

The Italian government recently released its 1997 budget aimed at reducing its budget deficit to 3 percent of GDP, although there is considerable uncertainty that this goal will be achieved given that this ratio is expected to be nearly 7 percent this year.

Individual country notes. In **Japan**, where real GDP increased 4.4 percent (SAAR) during the first half of 1996, third-quarter indicators point to continued expansion. Industrial production rose 1.4 percent from its second-quarter level, while new car registrations and housing starts grew at a robust pace. The unemployment rate dropped slightly, and the ratio of job offers to job applicants has increased gradually since late last year.

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

	1996						
	Q1	Q2	Q3	Jul	Aug	Sep	Oct
Industrial Production	0.4	-0.3	1.4	4.9	-2.3	1.0	n.a.
Housing Starts	1.6	1.4	2.6	13.4	-9.1	9.3	n.a.
Machinery Orders	3.4	0.8	n.a.	24.4	-19.5	n.a.	n.a.
New Car Registrations	2.4	-7.7	6.8	8.0	-3.1	8.7	n.a.
Unemployment Rate (%)	3.3	3.5	3.3	3.4	3.3	3.3	n.a.
Job Offers Ratio[1]	0.67	0.69	0.71	0.72	0.71	0.71	n.a.
Business Sentiment[2]	-12	-3	-7	...	...	...	...
CPI (Tokyo area)[3]	-0.3	0.1	0.0	0.4	0.0	-0.4	-0.1
Wholesale Prices[3]	0.0	1.3	0.7	1.4	0.5	0.0	n.a.

1. Level of indicator.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook (Tankan survey).
3. Percent change from previous year.

Wholesale and consumer prices had increased slightly earlier this year in response to the depreciation of the yen. Recently, however, prices have stabilized and 12-month inflation rates are close to zero. The further depreciation of the yen recently has been modest, but may put some upward pressure on prices in coming months.

The current account surplus has been on an erratic upward trend since last April, reaching an eight-month high of $8.2 billion (SA) in August. The merchandise trade surplus was $4.7 billion (SA) in September, down from $6.5 billion in August.

In elections for the Lower House of the Diet held on October 20, the Liberal Democratic Party (LDP) gained seats, but did not achieve an absolute majority. Although the LDP's former coalition partners, the Social Democratic party (SDP) and the New Harbinger Party (Sakigake) have decided not to join the government, they have agreed to support the LDP in forming a minority government under Prime Minister Hashimoto. The fiscally conservative tone of the likely new government has reduced prospects for tax cuts and supplemental spending in the near term.

Incoming data indicate that real activity in **Germany** continued to expand in the third quarter, albeit at a more muted pace than the 6 percent (SAAR) increase in the second quarter. Industrial production and manufacturing orders rose in the third quarter, but at an uneven pace. Both rose in July and August on average, but fell off in September, although the latest data are likely to be revised upward (due to the treatment of non-respondents in the estimate). The IFO business climate survey, an indicator of current and expected conditions in industry, showed significant improvement in the third quarter, particularly in the expectations component of the index. Unemployment, while still very high, has levelled out at just below 4 million workers (s.a.) and the all-German unemployment rate edged up to 10.4 percent in September. Inflation remained subdued in September, with producer prices down over the preceding 12 months and consumer prices up by a little less than 1-1/2 percent. The autumn forecast of the six research institutes projected real GDP growth of 1-1/2 percent in 1996, rising to 2-1/2 percent next year.

The 1997 federal budget is currently under consideration in the German parliament. Because the 1996 budget deficit is likely to overshoot official projections, it is widely expected that the Finance Ministry will propose cutting expenditure more than in the draft 1997 budget issued last summer, although those expenditure cuts remain unspecified. The tax legislation that formed part of the fiscal plan announced by Chancellor Kohl last spring has had a bumpy ride in the parliament, where approval of the SPD-dominated Bundesrat (the upper house) is required. It remains uncertain

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

	1996						
	Q1	Q2	Q3	Jun	Jul	Aug	Sep
Industrial Production	-2.4	3.0	0.8	0.4	0.8	0.0	-1.8
Orders	-0.5	3.8	0.7	1.8	0.9	0.1	-3.6
Unemployment Rate (%)	10.3	10.3	10.3	10.3	10.3	10.3	10.4
Western Germany	8.9	9.0	9.1	9.0	9.0	9.1	9.3
Eastern Germany	16.1	15.6	15.3	15.5	15.3	15.2	15.3
Capacity Utilization[1]	83.1	82.1	82.5	...	...	...	...
Business Climate[1,2]	-15.3	-17.7	-11.3	-21.0	-14.0	-12.0	-8.0
Consumer Prices[1,3]	1.4	1.3	1.4	1.2	1.3	1.4	1.4

1. Western Germany.
2. Percent of firms (in manufacturing, construction, wholesale, and retail) citing an improvement in business conditions (current and expected over the next six months) less those citing a deterioration in conditions.
3. Percent change from previous year.

whether Germany will be able to reduce its general government deficit the 3 percent of GDP reference value laid out in the Maastricht Treaty, although the Kohl government continues to maintain that fiscal measures will bring the deficit to 2-1/2 percent of GDP in 1997 from an expected 4 percent of GDP this year.

In **France**, third-quarter economic activity was boosted by a surge in car sales ahead of the expiration of a government auto-purchase incentive scheme at end-September. Consumption of manufactured products registered a sharp rise in August, but fell back in September, putting the third-quarter average 2-1/2 percent above the second-quarter level. Industrial production (excluding construction) in July-August rose to a level 1.9 percent above the second-quarter average, largely due to an increase in automobile production. However, consumer confidence dipped further in September reflecting general discontent with the French government and the rise in unemployment to a new post-war high of 12.6 percent. Consumer-price inflation continued to moderate, in part as the VAT increase of August 1995 no longer influenced the calculation of the year-over-year inflation rate. The October business confidence survey suggests that output will be subdued in the fourth quarter; the assessment of contemporaneous output declined while future output expectations were unchanged (with the notable exception of the automobile sector, which showed a large deterioration).

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

	1996						
	Q1	Q2	Q3	Jun	Jul	Aug	Sep
Consumption of Manufactured Products	4.9	-1.6	2.5	2.1	-0.7	3.4	-1.5
Industrial Production[1]	1.3	0.0	n.a.	-0.4	1.9	0.0	n.a.
Capacity Utilization	83.8	83.0	n.a.	...	...	...	...
Unemployment Rate (%)	12.1	12.4	12.5	12.4	12.4	12.5	12.6
Consumer Prices[2]	2.1	2.4	1.8	2.3	2.3	1.6	1.6

1. For the months of July and August, INSEE publishes a composite number for industrial production.
2. Percent change from previous year.

On October 31, the EU Commission announced that it accepted the French government's planned 37-1/2 billion franc financial transfer from state-owned France Telecom to the government to cover future pension liabilities. This transfer will lower France's 1997 deficit by about 1/2 percent of GDP.

In the **United Kingdom**, preliminary estimates indicate that real GDP grew 3 percent in the third quarter after expanding 2.2 percent in the previous quarter. Retail sales continued at a brisk pace in the third quarter while industrial production rose modestly. Consumer confidence remained very strong in October, while the purchasing managers' index continued to signal strength in manufacturing orders, especially for consumer goods. The unemployment rate continued to decline and in September reached 7.4 percent, its lowest level in five and a half years.

Consumer-price inflation ticked up in September to a 12-month rate of 2.9 percent, above the government's target rate of 2-1/2 percent or less. The underlying rate of increase of average earnings rose to 4 percent in August. The recent rise in underlying inflation likely contributed to the surprise decision to raise the

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

	1996						
	Q1	Q2	Q3	Jun	Jul	Aug	Sep
Real GDP (a.r.)	2.6	2.2	3.0	...	...	...	...
Non-oil GDP (a.r.)	2.7	1.9	3.0	...	...	...	...
Industrial Production	0.1	0.2	0.3	-0.8	0.6	-0.3	0.5
Retail Sales	0.4	1.3	0.8	1.5	-0.6	0.9	-0.3
Unemployment Rate (%)	7.9	7.7	7.5	7.7	7.6	7.5	7.4
Consumer Prices[1]	2.9	2.8	2.9	2.8	2.8	2.8	2.9
Producer Input Prices[2]	3.0	0.0	-2.6	-2.3	-2.4	-2.5	-2.9
Average Earnings[2]	3.7	3.8	n.a.	3.8	4.0	4.0	n.a.

1. Retail prices excluding mortgage interest payments. Percent change from previous year.
2. Percent change from previous year.

Bank of England's minimum lending rate by 25 basis points to 6 percent following the monthly meeting between Governor George and Chancellor Clarke on October 30.

In **Italy**, real GDP declined 1.6 percent (SAAR) in the second quarter. This drop retraced the modest rise in the first quarter, with both movements largely due to inadequate adjustments for the leap year. The second-quarter decline also reflected a significant drawdown in inventories. The drag of inventories on the economy is

ITALIAN REAL GDP
(percent change from previous period, SAAR)

	1995				1996	
	Q1	Q2	Q3	Q4	Q1	Q2
GDP	6.3	0.8	2.4	0.3	1.7	-1.6
Private Consumption	2.5	2.8	1.3	0.1	0.2	0.4
Investment	10.2	7.3	4.0	6.0	-2.4	2.5
Government Consumption	-0.6	-0.8	-0.2	-1.7	-1.0	0.4
Exports	24.7	14.6	2.1	-11.2	1.0	-2.0
Imports	0.3	16.0	10.7	-1.4	-6.7	-19.2
Total Domestic Demand	0.9	0.6	4.3	3.1	-0.1	-5.6
Net Exports (contribution)	5.4	0.3	-1.7	-2.7	1.7	3.9
Inv. Change(contribution)	-2.3	-2.2	2.7	2.2	0.4	-6.3

expected to have lessened in the third quarter and recently, Prime Minister Prodi announced that real GDP is likely to have grown 2 percent (SAAR) in the third quarter. However, the latest monthly indicators have been weak. Business sentiment remained gloomy while consumer confidence has declined in recent months. Industrial production rose slightly in August after dropping significantly in July.

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

	1996						
	Q1	Q2	Q3	Jul	Aug	Sept.	Oct.
Industrial Production	-2.0	-1.4	n.a.	-2.8	0.5	n.a.	n.a.
Cap. Utilization (%)	75.9	76.6	n.a.	...	...	...	...
Unemployment Rate (%)	12.0	12.2	12.2	...	...	...	...
Consumer Confidence[1]	107.7	113.8	114.1	115.0	115.2	112.0	106.00
Bus. Sentiment[2] (%)	15.7	-1.0	n.a.	-6.0	2.0	n.a.	n.a.
Consumer Prices[3]	5.0	4.3	3.5	3.6	3.4	3.4	3.0
Wholesale Prices[3]	7.7	3.4	n.a.	2.7	2.0	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. Percent change from previous year.

Good news on inflation continues. Consumer-price inflation on a year-over-year basis fell in October to 3 percent, its lowest level in 27 years. Further progress on consumer price inflation is likely in light of continued moderation in wholesale and producer price inflation, in part reflecting the appreciation of the lira over the past year and a half.

On September 27, the Italian government announced a tougher-than-expected 1997 budget that aims to reduce Italy's 1997 fiscal deficit to 3 percent of GDP. The deficit reduction package--which may generate $41 billion equivalent in deficit reduction--will be implemented in three phases. The core of the package, accounting for around $25 billion equivalent, will raise approximately $17 billion from spending cuts and around $8 billion from new revenues. The second phase of the budget, which will be implemented early next year, aims to generate an additional $8 billion equivalent through the so-called "Euro Tax". This tax will be applied to all but the poorest residents on a sliding scale of income. Finally, the government intends to generate a further $8 billion from what the authorities call "special Treasury operations," akin to France's creative accounting à la France Telecom[1]. By law, the parliament has until the end of the year to ratify the proposed budget.

Recent indicators for **Canada** suggest that the economy is continuing to expand, although at an uneven pace. Employment dropped in September and was up only slightly for the third quarter as a whole, while retail sales for July and August on average were only a little above the second-quarter level. However, housing starts rose again in the third quarter, and July-August averages of new factory orders and shipments were both 3 percent above second-quarter levels. Both business and consumer confidence slipped in the third quarter. Business confidence is still at a relatively high level, but consumer confidence remains weak. On October 23, the Canadian Auto Workers ratified a labor agreement with General Motors, ending a 20-day strike that had idled production at all of GM's Canadian facilities.

Core consumer-price inflation is near the bottom of the Bank of Canada's 1-3 percent target band. The low level of inflation combined with the recent appreciation of the Canadian dollar prompted the Bank of Canada to cut official interest rates again on October 28; at 3.50 percent, the Bank rate is now at its lowest level since 1963.

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[1]Specifically, this sum will be generated through the transfer of funds held in the reserves for severance payment of employees of state holding companies--ENEL and ENI--that will be fully privatized in 1996 and 1997.

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

	1996						
	Q1	Q2	Q3	Jun	Jul	Aug	Sep
Industrial Production	0.4	0.5	n.a.	-0.1	1.3	0.1	n.a.
Manufacturing Survey:							
Shipments	-0.5	2.4	n.a.	-0.2	2.9	-0.7	n.a.
New Orders	-0.0	2.6	n.a.	-1.8	3.9	-1.8	n.a.
Retail Sales	1.0	0.3	n.a.	0.4	0.1	-0.4	n.a.
Housing Starts	1.8	10.9	4.1	3.8	-5.2	0.3	2.2
Employment	0.7	0.2	0.1	-0.4	0.1	0.6	-0.3
Unemployment Rate (%)	9.5	9.6	9.7	10.0	9.8	9.4	9.9
Consumer Prices[1]	1.4	1.4	1.4	1.4	1.2	1.4	1.5
Consumer Attitudes[2]	96.4	101.5	100.8	...	...	...	...
Business Confidence[3]	137.6	149.1	148.3	...	...	...	...

1. Percent change from year earlier.
2. Level of index, 1991 = 100.
3. Level of index, 1977 = 100.

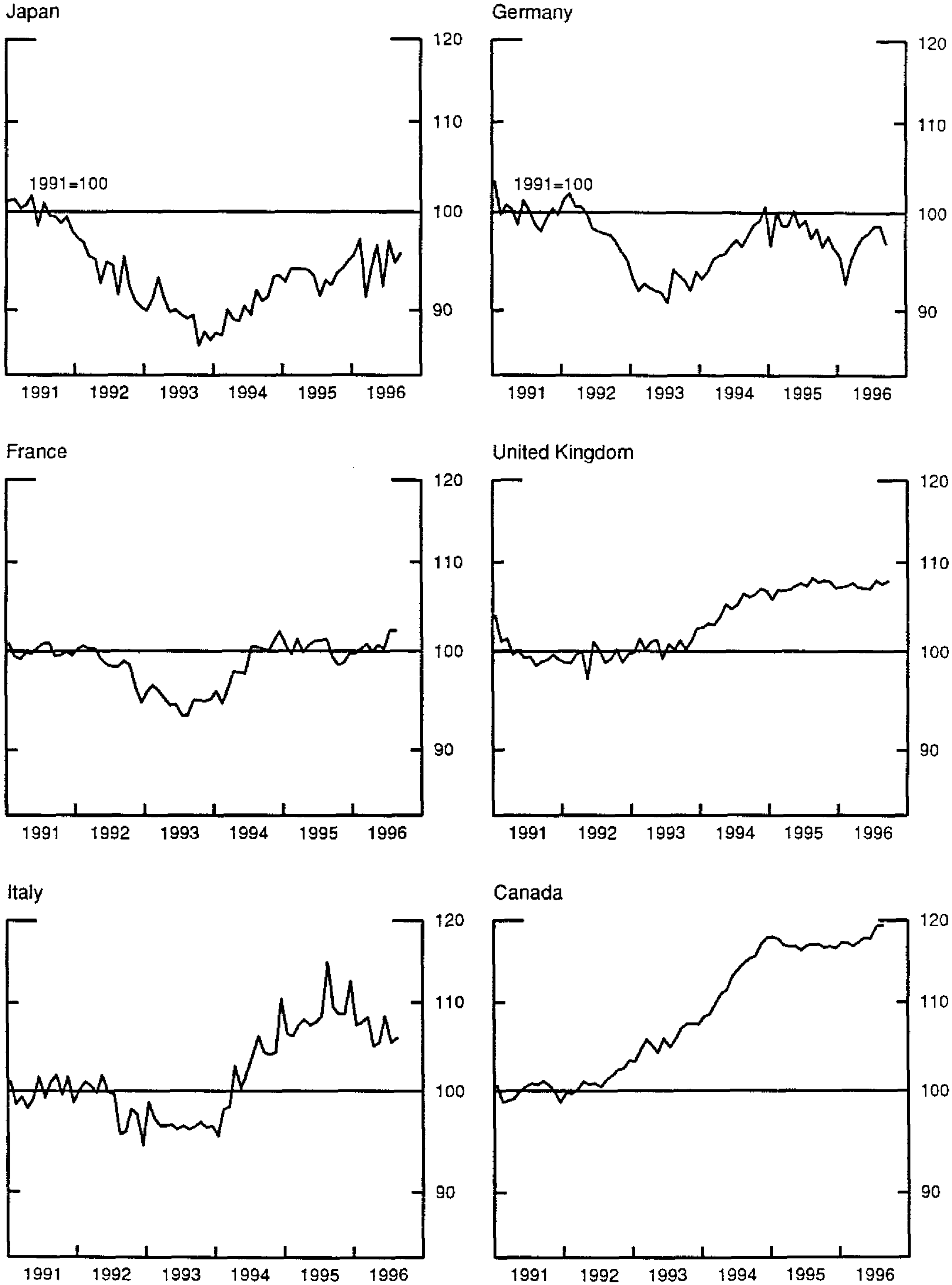
EXTERNAL BALANCES
(Billions of U.S. dollars, seasonally adjusted)

	1995	1996						
		Q1	Q2	Q3	Jun	Jul	Aug	Sep
Japan: trade	106.6	16.6	13.6	14.4	6.3	3.3	6.5	4.7
current account	110.6	15.4	15.3	n.a.	6.2	6.0	8.2	n.a.
Germany: trade[1]	63.6	14.1	16.4	n.a.	4.7	7.3	n.a.	n.a.
current account[1]	-16.7	-2.5	-3.3	n.a.	-1.4	-2.9	n.a.	n.a.
France: trade	20.1	5.8	4.7	n.a.	1.9	2.0	2.7	n.a.
current account	16.6	7.3	3.8	n.a.	1.6	0.0	n.a.	n.a.
U.K.: trade	-18.3	-5.6	-5.5	n.a.	-1.7	-1.9	-0.9	n.a.
current account	-4.6	-1.8	0.7	n.a.	...	...	...	...
Italy: trade	27.6	8.5	12.6	n.a.	4.2	n.a.	n.a.	n.a.
current account[1]	27.4	5.9	11.1	n.a.	4.3	n.a.	n.a.	n.a.
Canada: trade	20.7	5.9	7.1	n.a.	2.2	2.1	2.9	n.a.
current account	-8.1	-1.2	0.8	n.a.	...	...	...	...

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

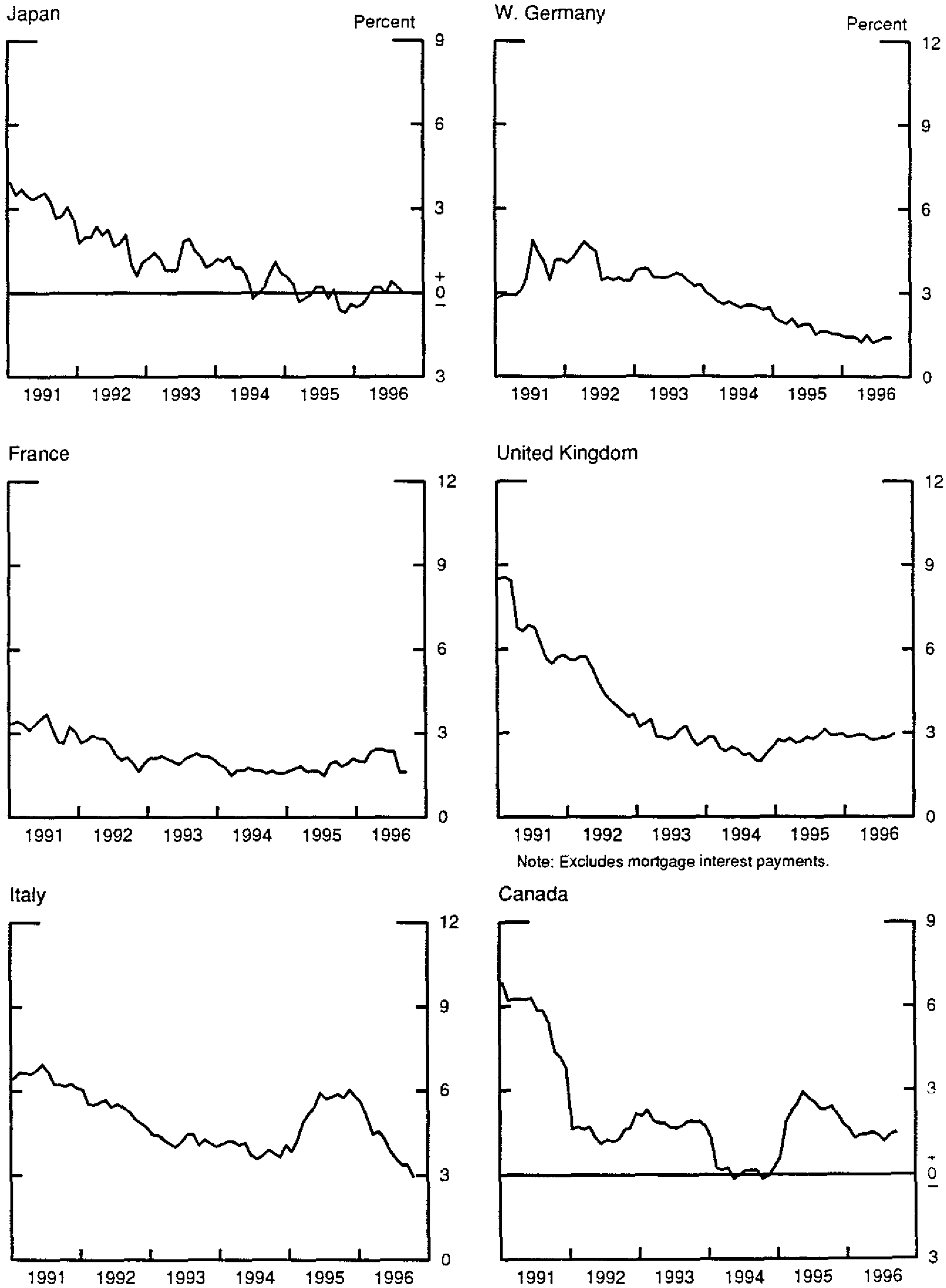
Industrial Production in Selected Industrial Countries

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



Consumer Price Inflation in Selected Industrial Countries

(12-month change)



Economic Situation in Other Countries

In Latin America, indications about economic activity have been mixed. Mexico and Argentina have been recovering from their low points in 1995, growth in Brazil appears to have slowed because of weak industrial performance, and economic performance in Venezuela has remained poor, except for the oil sector. In major Asian countries, economic expansion has slowed, while the Russian economy has continued to decline. Inflation in Mexico rose in September for seasonal reasons, has been low in Argentina and Brazil, and has declined in Venezuela. Trade surpluses narrowed in the third quarter in Mexico and Argentina, and the trade balance moved into deficit in Brazil. In the first three quarters of 1996, China's trade surplus was half of that recorded over the same period a year earlier, while Taiwan's trade surplus widened. In Korea, an export slowdown contributed to a significant widening in the trade deficit in the first eight months of the year.

Individual country notes. In **Mexico**, monthly indicators showed a resumption in the growth of economic activity in the third quarter after a pause in the second quarter. Industrial production rose 5 percent (SA, not annual rate) in the July-August period after a 2 percent decline in the second quarter. The continued recovery in domestic demand led to a rise in imports and a reduction in the trade surplus in that quarter to its lowest level since 1995:Q1.

Monthly inflation was 1.6 percent in September, up from a low of 1.3 percent in August but still well below the recent peak of 2.8 percent in April. Most of the uptick in September was due to a seasonal rise in education expenses associated with the start of the school year. The downward trend in inflation rates has been helped by the stability of the exchange rate during 1996 through September. However, the peso has depreciated about 5 percent since mid-September as market participants focused on the real appreciation of the peso during 1996 (about 15 percent on net even after the recent slip) and the potential loss of competitiveness for Mexican exports. The Bank of Mexico responded to the peso's depreciation by tightening conditions in the money market and rates on 28-day cetes have risen ore than 6 percentage points. The Bank of Mexico made clear that it was responding to the rapidity of the peso's decline, not to the level of the peso.

One specific factor that may have intensified pressure on the peso was the government's announcement on October 13 that it would not sell a majority stake in Pemex's petrochemical plants as planned, but would instead create a series of petrochemical subsidiaries and maintain a 51 percent stake in them, with only a minority stake sold to private investors. That was seen as a retreat due to pressure from the old guard of the ruling party (PRI) and, therefore, raised doubts about the government's commitment to its privatization plans.

Pressure on the peso also came from uncertainty ahead of the signing of a new "pacto" between Mexican government, labor, and business on October 26. In the event, the agreement provided few surprises. The minimum wage will increase 17 percent in December (with no further increases planned for 1997) versus a target of 15 percent inflation for 1997 (December-over-December), and compares with 1996 inflation that is expected to be about 27 percent. The government projected for 1997 real GDP growth of at least 4 percent, a small (0.5 percent of GDP) budget deficit, and a current account deficit of less than 2 percent of GDP.

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

	1994	1995	1996		1996	
			Q2	Q3	Aug	Sep
Real GDP	4.5	-6.2	7.2	n.a.	...	...
Industrial Production (SA)	4.5	-7.5	11.1	n.a.	12.7	n.a.
Unemployment Rate (%)	3.6	6.3	5.6	5.5	5.3	5.5
Consumer Prices[1]	7.1	52.1	6.4	4.4	1.3	1.6
Trade Balance[2]	-18.5	7.0	2.2	1.4	0.4	0.6
Imports[2]	79.4	72.5	21.4	22.9	7.5	7.8
Exports[2]	60.8	79.5	23.6	24.3	7.9	8.4
Current Account[2]	-29.5	-0.7	0.6	n.a.	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA

In **Argentina**, real GDP grew 2.6 percent in the second quarter from a year earlier, and August and September industrial production showed increases of 9.2 percent compared with a year earlier (SA), providing evidence that the recovery from the 1995 recession is well underway. Unemployment nonetheless remains very high, and inflation has been low. The recovery contributed to a narrowing of the trade surplus in July and August. International reserves have rebounded from the decline experienced following the resignation of Finance Minister Cavallo last summer, and stood at $15 billion at end-September.

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

	1994	1995	1996		1996	
			Q2	Q3	Aug	Sep
Real GDP	7.4	-4.4	2.6	n.a.	...	...
Industrial Production (SA)	5.7	-6.2	2.6	8.6	9.2	9.2
Unemployment Rate (%)[2]	11.7	17.4	17.1	...	...	...
Consumer Prices[1]	3.9	1.5	-0.2	0.7	0.0	0.2
Trade Balance[3]	-4.0	3.0	2.2	n.a.	0.2	n.a.
Current Account[3]	-9.1	-1.7	1.3	n.a.	...	...

1. Percentage change from previous period.
2. Unemployment figures available only in May and October of each year. The annual figure is the average of the two surveys.
3. Billions of U.S. dollars, NSA, current account under Q2 is for the first half of 1995.

Argentina's slow recovery from the recession led to lower-than-expected tax revenues and the larger-than-expected fiscal deficit for the first half of 1996, prompting the senate to pass a new package of tax increases in September. In October, Argentina was granted a waiver for missed fiscal performance criteria under its IMF standby arrangement.

In late September, Argentine labor unions launched a thirty-six hour general strike to challenge President Menem's free market reforms. Unshaken, President Menem signed a controversial decree deregulating the country's union-controlled health-care system and allowing Argentines to choose their own medical plans.

In **Brazil**, indications are that economic activity has slowed considerably since the second quarter, when real GDP rose by 7 percent (s.a.a.r.). Consumer prices were stable in September, for a twelve-month inflation of 13 percent, the lowest increase since the early 1970s.

The trade deficit widened to $0.7 billion in September, bringing the cumulative trade deficit to $1.4 billion for the year through September. Preliminary data suggest that the deficit could have widened further in October. The *real*/dollar exchange rate has continued to depreciate slowly. Brazil's international reserves stood at $59 billion at the end of September, down only slightly from its $60 billion peak in May. In late October, Brazil issued $750 million in 5-year global bonds, which traded at 280 basis points above U.S. Treasuries on October 30.

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

	1994	1995	1996		1996	
			Q2	Q3	Aug	Sep
Real GDP	5.9	4.2	2.3	n.a.	...	...
Industrial Production (SA)[1]	7.9	3.6	0.3	n.a.	-0.8	n.a.
Open Unemployment Rate (%)	5.1	4.4	5.9	5.5	5.6	5.2
Consumer Prices[1]	929.0	22.0	3.6	1.9	0.5	0.0
Trade Balance[2]	10.4	-3.2	0.1	-1.2	-0.3	-0.7
Current Account[2]	-1.8	-17.8	-4.1	-3.7	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA

In **Venezuela**, consumer price inflation continued to fall. The overall economy appears to be doing better than expected, but this is mostly due to high oil prices. The non-oil sectors continue to deteriorate. Venezuela is trying to improve its fiscal position and is using windfall revenues from higher oil prices partly to repay foreign and domestic debt. As a result of high oil prices, international reserves reached a record $9 billion (excluding gold) at end-September, a rise of $3 billion since December 1995.

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

	1994	1995	1996		1996	
			Q2	Q3	Aug	Sep
Real GDP	-2.8	2.2	n.a.	n.a.	...	...
Unemployment Rate (%)	8.8	10.8	11.1	...	...	...
Consumer Prices[1]	70.9	56.6	30.9	13.2	4.1	3.6
Trade Balance[2]	-3.6	-6.0	-2.1	n.a.	n.a.	n.a.
Current Account[2]	2.5	3.1	...	...	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA, non-oil trade balance.

In **China**, real GDP increased by 9.6 percent in the first three quarters of 1996 from its year-earlier level, indicating that real activity has continued to decelerate slightly. Despite some relaxation of credit conditions in recent months, the tight credit conditions that generally have prevailed since the latter part of 1993 succeeded in reducing the 12-month consumer price inflation rate to 7.4 percent in September, compared with an inflation rate of 25.5 percent in 1994. The trade balance in the first nine months of this year registered a surplus of $8.2 billion, compared with a $16.4 billion surplus a year earlier, as the dollar value of exports fell by 4 percent over the period. China has continued to receive strong capital inflows, particularly in the form of foreign direct investment. Direct investment was $29.3 billion in the first nine months of this year, a 17 percent rise from its year-earlier level. Foreign reserves were $95 billion at the end of September, up from $75 billion at the end of 1995.

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

	1994	1995	1996		1996	
			Q2	Q3	Aug	Sep
Real GDP[1]	11.8	10.2	9.8	9.6	...	...
Industrial Production	22.0	17.8	n.a.	n.a.	n.a.	n.a.
Consumer Prices	25.5	10.1	8.6	7.9	8.1	7.4
Trade Balance[2]	5.2	16.7	2.1	7.3	3.0	3.2

1. Cumulative from the beginning of the year
2. Billions of U.S. dollars, NSA

In **Taiwan**, growth in real activity has remained weak by historical standards, even though the central bank has allowed nominal interest rates to fall by 150 basis points since late 1995. Industrial production rose only 1.9 percent from its year-earlier level in the third quarter, and investment spending also appears to have remained subdued. Taiwan's trade surplus rose to $10.2 billion in the first nine months of this year, compared with a $4.2 billion surplus over the same period of 1995. The marked rise in the trade surplus mainly reflected a fall in the dollar value of imports of 3 percent over the period, due to sluggish domestic demand; exports rose by only four percent over the same period. Taiwan's 12-month inflation rate was 3.8 percent in September. Foreign exchange reserves stood at $86.7 billion at the end of September, compared with $90.4 billion a year earlier.

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

	1994	1995	1996 Q2	1996 Q3	1996 Aug	1996 Sep
Real GDP	6.5	6.1	5.4	...	...	...
Industrial Production	6.6	4.2	-0.5	1.9	0.1	3.9
Consumer Prices	2.6	4.6	2.3	3.5	5.1	3.8
Trade Balance[1]	7.8	8.3	3.2	4.6	1.1	2.1
Current Account[1]	6.2	5.0	n.a.	n.a.	...	...

1. Billions of U.S. dollars, NSA

In **Korea**, real GDP grew 6.7 percent in the second quarter from its year-earlier level, a marked decline from output growth rates of nearly 10 percent in the first three quarters of last year. A pronounced deceleration in exports, due to weak demand in several of Korea's principal export markets, including semiconductors, petrochemicals, and steel, has contributed to the slowdown in activity. In the first eight months of this year, Korea's exports were 7 percent higher than in the same period a year earlier, compared with 32 percent growth in 1995 as a whole. The export slowdown has been reflected in a significant widening in Korea's current account deficit to $15.2 billion in the first eight months of the year (about 4 percent of GDP). The central bank has allowed the won to depreciate against the U.S. dollar by about 5 percentage points since the end of May because of concern about the export slowdown. Consumer prices in September were 4.7 percent above their year-earlier level.

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

	1994	1995	1996 Q2	1996 Q3	1996 Aug	1996 Sep
Real GDP	8.4	9.0	6.7	n.a.	...	...
Industrial Production	10.7	11.7	7.3	n.a.	n.a.	n.a.
Consumer Prices	6.2	4.5	5.1	5.2	5.3	4.7
Trade Balance[1]	-3.1	-4.7	-2.8	n.a.	-2.8	n.a.
Current Account[1]	-4.5	-8.9	-4.7	n.a.	-3.5	n.a.

1. Billions of U.S. dollars, NSA

The OECD formally invited Korea to become its 29th member on October 11. Korea will become a member officially after the Korean legislature ratifies the agreement, which is expected to occur before the end of this year.

In **Russia**, the economy and economic reform have muddled along as President Boris Yeltsin prepared for and underwent bypass surgery, which was apparently successful. Indications are that real economic activity has continued to decline, but the rate of decline has been moderating. Over the past three months, monthly inflation has been under one percent, while the ruble-dollar exchange rate has depreciated by less than 3 percent per month and has stayed well within the crawling band "corridor" established by the Central Bank.

Russia missed fiscal revenue targets under its three-year, $10 billion IMF Extended Fund Facility, prompting the IMF to delay the release of this month's tranche. This marks the second time that Russia has missed fiscal performance criteria since the program began eight months ago. Tax revenue for January through September 1996 was only $32 billion, or 74 percent of the planned revenue. The Russian government has been taking action to strengthen tax collection, and announced shortly after the departure of the IMF mission that October revenue was up 30 percent over September's.

Russia is expected to introduce a Eurobond later this year and has received "speculative" ratings for its foreign currency debt of Ba2 from Moody's and BB-minus from Standard and Poor's. The rating places Russia above Brazil, Mexico, and Romania but below Hungary, Slovakia, and Poland.

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

	1994	1995	1996		1996	
			Q2	Q3	Aug	Sep
Real GDP	-15	-4	-7	-7	-8	-5
Industrial Production	-21	-3	-5	-7	-8.5	-6.8
Consumer Prices[1]	10	7	2	1	-0.2	0.3
Ruble Depreciation[1]	9	2	2	6	-2.6	-1.0
Trade Balance[2]	12.1	18.3	5.3	4.9	1.9	1.8
Current Account[2]	1.3	5.7	n.a.	n.a.	...	...

1. Percent change from previous period.
2. Billions of U.S. dollars.