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CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

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SUMMARY AND OUTLOOK

Outlook for economic activity

Recent developments strongly suggest that real GNP will grow more slowly this quarter than the 2 per cent annual rate of the previous two quarters, and a cessation of expansion--or possibly a small contraction--is in prospect for the first half of next year. Industrial production declined slightly in both August and September, and with retail sales continuing sluggish into mid-October any near-term reversal of the recent downrift in output of consumer goods seems unlikely. In early October, sales of new autos receded from the model-introduction bulge of late September, and auto manufacturers are reported to be trimming output schedules for late this year. Output of business equipment has been about level since June.

Most sectors of final demand over the three quarters ahead appear likely to provide appreciably less support to over-all growth than thus far this year. Federal defense spending is expected to drop substantially in line with recent official statements. Only rather moderate advances are in prospect for State and local spending, in line with the slowing that occurred last quarter, given the present tightness in the long-term municipal capital markets and the lags between financing and expenditures. Recent production developments for business equipment, along with the relatively flat trend in new orders for over the past years, are broadly consistent with a fairly marked prospective slowing in growth of plant and equipment outlays, and there

may well be little or no increase in real terms in the first half of next year. The increase in housing starts in September largely reflected special influences, and declines are likely to be resumed given continued tightness in financial markets.

Consumer spending is expected to continue to advance at about the moderate third quarter pace, with higher prices of both goods and services accounting for most of the increase. Growth in wages and salaries would be slowed by the anticipated weaker employment trend, but disposable income will be supported by the reduction in the surtax to 5 per cent on January 1, and by the sizable increase in the sizable increase in Social Security benefits assumed to be effective in the second quarter of 1970. There will be some further expansive potential in this sector, of course, if the surtax is eliminated on January 1 and if the rise in Social Security benefits is larger or comes sooner than assumed.

With projected developments in final demands, incentives for inventory accumulation will weaken. For a time, however, there may be some involuntary inventory accumulation until production schedules are adjusted. We are projecting only a moderate subsequent decline in the rate of inventory investment, but it must be noted that there is a distinct possibility of more accumulation early in the period and a much sharper subsequent decline.

Outlook for resource use and prices

Key measures of resource use eased in the third quarter and prospects are for a marked further easing to mid-1970. Industrial production is now anticipated to show little change--or possibly some decline--in the current quarter, and further declines are likely in the first half of next year. With capacity continuing to grow, the manufacturing capacity utilization rate is projected to fall to as low as 80 per cent in the second quarter of 1970, from around 84.5 per cent in the second quarter of this year.

Demand for labor slowed further in the third quarter and, consistent with the GNP projection, only a modest employment increase--if any--is expected in the first half of next year. As a result, the unemployment rate is likely to continue to rise irregularly.

Upward pressures on wage rates have remained strong. Although the calendar of new contract negotiations has been light this year, union wage rates have continued up weaker contracts negotiated in earlier years and large pay increases have been granted to non-union workers. Next year, a much larger number of workers will be covered in major contract negotiations and wage demands are expected to be unusually large and consistent. But reduced demands for labor, a shorter workweek and less overtime pay should dampen somewhat the increase on average in hourly earnings. Declining profits and profit margins are likely to make for more management resistance to large increases in wage rates and for more strikes in key industries than this year.

With wage rates still likely to increase fairly rapidly and with output per manhour unlikely to increase rapidly in the face of stable or declining output, labor costs per unit of output will continue to rise. This and efforts to sustain profits will maintain upward pressure on prices. But we expect price pressures to be mitigated by the prospective slackening in demands and the easier resource picture.

On balance, we look for some moderation in the pace of price increase at both the industrial and consumer levels by mid-1970. Over the past year, the steep rise in consumer prices has been in large part attributable to foods and services. For foods, slower income growth--along with generally ample supplies, except possibly for pork--is likely to contribute over the next three quarters to a smaller increase in demands and hence in prices than over the past year. For services, on the basis of our projection, a leveling off of mortgage interest rates seems more plausible than further sharp increases. While prices of some other services may also rise more slowly, on the whole we cannot expect any marked deceleration in this broad sector.

Prospective demands for funds

Business needs for funds will remain relatively large during the fourth quarter, even if growth in aggregate economic activity shows further signs of slackening. Inventory expansion is expected to remain close to the advanced third quarter rate, plant and equipment outlays are projected to grow further; and corporate profits are being eroded by rising business costs. Corporate liquidity appears to have declined substantially in the third quarter, and although a sizable further reduction seems likely in the current quarter, needs for external borrowing will also be large.

The share of business financing requirements being accommodated through banks may rise somewhat. In particular, hopes that the current down-trend of bond yields will persist may encourage corporate treasurers to defer capital market financing and turn in the interim to bank credit lines and the commercial paper market. While the recent volume of corporate bond financing has remained quite large, the forward calendar of issues definitely scheduled is only moderate.

Recent yield declines on municipal bonds have made it possible for a number of State and local government borrowers previously foreclosed by rate ceilings to return to the market. With the backlog of other deferred demands still very large, pressures from such borrowers are likely to continue to build-up, whenever rate ceilings permit, for some months ahead. Since several key States have recently raised their

rate ceilings, larger borrowing demands are now possible even at yields above 6 per cent. At the same time, in the absence of a change in monetary policy or regulation Q ceilings, the capacity of commercial banks to buy municipals will remain very limited. In fact, much of the recent yield down-turn appears to have reflected repositioning by dealers, rather than ultimate investor buying. In these circumstances the odds would thus seem to favor some back-up of municipal yields in the weeks just ahead.

Over the remainder of the year securities markets will also have to absorb a sizable volume of U.S. Government and Federal agency debt, though mostly in the shorter-term area. Because Federal cash spending has failed to taper off as much as anticipated this fall, fourth quarter Federal cash borrowing is now expected to exceed--by \$2 billion or more--the \$5 billion figure suggested as likely by Treasury spokesmen before the quarter began. In the market for Federal agency debt there is little prospect for any let up in the volume of FNMA and FHLBB borrowing. Together these two agencies are expected to raise possibly another \$1.5 billion of new money in November and December and to need an additional \$1 billion in January.

Prospective supply of funds

With no change in monetary policy or regulation Q ceilings, deposits at commercial banks will probably continue to decline on balance over the remainder of the year, although at a substantially reduced pace

compared to recent months. Demand deposits, including Government as well as private, while fluctuating substantially over the period may show little net change. Time and savings deposits are likely to decline further, however, although by less than in the third quarter.

CD runoff has moderated considerably over the past few weeks as sizable amounts of foreign official accounts have switched from Euro-dollar deposits in foreign branches of large U.S. banks to domestic CD's at the home office. While much of this switching was of the one-shot variety, prompted by changed interest rate relationships associated with changes in marginal reserve requirements on the two types of deposits, some inflow of foreign official funds may persist. If so, the continuing CD attrition may remain at a more moderate rate, particularly since total monthly maturities of outstanding CD's will at the same time be shrinking. Consumer-type time and savings deposits are expected to remain vulnerable to the competition of high rates on market securities. Attrition in such accounts has been large, as expected, during the October post-interest-crediting period, but should become smaller again in November and December.

Deposit pressures on banks in combination with increased loan demands are likely to encourage further growth of commercial paper issued through bank holding companies. Much of the fall expansion in such borrowing to date has reflected the emergence of new issuers, and this pattern is likely to persist.

Nonbank thrift institutions also experienced large net savings losses during the October reinvestment period. While it now seems likely that their fourth quarter net savings experience will be no better than that in the third, recent evidence--after rough allowance for seasonal factors--does not suggest any major further deterioration either. With expectations generally for significant further savings attrition early next year, with sizable backlogs of outstanding mortgage commitments to be worked down, and with lower levels of institutional liquidity, savings and loan associations and savings banks should, nevertheless, remain cautious in approving new mortgage commitments through year-end.

With expectations having already reduced interest rates substantially, and given the continued restraints anticipated on institutional supplies of funds, there may be relatively little room for further significant interest rates declines. Increases in mortgage interest rates and some back-up in municipal yields seem likely, and other rates could rise as the economy moves into the last two months of year when seasonal loan demand pressures peak.

Balance of payments outlook

Preliminary indications of a dip in imports in September, coupled with maintenance of exports at an advanced level, tend to support predictions that the current account of the U.S. balance of payments will show a moderate improvement in coming months. Abroad, economic activity is continuing to expand. Export orders for U.S.

machinery showed a further strong rise during the summer. Revaluation of the German mark is not expected to alter the general prospects for expansion in world trade. Its effects will help a little to damp down inflationary pressures in Germany, while moderately stimulating activity in neighboring countries. To the extent that the German trade surplus declines, the major benefit will accrue to Germany's EEC trade partners.

There is little basis in recent statistical or other news for modifying, or for sharpening, earlier uncertain views on prospective private capital flows from or to the United States. Liabilities of U.S. banks to their foreign branches have risen by over \$1/2 billion in the past two and a half weeks, while Euro-dollar interest rates for terms of one month to a year have dropped sharply--though to a level that is still exceptionally high, about 9-1/4 per cent.

The decline in Euro-dollar rates from peaks of over 11 per cent in June and July reduces the cost to U.S. banks of borrowing through foreign branches by about 1 percentage point when allowance is made for the new reserve requirements under Regulation M. In comparison with reserve-free funds obtainable by large banks for around 8 per cent or somewhat more in the commercial paper market, the present cost of Euro-dollars obtained through branches is, however, still high.

The growth to the middle of the month in U.S. banks' takings as well as the decline in rates continuing since then, probably reflects an easing in supply and demand for Euro-dollars in Europe. In August

and early September, the decline in rates had been temporarily reversed by heavy demand for Euro-dollar credit to hedge against appreciation of the German mark. Now that the DM rate has risen such demand has no doubt fallen off, and reflows from the mark have no doubt contributed to Euro-dollar supplies. Such reflows may continue for a while after the new DM parity is established, presumably at a level not far from its present market value. For the months ahead, however, there are no visible indications that large fresh supplies would be coming into the Euro-dollar market from other sources, given a continuation of present Euro-dollar interest rates.

SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally adjusted)

	Latest Period	Amount			Per Cent Change	
		Latest Period	Preced'g Period	Year Ago	Year Ago*	2 Yrs. Ago*
Civilian labor force (mil.)	Sept'69	81.4	81.1	78.8	3.2	4.6
Unemployment (mil.)	"	3.2	2.9	2.8	13.5	2.9
Unemployment (per cent)	"	4.0	3.5	3.6	--	--
Nonfarm employment, payroll (mil.)	"	70.4	70.4	68.2	3.2	6.7
Manufacturing	"	20.3	20.3	19.8	2.4	4.9
Other industrial	"	8.5	8.5	8.2	3.1	5.3
Nonindustrial	"	41.6	41.5	40.1	3.7	7.8
Industrial production (57-59=100)	"	173.8	174.3	165.1	5.3	10.8
Final products	"	171.6	172.3	165.7	3.6	9.4
Materials	"	175.9	176.0	165.1	6.5	12.0
Wholesale prices (57-59=100) ^{1/}	"	113.6	113.4	109.1	4.1	7.0
Industrial commodities (FR)	"	112.2	111.8	108.4	3.5	6.3
Sensitive materials (FR)	"	113.5	112.5	107.4	5.7	12.3
Farm products, foods & feeds	"	114.3	114.6	108.6	5.2	8.5
Consumer prices (57-59=100) ^{1/}	Aug'69	128.7	128.2	121.9	5.6	10.1
Commodities except food	"	118.2	118.1	113.5	4.1	8.0
Food	"	127.4	126.7	120.5	5.7	9.3
Services	"	145.0	144.0	135.5	7.0	13.1
Hourly earnings, mfg. (\$)	Sept'69	3.23	3.24	3.04	6.3	13.3
Weekly earnings, mfg. (\$)	"	131.06	131.63	124.33	5.4	12.9
Personal income (\$ bil.) ^{2/}	"	759.8	757.5	701.1	8.4	19.1
Corporate profits before tax (\$ bil.) ^{2/}	QII'69	95.4	95.5	90.7	5.2	20.6
Retail sales, total (\$ bil.)	Sept'69	29.7	29.4	28.9	2.8	10.4
Autos (million units) ^{2/}	"	9.1	8.1	9.0	0.7	19.3
GAF (\$ bil.)	"	8.1	8.1	7.5	7.3	14.9
Selected leading indicators:						
Housing starts, pvt. (thous.) ^{2/}	"	1,518	1,383	1,592	-4.6	5.1
Factory workweek (hours)	"	40.7	40.6	41.0	-0.7	-0.2
New orders, dur. goods (\$ bil.)	"	32.3	30.5	28.4	13.8	28.2
New orders, nonel. mach. (\$ bil.)	"	6.1	5.5	5.2	17.2	38.4
Common stock prices (1941-43=10)	Sept'69	94.51	94.18	101.34	-6.7	-1.4
Manufacturers' inventories, book val. (\$ bil.)	Aug'69	93.6	93.2	86.7	8.0	14.4
Gross national product (\$ bil.) ^{2/}	QIII'69	942.3	924.8	876.4	7.5	17.7
Real GNP (\$ bil., 1958 prices) ^{2/}	"	730.4	726.7	712.8	2.5	7.7

* Based on unrounded data. ^{1/} Not seasonally adjusted. ^{2/} Annual rates.

SELECTED DOMESTIC FINANCIAL DATA

	Week ended	4-week	Last 6 months	
	October 18, 1969	average	High	Low
Money Market <u>1/</u> (N.S.A.)				
Federal funds rate (per cent)	9.71	9.46	10.18	7.43
U.S. Treas. bills, 3-mo., yield (per cent)	7.01	7.03	7.12	5.93
U.S. Treas. bills, 1-yr., yield (per cent)	7.25	7.34	7.41	5.96
Net free reserves <u>2/</u> (\$ millions)	-1,190	-1,027	-349	-1,242
Member bank borrowings <u>2/</u> (\$ millions)	1,348	1,214	1,634	740
Capital Market (N.S.A.)				
Market yields (per cent)				
5-year U.S. Treas. bonds <u>1/</u>	7.47	7.74	7.97	6.25
20-year U.S. Treas. bonds <u>1/</u>	6.38	6.58	6.77	5.93
Corporate new bond issues, Aaa adj. <u>8/</u>	7.95	8.10	8.22	7.08
Corporate seasoned bonds, Aaa <u>1/</u>	7.39	7.31	7.39	6.75
Municipal seasoned bonds, Aaa <u>1/</u>	5.75	5.80	5.83	4.95
FHA home mortgages, 30-year <u>3/</u>	--	8.40	8.40	8.05
Common stocks, S&P composite series <u>4/</u>				
Prices, closing (1941-43=10)	96.25	94.29	105.94	91.83
Dividend yield (per cent)	3.31	3.36	3.42	2.98
<hr/>				
	Latest month	Amount	3-month average	Change from year earlier Latest 3-month month average
New Security Issues (N.S.A., \$ millions)				
Corporate public offerings <u>5/</u>	Nov. '69	1,500e	1,693e	95e 339e
State & local govt. public offerings	"	1,000e	908e	-21e -657e
Comm. & fin. co. paper (net change in outstandings) <u>6/</u>	Aug. '69	+1,130r	+1,390	+142r +618
<hr/>				
	Latest month	Out-standings Latest month	Change Latest 3-month average	Annual rate of change from Pre-ceding 3 months ago 12 months ago
Banking (S.A.)				
		(\$ billions)		(per cent)
Total reserves <u>1/</u>	Sept. '69	27.39	- .01	- 0.22 - 0.4 - 9.6 + 0.3
Credit proxy <u>1/ 10/</u>	"	285.8	+ 0.5	- 2.3 + 2.1 - 9.3 - 1.1
Bank credit, total <u>6/</u>	"	394.7	- 0.7	- 0.2 - 2.1 - 0.5 + 4.0
Business loans	"	104.0	+ 0.3	+ 0.5 + 3.5 + 5.5 +12.6
Other loans	"	166.4	+ 0.9	+ 0.3 + 6.5 + 2.4 + 6.5
U.S. Govt. sec.	"	54.5	- 2.1	- 0.5 -44.5 -10.7 -14.8
Other securities	"	69.8	+ 0.2	- 0.5 + 3.4 - 7.9 + 4.5
Total liquid assets <u>1/ 6/ 11/</u>	"	720.0	+ 2.2	+ 0.3 + 3.7 + 0.4 + 4.1
Demand dep. & currency <u>1/</u>	"	199.2	+ 0.1	+ 0.1 + 0.6 + 0.4 + 4.1
Time & sav. dep., comm. banks <u>1/</u>	"	194.2	- 0.3	- 2.2 - 1.9 -13.2 - 1.1
Savings, other thrift instit. <u>6/</u>	"	201.6	+ 1.1	+ 0.6 + 6.6 + 3.2 + 4.5
Other <u>6/ 7/ 11/</u>	"	125.0	+ 1.3	+ 1.8 +12.6 +18.4 +14.3

N.S.A. - Not seasonally adjusted. S.A. - Seasonally adjusted. e - Estimated.
1/ Average of daily figures. 2/ Average for statement week ending October 15. 3/ Latest figure is monthly average for September. 4/ End-of-week closing prices; yields are for Friday. 5/ Corporate security offerings include both bonds and stocks. 6/ Month-end data. 7/ U.S. savings bonds and U.S. Government securities maturing within 1 year. 8/ Adjusted to Aaa basis. 9/ Federal funds data are 7-day averages for week ending Sunday: latest figure is for week ending October 19. 10/ Reflects \$400 million reduction in member bank deposits resulting from withdrawal of a large country bank from System membership in January 1969. Percentage annual rates are adjusted to eliminate this break in series. 11/ Reflects \$1.7 billion increase beginning January 1969 in U.S. Government securities maturing within 1 year to conform to the new Budget concept. Percentage annual rates are adjusted where necessary.
r - Revised.

U.S. BALANCE OF PAYMENTS
(In millions of dollars)

	1968				1969				
	Year ^{1/}	II ^{2/}	III ^{3/}	IV ^{4/}	I ^{5/}	II ^{6/}	July ^{7/}	Aug. ^{8/}	Sept. ^{9/}
Good and services, net ^{1/}	2,516	841	909	301	363	283	n.a.	n.a.	
Trade balance ^{2/}	626	264	313	-75	-103	-7	54	75	
Exports ^{2/}	33,598	8,395	8,879	8,383	7,469	9,588	3,100	3,235	
Imports ^{2/}	-32,972	-8,131	-8,566	-8,458	-7,572	-9,595	-3,046	-3,160	
Service balance	1,890	577	596	376	466	290			
Remittances and pensions	-1,159	-274	-325	-285	-271	-286			
Govt. grants & capital, net	-3,955	-1,055	-968	-835	-793	-1,103			
U.S. private capital	-5,157	-1,537	-1,868	-947	-1,345	-1,962			
Direct investment	-3,025	-1,009	-1,262	-283	-928	-1,101			
Foreign securities	-1,266	-164	-337	-455	-323	-426			
Banking claims	269	243	-90	-120	78	-473	*330	*50	
Other	-1,134	-607	-179	-89	-172	38			
Foreign capital	9,277	2,645	2,515	2,902	3,349	4,340			
Official foreign, nonliquid	2,407	937	433	709	-42	-272			
Official foreign, liquid	-3,099	-2,186	-55	22	-1,132	-578			
Int'l and reg., liq. & nonliq. ^{3/}	235	-97	78	273	96	21			
Foreign private non-bank, liq.	374	103	44	223	-23	-147			
Foreign commercial banks, liq.	3,382	2,297	702	-74	2,959	4,787			
New direct invest. issues ^{4/}	2,129	585	586	378	401	145			
Other	3,849	1,006	727	1,371	1,090	384			
Errors and omissions	-642	-480	309	-60	-1,254	-973			
Balances, with and without seasonal adjustment (deficit -)									
Official settlements balance, S.A.		1,553	97	367	1,143	1,234			
Seasonal component		-3	-25	-442	567	-29			
Balance, N.S.A. ^{5/}	1,638	1,550	72	-75	1,710	1,205	291	-652	
Liquidity balance, S.A.		9	-139	862	-1,668	-3,850			
Seasonal component		96	-269	-124	395	64			
Balance, N.S.A.	168	105	-408	738	-1,273	-3,786	-1,221	-1,177	
Adjusted over-all balance, S.A. ^{6/}		-751	-613	464	-1,824	-3,560			
Seasonal component		96	-269	-124	395	64			
Balance, N.S.A.	-1,744	-655	-882	340	-1,429	-3,496	-1,191	-1,071	
Financed by: Liab. to comm. banks abroad, N.S.A. (decrease -)	3,382	2,205	954	-415	3,139	4,701	1,482	419	
Official settlements, N.S.A. ^{7/}	-1,638	-1,550	-72	75	-1,710	-1,205	-291	652	
Reserve changes, N.S.A. (decrease -)									
Total monetary reserves	880	137	571	1,076	48	299	-121	259	548
Gold stock	-1,173	-22	74	137	-56	317	-9	10	10
Convertible currencies	1,183	-267	474	575	73	-246	-189	233	398
IMF gold tranche	870	426	23	364	31	228	77	16	140

^{1/} Equals "net exports" in the GNP, except for latest revisions.

^{2/} Balance of payments basis which differs a little from Census basis.

^{3/} Long-term deposits and Agency securities.

^{4/} New issues sold abroad by U.S. direct investors.

^{5/} Differs from liquidity balance by counting as receipts (+) increase in liquid liabilities to commercial banks, private nonbanks, and international institutions (except IMF) and by not counting as receipts (+) increases in certain nonliquid liabilities to foreign official institutions.

^{6/} Represents the net result of all international transactions of the U.S. other than changes in reserve assets, in all liabilities to foreign monetary authorities and in liabilities to commercial banks abroad (including U.S. bank branches) reported by banks in the U.S.

^{7/} Minus sign indicates decrease in net liabilities.

* Not seasonally adjusted.

THE ECONOMIC PICTURE IN DETAIL

Domestic Nonfinancial Scene

Gross national product. Gross national product is estimated to have risen by \$17.5 billion in the third quarter, as compared with an increase of about \$16 billion in the second. The larger rise last quarter reflected the Federal pay raise (\$3 billion, annual rate) and an increase in inventory accumulation of \$2.5 billion. Private final sales (GNP less government purchases and inventory accumulation) rose \$3 billion less than in the second quarter. In real terms, GNP growth in the third quarter was at an annual rate of 2 per cent, the same as in the second quarter.

Despite the somewhat faster rise in current dollar GNP, most sectors of demand continued to weaken during the third quarter, and there was a perceptible reduction of pressure on resources. A decline in construction activity, continued sluggishness of retail sales, curtailed Federal spending for defense and a slower growth in State and local expenditures were reflected in a reduction in industrial output in the past two months, and some easing in demand for labor. Moreover, the apparent rise in inventory investment in the third quarter and high inventory-sales ratios in durables suggest that production is out of line with demand in some key sectors, and that further adjustments of output and employment may be in prospect. At the same time, business capital spending has continued to grow, and there was little evidence of significant reduction in inflationary pressures.

The available evidence continues to point to a substantially smaller increase in GNP in the fourth quarter. There are additional indications that the Federal government is working hard to hold the line on spending, and without the effect of the pay raise which increased Federal outlays last quarter, declines in Federal purchases are likely to resume. State and local expenditures already have been affected by the limited availability of funds and by high interest rates. Growth of such spending was \$1 billion less in the third quarter than in the second, and increases are likely to continue to run well below the \$3.5 - 4.0 billion average quarterly increase of the first half of 1969.

Construction activity, as well, is expected to be further affected by the continued monetary restraint. Investment in residential structures was down \$1.6 billion in the third quarter, and an additional reduction of \$1 billion is expected in the current quarter. The third quarter drop in housing starts (which lead housing activity) was somewhat less than we had anticipated; the decline in activity was apparently moderated temporarily by large commitments and efforts of builders to accelerate starts in the face of tightening money markets and rising interest rates. But now, with available commitments reduced, the decline in starts is expected to be sharper this quarter. We are projecting an annual rate of 1.25 million starts for the current quarter and further reductions in the first half of next year.

Business investment continued relatively strong in the third quarter, but there were indications that the slower growth forecast by businessmen for the current quarter in the last Commerce-SEC Survey will be confirmed. The recent leveling off in output of machinery and equipment and the relatively flat trend of new orders this year, despite the rise in September, suggest a more moderate growth of capital outlays in the near future.

The outlook for consumer demand remains most in question. Gains in consumer expenditures slowed in the third quarter despite a sharp increase in disposable income, and the saving rate rose to 6.4 per cent from 5.3 per cent in the preceding quarter. It would not be surprising, therefore, if consumption increased somewhat faster in the fourth quarter, with some decline in the saving rate. But retail sales so far in October have remained relatively weak. Moreover, with employment growth and gains in personal income expected to continue to slow, it is unlikely that increases in consumption in the next few months will be large enough to offset the waning strength of the government and business sectors, and a further substantial drop in growth of final sales appears likely in the current quarter. We expect that production adjustments will lag the weaker final sales increase, and that inventory accumulation will continue at about the third quarter rate, but that more of the additional stock-building will be involuntary.

GNP growth in real terms is likely to come to a halt in the first half of next year. With money markets continuing under restraint,

it seems fairly clear that we will see a substantial further reduction of housing activity early next year, with starts off perhaps to an annual rate of around 1 million units by the second quarter. Similarly, growth of State and local government spending is likely to continue to be limited by the problems of financing in tight capital markets. Some downward adjustments of business investment plans for 1970 also seem probable in view of limited availability of funds, high interest rates and declining profits, particularly if, as we assume, the investment tax credit is removed by the end of this year.

Disposable income and consumption will get a boost on January 1, when the surcharge is scheduled to be cut. Our projections assume reduction of the tax to 5 per cent for the first half of 1970, which adds about \$4.4 billion (annual rate) to disposable income in the first quarter; elimination of the surcharge entirely would double the amount. A further lift to disposable income is expected in the second quarter when a proposed increase in Social Security benefits could add another \$3 billion. But these increases in disposable income are likely to be moderated by slower growth of employment and cuts in the workweek. Thus, we expect that increases in consumption will be moderate in the first half of 1970, and that the saving rate will be only slightly below the third quarter.

The rate of inventory accumulation should slow markedly as businessmen adjust their production schedules to the reduced growth of final sales. Under such conditions, real GNP is expected to show

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income
figures are billions of dollars, with quarterly figures at annual rates.)

	1967	1968	1969 Proj.	1969*			1970*		
				I	II	III	Projected		II
				IV	I				
Gross National Product	793.5	865.7	932.5	908.7	924.8	942.3	954.3	961.8	968.8
Final sales	786.2	858.4	924.5	902.1	917.9	932.9	945.0	954.5	962.7
Private	606.1	658.1	709.2	692.1	705.0	715.1	724.7	733.3	741.1
Excluding net exports	600.9	655.6	707.4	690.6	703.4	713.1	722.3	730.6	737.8
Personal consumption expenditures	492.3	536.6	576.8	562.0	572.8	581.6	590.8	599.9	609.9
Durable goods	73.0	83.3	89.9	88.4	90.6	90.3	90.3	90.3	90.3
Nondurable goods	215.1	230.6	244.5	238.6	242.1	246.4	250.7	254.9	260.0
Services	204.2	222.8	242.5	235.0	240.1	244.9	249.8	254.7	259.6
Gross private domestic investment	116.0	126.3	138.6	135.2	137.4	140.9	140.8	138.0	134.0
Residential construction	25.0	30.2	31.8	33.3	32.7	31.1	30.1	28.0	25.2
Business fixed investment	83.7	88.8	98.8	95.3	97.8	100.5	101.7	102.7	102.7
Change in business inventories	7.4	7.3	8.1	6.6	6.9	9.4	9.3	7.3	6.1
Nonfarm	6.8	7.4	7.8	6.6	6.7	8.9	8.9	6.9	5.9
Net exports of goods and services	5.2	2.5	1.9	1.5	1.6	2.0	2.4	2.7	3.3
Gov't. purchases of goods & services	180.1	200.3	215.2	210.0	212.9	217.8	220.0	221.2	221.6
Federal	90.7	99.5	102.1	101.6	100.6	103.3	102.8	101.2	99.1
Defense	72.4	78.0	79.4	79.0	78.5	80.6	79.6	77.6	75.1
Other	18.4	21.5	22.7	22.6	22.1	22.7	23.2	23.6	24.0
State & local	89.3	100.7	113.1	108.5	112.3	114.5	117.2	120.0	122.5
Gross national product in constant (1958) dollars	674.6	707.6	728.2	723.1	726.7	730.4	732.6	731.8	731.1
GNP implicit deflator (1958=100)	117.6	122.3	128.1	125.7	127.3	129.0	130.3	131.4	132.5
Personal income	629.4	687.9	747.1	724.4	740.5	756.2	767.1	776.4	789.0
Wages and salaries	423.5	465.0	509.9	493.3	504.3	516.6	525.4	531.7	538.4
Disposable income	546.5	590.0	629.5	610.2	622.0	638.8	646.8	657.9	667.9
Personal saving	40.4	38.4	36.7	32.5	33.3	41.1	39.9	41.3	41.0
Saving rate (per cent)	7.4	6.5	5.8	5.3	5.3	6.4	6.2	6.3	6.1
Corporate profits before tax	80.3	91.1	93.0	95.5	95.4	91.7	89.5	85.5	80.5
Federal government receipts and expenditures (N.I.A. basis)									
Receipts	151.1	176.3	201.1	198.6	202.8	200.4	202.4	196.9	196.6
Expenditures	163.8	181.5	191.9	188.5	189.3	194.1	195.5	196.3	199.4
Surplus or deficit (-)	-12.7	-5.2	9.2	10.1	13.5	6.3	6.9	0.6	-2.8
Total labor force (millions)	80.8	82.3	84.2	83.7	83.8	84.6	84.8	85.0	85.3
Armed forces "	3.4	3.5	3.5	3.5	3.5	3.5	3.5	3.4	3.3
Civilian labor force "	77.2	78.7	80.7	80.2	80.3	81.1	81.3	81.6	82.0
Unemployment rate (per cent)	3.8	3.6	3.6	3.3	3.5	3.7	4.0	4.2	4.5
Nonfarm payroll employment (millions)	65.9	67.9	70.1	69.5	70.0	70.3	70.6	70.8	70.8
Manufacturing	19.4	19.8	20.2	20.1	20.1	20.3	20.2	20.1	19.9
Industrial production (1957-59=100)	158.1	165.4	172.7	170.2	172.7	174.2	173.8	172.8	172.0
Capacity utilization, manu- facturing (per cent)	85.3	84.5	84.0	84.5	84.6	84.1	83.0	81.5	80.2
Housing starts, private (millions A.R.)	1.29	1.51	1.48	1.72	1.51	1.42	1.25	1.13	1.00
Sales new domestic autos (millions, A.R.)	7.57	8.62	8.43	8.37	8.54	8.42	8.40	8.40	8.40

* Assumes Administration's proposals for repeal of investment tax credit and extension of tax surcharge at 10% through 1969 and then at 5% through June 1970.

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1967	1968	1969 Proj.	1969 ^{1/}				1970 ^{1/}	
				I	II	III	IV	Projected	
				I	II	III	IV	I	II
-----In Billions of Dollars-----									
Gross National Product	43.6	72.2	66.8	16.2	16.1	17.5	12.0	7.5	7.0
Inventory change	-7.4	-0.1	0.8	-3.9	0.3	2.5	-0.1	-2.0	-1.2
Final sales	51.1	72.2	66.1	20.1	15.8	15.0	12.1	9.5	8.2
Private	27.8	52.0	51.1	16.8	12.9	10.1	9.6	8.6	7.8
Excluding net exports	27.9	54.7	51.8	16.5	12.8	9.7	9.2	8.3	7.2
Net exports	-0.1	-2.7	-0.6	0.3	0.1	0.4	0.4	0.3	0.6
Government	23.3	20.2	14.9	3.3	2.9	4.9	2.2	1.2	0.4
GNP in constant (1958) dollars	16.5	33.0	20.6	4.6	3.6	3.7	2.2	-0.8	-0.7
Final sales	23.5	33.3	20.2	8.2	3.5	1.7	1.9	0.8	0.6
Private	10.0	24.9	18.5	7.8	3.9	1.9	2.3	1.1	1.5
-----In Per Cent Per Year-----									
Gross National Product	5.8	9.1	7.7	7.3	7.1	7.6	5.1	3.1	2.9
Final sales	7.0	9.2	7.7	9.1	7.0	6.5	5.2	4.0	3.4
Private	6.1	8.5	7.8	9.9	7.5	5.7	5.4	4.7	4.3
Personal consumption expenditures	5.6	9.0	7.5	8.2	7.7	6.1	6.3	6.2	6.7
Durable goods	3.1	14.1	7.9	9.7	10.0	-1.3	0.0	0.0	0.0
Nondurable goods	4.0	7.2	6.0	7.3	5.9	7.1	7.0	6.7	8.0
Services	8.3	9.1	8.8	8.5	8.7	8.0	8.0	7.8	7.7
Gross private domestic investment	-4.4	8.9	9.7	3.9	6.5	10.2	-0.3	-8.0	-11.6
Residential construction	0.0	20.8	5.3	17.6	-7.2	-19.6	-12.9	-27.9	-40.0
Business fixed investment	2.6	6.1	11.3	16.6	10.5	11.0	4.8	3.9	0.0
Gov't. purchases of goods & services	14.9	11.2	7.4	6.4	5.5	9.2	4.0	2.2	0.7
Federal	16.6	9.7	2.6	-1.2	-3.9	10.7	-1.9	-6.2	-8.3
Defense	19.3	7.7	1.8	-1.5	-2.5	10.7	-5.0	-10.0	-12.9
Other	7.6	16.8	5.6	1.8	-8.9	10.9	8.8	6.9	6.8
State & local	13.0	12.8	12.3	14.1	14.0	7.8	9.4	9.6	8.3
GNP in constant (1958) dollars	2.5	4.9	2.9	2.5	2.0	2.0	1.2	-0.5	-0.4
Final sales	3.6	5.0	2.9	4.6	2.0	0.9	1.1	0.4	0.3
Private	1.9	4.7	3.3	5.6	2.8	1.3 ^{2/}	1.6	0.8	1.0
GNP implicit deflator	3.2	4.0	4.7	4.7	5.1	5.5 ^{2/}	3.9	3.6	3.3
Personal income	7.2	9.3	8.6	7.4	8.9	8.5	5.8	4.8	6.5
Wages and salaries	7.4	9.8	9.7	9.3	8.9	9.8	6.8	4.8	5.0
Disposable income	6.8	8.0	6.7	3.9	7.7	10.8	5.0	6.9	6.1
Corporate profits before tax	-4.6	13.4	2.1	4.2	-0.4	-15.5	-9.6	-17.9	-23.4
Federal government receipts and expenditures (N.I.A. basis)									
Receipts	6.0	16.7	14.1	24.1	8.5	-4.7	4.0	-10.9	0.6
Expenditures	14.7	10.8	5.7	2.3	1.7	10.1	2.9	1.6	6.3
Nonfarm payroll employment	3.0	3.0	3.2	4.7	2.9	1.7	1.7	1.1	0.0
Manufacturing	1.0	2.1	2.0	4.0	0.0	4.0	-2.0	-2.0	-4.0
Industrial production	1.2	4.6	4.4	6.7	5.9	3.5	-0.9	-2.3	-1.9
Housing starts, private	10.9	16.7	-2.2	28.2	-48.3	-22.8	-48.9	-40.0	-44.4
Sales new domestic autos	-9.7	14.0	-2.2	-20.4	8.4	-5.7	-1.0	0.0	0.0

^{1/} Assumes Administration's proposals for repeal of investment tax credit and extension of tax surcharge at 10 % through 1969 and then at 5 % through June 1970.

^{2/} Excluding Federal pay increase 4.2 per cent.

virtually no growth, or to decline slightly, in the first half of next year. As pressures on resources ease, the rate of increase in the GNP deflator is likely to slow somewhat; we are projecting a rate of increase of under 3-1/2 per cent by the second quarter.

Industrial production. Industrial production in September dipped 0.3 per cent further to 173.8 per cent of the 1957-59 average. The decline, as in August, was due in part to special factors. Auto assemblies, largely because of strikes, declined 5 per cent from an annual rate of 9.1 million units in August to 8.7 million units in September. While production schedules for October were set at a 9.0 million unit rate, some strikes have continued so far this month. The drop in autos plus declines in industrial chemicals (essentially synthetic fibers), coal, crude oil, and residential electricity accounted for the easing in the total index, as output of business equipment and most other industrial materials was about unchanged.

The turn around in industrial production from an increase of 3.2 per cent from January to July, to a decline of 0.5 per cent from July to September is fairly abrupt. The extent of the recent decline, however, is considerably less than in the first two months of the 1967 "mini-recession" and the relatively sharp recession in 1958. In the 1967 slowdown, the decline was preceded by 3 months of leveling out and in 1957 by 11 months of little change.

INDUSTRIAL PRODUCTION

	Per cent change		Number of months of decline from peak to trough
	First two months of	Total decline from peak to trough	
1957-58 Recession	- 3.2	14.2	8
1966-67 Slowdown	- 1.8	2.4	6
<u>Memorandum:</u>			
1969 Decline, August-Sept.	- 0.5		

The outlook for industrial production in the fourth quarter is for further declines, probably at a somewhat accelerated rate. Production schedules for autos, if met, call for a reduction from a 9.0 million unit rate in October to 8.2 million in December. With consumer demand continuing sluggish, some further cutback in output of consumer goods is probable. Production of business equipment is likely to show little change from current levels and output of defense equipment to continue to decline. Under these conditions, demand for and production of industrial materials should weaken.

Retail sales. Despite a strong pickup in the automotive group, retail sales in September and the first two weeks in October suggest that consumers have continued to exercise the moderation in spending which has been evident since last fall. Even though total retail sales in September rose almost 1 per cent from August, according to present data this only brought the level 2.4 per cent above January and 3 per cent above a year earlier. Sales in the first two

weeks in October were only about 2-1/2 per cent above a year earlier. In real terms, October may be the fifth consecutive month that sales have been below 1968 levels.

Sales at durable goods stores rose 3 per cent from August, as the automotive group increased 4.6 per cent and furniture and appliance sales rose 1.3 per cent. Part of the strength in new car sales is probably attributable to larger than normal fleet purchases, but the importance of fleet sales will not be known for some weeks. Sales at nondurable goods stores on average were unchanged from August, although sales at department stores declined for the second month.

Next month the Census Bureau plans to revise its seasonal factor for the automotive group of stores. The new seasonal factors are expected to lower automotive sales in the first part of the year and increase the level in recent months.

Sales of new domestic autos in the first 10 days of October were at a seasonally adjusted annual rate of 8.5 million units, 4 per cent above the first 10 days of September, but 11 per cent below a year earlier. The early October sales represent a sharp drop from the final 10 days of September when introductions of new models resulted in record sales.

Stocks of new autos on October 10 totaled 1.4 million units (not seasonally adjusted), 3 per cent above 10 days earlier and 12 per cent above a year earlier.

Sales of used cars for the month of September were 6 per cent more than in August, seasonally adjusted, and 4 per cent above last year. Auction prices of used cars in September were up 3 per cent from August.

QUARTERLY PERCENTAGE CHANGES IN THE SALES OF
RETAIL STORES
(Change from previous quarter)

	I	II	III
All retail stores	1.6	1.2	0.0
Total, less automotive	1.7	1.4	0.3
Durable	1.9	0.6	-2.9
Nondurable	1.4	1.4	1.4
Food group	2.3	-0.6	1.7
Department stores	0.8	4.6	1.4
All retail stores - Real *	0.8	-0.4	-1.3

* Deflated by all commodity CPI; third quarter estimated.

Consumer credit. Consumer instalment credit outstanding increased at a seasonally adjusted annual rate of \$7.3 billion in the July-August period, compared with \$9 billion in the first half of 1969. The smaller rise in recent months is attributable to a marked reduction in growth of auto credit--from a \$2.9 billion rate in the first half of the year to \$1.1 billion this summer.

Auto credit developments have largely reflected variations in unit sales, product mix, and prices; there have been no significant changes in contract terms. On a seasonally adjusted basis, the proportion of new car contracts with maturities over 30 months--mostly

36 month contracts--held by sales finance companies edged up to 84 per cent this summer from 83.2 per cent in the first half of the year.

Data from commercial banks indicate a slightly larger but partly seasonal increase in maturities. As compared to a year or two earlier, both sales finance companies and commercial banks are writing somewhat higher proportions of their new car contracts for amounts in excess of the dealer cost of the unit financed.

NEW CAR FINANCING
(Per cent of contracts, monthly averages)

	Sales finance companies <u>1/</u>	Commercial banks <u>2/</u>
<u>Over 30 months maturity</u>		
1967: Jan.-June	82.7	78.1
July-August	82.7	80.6
1968: Jan.-June	83.3	78.6
July-August	83.8	80.4
1969: Jan.-June	83.2	80.5
July-August	84.0	81.7
<u>Over 100 per cent of dealer cost</u>		
1967: Jan.-June	23.8	21.1
July-August	23.9	22.1
1968: Jan.-June	23.7	19.6
July-August	23.3	19.3
1969: Jan.-June	24.4	22.8
July-August	24.5	24.6

1/ Seasonally adjusted.

2/ Reduced sample basis in 1969 as compared with 1967 and 1968.

Inventories. The rate of inventory accumulation dropped in August at both manufacturing and trade establishments. In part this

reflected a substantial drop in inventories at wholesalers, reportedly in part associated with shipments of cotton abroad under Public Law 480. Accumulation slowed substantially at manufacturers and was somewhat reduced at retail establishments.

CHANGE IN BOOK VALUE OF BUSINESS INVENTORIES
Seasonally adjusted annual rates, billions of dollars

	1969			
	Q II	July-August average	July	August
Manufacturing and trade, total	11.1	10.7	15.3	6.0
Manufacturing, total	7.6	8.6	11.4	5.8
Durable	6.0	7.4	11.5	3.2
Nondurable	1.6	1.2	- 0.1	2.6
Trade, total	3.5	2.1	3.9	0.2
Wholesale	1.8	- 2.3	- 1.3	- 3.2
Retail	1.7	4.4	5.2	3.4
Durable	- 0.7	1.4	- 0.1	2.8
Nondurable	2.4	3.0	5.3	0.6

The OBE preliminary estimate of a \$9.4 billion rate increase in inventories (after valuation adjustment) in the third quarter implies a return in September to around the July rate of book value increase. The estimated third-quarter rate of accumulation could not be long sustained without a considerable increase in orders and sales. Unless this occurs, a slowdown in inventory investment by the turn of the year is likely.

INVENTORY RATIOS

	1966		1969		
	Sept.	Dec.	April	July	Aug.
<u>Inventories to sales:</u>					
Manufacturing & trade, total	1.50	1.56	1.54	1.55	1.54
Manufacturing, total	1.65	1.72	1.71	1.70	1.71
Durable	1.89	2.00	2.00	2.04	2.03
Nondurable	1.35	1.37	1.34	1.28	1.31
Trade, total	1.34	1.39	1.36	1.38	1.36
Wholesale	1.15	1.22	1.19	1.20	1.16
Retail	1.46	1.51	1.46	1.51	1.50
Durable	2.01	2.10	2.04	2.12	2.13
Nondurable	1.19	1.23	1.19	1.23	1.21
<u>Inventories to unfilled orders:</u>					
Durable manufacturing	.617	.639	.687	.711	.718

The over-all inventory-sales ratio declined in August, mainly because of the drop in wholesale inventories combined with the associated rise in sales. The retail ratio also declined, but the decline was mainly at food and other staples stores; stocks rose relative to sales at automotive dealers and at G.A.F. stores.

The trade inventory-sales ratio has fluctuated in a rather narrow band since late 1966; it is high by the standards of 1962-65, but has not shown in recent months the kind of sustained upward movement that preceded the 1960 downturn or the 1966 slowdown. It is not a very consistent leading indicator, however; at mid-1957 it had been fluctuating around 1.35, with a downward tendency, for a year and a half. The manufacturing durable goods inventory-backlog ratio, whose

rise signaled past recessions and the 1967 slowdown with leads ranging from 3 to 11 months, rose in August for the fourth month.

Residential construction and real estate. Seasonally adjusted private housing starts, which were revised upward to show a slight rise for August, increased a tenth further in September to an annual rate of 1.52 million units. While the September rate was the highest since April, like the greater than expected month-to-month drop initially reported for July, it can be largely discounted on the basis of special seasonal adjustment problems and other factors typically associated with the monthly series. Concentrating on the quarterly series--a much more reliable indicator of trend--starts in the third quarter were at an annual rate of 1.42 million, down 6 per cent from the second quarter rate and 17 per cent below the recent peak reached in the first quarter of the year.

Based on the third quarter averages, the downtrend continued to be less pronounced for multifamily units than for single-family units, as shown in the table, reflecting in part the greater willingness and ability of multifamily builders to compete for funds in this year's increasingly stringent credit markets. Regionally, starts moved counter to the general decline only in the North Central states where an upward adjustment in usury ceilings had helped to produce a short-lived spurt in starts earlier in the third quarter. In the Northeast, where usury ceilings have become a particularly limiting factor, starts showed by

far the greatest further drop and were the lowest since the fourth quarter of 1966.

PRIVATE HOUSING STARTS AND PERMITS

	QIII 1969 (Thousands of units) <u>1/</u>	Per cent change from	
		Q II 1969	Q III 1968
Starts	1,424	- 6	- 8
1-family	774	- 7	-14
2-or-more-family	650	- 5	+ 1
Northeast	179	-27	-38
North Central	348	+ 5	- 3
South	562	- 5	- 3
West	334	- 4	+15
Permits	1,213	-12	- 8
1-family	567	-12	-17
2-or-more-family	651	-13	+ 1

1/ Seasonally adjusted annual rates; preliminary.

Some acceleration in the starts decline is expected during the current quarter in view of the further attrition indicated in outstanding mortgage commitments in recent months and the persistent reduction in building permits since April. Even so, the seasonally adjusted average for the quarter as a whole may hold at least somewhat above a 1.2 million annual rate. A lower average than that appears unlikely given the fact that unadjusted starts normally show a sharp seasonal drop after October, and considering the probability that, under presently reduced housing-supply conditions, builders with commitments may continue efforts to move ahead of normal schedules.

New orders. The Greenbook Supplement will carry a more detailed account of manufacturers' new orders of durable goods in September, but the major results are as follows:

1. Such orders rose 5.9 per cent from August to a new high.
2. Increases were widespread, with a decline in defense orders a major exception.

3. The most striking development was an increase of 17 per cent in orders for machinery and equipment. Orders for nonelectrical machinery were up 10 per cent while orders in the "other" subgroup of transportation equipment rose 78 per cent, primarily reflecting, to our present knowledge, an upsurge for ships. Orders for electrical machinery were off slightly.

4. For the third quarter as a whole, total durable goods orders were up about 4 per cent from the second quarter, but orders for machinery and equipment did not quite equal the volume of the preceding quarter.

5. Shipments were up about 2.5 per cent and unfilled orders returned to close to their high earlier in the summer. For machinery and equipment, backlogs did advance to a new high.

Labor market. The labor market has eased in recent months from the extremely tight situation that prevailed last winter, and a further weakening appears likely. Employment growth has slowed measurably and, as demands for labor tapered off, the unemployment rate moved up from 3.3 per cent in the first quarter to 3.7 per cent in the third. Unemployment rates for most groups showed relatively steady increases after the end of the first quarter with the rate for men in prime working ages (25 years and over), edging up from 1.5 per cent in February to 1.9 per cent in September. Claims for unemployment insurance, reflecting the rise in joblessness among covered workers, have risen slowly since spring and in the most recent four-week period averaged about 5 per cent higher than a year earlier.

Nonfarm employment rose by only 100,000 over the three months ending in September. Limits on Federal expenditures resulted in a decline in Federal employment between June and September, while construction employment edged down in response to reduced residential building. Further declines are anticipated in these two sectors. State and local government employment also declined slightly, but advances are likely in the months ahead.

NONFARM PAYROLL EMPLOYMENT
(In Thousands, Seasonally Adjusted)

	1969 Average Monthly Changes		
	December- March	March- June	June- September
Total	278	197	33
Government	33	42	- 31
Private industry	245	154	64
Construction	15	31	- 25
Manufacturing	55	25	31
All others	175	98	58

In manufacturing, employment increased at a relatively steady pace, with the bulk of the rise occurring in the five major metal-producing and metal-using industries. In the construction-related and non-durable goods categories employment has shown no increase over the last six months. In defense-related manufacturing industries, employment declined slightly over the period with the largest decline in ordnance.

Growth of total wage and salaries averaged \$3.5 billion per month over the summer--only slightly less than in the early part of the year. But the Federal pay raise accounted for about one-fourth of the average monthly rise, while the growth rate of private wages and salaries fell off sharply in nonmanufacturing industries. This pattern was in line with the markedly slower growth of employment in these industries. On the other hand, manufacturing payrolls have continued to expand steadily. Proprietors' income stayed level this summer after rising strongly in the March to June period, while income from such sources as rent, interest and dividends continued to increase.

Personal income increased only \$2.3 billion in September compared to \$6.1 billion in August. But the disparity in the two changes reflects in large part a temporary situation in autos, where the early model changeover probably had the effect of advancing some of the payroll rise in this industry into August.

PERSONAL INCOME
(Billions of dollars, seasonally adjusted)

	1959 Average Monthly Changes		
	Dec. - March	March- June	June- Sept.
Personal income	4.9	5.1	4.6
Wage and salary disbursements	4.0	3.5	3.5
Government	0.5	0.5	1.4
Private	3.5	3.0	2.1
Manufacturing	1.0	1.0	0.9
Nonmanufacturing	2.5	2.0	1.2
Other sources of income	0.8	1.7	1.1

Industrial relations. In the first of a major round of important collective bargaining negotiations--which will also include the railroad, trucking, rubber, and auto industries--negotiations appear to have reached a stalemate at General Electric. The first company offer was rejected and it appears likely that the workers will strike after the current contract expires October 26. In addition to improved fringe benefits, the company had offered a 6 per cent across-the-board first-year wage increase and reopenings on wages in the second and third contract years.

Skilled workers were offered an additional 5 to 25 cent increase in the first year. The company's offer came far from meeting the union's wage demands which average close to 10 per cent per annum over a 2-1/2 year contract term, and include an additional 50 cent first year increase for skilled workers.

Negotiations at American Motors with 10,000 members of the UAW did not result in settlement before the old contract expired and the workers went on strike October 16. The main economic issues have been decided and workers will vote on a package which provides an 8 per cent increase in wages and benefits as soon as the negotiators clean up a variety of local plant issues. The threatened strike of 120,000 members of shopcraft unions against seven major railroads on October 4 was averted for 60 days by the President's appointment of an Emergency Board. The unions are seeking a substantial wage increase retroactive to January 1, 1969.

Wholesale prices. Average wholesale prices of all commodities this past quarter rose at a substantially slower pace than in the previous two quarters, as may be seen in the table. But this deceleration in the over-all average blurs two important developments: (1) a faster rise in average industrial prices, which was largely offset by (2) a decline in prices of foods and foodstuffs following an extraordinarily sharp spring increase. These recent gyrations in farm and food prices are attributable to a very rapid run-up in livestock and meats and a subsequent easing. So

far as industrial commodities are concerned, price increases in the third quarter were widespread. Particularly important were large advances in prices of steel mill products and nonferrous metals. An important exception was lumber and plywood, for which substantial price declines continued but far smaller than in the spring.

WHOLESALE PRICES
(Percentage changes at annual rates)

	Dec. 1968 to March 1969	March 1969 to June 1969	June 1969 to Sept. 1969
All commodities	6.8	5.2	1.6
Industrial commodities	6.4	0.8	3.6
Materials	8.4	0.4	4.4
Steel mill products	9.6	4.0	9.6
Nonferrous metals	20.8	17.2	23.6
Lumber & plywood	61.2	-78.4	-28.0
Finished products	2.8	2.4	2.8
Foods and foodstuffs	9.2	18.8	- 4.4

Wholesale prices rose 0.2 per cent from mid-August to mid-September, 0.1 percentage point more than the original BLS estimate. Industrial commodity prices increased 0.4 per cent, somewhat more than estimated earlier, as prices for more than one-half of the industrial product classes advanced, but prices of farm and food products declined 0.3 per cent and held down the increase in the total index.

Price increases for metals--especially nonferrous--accounted for about one-half of the increase in industrial prices last month. Increases in prices of machinery and equipment were at the fastest rate since November 1966 and were responsible for about one-fourth of the over-all rise. But sizable price increases were also registered for other commodities, including apparel and some paper products. Prices of lumber declined for the fifth consecutive month, but plywood rose for the first time since March.

Since mid-September, price increases have been announced for a variety of commodities, including steel mill products, chemicals, aluminum ingot and mill products, autos, tires, and major home appliances. Prices of steel scrap declined during this period as ample supplies interacted with reduced demand by steel mills.

Livestock prices dropped sharply from mid-August to mid-September and were primarily responsible for the decline in prices of farm and food products. Livestock prices are now at about the mid-September level. Prices for meats were also lower over the month to mid-September, and declined further in the latter part of the month.

Consumer prices. Despite a sharp rise in September consumer prices rose somewhat less rapidly in the quarter just ended than in the second quarter, mainly because food prices were up significantly less. Also, prices of new and used autos declined. Prices of other durable goods continued to rise. The rate of advance in service prices

accelerated somewhat, despite a less rapid rise in mortgage rates. The third quarter increase was also smaller than in the first quarter, mainly because of an exceptionally large rise in used car prices which raised significantly the first quarter average. Most major groups except some services, increased more rapidly than in the first quarter.

From August to September consumer prices advanced at an annual rate of about 6 per cent, somewhat more than for the third quarter as a whole. Food prices rose only a little, but after allowance for seasonal influences the increase was considerable. There were sharp advances in the price of meats and in the cost of restaurant meals. Fruit and vegetable prices dropped less than seasonally.

Apparel prices rose markedly in September, with only part of the increase reflecting the usual seasonal influences. Prices of both new and used cars fell prior to the introduction of new models. The cost of consumer services continued to rise rapidly, with further advances in mortgage interest rates, household services, and medical care.

SIGNIFICANT CONSUMER PRICE CHANGES
(Per cent, at annual rates)

	Quarters			August 1969 to Sept. 1969
	Dec. 1968 to March 1969	March 1969 to June 1969	June 1969 to Sept. 1969	
All items	6.0	6.4	5.2	6.0
Food	4.0	10.0	6.4	1.2
Apparel and upkeep	2.0	6.8	5.2	20.4
Durable goods	8.8	2.0	- 0.4	- 3.6
Services	8.0	6.8	7.6	8.4
Mortgage interest rates	13.6	16.8	9.6	9.6
Addendum:				
Selected components, seasonally adjusted				
Food	4.0	8.8	5.2	7.2
Apparel and upkeep	5.2	5.2	4.8	9.6

Farm income and production prospects. Farmers' net realized incomes averaged \$1.1 billion above a year earlier (seasonally adjusted annual rate) during the first three quarters of 1969, and the year promises to be the most profitable for farmers since 1966. The major factor in this gain through the third quarter was a sharp rise in prices of livestock products in response to a leveling out in marketings. The margin over a year ago in net income may narrow in the fourth quarter as prices of crops, and possibly broilers, sag under the impact of heavy marketings but prices of most livestock products are expected to continue strong.

FARM INCOME, PRICES RECEIVED & MARKETINGS

	1969		Per cent change from 1968	
	QIII	Average: 1st 3 quarters	QIII	Average: 1st 3 quarters
<u>Farm income</u>				
Gross realized income	55.3	54.4	6.8	6.9
Minus: Production expenses	38.8	38.5	6.3	6.6
Net realized income	16.5	15.9	7.8	7.4
Indexes, 1957-59=100				
<u>Prices received by farmers</u>				
Total	115.3	113.6	5.8	5.7
Livestock and products	128.0	123.1	12.0	11.0
Crops	98.3	101.0	- 3.0	- 2.1
<u>Volume of marketings</u>				
Total	133.0	113.6	0.2	1.0
Livestock and products	126.1	121.6	- 0.2	0
Crops	142.3	102.9	0.9	2.6

With crops largely matured, total crop output about 1 per cent above last year's record was virtually assured by October 1 conditions. Shifts in prospects during September were largely offsetting with deterioration in cotton balanced by general improvement in feed crops and soybeans. Since the October 1 survey, a severe freeze extending to the Texas Panhandle has hurt some crops, but this damage is not likely to reduce national output prospects.

Cotton crop prospects are down to 10.5 million bales, about one-half million bales below expected use, but prices are likely to hold stable because trade stocks are large, demand is down, and next year's

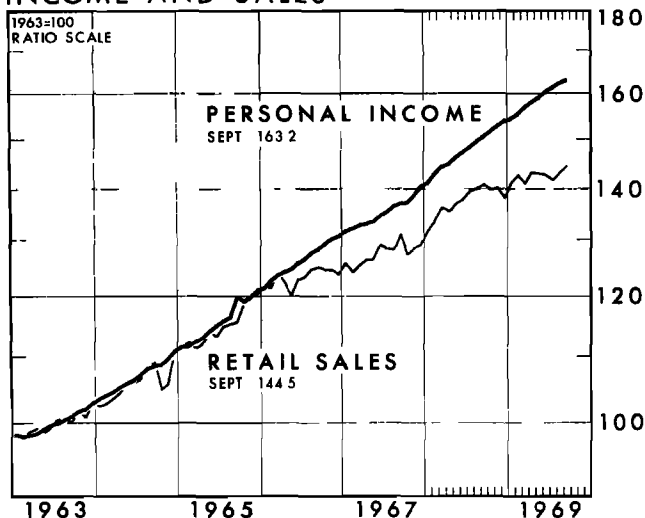
program calls for a big increase in acreage. Plentiful supplies of vegetables and fruits, items accounting for more than a fifth of consumer food budgets, were in prospect on October 1.

In the fourth quarter red meat production is expected to equal that of a year earlier, with expansion in beef offset by declining veal and lamb output and by a sharp cut in pork if the predicted cutback in hog marketings materializes. Production of milk and poultry products, especially broiler and turkey meat, is expected to exceed a year earlier. These trends are likely to extend into the first quarter of 1970 with pork output down sharply at least through January. A survey released on October 17 showed 10 per cent more cattle on feedlots than a year earlier, substantiating earlier indications of large marketings of fed cattle throughout the fall and also suggesting that large marketings may continue in the January-March period.

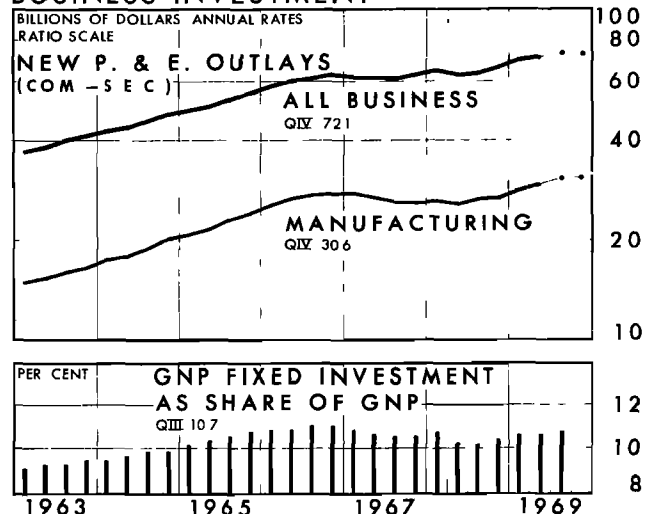
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

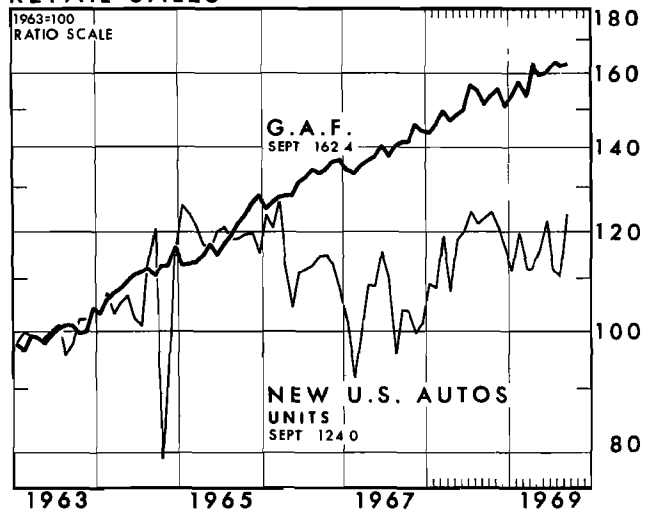
INCOME AND SALES



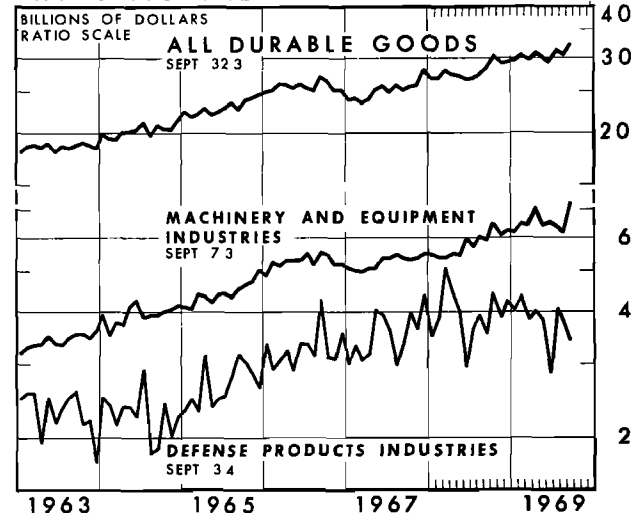
BUSINESS INVESTMENT



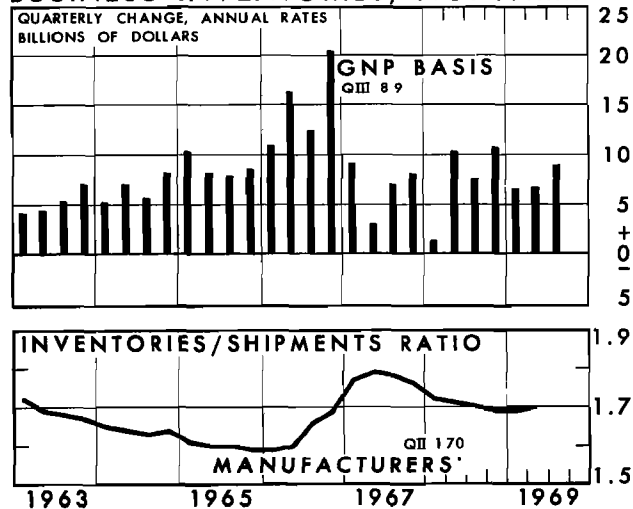
RETAIL SALES



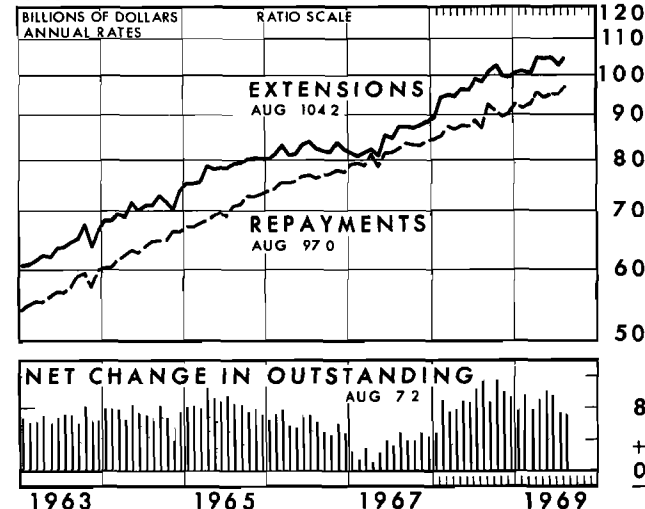
MANUFACTURERS' NEW ORDERS



BUSINESS INVENTORIES, NONFARM



INSTALMENT CREDIT



 THE ECONOMIC PICTURE IN DETAIL

Domestic Financial Situation

Bank credit. Commercial bank credit declined moderately in September as a comparatively sharp drop in holdings of U.S. Treasury securities more than offset a fairly strong rise in total loans and a modest increase in other investment holdings. Weekly reporting bank data suggest that bank credit leveled out during late September and the early part of October as further growth in loans about matched investment reductions. It may then have increased to some extent as banks acquired a larger proportion of the TAB's issued by the Treasury on October 14, for which 50 per cent of payment could take the form of credit to tax and loan accounts.

NET CHANGE IN BANK CREDIT
 All Commercial Banks
 (Seasonally adjusted percentage change, at annual rates)

	1968	1969		
	Year	1st 5 months	June-September	September
Total loans & investments ^{1/}	11.0	3.9	-0.7	-2.1
U.S. Gov't. securities	3.0	-21.5	-8.0	-44.5
Other securities	16.4	--	-6.3	3.4
Total loans	11.6	11.2	2.3	5.3
Business loans	11.1	16.8	4.1	3.5
Other loans	11.9	7.7	1.3	6.5

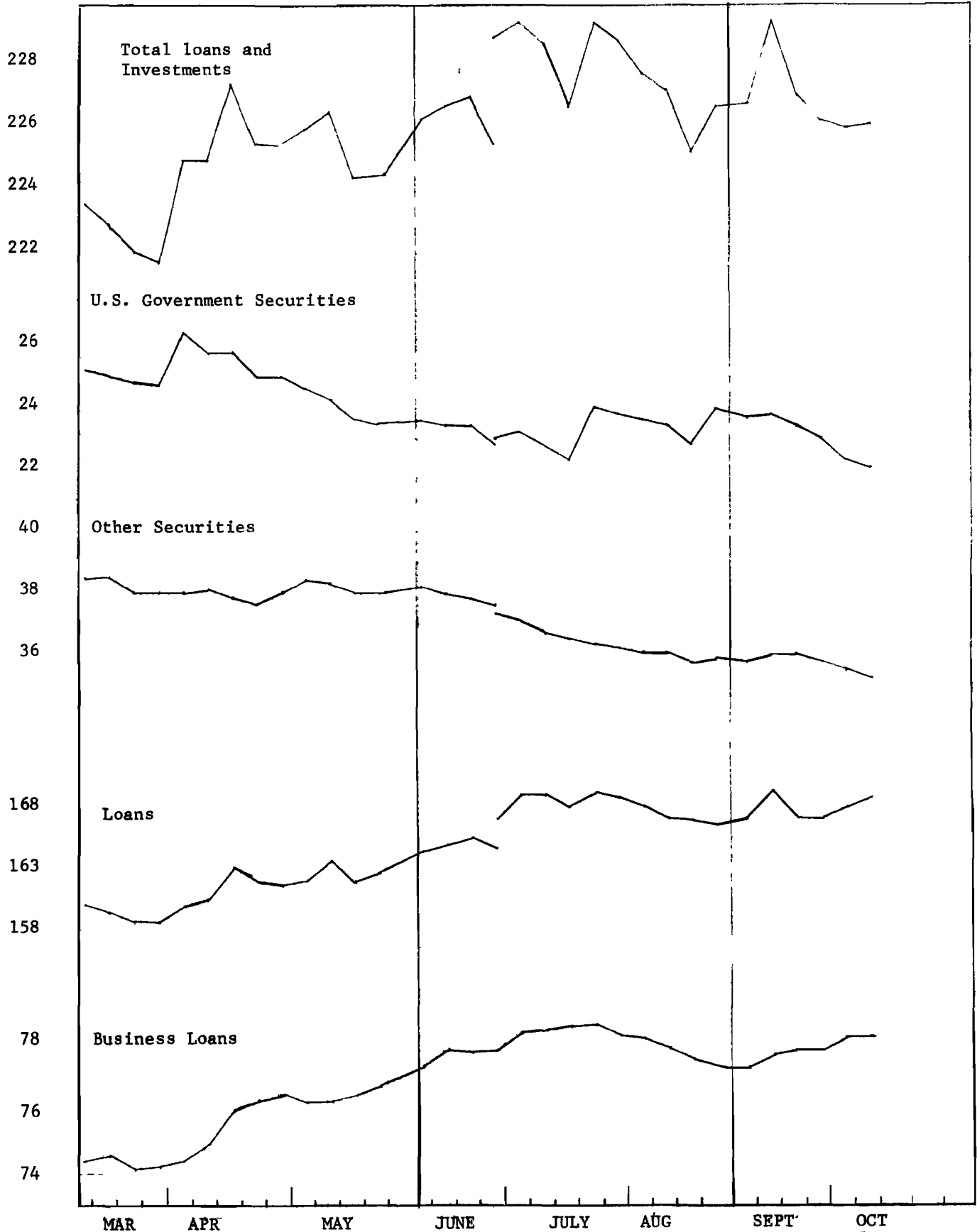
^{1/} Last Wednesday of month series.

Although the September advance in total loans was somewhat stronger than recorded in the summer months, the advance was fairly widespread--gains being recorded in all major loan categories except loans to nonbank financing institutions--and there was no strong rise in any specific loan category. Real estate loans did advance more than in any month since May, but much of this increase was due to loan reclassification.

Business loans increased in September at a pace just slightly below that established during the summer months. Toward the end of September and in early October, however, business lending at weekly reporting banks accelerated somewhat. Loans to producers of metal and metal products continued to expand at a relatively rapid pace, and there was additional borrowing recently associated with final payments on Alaskan oil leases. Loans to firms engaged in wholesale and retail trade, on the other hand, were about normal for this time of year and loan extensions to firms in the petroleum industry and chemical industry were below normal.

The September decline in U.S. Treasury holdings mainly reflected bank distribution of securities acquired in the Treasury's late August financing. Weekly reporting bank data indicate that liquidation of Treasury issues continued on into the early part of October and that prior to the October 14 financing, bank holdings of Treasury securities had dropped below their late August level. The September run-off of Treasury securities was offset to some extent by a temporary increase in holdings of other securities. This increase largely reflected New York bank underwriting of a mid-September

III - 3
 LOANS AND INVESTMENTS AT WEEKLY REPORTING BANKS 1/



1/ Seasonally adjusted levels; experimental series based on preliminary seasonal factors.

NET CHANGE IN TIME AND SAVINGS DEPOSITS
Weekly Reporting Banks
(Millions of dollars, not seasonally adjusted)

	Dec. 11 - Sept. 24 ^{1/}			Sept. 24 - Oct. 8 ^{1/}		
	1967	1968	1969	1967	1968	1969
Total time & savings	12,899	5,259	-14,738	410	1,027	-215
Consumer-type deposits	7,486	4,049	-977	395	617	64
Savings	1,363	-222	-2,239	65	152	80
IPC time deposits	6,123	4,271	1,262	330	465	-16
Negotiable CD's	4,490	1,145	-12,515	171	439	-83
All other time	923	65	-1,246	-156	-29	-196

MEMORANDUM:

Euro-dollar borrowings	-290	2,470	6,993	234	-248	260
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1/ Dates are for 1969; corresponding dates used for other years.

The outflow of large CD's continued in recent weeks, but the rate has diminished considerably. Large CD purchases by the Bank for International Settlements from the head offices of several large banks partly offset the continued sharp rundown of CD's held by other customers of the banks. Excluding BIS and other foreign official deposits, CD's declined by about \$400 to \$500 million over the three weeks ending October 15. This is approximately in line with the attrition rate prevailing since the latter part of the summer.

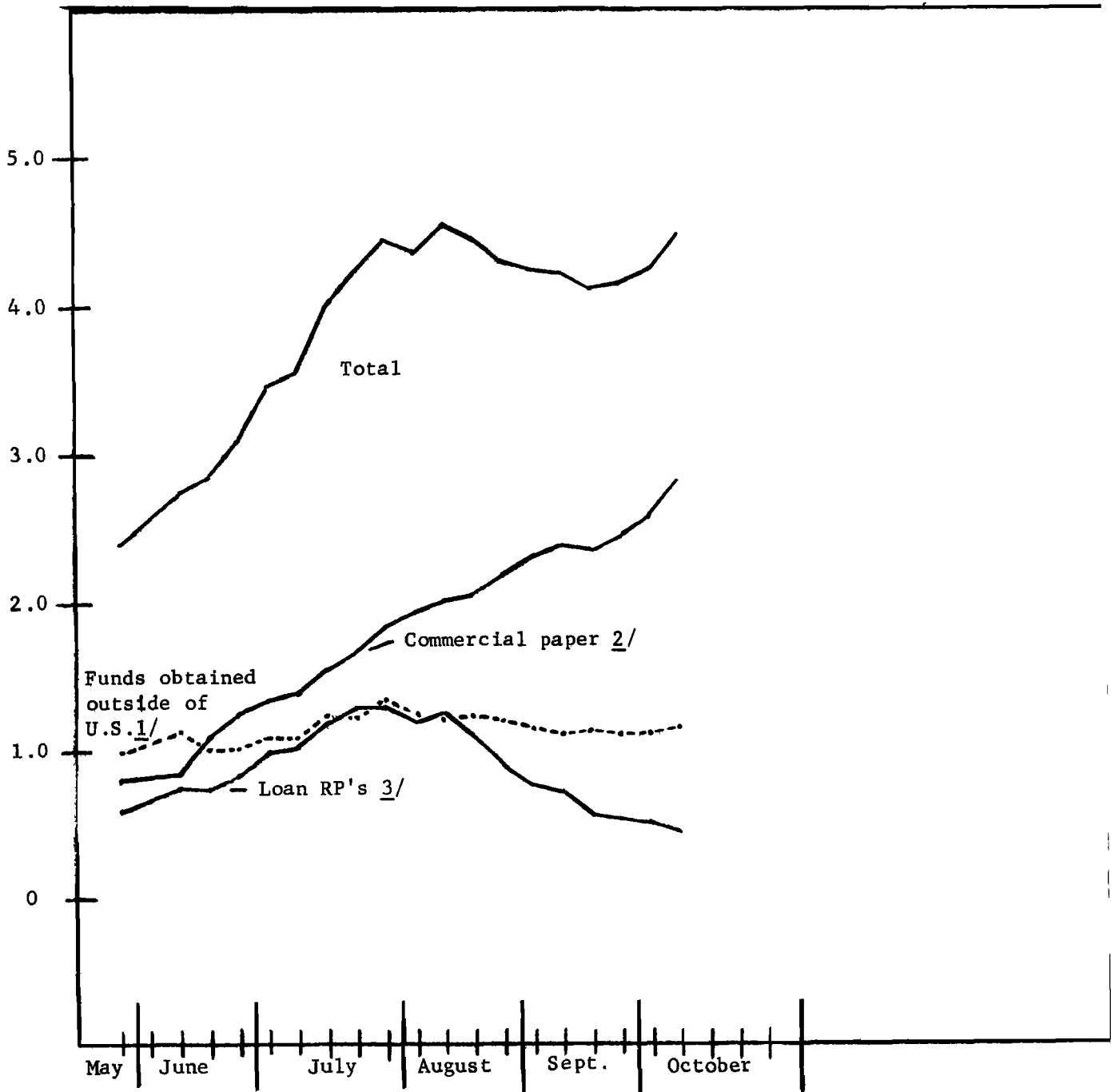
After tapering off in September, attrition on consumer-type time and savings deposits resumed in the weeks following the October quarterly interest crediting. However, data through the week ending October 8 suggest that, although interest yields on most market instruments

recently have been higher than in July, attrition in the present period is substantially below that in July, presumably because not as many banks credit savings accounts on a quarterly basis. Total consumer-type time and savings deposits, including the amounts of interest credited, showed a slight increase for the two weeks ending October 8 which compares with a \$260 million decline in the similar two-week period following the interest crediting in the middle of this year. However, the recent deposit movement contrasts with the gain of more than \$600 million recorded last year in the corresponding weeks of October.

As for nondeposit sources of funds, in recent weeks commercial banks have tapped the Euro-dollar market for additional funds and borrowing by bank affiliates in the commercial paper market has also stepped up. These increased borrowings have more than offset further declines in loan RP's, which dropped nearly \$800 million from their mid-July peak of \$1.3 billion.

SELECTED NONDEPOSIT SOURCES OF FUNDS

(Outstandings in billions of dollars)



1/ Euro-dollars borrowed directly or through brokers or dealers, and liabilities to bank's own branches in U.S. territories and possessions. Does not include liabilities to own foreign branches.

2/ Issued by a bank holding company or other bank affiliate.

3/ Loans or participations in pools of loans sold under repurchase agreement to other than banks and other than banks' own affiliates or subsidiaries.

Nonbank depository intermediaries. Outflows of savings (net of interest credited) from both savings and loans and savings banks during the current reinvestment period were sizable, as had been expected. But these current outflows do not appear to indicate any marked further weakening from the June-July period, bearing in mind the difference in seasonal forces. As in the mid-year interest crediting period, outflows from savings banks were much larger than in 1966, but in that earlier period mid-year increases in offering rates had been effective in limiting outflows throughout the second half of the year. For savings and loans, outflows were a smaller share of outstanding deposits during the latest investment period, as compared to that in 1966. For the third quarter as a whole, the seasonally adjusted annual rate of growth in both types of accounts continued to fall and at two per cent was the lowest since the second quarter of 1966.

REINVESTMENT PERIOD SAVINGS FLOWS
Excluding Dividends Credited
(Millions of dollars, not seasonally adjusted)

	1966	1967	1968	1969
<u>Savings & Loan Associations</u>				
September grace days	-353	-166	-301	-425
October 1-3		129	21	-289
October 6-10 ^{1/}	-265	297	324	68
Total	-618	260	44	-646
As a per cent of deposits	-.56	.21	.03	-.48
<u>New York Savings Banks^{2/}</u>				
September grace days	- 73	- 58	- 62	-135
October 1-7	6	- 2	- 10	- 95
October 8-15	24	39	24	- 30
Total	- 43	- 21	- 48	-260
As a per cent of deposits	-.28	-.13	-.26	-1.38

^{1/} The dates indicate the periods covered during 1969; there is rough comparability with respect to the number of business days in other years except for 1966, which covers only the first 5 days in October.

^{2/} 15 largest mutual savings banks in New York City. Repayments of pass-book loans made earlier to take advantage of interest crediting have been excluded.

GROWTH IN SAVINGS*
(Seasonally adjusted annual rates, in per cent)

	Mutual Savings Banks	Savings and Loan Associations	Both
1968 - QIII	6.5	5.9	6.1
QIV	7.1	6.2	6.5
1969 - QI	6.2	6.1	6.1
QII	4.3	3.5	3.8
QIII ^{p/}	1.9	2.0	2.0
June	3.3	4.4	4.0
July	-0.9	-0.4	-0.5
August	3.5	2.5	2.8
September ^{p/}	3.0	4.0	3.7

^{p/} Preliminary.

* Because of seasonal adjustment difficulties, monthly patterns may not be significant.

Although mortgage lending of savings and loans declined on a seasonally adjusted basis in the third quarter, such lending was as large as a year ago, despite the pressure on savings, sustained by heavy reliance on FHLB advances. The FHLBB has endeavored to support the home mortgage market this year by maintaining an expansive policy with regard to advances and, to a lesser extent, by relaxing requirements for S&L liquid asset holdings. During the third quarter alone, the net amount of funds borrowed by S&Ls was \$1.5 billion, much more than the \$200 million in actual outflows of savings (i.e., not seasonally adjusted) during the same period. Indeed, through the first three quarters of 1969, the increase in borrowed funds nearly matched the \$3.1 billion savings inflow, and exceeded by far the support received from FHLB advances in earlier years.

SOURCES AND USES OF FUNDS
INSURED SAVINGS AND LOAN ASSOCIATIONS
(Billions of dollars, not seasonally adjusted)

	Third Quarter				Year through September			
	1966	1967	1968	1969	1966	1967	1968	1969
Savings inflow	-.7	1.9	.9	-.2	1.3	7.8	4.5	3.1
Borrowed funds	<u>.4</u>	<u>-.1</u>	<u>.1</u>	<u>1.5</u>	<u>1.3</u>	<u>-3.1</u>	<u>.6</u>	<u>2.6</u>
Subtotal	-.4	1.7	1.1	1.3	2.6	4.8	5.2	5.7
Mortgage sales and repayments <u>1/</u>	3.4	3.9	3.7	3.6	10.9	10.5	10.8	10.8
Liquid assets <u>2/</u>	.6	.3	.7	1.0	1.2	-.9	.4	1.5
Other <u>3/</u>	<u>.2</u>	<u>1.0</u>	<u>.6</u>	<u>--</u>	<u>-.1</u>	<u>1.3</u>	<u>1.1</u>	<u>.6</u>
Gross mortgage acquisitions	3.8	6.9	6.1	6.0	14.6	15.6	17.5	18.6
Memo: Net mortgage acquisitions	.4	3.0	2.4	2.4	3.7	5.1	6.7	7.8

1/ Includes funds from sales of loans and participations, loan repayments, and miscellaneous credits. Excludes interest, taxes, etc.

2/ A drawdown of liquid assets is shown as a positive source of funds.

3/ "Other" includes the net amount from loans in process, allocations to reserves and surplus, accruals of dividends, and other loans and investments.

NOTE: Components may not add to totals because of rounding.

Life insurance companies. Policy loans extended by life insurance companies remained large during the third quarter. Although the net extensions tended to taper off slightly during August and September, these loans probably continued to absorb about 15 per cent of funds invested during the quarter. With large policy loan volume expected to persist, industry projections of funds available for investment are being held at modest levels. Sales of securities from portfolio will probably remain an important supplementary source of funds for disbursements under existing commitments.

NET CHANGE IN POLICY LOANS AT 15 LIFE INSURANCE COMPANIES^{1/}
(Millions of dollars)

	QI	QII	QIII	QIV
1966	126	210	334	311
1967	190	162	130	134
1968	181	247	219	169
1969	269	414	542	--

MEMO: Policy Loans as a Per Cent of Cash Flows^{2/}

1966	4.0	7.9	14.1	13.6
1967	7.6	7.5	6.0	4.7
1968	6.7	9.1	8.6	5.2
1969	9.8	14.6	15.0 (est.)	--

1/ These companies account for about two-thirds of industry policy loan activity.

2/ As reported by a sample of companies representing 80 per cent of industry assets. Increases in the reporting sample have occurred but have not materially altered these ratios, which express net increases in policy loans as a share of total funds--including policy loans--invested during the quarter.

The volume of new investment commitments has decreased sharply recently, reflecting historically very large backlogs of outstanding commitments and endeavors to maintain cushions between scheduled disbursements and reduced projected fund flows. In August, for the first time this year, new commitments made for both securities and mortgages was appreciably below the rate of a year earlier. There are early indications that this reduced pace in commitment activity continued in September, at least in direct placements.

NEW COMMITMENTS MADE BY LIFE INSURANCE COMPANIES
(Billions of dollars)

STRICTLY CONFIDENTIAL - FRB

	Total		Securities		Mortgage & Real Estate	
	1968	1969	1968	1969	1968	1969
January ^{1/}	.9	.8	.3	.3	.7	.5
February ^{1/}	.9	.9	.4	.3	.6	.6
March ^{1/}	1.0	1.0	.4	.3	.6	.7
April ^{2/}	1.2	1.2	.4	.4	.8	.8
May ^{2/}	1.3	1.2	.4	.3	.9	.9
June ^{2/}	1.0	1.0	.3	.3	.7	.7
July ^{2/}	1.1	1.1	.5	.5	.6	.7
August ^{2/}	1.2	.8	.5	.3	.8	.5

Note: Components may not add to totals because of rounding.

1/ Sample representing two-thirds of industry assets (for both 1968 and 1969).

2/ Sample representing four-fifths of industry assets (for both 1968 and 1969).

Mortgage market. With savings inflows at thrift institutions continuing very limited, the availability of new commitments for residential mortgages remained tight in early October, despite sustained support from FNMA. In the secondary market, the scarcity of funds from private lenders was reflected in additional increases in yields in FNMA's weekly auction of FHA and VA home loan commitments. By the October 20 auction, yields averaged 37 basis points above their recent low in late July. In the latest two auctions, yields rose even though there was a decline in the volume of bids submitted for FNMA's forward-purchase commitments. The decline stemmed in part from the increasingly restrictive discounts on these Government underwritten mortgages.

AVERAGE CONTRACT INTEREST RATES ON CONVENTIONAL
FIRST MORTGAGES FOR NEW-HOME PURCHASE
(Per cent)

	September		Year-over-year increase (basis points)
	1968	1969	
Northeast	7.15	7.80	65
Middle Atlantic	7.35	7.60	25
South East	7.25	8.10	85
North Central	7.05	8.00	95
South West	7.35	8.55	120
West	7.45	8.90	145
U. S., total	7.30	8.25	95

Source: Federal Housing Administration, for field-office regions which differ slightly from Census regions.

With returns on new issues of high-grade corporate bonds up sharply in September, yield spreads favoring investment in home mortgages became unusually narrow.

FNMA WEEKLY AUCTIONS

	<u>Amount of total offers</u>		<u>Implicit private market yield 6-month commitments</u> (Per cent)
	<u>Received</u> (Millions of dollars)	<u>Accepted</u> (Millions of dollars)	
<u>Highs</u>			
1968	\$232 (6/3)	\$ 89 (7/1)	7.71 (6/10)
1969	410 (6/16)	152 (9/8)	8.63 (10/20)
Sept. 22	247	145	8.44
29	258	144	8.48
Oct. 6	251	147	8.52
13	218	146	8.59
20	162	135	8.63

Note: Average secondary market yield after allowance for commitment fee and required purchase and holding of FNMA stock, assuming prepayment period of 15 years for 30-year Government-underwritten mortgages. Yields shown are gross, before deduction of 50 basis point fee paid by investors to servicers. The first auction date was May 6, 1968.

During September, average contract interest rates and yields moved slightly higher in both the primary and secondary home-mortgage market, although the increase continued to be limited by usury ceilings of 8 per cent or less still prevailing in more than 20 states. Regionally, year-over-year increases in contract rates on conventional new-home mortgages have been largest in the Southwest and West, where usury ceilings tend to be most liberal. They have been smallest in the Northeast and Middle Atlantic regions, where statutory limits in a number of important states have been quite restrictive. A few of these ceilings may be raised after the November elections.

AVERAGE RATES AND YIELDS ON SELECTED NEW-HOME MORTGAGES

	Primary Market: Conventional loans		Secondary Market: FHA-insured loans		
	Level (per cent)	Yield spread (basis points)	Level (per cent)	Yield spread (basis points)	Discount (points)
<u>1968</u>					
Low	6.75 (Jan.Feb.)	23 (Mar.)	6.78 (Feb.)	26 (Mar.)	4.4 (Sept.)
High	7.40 (Dec.)	115 (Aug.)	7.52 (June)	120 (Aug.)	7.9 (Apr.)
<u>1969</u>					
January	7.55	63	7.85e	93e	2.8e
February	7.60	69	7.99	108	3.9
March	7.65	28	8.05	68	4.4
April	7.75	58	8.06	89	4.5
May	7.75	53	8.06	84	4.5
June	8.00	42	8.35	77	6.7
July	8.10	47	8.36	73	6.8
August	8.20	55	8.36	71	6.8
September	8.25	27	8.40	42	7.1

Note: FHA series: Interest rates on conventional first mortgages (excluding additional fees and charges) are rounded to the nearest 5 basis points. Data for FHA loans in January 1969 estimated by Federal Reserve for 7-1/2 per cent regulatory interest rate, on which a change of 1.0 points in discount is associated with a change of 12 to 14 basis points in yield. Gross yield spread is average mortgage return, before deducting service fees, minus average yield on new issues of high grade corporate bonds with 5-year call protection.

e/ Estimated.

With savings flows at a reduced pace in the third quarter and uncertain prospects about the current quarter, seasonally adjusted new mortgage commitments approved by insured savings and loan associations declined somewhat further in the July-September period, and S&L commitment backlogs dropped to the lowest level in a year. For both

new and outstanding S&L commitments, however, the declines experienced so far in 1969 have been substantially less than in 1966. Unlike 1966, moreover, a sharp step-up in FNMA's commitment activity has more than offset the declines indicated for S&L's.

During the July-September period, seasonally adjusted net expansion in total mortgage debt outstanding, while relatively high, edged down for the third consecutive quarter, reaching a level about 15 per cent below the record pace attained late last year. Across-the-board reductions in net mortgage lending on home, income, and farm properties alike apparently reflected quarter-to-quarter cutbacks by all major types of private lenders. These cutbacks were only partly counterbalanced by further substantial increases in net loan acquisitions by federal agencies, including record net takings by FNMA.

Corporate security and State and local bond markets. A shift in market expectations in early October produced relatively sharp declines in corporate and municipal bond yields. And, while stock prices did not break out of the narrow band prevailing during the summer and early fall, at mid-month they rose substantially on a very large volume, with institutional purchases reported to be extremely high. Apparently, all security markets were influenced by a growing feeling that some breakthrough in Vietnam peace negotiations might be announced by the President in his speech scheduled for November 3 and also by some further indications that the business outlook was weakening and pressure in the money and credit markets might soon be subsiding. The tax-exempt bond market also reacted favorably to the Senate Finance Committee decision reversing House action that would have taxed interest on municipal bonds.

STOCK PRICES AND BOND YIELDS

	Stock Prices <u>1/</u>		Bond Yields	
	NYSE	AMEX	New Corporate Aaa <u>2/</u>	Long-term State & local bonds <u>3/</u>
<u>1968</u>				
Low	48.66 (3/4)	21.58 (3/5)	6.13 (8/30)	4.07 (8/9)
High	61.27 (11/29)	33.25 (12/20)	6.92 (12/13)	4.85 (12/29)
<u>1969</u>				
Low	49.31 (7/29)	25.02 (7/29)	6.90 (1/10)	4.82 (12/24)
High	59.32 (5/14)	32.91 (1/3)	8.22 (10/3)	6.37 (9/5)
<u>Week of:</u>				
Sept. 19	52.84	26.77	8.04	6.25
26	52.23	26.63	8.13	6.08
Oct. 3	51.77	26.57	8.22	6.19
10	51.98	26.71	8.10	6.14
17	53.72	27.66	7.95	5.92

1/ Prices as of the day shown. NYSE is New York Stock Exchange. AMEX is American Stock Exchange.

2/ With call protection (includes some issues with 10-year call protection).

3/ Bond Buyer (mixed qualities).

With long-term municipal yields declining and State interest rate ceilings raised or removed in some areas, short-term financing by State and local governments appears to have declined contra-seasonally and long-term tax-exempt offerings are likely to rise sharply in October to an estimated \$1.2 billion, about 50 per cent above the third quarter average. For November, the staff expects the volume of long-term municipal offerings to decline somewhat, despite the very large backlog of financing by State and local governments and the change in rate ceilings in some areas. This assumes that, on the demand side, the major buyers of tax-exempt bonds--commercial banks--will remain under

pressure and will be unable to increase their purchases of municipals significantly. Moreover, it is reported that inter-dealer transactions have contributed significantly to the decline in tax-exempt yields. With continued absence of bank demand and a high volume of new offerings, dealers may become increasingly reluctant to absorb additional inventory. If the decline in yields is reversed, as suggested by these considerations, a drop-off in new offerings might again be forced by statutory interest ceilings.

STATE AND LOCAL GOVERNMENT OFFERINGS
Monthly or Monthly Averages
(Millions of dollars)

	Long-Term <u>1/</u>		Net Short-Term <u>2/</u>		Total <u>3/</u>	
	1968	1969	1968	1969	1968	1969
Year	1,381	--	-20	--	1,361	--
QI	1,246	930	-51	302	1,195	1,232
QII	1,285	1,208	+11	344	1,296	1,552
QIII	1,537	792e	-73	290e	1,464	1,082e
September	1,444	525e	-913	80e	531	605e
October	2,230	1,200e	250	-15e	1,980	1,185e
November	1,021	1,000e	413	n.a.	1,434	n.a.

e/ Estimated.

1/ Data are for principal amounts of new issues.

2/ EXCLUDES note offerings of Housing Assistance Administration and Renewal Assistance Administration.

3/ Combines GROSS long-term and NET short-term issues.

In the corporate market, public bond offerings in October are expected to match the high September pace, although the present forward calendar suggests that some moderation is likely in November. The marked improvement in market sentiment, referred to above, has produced

generally quick distribution of new and older issues still in syndicate; in the secondary market, prices have risen from 1 to 4 points since early October. Market demands are reported to center among State and local pension funds--which had been hesitant to make commitments last month--although individuals were also said to be continuing to absorb relatively large quantities of corporate bonds.

CORPORATE SECURITY OFFERINGS^{1/}
 Monthly or Monthly Averages
 (Millions of dollars)

	Public Bond Offerings		Private Bond Offerings		Stocks		Total	
	1968	1969	1968	1969	1968	1969	1968	1969
Year	894	--	554	--	382	--	1,830	--
QI	821	886	574	513	330	674	1,726	2,073
QII	1,035	1,136	548	526	319	709	1,902	2,371
QIII	869	1,063e	454	517e	389	533e	1,711	2,113e
September	727	1,230e	433	550e	398	700e	1,556	2,480e
October	1,009	1,150e	595	500e	525	500e	2,129	2,150e
November	939	1,000e	362	500e	466	500e	1,767	2,000e

e/ Estimated. 1/ Data are gross proceeds.

While private placements of bonds are expected to remain at about the summer pace in October and November, stock offerings are expected to decline from the rate of September, when several large public utility issues had been marketed. No large issues are now scheduled, but a continued uptrend in the stock market could well stimulate additional offerings of equities. At this time, the staff's best estimate suggests that total corporate security issues in October and

November may remain fairly close to the \$2.1 billion average monthly rate of the third quarter.

Under present circumstances, these projections of underwriting volume appear subject to unusually wide margins of error. If borrowers expect yields to continue to decline, bond offerings could drop sharply in the near-term. On the other hand, with corporate liquidity expected to decline further and bank credit availability very tight, corporations might be encouraged to accelerate their capital market demands. This would most likely occur if market expectations were to be reversed once more, by either Vietnam developments or public statements regarding the policy outlook.

Government securities market. The rally in the market for U.S. Government notes and bonds, which began in the first week of October, has continued to date under the impetus of additional indications of a cooling in economic activity and renewed optimism on the possibility of a peace breakthrough in Viet Nam. Yields on intermediate-term issues have fallen by around 85 basis points since the first of the month and long-term yields have declined by about 60 basis points. While not moving as sharply, Treasury bill rates also have declined on balance and are now down, mostly 10 to 35 basis points.

MARKET YIELDS ON U. S. GOVERNMENT SECURITIES^{1/}
(Per cent)

	Lows	Highs	Oct. 6	Oct. 14	Oct. 20
<u>Bills</u>					
1-month	5.30 (3/25)	7.20 (9/22)	6.91	6.75	6.62
3-month	5.87 (4/30)	7.17 (10/1)	6.94	7.04	6.91
6-month	5.96 (4/30)	7.42 (10/9)	7.27	7.29	7.26
1-year	5.86 (1/16)	7.47 (7/1)	7.37	7.28	7.08
<u>Coupons</u>					
3-year	6.02 (1/20)	8.14 (10/1)	7.94	7.54	7.19
5-year	6.11 (1/20)	8.04 (10/1)	7.82	7.54	7.17
7-year	6.09 (1/16)	7.76 (10/1)	7.58	7.32	6.94
10-year	5.95 (1/20)	7.52 (10/1)	7.35	7.10	6.84
20-year	5.91 (5/5)	6.82 (9/30)	6.62	6.38	6.24

^{1/} Latest dates of high or low rates in parentheses.

Improvement in the coupon-bearing sector was sparked initially by a pick-up in distribution of the securities involved in the Treasury's September financing following purchases by the Federal Reserve and

Treasury investment accounts early in October. With the technical position of the market thus improved, the news of the increase in the unemployment rate to 4 per cent provided impetus for a rally. As yields have moved markedly lower, a growing number of market participants have apparently come to the conclusion that the peak in interest rates may have been passed, with the result that demands for securities have remained buoyant in a rising market, as evident in the decline in dealers' positions in coupon issues.

The Treasury bill market has been in a good technical position in the last several weeks, partly due to the effect of heavy buying by foreign accounts in late September. Although much of this buying has since been reversed, a large proportion of foreign account sales so far this month have been absorbed directly by the System as part of its reserve supplying operations. Thus, the market has remained technically strong and was able to absorb with little rate effect the \$2 billion of April tax bills auctioned on October 8. More recently there has been a continuing steady demand for bills, allowing fairly easy distribution of dealers' weekly awards with little or no upward rate pressures. The net increase in dealer inventories in bills due in over 3 months since early October has reflected in part positioning of the tax bills as banks sold some of their awards to dealers. Nonetheless, with the bill market in a generally strong, technical position, the Treasury's announcement of a further \$3 billion tax bill auction on October 23 had little or no effect on rates.

DEALER POSITIONS IN GOVERNMENT SECURITIES
(In millions of dollars)

	October 6	October 14	October 20
Total	<u>1,177</u>	<u>2,720</u>	<u>1,791</u>
Treasury bills (total)	<u>624</u>	<u>2,210</u>	<u>1,306</u>
Due in 92 days or less	-76	209	-158
93 days or over	700	2,001	1,464
Treasury notes and bonds (total)	<u>553</u>	<u>510</u>	<u>485</u>
Due within 1 year	-7	35	69
1-5 years	302	252	195
over 5 years	258	223	220

Other Short-Term Credit Markets. In line with developments in the Government securities market, rate pressures on private short-term credit instruments generally eased during the first half of October. Three-month commercial paper declined about 40 basis points by mid-month to a level of around 8-5/8 per cent, and rates for bankers' acceptances held at their early October levels. Rates on 3- and 6-month finance paper, however, moved about 1/8 point higher, probably largely reflecting seasonal influences associated with introduction of the new automobile models.

Along with other short-term rates, yields in the short-term Agency market also showed substantial declines during the first half of October. Issues due within 3 months declined about 50 basis points, while other issues due within one year showed average declines of about 15 basis points. Rates on maturities beyond one year have shown larger declines, as evidenced by the substantial drops in yields on new issues. For example, on October 2 the 16-month FNMA notes were offered at 8.70 per cent, whereas the 13-month FHLB notes offered on October 15 yielded 8.20 per cent. A total of \$1.9 billion of Agency debt was issued in the first half of October, \$1.2 billion of which represented new money. This volume of new money already raised in October equals the year's record high June figure. (See Appendix A for further details).

NOTE: The latest figures available on commercial and finance company paper outstanding are for August. During August, the volume of such paper rose to a seasonally adjusted annual level of \$28.9 billion, 4 per cent above July and 43 per cent above August 1968. About one-third of the \$1 billion increase during the month of August was accounted for by "bank related" paper issued by bank holding companies, affiliates of bank holding companies, or affiliates of banks.

Table 1
 CHANGES IN
 COMMERCIAL AND FINANCE PAPER AND
 BANKERS' ACCEPTANCES OUTSTANDING
 (In millions of dollars)

	June	July	August
Commercial and finance paper <u>1/</u>			
Total	1,858	1,116	1,050
Placed through dealers	584	- 211	705
Paper placed directly <u>2/</u>	1,274	1,327	345
Bankers' Acceptances	212	111	154

1/ Data for commercial and finance paper in this table are seasonally adjusted: adjustment factors are revised at the end of each year. Data published in the Bulletin are seasonally unadjusted.

2/ As reported by companies that place paper directly with investors. As of June 1969, these figures include for the first time directly placed commercial paper issued by bank related companies. Dealer totals have always included paper issued by bank related companies.

SELECTED SHORT-TERM INTEREST RATES
(WEDNESDAY QUOTATION - DISCOUNT BASIS)

	September 17	October 1	October 15
<u>3-Month</u>			
Commercial paper	8.63	9.00	8.63
Finance paper	7.63	8.00	8.13
Bankers' Acceptances	8.13	8.25	8.25
Federal agencies (secondary market) ^{1/}	7.57	7.86	7.39
Treasury bill	7.13	7.17	7.04
<u>6-Month</u>			
Commercial paper	8.50	8.88	8.50
Finance Paper	7.63	7.63	7.75
Bankers' Acceptances	8.13	8.25	8.25
Federal agencies ^{1/}	7.88	7.87	7.77
Treasury bill	7.32	7.35	7.31
<u>12-Month</u>			
Prime municipals ^{1/}	5.85	5.75	5.45
Treasury bill	7.31	7.44	7.27

^{1/} Bond yield basis.

Federal Finance. The Staff is continuing to project the fiscal 1970 budget surplus at about \$3.5 billion, considerably below the \$5.9 billion Administration estimate. This \$2.4 billion difference is accounted for by the Staff's projection of lower receipts that results from our assumption of more sluggish economic growth than was assumed in the Administration estimates. Thus, the smaller surplus projected here does not imply a discretionary shift to a less restrictive fiscal policy, but rather the automatic effect on revenues of a projected decline in corporate profits and slower growth in personal income.

The receipts projection assumes that the surtax will be extended at 5 per cent through June 1970. While the Senate Finance Committee recently voted to support the Administration and affirm the House decision on the surtax extension, the future of this extension is still uncertain, linked as it is to the tax reform bill that may still be stopped by either the full Senate or the President.

On the outlays side, the staff has used the official estimate of \$192.9 billion; however, evidence is accumulating that it will take an unusual struggle by the Administration to keep to this fiscal year total. Budget Director Mayo mentioned in his October 7 statement that an additional \$4 billion in outlays could result from Congressional action and inaction not considered in last month's Summer Budget Review. Military and civilian pay raises as passed

in the House would add \$1.5 billion to planned spending this fiscal year, but a veto has been threatened if this bill clears both Houses. Increased veterans benefits, larger outlays by the departments of Labor and HEW, and a more liberal Food Stamp program could add another \$1.6 billion to the Administration's figure. Other small program changes might cost almost \$1 billion. The Administration's determination to offset such increases with budget cuts of comparable magnitude--probably concentrated in defense--might be generally successful, but spending must be slowed substantially from its third quarter rate to keep outlays down to \$192.9 billion.

The unusually high expenditures so far in this fiscal year are revealed much more sharply in the Treasury's cash accounts than in the third quarter NIA estimates. Cash withdrawals to date^{1/} by the Commodity Credit Corporation are up almost \$1 billion from the corresponding period last year, and other nondefense outlays are up \$6 billion. Military cash spending has, however, been moderate, up only \$.5 billion from the same period last year. In all, cash outlays to date have increased 12 per cent over last year, compared to a planned increase of 4.4 per cent for the entire fiscal year.

The Treasury has announced an October 23 auction of \$3.0 billion of June tax bills for payment October 29. With this new money in addition to the \$2.0 billion of April tax bills sold earlier this month, the Treasury cash balance should be \$6.0 billion at the end of the month. According to staff estimates another \$2 to

\$2-1/2 billion of new cash will probably have to be raised during November and December to maintain the cash balance above the minimal \$2 billion through its seasonal low in mid- December. Thus total fourth quarter gross financing of \$7 to \$7-1/2 billion would be well above the \$6 billion expected earlier and, given the Staff projection of receipts and expenditures, would yield an end-of-year balance of around \$6 billion.

1/ July 1, 1969, to October 16, 1969.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	Sept.	Oct.	Nov.	Dec.
<u>Borrowing operations</u>				
New cash raised:				
Weekly and monthly bills	--	--	.4	.4
Tax bills	--	5.0	--	1.5
Coupon issues	--	--	--	--
Other (agency, debt repayment, etc.)	--	-1.1	--	-2.5
Total net borrowing from public	--	3.9	.4	- .6
Plus: Other net financial sources ^{b/}	- .5	1.0	- .8	--
Plus: <u>Budget surplus or deficit (-)</u>	3.1	-5.5	-1.5	2.4
Equals: <u>Change in cash balance</u>	2.6	-0.6	-1.9	1.8
Memoranda: Level of cash balance end of period	6.6 ^{a/}	6.0	4.1	5.9
Derivation of budget surplus or deficit				
Budget receipts	21.2	11.9	14.5	18.0
Budget outlays	18.1	17.4	16.0	15.6

^{a/} Actual

^{b/} Checks issued less checks paid and other accrual items.

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

	FY 1969 Actual	Calendar year 1969 ^{e/}	Fiscal 1970		Calendar quarter				
			Summer Budget Review	.F.R. Board	1969			1970	
					II	III ^{e/}	IV ^{e/}	I ^{e/}	II ^{e/}
<u>Quarterly data, unadjusted</u>									
New budget:									
Surplus/deficit	3.1	6.5	5.9	3.5	15.3	-2.2	-4.6	-3.2	13.5
Receipts	187.8	198.0	198.8	196.4	60.8	48.7	44.4	44.1	59.2
Total expenditures and net lending	184.8	191.5	192.9	192.9	45.5	50.9	49.0	47.3	45.7
Means of financing:									
Total borrowing from the public	-1.4 ^{1/}	-5.1	n.a.	-2.5	-12.6	3.6 ^{2/}	3.7	2.5	-12.3
Decrease in cash operating balance	-.6	-1.2		--	-1.1	-.7	.7	--	--
Other <u>3/</u>	-1.1	-.3		-1.0	-1.7	-.7	.2	.7	-1.2
Cash operating balance, end of period	5.9	5.9		5.9	5.9	6.6*	5.9	5.9	5.9
<u>Seasonally adjusted annual rate</u>									
Federal surplus/deficit									
in national income accounts	4.8	9.2	n.a.	2.8	13.5	6.3	6.9	0.6	-2.8
Receipts	192.2	201.1	n.a.	199.1	202.8	200.4	202.4	196.9	196.6
Expenditures	187.4	191.9	195.8 ^{4/}	196.3	189.3	194.1	195.5	196.3	199.4
High employment budget surplus/deficit ^{4/}	2.5	8.9	n.a.	6.4	12.3	6.3	8.8	5.4	5.0

*--Actual

e--Projected. Assumes extension of surcharge at 5 per cent from January to June 1970. Also assumes discontinuance of investment tax credit effective, retroactively, April 1969.

n.a.--Not available.

1/ Excludes effect of conversion of agencies to private ownership.

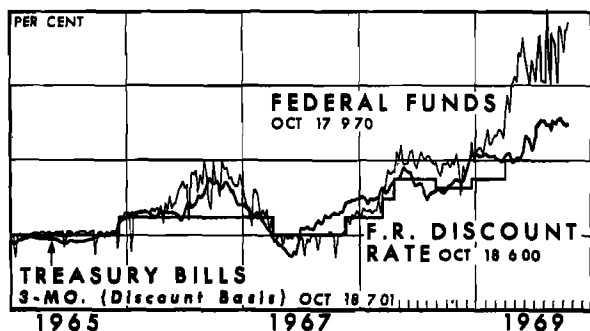
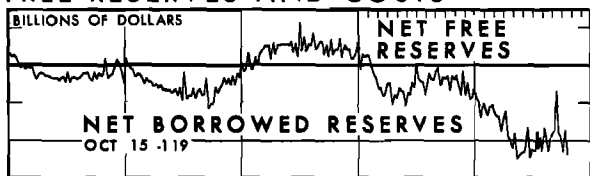
2/ Excludes effect of reclassification of \$1.6 billion of CCC certificates of interest from Budget transactions to borrowing from the public.

-3/ Includes such items as deposit fund accounts and clearing accounts.

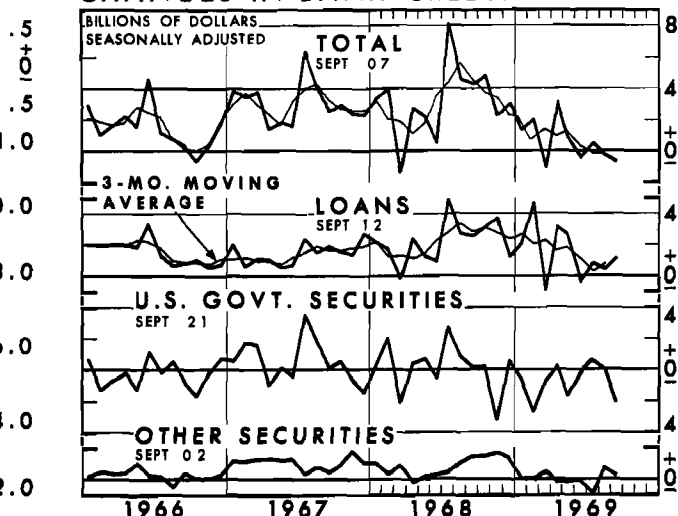
4/ National Income account translation estimated by Federal Reserve staff.

FINANCIAL DEVELOPMENTS - UNITED STATES

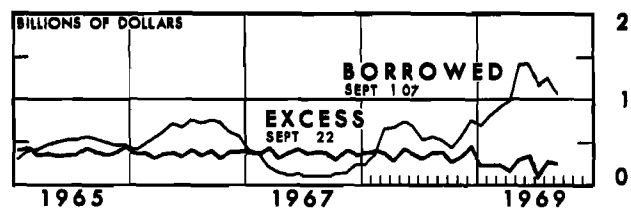
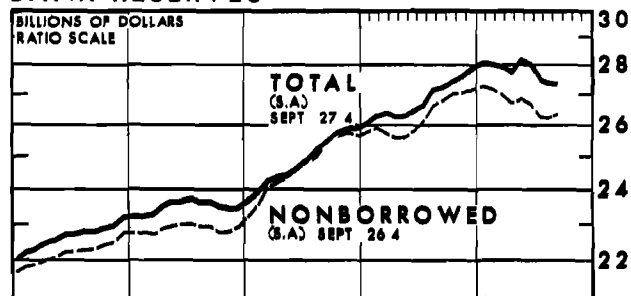
FREE RESERVES AND COSTS



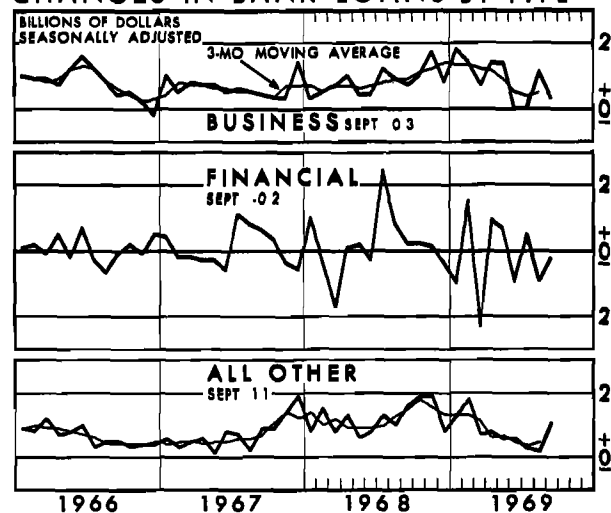
CHANGES IN BANK CREDIT



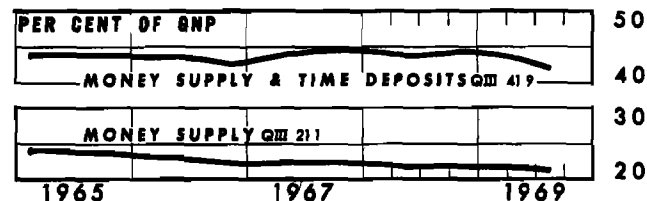
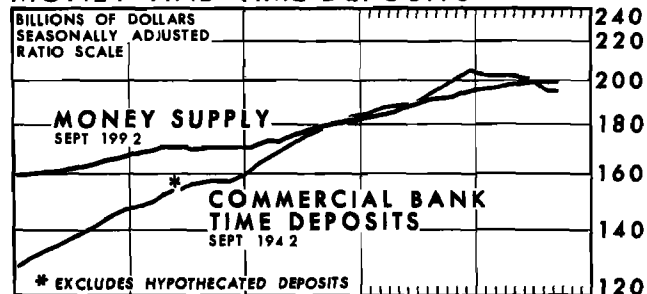
BANK RESERVES



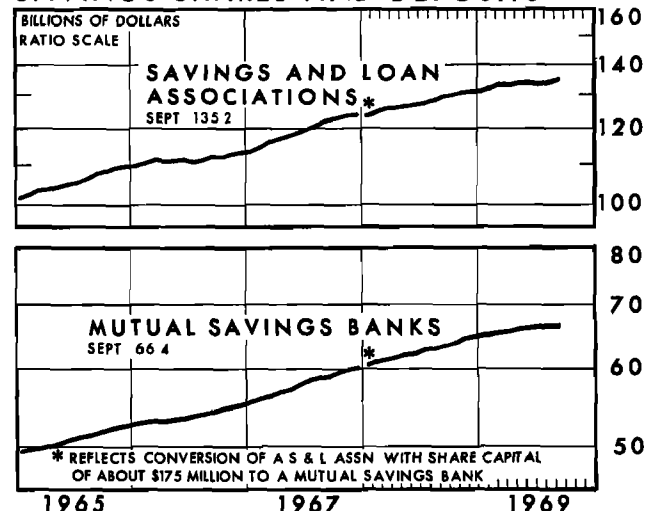
CHANGES IN BANK LOANS-BY TYPE



MONEY AND TIME DEPOSITS

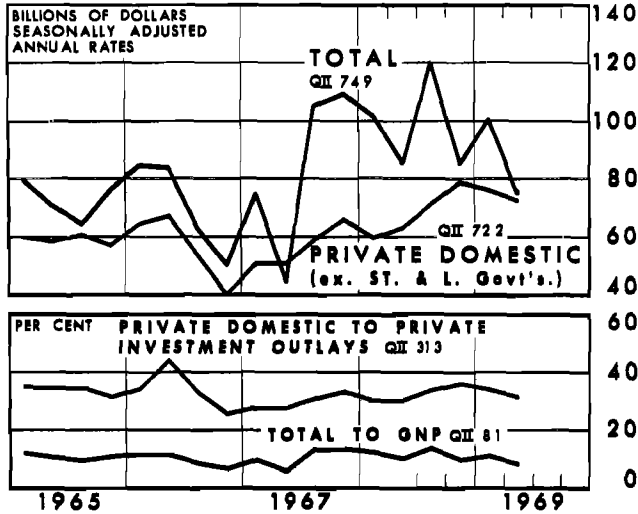


SAVINGS SHARES AND DEPOSITS

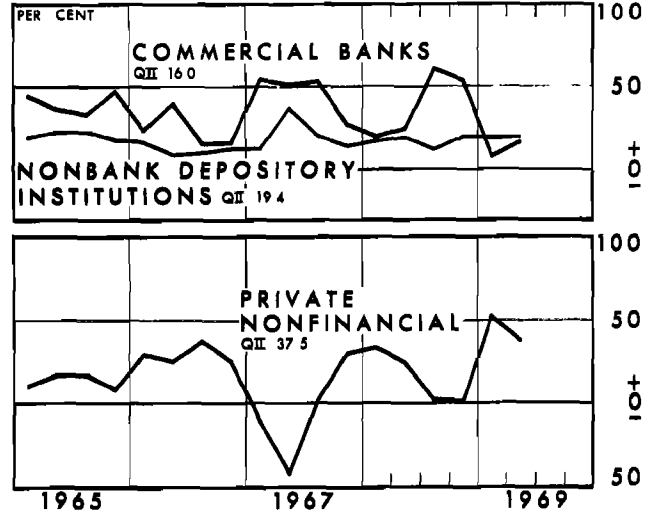


FINANCIAL DEVELOPMENTS - UNITED STATES

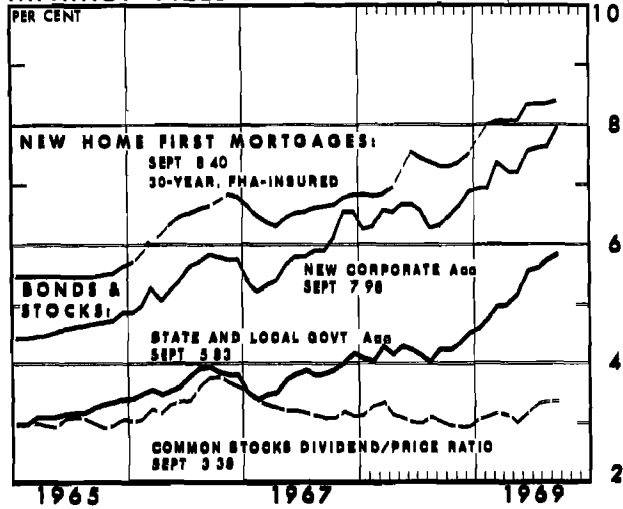
NET FUNDS RAISED - NONFINANCIAL SECTORS



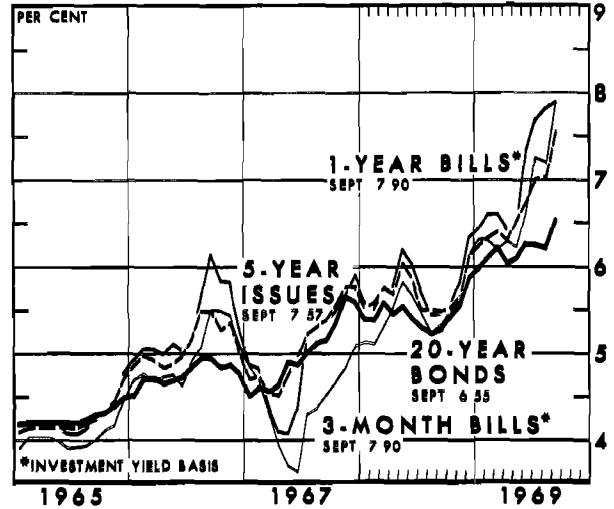
SHARES IN FUNDS SUPPLIED



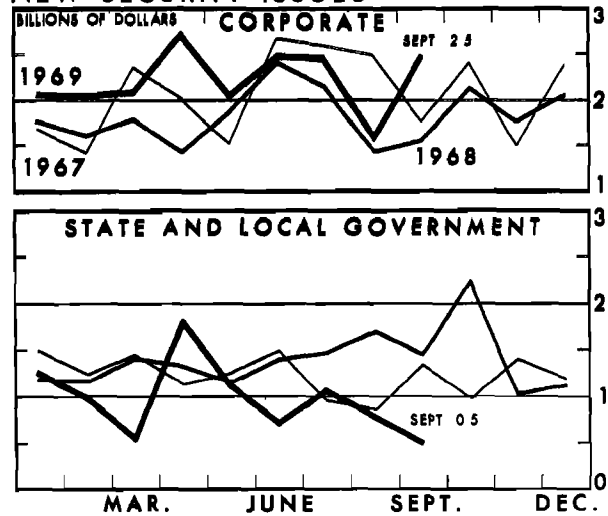
MARKET YIELDS



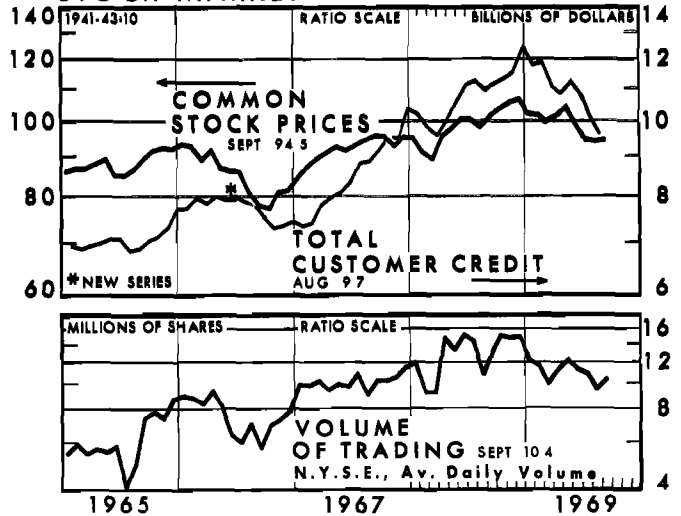
MARKET YIELDS - U.S. GOVT. SEC.



NEW SECURITY ISSUES



STOCK MARKET



THE ECONOMIC PICTURE IN DETAIL

International Developments

Foreign Exchange Market. The experiment since September 30 of floating the German mark exchange rate to a promised but still unspecified new parity has been accompanied by generally orderly conditions in exchange markets. During the first week of the floating arrangement, the mark rate moved -- at its highest point -- to a level about 6.4 per cent above par. The further rise during the past two weeks has been much slower, and at its current level of 26.84 cents (October 22) the mark exchange rate is about 7.4 per cent above par. The Bundesbank has lifted its support point for the mark in line with the rising market rate to prevent any significant reversal. Since September 30 it has sold slightly more than \$1 billion, about 60 per cent of its \$1.7 billion of spot purchases in September prior to allowing the mark rate to float.

Currently attention is focused on Monday, October 27, as the most likely date for a new DM par value to become effective. German authorities have scheduled a meeting with the EEC Monetary Commission on Saturday, October 25, for consultation on the new par, which then will be announced -- observers speculate -- during that weekend. The German Government suspended the 4 per cent border tax adjustment from October 11 until December 1. For exports and imports of nonagricultural goods this had the effect of offsetting over one-half of the mark's upward revaluation in the market to date.

Demand for sterling has been generally strong since October 1, perhaps in part reflecting the favorable impact of the mark appreciation and in part reflecting the favorable impact on market sentiment of the September trade surplus announced at mid-October. There was also fairly sizable demand from oil companies with royalty payments to make at the end of the month. The pound rate climbed to a high of \$2.3930 -- the first time it has been above \$2.39 since late July -- and the Bank of England has been able to purchase about \$350 million in the market since the beginning of the month.

Demand for the Dutch guilder, Swiss franc, and Belgian franc has been strong during the past three weeks. For the guilder and Swiss franc this strength may possibly be explained by a combination of three factors: (1) tighter money market conditions in these countries leading to repatriation of assets held abroad, (2) some reflow of speculative funds from marks, and (3) perhaps some flow of funds speculating on possible revaluations of these currencies. The sharp turnaround in the Belgian franc market was reflected in a movement of the franc rate from its lower limit to above par -- the first time it has been this high in 14 months. The Dutch, Swiss and Belgian central banks purchased large amounts of foreign exchange in the period October 1-22; \$410 million, \$110 million and \$130 million respectively.

The mark appreciation also apparently moderated selling pressure against the Italian lira and the French franc, although the lira continues

to suffer from a tenacious capital outflow and the French franc from an imbalance in trade and service payments. The lira exchange rate has hovered at its lower limit during most of the past three weeks. However, during the past three trading days (October 20-22) demand for the lira has increased sharply and the exchange rate has moved up almost to par. The French franc rate dropped to a new post-devaluation low about mid-October but more recently has recouped some of this loss. Throughout the month to date both the Italian and French central banks have continued to lose dollars through market intervention but on a smaller scale than during September.

The price of gold fell from \$40.75 an ounce (the London fixing price) on October 1 to \$40.25 on October 22, its lowest price during the year to date.

Euro-dollar market. Euro-dollar interest rates -- particularly for maturities of three-months and longer -- have declined markedly since early October. As of October 22, rates on deposits with maturities ranging from one to twelve months were at their lowest levels since May of this year. The three-month deposit rate, for example, was 9.19 per cent per annum on October 22, down almost 2 per cent from its average of 11.08 per cent in the week ending October 1. Rates for shorter-dated (call and one-month) funds have declined by about 1 per cent since the first of the month.

Perhaps the most significant influence on the market in recent weeks has been the situation of the German mark. The virtual certainty of a change in the mark parity and its de facto revaluation in the market

have resulted in a sizable reflow of funds from marks, contributing to a Bundesbank reserve decline of over \$1 billion since the end of September. Though much of this reduction went to restore the reserve positions of other central banks, some part of this reflow has probably been reflected either in an increased demand for Euro-dollar deposits or the paying off of borrowings of Euro-dollars made to finance mark purchases prior to the German elections. Moreover, the mark appreciation has probably contributed to an easing of Euro-dollar rates by removing the risk that the Euro-dollar market would feel the pressures of yet another speculative flow of funds to Germany in the near future.

In addition to the above factors, the apparent shift in recent weeks in market expectations about the future course of interest rates in the United States may also have had some influence. A widespread belief that U.S. rates will ease during the foreseeable future would certainly have a dampening impact on Euro-dollar rates. Furthermore, the Japanese authorities have recently stepped up their "yen shift" program aimed at bringing about a further reduction in outstanding borrowings of Japanese banks from the Euro-dollar market.

During this period of easing Euro-dollar rates, U.S. bank takings of Euro-dollar funds through foreign branches have increased by a considerable amount. These borrowings increased by over \$850 million in the two weeks ending October 15, more than offsetting the decline in the last three weeks of September. There has been a moderate decline in U.S. bank Euro-dollar borrowings since October 15, according to daily data available through October 20.

SELECTED EURO-DOLLAR AND U.S. MONEY MARKET RATES
(weekly average of daily figures)

Average for week ending Wednesday	(1) Call Euro-\$ Deposit	(2) Federal Funds	(3) =(1)-(2) Differ- ential	(4) 3-month Euro-\$ Deposit	(5) 3-month Treasury Bill	(6) =(4)-(5) Differ- ential
Sept. 3	10.35	9.57	0.78	11.25	7.01	4.23
10	9.45	8.57	0.88	11.34	7.09	4.25
17	8.85	9.07	-0.22	11.14	7.11	4.03
24	9.00	9.61	-0.61	10.68	7.13	3.55
Oct. 1	10.00	9.11	0.89	11.08	7.07	4.01
8	9.60	9.43	0.17	10.65	7.00	3.65
15	9.16	9.68	-0.52	10.39	7.02	3.37
22	8.90	8.68 ^{p/}	0.22	9.63	6.93 ^{p/}	2.70

^{p/} preliminary

U.S. balance of payments. As the fourth quarter begins there are few signs of any major departures from the course of the balance of payments accounts described three weeks ago. The liquidity deficit in the opening weeks of October was very large, but this period is seasonally very adverse. At the same time there was a sharp rise in borrowings by banks from their foreign branches, and also some increase in liabilities to other commercial banks abroad, so that the balance on official settlements has registered a small surplus. This also is probably not indicative of the outcome for the quarter as a whole.

Early estimates of the September trade results show a somewhat faster improvement than expected (as noted below) and further gains in the fourth quarter are likely. Moreover, in view of the very large outflow of U.S. direct-investment capital in the first half of the year, and

perhaps also in the third quarter, the Office of Foreign Direct Investments believes there will once again be a steep drop in fourth-quarter outflows as companies act to stay within their ceilings. Another favorable factor in the fourth quarter should be the reversal (or at least the cessation) of capital outflows from the United States for the purpose of speculation on a DM revaluation or to take advantage of high Euro-dollar rates. It seems reasonable to expect, therefore, that the liquidity deficit in the fourth quarter will be much lower than in the second or third quarters. However, the "special" transactions that also contributed to the liquidity surplus in the fourth quarter of 1968 will be missing this year.

Data on third-quarter transactions are still very partial. The liquidity deficit in September apparently was about \$500 million, resulting in a deficit for the quarter (seasonally adjusted) somewhat above \$2.5 billion. The official settlements deficit for the quarter is estimated at about \$1.3 billion.

Bank lending to foreigners, according to early reports, resulted in an insignificant outflow in September, as outflows by banks in New York appear to have been matched by inflows elsewhere. This would bring the seasonally adjusted inflow for the third quarter to about \$150 million, compared to an outflow of over \$500 million in the second. U.S. net purchases of foreign securities were about \$100 million in September -- close to the monthly average for the year -- once again featuring Canadian issues. Foreign investments in U.S.

corporate stocks apparently registered a very small net inflow in September, and amounted to about \$50 million for the third quarter as a whole. Sales of new direct-investment issues in Europe remained at a relatively low level.

U.S. foreign trade. Although the official trade statistics for September are not yet available, it is roughly estimated (based on customs receipts, counts of export documents, etc.) that the export surplus in that month increased further. Exports in September are believed to have held at close to the high August level, with an increase in agricultural shipments offsetting a drop in deliveries of commercial aircraft. Imports in September may have been down by about 5 per cent from August. Including these estimates for September, the third quarter export balance would be about \$1-1/4 billion at an annual rate (balance of payments basis) compared with a small deficit in the first half of the year, and a surplus of only \$1/2 billion at an annual rate in the second half of 1968.

Still undetermined is whether this recent expansion in the export surplus represents a basic improvement in our trade position or was still influenced by secondary effects of the dock strike earlier in the year. The strike had a greater adverse effect on exports than on imports, and some foreign users probably drew down inventories of some commodities sharply when certain types of goods could not be obtained from the United States in the first quarter. These inventories may not have been immediately replaced, and some stockbuilding may now be

occurring. This situation may exist not only for tobacco and other agricultural items but also for some crude and semifinished nonagricultural materials.

The export advance in July-August was quite widely distributed by commodities and areas. The value of shipments of both agricultural and nonagricultural products was considerably above the strike-depressed rate in the first half of the year. Compared with the second half of 1968, agricultural exports were about unchanged in July-August, but nonagricultural shipments were 12 per cent higher.

The increase in nonagricultural exports in July-August was broadly dispersed, with large gains recorded for machinery, chemicals, steel and paper products. These advances probably reflect supply stringencies and peak capacity-utilization manufacturing rates in Europe. Machinery deliveries were particularly high in August, the first significant rise since March when most of the struck ports reopened. Foreign orders for U.S. machinery, which have expanded steadily since the beginning of 1968, increased very sharply in July-August, promising further advances in deliveries later this year and in 1970. Shipments of automotive products to Canada were down from those in the first half but this may reflect a shift in the seasonal pattern resulting from the early changeover to the 1970 models. Deliveries of commercial aircraft in July-August held at the relatively low rate of the first half but deliveries in September may have been the lowest in more than two years.

Exports to all areas except Canada were up sharply in July-August. The expansion in shipments to Europe and to Latin America was all in nonagricultural commodities; shipments of agricultural goods to these countries, which had fallen from the last half of 1968 to the first half of this year, declined further in July-August. The advance in exports to Japan and the developing countries of Asia and Africa included both agricultural and nonagricultural products.

Imports in the third quarter (including a rough estimate for September) continued to rise faster than GNP. The import/GNP ratio in the third quarter may be over 3.9 per cent, compared with an average 3.8 per cent in the first half of this year and in calendar 1968. Continued heavy arrivals of automobiles, other nonfood consumer goods, and capital equipment in July-August were complemented by increased imports of foods and industrial materials. The latter two categories of imports had declined in the first six months of this year from the values in the last half of 1968. All principal types of industrial products -- steel and other materials related to durable manufacturing, textiles, and other nondurable goods -- were all being imported at appreciably higher rates in July-August than in the first half. The value of building materials was virtually the only major item among industrial materials that was lower in July-August than in the first half, as housing starts fell off and lumber prices eased.

Imports of automobiles, other than from Canada, were up sharply in July-August following a drop in value in the first half of the year. Sales of foreign cars in the U.S. have been 6 per cent larger in number in January-September of this year compared with the same period a year earlier. Sales of Volkswagens are down by more than 10 per cent this year, but this has been more than offset by larger sales of Toyotas and Datsuns from Japan, Fiats from Italy, and Opels from Germany. The VW share of foreign car sales in the United States in January-September of this year was down to about 45 per cent compared with over 55 per cent a year earlier. Imports of automobiles from Canada also continued to expand this year although the rate of increase is more moderate than from 1967 to 1968.

For the first 8 months of 1969 combined, U.S. exports and imports were about in balance, compared with a surplus of \$1/2 billion (annual rate) in the last half of 1968. The balance with various regions, however, showed divergent movements. The average monthly import balances with Canada and Japan were further enlarged this year as imports advanced more than exports. About one-half of the worsening in our trade balance with Canada resulted from the continued weakening in our automotive trade position with that country. Our export balance with the less-developed countries of Asia and Africa declined as imports increased. However, there was a sharp swing in the opposite direction in our trade position with the Latin American countries, from a deficit

of 1/2 billion at an annual rate in the second half of 1968 to a surplus at that rate in the first 8 months of this year. This shift resulted from a sharp drop in imports, particularly coffee and petroleum.

The export balance with continental Western European countries was about the same, with both exports and imports larger. Improvement in the balance with the EEC countries was just about offset by worsening in the balance with other countries of continental Western Europe. Our trade position with the United Kingdom -- a small import balance -- showed little change.

Economic developments in other industrial countries. Economic activity in most industrial countries through the third quarter of this year showed no signs of flagging. However, general expectations are that restrictive policy measures taken in various countries will combine to produce some slowdown in growth later this year and early in 1970. In Canada, industrial production should rebound in the fourth quarter following the settlement of damaging strikes, but in 1970 it is expected to level off and might even decline. The German and Japanese economies are expected to expand at a somewhat reduced rate, while in France extremely restrictive monetary policy, possibly reinforced by further fiscal restraint, may result in a sharply reduced rate of growth early next year. Only in the United Kingdom is the rate of expansion expected to quicken next year.

INDUSTRIAL PRODUCTION
(1963=100)

	1968		1969		
	Q-III	Q-IV	Q-I	Q-II	Q-III
Germany	129	135	140	144	145 ^{a/}
France	131	139	138	141	141 ^{a/}
Italy	136	140	144	146	149 ^{b/}
Belgium	121	123	129	130	134 ^{c/}
Netherlands	145	151	153	157	159 ^{c/}
United Kingdom	120	122	123	123	125 ^{b/}
Japan	194	203	205	218	224 ^{b/}
Canada	138	142	145	144	143 ^{a/}
United States	133	135	137	139	140

^{a/} July-August known; September estimated.

^{b/} July known; August-September estimated.

^{c/} estimated.

Economic developments through the rest of this year and in 1970 will be influenced by the revaluation of the German mark. Early in 1970, another influence will also be felt, as economic activity in the United States declines and our imports level off. By contrast, the impact of last August's devaluation of the French franc is expected to be very slight.

The DM revaluation will have some disinflationary effect on the German economy, but will nevertheless provide a spur to economies of other countries, especially in Europe. Alternative measures that might have been used to brake the speed of the German expansion would not have had this desired effect. The expected U.S. slowdown, on the other hand, will remove a stimulating influence on the other countries' activity. The impact of these two factors will be felt with a considerable and varying lag and the economies of the various countries will be differently affected by them, depending partly on the relative importance to them of the German and U.S. markets.

TRADE OF SELECTED COUNTRIES WITH GERMANY AND THE U.S. IN 1968
(in per cent of each country's own trade)

	<u>Trade with Germany</u>		<u>Trade with the U.S.</u>	
	<u>Exports</u>	<u>Imports</u>	<u>Exports</u>	<u>Imports</u>
Germany	--	--	11	11
France	19	21	6	10
Italy	19	18	11	12
Belgium-Luxemburg	21	21	9	8
Netherlands	28	26	5	11
United Kingdom	5	6	14	13
Japan	2	3	32	27
Canada	2	2	68	73
United States	5	8	--	--

As yet there are no signs that the German boom is moderating. Real GNP in the first half of 1969 grew at a 6.4 per cent annual rate, and is expected to grow even slightly faster in the second half of the year. Third quarter economic indicators so far support these estimates: in July, new orders for manufactured goods rose by 4 per cent over the second quarter average, with orders for capital goods rising by 3 per cent and those for consumer goods rather more, indicating an expected shift in the demand structure.

The strength of both domestic and foreign demand has forced the economy to operate very close to capacity, which, however, appears to have been higher than previously estimated. Unemployment is very low and unfilled vacancies outnumber the unemployed by 8-1/2 times in spite of the fact that the number of foreign workers in Germany is now at an all-time high. Price increases this year through August--since the introduction in January of border tax adjustments--have been moderate; wholesale prices from January to August rose by about 2.5 per cent, while the increase in retail prices during this period just barely exceeded 1 per cent. However, wage negotiations now going on are expected to result in wage increases higher than in previous years and price rises may be expected to accelerate before long.

For the next few months, the prospects--on an assumption of unchanged economic policy--are for continuing expansion. Order backlogs, particularly in the capital goods industries, are very large and equivalent to more than 5 months of production--a record level. However, delivery delays may divert some new demand to outside

sources. Also, if the new Brandt government puts through its intention to remove tax incentives to capital investment, future demand may moderate to some extent. A moderation of external demand is also expected after the government establishes a new parity for the DM; a large number of outstanding foreign orders were clearly of an anticipatory nature, so that the current growth rate of orders is above the underlying basic rate.

Some of the moderation will be offset by rapid increases in the demand for consumer goods -- following large increases in disposable income -- and by rapidly increasing demand for non-residential private construction. Building permits for business construction increased 9 per cent between March/April and May/June.

In contrast to moderate domestic price increases thus far this year, export prices of German goods to foreign buyers have risen much faster. Since the end of 1968, these prices have increased by over 5 per cent, suggesting that most of the 4 per cent reduction of the border tax rebate on exports has been passed on to foreign buyers. This sizable increase in German export prices, however, has been only slightly higher than price increases in other countries. The German trade surplus for the first 8 months of 1969 stood at \$2.3 billion, not significantly below the \$2.6 billion surplus a year earlier.

The German border tax adjustments are now suspended until December 1, and it seems unlikely that they will be resurrected -- even in part -- after the new mark parity is set. Thus, the effect of the DM revaluation will be reduced by 4 percentage points at least, and probably by a somewhat larger amount to take account of the fall in the

forward exchange rate differential. Nonetheless, even a small revaluation will have some effect on German exports but the timing and amount of the impact will depend on the extent to which the revaluation will be passed on in final prices. Experience with the border tax adjustment of last year shows that lags can be substantial and that German exporters -- with generally high profit margins -- react very flexibly to market conditions.

The projected leveling of U.S. imports in the first half of 1970 will also adversely affect German exports. German automobile and steel exports to the United States -- 4 per cent of all German exports in 1968 -- may prove to be quite sensitive to the level of demand and competition in the U.S. market.

Two and a half months after the franc devaluation the French economy still shows signs of severe overheating. Political considerations have prevented the Government from imposing the much needed strong fiscal restraint and the authorities are relying heavily on a very restrictive monetary policy. Short- and medium-term bank credits will be allowed to expand at a very low rate through mid-1970, reserve requirements for commercial banks were raised when the Bank of France's discount rate was set at a record high of 8 per cent earlier this month, and banks are heavily penalized for exceeding credit expansion limits.

In France all sectors, except the construction industry, contributed to the high level of activity in 1969 and capacity limits, in part caused by a shortage of skilled labor, were reached in most industries at varying times, resulting in an erratic behavior of the

industrial production index. Although French exports have been increasing rapidly, the inability of the domestic economy to satisfy internal demand, coupled with anticipatory buying that preceded the franc devaluation, caused imports to soar, and the current account deficit this year is expected to exceed \$1.2 billion. The trade deficit in September, the first full month after devaluation, has been a record high for France according to preliminary figures published last week.

The government's policy stance is now strongly restrictive, with fiscal policy being moderately so and monetary policy extremely tight. However, the full effect of these policies and the devaluation will not be felt until next year. The revaluation of the DM should benefit the French trade balance, but structural rigidities within the economy will hamper the needed shift of resources to production for export. Wage negotiations, about to be concluded, will probably result in higher wage increases than the authorities deem desirable. Most French exporters, anticipating higher wage costs, did not reduce their foreign currency prices following the devaluation. French-U.S. trade is not very large and most French exports to the United States are not very sensitive to small downward changes in the level of U.S. demand.

Following a decline in the first quarter of 1969, the United Kingdom's GDP staged a moderate recovery in the second quarter. The recovery was led by exports and slightly increased consumer spending, with aggregate investment outlays remaining unchanged. In the third quarter scattered data suggest that another moderate quarter-to-quarter rise in GDP will be registered. Growth is expected to continue in 1970, probably at a somewhat faster pace, especially if some restraint is removed early next spring.

Price increases this year have been moderate. The retail price index rose by 1.7 per cent from January/March to July/August. Wages during this period grew by 2.7 per cent. Unemployment reportedly increased from about 2.2 per cent in the first quarter to 2.5 per cent in the third quarter. However, the actual rise may have been less, as doubts exist about the accuracy of the seasonal adjustment. Unemployment in excess of 2 per cent is high by British standards, but current unemployment rates may not be strictly comparable with the rates of the past, because of more generous unemployment benefits and a rise in structural unemployment.

During the second quarter of 1969 the United Kingdom had a substantial surplus on the basic balance of payments, which had been in deficit in the first quarter. Moreover, in two successive months-- August and September--a large surplus on the merchandise trade account was recorded. The authorities have not eased the restraints imposed on the economy since the 1967 devaluation of the pound and earlier this week announced that the import deposit scheme, due to expire on December 5, will be extended in a slightly milder form for another 12 months.

Although British-German direct trade is not very significant, the DM revaluation should work out to Britain's advantage in many third markets where the goods of the two countries compete. However, the beneficial effects of the mark parity change on trade will be felt with some lag. The rise in the floating DM exchange rate has already helped to reverse speculative capital flows that in the past caused reserve losses for the United Kingdom.

By contrast, a leveling off or a drop in U.S. imports will rapidly prove harmful to the United Kingdom. The United States is Britain's largest customer and accounted for 14 per cent of that country's exports in 1968.

In Italy the expansion of activity has remained strong during this year, with stronger than expected domestic demand leading the expansion. This has resulted in an acceleration of the rate of import growth and some shrinkage of the Italian trade surplus. Wages have been increasing faster than in recent years and price increases have been more marked after a prolonged period of exceptional stability. Expansion is expected to affect Italian imports only very slightly, but Italian exports should benefit fairly strongly. About one-tenth of all German imports originate in Italy and, in addition, Italian manufacturers compete with German exporters in many third markets.

In the Netherlands economic expansion continued through July at a very rapid pace, led by an exceptionally good performance of the export sector. In August, unfilled job vacancies exceeded the

number of unemployed by nearly 1-1/2 to 1. It appears that the economy is operating nearly at capacity with a shortage of skilled labor being a major restraint on further rapid expansion of production. Dutch price developments this year were very unsatisfactory--with consumer prices rising 6 per cent from mid-December to mid-April--and the authorities were forced to impose a price freeze in April. The freeze was lifted in September after the consumer price index showed a small decline from the April level.

The DM revaluation should benefit Dutch exports, more than a fourth of which go to Germany. Thus the economic expansion may be expected to continue, perhaps at a slightly slower rate, through the spring of 1970. At the same time, it is not expected that Dutch imports from Germany will decline to any great extent and their higher prices could intensify inflationary pressure. If the DM revaluation is sizable, the Dutch authorities may decide to revalue the guilder, but by a smaller percentage than the change in the parity of the mark.

The Belgian economy continued to expand strongly through the year and it is expected that the expansion will continue, although somewhat more slowly, through the first half of 1970 in spite of the very sharp increases in interest rates this year. The revaluation of the DM will clearly benefit Belgian exports, but the increased cost of imports from Germany will intensify the pressure on Belgian prices, which at the retail level have recently been rising at about a 4 per cent annual rate.

The inflationary pressures in Japan, led by sustained consumer spending and private equipment outlays, may cause some deceleration in the rate of industrial production expansion as policies become more restrictive. Increasing imports caused a swing in the trade account from a surplus of \$178 million in March to a deficit of \$7 million in August. Pressure on prices has been acute, and consumer prices in August were 8 per cent higher than a year earlier--a much higher rate of increase than in recent years.

Wage increases have also been exceptionally high, with nominal wages in July 21 per cent higher than a year earlier. The signs of overheating in the economy caused the authorities to tighten monetary policy significantly early in September. Further restrictive measures may be expected should the economy not show signs of cooling off.

While direct German-Japanese trade is quite small, the Japanese trade balance should nevertheless benefit from the DM revaluation through shifts in third markets. On the other hand, the U.S. market is of crucial importance to Japan--nearly a third of Japanese exports come here--and the expected leveling of U.S. imports will significantly affect the Japanese economy.

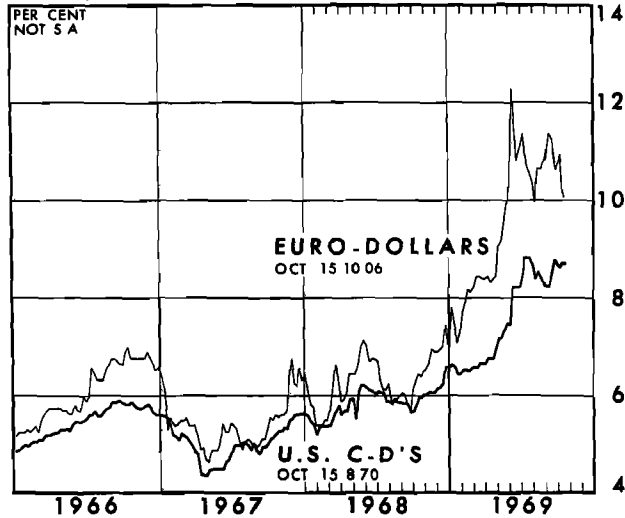
In Canada, industrial production, handicapped by a record number of man-hours lost through strikes, has shown little change since early 1969 and, after some improvement in the last quarter of this year, is expected to level off again during the first half of 1970. In the second quarter of 1969 GNP fell by about 0.2 per cent.

To some extent, demand has moderated as a result of deliberately tight monetary and fiscal policies, which appear to be resulting in a desired slowing of price advances. The earlier rise in Canada prices may have affected the competitiveness of Canadian exports, which have lately showed a decrease in their rate of growth. However, other factors have probably been more important--world wheat glut, iron ore, steel and nickel strikes. Should labor unrest end in the near future--the only major strike still in progress is in the nickel industry--the industrial production index in the fourth quarter may show a sharp increase from the depressed level in the third quarter. Unless there is some easing of the now very tight monetary policy, the Canadian economy may experience a mild recession in the first half of 1970. The projected slowdown of the U.S. economy will contribute to this outcome, since two-thirds of Canadian exports go to the United States.

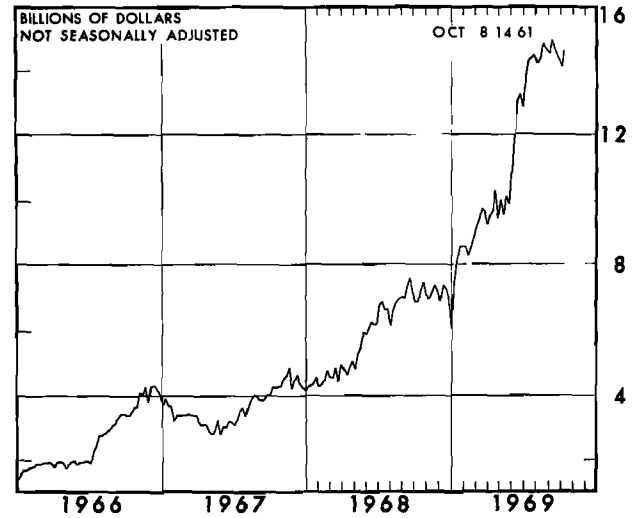
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED

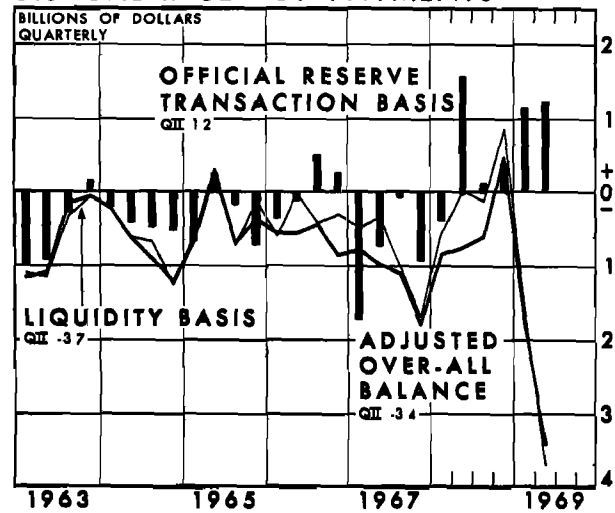
90-DAY RATES



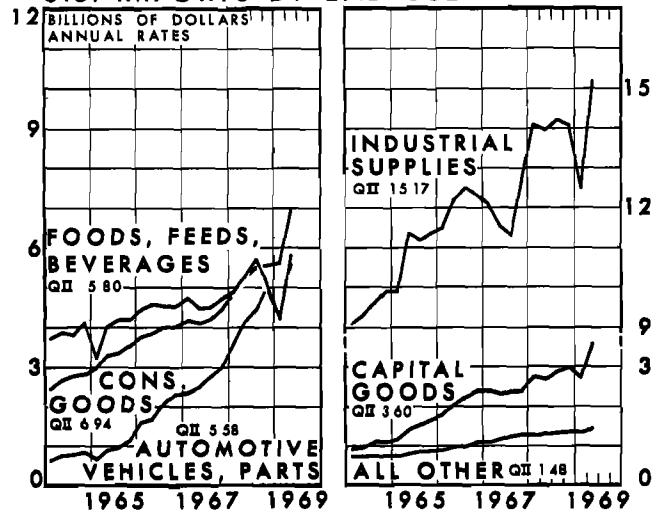
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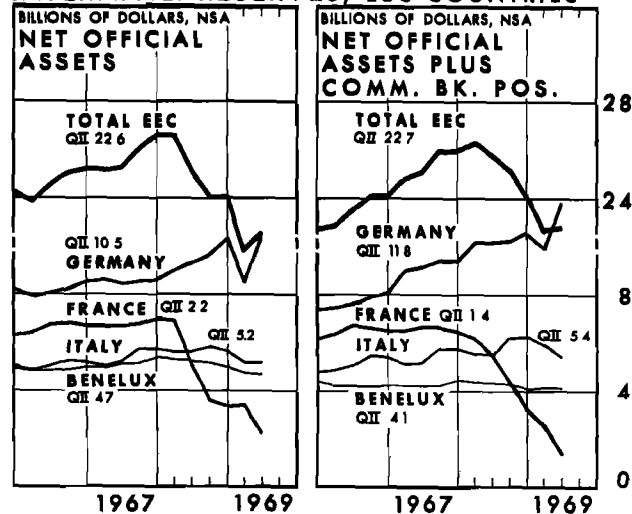
U.S. BALANCE OF PAYMENTS



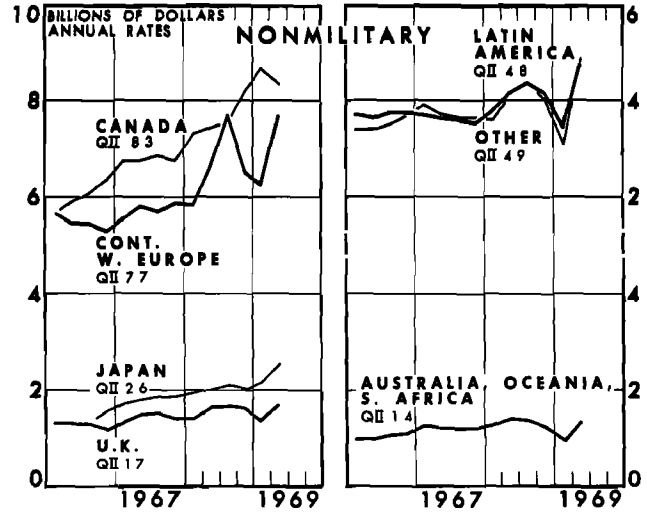
U.S. IMPORTS BY END USE



INTERNATL. RESERVES, EEC COUNTRIES



U.S. EXPORTS BY AREA - NONAGRICULTURAL



APPENDIX A: RECENT BORROWING OPERATIONS OF FHLB AND FNMA.*

The Federal Home Loan Banks and Federal National Mortgage Association recently have sharply increased their borrowings in the securities markets to provide funds to the housing industry. During the second and third quarters of this year, these Agencies borrowed a total of \$4.2 billion of new money as compared with \$2.2 billion of new cash raised during the same period of 1966.

1. NET NEW MONEY RAISED BY FHLB AND FNMA^{1/}
(In millions of dollars)

Quarter	FHLB	FNMA
1966 I	- 161	764
II	1,249	621
III	456	-91
IV	94	622
1967 I	-1,118	210
II	-1,156	68
III	- 425	-151
IV	- 100	992
1968 I	65	562
II	576	406
III	- 200	145
IV	200	344
1969 I	- 54	816
II	874	884
III	1,550	884

^{1/} Excluding participation certificates.

This note first examines briefly the relation of liquid asset positions of the Home Loan Banks and FNMA to their market borrowing schedules. Second, given the need for market borrowing, it looks at pricing of new issues in the context of an already heavy capital markets calendar, with some reference to dealer positions in Agencies during these months.

* - Prepared by Paul L. Kelty, Economist, Government Finance Section, Division of Research and Statistics; with the assistance of Ann Lacy Shockley.

Timing of Market Borrowing. In the first six months of 1969, the Home Loan Banks were able to hold down their market borrowing by drawing down their liquidity. As shown in table 2, Home Loan Bank liquid assets (cash plus investments) declined from \$2.5 billion to under \$1.6 billion between December 1968 and July 1969. The latter amount appears close to what the Banks regard as a minimum liquidity cushion, considering that their net payments to savings and loan associations during a single month have amounted to as much as nearly \$1 billion. In 1966, for example, the low point in their liquid asset position was \$1.3 billion.

As would be expected, the sharpest drops in their liquid asset holdings often occurred in the months which included savings and loan quarterly reinvestment periods. For instance, in July of this year, the decline in these assets was over a half billion dollars, thereby financing a large portion of the nearly \$1 billion in net advances. Similarly, in other months, by using their liquid assets as a cushion, the Home Loan Banks have been able to schedule their borrowing in a much smoother pattern than their need for funds to finance advances to savings and loan associations.

If advances to members continue large in the months ahead--as seems likely given prevailing interest rate relationships--the Home Loan Banks will have to undertake further very large borrowings in the securities markets. Moreover, from here on out their advances to savings and loan associations will have to depend more on borrowed funds in view of their reduced liquidity reserves. Also, if market rates should decline appreciably, the Home Loan Banks, like many other borrowers, can be expected to tap the market to rebuild their liquidity position.

Table 2 reveals a number of interesting differences in the management of the liquidity position of FNMA in contrast to that of the Home Loan Banks. FNMA apparently has only a small demand for liquid assets and is willing to utilize them fully when it does have them. At the latest reading--in August--the Association had a working balance of only \$7 million, a very sharp drop from June and July.

An important distinction in the financial management of FNMA versus that of the FHLB's is that the former decides in advance the total amount of mortgage holdings it will take. In contrast, the Home Loan Banks do not know ahead of time the size of net advance to S and L's. FNMA also raises some of its money on quick notice through the sale of discount notes, thus supplementing the sale of coupon-bearing obligations, which follows a more regular pattern.

2. LIQUIDITY POSITIONS OF FHLB AND FNMA--1966 AND 1969
(millions of dollars)

	FHLB						FNMA					
	Changes			Levels			Changes			Levels		
	Borrow-ings	Liquid assets 1/	Net Advances2/	Borrow-ings	Liquid assets1/	Net Advances2/	Borrow-ings	Liquid Assets1/	Mortgage Holdings	Borrow-ings	Liquid Assets1/	Mortgage Holdings
1966 - Jan.	-153	-212	+ 48	5,068	1,557	5,000						
Feb.	- 18	+123	-107	5,050	1,680	4,893						
Mar.	+ 10	+ 71	- 60	5,060	1,751	4,833						
Apr.	+375	-435	+818	5,435	1,316	5,651						
May	+460	+279	+210	5,895	1,595	5,861						
June	+414	+518	- 93	6,309	2,113	5,768						
July	+285	-575	+838	6,594	1,538	6,606						
Aug.	+ 21	+215	-145	6,615	1,753	6,461	n. a.			n. a.		
Sept.	+150	+165	- 21	6,765	1,918	6,440						
Oct.	+194	+164	+ 40	6,959	2,082	6,480						
Nov.	+100	+215	-261	6,859	2,297	6,219						
Dec.	--	+339	-321	6,859	2,636	5,898						
1969 - Jan.	--	-370	+370	4,701	2,131	4,246	+227	- 1	+167	6,603	1	7,334
Feb.	-100	+ 20	- 79	4,601	2,151	4,167	+215	+ 1	+176	6,818	2	7,510
Mar.	+ 46	+127	- 80	4,647	2,278	4,087	+374	+ 51	+179	7,192	53	7,689
Apr.	+374	-128	+498	5,021	2,150	4,585	+124	- 22	+162	7,316	31	7,851
May	+500	+316	+184	5,521	2,466	4,769	- 75	- 22	+147	7,241	- 9	7,998
June	--	-361	+366	5,521	2,105	5,135	+835	+353	+177	8,076	362	8,175
July	+500	-517	+986	6,021	1,588	6,121	+ 16	-183	+242	8,092	179	8,417
Aug.	+551	+ 11	+575	6,572	1,599	6,696	+268	-172	+470	8,360	7	8,887
Sept.	+500	+155	+353	7,072	1,754	7,049	+600	+ 37	+439	8,960	44	9,326
Oct ^{p/}	+500	n.a.	n.a.	7,572	n.a.	n.a.	+600	n. a.	n. a.	9,560	n. a.	n. a.

1/ Cash plus Federal securities.

2/ Advances to members less deposits by members.

n.a. -- not available.

p/ Preliminary.

Marketing of New Issues. The yields on new FHLB and FNMA offerings rose steadily over the first 9-months of 1969, reaching a record 8.75 per cent on October 2 on a 16-month FNMA issue, more than 2 percentage points above the yield set on a 1-year FNMA offering in January. To a large extent, these increases reflect the general rise in interest rates that has taken place in 1969. Importantly, however, the spreads on these new issues from outstanding direct Government securities of comparable maturities also widened considerably on average in the second and third quarters of 1969 (See Table 4). There has also been a concentration of the major share of recent FHLB and FNMA financings in the shorter-term area. In the first three quarters of this year, 20 of the 23 offerings of these Agencies have had final maturities of 3 years

3. MATURITY AREAS OF FHLB AND FNMA ISSUES^{1/}

	Maturity, in Years			
	Within 1	1-3	3-5	Over 5
	Number of Issues			
1966 Jan.-Sept.	7	8	--	1
1967 Jan.-Sept.	3	7	4	2
1968 Jan.-Sept.	7	6	2	--
1969 Jan.-Sept.	6	14	3	--
	Amounts Issued ^{1/} --In millions of dollars			
1966 Jan.-Sept.	3,224	3,975	--	410
1967 Jan.-Sept.	1,235	2,625	1,050	600
1968 Jan.-Sept.	2,661	1,725	950	--
1969 Jan.-Sept.	2,800	4,996	701	--

^{1/} Excluding participation certificates.

or less, as shown above. Similarly, during January-September 1966, 15 of the 16 issues offered by FHLB and FNMA were due within 3-years. In contrast, in the corresponding period of 1967--a time of easier credit conditions--the mortgage-related Agencies sold 10 issues due within 3 years and 6 with longer maturities.

4. FHLB AND FNMA FINANCINGS--1969^{1/}
(in millions of dollars)

Offering Date	Agency	Amount	New Money	Maturity	Reoffering Yield	Spread from Govts. ^{2/}
(1) Jan. 15	FHLB	300	--	7 mo.	6.62	.08
(2) Jan. 24	FNMA	250	250	1 yr.	6.60	.35
(3) Feb. 14	FHLB	400 200	((-100	8 mo. 2 yr.	6.62 6.60	.22 .31
(4) Feb. 26	FNMA	250	250	3 yr.		.37
(5) Mar. 12	FHLB	346	46	1 yr.	6.85	.48
(6) Mar. 27	FNMA	250	162	26 mo.	6.85	.56
(7) Apr. 15	FHLB	500 200	((374	9 mo. 16 mo.	6.75 6.70	.51 .52
(8) Apr. 29	FNMA	350	50	2-1/2 yr.	6.85	.55
(9) May 14	FHLB	350 150	((500	9 mo. 2 yr.	7.00 7.00	.72 .57
(10) May 28	FNMA	400 200	((350	13 mo. 28 mo.	7.38 7.40	.80 .75
(11) Jun. 12	FHLB	550	--	1 yr.	8.00	.85
(12) Jun. 26	FNMA	250	--	17 mo.	8.10	.86
(13) Jul. 15	FHLB	500 400	((500	10 mo. 19 mo.	8.00 8.00	.60 .51
(14) Aug. 13	FHLB	650 201	((551	1 yr. 5 yr.	8.20 7.65	.58 .58
(15) Aug. 28	FNMA	350 250	((600	14 mo. 5 yr.	8.30 7.85	.68 .74
(16) Sep. 11	FHLB	650 250	((500	10 mo. 19 mo.	8.40 8.38	.82 .64
(17) Oct. 2	FNMA	400 200	((600	16 mo. 29 mo.	8.75 8.70	.69 .56
(18) Oct. 15	FHLB	650 250	((500	1 yr. 25 mo.	8.25 8.20	.59 .61

^{1/} Excluding the regular sales of FNMA discount notes.

^{2/} Estimated from a segment of the Treasury constant maturity yield curve, using the 6-month bill yield on an investment basis where necessary.

Most of the FHLB and FNMA financings in the last few months met good initial market receptions, partly because their yields were high enough to attract an increasing number of investors, and most of the issues were quoted at premiums just after coming to market; as indicated in the following table.

5. PRICE QUOTATIONS IN SECONDARY MARKET^{1/}
(in 1/32's)

Offering Date	Agency	Issue	First 3 trading days after offering		
			(1)	(2)	(3)
Aug. 13	FHLB	8.20 of 8/70	100.00--.03	100.01--.02	100.02--.03
		7.65 of 8/74	100.02--.05	100.05--.08	100.07--.10
Aug. 28	FNMA	8.30 of 11/70	100.00--.01+	100.00--.01	99.31--100.01
		7.85 of 9/74	99.23--.27	99.14--.22	99.04--.12
Sept. 11	FHLB	8.40 of 7/70	100.00--.02	100.00--.02	100.01--.03
		8-3/8 of 4/71	100.02--.06	100.00--.06	100.01--.05
Oct. 2	FNMA	8.75 of 2/71	100.05--.08	100.03--.08	100.07--.10
		8.70 of 3/72	100.10--.14	100.09--.15	100.13--.18
Oct. 15	FHLB	8.25 of 10/70	100.01--.03	100.02--.04	100.04--.07
		8.20 of 11/71	100.0+--.06	100.05--.07	100.10--.14

^{1/} All issues initially priced at par.

One issue which failed to sell well, however, was the 5-year FNMA option marketed at the end of August, when rates generally were dimbing to new peaks. The 7.85 per cent yield was priced too close to the yields on outstanding Agencies in the 5-year area, and the issue was bid nearly a point below par after three days on the market. In an effort to lighten their inventories of this issue, dealers experienced an underwriting loss, since any trading below about 99-25/32 would wipe out the dealers' reoffering spread.

The improvement that has characterized the Government and other securities markets since the beginning of October also has affected the Agency market. In consequence, the 8.25 and 8.20 per cent

yields set on the 1-year and 25-month FHLB offerings on October 15 were well below the 8.75 and 8.70 per cent rates FNMA had to pay on roughly comparable maturities just two weeks earlier. A special factor helping the Agency market is the growing awareness of the attractive interest return. A large motor company, for instance, recently made substantial purchases of short-term Agency issues.

Dealer Positions. Dealers' total positions in all Agency issues fluctuated widely, as the accompanying chart shows, in response to the size, timing and attractiveness of new issues. 1/ The generally advanced levels of dealer positions in Agency securities between April and July reflected congestion in the Agency market during that period. In view of the even larger amount of Agency borrowing in the third quarter, it is surprising that dealer positions have remained relatively low since August. Apparently Agency offerings were priced sufficiently attractively to enable a quick distribution by the underwriters. Thus the Agency market now is in a good technical position and there is no immediate difficulty in sight for the marketing of the forthcoming Agency borrowing.

1/ The chart takes special note of FHLB and FNMA financing operations, but dealer inventories are also influenced by offerings by Federal Land Banks, Federal Intermediate Credit Banks and Banks for Cooperatives, as well as acquisitions in the secondary market.

DEALER POSITIONS IN FEDERAL AGENCY SECURITIES

(Numbers in parentheses refer to 1969 FHLB and FNMA financings as numbered in Table 4.)

