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Part II

CONFIDENTIAL (FR)

CURRENT ECONOMIC
and
FINANCIAL CONDITIONS

Prepared for the
Federal Open Market Committee

By the Staff

BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM

November 13, 1974

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DOMESTIC NONFINANCIAL SCENE

November 13, 1974

II -- T - 1

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

	Latest Data			Per Cent Change From		
	Period	Release Date	Data	Preceding Period	Three Periods Earlier	Year Earlier
				(At Annual Rates)		
Civilian labor force	Oct.	11/1/74	92.0	2.3	3.8	2.5
Unemployment rate (per cent)	Oct.	11/1/74	6.0	5.8 1/	5.3 1/	4.6 1/
Insured unemployment rate (%)	Oct.	11/1/74	3.6	3.4 1/	3.4 1/	2.6 1/
Nonfarm employment, payroll (mil.)	Oct.	11/1/74	77.4	.5	2.0	1.4
Manufacturing	Oct.	11/1/74	19.8	-5.1	-2.9	-1.2
Nonmanufacturing	Oct.	11/1/74	57.7	2.4	3.7	2.3
Private nonfarm:						
Average weekly hours (hours)	Oct.	11/1/74	36.6	36.7 1/	36.7 1/	37.0 1/
Hourly earnings ($)	Oct.	11/1/74	4.33	11.2	10.4	8.8
Manufacturing:						
Average weekly hours (hours)	Oct.	11/1/74	40.0	40.1 1/	40.2 1/	40.6 1/
Unit labor cost (1967=100)	Sept.	10/31/74	135.4	.9	10.9	9.8
Industrial production (1967=100)	Oct.	11/15/74	124.9	-6.7	-1.9	-1.7
Consumer goods	Oct.	11/15/74	128.3	-1.9	-5.2	-3.2
Business equipment	Oct.	11/15/74	132.4	6.4	3.4	4.9
Defense & space equipment	Oct.	11/15/74	83.8	.0	5.8	4.8
Materials	Oct.	11/15/74	128.2	-9.3	.6	-2.2
Consumer prices (1967=100)	Sept.	10/22/74	151.9	15.0	13.5	12.1
Food	Sept.	10/22/74	164.7	22.3	11.8	11.3
Commodities except food	Sept.	10/22/74	141.7	12.0	15.5	13.9
Services 2/	Sept.	10/22/74	155.9	13.2	13.3	10.9
Wholesale prices (1967=100)	Sept.	10/10/74	167.3	1.1	31.3	19.7
Industrial commodities	Sept.	10/10/74	163.3	12.4	25.7	27.9
Farm products & foods & feeds	Sept.	10/10/74	179.5	-23.0	49.3	3.3
Personal income ($ billion) 3/	Sept.	10/16/74	1174.0	9.1	10.7	8.7
				(Not at Annual Rates)		
Mfrs. new orders dur. goods ($ bil.)	Sept.	11/1/74	46.5	5.9	.6	13.1
Capital goods industries:	Sept.	11/1/74	13.7	9.1	- .1	16.5
Nondefense	Sept.	11/1/74	11.9	.7	-1.1	14.4
Defense	Sept.	11/1/74	1.8	-44.8	1.8	33.3
Inventories to sales ratio:						
Manufacturing and trade, total	Aug.	10/15/74	1.47	1.47 1/	1.46 1/	1.46 1/
Manufacturing	Sept.	11/1/74	1.65	1.63 1/	1.65 1/	1.61 1/
Trade	Aug.	10/15/74	1.31	1.31 1/	1.31 1/	1.32 1/
Ratio: Mfrs.' durable goods inventories to unfilled orders	Sept.	11/1/74	.682	.678 1/	.693 1/	.737 1/
Retail sales, total ($ bil.)	Oct.	11/11/74	45.9	- .4	-1.0	6.8
GAF	Oct.	11/11/74	11.9	- .2	- .2	8.1
Auto sales, total (mil. units) 3/	Oct.	11/7/74	8.1	-18.1	-15.5	-21.8
Domestic models	Oct.	11/7/74	6.4	-20.7	-22.1	-26.8
Foreign models	Oct.	11/7/74	1.7	-5.9	25.6	6.3
Plant & equipment expen. ($ bil.) 4/						
All industries	1975	11/8/74	125.38	--	--	11.8
Manufacturing	1975	11/8/74	55.40	--	--	21.3
Housing starts, private (thous.) 3/	Sept.	10/17/74	1,120	.4	-29.8	-39.3
Leading indicators (1967=100)	Sept.	10/31/74	171.9	-2.5	-2.3	4.1

1/ Actual data. 2/ Not seasonally adjusted. 3/ At annual rate. 4/ Planned--McGraw-Hill Fall sur.

DOMESTIC NONFINANCIAL DEVELOPMENTS

Declines in economic activity have become deeper and more pervasive in recent weeks, and incoming statistics have begun to display the cumulative downward movements characteristic of a typical business recession. Moreover, a protracted coal strike could have a substantial--though temporary--depressing effect on the economy. Meanwhile, upward price pressures continue strong--although signs of slowing have appeard in some commodity prices--and wage pressures remain intense.

Industrial production in October is estimated to have declined more than 1/2 per cent, as cutbacks in nonautomotive consumer durable goods and industrial materials continued to spread. The index was about 2 per cent below a year earlier.

Business equipment production was apparently maintained at about the level reached in June. Auto assemblies were at an 8.3 million unit annual rate, up 8 per cent from September. But this level was far above the rate of sales, and with dealer stocks mounting, sharp cutbacks in production and layoffs have already been announced. Meanwhile output of other consumer durables continued to fall in October, but factory unit sales of such goods apparently dropped more than output, so that factory stocks rose further. Output of construction products is also estimated to have been cut back further because of the continued weakness in building activity. Declines in materials output seem to be widening, with cutbacks indicated in nonferrous metals, fabricated metal parts, textiles, rubber, crude oil, and paperboard. Steel production, however, has remained strong, probably reflecting in part hedge buying by consumers against the possibility of a prolonged coal strike.

A further decline in industrial production appears likely this month, with auto assemblies drastically reduced and efforts increased to cut excessive inventories in other industries. The bituminous coal strike is also a dampening factor.

Sluggish industrial production this year in the face of further increases in capacity has resulted in declines in capacity utilization rates. Thus, the Board's index of capacity utilization of major materials edged off further to 87 per cent in October, to a level about 8 per cent below the peak of July 1973. The October decline would have been larger had it not been for the increase in steel.

Retail sales continue weak. Sales of new domestic-type autos fell sharply in October to a 6.4 million unit annual rate, a fifth below September and more than one-fourth below a year earlier. Unit stocks of new domestic-type autos at the end of October were at a record level for the period. Major reasons for weakness in auto demand appear to be the sharp rise in prices of 1975 models (including the cost of mandated equipment), the erosion of real wages, and growing consumer apprehension about the future. The October decline in auto sales was even sharper than expected, and the staff has revised downward its estimate of auto sales in the current quarter. Sales of foreign autos, however, remained strong, probably because the delay in the introduction of 1975 foreign models has temporarily given them a price advantage in relation to American models.

An executive of a major auto company recently asserted that sharply reduced availability of bank financing has been a major influence in a decline in new auto sales. An informal staff survey of about 30 commercial banks suggests that although bank financing is less readily available than earlier, the change in consumers credit availability has been quite moderate.

The labor market weakened further in October. The unemployment rate rose to 6.0 per cent,up 0.2 percentage points from September; the rate in October 1973 was 4.6 per cent. There was a particularly sharp rise in the unemployment rate of adult males last month, from 3.9 per cent to 4.3 per cent. Since the reporting date in October, there have been numerous reports of layoffs, and both initial claims and the insured unemployment total have increased further, so that another increase in the unemployment rate of experienced workers is likely in November.

Growth in the civilian labor force recently has been more rapid than past experience would suggest for a period of declining output--in October the labor force was more than 2 million higher than a year earlier. The composition of the growth (adult women up 1 million, adult men up 800,000 and teenagers up 300,000) suggests that the impact of inflation in reducing real wages has induced many teenagers and women to enter the work force. In addition, workers who have been laid off have tended to stay in the labor force, seeking work.

The rise in employment over this past year has also been surprisingly large. The total payroll figures show an increase of 1.1 million, with large increases in service sectors partially offset by a 400,000 decline in goods-producing industries.

Outlays for business fixed investment may already have peaked in real terms. In constant dollars, orders for nondefense capital goods were off 5.3 per cent in the third quarter and in September real unfilled orders for nondefense capital goods declined for the first time in over two years. Nonresidential construction activity in real terms has now declined for two consecutive quarters and construction commitments remain weak.

The McGraw-Hill survey, taken in October, also suggests weakness in the capital goods sector. This survey reports a prospective increase of about 12 per cent in business plant and equipment spending for 1975, close to the indications from two other private surveys. But McGraw-Hill also found that business expects prices it pays for fixed capital to rise by some 12 per cent, indicating no increase in the physical fixed volume of investment.

All of the private surveys indicate that expected outlays in the manufacturing sector, particularly those of materials producers who have recently experienced severe pressures on existing capacity, remain relatively strong. However, public utilities and automobile producers have been scaling down capital spending plans for some time, and the McGraw-Hill survey suggests that other industries are now also cutting back their investment plans--as would be expected in a period of weakening economic activity. Aprroximately 54 per cent of the survey respondents indicated they had reduced earlier plans for this year, with over half of these citing interest rates as the primary reason for such action. Secondary reasons include a falling off in demand and a lack of corporate liquidity. Based on past recession experience, the prospective weakness in economic activity may well lead to additional cutbacks in fixed investment plans.

The outlook for business inventory spending is also beginning to look much more questionable. New orders for durable goods recently have been relatively flat in current dollars--and declining in real terms. The third quarter rate of book value inventory accumulation was well ahead of the second quarter, but the increase was attributable to inflation. On a N.I.A. basis, investment in nonfarm business inventories declined. Reports indicate that a number of firms are already attempting to liquidate excessive inventories. If a coal strike of significant duration materializes, a sharp reduction in coal and steel stocks would ensue.

New residential construction continues in the doldrums. Private housing starts remained at a 1.1 million unit annual rate in

September, while permits declined again. The third quarter average of 1.2 million starts was nearly a fourth below the already reduced second quarter rate and the lowest in over seven years, mainly because of multi-family units. Even if money market conditions should ease somewhat further, housing starts are not likely to improve this winter, because savings institutions are expected to restore their liquidity before significantly increasing their mortgage loan commitments. In addition to the normal lag between an upswing in deposit flows and a rise in housing starts, the recovery of starts may be dampened by higher building and land costs and the large numbers of new units still in the market. In late September, merchant builder inventories of unsold new single-family homes equaled a near-record 10-1/2 months' supply.

In contrast to the weakness in new home sales, the rental market apparently strengthened in the third quarter. The average vacancy rate for rental properties was little changed in the third quarter at a level only moderately above a year earlier. Also, existing home sales were maintained in September at near year-earlier levels, supported in part by expanded reliance on mortgage assumptions and other types of special arrangements with sellers.

Price pressures have remained intense, but with some indication of possible slowing in wholesale industrial prices. The September increase of 1 per cent in <u>wholesale prices of industrial commodities</u>--while rapid--was nonetheless the smallest rise this year.

Actually, there were declines in September in a few components--notably nonferrous metals, textiles, fuels, and lumber--and smaller increases than previously for a few others. However, advances were still substantial for most chemicals, metal products, nonmetallic minerals, and household durables. And the rise in machinery and equipment prices was only a little slower than the exceptional rate of preceding months. It should be noted that the October wholesale price index will include substantially higher prices for 1975 model cars--even after BLS adjustment for quality change.

Consumer prices advanced at a 15 per cent annual rate in September, about the same as the preceding month. Foods showed the sharpest rise, but prices of services and nonfood commodities continued to increase rapidly. Any slowing of the rise in prices at producer levels would be expected to take a number of months to work through to the retail level.

In October, prices received by farmers rose 4 per cent following a 2 per cent decline in September. Food prices are expected to rise over the months ahead reflecting shortfalls in crops of feed grains, which are expected to result in reduced supplies of pork and broilers, and a further widening of the gross retail margin. However, beef supplies, a major item in the consumer budget, are very large and are expected to exert a moderating influence on the overall advance in food prices.

Wage increases have continued large as workers attempt to maintain the purchasing power of their earnings. The adjusted average hourly earnings index for the private nonfarm economy rose at an annual rate of 11.5 per cent in the third quarter. In October the index was 9.2 per cent above a year ago; the sharpest increase was in manufacturing, but gains were also large in trade and services.

The strike in the bituminous coal industry, which began November 12, is now expected to last more than two weeks. Any settlement requires approval by the rank and file, which would take about 10 days. Costs of the settlement are certain to be high, adding to price pressures in numerous consuming industries--especially steel and steel products and utilities.

TABLE 1

SURVEY RESULTS OF ANTICIPATED PLANT AND EQUIPMENT EXPENDITURES
(Per cent change from prior year)

	1974	1975		
	BEA August Survey	Rinfret Fall Survey 1/	Edie Fall Survey 2/	McGraw-Hill Fall Survey
All industry	12.5	14.4	10	11.8
Manufacturing	20.2	22.9	17	21.3
Durables	19.2	16.1	15	13.5
Nondurables	21.2	29.9	18	29.2
Nonmanufacturing	7.7	8.5	5	5.2
Mining	12.2	17.1	- 7	63.2
Railroads	22.8	31.6	15	29.1
Air and other transportation	6.4	-13.6	- 2	3.7
Electric utilities	12.0	8.2	12	.0
Gas utilities	10.9	16.7	16	11.1
Communications	10.2	2.9	5	4.0
Commercial and other	.9	12.0	1	- 1.0
Survey errors: 1968-73 3/				
Average error		1.5	.7	- .5
Average absolute error		5.2	3.0	2.2

1/ Preliminary tabulation based on response rate of 57 per cent; confidential results.
2/ Confidential results.
3/ Errors are calculated as anticipated percentage change minus actual percentage change.

TABLE 2

MAJOR MATERIALS UTILIZATION
October 1974

(Seasonally adjusted, per cent)

	1973			1974			1974			
	II	III	IV	I	II	III	July	Aug.	Sept.	Oct.*
Textiles (yarn, fibers, woven fabric)	94.0	93.5	92.9	92.5	90.4	88.8	91.5	88.3	86.7	85.3
Paper, pulp, board	95.6	98.0	96.4	95.1	96.6	95.2	98.0	91.7	95.7	92.1
Paperboard	95.4	94.1	93.7	93.0	95.9	91.7	98.0	84.7	92.5	84.2
Petroleum Refining	97.5	95.3	92.8	84.7	90.8	89.2	90.9	89.7	86.9	88.1
Metals 1/	91.3	92.3	92.6	91.1	90.5	87.9	88.5	86.8	88.4	89.5
Basic Iron and Steel	93.4	94.3	94.7	92.6	91.5	90.0	90.7	89.5	89.6	91.8
Aluminum	92.0	92.7	95.3	98.1	99.1	98.4	99.0	98.7	97.5	96.6
Chemicals	91.2	91.1	90.0	88.6	86.7	87.3	88.4	87.8	85.8	87.0
Cement	90.3	91.8	90.7	92.7	86.1	77.6	78.3	77.9	76.6	78.5
Plywood	94.6	91.3	87.9	83.3	84.7	80.0	81.4	80.3	78.3	74.7
Major Materials	93.4	93.5	92.3	90.2	90.2	88.3	90.0	87.8	87.3	87.0

1/ Consists of basic iron and steel, aluminum, and copper.
* Estimated.

TABLE 3

LABOR FORCE, EMPLOYMENT AND UNEMPLOYMENT
(Seasonally adjusted, in thousands)

	Change from: Sept. 1974-Oct. 1974	Change from: Oct. 1973-Oct. 1974
Civilian labor force	174	2,275
Total employment	-27	862
Unemployed	201	1,413
Nonfarm payroll employment	30	1,076
Manufacturing	-84	-246

UNEMPLOYMENT RATES
(Per cent)

	Oct. 1973	July 1974	Sept. 1974	Oct. 1974
Total	4.6	5.3	5.8	6.0
Males 20+	3.0	3.5	3.9	4.3
Females 20+	4.4	5.2	5.7	5.6
Teenagers	14.0	16.2	16.7	16.9
State insured	2.6	3.4	3.4	3.6
Household heads	2.7	3.0	3.4	3.7
Married men	2.1	2.6	2.8	2.9
Full-time workers	4.1	4.8	5.3	5.6
Part-time workers	7.5	8.6	8.8	8.5
Blue-collar workers	5.1	6.1	6.8	7.3
White-collar workers	2.6	3.3	3.5	3.3
Negroes	8.4	9.4	9.8	10.9
White	4.1	4.8	5.3	5.4

TABLE 4

NEW HOUSING UNITS
(Seasonally adjusted annual rates, in millions of units)

	1974				Per cent change in September from:	
	QII	QIII	Aug.	Sept. (p)	Month ago	Year ago
Permits	1.17	.91	.90	.83	-8	-50
Starts	1.57	1.19	1.12	1.12	--	-39
1-family	.98	.86	.81	.82	+2	-17
2- or more-family	.59	.33	.31	.30	-3	-65
Under construction 1/	1.48	n.a.	1.41	n.a.	-3 2/	-18 2/
Completions	1.74	n.a.	1.45	n.a.	-14 2/	-22 2/
MEMO:						
Mobile home shipments	.44	.36	.37	.32	-15	-34

1/ Seasonally adjusted, end of period.
2/ Per cent changes based on August.

TABLE 5

PRICE BEHAVIOR
(Percentage changes, seasonally adjusted annual rates)1/

	Relative importance Dec. '73	Dec. '72 to Dec. '73	Dec. '73 to Mar. '74	March to June '74	June to Sept. '74	Aug. to Sept. '74
			CONSUMER PRICES			
items	100.0	8.8	14.2	10.9	14.2	15.0
Food	24.8	20.1	19.4	3.1	12.3	22.3
Commodities less food	38.6	5.0	16.0	15.8	16.5	12.0
Services2/	36.6	6.2	9.2	11.0	13.9	13.2
lendum						
All items less food and energy components3/4/	68.8	4.7	8.6	12.8	15.2	12.4
Petroleum products3/5/	4.0	23.4	99.3	26.6	-4.1	-15.1
Gas and electricity	2.4	6.9	28.2	16.1	20.2	17.7
			WHOLESALE PRICES			
l commodities	100.0	15.4	24.5	12.2	35.2	1.1
Farm and food products	31.7	26.7	10.8	-29.3	59.2	-23.0
Industrial commodities6/	68.3	10.7	32.3	35.7	28.3	12.4
Materials, crude and intermediate	43.5	13.3	36.9	40.6	31.7	9.0
Finished goods:						
Consumer excluding foods	17.6	7.4	28.3	25.3	18.5	14.3
Producer	8.5	5.3	13.2	27.2	31.8	25.6
Consumer foods	14.3	22.5	17.3	-16.7	29.4	-3.6

Not compounded for one-month changes.
Not seasonally adjusted.
Confidential--not for publication.
Excludes food, gasoline and motor oil, fuel oil and coal, and gas and electricity.
Includes coal.
Stage of processing components do not add to the total because they include some items found in farm and food products group.

TABLE 6

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

	Fiscal Year 1974*	Fiscal 1975 e/ Adm. Est. 5-30-74	Fiscal 1975 e/ F.R. Board	Calendar Years 1973 Actual	Calendar Years 1974 FRB e/	Calendar Quarters 1974 I*	Calendar Quarters 1974 II*	Calendar Quarters 1974 III*	F.R.B. Staff Estimates Calendar Quarters 1974 IV	F.R.B. Staff Estimates Calendar Quarters 1975 II	F.R.B. Staff Estimates Calendar Quarters 1975 II
Federal Budget											
Surplus/deficit	-3.5	-11.4	-4.9	-7.9	-8.2	-7.1	9.7	-1.6	-9.2	-5.3	11.1
Receipts	264.9	294.0	294.6	250.4	279.8	60.5	80.1	72.9	66.3	67.5	87.8
Outlays	268.4	305.4	299.5	258.3	288.0	67.6	70.4	74.5	75.5	72.8	76.7
Means of financing:											
Net borrowing from the public	3.0	n.a.	8.4	7.9	10.0	3.4	-6.4	4.5	8.5	1.7	-6.3
Decrease in cash operating balance	3.4	n.a.	.3	.7	3.8	2.0	-.8	.5	2.1	1.6	-3.9
Other 1/	-2.9	n.a.	-3.7	-.7	-5.6	1.7	-2.5	-3.4	-1.4	2.0	-.9
Cash operating balance, end of period	9.2	n.a.	8.9	10.4	6.6	8.4	9.2	8.7	6.6	5.0	8.9
Memo: Sponsored agency borrowing 2/	14.8	n.a.	17.3	16.3	16.9	--	5.5	7.1	4.2	2.8	3.1
National Income Sector											
Surplus/deficit	-4.7 p/	-12.8	-4.5 3/	-5.6	-.6	-1.5	-1.3	4.3 e/	-3.8	-5.9	-10.0
Receipts	273.3 p/	304.3	306.6 3/	258.5	295.0	279.4	290.3	306.2 e/	304.1	308.2	310.2
Expenditures	278.0 p/	317.1	311.0	264.2	295.6	281.0	291.6	301.9 p/	307.9	314.1	320.2
High Employment surplus/deficit (NIA basis) 4/ e/	-3.9	n.a.	10.7	-6.6	-.8	-3.0	-3.5	-2.4	5.9	15.8	23.6

* Actual e--projected n.e.--not estimated n.a.--not available p--preliminary

1/ Includes such items as deposit fund accounts and clearing accounts.

2/ Federally-sponsored credit agencies, i.e., Federal Home Loan Banks, Federal National Mortgage Assn., Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.

3/ Quarterly average exceeds fiscal year total by $.6 billion for fiscal 1975 due to spreading of wage base effect over calendar year.

4/ Estimated by F.R. Board Staff.

DOMESTIC FINANCIAL SITUATION

SELECTED DOMESTIC FINANCIAL DATA
(Dollar amounts in billions)

Indicator	Latest data Period	Level	Net change from Month ago	Three months ago	Year ago
Monetary and credit aggregates				SAAR (per cent)	
Total reserves	October	36.9	.8	.7	8.3
Reserves available (RPD's)	October	34.9	- .5	5.0	9.1
Money supply					
M_1	October	281.8	4.7	2.6	5.7
M_2	October	607.9	9.6	6.0	8.2
M_3	October	944.7	8.1	5.1	7.3
Time and savings deposits (Less CD's)	October	326.1	14.1	8.9	10.4
CD's(dollar change in billions)	October	85.2	- .8	- .2	21.4
Savings flows (S&L's + MSB's)	October	336.7	5.0	3.2	5.7
Bank credit (end of month)	October	691.9	--	.2	10.1
Market yields and stock prices			Percentage or index points		
Federal funds wk. endg.	11/6/74	9.63	-1.41	-2.46	- .08
Treasury bill (90 day) "	11/6/74	7.76	.89	- .66	.54
Commercial paper (90-119 day) "	11/6/74	9.00	-1.13	-2.55	.22
New utility issue Aaa "	11/1/74	9.42	-1.19	- .89	1.66
Municipal bonds (Bond Buyer) 1 day	11/7/74	6.66	.14	.08	1.47
FNMA auction yield (FHA/VA)	11/4/74	9.93	- .39	- .20	1.05
Dividends/price ratio (Common stocks) wk. endg.	10/31/74	5.03	- .47	.42	1.93
NYSE index (12/31/65=50) end of day	11/5/74	39.54	6.64	-1.99	-17.17

Credit demands		Net change or gross offerings Current month 1974	Current month 1973	Year to date 1974	Year to date 1973
Business loans at commercial banks	October	1.7	- .1	27.0	25.1
Consumer instalment credit outstanding	September	.7	1.4	9.2	16.2
Mortgage debt outst. (major holders)	August	3.2	5.4	32.7	44.1
Corporate bonds (public offerings)	October	3.4e	1.8	20.4e	10.4
Municipal long-term bonds (gross offerings)	October	2.3e	2.3	18.7e	19.6
Federally sponsored Agcy. (net borrowing)	October	2.3e	2.6	15.0e	15.8e
U. S. Treasury (net cash borrowing)	November	3.8e	2.2	6.0e	4.8
Total of above credits		17.4	15.6	129.0	136.0

e - Estimated

DOMESTIC FINANCIAL SITUATION

The further decline in the Federal funds rate following the October FOMC meeting, occurring against a backdrop of sluggish growth in M_1 and increasing evidence of softness in business activity, buttressed market expectations of an easing of monetary policy. These expectations were fostered also by the continuation of moderate demands of businesses for short-term credit. Consequently, private short-term market rates have fallen 1/2 to 3/4 percentage points since mid-October. Only in the Treasury sector, where there have been sizable new supplies of bills, has there been any firmness in short-term market rates since the October FOMC meeting, and most recently a rally has carried even these yields 40 basis points or more below their mid-October levels.

Interest rate developments in longer-term markets have been more mixed. Yields on new high grade corporate bonds have dropped sharply, despite exceptionally large current and prospective volumes of new securities being issued by firms seeking to restore liquidity and to finance capital expenditures. The Treasury coupon sector also has managed a modest rally in the face of new supplies, but the municipal bond market has been able to absorb a large volume of new issues only at somewhat higher yields.

The decline in market rates of interest has brought an improvement in inflows to thrift accounts at banks and at thrift institutions. This improvement has contributed to some easing of residential mortgage market conditions, reflected in declines in both primary and secondary market rates.

SELECTED INTEREST RATES

	Aug. FOMC Aug.20	Sept. FOMC Sept.11	Oct. FOMC Oct. 15	October 22	October 29	November 4	November 12
hort-term							
Federal funds (weekly average	12.23	11.48	10.11	9.81	9.72	9.63	9.54 1/
3-month Treasury bills	9.05	9.06	7.74	7.43	8.03	7.82	7.35
6-month Treasury bills	9.13	8.83	7.92	7.45	7.85	7.75	7.48
1-month commercial paper	12.00	11.75	9.75	9.50	9.00	9.13	9.13
3-month large negotiable CD's	12.35	11.85	9.63	9.13	8.88	9.00	8.88
Bank prime rate	12.00	12.00	11.75	11.50	11.25	11.00	11.00
ong-term							
New Aaa utility bonds(FR)*	10.26	10.27	10.44	10.03	9.42	9.00p	n.a.
Recently offered Aaa utility bonds (FR)*	10.28	10.30	10.36	10.02	9.82	9.49p	n.a.
Bond Buyer municipal*	6.73	6.79	6.48	6.51	6.65	6.66	n.a.
U.S. Government 20-year constant maturity	8.58	8.59	8.31	8.29	8.25	8.12	8.03 2/

Figures for Thursday following date.
/ 6-day average.
/ November 8.

Monetary aggregates. Growth of M_1 picked up somewhat in October from its depressed third quarter pace. Nevertheless, at a 4-1/2 per cent annual rate, M_1 expansion remained relatively slow. Some further expansive effect on M_1 growth of the recent decline in interest rates may occur, but the sluggish economic activity projected for the fourth quarter will tend to hold down the growth of demand deposits.

A more immediate impact of the fall in interest rates was the improved inflows to consumer-type time and savings accounts at

MONETARY AGGREGATES
(Seasonally adjusted changes)

	1974					
	QI	QII	QIII	Aug.	Sept.	Oct. p
			Per cent at annual rates			
M_1	5.6	6.4	1.6	2.6	0.4	4.7
M_2	9.0	7.7	4.5	6.2	2.2	9.6
M_3	8.9	6.4	4.9	4.5	2.6	8.1
Adjusted bank credit proxy	8.5	20.9	6.4	5.2	4.2	-1.5
Time and savings deposits						
At commercial banks:						
a. Total	15.6	23.7	8.4	5.3	6.5	8.8
b. Other than large CD's	12.2	8.7	7.3	9.0	3.4	14.1
At savings and loans 1/	10.1	5.3	3.6	1.7	6.1	5.5
At mutual savings banks 1/	5.2	1.9	0.3	0.4	2.1	4.0
			Billions of dollars 2/			
Memoranda:						
a. U.S. Government demand deposits	-.4	--	.7	2.8	.4	-1.1
b. Negotiable CD's	1.6	5.2	2.7	-.7	1.3	-0.8
c. Nondeposit sources of funds	.4	.6	-.1	-.7	-.4	-0.8

1/ Based on month-end series.
2/ Change in average levels month-to-month or average monthly change for the quarter, measured from last month in quarter to last month in quarter, not annualized.
p - Preliminary.

commercial banks and at thrift institutions. The spread between the yields on money market instruments and the ceiling rates on small denomination deposits narrowed in October to the smallest margin since the first quarter of the year. With diminished consumer confidence and reduced consumer durables expenditures perhaps also enhancing demands for such savings vehicles, commercial bank time deposits other than large CD's at weekly reporting banks rose at a 14 per cent annual rate--twice the third quarter pace.

Sample data indicate that savings and loan associations in October experienced a net inflow of new money--their first since June--and that deposit losses at mutual savings banks diminished. Although the estimated seasonally adjusted growth rate for total nonbank thrift institution deposits in October, 5 per cent, is the same as that for September, the seasonal adjustment factors apparently fail to capture the full impact of interest crediting in September and thus mask the degree of improvement in October. An indication of the lessened pressures on the thrift institutions was the reduced net flow of FHLB advances, from $1,140 million in September to $600 million in October. The October figure included the $500 million monthly allocation of below market rate advances; these subsidized advances will be exhausted after the November and December disbursements.

<u>Private short-term credit</u>. Total short-term funds raised by nonfinancial and nonbank financial firms, which had fallen off sharply in September, remained significantly lower in October than in earlier months of the year. Spreading economic weakness accounted for some of

the easing of short-term credit demands, but an added factor of increasing importance was the funding of short-term debt by business borrowers.

Total loans and investments at commercial banks (last-Wednesday-of-the-month series, seasonally adjusted) were unchanged during October, as the loan component increased at only a 3 per cent annual rate and holdings of Treasury securities dropped again. The flatness of bank credit in recent months reflects supply factors in addition to the easing of short-term credit demands. The large money center banks, which are heavily reliant on purchased funds and have thin capital cushions, appear to be retrenching--by husbanding their remaining liquidity and following stringent lending policies. This was evident in the September survey of lending commitments at 138 large banks which showed the largest decline in unused commitments this year. Moral suasion by the Federal Reserve undoubtedly has played a role in these bank decisions.

With consumer-type time deposit flows increasing, the slowing of loan growth has allowed banks to reduce large CD's and nondeposit liabilities. The adjusted bank credit proxy in fact contracted in October--the first monthly decline in over 4-1/2 years. Unlike past periods in which loan growth has slowed, the big banks as a group are showing no inclination to expand securities portfolios with the use of purchased money.

One aspect of the retrenchment is the relatively slow decline of the prime rate. Most recently reaching 10-1/2 per cent at a few key banks, the prime rate has declined less than half as much as commercial

COMMERCIAL BANK CREDIT 1/
(Seasonally adjusted changes at annual percentage rates)

	1974					
	QI	QII	QIII	Aug.	Sept.	Oct.
Total loans and investments 2/	17.5	12.0	5.6	9.4	-8.6	--
U. S. Treasury securities	27.3	--	-29.8	-10.8	-67.3	-57.5
Other securities	8.3	10.8	--	--	.9	11.4
Total loans 2/	19.0	13.8	11.2	14.2	-4.8	2.9
Business loans 2/	24.0	22.9	14.0	19.2	.7	11.1
Real estate loans	12.9	14.2	6.0	6.6	3.8	2.8
Consumer loans	5.4	4.4	7.2	8.6	2.9	1.4

1/ Last-Wednesday-of-month series except for June and December, which are adjusted to the last business day of the month.
2/ Includes outstanding amounts of loans reported as sold outright by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.
NOTE: Data shown reflect revisions based on the June 30, 1974, Call Report; revisions are discussed in detail in the Supplement to the Greenbook.

RATE SPREADS AND CHANGES IN SELECTED BANK LOANS AND COMMERCIAL PAPER
(Amounts in billions of dollars, seasonally adjusted monthly changes)

	Nonfinancial Businesses				Nonbank Financial Businesses			
	Prime rate less 30-59 day commercial paper rate	Business loans at all commercial bank 1/	Commercial paper 2/	Annual rate of change in total short-term credit	Prime rate less 15-29 day finance rate	Loans to nonbank financial institutions 1/	Commercial paper (excluding bank related) 2/	Annual rate of change in total short-term credit
	(Per cent)	(Average monthly changes)		(Per cent)	(Per cent)	(Average monthly changes)		(Per cent)
1974--QI	--	3.2	--	22.5	--	.8	.5	27.0
QII	--	3.2	.5	24.9	--	.3	-.6	-6
QIII	--	2.1	.8	18.1	--	1.0	.4	29.1
Aug.	.22	2.7	.2	19.4	.64	1.5	1.2	53.5
Sept.	.53	--	.8	4.9	1.25	-.5	.8	5.7
Oct.	1.95	1.7	.9	15.9	2.69	.2	-.1	1.9
Weekly pattern:								
1974--Oct. 2	1.28				2.50			
9	1.58				2.23			
16	2.00				3.38			
23	2.00				2.60			
30	2.38				2.88			
Nov. 6	1.94				2.35			

1/ Changes are based on last-Wednesday-of-month data and are adjusted for outstanding amounts of loans sold to affiliates.
2/ Measured from end-of-month to end-of-month.

paper and CD rates. The resulting high cost of bank loans has induced many prime borrowers to shift their short-term credit demands to the commercial paper market. Moreover, there are reports that non-prime borrowers at commercial banks are receiving even closer scrutiny than before and loan repayments are being encouraged.

Business loans at commercial banks are estimated to have grown at an 11 per cent annual rate in October. Probably more indicative of the recent trend of business loans, however, is the 6 per cent average growth rate for September and October combined, a rate well below the 20 per cent average of the first three quarters of 1974. Data for large banks indicate particular weakness in loans to concerns in the wholesale and retail trade, textile, and public utility sectors; on the other hand, loans to the metals, petroleum refining, and mining industries have been relatively strong.

In addition, loans to commodity dealers increased sharply in October. This year's feed grain and oilseed crops are being sold off the farm and are entering storage and processing at close to the year's peak prices, more than 50 per cent higher than November 1973. Furthermore, demand for bank credit has been increased by changes in Commodity Credit Corporation programs that have made sales to commodity dealers more attractive relative to government-financed storage. It should be noted that, because peak prices are more fully reflected in warehousing transactions this year, a drop in prices this year or early next year would have a larger impact on the solvency of the dealers and their creditors.

Total consumer instalment debt outstanding grew at its slowest rate of the year in September, and available data for commercial banks suggest that expansion continued slow in October. Weakness of consumer spending probably has been the main factor in the reduced growth of instalment debt, but firmness in consumer finance rates and nonprice terms also has tended to restrain credit growth. A spot survey of automobile financing activity at about 30 banks, conducted by the staff in late October, revealed that this nonprice credit tightening, while modest in extent, has taken such forms as lending only to depositors and raising downpayment requirements. Some banks reported that they were advertising less and/or that they no longer were seeking arrangements with dealers to purchase loans.

U. S. Government securities market. The Treasury has marketed a sizable volume of debt since the October meeting. It has raised $200 million in each regular bill auction since October 10; this is expected to continue through mid-December. The Treasury also sold $1.5 billion of 9-month bills on October 29 and has expressed its intention to auction another $3.0 billion or so of bills before mid-December. Although the supply pressures on bill yields were partially relieved by large purchases by the Desk for foreign accounts, the 3-month bill rate rose to about 8 per cent in late October before receding to around 7½ per cent in recent days.

In addition to the bill financings, the Treasury sold $1 billion of 4½ year notes on October 23, and raised another $550 million of new money in conjunction with its November refunding operation. Net cash borrowing by the Treasury is expected to total $8.5 billion in the fourth quarter, about average for the period.

Contrary to some expectations, there have been no significant purchases of special nonmarketable issues by OPEC countries. Identifiable flows of OPEC funds into U. S. assets have mainly taken the form of purchases of marketable Treasury securities and bankers' acceptances.

Corporate and tax-exempt bond markets. The volume of corporate public bond offerings in October was the second largest on record, and the November calendar is only slightly smaller. Nevertheless, yields on new issues have dropped dramatically. Strong retail

PROJECTION OF FEDERAL BORROWING--MONTHLY
(In billions of dollars--not seasonally adjusted)

	Oct. e/	Nov.	Dec.	Jan.
Derivation of borrowing				
Budget surplus or deficit (-)	-6.8	-1.1	-1.3	-1.0
Plus: Other sources a/	- .4	-1.3	.3	1.1
Less: Increase in cash balance	-6.5 b/	1.4	3.0	.1
Total net Treasury borrowing	.7	3.8	4.0	--
Weekly and monthly bills	1.0	1.0	.4	--
Other bill issues	--	1.5	3.3	--
Coupon issues, net	--	1.3	.3	--
As yet unspecified new borrowing	--	--	--	--
Federal financing bank	--	--	--	--
Debt repayment and other	- .3	--	--	--
Memo items:				
Maturing coupon issues held by the public	--	4.3	2.0	--
Level of cash balance, end of period	2.2 b/	3.6	6.6	6.7
Net borrowing by government-sponsored agencies	2.3	0.4	1.6	1.0

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e--estimated
a/ Checks issued less checks paid, outlays of off-budget Federal agencies, accrued items, and other transactions.
b/ Actual.

OPEC INVESTMENTS IN SELECTED DOLLAR ASSETS
($ millions)

	1974			
	1st Qtr.	2nd Qtr.	3rd Qtr.	Oct.
U.S. bank deposits	504	875	1,325	n.a.
U.S. Government securities	505	1,424	2,239	437
Federal agencies securities	--	--	327	53
Bankers acceptances	--	5	182	383
Deposits and deferred credits at Fed Bank of New York	18	7	99	-22
Eurocurrency deposits 1/	3,300 e/	6,000 e/	4,500 e/	n.a.
Total	4,300 e/	8,300 e/	8,700 e/	n.a.

1/ Primarily Eurodollars
e - Rough estimates

demand has supported the recent rally, as investors have shown an increased willingness to lengthen the average maturities of their purchases—at least to the 5 to 10 year maturity range that accounted for almost two-thirds of the October volume.[1/] The emerging consensus that economic activity will be in a downtrend until at least mid-1975 and the more accommodative stance of the Federal Reserve led many investors to believe that a cyclical peak in long-term rates probably had been reached. The fact that the yield curve in the corporate market had become upward sloping for the first time this year provided a further incentive for lengthening.

Investor interest in the corporate market was enchanced by the availability of several large bond issues by highly regarded manufacturing firms. Utilities and finance companies dominated the October calendar, but manufacturing firms are expected to sell $1.2 billion of debt in November. As noted in previous Greenbooks, manufacturers have had more financial flexibility than the utilities, and have waited for improvement in market conditions before coming to the long-term market.

Stock prices have risen slightly since mid-October and, as measured by the NYSE composite index, are nearly 20 per cent above

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1/ Flows to liquid asset mutual funds continue strong, however; in early November, the total assets of the 5 largest funds were $1.7 billion, up from less than $1.3 billion at the end of September.

CORPORATE AND MUNICIPAL LONG-TERM SECURITY OFFERINGS
(Monthly or monthly averages, in millions of dollars)

	1973 Year	1974 Half I e/	QIII e/	QIV f/	Oct. e/	Nov. f/	Dec. f/
Corporate securities - Total	2,779	3,047	2,600	4,117	4,600	4,150	3,600
Public bonds	1,125	1,950	1,767	3,000	3,400	3,200	2,400
Privately placed bonds	725	543	467	567	400	400	900
Stock	929	555	367	550	800	550	300
State and local government securities	1,942	2,113	1,833	2,033	2,300	2,000	1,800

e/ Estimated.
f/ Forecast.

their 1974 lows. The cost of equity funds remains high, however, so no immediate pick-up in stock issuance is projected.

Meanwhile, the municipal bond market encountered some difficulty in absorbing a substantial volume of new issues, some of which were displaced from the third quarter of the year. Yields moved moderately higher as dealer inventories rose. Institutional demand for tax-exempts continued light, but some market participants expressed the belief that commercial bank demand would be forthcoming in the near future. November and December new issue volumes are expected to be somewhat lighter than October's, with the fourth quarter total equaling the average for the first 3 quarters of the year.

Mortgage markets. The further decline in market interest rates and the improvement in deposit flows to thrift institutions were interpreted by many market participants as presaging an earlier easing of residential mortgage credit conditions than had previously been expected. In the primary market, average interest rates on new commitments by S&L's for conventional home mortgages, which had risen more than 1½ percentage points between March and September, declined in several regions during October. The national average rate of 9.79 per cent on November 8 was 24 basis points below the peak in late September the much greater decline in new corporate bond rates over that span restored much of the yield margin normally favoring mortgage investments.

CONVENTIONAL HOME MORTGAGES
AT 120 S&L's

	Average going rate on 80% loans (per cent)	Basis point change from month or week earlier	Spread 1/ (basis points)	Federal Home Loan Bank districts with funds in short supply
1973--High	8.85 (9/28)	--	107 (9/12)	12 (Aug.-Sept.)
Low	7.43 (1/26, 2/2, 2/9)	--	-12 (8/8)	0 (Jan.-Mar.)
1974--High	10.03 (9/27)	--	44 (11/1)	12 (May, July-Oct.)
Low	8.40 (3/15, 3/22)	--	-106 (7/12)	0 (Feb.-Mar.)
Oct. 11	9.96	-6	n.a.	12
18	9.99	+3	-45	12
25	9.94	-5	--9	12
Nov. 1	9.87	-7	44	12
8	9.79	-8	79	12

1/ Average mortgage return before deducting servicing costs minus average yield on new issues of Aaa utility bonds paying interest semi-annually and with 5-year call protection.

FNMA AUCTION RESULTS
HOME MORTGAGE COMMITMENTS

Date of auction	Government-underwritten			Conventional		
	Amount (In $ millions)		Average yield	Amount (In $ millions)		Average yield
	Offered	Accepted		Offered	Accepted	
1973--High	551 (9/3)	289 (9/3)	9.37 (9/17)	171 (8/20)	88 (4/16)	9.68 (9/17
Low	25 (10/15)	17 (10/15)	7.69 (1/8)	9 (10/1)	7 (10/1)	7.84 (1/2)
1974--High	1,155 (3/25)	333 (3/25)	10.59 (11/9)	164 (4/18)	63 (4/8)	10.71 (9/9)
Low	35 (10/21)	25 (11/4)	8.43 (2/25)	14 (10/21)	11 (6/17)	8.47 (3/11
Oct. 7	46.6	29.7	10.32	26.1	23.3	10.46
21	34.5	26.0	10.11	14.1	12.2	10.27
Nov. 4	47.8	24.7	9.93	20.4	12.1	10.11

In the relatively more sensitive secondary market, average yields in the FNMA auctions of forward purchase commitments declined 60 basis points between September 9 and November 4. The drop in rates, and the light volume of offerings to FNMA which accompanied it, reflected in part some shift toward speculative warehousing of mortgages by mortgage bankers in anticipation of further declines in interest rates. Another factor was the sharp improvement in prices of GNMA-guaranteed mortgage-backed securities, making them a relatively attractive vehicle for the sale of FHA/VA mortgages. Demand for such securities apparently has strenghtened recently among investors, including in some instances S&L's and life insurance companies. Such a development would be consistent with a turnaround in market conditions, since secondary market purchases are a means of investing funds without the delay of the commitment process.

The $1.6 billion of new mortgage commitments made by S&L's during September--the most recent month for which data are available--was the smallest volume of the year. With commitments (including loans in process) at S&L's already the lowest since 1971, and with loan repayment flows now sufficient to finance about 70 per cent of new loans being made, the likelihood of further substantial declines in new commitments is small. However, liquidity positions of nonbank thrift institutions are strained (the average liquidity ratio of insured S&L's fell in September to the lowest level since 1970) and they are faced with a substantial volume of high cost indebtedness. Some restoration of liquidity and debt repayment must be expected before these institutions become more aggressive lenders, although the possibility exists that the FHLB Board may devise incentives for S&L's to retain their outstanding advances and to use new deposit inflows for mortgage loans.

A new GNMA rate-subsidy program for conventional new home mortgages was enacted on October 22 to supplement the GNMA Tandem Plan for FHA/VA mortgages. Under the plan, GNMA is to issue commitments to purchase $3 billion of 8½ per cent mortgages by year-end. The greatest impact of the program on the housing sector likely will occur in early 1975, but that impact may be appreciably smaller than is suggested by the dollar amount indicated. The new subsidized loans will to some extent substitute for market rate loans; moreover, if GNMA sells the mortgages back into the market at a loss or if the Treasury sells additional debt to finance the holding of the mortgages, the resultant demands on credit markets will put upward pressure on interest rates and will tend to divert funds from the thrift institutions.

INTERNATIONAL DEVELOPMENTS

CONFIDENTIAL (FR)

IV -- T - 1

11/13/74

U.S. Balance of Payments
(In millions of dollars; seasonally adjusted)

	1973	1974P			
	YEAR	1Q	2Q	3Q	Sept.*
Goods and services, net 1/	4,391	2,928	-122		
Trade balance 2/	471	-74	-1,631	-2,596	-507
Exports 2/	70,277	22,299	24,089	24,632	8,170
Imports 2/	-69,806	-22,373	-25,720	-27,228	-8,677
Service balance	3,920	3,002	1,509		
Remittances and pensions	-1,943	-390	-461		
Govt. grants & capital, net	-3,471	-1,218	-1,007		
U.S. private capital (- = outflow)	-14,101	-8,585	-9,528		
Direct investment abroad	-4,872	-627	-1,552		
Foreign securities	-807	-646	-357	-306	-32
Bank-reported claims -- liquid	-1,103	-2,239	-1,246	-333	247
" " " other	-4,773	-2,958	-6,081	-1,578	968
Nonbank-reported claims -- liquid	-841	-361	126		
" " " other	-1,704	-1,754	-418		
Foreign capital (excl. reserve trans.)	12,444	7,118	4,610		
Direct investment in U.S.	2,537	1,281	1,516		
U.S. corporate stocks	2,758	376	10	82	3
New U.S. direct investment issues	1,223	24	67		
Other U.S. securities (excl. U.S. Treas.)	69	287	320		
Liquid liabilities to:	4,436	4,630	2,821	4,199	-875
Commercial banks abroad	2,978	4,616	1,977	3,009	-1,358
Of which liab. to branches 3/	(309)	(3,379)	(-1,120)	(-566)	(-2,919)
Other private foreign	1,082	599	557	909	527
Intl. & regional organizations	376	-585	292	281	-44
Other nonliquid liabilities	1,420	520	-123		
Liab. to foreign official reserve agencies	5,095	-852	4,887	1,541	1,573
U.S. monetary reserves (increase, -)	209	-210	-358	-1,003	-426
Gold stock	--	--	--	--	--
Special drawing rights	9	--	-29	-123	-78
IMF gold tranche	-33	-209	-244	-728	-326
Convertible currencies	233	-1	-85	-152	-22
Errors and omissions	-2,624	1,209	1,979		
BALANCE (deficit -)					
Official settlements, S.A.		1,062	-4,529	-538	
" " , N.S.A.	-5,304	1,495	-4,104	-1,541	-1,147
Net liquidity, S.A.		-968	-6,229		
" " , N.S.A.	-7,796	-158	-6,609		
Liquidity, S.A. 4/		-3,568	-7,349	-4,737	
" , N.S.A.	-9,740	-2,900	-7,778	-5,711	-272
Basic balance, S.A.		1,786	-2,740		
" " , N.S.A.	-896	2,163	-2,692		

* Monthly, only exports and imports are seasonally adjusted.
1/ Equals "net exports" in the GNP, except for latest revisions.
2/ Balance of payments basis which differs a little from Census Basis.
3/ Not seasonally adjusted.
4/ Measures by changes in U.S. monetary reserves, all liabilities to foreign official reserve agencies and liquid liabilities to commercial banks and other foreigners.
5/ "Commercial banks abroad" includes "Other private foreigners."

INTERNATIONAL DEVELOPMENTS

Foreign exchange markets. Foreign exchange trading has been moderately active during the past five weeks. The weighted average foreign exchange value of the dollar declined approximately 3/4 per cent during the period and about 2 per cent since early September, generally in response to the continuing decline in interest rates on dollar-denominated assets. On Tuesday of this week, the dollar strengthened sharply following the announcement by the British government that the U.K. will not renew its sterling guarantees which expire at year-end. The dollar was also strengthened by reports that the System, the Bundesbank and the BNS had agreed to consult for purposes of intervening in concert in support of the dollar.

During the five week period, there was a substantial amount of intervention in dollars, by both the System and other central banks. There were sales of more than $800 million by the central banks of Italy, Japan and England, whose currencies tended to weaken against the dollar. There were net dollar purchases of more than $60 million by the System and the central banks in the EC snake. There was no dollar/Swiss franc intervention, however.

The Swiss franc advanced 4-1/2 per cent against the dollar during the past five weeks, strengthened by the relative firmness of Swiss interest rates and by the lifting of the ban on interest payments on bank deposits held by foreigners.

The pound sterling has dropped more than 4 U.S. cents during the past week, particularly following the Budget announcement and the proposal to let the sterling guarantee expire. In addition to outright sales of dollars, the Bank of England has done a substantial amount of swaps with British banks in an effort to keep short-term sterling interest rates high.

The price of gold reached a new high of $183.00 last Friday. The price returned to that level in midweek, following the announcement by Undersecretary Bennett of the Treasury, that the U.S. government will not seek a postponement of the effective date on which U.S. citizens can purchase gold.

Euro-dollar market. Euro-dollar deposit rates have continued to decline in the past five weeks, primarily in response to falling U.S. interest rates. The 3-month rate has declined about 1-3/4 percentage points to 9.94 per cent on November 13. The cost of overnight Euro-dollars to U.S. banks (including reserve requirements) exceeded the Federal funds rate by about 70 basis points in the week of November 13, less than in early October but about the same as in September.

Since early October the cost to prime nonbank borrowers of short-term Euro-dollar loans has decreased more rapidly than the cost of borrowing at U.S. banks, and, as shown in the accompanying table, the already substantial cost advantage of Euro-loans has been further enlarged. However, recent inquiries indicate that customers of domestic offices of U.S. banks remain exceedingly reluctant to disrupt existing banking relationships by shifting borrowings to a foreign branch or foreign-owned bank abroad.

SELECTED EURO-DOLLAR AND U.S. MONEY MARKET RATES

Average month week ending Wednesday	(1) Over-night Euro-$	(2) Federal Funds	(3) Differ-ential (1)-(2)(*)	(4) 3-month Euro-$ Deposit	(5) 60-89 day CD rate	(6) Differ-ential (4)-(5)(*)
1974-July	12.18	12.88	-0.70 (0.36)	13.52	11.70	1.82 (1.98)
Aug.	11.29	12.01	-0.72 (0.26)	13.57	11.63	1.94 (2.11)
Sept.	11.07	11.34	-0.27 (0.69)	12.41	11.17	1.18 (1.35)
Oct.	9.77	10.06	-0.29 (0.56)	10.95	9.40	1.45 (1.68)
1974-Oct. 9	10.46	10.43	0.03 (0.95)	11.64	9.50	2.14 (2.32)
16	9.22	10.11	-0.89 (-0.09)	11.04	9.50	1.54 (1.67)
23	9.52	9.81	-0.29 (0.54)	10.65	9.00	1.65 (1.80)
30	9.29	9.72	-0.43 (0.38)	10.21	8.88	1.33 (1.45)
Nov. 6	9.13	9.63	-0.50 (0.29)	10.00	8.88	1.12 (1.22)
13p/	9.40	9.54	-0.14 (0.68)	9.89	8.88	1.01 (1.10)

*/ Differentials in parentheses are adjusted for the cost of required reserves.

p/ Preliminary

SELECTED EURO-DOLLAR AND U.S. COSTS FOR PRIME BORROWERS
(1974; Friday dates)

	Oct. 4	Oct. 25	Nov. 8	Nov. 13d/
1) 3-mo. Euro-$ loan a/	12.69	11.00	10.56	10.69
2) 90-119 day com'l. paper b/	10.38	9.00	9.13	9.13
3) U.S. bank loan:				
a) predominant prime rate	12.00	11.50	11.00	11.00
b) with 15% comp. bal's. c/	14.12	13.53	12.94	12.94
c) with 20% comp. bal's. c/	15.00	14.38	13.75	13.75
Differentials:				
(1) - (2)	2.31	2.00	1.43	1.56
(1) - (3a)	.69	-.50	-.44	-.31
(1) - (3b)	-1.43	-2.53	-2.38	-2.25
(1) - (3c)	-2.31	-3.38	-3.19	-3.06

a/ 3/4 per cent over deposit bid rate.

b/ offer rate plus 1/8 per cent.

c/ prime rate adjusted for compensating balances.

d/ Wednesday

U.S. banks' gross liabilities to their foreign branches have continued the decline initiated in early September. Liabilities averaged $2.3 billion per day in the week of November 6, down from $3.8 billion in July-August. The decrease reflected banks' reduced demands for money market funds generally as customers have shifted to the commercial paper market.

In the London Euro-currency market, non-sterling deposits of oil-exporting countries with banks there (including branches of U.S. banks) rose $3.4 billion in the third quarter, and $10.4 billion in the first nine months of 1974, to a level of $15.0 billion outstanding on September 30. The third quarter increase was somewhat smaller than the $4.5 billion in the second quarter. In contrast with the continuing inflows from these countries, the growth in total non-sterling deposits in London slowed abruptly in late spring. The total rose from $94 billion in mid-December 1973 to $115.0 billion on June 19, and was $115.3 billion on September 18 (all figures excluding liabilities to the London interbank market).

The strong preference of the OPEC countries for very short-term Euro-currency deposits has shortened the average maturity of the non-sterling liabilities of London banks. Liabilities of less than three months rose from 64.6 per cent of total liabilities at the end of September 1973 to 69.5 per cent at the end of August 1974. On the assets side, the proportion with maturities of less than a year decreased, while the share in the total for maturities of three years and over rose sharply from 7.7 per cent to 12.0 per cent.

U.S. balance of payments. The balance on goods and services for the third quarter is estimated to have been in deficit at an annual rate of $3.2 billion, compared with a $.5 billion deficit rate in the second quarter. The merchandise trade deficit increased from a $6.5 billion rate in the second quarter to $10.4 billion in the third quarter (as detailed in the following section), offset somewhat by an estimated increase in the net surplus on the services accounts.

This increase in the goods and services deficit was more than offset by a sharp shift in bank-reported private capital flows. In the third quarter there was a $2.5 billion net inflow of bank-reported private capital not an annual rate, reversing a net outflow of $3.6 billion during the previous quarter. As shown in the Table, this shift occurred for both U.S. banks and U.S. agencies and branches of foreign banks; both groups of institutions showed reductions in net foreign claims during the third quarter, following increases in net foreign claims during the second quarter. Underlying this shift has probably been a slowdown in foreign demand for bank credit, as Japan and other petroleum-importing areas now receive some loans directly from OPEC countries. In addition, banks have apparently become more selective in extending their credit positions

CHANGES IN BANK-REPORTED CLAIMS ON AND LIABILITIES TO PRIVATE FOREIGNERS*
(Billions of dollars, not seasonally adjusted)

	Q-I	Q-II	July	Aug.	Sept.p	Q-IIIp
Claims	5.1	7.3	1.3	1.5	-1.2	1.6
U.S. Banks	4.0	5.7	1.9	-0.7	0.2	1.4
Agencies and Branches	1.1	1.6	-0.6	2.2	-1.4	0.2
Liabilities	4.5	3.7	2.0	3.1	-1.0	4.1
U.S. Banks	3.2	3.0	0.6	3.1	-1.7	1.9
Agencies and Branches	1.3	0.7	1.4	0.0	0.7	2.2
Net Claims	0.6	3.6	-0.7	-1.6	-0.2	-2.5
U.S. Banks	0.8	2.7	1.3	-3.8	1.9	-0.5
Agencies and Branches	-0.2	0.9	-2.0	2.2	-2.1	-2.0

*The breakdown between U.S. Banks and U.S. Agencies and Branches of Foreign Banks is partially estimated based on VFCR data.
p = Preliminary.

Net purchases of U.S. equities by foreigners have been small since March. The removal of the Interest Equalization Tax in January had a depressing effect on offshore bond issues by U.S. corporations, and net foreign purchases of U.S. bonds during the first three quarters fell to roughly 60 percent of the average rate recorded in 1972 and 1973.

Official liabilities to OPEC countries increased by over $4 billion (not seasonally adjusted) in the third quarter, raising official OPEC holdings in the United States to over $10 billion. Liabilities to other official institutions declined by $1.5 billion in the third quarter, while the stock of U.S. reserve assets increased by $1 billion, primarily through changes in the U.S. reserve position at the IMF. During October, foreign official holdings at the Federal Reserve Bank of New York increased $1.5 billion; data for the change in holdings at commercial banks are not yet available. Slightly over half of this $1.5 billion was for OPEC countries. The stock of U.S. reserve assets showed little change during the month.

U.S. merchandise trade. In the third quarter, the trade deficit was $10.4 billion at an annual rate (balance of payments basis), compared to a rate of $6.5 billion in the second quarter; the value of imports rose nearly three times faster than exports. Prices of both exports and imports rose by about 6-1/2 percent, but the volume of exports declined by 4 percent -- the first quarterly decline in about two years -- while the volume of imports was little changed from the low levels that have been recorded since mid-1973. Nearly all of the worsening of the trade balance resulted from a sharp decline in the value of agricultural exports and a further rise in the value of fuel imports. Apart from these two categories, the deficit was little changed between the second and third quarters.

U.S. exports to OPEC countries continued to increase. In the third quarter they were at an annual rate of $6.8 billion compared to a $3.4 billion rate a year earlier and an annual average of $2.4 billion for 1970-72.

U.S. MERCHANDISE TRADE, BALANCE OF PAYMENTS BASIS
(billions of dollars, seasonally adjusted annual rates)

	1973	1974			1973	1974		
	Year	1Q	2Q	3Q	Year	1Q	2Q	3Q
	(current dollars)				(1967 dollars)			
Exports	70.3	89.2	96.4	98.5	51.1	54.8	57.1	54.8
Agric.	17.9	23.6	22.8	20.5	10.5	10.4	10.0	9.0
Nonagric.	52.4	65.6	73.5	78.0	40.7	44.7	47.7	46.5
Imports	69.8	89.5	102.9	108.9	47.0	46.5	46.9	46.6
Fuels	8.8	20.4	28.2	29.9	6.0	5.1	5.6	5.9
Nonfuels	61.0	69.1	74.6	79.0	41.1	41.5	41.0	40.2
Trade Balance	+0.5	-0.3	-6.5	-10.4	+4.1	+8.3	+10.2	+8.2
(Bal. excl. fuel imp. & agric. exp.	(-8.6)	(-3.5)	(-1.1)	(-1.0)	(-.4)	(+3.2)	(+6.7)	(+6.3)

The increase in petroleum imports in the third quarter was virtually all in volume; imports averaged 6.8 million barrels per day (not seasonally adjusted) compared to a rate of 6.5 million barrels per day in the second quarter. The increase was entirely in crude oil imports, mainly from Saudi Arabia and Nigeria. The average price for all imports of petroleum and petroleum products was $11.62 per barrel in the third quarter, the same as in the second quarter.

Nonfuel imports rose by 6 percent in the third quarter but all of this rise was due to higher prices as the quantity declined for the second quarter in a row. The decrease in volume stemmed from a sharp fall in food imports (particularly coffee) and in cars from Europe and Japan. There were, however, rises in the imports of nonfuel industrial supplies -- steel and metals related to steel production (nickel and tin). The price increases were broadly distributed over most commodity categories with a particularly large increase in the price of cars from Canada as higher priced 1975 models began to arrive.

Agricultural exports declined further (by 10 percent) in the third quarter mainly reflecting lower volumes shipped while prices on average remained relatively unchanged since the first quarter. However, prices moved up sharply in September reflecting the recent run-up in domestic prices following the announcement of lower U.S. crop estimates.

Nonagricultural exports declined in volume in the third quarter, but the value increased by $4.5 billion at an annual rate, as prices increased by 9 percent. More than half of the value increase was in machinery exports which rose in both volume and price. Automotive exports, mostly to Canada, were also up sharply in both volume and price. Exports of nonagricultural industrial supplies increased in value (mostly coal, chemicals, paper, and steel), but the average volume of these items declined by 8 percent. Coal prices increased by nearly 50 percent between the second and third quarters (prices have more than double since the end of last year). In the first nine months of this year the volume of coal exports was about 15 percent greater than in the same period last year. Consumer goods exports (nonautomotive) declined by nearly 5 percent in the third quarter as the volume fell by nearly 10 percent.

<u>Economic activity and prices in major foreign industrial countries</u>. In the four months since this topic was last covered in these pages, economic activity in the principal OECD countries has continued to be weaker than expected. It is now clear, contrary to hopes expressed in the early part of the year, that no strong second-half recovery will take place in 1974, and no recovery of significant strength appears likely in the first half of 1975. With the exception of France and Canada, where industrial production is modestly higher than levels attained a year ago, latest available figures - for August and September - for the major countries show decreases from output levels of a year earlier.

Difficulties in particular sectors have become acute in many places. Activity in the construction sector has declined nearly everywhere during the entire year in response to tight monetary conditions and, in some cases, speculative overbuilding during the 1972-73 boom. Automotive sales in most countries have fallen off sharply in the wake of the oil crisis, and in Germany major vehicle producers continue to offer workers bounties to resign. Textiles and certain other consumer goods industries are also experiencing production cutbacks as growth in real disposable income has declined.

The softening in demand and output is now being reflected in the labor markets. During recent months unemployment has increased, in contrast to the labor hoarding which characterized the earlier phase of the downturn. In Germany, for instance, the unemployment level climbed through the summer and fall more rapidly than anticipated, and now stands at the highest rate (3.7 per cent) since postwar reconstruction. In a number of other countries, such as Japan, Italy and the United Kingdom, registered unemployment is rising more slowly, but the average work-week has been reduced and overtime has been curtailed or disappeared in many sectors. Despite the fact that nominal wage gains in most countries during the past two years have been above the inflation rate, the fiscal drag of progressive tax systems and reductions in weekly hours worked have combined to put a brake on the growth of real disposable income.

As an example of current prospects, the table on the following page contrasts historical real GNP growth rates in the major countries with the OECD Secretariat's October forecasts for economic growth by half-years for 1974 and 1975. While these forecasts are based on a no-policy-change assumption, it is unlikely that policy changes at this phase of the cycle would have much effect on the outlook for the first half of 1975. In addition, little if any increase in the growth rate is expected for the six foreign countries during the second half of 1975. Forecasts for the year as a whole show a growth in real GNP in all major countries that is substantially below longer-term averages, and in at least one case is negative.

Growth Rates of Real GNP in Major Countries, 1960-73,
and OECD Forecasts, 1974.H2 to 1975.H2
(percentage changes from previous period)[a]

	Actual			Forecast		
	Average 1960-1972	1973	1974.H1[b]	1974.H2	1975.H1	1975.H2
France[c]	5.8	6.1	4.5[d]	4-1/4	3	1-3/4
Germany	4.8	5.3	2.1	0	3	3/4
Italy	5.3	5.9	4.5[e]	0	-1/4	-1/4
United Kingdom[c]	2.9	5.3	-1.9	5	-1	3/4
Japan	10.9	10.5	-8.1	3	1-1/2	1-3/4
Canada	5.0	6.8	5.6	2-1/2	2-1/2	3-3/4
Average of 6 Above	6.6	7.1	-0.3	2-1/2	1-3/4	1-1/2
United States[f]	4.1	5.9	-3.5	-3-1/4	-3-1/4	3/4
Average of 7 Above	5.4	6.5	-1.8	-1/4	-3/4	1

a/ 1960 to 1972 rates are averages of annual changes. Half-yearly data are seasonally adjusted at annual rates. OECD forecasts were made in late October. Totals derived using 1973 GNP weights and exchange rates.
b/ Preliminary, national sources.
c/ GDP.
d/ OECD estimate.
e/ FRB staff estimate.
f/ Half-yearly projections made by FRB staff.

Progress in combating price inflation has been very slow. Though recent month-to-month increases in general wholesale prices have slowed somewhat in most countries, year-over-year increases are still quite sharp everywhere, ranging, in September, from 15.7 per cent in Germany to 43.7 per cent in Italy. The recent softening in industrial commodity prices may also be partially offset by continuing increases in prices for food and agricultural products. Wholesale prices for manufactured goods have risen between 20 and 30 per cent over the past twelve months, and in Italy by almost 50 per cent.

Consumer prices in most industrial countries continue to rise at double-digit rates, year-over-year. Exceptions to this picture are Germany (7.3 per cent) and a few of the smaller countries, but in Italy and Japan the rate of consumer price increase is well above 20 per cent. Further, though figures for the July to September period show some deceleration of month-to-month changes in the CPI, a reacceleration of the upward climb of consumer prices cannot be ruled out in the months ahead. Factors contributing to this possibility include the continued working through of earlier wholesale price increases, hefty wage gains attained by large numbers of workers during 1974 and decreases in productivity associated with stagnating levels of output.

There are some indications that monetary and fiscal authorities in various countries are starting to respond to the sluggish economic situation by moderately easing their previous restrictive policies.

The German monetary authorities, for example, recently took steps toward easing their stringent stance by lowering the discount rate, the first such decrease since early 1972. On the following day the Netherlands Bank announced a one percentage point reduction in its discount rate. In Belgium, which has relied largely on credit ceilings to enforce tight monetary conditions, the authorities did not follow suit by lowering the discount rate, but have somewhat relaxed limits on year-to-year credit expansion. No distinct changes in monetary policy have occurred in the United Kingdom, France and Italy. Conditions in Japan remain tight despite a small expansion of fourth quarter credit ceilings. In most industrial countries, however, money market conditions have eased a bit in the past few months, and both short- and long-term rates have declined from the peaks reached in June and July. In some countries -e.g., in the United Kingdom and Germany - some fiscal stimulation is underway or in the offing, but in Italy, France and Japan fiscal conditions remain restrictive.

In Germany, consumer price developments have been much more favorable than elsewhere, but domestic economic activity has remained sluggish for most of the year, and so far shows little sign of improvement. Since May, gains in industrial production (excluding construction) have been negligible, and in August output was down almost 4 per cent compared to year-earlier levels. Real personal consumption and investment have also remained depressed. The seasonally adjusted unemployment rate has risen from 1.6 per cent at the beginning of the year to almost 3.7 per cent in October. Certain sectors of the economy, such as construction - where completions in August were down 13 per cent from a year earlier - and automobiles, appear to be in genuine distress.

The only continuing source of strength in the current picture is in the foreign balance, which in view of the decline in domestic demand has been responsible for the entire growth in real GNP this year. Data through September suggest that, despite the adverse impact of the oil situation, the German trade surplus for 1974 will be near DM 50 billion (about $19.6 billion), 50 per cent higher than in 1973.

Monetary policy has been actively used to combat inflation. During this past summer several apparent moves toward relaxation were described by the authorities as "offsets" to the Herstatt failure and capital outflows. On October 25, however, acknowledging "changed economic conditions", the Bundesbank reduced both the discount and Lombard rates by 1/2 percentage point, to levels of 6-1/2 per cent and 8-1/2 per cent respectively. In addition, the Bundesbank increased bank rediscount quotas by DM 2.5 billion. Both decisions are interpreted as a sign of genuine but moderate easing of policy. Some fiscal stimulation is also taking place. The construction sector will receive some help from a limited program announced in September. Disposable income, mainly in low-income groups, will be increased by DM 13-15 billion under the tax reform going into effect in January, 1975, and Chancellor Schmidt has recently indicated that stronger expansionary measures may be forthcoming if the domestic situation continues to worsen.

The problems facing British industry have become increasingly apparent. Corporate profits are being squeezed between sharply rising labor costs and continued controls on prices which do not allow all of the higher labor costs to be passed on. And the financial position of companies has deteriorated severely, to precarious levels. The latest investment intentions surveys indicate a decline in investment next year. Moreover, there is distinct weakness in most other sectors of the economy; for example, private housing starts are at a 20-year low. In light of the poor outlook for production and employment, on November 12 Chancellor of the Exchequer Denis Healey announced a budget designed primarily to benefit the corporate sector and thereby to stimulate investment. Some tax relief will be provided for companies, and the program of price restraint will be eased.

The mildly reflationary budget was presented despite continuing sharp increases in wages and prices and a massive current account deficit. The Chancellor also announced an increase in the value-added tax rate on gasoline from 8 to 25 per cent (there is a large excise tax on gasoline, as well); this will increase the retail price index directly by an estimated 1/2 per cent. Details and an assessment of the budget will be provided in the supplement to this Greenbook.

In France, current output and demand have been stronger than in most of the major countries, and industrial output in August was 4.1 per cent above year-earlier levels. Real GDP is expected to increase by about 4-1/4 per cent for the year as a whole. Consumer prices have, however, risen almost 15 per cent over the past year, and nominal wage rates have increased by almost 20 per cent. Although demand pressure has abated since the summer, some sectors of the economy are still reported to be working near capacity, and shortages of certain materials and skilled labor remain a problem. A major drive, which includes value limits on petroleum imports during the coming year, is underway to bring the external sector into balance by the end of 1975, but it is doubtful whether this goal can be accomplished.

French policy has become progressively more restrictive during 1974. The present austerity program aims at bringing increases in the CPI down to around 0.5 per cent per month by mid-1975. Recently, the authorities have announced further measures, including selective "voluntary" freezes on certain consumer prices each month. Also, beginning next year a controversial "conjunctural tax" will go into effect which is designed to penalize firms which fail to pass on productivity gains to the consumer. The danger of strikes and social unrest may well limit the extent to which policy can be further tightened.

Economic conditions in Italy have shown a general weakening in recent months, following strong growth in 1973 and the first half of 1974. The rate of inflation continues much higher than in most other countries, and has as yet shown no improvement. As of September, general wholesale prices were nearly 44 per cent above, and consumer prices were 22 per cent higher than year-earlier levels, but nominal wage gains have almost kept pace with consumer price rises. Unemployment, after falling to the low level of 2.5 per cent last spring, is rising again, particularly in the automotive and textile sectors. The current external balance, though slightly improved in the past two months, remains a matter of serious concern and is a problem which dominates the short-term picture.

While it would be difficult to argue that Italian monetary conditions are restrictive in view of low real interest rate levels and the strong growth of the monetary base, the import-deposit measures implemented last May do appear to have tightened liquidity conditions. Also, the austerity program announced in July implies a real tightening of fiscal policy. If the program is fully implemented, tax collections will increase by almost 3 per cent of GNP as a result of increases in certain VAT rates, higher utility charges and efforts to keep the central budget deficit unchanged from 1974 levels.

Activity in Japan has declined sharply this year, partly in response to shocks generated by the oil crisis and restrictive policies in effect since early 1973. The weakness in output has also begun to affect sectors such as chemicals and iron and steel, which had generally been buoyant in recent months. As recently as mid-year, some real growth was foreseen for 1974, but subsequent revisions now indicate that real GNP may decline by perhaps 3 per cent this year. In September the aggregate index for industrial output stood 6.9 per cent below the year-earlier level. For institutional reasons, registered unemployment remains only slightly above 1 per cent of the labor force, but employers have trimmed work-weeks, overtime in many sectors has declined, and the ratio of job offers to applicants has fallen sharply.

Price and wage increases in Japan this year have been particularly sharp. While nominal wage rates in manufacturing increased by over 30 per cent from August 1973 to August 1974, real wage gains amounted to around 5 per cent, and earnings' gains to less. For the year ended in September, wholesale prices for manufactures rose by over 26 per cent, and in October Tokyo consumer prices were 25.8 per cent above year-earlier levels.

Japanese authorities are giving clear priority to price stabilization objectives. While the price control system in effect for much of the year was dismantled in September, fourth quarter credit expansion ceilings were relaxed only slightly, and Japanese industries continue under considerable administrative guidance. No significant easing of monetary policy is expected until sometime next year, perhaps after the spring wage round. Fiscal policy this year has been contractionary, and will probably be neutral under the budget for FY1975, according to preliminary information.