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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**

December 11, 1974

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DOMESTIC NONFINANCIAL SCENE

December 11, 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	Nov.	12/6/74	91.7	-4.2 ^{1/}	2.8 ^{1/}	2.0
Unemployment rate (per cent)	Nov.	12/6/74	6.5	6.0 ^{1/}	5.4 ^{1/}	4.7 ^{1/}
Insured unemployment rate (%)	Nov.	12/6/74	4.3	3.6 ^{1/}	3.3 ^{1/}	2.6 ^{1/}
Nonfarm employment, payroll (mil.)	Nov.	12/6/74	78.4	-6.7	-1.5	.6
Manufacturing	Nov.	12/6/74	19.6	-20.8	-9.6	-3.4
Nonmanufacturing	Nov.	12/6/74	58.7	-1.9	1.3	2.0
Private nonfarm:						
Average weekly hours (hours)	Nov.	12/6/74	36.2	36.6 ^{1/}	36.7 ^{1/}	36.9 ^{1/}
Hourly earnings (\$)	Nov.	12/6/74	4.35	2.8	7.5	7.9
Manufacturing:						
Average weekly hours (hours)	Nov.	12/6/74	39.5	40.1 ^{1/}	40.2 ^{1/}	40.6 ^{1/}
Unit labor cost (1967=100)	Oct.	12/2/74	137.6	18.6	10.4	10.3
Consumer prices (1967=100)	Oct.	11/21/74	153.2	10.3	13.9	12.2
Food	Oct.	11/21/74	166.9	16.0	18.8	11.9
Commodities except food	Oct.	11/21/74	142.5	6.8	12.4	14.0
Services ^{2/}	Oct.	11/21/74	157.3	10.8	12.6	10.6
Wholesale prices (1967=100)	Oct.	11/14/74	171.2	27.9	25.5	22.6
Industrial commodities	Oct.	11/14/74	165.1	13.4	19.0	28.3
Farm products & foods & feeds	Oct.	11/14/74	188.0	56.8	41.8	10.6
Personal income (\$ billion) ^{3/}	Oct.	11/14/74	1186.4	8.6	9.3	8.8
						(Not at Annual Rates)
Mfrs. new orders dur. goods (\$ bil.)	Oct.	12/3/74	45.3	-2.3	-5.0	4.7
Capital goods industries:	Oct.	12/3/74	12.8	-5.0	-9.5	.6
Nondefense	Oct.	12/3/74	11.5	-3.0	-10.3	5.0
Defense	Oct.	12/3/74	1.4	-19.5	-1.9	-26.1
Inventories to sales ratio:						
Manufacturing and trade, total	Sept.	11/14/74	1.49	1.47 ^{1/}	1.49 ^{1/}	1.47 ^{1/}
Manufacturing	Oct.	12/3/74	1.65	1.66 ^{1/}	1.63 ^{1/}	1.57 ^{1/}
Trade	Sept.	11/14/74	1.34	1.31 ^{1/}	1.33 ^{1/}	1.33 ^{1/}
Ratio: Mfrs.' durable goods inventories to unfilled orders	Oct.	12/3/74	.704	.687 ^{1/}	.689 ^{1/}	.727 ^{1/}
Retail sales, total (\$ bil.)	Nov.	12/10/74	45.3	-1.3	-3.8	5.3
GAF ^{5/}	Nov.	12/10/74	11.7	-1.1	-1.8	3.5
Auto sales, total (mil. units) ^{3/}	Nov.	12/5/73	7.0	-13.1	-35.2	-33.3
Domestic models	Nov.	12/5/73	5.7	-11.0	-37.9	-35.0
Foreign models	Nov.	12/5/73	1.3	-21.5	-19.5	-24.4
Plant & equipment expen. (\$ bil.) ^{4/}						
All industries	1974	12/3/74	111.92	--	--	12.2
All industries	'74:Q3	12/3/74	113.99	2.3	--	13.0
All industries	'74:Q4	12/3/74	114.40	.4	--	10.3
All industries	'75:Q1	12/3/74	118.06	3.2	--	10.1
All industries	'75:Q2	12/3/74	119.47	1.2	--	7.2
Housing starts, private (thous.) ^{3/}	Oct.	11/21/74	1,124	-.7	-16.0	-32.9
Leading indicators (1967=100)	Oct.	12/2/74	170.3	-1.3	-5.4	2.1

^{1/} Actual data. ^{2/} Not seasonally adjusted. ^{3/} At annual rate. ^{4/} Planned--
Commerce November plans. ^{5/} Advance confidential.

DOMESTIC NONFINANCIAL DEVELOPMENTS

A substantial downward adjustment in economic activity is now well underway, and appears to be spreading rapidly. The November decline in industrial production and the rise in unemployment were very sharp. Consumer expenditures generally have weakened further, while sales of motor vehicles have declined precipitously. Recent reports indicate that businessmen are cutting capital spending plans; actually, fixed investment in real terms appears to be declining in the current quarter. Moreover, producers and distributors are now making vigorous efforts to reduce inventories. Wage and price pressures remain strong but recent movements in both wages and prices show some signs of moderation.

Industrial production in November is tentatively estimated to have dropped at least 2 per cent, an abrupt decline by historical standards. Well publicized reductions in output of automotive products, coal, and steel--though large--accounted for less than half of the total decrease. Household goods, apparel, construction products, nonferrous metals, textiles, paper, chemicals, and rubber products were all down appreciably. In addition, presently available data suggest a cut in output of business equipment.

Auto assemblies dropped about one-fifth in November to an annual rate of 6.8 million units, but production remained far above sales for the second month in a row. Inventories of new autos mounted, and stocks of domestic-type new cars at the end of November were

equivalent to 106 days' supply at the reduced current sales rate, a post-World War II high. Stocks of imported cars were reported to be even higher in terms of number of days supply. Producers have scheduled another 20 per cent cutback in assemblies for December to about a 5-1/2 million rate, about equal to the November sales rate.

As a result of the strike, production of coal was off about 30 per cent in November. Output of raw steel declined 5 per cent for the month as a whole, partly because of shortages of coal, and by the last week of November was about 10 per cent below the October average.

With auto assemblies being reduced drastically and with further weakness clearly evident in other sectors, industrial production is expected to decline again in December. The resumption of coal production in mid-December will provide only a small offset to the prospective decline, nor is the steel industry likely to provide any stimulus to output. Final demands for steel appear to be easing and the temporary hedging against a coal strike now has been eliminated.

Weakened demands have substantially reduced pressure on manufacturing capacity. Capacity utilization rates in major materials decreased further in November, with the index down more than 3 per cent to 84.0, the largest decline so far this year. This index has fallen about 7 per cent since last July, and is 11 per cent below its peak in mid-1973.

An accelerating deterioration is evident in the labor market. In November the unemployment rate jumped to 6.5 per cent, up from 6.0

the previous month. Although the labor force declined by more than 300,000, this was more than offset by a drop in employment of nearly 800,000. Moreover, an additional 300,000 workers who usually work full-time work were on part-time for economic reasons.

The increase in the unemployment rate from September to November was the sharpest two month rise since 1958. There were large increases in unemployment in both months among experienced workers, particularly those employed in manufacturing and in construction.

Nonfarm payroll employment fell by 440,000 in November with declines recorded in nearly every goods-producing sector. The largest decrease was in manufacturing, especially electrical equipment, transportation equipment and textiles. Factory hours of work were also off sharply. Because of the timing of the survey, the employment figures were little affected by the coal strike and they take account of only a small portion of the announced layoffs of automobile workers. In the service-producing industries, a large drop in employment in retail trade more than offset moderate gains in services and in State and local governments.

Retail sales weakened further in November. According to the advance Census estimates, total retail sales in current dollars dropped 1.3 per cent, the third consecutive monthly decline. The largest decrease last month was in the automotive group but outlays for general merchandise were off as well. Total retail sales apart from autos and nonconsumer items were down .4 per cent. Compared with a year earlier, sales of all stores were up only 5.3 per cent.

Sales of new domestic-type autos were at a 5.7 million unit annual rate in November, 11 per cent below October and 35 per cent below November 1973. Sales of foreign autos, which had been relatively strong in October fell even more sharply in November, to a 1.3 million annual rate. The decline in total auto sales has been deeper than anticipated and the staff again has revised downward its estimate of fourth quarter unit sales.

The sharp slump in demand for autos reflects several factors, including the increase in new auto prices, the decline of real earnings and mounting consumer apprehension concerning inflation and unemployment. The recently released Conference Board and Michigan Surveys report measures of consumer confidence down substantially--for Michigan, lower than at any time in its twenty-five year history. The Michigan survey also reported more intense inflationary expectations but less willingness to buy in advance of expected price increases.

Financial influences also may have played a part. There has been some attempt to stimulate sales through lengthening maturities over the past year. Thus, in September 10.5 per cent of new car loans at finance companies were written with maturities of over 36-months, up from 3.2 per cent a year earlier. However, there has been a counteracting increase in interest charges and in downpayment requirements, as evidenced by a decline in loan to value ratios.

Recent indications portend a further contraction in real expenditures for business fixed investment in most sectors other than the materials industries. Total new orders for durable goods have continued to drop; in constant dollars, nondefense capital goods orders fell by 5.9 per cent further in October--the third consecutive month of decline. Contracts for commercial and industrial construction weakened further in October with reductions in both commercial and industrial categories; total contracted floor space was more than 30 per cent below a year earlier.

The Commerce Department's latest quarterly plant and equipment survey--conducted from mid-October through November--indicates that outlays for the first half of 1975 are expected to rise at an annual rate of 8.2 per cent, down from the 12.2 per cent increase now anticipated for calendar 1974, and somewhat less than implied by the McGraw-Hill survey taken earlier. Both the Commerce survey and Conference Board data on capital appropriations in manufacturing indicate that prospective capital spending plans by materials producers remain relatively strong, whereas planned expenditures of other industries are virtually flat in constant dollars.

Residential construction activity as yet shows no signs of an imminent turnaround. Private housing starts in October were slightly below the third quarter average and the lowest since the first quarter of 1967. Given the extent of the drop from the cyclical peak in the first quarter of 1973--more than 50 per cent--plus the leveling

off of starts in the past few months and the recent improvement in savings flows to thrift institutions, it is the staff judgment that starts are bottoming out. However, under prevailing market conditions, lags are likely to be longer than usual, and the recent improved flows to savings institutions are expected to have little impact on starts before next spring. In October, sales of new single-family homes by merchant builders fell to a 4-1/2 year low and related stocks rose to 12 months' supply--a near record high for the series.

Recent rates of price rise have shown signs of moderation in some sectors, although price increases continue large, particularly for finished goods. Prices of industrial materials in spot markets have fallen further, and as of December 3 they were down more than 25 per cent from their early April peak, based on the FR basic commodity price index. While wholesale prices of industrial commodities rose at an annual rate of about 15 per cent from August to October, this was an improvement from the over 30 per cent rate of increase recorded previously this year. Several components of the WPI have actually declined recently, including textile products, nonferrous metals, hides and skins and lumber and wood products. Advances in October were smaller than in earlier months for several groups such as iron and steel and most paper products. However, increases were still substantial for chemicals, fuels and power, motor vehicles and machinery and equipment.

Consumer prices in October increased at an annual rate of about 10 per cent. Food prices rose at a 16 per cent rate despite a decline in beef. However, the increase of close to 7 per cent for nonfood commodities was the smallest this year. Price increases were large for most groups, but gasoline prices declined again and apparel prices have changed little since August. The cost of services rose at about an 11 per cent annual rate.

The average hourly earnings index for the private nonfarm economy rose at an annual rate of 6.6 per cent in November following a 7.4 per cent rise in October, compared to a 11.0 per cent increase in the third quarter. A more moderate rate of increase was evident in manufacturing, trade and services but wages continued to climb rapidly in the construction and transportation and public utilities industries.

The new three year contract accepted by coal miners, ending a four week walkout, reportedly will raise wages and benefits by over 50 per cent over the life of the contract, assuming the maximum payable (8 per cent per year) under the escalator clause. In other collective bargaining developments, aerospace workers for United Aircraft settled a new three year contract which will provide increased benefits and a first year wage increase of 14 per cent, and about a 40 per cent wage rise over the life of the contract.

The staff is currently projecting Federal budget outlays for fiscal year 1975 at \$307 billion, sharply higher than the projection of \$299.5 billion contained in the November Greenbook. For the first four

months of the fiscal year expenditures have been running well above the amount implied by the Administration's former budget target. In his November 26 Message on Budget Restraint, the President revised upward the outlay target to \$302.2 billion. The current staff projection of \$307 billion differs from the new Administration estimate because we expect higher unemployment compensation outlays, a larger public service employment program, and we also assume that Congress will respond to only a small part of the President's proposed \$4.6 billion cut in outlays.

Budget receipts are now estimated at \$290.1 billion, yielding a fiscal year 1975 deficit of \$16.9 billion. The current receipts projection is \$4.5 billion below the estimate contained in the November Greenbook. This shortfall is accounted for by revisions which reflect the pattern of actual receipts and by an adjustment reflecting corporate shifts to a LIFO method of inventory valuation. In view of uncertainties regarding congressional action, these projections assume no new tax legislation.

RETAIL SALES
 (Seasonally adjusted, percentage change from
 previous period)

	1974				
	QII	QIII	Sept.	Oct.	Nov.
Total sales	2.9	4.4	-1.9	- .7	-1.3
Durable	4.4	5.9	-6.3	-5.2	-2.8
Auto	5.5	10.6	-9.4	-8.6	-6.0
Furniture & appliance	3.7	2.0	- .6	-2.3	3.3
Nondurable	2.3	3.6	.3	1.3	- .7
Food	1.7	5.0	1.0	1.1	1.4
General merchandise	2.0	.9	.7	- .4	-1.7
Gasoline	8.8	4.7	.7	- .8	-1.0
Total, less auto and nonconsumption items	2.6	3.4	.0	1.1	- .4
GAF	1.6	1.6	.3	- .9	-1.1
Real*	.1	1.3	-3.1	-1.6	n.a.

* Deflated by all commodities CPI, seasonally adjusted.

MAJOR MATERIALS UTILIZATION
(Seasonally adjusted, per cent)

	1973			1974			1974					
	II	III	IV	I	II	III	June	July	Aug.	Sept.	Oct.	Nov.**
Major materials	93.4	93.5	92.3	90.2	90.2	88.2	89.2	90.0	87.8	87.3	86.8	84.0
Textiles (yarn, fibers, woven fabric)	94.0	93.5	92.9	92.5	90.4	88.3	88.2	91.5	88.3	86.7	85.3	
Paper, pulp, board	95.6	98.0	96.4	95.1	96.6	95.6	96.3	98.0	91.7	95.7	92.1	
Paperboard	95.4	94.1	93.7	93.0	95.9	91.8	95.7	98.0	84.7	92.5	84.2	75.0
Petroleum Refining	97.5	95.3	92.8	84.7	90.8	88.8	90.4	90.9	89.7	86.9	88.1	
Metals*	91.3	92.3	92.6	91.1	90.5	88.0	89.8	88.5	86.8	88.4	89.5	
Basic Iron and Steel	93.4	94.3	94.7	92.6	91.5	90.0	91.0	90.7	89.5	89.6	91.8	86.0
Aluminum	92.0	92.7	95.3	98.1	99.1	97.9	98.6	99.0	98.7	97.5	96.6	
Chemicals	91.2	91.1	90.0	88.6	86.7	86.7	85.3	88.4	87.8	85.8	87.0	
Cement	90.3	91.8	90.7	92.7	86.1	77.6	85.8	78.3	77.9	76.6	78.5	
Plywood	94.6	91.3	87.9	83.3	84.7	79.8	79.7	81.4	80.3	78.3	74.7	73.0

*Consists of basic iron and steel, aluminum, and copper.

**Projection, based on weekly data.

Monthly data are confidential.

SELECTED UNEMPLOYMENT RATES
(Seasonally adjusted)

	<u>1973</u>	<u>1974</u>	
	November	October	November
Total	4.7	6.0	6.5
Men 20 years and over	3.0	4.3	4.6
Women 20 years and over	4.7	5.6	6.6
Teenagers	14.5	16.9	17.3
Household heads	2.8	3.7	3.9
White	4.2	5.4	5.8
Negro and other races	8.9	10.9	11.7
White collar workers	2.8	3.3	3.7
Blue collar workers	5.4	7.3	8.2

CHANGES IN NONFARM PAYROLL EMPLOYMENT

	Employment (Nov. 1974)	Average Monthly Change	
		Oct. 1974- Nov. 1974	Nov. 1973- Nov. 1974
Total nonfarm	78,368	-443	+38
Goods-producing	24,162	-408	-75
Construction	3,855	- 49	-20
Manufacturing	19,628	-348	-57
Service-producing	54,206	- 35	+113
Trade	17,041	-119	+11
Services	13,748	+ 37	+44
State and local gov't.	11,782	+ 48	+44

RESULTS OF COMMERCE PLANT AND EQUIPMENT SURVEY
(In billions of dollars) 1/

	1974				1975	
	I	II	III	IV	I	II
	-----Anticipated ^{2/} -----					
All industry	107.27 (14.3)	111.40 (16.3)	113.99 (9.6)	114.40 (1.4)	118.06 (13.4)	119.47 (4.9)
Manufacturing	42.96 (25.2)	45.32 (23.9)	47.04 (16.1)	47.33 (2.5)	50.68 (31.5)	52.62 (16.2)
Durables	21.43 (19.9)	22.50 (21.5)	23.08 (10.7)	23.45 (6.6)	24.09 (11.4)	24.50 (7.0)
Nondurables	21.53 (30.9)	22.82 (26.2)	23.96 (21.5)	23.88 (-1.3)	26.59 (53.7)	28.12 (25.1)
Nonmanufacturing	64.31 (7.8)	66.08 (11.5)	66.94 (5.3)	67.06 (.7)	67.38 (1.9)	66.85 (-3.1)

1/ Figures in parentheses are percentage change from previous quarter at compound annual rate.

2/ Survey conducted in late October and November.

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

	1974				Per cent change in October from:	
	QII	QIII	Sept.	Oct.(P)	Month ago	Year ago
Permits	1.17	.91	.82	.80	- 3	-42
Starts	1.57	1.20	1.13	1.12	- 1	-33
1-family	.98	.87	.84	.79	- 6	-18
2- or more-family	.59	.33	.30	.34	+14	-53
Under construction ^{1/}	1.48	1.37	1.37	n.a.	- 3 ^{2/}	-20 ^{2/}
Completions	1.74	1.54	1.46	n.a.	- 2 ^{2/}	-25 ^{2/}
MEMO:						
Mobile home shipments	.44	.36	.32	.25	-22	-46

^{1/} Seasonally adjusted, end of period.

^{2/} Per cent changes based on September.

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

CONSUMER PRICES						
	Relative importance to Dec. 1973	Dec. 1972 to Dec. 1973	Dec. 1973 to Mar. 1974	March to June 1974	June to Sept. 1974	Sept. to Oct. 1974
All items	100.0	8.8	14.2	10.9	14.2	10.3
Food	24.8	20.1	19.4	3.1	12.3	16.0
Commodities less food	38.6	5.0	16.0	15.8	16.5	6.8
Services ^{2/}	36.6	6.2	9.2	11.0	13.9	10.8
Addendum						
All items less food and energy components ^{3/4/}	68.8	4.7	8.6	12.8	15.2	10.6
Petroleum products ^{3/5/}	4.0	23.4	99.3	26.6	-4.1	-17.3
Gas and electricity	2.4	6.9	28.2	16.1	20.2	11.9

WHOLESALE PRICES

All commodities	100.0	15.4	24.5	12.2	35.2	27.9
Farm and food products	31.7	26.7	10.8	-29.3	59.2	56.8
Industrial commodities ^{6/}	68.3	10.7	32.3	35.7	28.3	13.4
Materials, crude and intermediate	43.5	13.3	36.9	40.6	31.7	11.0
Finished Goods:						
Consumer excluding foods	17.6	7.4	28.3	25.3	18.5	20.8
Producer	8.5	5.3	13.2	27.2	31.8	29.1
Consumer foods	14.3	22.5	17.3	-16.7	29.4	47.5

^{1/} Not compounded for one-month changes.

^{2/} Not seasonally adjusted.

^{3/} Confidential -- not for publication.

^{4/} Excludes food, gasoline and motor oil, fuel oil and coal, and gas and electricity.

^{5/} Includes coal.

^{6/} Stage of processing components do not add to the total because they include some items found in farm and food products group.

Note: Changes in CPI since March 1974 subject to revision next month to correct for error in used car component. WPI for October also subject to change because of correction for price of raw sugar.

TABLE 6
FEDERAL BUDGET AND FEDERAL SECTOR IN NATIONAL INCOME ACCOUNTS
(In billions of dollars)

	Fiscal Year 1974*	Fiscal 1975 e/		Fiscal 1976 FRB e/	Calendar Years			F.R. B. Staff Estimates				
		Adm. Est. 11-26-74 1/	F.R. Board		1973 Actual	FRB e/		Calendar Quarters		1975		
						1974	1975	1974	1975	III*	IV	I
								Unadjusted data				
Federal Budget												
Surplus/deficit	-3.5	-9.2	-16.9	-31.5	-7.9	-10.4	-22.1	-1.6	-11.4	-9.9	6.0	
Receipts	264.9	293.0	290.1	307.5	250.4	279.4	299.1	72.9	65.8	67.0	84.4	
Outlays	268.4	302.2	307.0	339.0	258.3	289.8	321.2	74.5	77.2	76.8	78.4	
Means of financing:												
Net borrowing from the public	3.0	n.a.	18.0	n.e.	7.9	12.4	25.6	4.5	10.9	7.7	-5.1	
Decrease in cash operating balance	3.4	n.a.	2.4	n.e.	.7	3.4	--	.5	1.7	.2	--	
Other 2/	-2.9	n.a.	-3.5	n.e.	-.7	-5.4	-3.5	-3.4	-1.2	2.0	-.9	
Cash operating balance, end of period	9.2	n.a.	6.8	n.e.	10.4	7.0	7.0	8.7	7.0	6.8	6.8	
Memò: Sponsored agency borrowing 3/	14.8	n.a.	16.3	n.e.	16.3	16.4	n.e.	7.7	3.2	2.4	3.1	
								Seasonally adjusted, annual rates				
National Income Sector												
Surplus/deficit	-5.4 ^{p/}	n.a.	-12.4 ^{4/}	-30.9 ^{4/}	-5.6	-3.8	-22.9	-1.1	-8.4	-16.4	-21.2	
Receipts	272.6 ^{p/}	n.a.	303.6 ^{4/}	318.1 ^{4/}	258.5	293.7	308.4	303.5	304.4	304.6	304.4	
Expenditures	278.0 ^{p/}	n.a.	316.0	349.0	264.2	297.5	332.4	304.7	312.8	321.0	325.6	
High Employment surplus/deficit (NIA basis) 5/ p/	8.1	n.a.	17.5	32.9	1.9	10.5	25.7	8.8	14.8	19.7	26.5	

- * Actual e--projected n.e.--not estimated n.a.--not available p--preliminary
- 1/ Estimates presented in the President's Message on Budget Restraint. \$302.2 billion outlay total assumes favorable Congressional action on \$4.6 billion of proposed reductions.
- 2/ Includes such items as deposit fund accounts and clearing accounts.
- 3/ 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.
- 4/ Quarterly average exceeds fiscal year total by \$.6 billion for fiscal 1975 and \$1.3 billion for fiscal 1976 due to spreading of wage base effect over calendar year.
- 5/ Estimated by F.R. Board Staff.

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DOMESTIC FINANCIAL SITUATION

III-T-1

SELECTED DOMESTIC FINANCIAL DATA
(Dollar amounts in billions)

Indicator	Latest data		Net change from			
	Period	Level	Month ago	Three months ago	Year ago	
<u>Monetary and credit aggregates</u>			<u>SAAR (per cent)</u>			
Total reserves	November	37.0	1.5	2.5	8.6	
Reserves available (RPD's)	November	35.0	.8	2.6	9.4	
Money supply						
M1	November	283.1	6.0	3.7	5.1	
M2	November	612.6	9.5	7.0	8.0	
M3	November	951.0	8.5	6.2	7.1	
Time and savings deposits (Less CDs)	November	329.5	12.5	10.0	10.7	
CDs (dollar change in billions)	November	85.5	-.7	1.7	22.4	
Savings flows (S&Ls + MSBs)	November	338.4	6.4	4.7	5.6	
Bank credit (end of month)	November	693.2	4.2	-1.3	9.8	
<u>Market yields and stock prices</u>			<u>Percentage or index points</u>			
Federal funds	wk. endg.	12/4/74	9.02	-.61	-2.62	-1.15
Treasury bill (90 day)	"	12/4/74	7.45	-.31	-1.73	.09
Commercial paper (90-119 day)	"	12/4/74	9.22	.22	-2.72	-.11
New utility issue Aaa	"	12/6/74	9.49	.49	-1.12	1.43
Municipal bonds (Bond Buyer)	1 day	12/5/74	6.89	.23	.01	1.74
FNMA auction yield (FHA/VA)		12/2/74	9.61	-.32	-.98	.80
Dividends/price ratio (Common stocks)	wk. endg.	11/30/74	5.23	.20	-.01	1.68
NYSE index (12/31/65=50)	end of day	12/3/74	35.65	-2.88	-.28	-14.23
<u>Credit demands</u>			<u>Net change or gross offerings</u>			
			<u>Current month</u>		<u>Year to date</u>	
			1974	1973	1974	1973
Business loans at commercial banks	November		.9	1.2	27.9	26.3
Consumer instalment credit outstanding	October		.4	1.7	9.6	17.9
Mortgage debt outst. (major holders)	September		2.6	4.2	35.9	48.3
Corporate bonds (public offerings)	November		2.9e	1.7	23.3e	12.1
Municipal long-term bonds (gross offerings)	November		2.2e	2.3	21.4e	21.9
Federally sponsored Agcy. (net borrowing)	November		-.2e	-	15.2e	15.8
U.S. Treasury (net cash borrowing)	December		5.8e	3.1	12.4e	7.9
Total of above credits			14.6	14.2	145.7	150.2

e - Estimated

DOMESTIC FINANCIAL DEVELOPMENTS

Market interest rates generally backed up significantly in the weeks immediately following the November FOMC meeting. But with Federal funds trading at rates below 9 per cent in recent days and the Board's announcement of a lowering of the discount rate to 7-3/4 per cent from 8 per cent last Friday, short term rates have dropped back to levels near or below those prevailing at the time of the November meeting. Yields on corporate and Treasury bonds also have declined recently, but are up somewhat on balance, while yields on municipals have continued to advance.

With interest rates remaining well below their summer and early fall highs, inflows into consumer-type time and savings deposits at banks and non-bank thrift institutions have continued to improve in recent weeks. Also, demand deposit growth at banks has strengthened. Banks and other thrift institutions have used a substantial share of these incoming funds to repay other short term liabilities and/or rebuild liquidity positions. At the same time, demand for credit at intermediaries has continued on the weak side, so that growth in loans and investments at banks and in mortgage holdings at thrift institutions has been relatively slow.

Short term markets. After posting sharp and fairly steady declines from early August until about the time of the November FOMC meeting, private short term rates backed up from 1/4 to close to a full percentage point in the weeks immediately following the meeting, and Treasury bill rates have fluctuated within a fairly narrow range. Interruption of the

earlier downtrend in short-term rates was attributable largely to the behavior of the Federal funds rate, which leveled off at slightly below 9.50 per cent during the final three statement weeks of November after previously declining in every statement week but one beginning in the second week of July.

In the statement week ended last Wednesday, however, the Federal funds rate dropped to an average of 9.02 per cent and on subsequent days funds generally have traded at rates below 9 per cent without eliciting System intervention in the market. This easing in the funds market, together with last Friday's 1/4 percentage point reduction in the discount rate to 7-3/4 per cent, has renewed downward pressures on short-term rates generally. As a result, these rates have dropped back to levels near or somewhat below those prevailing at the time of the November meeting, and about 225 to 350 basis points below their record high levels reached this past summer.

Demands for short-term funds in securities markets remained fairly heavy in November. Large businesses continued to issue an appreciable volume of commercial paper, as rates on these issues remained considerably under the lagging prime rate. In addition, the U.S. Treasury continued to add \$200 million to each of its weekly and monthly bill auctions and recently sold a substantial block of tax anticipation bills. Finally, CD's and nondeposit liabilities at banks showed a sizable increase in recent weeks, after declining on balance in November.

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Selected Short-Term and Long-Term Interest Rates
(in per cent)

	Aug. FOMC Aug. 20	Sept. FOMC Sept. 11	Oct. FOMC Oct. 15	Nov. FOMC Nov. 19	Nov. 26	Dec. 3	Dec. 10
<u>Short Term</u>							
Federal funds (weekly average)	12.23	11.48	10.11	9.34	9.46	9.02	8.89 ^{1/}
Treasury bills							
3-month	9.05	9.06	7.74	7.46	7.42	7.53	7.15
6-month	9.13	8.83	7.92	7.37	7.56	7.40	6.98
1-year	8.86	8.63	7.70	7.18	7.29	7.16	6.90
Commercial paper							
1-month	12.00	11.75	9.75	9.13	9.13	9.63	9.13
3-month	11.88	11.75	9.50	8.88	9.00	9.25	8.88
Large neg. CD's ^{2/}							
3-months	12.35	11.85	9.63	8.63	9.35	9.60	8.80
6-months	12.15	12.00	9.50	8.50	9.00	9.10	8.55
Federal agencies							
1-year	9.65	9.77	8.57	8.04	7.94	n.a.	n.a.
Bank prime rate	12.00	12.00	11.75	10.75	10.50	10.50	10.50
<u>Long Term</u>							
Corporate							
New AAA	10.26	10.27	10.44	9.17	9.68	9.49	n.a.
Recently offered	10.28	10.30	10.36	9.29	9.38	9.35 ^p	n.a.
Municipal (Bond Buyer)							
	6.73	6.79	6.48	6.53	6.71	6.89	n.a.
U.S Treasury 20-yr. constant maturity)							
	8.58	8.59	8.31	7.93	7.96	8.06	7.84
Stock Prices							
Dow-Jones	726.85	654.72	658.40	614.05	617.26	596.61	593.87
N.Y.S.E	39.32	35.82	37.67	36.19	36.86	35.65	35.53

^{1/} First 6 days of statement week ending December 10.

^{2/} Highest quoted new issues.

Long-term markets. Bond yields have increased on balance since the November FOMC meeting. They rose significantly in the latter part of November and the first few days of December, partly in response to the back-up in short-term rates, and then edged down along with the yield decline in short markets. An additional factor contributing to upward rate pressures in the bond markets has been the recent and prospective large volume of financing by corporations, State and local governments, and the U.S. Treasury.

Despite AT&T's decision to postpone a \$600 million issue because of an anti-trust suit recently filed by the Justice Department, the volume of new corporate issues brought to market has remained particularly heavy and corporate new issue yields have moved up as much as 30 basis points. The projected volume for December is \$2.7 billion, which, although smaller than the near record volumes of October and November, is unusually large for this month. Another relatively heavy calendar is in prospect for January.

SECURITY OFFERINGS
(Monthly or monthly averages, in millions of dollars)

	1973	1974					1975
	Year	Half I ^{e/}	QIII ^{e/}	QIV ^{f/}	Nov. ^{e/}	Dec. ^{f/}	Jan. ^{f/}
<u>Gross offerings, long term</u>							
Corporate securities -							
Total	2,779	3,047	2,600	4,183	3,850	4,000	3,200
Public bonds	1,125	1,950	1,767	3,000	2,900	2,700	2,200
Privately placed							
bonds	725	543	467	567	400	900	600
Stock	929	555	367	616	550	400	400
State and Local govern- ment securities	1,942	2,113	1,833	1,967	2,200	1,400	2,000
<u>Net offerings, total</u>							
U.S. Treasury	658	-501	1,498	3,640	4,400	5,800	2,700
Sponsored Federal Agency	1,367	925	2,519	1,066	-200	1,200	900

e/ Estimated.

f/ Forecast.

The volume of new issues in the municipal market has been smaller than in the corporate market but the largest yield advances were posted in this sector as traditional buyers of tax exempts-- commercial banks and casualty companies--reportedly have shown only modest interest in acquiring such issues. As a result, dealer inventories rose further to unusually high levels in late November, and have remained relatively high in early December. Last week, moreover, municipal yields were given an additional boost by a record-setting yield on a New York City financing operation.

Yields on long-term Treasury securities were subject to the least upward pressure following the November Committee meeting and recently have edged back near levels prevailing at the time of the meeting. Conditions in this sector of the market have been quiet since the Treasury's mid-November refunding operation, as dealers have remained content to hold sizable quantities of the coupon issues they were awarded in this financing. It is widely believed that the Treasury's deficit will considerably exceed the upward revised \$9.2 billion figure recently announced by the President, perhaps by as much as \$6-10 billion. The impact of this reassessment of the Treasury financing outlook has been tempered to some extent, however, by downward adjustments in projections of borrowing by the sponsored Federal agencies in light of the improving deposit inflows at thrift institutions.

In equity markets, prices have declined approximately 10 per cent since early November. The Dow-Jones Industrial index closed

last Friday at 577.50, its lowest level in 12 years, but has moved up about 12 points so far this week. It appears that the further decline in prices was prompted mainly by the spate of news portraying a much weaker pattern of economic activity--and thus lower corporate profits--than was previously believed likely by investors.

Monetary and deposit aggregates. Responding to the sharp net decline in market interest rates over the past 4 months, inflows into demand deposits at commercial banks increased further in November, and, with public demands for currency remaining unusually strong, M_1 rose at a 6.0 per cent annual rate, well above the 2 per cent rate of expansion in the 4 months ending with October. Growth of time and savings deposits other than money market CD's was about the same in November as October's rapid rate and M_2 expanded at a 9.5 per cent rate, the highest since the first quarter. A further strengthening of deposit inflows at mutual savings banks and savings and loan associations is also indicated by sample deposit data for November. It is currently estimated that aggregate deposits at these institutions grew at about a 7-1/2 per cent annual rate, the largest monthly increase of the year except for March.

Commercial banks also experienced a sizable buildup in Treasury balances during November. Banks, in general, used a considerable portion of their regular deposit flows to reduce nondeposit liabilities and money market CD's. Since late November, however, a number of large New York City banks have again increased their large CD's and Euro-dollar borrowings.

MONETARY AGGREGATES
(Seasonally adjusted changes)

	1 9 7 4					
	QI	QII	QIII	Sept.	Oct.	Nov. p
	<u>Per cent at annual rates</u>					
M ₁	5.5	6.5	1.6	1.3	3.8	6.0
M ₂	9.3	7.7	4.6	3.2	8.3	9.3
M ₃	8.8	6.4	4.0	2.9	6.9	8.4
Adjusted bank credit proxy	8.2	20.4	6.6	3.9	- .2	5.9
Time and savings deposits						
At commercial banks:						
a. Total	15.1	21.3	9.2	6.8	13.8	7.6
b. Other than large CD's	12.8	8.6	7.3	4.9	12.3	12.1
At savings and loans ^{1/}	9.6	5.2	3.3	4.2	6.5	8.5
At mutual savings banks ^{1/}	4.8	1.8	.4	1.9	3.3	5.0
Combined	8.2	4.2	2.4	3.5	5.6	7.5

Billions of dollars ^{2/}

Memoranda:

a. U. S. Government demand deposits	- .2	.7	.3	.1	-2.6	.9
b. Negotiable CD's	1.4	4.4	1.2	1.0	1.4	- .8
c. Nondeposit sources of funds	.3	.3	.1	-.4	- .7	- .2

^{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.

Nonbank thrift institutions similarly used a large share of their recent fund inflows to repay loans at commercial banks and many S&L's reduced FHLB advances. Although FHLB's extended the entire \$500 million monthly allocation of subsidized advances, net advances over the month rose only \$100 million.

Credit developments. Banks and other thrift institutions generally appear to be following more conservative balance sheet policies than in comparable periods of earlier cyclical downturns. This is suggested by the pay-down of money market type liabilities referred to above. In addition, replies to the November Lending Practices Survey suggest that non-price lending terms have remained quite stringent. (The results of this survey will be summarized in the Supplement to the Greenbook.) Finally, the lagged response in bank prime rates to the decline of market rates--with most banks still quoting 10-1/2 per cent--illustrates the continuing bank efforts to discourage loan expansion.

Reflecting these constraints, total loans and investments at commercial banks are estimated to have increased at only a 4 per cent annual rate in November, about in line with the sharply reduced rate of growth since mid-year. Investment holdings rose only slightly as a significant increase in holding of municipals and agency securities--the second such advance in as many months--was largely offset by a further rundown in holdings of U.S. Treasury securities. Total loans also rose only moderately and no significant strength was displayed in any of the major loan categories.

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

	1974					
	QI	QII	QIII	Sept.	Oct.	Nov.
Total loans and investments ^{2/}	17.5	12.0	5.6	-8.6	--	4.2
U.S. Treasury securities	27.3	--	29.8	-67.3	-57.5	-9.7
Other securities	8.3	10.8	--	.9	11.4	7.8
Total loans ^{2/}	19.0	13.8	11.2	-4.8	2.9	4.5
Business loans ^{2/}	24.0	22.9	14.0	--	11.1	5.8
Real estate loans	12.9	14.2	6.0	3.8	2.8	4.7
Consumer loans	5.4	4.4	7.2	2.9	1.4	0.0

MEMO:

Business loans plus nonfinancial commercial paper (per cent)	22.5	24.9	18.1	4.9	15.9	10.9
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^{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.

Business loans increased at about a 6 per cent annual rate, roughly equivalent to the September-October average pace of advance and well below that of the third quarter, as prime borrowers continued to tap the relatively low cost funds available in short-term securities markets. Growth in aggregate short-term borrowing by businesses--at banks and in the market--has remained relatively modest, as has been the case since mid-summer. In addition to the rise of capital market borrowing and general slow down of economic activity, it is likely that the need to finance a further unintended buildup of inventories in autos and other industries is being only partly counterbalanced by a rundown of inventories due to the coal strike.

Credit demands of other principal borrowing groups appear to have diminished significantly further recently. Consumer loans are estimated to have remained about unchanged at banks in November following a modest rise in October. If recent trends are continued, consumer borrowing from all lenders may weaken considerably further during November. Following a brief acceleration in July-August, when consumers increased their purchases of 1974 autos, the pace of advance in total consumer installment credit at all lenders dropped sharply in September and slowed further in October.

Real estate loans at commercial banks are estimated to have grown at a somewhat more rapid pace in November than in the two preceding months, but the rate was still below the already depressed

third quarter level. Data on net mortgage extensions at thrift institutions in November are not yet available, but fragmentary evidence suggests a slight increase in commitments is likely. This appears consistent with the downtrend in mortgage yields that has continued uninterrupted through November and into early December. As is typical of the early stage of a decline, rates have dropped more sharply in the secondary mortgage market than in the primary market.

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 <u>1</u> / (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)	--	94 (11/15)	12 (May, July-Oct.)
Low	8.40 (3/15, 3/22)	--	-106 (7/12)	0 (Feb.-Mar.)
Nov. 1	9.87	-7	45	12
8	9.81	-6	81	12
15	9.81	--	94	12
22	9.73	-8	56	12
29	9.72	-1	4	11
Dec. 6	9.69	-3	20	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 (9/9)	164 (4/18)	63 (4/8)	10.71 (9/9)
Low	26 (11/18)	18 (11/18)	8.43 (2/25)	14 (10/21)	7 (11/18)	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
18	25.7	17.6	9.81	20.6	6.8	9.92
Dec. 2	52.5	23.3	9.61	24.0	12.0	9.80

INTERNATIONAL DEVELOPMENTS

CONFIDENTIAL (FR)

12/11/74

IV -- T - 1

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

	1973	1974P			
	YEAR	1Q	2Q	3Q	OCT.*
<u>Goods and services, net</u> ^{1/}	4,391	2,928	-122		
Trade balance ^{2/}	471	-74	-1,631	-2,596	-200
Exports ^{2/}	70,277	22,299	24,089	24,632	8,560
Imports ^{2/}	-69,806	-22,373	-25,720	-27,228	-8,760
Service balance	3,920	3,002	1,509		
<u>Remittances and pensions</u>	-1,943	-390	-461		
<u>Govt. grants & capital, net</u>	-3,471	-1,218	-1,007		
<u>U.S. private capital</u> (- = outflow)	-14,101	-8,585	^{e/} -9,710		
Direct investment abroad	-4,872	-627	-1,552		
Foreign securities	-807	-646	-357	-312	-340
Bank-reported claims -- liquid	-1,103	-2,239	-1,246	-334	322
" " " other	-4,773	-2,958	-6,263	-1,582	-336
Nonbank-reported claims -- liquid	-841	-361	126		
" " " other	-1,704	-1,754	-418		
<u>Foreign capital</u> (excl. reserve trans.)	^{e/} 12,241	^{e/} 7,152	^{e/} 4,652		
Direct investment in U.S.	2,537	1,281	1,516		
U.S. corporate stocks	2,758	376	10	84	-80
New U.S. direct investment issues	1,223	24	67	13	
Other U.S. securities (excl. U.S. Treas.)	69	287	320	67	
Liquid liabilities to:	4,234	4,664	2,862	4,190	521
Commercial banks abroad	2,982	4,616	1,969	2,999	318
Of which liab. to branches ^{3/}	(309)	(3,379)	(-982)	(-567)	(-1,835)
Other private foreign	876	633	601	910	74
Intl. & regional organizations	376	-585	292	281	129
Other nonliquid liabilities	1,420	520	-123		
<u>Liab. to foreign official reserve agencies</u>	5,095	-852	4,887	1,333	1,062
<u>U.S. monetary reserves</u> (increase, -)	209	-210	-358	-1,003	30
Gold stock	--	--	--	--	--
Special drawing rights	9	--	-29	-123	-8
IMF gold tranche	-33	-209	-244	-728	-15
Convertible currencies	233	-1	-85	-152	53
<u>Errors and omissions</u>	-2,624	1,209	1,979		
<u>BALANCE</u> (deficit -)					
Official settlements, S.A.		1,062	4,529	-330	
" " , N.S.A.	-5,304	1,495	-4,104	-1,541	-1,092
Net liquidity, S.A.		-987	-6,254	-4,810	
" " , N.S.A.	-7,594	-177	-6,634	-6,042	
Liquidity, S.A. ^{4/}		-3,602	-7,391	-4,520	
" " , N.S.A.	-9,538	-2,934	-7,820	-5,711	-1,613
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/} Measured by changes in U.S. monetary reserves, all liabilities to foreign official reserve agencies and liquid liabilities to commercial banks and other foreigners.

INTERNATIONAL DEVELOPMENTS

Foreign exchange markets. The dollar depreciated by a little over one per cent on a weighted average in the past month, showing declines of around 6 per cent against the Swiss franc and 3 per cent against the mark, but smaller or no change against other major currencies. Exchange rates for the Swiss franc and, to a lesser extent, the mark were quite volatile at times, primarily owing to contradictory and confusing actions and statements by Swiss and German officials regarding their willingness to intervene to moderate upward pressures on their respective currencies. Toward the end of the period under review, sterling came under strong selling pressure in response to a move by Saudi Arabia to reduce to zero the proportion (formerly about 20 to 25 per cent) of its mid-December oil royalty payments denominated in sterling.

The Swiss franc had been under some upward pressure for a time as a result of fairly tight liquidity conditions in Switzerland at a time when there were indications that conditions were easing in some other major money markets, particularly the United States. This pressure intensified after late October when Swiss authorities removed the ban on payment of interest on non-resident franc deposits with Swiss banks. As the Swiss franc appreciated, the BNS indicated its willingness to intervene in concert to preserve orderly market conditions, but when it was not seen to intervene and when it continually denied that it had intervened, the franc soared. The BNS then moved to impose a negative interest charge on increases in non-resident franc deposits, retroactive to end-October, to prohibit

increases in banks' forward sales of francs to non-residents, and to raise reserve requirements on non-resident deposits. After having risen by about 10 per cent against the dollar in one week, the franc quickly declined by about that amount. Daily fluctuations in the dollar/franc rate reached 4 per cent on occasion in this brief period, and the rate at present continues to be extremely volatile.

The mark, which had begun to appreciate in October following a sharp decline in U.S. interest rates, surged ahead in November, particularly after a statement by Chancellor Schmidt reaffirming Germany's intention not to resist an appreciation of the mark produced by market forces.

In the period from mid-November to mid-December there were net dollar sales by major central banks amounting to nearly \$840 million, a factor contributing to the decline in the dollar's weighted average exchange value. The Bank of England sold about \$880 million, of which \$480 million came in the wake of Saudi Arabia's decision on sterling-denominated oil receipts. The Bank of Italy's dollar sales in this period amounted to \$360 million. Only partly offsetting these sales were purchases of dollars by the System and the Bundesbank. The System sold a substantial amount of marks and small amounts of guilders and Belgian francs in late November, most of which it later repurchased. The Bundesbank purchased, net, some \$240 million.

Euro-dollar market. Euro-dollar deposit rates have shown mixed movements in the past four weeks. After many weeks of a declining trend the weekly average 3-month rate has risen about 30 basis points, approximately in line with the upturn in the rate on 60-89 day CD's in the United States. In contrast, the overnight Euro-dollar rate in the latest week was down more than a percentage point from four weeks earlier, a decline that exceeded the decrease in the Federal funds rate. U.S. banks' gross liabilities to their foreign branches rose from an average of \$2.3 billion in the week of November 6 to \$3.0 billion in the week of December 4.

Recent inquiries substantiate reports that Euro-dollar deposits held by official institutions in oil-exporting countries tend to be of very short maturity. Three large U.S. banks report confidentially that dollar deposits of oil-exporting countries at their foreign branches are almost entirely of maturities of six months or less, and two banks said that a high proportion consisted of call deposits. There have been no significant shifts in the maturity composition of these deposits in recent months. These banks said they were paying 1/2 to 1 per cent below quoted rates for deposits of oil-exporting countries, because of the exceptionally large size of such deposits. (The size of the rate concession also varies with banks' expectations about future interest rate levels.)

In the past month, the cost to prime corporate borrowers of short-term Euro-dollar loans has risen slightly while the cost of bank credit in the United States declined by 1/2 to 5/8 per cent, as shown in the accompanying table. But relative costs of Euro-dollar financing and U.S.

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

Average for month or 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-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-Nov. 6	9.13	9.63	-0.50 (0.29)	10.00	8.88	1.12 (1.22)
13	9.41	9.37	0.04 (0.86)	9.89	8.75	1.14 (1.24)
20	9.19	9.34	-0.15 (0.65)	10.00	8.50	1.50 (1.63)
27	8.97	9.46	-0.49 (0.29)	10.29	9.06	1.23 (1.33)
Dec. 4	9.34	9.02	0.32 (1.13)	10.81	9.15	1.66 (2.02)
11 ^{p/}	8.14	8.89	-0.75 (-0.04)	10.21	9.15	1.06 (1.37)

*/ 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)

	Nov. 8	Nov. 29	Dec. 6	Dec. 11 ^{d/}
1) 3-mo. Euro-\$ loan ^{a/}	10.94	11.69	11.50	11.07
2) 90-119 day com'l. paper ^{b/}	9.13	9.25	9.25	9.00
3) U.S. bank loan:				
a) predominant prime rate	11.00	10.50	10.50	10.50
b) with 15% comp. bal's. ^{c/}	12.94	12.35	12.35	12.35
c) with 20% comp. bal's. ^{c/}	13.75	13.13	13.13	13.13
Differentials:				
(1) - (2)	1.81	2.44	2.25	2.07
(1) - (3a)	-0.06	1.19	1.00	-0.57
(1) - (3b)	-2.00	-0.66	-0.85	1.28
(1) - (3c)	-2.81	-1.44	-1.63	2.06

a/ 1-1/8 per cent over deposit bid rate.

b/ offer rate plus 1/8 per cent.

c/ prime rate adjusted for compensating balances.

d/ Wednesday

commercial paper borrowing have changed much less. The spreads over deposit rates which banks charge on their Euro-dollar loans to nonbank borrowers have risen further. Short-term (one year and under), fixed-interest rate loans to the highest quality borrowers now carry a minimum spread of 1 per cent over the London interbank offer rate (LIBO), normally equivalent to 1-1/8 per cent over the deposit bid rate. Spreads over LIBO are generally somewhat higher on medium-term loans.

Publicized medium-term Euro-currency credits completed in the third quarter came to \$4.6 billion compared with a quarterly average of \$9.6 billion in the first half, according to World Bank compilations. Credits completed by both developed and developing countries fell sharply in the third quarter. Preliminary data for October and November show some further decline in loan completions from the third-quarter level. The Bank said that the reasons for the reduced volume included decreased confidence in the banking system (making it difficult for smaller banks to raise funds), greater reluctance by banks to relend short-term deposits at longer term, and banks' increased concern over risk and exposure. Maturities of these credits have shortened markedly; the proportion with final maturities of seven years and over dropped from 94 per cent in the first half to 58 per cent in the third quarter.

U.S. balance of payments. During November, foreign official holdings at the Federal Reserve Bank of New York increased by \$1.5 billion, about the same rise as in October. In both November and October, most of the increase was in official holdings of oil-exporting countries. Data for the November change in official holdings at commercial banks are not yet available; however there was a decline of \$400 million in these holdings in October. U.S. reserve assets declined by \$90 million in November, compared to a \$30 million decline in October. The main element in the November reserve decline was the prepayment by Mexico of a swap with the Federal Reserve System (\$180 million) that more than offset increases in the U.S. reserve position in the IMF (\$60 million) and in foreign currency holdings (\$30 million). In October, decreases in foreign currency holdings (\$53 million) were partly offset by increases in the IMF position and in SDR holdings.

Bank-reported private capital transactions in October (the latest month for which there are data) showed a net inflow of about \$500 million (not at an annual rate), somewhat less than the monthly average inflow in the third quarter. The October net inflow can be attributed mainly to inflows from the Euro-currency market. Liabilities of U.S. banks to their foreign branches declined (by about \$1.8 billion), but this decline was more than offset by an increase in liabilities of banks in this country (including foreign bank branches and agencies) to other banks abroad (by about \$2.1 billion).

Bank-reported claims on foreigners were reduced only slightly in October compared with repayments in September exceeding \$1 billion. Earlier in the year, outflows of bank credit were large. At least part of the turn-around in the past two months occurred as foreign countries, such as Japan, obtained funds directly from oil-producing countries and were therefore able to begin to repay loans made earlier in the year in the United States. Another contributing factor may have been that during September-October, U.S. lending rates declined more slowly than Euro-dollar rates. The small net reduction in claims in October resulted from a reduction in lending by U.S. agencies and branches of foreign banks (about \$900 million) that was partly offset by increased lending by U.S. commercial banks (nearly \$800 million). Despite the October increase in bank lending, U.S. commercial banks indicate they are becoming increasingly selective in extending credits to foreigners.

In October, there was an outflow of capital through private securities transactions amounting to about \$300 million compared with an outflow of about \$200 million for the entire third quarter. U.S. purchases of Canadian new bond issues accounted for most of the outflow, but there were also U.S. purchases of stocks in the United Kingdom amounting to about \$75 million. Throughout 1974 there have been fairly steady U.S. purchases of stocks in the United Kingdom; for 10 months this totaled \$290 million, about half of which was purchased in the first quarter. Transactions in U.S. securities other than Treasury issues showed a

small net inflow as foreign purchases of bonds (mainly by international institutions) exceeded foreign sales of U.S. stocks (primarily through the United Kingdom, Switzerland, and Germany).

U.S. merchandise trade. In October, the U.S. trade deficit declined to \$2.4 billion at an annual rate (balance of payments basis) as exports rose almost \$5 billion and imports rose less than \$1 billion from their September rates. The \$3.9 billion change in the rate of the overall trade deficit between September and October reflected a similar change in the balance excluding agricultural exports and fuel imports.

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

	1973				1974				
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	Sept.	Oct.
EXPORTS	<u>60.9</u>	<u>66.7</u>	<u>72.6</u>	<u>80.9</u>	<u>89.2</u>	<u>96.4</u>	<u>98.5</u>	<u>98.0</u>	<u>102.7</u>
Agricultural	<u>14.7</u>	<u>16.5</u>	<u>19.0</u>	<u>21.2</u>	<u>23.6</u>	<u>22.8</u>	<u>20.5</u>	<u>19.5</u>	<u>19.9</u>
Nonagricultural	<u>46.2</u>	<u>50.2</u>	<u>53.6</u>	<u>59.7</u>	<u>65.6</u>	<u>73.5</u>	<u>78.1</u>	<u>78.5</u>	<u>82.8</u>
IMPORTS	<u>64.7</u>	<u>68.2</u>	<u>70.3</u>	<u>76.0</u>	<u>89.5</u>	<u>102.9</u>	<u>108.9</u>	<u>104.3</u>	<u>105.1</u>
Fuels	<u>6.7</u>	<u>7.8</u>	<u>9.0</u>	<u>11.6</u>	<u>20.4</u>	<u>28.2</u>	<u>29.9</u>	<u>27.6</u>	<u>28.0</u>
Nonfuels	<u>58.1</u>	<u>60.3</u>	<u>61.3</u>	<u>64.5</u>	<u>69.1</u>	<u>74.6</u>	<u>79.0</u>	<u>76.7</u>	<u>77.1</u>
TRADE BALANCE	<u>-3.8</u>	<u>-1.5</u>	<u>+2.3</u>	<u>+4.8</u>	<u>-0.3</u>	<u>-6.5</u>	<u>-10.3</u>	<u>-6.3</u>	<u>-2.4</u>
(excluding fuel imports and agricultural exports)	<u>(-11.9)</u>	<u>(-10.1)</u>	<u>(-7.7)</u>	<u>(-4.8)</u>	<u>(-3.5)</u>	<u>(-1.1)</u>	<u>(-0.9)</u>	<u>(+1.8)</u>	<u>(+5.7)</u>

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

October was the second consecutive month in which the trade deficit declined. While it is dangerous and inappropriate to read very much into the trade data for one or even two months, the data for the past two months suggest a possible leveling off of the trade deficit from the average increase of \$5 billion (annual rate) in the first three quarters of 1974.

The average value of total exports in September and October was only one percent above the value in the three previous months. The value of nonagricultural exports in September-October was up about 3.5 percent over the earlier period, but their volume was down 1.5 percent. The only major categories to show a substantial increase in the value of exports in September-October were machinery and civilian aircraft and parts. All other major categories of exports in this period were down in both value and volume from the previous three months. This general weakness is, of course, primarily due to the weakness in real demand abroad.

Exports of machinery were at an average seasonally adjusted annual rate of \$24.7 billion during September and October, 6 percent above the average rate in the previous three months. The value of new orders for machinery continued to increase in October, but in real terms they appear to have been on a slight downtrend since early summer. The value of exports of civilian aircraft and parts, always a volatile component in U.S. export statistics, increased in September and October to an average seasonally adjusted annual rate of over \$6 billion from their

depressed level in July and August and should remain high through mid-1975. Exports of automotive equipment to Canada increased to an average seasonally adjusted annual rate of \$6.5 billion in September and October. The strength of such exports is in part the reflection of sales of commercial vehicles in Canada in the first ten months of 1974 that were 28 percent above the rate in the same period in 1973. Exports of coal in October, prior to the strike by the miners of bituminous coal, were at an annual rate of \$4.3 billion, up 40 percent from September; all of the increase was in volume.

Agricultural exports in September and October were generally unchanged, down 10 percent from the previous three months. Volume was down by about 15 percent. The average price of agricultural exports in October was up about 9 percent from the low in June and July.

The value of total imports in October was less than one percent above the rate in September. The average for the two months was 4.5 percent below that for the period June through August, reflecting the recent weakness in U.S. aggregate demand and some downturn in fuel imports. In real terms, the September-October rate of imports was lower than in any pair of months since June-July 1972. The entire increase in non-fuel imports in October was accounted for by imports of iron and steel products which increased by 40 percent over the third quarter's rate presumably for inventory buildup in anticipation of the coal strike.

Petroleum imports in October averaged 6.4 million barrels per day (not seasonally adjusted), about the same as in September. The average price of oil imports in October was \$11.38 per barrel, down slightly from September. In September and October, the volume of imports of petroleum average 3 percent below the rate in the previous five months, and they averaged 2 percent lower in price. The small price declines were spread over all categories of oil imports.

Recent policy changes in foreign industrial countries. As new data become available, showing a marked weakness in demand and output, and as economic forecasts continue to be revised downward, the focus of policy in industrial countries has begun to shift noticeably. Governments and central banks in all countries continue to cite inflation as a problem demanding high priority, but, since the summer, the authorities in most countries have been acknowledging publicly that the outlook for sharply higher unemployment is a major concern of policy as well. Although some measures have been adopted to provide a stimulus to demand -- notably in Germany, Canada, the Netherlands, the United Kingdom, and Australia -- and some easing of policy seems likely in France and Japan early next year, policy actions have generally not yet caught up to the change in policy rhetoric. However, if activity is as weak next year as expected, further expansionary measures will undoubtedly be forthcoming.

The similarities in the internal situations in the various countries are striking, despite some important differences. Unemployment is rising sharply, yet price and wage inflation is continuing at high levels. Domestic demand is generally weak in all countries, with the automobile and construction industries exceptionally weak, and with activity in the steel, coal, capital goods, and basic chemical industries in some countries relatively strong. All industrial countries have relied on exports as a major stimulus to aggregate demand and are thus

concerned about the gloomy outlook for world trade in 1975. Financial markets are depressed. Of course, the extent of the weakness of demand, and the relative rates of wage and price inflation, differ considerably among countries.

The response of policy to these internal problems has been cautious, and special attention has been given to reducing the sectoral imbalances. In general, the policy response in the various countries has been influenced -- and is likely to continue to be influenced -- largely by their respective external situations. The consensus among all foreign countries -- as expressed, for example, in the recent meeting of the OECD's Economic Policy Committee -- is that countries with "strong" balance of payments positions have a responsibility to ensure that the level of demand in their countries is sufficiently high to avoid a world recession. The term "strong" in this context implies either an expected current account surplus or, at least, no expectation of serious financing problems; in other words, it implies the absence of a balance of payments constraint. The major "strong" countries are generally considered to be Germany and the United States, in particular, and, to a lesser extent, the Netherlands, Belgium, Austria, Norway, Canada, and Japan.

Recognizing that their domestic situation demands action, and also acknowledging their global responsibility, the German authorities have recently eased their restrictive posture. In late October the Bundesbank reduced both its discount and Lombard rates by 1/2 percentage point, and increased rediscount quotas, in a move

interpreted as a moderate but significant change in policy. On the fiscal side, the tax reform package going into effect in January 1975 will add over the year DM 13-15 billion (or about 1.5 per cent of GNP) to consumers' disposable income. The government has also announced DM 900 million in assistance primarily to the construction sector. Additional measures are scheduled to be announced on December 12.

In mid-November the Dutch authorities proposed a package of expansionary measures to moderate the upward trend of unemployment. Personal income taxes are to be reduced and social transfers are to be increased. Several measures to stimulate private investment, and to help the construction industry in particular, were also proposed.

A budget was presented in Canada on November 18. Concerned that the slowdown in other countries -- especially in the United States -- would have an increasingly severe adverse effect on the Canadian economy, Finance Minister Turner announced cuts in personal income taxes and other tax measures designed to encourage business capital expenditure and residential construction. At the same time, measures were proposed to reduce prices and costs directly (a reinstatement of tariff reductions and cuts in sales taxes).

The Japanese have basically maintained their restrictive policy stance, in view of the persistence of high rates of inflation. However, policy changes may be forthcoming after the wage bargaining round in April-May.

The "weak" countries, i.e., those that have present or prospective difficulties in financing their current account deficits, are not in a position to expand their domestic demand to ensure desired levels of output and employment. Most prominent among these countries is Italy. Italy's balance of payments problem has been so severe since the increase in oil prices, and its rate of inflation has been so high, that Italian stabilization policy has, by necessity, been restrictive. On December 2, Premier-designate Moro outlined his economic program -- essentially a continuation of the existing policy stance. He placed renewed emphasis on the urgent need to redress the balance of payments and to reduce the rate of inflation. Tight controls on credit will remain in force, but more guidance will be provided on its allocation. Domestic interest rates may come down, but will remain above foreign rates to discourage capital outflows. Public expenditures will be kept under tight rein.

Other "weak" countries include the Scandinavian countries, except for Norway, which can rely upon capital inflows associated with North Sea Oil to finance its current account deficit, and many of the smaller OECD countries, e.g., Ireland, Iceland, Spain, Portugal, Greece, Turkey, and New Zealand. With the exception of Denmark, these countries have generally maintained relatively easy demand management, and, as a result, have experienced relatively high rates of growth of output in 1974. But such growth cannot be maintained without running into serious external financing difficulties.

The international payments positions of France and the United Kingdom cannot easily be characterized as either "strong" or "weak". Both have large current account deficits, but so far they have been able to finance these deficits easily and no major financing problems are foreseen. The French authorities have chosen, up to now, to maintain credit ceilings and price controls, and to moderate growth of government expenditures. On December 6, the Assembly passed an anti-inflation tax, to be effective early next year, which will tax certain firms whose "value added" increases by more than the expected growth of nominal GDP of 14.3 per cent in 1975. However, the stance of policy may not be as restrictive as it first appears. The credit ceilings are not likely to be binding, since the demand for credit has been weakening and several types of credit are exempt from the ceilings, in any case. And given recent indications of sharply slower activity, and strong union opposition, it is reasonable to expect some easing of policy following a general economic review on December 19.

In Britain, although wage and price increases from 1974 to 1975 are both expected to be around 20 per cent, the authorities moved in mid-November to moderate the decline in private fixed investment, mainly by actions to improve the corporate sector's financial positions. In the absence of further measures, output is expected to remain virtually flat next year. With unemployment likely to be rising, more stimulus may well be proposed when the Budget is presented next March.

APPENDIX A: THE FULL-EMPLOYMENT SURPLUS: A REVISION OF THE TIME SERIES*

The staff has made a basic change in its choice of a price deflator for computing full-employment tax revenues. Up to now, the deflator which was used reflected not the current rate of inflation, but rather the inflation rate experienced four quarters in the past, adjusted downward toward a long-run "normal" rate. This deflator--sometimes referred to as the Okun deflator--was generally smaller than the actual deflator, and thus produced less full-employment revenue and a more stimulative portrayal of fiscal policy.

The justification for our previous use of the Okun deflator was that when the economy was operating near or above full employment, use of the actual price deflator would fail to record the inflationary impact of an increase in government spending, because the inflation induced increase in revenues would leave the full-employment surplus relatively unchanged. Given the current state of the economy, however, with expected increases in unemployment and a high, although decreasing, projected rate of inflation, use of the Okun deflator no longer seems appropriate. On the one hand, its implicit assumption of return to a long-run normal price path has depressed current full-employment receipts to about their actual levels; thus causing fiscal restraint to be understated. On the other hand, with respect to projections for 1975 and 1976, the lagged nature of the Okun deflator produces a larger increase in full-employment receipts than that indicated by the declining projected rate of inflation. Thus, for the forecasted period, the Okun method seems to overstate the degree of movement toward greater fiscal restraint. While under some assumptions one can defend continued use of the Okun deflator, its results are becoming difficult to interpret and thus can easily lead to confusion.

For these reasons, the decision has been made to abandon the Okun deflator and instead to use the actual or projected deflator for computing the full-employment surplus. The following table provides a historical series of the full-employment measure under the differing deflator assumptions. It should be noted that our new estimates use the same approach as other published series, but may still differ due to different assumptions regarding the path of expenditures, full-employment income shares, and tax rates. Our estimates as well as those provided by other analysts assume a constant 4 per cent growth rate for the potential path of real GNP which presumably would yield an unemployment rate of around 4 per cent over the long run. 1/

1/ The 4 per cent growth in potential GNP reflects an assumed 1.8 per cent growth in the labor force, a .3 per cent decrease in annual hours worked, and a 2.5 per cent rise in output per man hour when the economy is operating at its potential.

* Prepared by Frank Russek, Economist, Government Finance Section, Division of Research and Statistics.

If one were to assume that a constantly higher unemployment rate of, say, 5 per cent represented full-employment, the level of capacity GNP would be smaller. However, the growth rate of capacity GNP would be affected very little, and hence, the changes in the full-employment surplus would not differ by much.

Full Employment Surplus
(billions of dollars)

<u>Calendar Year</u>	<u>Using GNP Deflator</u>	<u>Using Okun Deflator</u>
1964	3.4	3.6
1965	.1	.2
1966	-4.9	-6.1
1967	-12.5	-13.3
1968	-9.1	-11.1
1969	8.8	5.6
1970	6.2	2.8
1971	2.6	.6
1972	-3.5	-4.3
1973	1.9	-5.1
1974	10.4	-3.3
1975	25.7	16.2
1976 <u>1/</u>	36.3	31.2

1/ This estimate extends beyond the period considered in the current Greenbook projections.