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Confidential (FR) Class III FOMC

October 31, 1984

RECENT DEVELOPMENTS

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

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Final demand appears to have picked up again in September, as there were healthy gains in consumer spending, housing starts, and business equipment outlays. At the same time, much of the recent growth in spending has been met by reduced inventory investment and rising imports, thereby damping the stimulus to domestic production. The rise in payroll employment in September was much smaller than the average gains registered earlier in the year, and industrial production declined in September for the first time since the recovery began. On balance, wage and price inflation has maintained the relatively moderate pace observed earlier in the year.

Industrial Production

Industrial production dropped 0.6 percent in September, after edging up just 0.1 percent in August. About half of the September decrease was due to reduced motor vehicle production, which had been affected by the one-week strike at General Motors as well as by continuing production problems related to the availability of quality parts. Declines also occurred in the output of other consumer goods, metals, construction supplies, and materials for a second consecutive month. Business equipment production continued to expand in September, although at a slower rate than during the preceding five months.

Limited information suggests that output in several sectors that had depressed industrial production in September, most importantly metals and motor vehicles, will be unchanged or slightly higher in October. The significant curtailment of steel output, under way since June, did not continue into late September and early October. In the auto sector, current

INDUSTRIAL PRODUCTION
(Percentage change from preceding period;
based on seasonally adjusted data)

	1984			1984		
	Q1	Q2	Q3	July	Aug.	Sept.
				---Monthly rate--		
Total	11.5	8.6	6.5	.9	.1	-.6
Final products	11.9	8.9	9.6	1.3	.2	-.4
Consumer goods	7.4	6.0	2.2	.6	-.5	-1.0
Durable	16.0	-1.4	-1.5	.1	-.7	-2.2
Nondurable	4.1	9.1	3.8	.9	-.4	-.6
Business equipment	19.1	13.4	25.0	2.3	1.5	.3
Defense and space equipment	17.4	12.8	10.7	1.8	.4	1.0
Construction supplies	14.8	7.6	2.9	.3	-.1	-.4
Materials	12.3	8.6	2.6	.4	.2	-1.1
Durable goods	20.6	11.7	4.3	.7	.4	-1.8
Nondurable goods	.5	6.3	.2	.1	-.1	-.3
Energy materials	10.9	3.7	2.2	.2	-.2	-.5

CAPACITY UTILIZATION IN INDUSTRY
(Percent of capacity, seasonally adjusted)

	1978-80	1982	1967-82	1984		
	High	Low	Avg.	July	Aug.	Sept.
Total industry	87.3	69.6	82.4	82.7	82.6	81.9
Manufacturing	87.5	68.8	81.8	82.9	82.8	82.1
Durable	89.4	64.8	80.5	82.6	82.9	82.0
Nondurable	87.2	73.8	83.9	83.1	82.8	82.3
Mining	90.4	69.6	86.5	78.1	77.5	77.4
Utilities[1]	86.8	79.0	88.6	84.1	84.1	83.6
Industrial materials	88.9	66.6	83.3	83.1	83.1	82.0
Metal materials	95.4	46.2	82.2	70.8	70.4	67.6
Paper materials	97.9	86.3	93.4	101.1	98.7	n.a.
Chemical materials	91.3	64.0	85.1	78.4	78.4	n.a.

1. The 1978-80 high is below the 1967-82 average because of the unusually slow growth in demand for electricity.

estimates indicate production was 7.0 million units at an annual rate in October, marginally higher than the 6.9 million unit rate posted in September. With the ending of the strike at GM factories in Canada, auto assemblies currently are scheduled to rise to about an 8 million unit annual rate in November and December.

Employment and Unemployment

The growth in labor demand slowed considerably in the third quarter, with monthly advances in nonfarm payroll employment averaging about half the pace observed in the first half of this year. In line with the smaller gains in employment, the civilian unemployment rate in the third quarter remained close to its second-quarter average of 7.5 percent. However, initial claims for unemployment insurance benefits edged up during the first two weeks of October, an indication that layoffs may have picked up in some sectors.

Employment, as measured by the payroll survey, rose just 65,000 on a strike-adjusted basis in September, continuing the slowdown that began in July. In manufacturing, employment fell 125,000, with declines particularly notable in the metals, machinery, and apparel industries--sectors in which new orders had weakened during the summer months. Outside of manufacturing, employment growth in the services industry, which had been quite strong earlier in the recovery, slowed in September after accounting for the return to work of 50,000 striking hospital workers; in contrast, strong employment gains were reported at trade establishments and by local governments.

In the household survey, employment rose 270,000 in September after declining in the two preceding months. As in many recent months, the household

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

	1983	1984 Q1	Q2	Q3	July	Aug.	Sept.
		-Average monthly changes-					
Nonfarm payroll employment[2]	282	344	359	179	215	182	139
Strike adjusted	282	339	366	171	204	244	66
Manufacturing	92	108	54	-9	67	29	-124
Durable	70	82	46	9	50	52	-74
Nondurable	22	25	8	-19	17	-23	-50
Construction	22	22	64	9	13	-12	27
Trade	69	86	87	70	64	45	100
Finance and services	96	105	122	51	20	51	83
Total government	3	1	7	46	34	38	67
Private nonfarm production workers	249	259	307	91	131	111	30
Manufacturing production workers	84	81	35	-12	49	20	-106
Total employment[3]	330	400	536	-170	-353	-426	270
Nonagricultural	336	425	495	-140	-294	-306	179

1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments. Strike-adjusted data noted.
3. Survey of households.

SELECTED UNEMPLOYMENT RATES
(Percent; based on seasonally adjusted data)

	1983	1984 Q1	Q2	Q3	July	Aug.	Sept.
Civilian, 16 years and older	9.6	7.9	7.5	7.5	7.5	7.5	7.4
Teenagers	22.4	19.6	18.7	18.7	18.3	18.4	19.3
20-24 years old	14.4	11.9	11.5	11.5	11.3	11.9	11.4
Men, 25 years and older	7.8	6.1	5.7	5.6	5.7	5.5	5.5
Women, 25 years and older	7.2	6.1	5.9	6.1	6.1	6.3	5.9
White	8.4	6.8	6.4	6.4	6.4	6.4	6.4
Black	19.5	16.5	15.9	16.0	16.9	16.0	15.1
Fulltime workers	9.5	7.6	7.2	7.2	7.2	7.2	7.1
Memo:							
Total national[1]	9.5	7.8	7.4	7.4	7.4	7.4	7.3

1. Includes resident Armed Forces as employed.

survey reported that large changes in employment and the labor force occurred again among youth, but such changes may be reflecting seasonal adjustment problems. Jobless rates for most demographic groups have changed very little, on balance, since May.

Personal Income and Consumption

Personal income rose at a $26.1 billion annual rate in September, a pickup from the two preceding months. Higher interest and dividend receipts contributed substantially to income growth last month, adding almost $8 billion to the September advance. Wage and salary disbursements, boosted by continued gains outside of the manufacturing sector, rose $11.7 billion. Manufacturing payrolls declined in September, owing to reduced factory hiring as well as to the six-day strike at General Motors. For the third quarter as a whole, growth of real disposable income slowed to a 3.5 percent annual rate, compared with a 7-1/2 percent pace in the first half of the year.

Real consumer outlays rebounded in September, after two consecutive monthly declines. Expenditures at retail outlets retraced part of their earlier declines, while spending on consumer services continued to trend upward. The broadly-based increases in spending at the retail level included sharp gains among such largely discretionary items as apparel and general merchandise. Sales at gasoline stations rose in September, in part reflecting the turnaround in gasoline prices.

Sales of domestically-produced new automobiles have been influenced recently by a variety of supply factors. Problems with parts availability and auto strikes at General Motors plants, both in the U.S. and Canada, have limited production and exacerbated the existing tight inventory situation. As a result, domestic auto sales during the past several weeks

PERSONAL INCOME AND EXPENDITURES
(Based on seasonally adjusted data)

	1984 Q1	1984 Q2	1984 Q3	1984 July	1984 Aug.	1984 Sept.
	—Percent change from previous quarter[1]—			—Percent change from previous month—		
Total personal income						
Nominal	12.4	9.1	8.7	.7	.6	.9
Real[2]	8.3	6.7	4.1	.0	.1	.6[e]
Disposable personal income						
Nominal	12.7	8.6	8.1	.7	.6	.8
Real[2]	8.6	6.3	3.5	.0	.0	.6[e]
Personal consumption expenditures						
Nominal	8.6	10.2	4.6	.0	.0	1.4
Real[2]	4.6	7.9	.2	-.6	-.6	1.1[e]
	--Changes in billions of dollars from previous quarter--			--Changes in billions of dollars from previous month--		
Total expenditures	46.3	56.2	26.6	.8	-.9	33.5
Durables	11.1	9.8	-3.4	-6.7	-6.6	4.5
New autos	4.4	1.5	-2.0	-3.4	-2.5	1.0
Furniture & appliances	3.2	3.6	-1.5	-4.9	.6	1.6
Nondurables	18.3	17.0	5.0	-.5	-3.1	18.4
Food	8.8	8.2	7.3	9.5	-6.3	8.8
Apparel	3.6	6.1	-3.1	-7.5	-.1	4.6
Services	16.9	29.3	25.0	8.0	8.9	10.6
Total personal income	84.0	64.1	63.1	20.3	18.3	26.1
Disposable personal income	73.6	52.1	50.5	16.7	15.9	21.8
Addendum:						
Personal saving rate (percent)	6.1	5.7	6.3	6.1	6.7	6.2

1. Changes from previous quarter are at compound rates; monthly changes are not compound.
2. Personal income is deflated by the implicit deflator for personal consumption expenditures.
e. Staff estimate.

RETAIL SALES
(Percent change from previous period;
based on seasonally adjusted data)

	1984			1984		
	Q1	Q2	Q3	July	Aug.	Sept.
Total sales	3.5	2.9	-.7	-1.7	-.6	1.6
(Real)[1]	2.7	3.0	n.a.	-2.0	-.7	n.a.
Total, less automotive, gasoline and nonconsumer stores	3.0	2.5	.6	-1.0	.3	1.7
GAF[2]	3.2	3.9	-1.2	-3.8	.3	2.1
Durable	5.1	4.3	-2.7	-3.2	-2.1	.6
Automotive group	5.7	4.6	-4.5	-4.2	-4.3	1.3
Furniture & appliances	3.5	3.8	-1.0	-2.6	.3	-.4
Nondurable	2.7	2.1	.4	-.9	.2	2.1
Apparel	2.4	6.3	-2.6	-4.4	-1.9	5.2
Food	2.2	2.3	1.3	.8	-1.1	2.6
General merchandise[3]	3.4	3.0	-.7	-4.0	1.1	1.9
Gasoline stations	.3	1.4	-2.3	-2.4	1.2	2.8

1. BCD series 59. Data are available approximately three weeks following the retail sales release.
2. General merchandise, apparel, furniture and appliance stores.
3. General merchandise excludes mail-order nonstores.

AUTO SALES, PRODUCTION & INVENTORIES
(Millions of units; seasonally adjusted annual rates)

	1984		1984		
	Q2	Q3	Aug.	Sept.	Oct.
Total sales[1]	10.6	10.3	9.9	10.2	
Imports	2.4	2.4	2.4	2.3	
Domestic	8.2	7.9	7.6	7.8	7.3[2]
Small	3.7	3.7	3.4	3.8	
Intermediate & standard	4.5	4.3	4.1	4.1	
Domestic production[1]	7.7	7.5	7.7	6.9	
Small	3.8	3.6	3.7	3.5	
Intermediate & standard	3.9	3.9	4.0	3.5	
			.1	.6	
Domestic inventories	1.43	1.32	1.39	1.32	
Days' supply[3]	54	51	47	52	

1. Components may not add to totals due to rounding.
2. First 20 days.
3. Quarterly days' supply are based on end of quarter stocks and average sales for the quarter.

have sagged to about a 7-1/2 million unit annual rate, considerably below the 8.2 million unit pace seen in the first half of 1984. Sales of foreign cars held steady at a 2.4 million unit annual selling pace in the third quarter.

On the whole, the consumer surveys of the Michigan Survey Research Center and the Conference Board continued to point to a high level of consumer optimism. The Michigan index of consumer sentiment advanced in September to just below the recent peak of March 1984. The Conference Board measure, while lower than in the first half of 1984, remained at a relatively high level through October.

Business Fixed Investment

Real business fixed investment expanded another 8 percent at an annual rate in the third quarter--a rapid pace, but well below the extraordinary rate of expansion during the preceding year. Virtually all of the third-quarter gain was in equipment spending. In particular, outlays for machinery, including high-technology items as well as heavy industrial machinery, continued to expand rapidly. Shipments of nondefense capital goods by domestic producers, which were relatively weak in July and August, rebounded sharply in September. In addition, there was a substantial rise in imports of capital goods.

In the nonresidential construction sector, nominal expenditures fell in both June and July and showed only a small gain in August. Outlays for commercial and industrial construction were little changed, on balance, in July and August relative to the second quarter. In contrast, petroleum drilling and mining showed a small increase in the third quarter, after declining sharply over the first half of the year.

BUSINESS CAPITAL SPENDING INDICATORS
(Percentage change from preceding comparable period;
based on seasonally adjusted data)

	1984			1984		
	Q1	Q2	Q3	July	Aug.	Sept.
Producers' durable equipment						
Nondefense capital goods						
Shipments	1.1	5.6	2.3	-3.8	.7	5.4
Orders	5.2	4.9	-2.0	-1.4	-4.2	2.3
Unfilled orders	4.4	4.1	1.4	1.3	.3	-.3
Sales of heavy-weight trucks (thousands of units, A.R.)	232	269	261	293	265	226
Nonresidential structures						
Nonresidential construction	8.0	8.7	n.a.	-1.4	.3	n.a.
Commercial building	13.7	13.7	n.a.	-.9	1.8	n.a.
Industrial building	20.5	4.0	n.a.	-3.0	4.7	n.a.
Contracts for nonresidential building	-9.8	19.7	2.9	12.9	5.8	-17.8
Commercial contracts	-2.5	13.3	-.5	16.2	1.3	-14.1
Industrial contracts	.8	14.1	15.1	4.2	26.2	-19.8

Most forward-looking indicators point to continued growth in investment spending, although at much slower rates than observed earlier in the recovery. New orders for nondefense capital goods weakened in the summer months but rose about 2-1/2 percent in September, and the backlog of unfilled orders showed a small gain for the third quarter as a whole. Growth in the value of new contracts for nonresidential construction also slowed in the third quarter from the rapid pace posted over the previous year. The McGraw-Hill survey of plant and equipment spending plans for 1985 (confidential until November 9) reported that businesses expect to increase capital expenditures by nearly 10 percent in 1985, following the 14 percent gain projected for this year by the August Commerce Department survey.

Business Inventories

Business inventories rose rapidly in July and August, advancing at an average annual rate of $23-3/4 billion in real terms. The pace was somewhat faster than the second-quarter average of $19-3/4 billion, mainly because of a more rapid rise in wholesale inventories. With sales slackening in July and August, the overall inventory-to-sales ratio based on constant-dollar values edged up to 1.53, slightly higher than the average level during the first half of this year.

Manufacturers' inventories rose at an annual rate of $15-3/4 billion in August, roughly the same as the average pace since February. Although factory stocks are still low relative to sales by historical standards, recent production and employment data suggest that a number of industries, most notably metals, apparel, and machinery, have adjusted their production, apparently in an attempt to slow further inventory accumulation. Indeed,

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars at annual rates)

	1984 Q1	1984 Q2	1984 Q3	1984 July[r]	1984 Aug.[p]	1984 Sept.[p]
Book value basis						
Total	73.7	56.3	n.a.	54.4	55.1	n.a.
Manufacturing	27.8	40.4	30.8	30.5	42.1	19.9
Wholesale trade	13.6	10.1	n.a.	26.8	.4	n.a.
Retail trade	32.3	5.8	n.a.	-2.9	12.6	n.a.
Automotive	10.5	-4.3	n.a.	-9.3	5.5	n.a.
Ex. auto	21.8	10.1	n.a.	6.5	7.2	n.a.
Constant dollar basis						
Total	24.4	19.7	n.a.	25.4	22.2	n.a.
Manufacturing	9.1	13.8	n.a.	12.0	15.8	n.a.
Wholesale trade	3.9	4.1	n.a.	11.2	5.1	n.a.
Retail trade	11.4	1.7	n.a.	2.2	1.2	n.a.
Automotive	3.8	-3.0	n.a.	-2.1	-.1	n.a.
Ex. auto	7.7	4.7	n.a.	4.3	1.3	n.a.

r—revised estimates.
p—preliminary estimates.

INVENTORIES RELATIVE TO SALES[1]

	Cyclical Reference Points[2] 1981 Low	Cyclical Reference Points[2] 1982 High	1984 Q1	1984 Q2	1984 July[r]	1984 Aug.[p]	1984 Sept.[p]
Book value basis							
Total	1.39	1.53	1.33	1.33	1.34	1.35	n.a.
Manufacturing	1.60	1.77	1.44	1.47	1.47	1.48	1.50
Wholesale trade	1.06	1.28	1.11	1.09	1.11	1.13	n.a.
Retail trade	1.36	1.44	1.37	1.34	1.35	1.37	n.a.
Automotive	1.59	1.88	1.49	1.37	1.37	1.45	n.a.
Ex. auto	1.29	1.36	1.34	1.33	1.35	1.35	n.a.
Constant dollar basis							
Total	1.62	1.75	1.52	1.51	1.52	1.53	n.a.
Manufacturing	1.91	2.11	1.73	1.76	1.76	1.76	n.a.
Wholesale trade	1.34	1.52	1.33	1.30	1.32	1.35	n.a.
Retail trade	1.34	1.44	1.34	1.31	1.33	1.34	n.a.
Automotive	1.49	1.81	1.38	1.27	1.28	1.30	n.a.
Ex. auto	1.28	1.37	1.33	1.33	1.33	1.35	n.a.

1. Ratio of end-of-period inventories to average monthly sales for the period.
2. Highs and lows are specific to each series and are not necessarily coincident.
r--revised estimates.
p--preliminary estimates.

the book value of manufacturers' inventories rose at only a $19 billion annual rate in September, about half the pace recorded in August. By and large, recent inventory problems have been in industries that are particularly vulnerable to import competition and that have experienced some softening in orders in recent months; both are factors that may have contributed to a lowering of sales expectations for the near term.

In the trade sector, wholesale inventories grew rapidly over the summer; the increase was concentrated in stocks of motor vehicles, electrical goods, and hardware, and may consist of a sizable portion of imports. Retail inventories rose, on balance, only slightly in July and August. Stocks at general merchandise and apparel stores were quite high relative to sales through August, but strong gains in sales in September may have led to some improvement in their inventory positions. Auto dealers' stocks continued to be drawn down in September, owing to the disruptions to auto production.

Housing Markets

Housing activity rebounded somewhat last month, after weakening throughout the summer. Total housing starts in September rose 9 percent, after an August decline to the lowest rate since late 1982. The September advance was broadly based; single-family and multifamily starts increased by similar margins, and starts rose in all four regions of the country. In addition, sales of new homes rose sharply in September, more than reversing the downtrend of the previous two months.

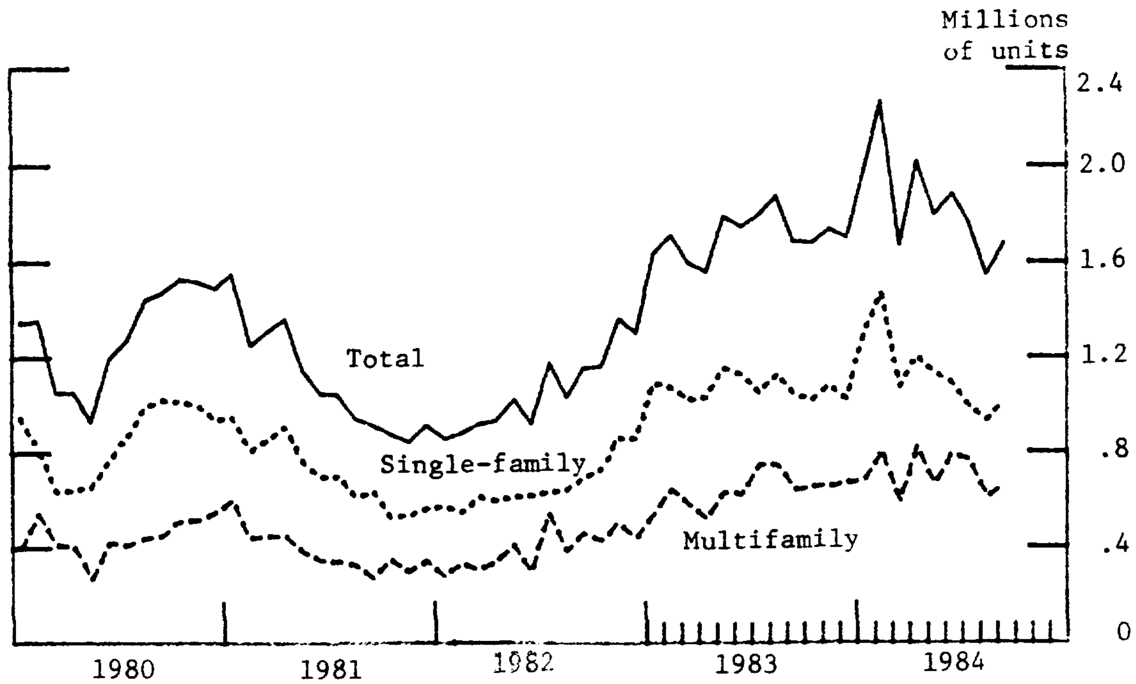
In contrast to the upturn in housing starts during September, newly issued residential building permits fell for the third consecutive month,

PRIVATE HOUSING ACTIVITY
(Seasonally adjusted annual rates, millions of units)

	1983	1984					
	Annual	Q1	Q2	Q3	July	Aug.	Sept.[1]
All units							
Permits	1.61	1.81	1.76	1.50	1.57	1.51	1.42
Starts	1.70	1.97	1.90	1.66	1.75	1.54	1.68
Single-family units							
Permits	.90	1.02	.93	.82	.82	.80	.83
Starts	1.07	1.28	1.14	.98	.99	.93	1.01
Sales							
New homes	.62	.69	.63	.62	.61	.56	.68
Existing homes	2.72	2.94	3.04	2.71	2.77	2.70	2.67
Multifamily units							
Permits	.70	.79	.83	.68	.74	.70	.59
Starts	.64	.69	.76	.68	.76	.61	.67
Mobile home shipments	.30	.30	.29	n.a.	.30	.30	n.a.

1. Preliminary estimates.
n.a.--not available.

PRIVATE HOUSING STARTS
(Seasonally adjusted annual rate)



as a sharp drop in multifamily permit issuance more than offset a moderate rise in single-family permits. However, the steep decline in the multifamily component of permits last month was due in part to a distortion in seasonal factors resulting from the phasing out of federal subsidies for construction of low-income housing under the Section 8 program. In previous years, this program had triggered a runup in permits at the end of the fiscal year.

Federal Government

The federal government recorded a deficit of $175 billion in fiscal year 1984, $20 billion less than in the preceding year. Receipts rose $66 billion in FY1984, owing to the sharp rise in income over the period, an end to the phase-in of income tax cuts that began in 1981, and the increase in social security tax rates last January. In addition to boosting receipts, the rise in economic activity cut the growth of outlays, particularly for unemployment insurance. A sharp reduction in agricultural support payments also helped limit the increase in outlays. However, defense expenditures and interest payments were up by substantial amounts.

During the final days of the 98th Congress, three important fiscal 1985 budget measures were enacted. First, agreement was reached on a budget resolution that projects a deficit of $181 billion for the current fiscal year and somewhat larger deficits in FY1986 and FY1987. Second, a continuing resolution was enacted; it provides interim FY1985 funding for agencies operating without appropriations, as only four of the thirteen required appropriations bills had been passed. The interim funding levels are roughly consistent with the budget resolution. Finally, the debt ceiling was raised to $1.823 trillion. Based on the figures in the budget

FEDERAL GOVERNMENT RECEIPTS AND OUTLAYS
(Unified budget, billions of dollars)

	Fiscal year 1983	Fiscal year 1984	FY1984 less FY1983
Receipts	600.6	666.5	65.9
Individual income	288.9	296.0	7.1
Corporate income	37.0	56.9	19.9
Social insurance	209.0	241.9	32.9
Other receipts[1]	65.6	71.7	6.1
Outlays	795.8	841.8	46.0
National defense	210.5	227.4	16.9
Human resources	411.8	415.1	3.3
Unemployment insurance	32.7	26.1	-6.6
Net interest	86.9	111.0	24.1
Other outlays[2]	86.6	88.3	1.7
Deficit	195.2	175.3	-19.9

1. Includes excise taxes, custom duties, estate and gift taxes, FR earnings and miscellaneous receipts.
2. Includes spending on energy, agriculture, transportation, and community and regional development.

resolution, the higher debt limit is expected to be sufficient for financing needs through the end of fiscal 1985.

State and Local Government

Activity in the state and local sector continued to expand in the third quarter as real outlays for goods and services increased substantially for the third consecutive quarter. As was the case earlier in the year, a large advance was reported for real construction expenditures, most likely reflecting ongoing public works programs, particularly for highways and roads. Employment in the state and local sector expanded rapidly in September for a third consecutive month.

Over the past year and a half, the fiscal position of the state and local sector, as a whole, has strengthened remarkably, and large surpluses in the operating and capital accounts have been reported for the first time since early 1981. However, with economic activity slowing, surpluses probably dropped in the third quarter. Furthermore, referenda will appear on many state ballots in November that would either reduce state taxes or limit governmental spending. In contrast, several states operating with relatively weak fiscal positions have taken action to raise taxes. In fiscal year 1984, tax reductions were more numerous than tax increases, but quantitatively the effect of increases outweighed the effect of reductions by an estimated $1 billion.

Exports and Imports

The merchandise trade deficit widened in September from the August level, but was less than the extraordinary July deficit; imports increased in September while exports were little changed. For the third quarter as a whole, the trade deficit was more than $30 billion (annual rate) larger than in either the first or second quarter.

The strong increase in imports in the third quarter occurred among a wide range of manufactured goods. The increase reflected, in part, the effects of the strong exchange value of the dollar on the relative prices of imported goods and the continued growth of income in the United States. The value of exports in the third quarter was slightly higher than in the second quarter. Some of the increase in exports was in intermediate products such as electronic parts and equipment to the Far East and automotive parts to Canada, a significant portion of which return to the United States after further processing.

As a result of the rising value of the dollar and moderate foreign inflation, prices of non-oil imports in July and August were little changed from their second-quarter levels. The price of imported petroleum drifted down during this period and in September. (Further discussion of international economic developments is included in Part IV.)

Prices

Consumer prices for goods and services continue to increase at a 4 to 5 percent annual pace; the consumer price index advanced 0.4 percent in September. The producer price index for finished goods fell 0.2 percent in September and has remained essentially constant over the past two quarters.

The decline in producer prices in September was the result of an 0.8 percent drop in energy prices, which are lagged one month in the PPI, and a 0.4 percent decrease in finished foods prices. Excluding food and energy, producer prices for both capital equipment and finished consumer goods were unchanged last month. Price stability also was evident, on balance, at the intermediate stage of processing; the prices for intermediate materials excluding food and energy were unchanged in September, bringing the increase in the third quarter to just 0.5 percent at an annual rate.

Consumer food prices declined 0.1 percent in September, after a 0.6 percent increase in August. Prices for fresh vegetables reversed some of their August climb, while the prices of fresh fruit rose sharply last month. Prices for beef and pork fell in September, and recent developments in commodity markets suggest that meat prices may continue to fall in coming months.

Retail energy prices advanced 0.6 percent in September, the largest monthly increase since April. A 1.1 percent jump in gasoline prices, which only partially retraced the summer declines, was primarily responsible for the increase. Nevertheless, spot prices for both crude oil and refined petroleum products have dropped recently, suggesting the September spurt in gasoline prices could be temporary. Electricity and natural gas prices rose slowly last month, after large increases in August.

Excluding food and energy, the consumer price index rose 0.4 percent in September, after a 0.5 percent increase the preceding month. Over the first nine months of 1984, this measure of inflation has been running at about a 5 percent annual rate, the same pace as observed last year. Prices for services increased 0.4 percent in September, while the prices of consumer commodities advanced 0.5 percent.

Wages and Labor Costs

Wage inflation remained relatively moderate through the third quarter. The comprehensive employment cost index for wage and salary rates rose at a 3-1/4 percent annual rate during the July to September period. Over the

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

	Relative Importance Dec. 1983	1982	1983	1984 Q1	1984 Q2	1984 Q3	1984 Aug.	1984 Sept.
				—Annual rate—			--Monthly rate-	
Finished goods	100.0	3.7	.6	5.7	.0	.0	-.1	-.2
Consumer foods	24.0	2.1	2.3	16.9	-8.5	3.3	-.1	-.4
Consumer energy	12.0	-.1	-9.2	-8.1	9.6	-18.3	-2.5	-.8
Other consumer goods	41.9	5.3	1.9	4.5	1.3	2.5	.4	.0
Capital equipment	22.2	3.9	1.9	3.8	2.8	2.5	.3	.0
Intermediate materials[2]	94.8	.3	1.4	2.9	3.4	-1.1	-.1	.0
Exc. energy	79.5	.6	3.0	3.8	1.9	.5	.1	.0
Crude food materials	52.8	1.5	8.0	12.5	-21.3	-5.4	-1.8	.0
Crude energy	31.3	2.6	-4.6	-1.6	4.2	.8	.7	-.8
Other crude materials	15.9	-7.6	15.5	-9.7	30.6	-13.3	-3.1	1.2

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

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

	Relative Importance Dec. 1983	1982	1983	1984 Q1	1984 Q2	1984 Q3	1984 Aug.	1984 Sept.
				-Annual rate-			-Monthly rate-	
All items[2]	100.0	3.9	3.8	5.0	3.3	4.5	.5	.4
Food	18.7	3.1	2.6	9.0	-.7	3.4	.6	-.1
Energy	11.9	1.3	-.5	-1.4	.8	1.7	.1	.6
All items less food and energy[3]	69.4	6.0	4.9	5.1	4.7	5.4	.5	.4
Commodities[3]	26.5	5.0	5.0	3.4	3.7	4.0	.4	.5
Services[3]	42.9	6.9	4.8	5.9	5.3	6.2	.5	.4
Memorandum:								
CPI-W[4]	100.0	3.9	3.3	2.3	2.7	7.5	.9	.5

1. Changes are from final month of preceding period to final month of period indicated.
2. Official index for all urban consumers, based on a rental equivalence measure for owner-occupied housing after December 1982.
3. Data not strictly comparable. Before 1983, they are based on unofficial series that exclude the major components of homeownership; beginning in 1983, data include a rental equivalence measure of homeowners costs.
4. Index for urban wage earners and clerical workers.

first three quarters of 1984, this wage measure has been running at a bit less than a 4 percent annual rate, about 1 percentage point less than the figure recorded in 1983. Much of the slowing this year has come from smaller wage adjustments for white-collar workers, who enjoyed fairly sizable real wage gains, on balance, during the previous two years.

Union settlements have generally been quite temperate this year. First-year wage adjustments under major collective bargaining agreements that were signed during the first nine months of 1984 averaged 2.5 percent exclusive of COLAs; this is nearly identical to the record low posted last year for this series, which dates back to 1968.[1] Pay cuts and wage freezes in new contracts have been less prevalent this year than during 1982 and 1983, but at the same time first-year guaranteed wage increases in excess of 8 percent have virtually disappeared. Wage adjustments for all union workers have averaged a bit less than those for nonunion workers for almost two years now, in marked contrast with the 1970s and early 1980s when union-nonunion wage differentials widened steadily.

For the private nonfarm sector as a whole, hourly compensation, which includes fringe benefits and employer payroll taxes in addition to wages, increased at a 3-3/4 percent annual rate in the third quarter. At the same time, productivity in the nonfarm business sector--which had shown strong cyclical gains earlier in the recovery--was unchanged last quarter. Productivity typically levels out or declines when output growth slows

1. The latest data do not include the recently ratified contracts at General Motors and Ford that call for an initial wage hike averaging 2-1/4 percent plus COLAs and profit-sharing.

SELECTED MEASURES OF LABOR COSTS IN THE NONFARM BUSINESS SECTOR
(Percentage change at annual rates; based on seasonally adjusted data)

	1981	1982	1983	1984 Q1	1984 Q2	1984 Q3	1984 to date
Hourly earnings index, wages of production workers[1]							1983-Q4 to 1984-Q3
Total private nonfarm	8.3	6.1	3.9	3.5	3.2	2.8	3.1
Manufacturing	8.8	6.0	2.7	3.8	3.0	3.3	3.4
Contract construction	8.3	5.4	1.5	2.3	1.9	-1.0	1.0
Transportation and public utilities	8.5	6.1	4.3	3.7	3.1	2.6	3.1
Trade	6.9	5.4	4.7	2.7	2.5	1.8	2.3
Services	9.1	7.0	4.9	3.3	4.9	4.2	4.1
Employment cost index, wages and salaries of all persons[2]							1983-Q4 to 1984-Q3
Total	8.8	6.3	5.0	4.2	4.1	3.2	3.8
By occupation:							
White collar	9.1	6.5	6.0	3.1	6.4	2.8	4.1
Blue collar	8.6	5.6	3.8	4.9	2.5	1.8	3.1
Service workers	8.3	8.5	4.6	5.2	1.8	8.2	5.0
By union status							
Union	9.6	6.5	4.6	6.1	3.2	1.1	3.4
Nonunion	8.5	6.1	5.2	3.2	4.8	3.9	3.9
Major collective bargaining agreements[3]							First nine months
First-year wage adjustments	9.8	3.8	2.6	--	--	--	2.5
Total effective wage change	9.5	6.8	4.0	--	--	--	4.0
Labor costs and productivity, all persons							1983-Q4 to 1984-Q3
Compensation per hour	8.8	7.2	3.9	6.1	3.7	3.7	4.5
Output per hour	.5	1.4	3.9	2.9	5.5	0.0	2.8
Unit labor costs	8.2	5.8	.0	3.1	-1.7	3.7	1.7

1. Changes are from final quarter of preceding period to final quarter of period indicated. Quarterly changes at compound rates.
2. Seasonally adjusted by the Board staff.
3. Agreements covering 1,000 or more workers; not seasonally adjusted.

sharply, as it did last quarter, and the latest data still appear consistent with a trend growth rate in output per hour of 1 to 1-1/2 percent annually. With productivity unchanged in the third quarter, unit labor costs advanced at a 3-3/4 percent annual rate, after rising at only a 3/4 percent annual pace in the first half of 1984.

SELECTED FINANCIAL MARKET QUOTATIONS[1]
(Percent)

	1983 Cyclical low	1984 Highs	1984 FOMC Aug. 21	1984 FOMC Oct. 2	1984 Oct. 30	Change fro 1984 Highs	Change fro FOMC Oct. 2
Short-term rates							
Federal funds[2]	8.42	11.63	11.63	10.60	9.84	-1.79	-.76
Treasury bills							
3-month	7.55	10.67	10.42	10.23	9.19	-1.48	-1.04
6-month	7.62	10.77	10.59	10.36	9.38	-1.39	-.98
1-year	7.73	11.13	10.68	10.39	9.49	-1.64	-.90
Commercial paper							
1-month	8.00	11.42	11.30	10.77	9.56	-1.86	-1.21
3-month	7.97	11.35	11.24	10.73	9.63	-1.72	-1.10
Large negotiable CDs[3]							
1-month	8.08	11.52	11.42	10.86	9.64	-1.88	-1.22
3-month	8.12	11.79	11.56	11.01	9.80	-1.99	-1.21
6-month	8.20	12.30	11.76	11.25	10.09	-2.21	-1.16
Eurodollar deposits[4]							
1-month	8.68	11.89	11.66	11.09	9.99	-1.90	-1.10
3-month	8.71	12.20	11.81	11.41	10.29	-1.91	-1.12
Bank prime rate	10.50	13.00	13.00	12.75	12.00	-1.00	-.75
Treasury bill futures							
Dec. 1984 contract	8.89	11.96	10.59	10.25	9.24	-2.72	-1.01
Dec. 1985 contract	10.86	13.20	11.56	11.43	10.69	-2.51	-.[illegible]
Intermediate- and long-term rates							
U.S. Treasury (constant maturity)							
3-year	9.33	13.49	12.44	12.29	11.37	-2.12	-.92
10-year	10.12	13.99	12.62	12.54	11.75	-2.24	-.79
30-year	10.27	13.94	12.35	12.35	11.61	-2.33	-.74
Municipal revenue (Bond Buyer index)	9.21	11.44	10.47[5]	10.65[5]	10.54[5]	-.90	-.11
Corporate--A utility Recently offered	11.64	15.30	14.10e	13.90e	13.12e	-2.18	-.78
Home mortgage rates							
S&L fixed-rate	12.55	14.68	14.39[6]	14.26[6]	14.05[6]	-.63	-.21
FNMA ARM, 1-yr.	10.49	13.70	13.25[6]	12.90[6]	12.20[6]	-1.50	-.70

	1982 Lows	1983 Highs	1984 FOMC Aug. 21	1984 FOMC Oct. 2	1984 Oct. 30	Percent change from: FOMC Aug. 21	Percent change from: FOMC Oct. 2
Stock prices							
Dow-Jones Industrial	776.92	1287.20	1239.73	1191.36	1217.31	-1.8	2.2
NYSE Composite	58.80	99.63	96.30	94.38	96.11	-.2	1.8
AMEX Composite	118.65	249.03	209.78	212.77	209.05	-.3	-1.7
NASDAQ (OTC)	159.14	328.91	253.33	246.10	247.45	-2.3	.5

1. One-day quotes except as noted.
2. Averages for two-week reserve maintenance period closest to date shown. Last observation is for maintenance period ended October 24.
3. Secondary market.
4. Averages for statement week closest to date shown.
5. One-day quotes for preceding Thurs
6. One-day quotes for preceding Frida
e--estimated.

Interest rates have declined substantially since the October FOMC meeting, extending the downtrend that began this summer. Most market rates are now 1-1/2 to 2-1/4 percentage points below their highs for the year. Continuing evidence of slower economic growth and subdued inflationary pressure helped to sustain the rally in October. In addition, the market was buoyed by an appreciable easing in the federal funds rate as discount window borrowing averaged below $1 billion and large banks evidently modified the cautious approach to reserve management that characterized the first months following Continental Illinois' funding crisis. The biggest yield declines have been registered by private short-term instruments, with commercial bank liabilities participating fully in the narrowing of risk premiums even as reports of increased loan loss provisions made the headlines.

Market optimism that Federal Reserve policy will remain on the less restrictive side has been based in part on continued sluggish monetary growth. Incoming data for M1 and M2 have pointed to renewed weakness in October after a brief reacceleration in September; both aggregates are in the lower halves of their annual target ranges. M3, meanwhile, appears to be holding near the upper bound of its 1984 range.

Private sector borrowing has slowed somewhat on balance since the summer, but has still been quite strong. A slackening of short-term borrowing by nonfinancial businesses has reflected primarily a marked shift toward long-term financing to take advantage of lower bond rates. Mortgage borrowing by households has diminished, and consumer debt growth apparently has been below the ebullient pace of the first half of the year. In the

MONETARY AGGREGATES
(Based on seasonally adjusted data unless otherwise noted)[1]

	1983 Q4	1984 Q1	1984 Q2	1984 Q3	1984 Aug.	1984 Sept.	Growth from Q4 1983 to Sept. 1984
	------- Percentage change at annual rates ------						
1. M1	4.8	7.2	6.1	4.6	1.5	5.9	5.9
2. M2	8.5	6.9	6.8	6.1	4.7	7.9	6.8
3. M3	9.8	8.9	10.2	8.0	4.6	7.7	9.0
							Levels in billions of dollars Sept. 1984
Selected components							
4. Currency	9.7	8.7	7.2	7.6	7.7	4.6	156.6
5. Demand deposits	-0.5	1.2	3.4	0.3	-7.8	4.9	246.5
6. Other checkable deposits	9.6	15.9	9.9	8.8	11.3	9.5	140.7
7. M2 minus M1[2]	9.7	6.8	7.1	6.6	5.6	8.5	1756.3
8. Overnight RPs and Eurodollars, NSA[3]	23.4	19.3	-8.2	-2.1	42.5	-32.8	56.9
9. General purpose and broker/dealer money market mutual fund shares, NSA	-1.2	9.8	15.5	10.6	0.0	11.2	151.9
10. Commercial banks	12.4	5.4	6.7	7.2	5.8	8.2	751.8
11. Savings deposits, SA, plus MMDAs, NSA[4]	5.9	6.5	4.9	-3.4	-7.8	2.6	369.7
12. Small time deposits	19.3	4.4	8.6	18.4	19.4	14.0	382.2
13. Thrift institutions	7.3	6.4	6.2	7.7	6.6	8.7	804.5
14. Savings deposits, SA, plus MMDAs, NSA[4]	-7.0	-0.9	2.6	-13.3	-23.2	-9.9	312.2
15. Small time deposits	18.8	11.8	8.9	22.6	27.1	20.6	492.2
16. M3 minus M2[5]	15.8	17.5	24.6	15.5	4.4	6.9	580.5
17. Large time deposits	15.7	24.8	31.5	25.9	8.3	3.7	393.0
18. At commercial banks, net[6]	-0.4	10.0	24.2	21.2	1.9	11.7	258.0
19. At thrift institutions	58.1	59.0	46.4	35.1	20.6	-12.3	134.9
20. Institution-only money market mutual fund shares, NSA	16.6	10.9	6.8	7.6	2.8	14.1	43.2
21. Term RPs, NSA	50.0	18.4	41.8	14.6	76.5	22.7	64.6
22. Term Eurodollars, NSA	-4.4	4.9	-0.4	-31.0	-31.9	-18.5	82.9
	-- Average monthly change in billions of dollars --						
MEMORANDA:							
23. Managed liabilities at commercial banks (24+25)	5.3	4.6	7.0	2.4	1.5	2.3	425.4
24. Large time deposits, gross	0.1	2.0	7.9	-0.1	-2.4	-0.7	312.6
25. Nondeposit funds	5.2	2.6	-0.9	2.5	3.7	3.2	112.8
26. Net due to related foreign institutions, NSA	3.2	1.9	0.9	-0.4	-1.6	0.8	-35.2
27. Other[7]	2.1	0.6	-1.8	2.9	5.3	2.4	148.0
28. U.S. government deposits at commercial banks[8]	-1.2	1.2	-1.3	1.2	1.0	3.8	16.5

1. Quarterly growth rates are computed on a quarterly average basis. Dollar amounts shown under memoranda for quarterly changes are calculated on an end-month-of-quarter basis.
2. Nontransactions M2 is seasonally adjusted as a whole.
3. Overnight and continuing contract RPs issued to the nonbank public by commercial banks plus overnight Eurodollar deposits issued by branches of U.S. banks to U.S. nonbank customers, both net of amounts held by money market mutual funds. Excludes retail RPs, which are in the small time deposit component.
4. Growth rates are for savings deposits, seasonally adjusted, plus money market deposit accounts (MMDAs), not seasonally adjusted. Commercial bank savings deposits excluding MMDAs declined during August and September at rates of 10.4 and 3.8 percent respectively. At thrift institutions, savings deposits excluding MMDAs decreased in August and September at rates of 12.3 and 2.1 percent respectively.
5. The non-M2 component of M3 is seasonally adjusted as a whole.
6. Net of large-denomination time deposits held by money market mutual funds and thrift institutions.
7. Consists of borrowings from other than commercial banks in the form of federal funds purchased, securities sold under agreements to repurchase and other liabilities for borrowed money (including borrowings from the Federal Reserve and unaffiliated foreign banks), loans sold to affiliates, loan RPs and other minor items. Data are partially estimated.
8. Consists of Treasury demand deposits at commercial banks and Treasury note balances.

public sector, borrowing by state and local governmental units continued strong in September and October. A surplus in the federal budget in September resulted in a somewhat lower volume of Treasury borrowing in that month, but heavy federal borrowing resumed in October.

Monetary Aggregates and Bank Credit

Following a moderate rebound to a 6 percent annual rate of growth in September, M1 weakened again in the first half of October, placing this aggregate well below the midpoint of its 4- to 8-percent target range. Runoffs of demand deposits resumed in early October after an interlude of moderate expansion in September; other checkable deposits also had been drawn down by mid-month. Currency expansion in October apparently moved only a bit above the sluggish pace registered during September.

M2 growth picked up in September to an 8 percent annual rate, but evidently slowed somewhat in October. Its nontransactions component accelerated to an 8-1/2 percent rate of growth in September and apparently remained close to that pace in October. Inflows to general purpose and broker/dealer money market mutual funds quickened in September and October as returns posted on the funds (which included effective capital gains) moved down more slowly than market interest rates.

The drop in market interest rates also enhanced the attractiveness of retail nontransactions instruments offered by depository institutions, on which rate adjustments have lagged market movements. Weekly data indicate that MMDAs increased in early October, likely heralding the first monthly increment in these accounts since April. Small time deposits, although slowing somewhat, nevertheless grew at a brisk 17-3/4 percent rate in September, and data for commercial banks suggest only a modest further slowing in the first half of October. In addition, outflows from savings deposits have abated since August.

M3 recovered from its sluggish August pace to grow at a 7-3/4 percent annual rate in September, and was at the top of its 1984 target range of 6 to 9 percent. Growth in the non-M2 component of M3 edged up only slightly in September to a 7 percent annual rate; however, available data suggest that this component accelerated sharply in October, despite apparently larger runoffs of term Eurodollars. Inflows to institution-only money market funds had picked up in September as market yields declined relative to returns recorded on these accounts, and even stronger inflows were recorded in October. Growth of large time deposits (net of MMMF holdings) may have strengthened again in October after subsiding further in September.

Growth of large time deposits in September had been restrained by a runoff in these deposits at thrift institutions. The contraction at thrifts reflected in large part the problems of Financial Corporation of America, whose S&L subsidiary had issued massive amounts of these deposits earlier, and in part some easing of demands for mortgage credit; thrifts evidently resumed net issuance of large time deposits in October. At commercial banks, a runoff of gross large time deposits in September and sizable issuance in early October were apparently in response to sharp swings in U.S. government deposits. Treasury deposits surged in September, reducing the need for managed liabilities, then were drawn down in October when debt-ceiling problems were not resolved until midmonth.

Bank credit expanded at a 7-1/4 percent annual rate during September, a little slower than in August. Banks substantially reduced their holdings of U.S. Treasury securities, principally in their investment accounts, and cut back some on their acquisition of other securities. Loan growth, in contrast, increased moderately in September--to a 9-1/4 percent rate--but was much slower than earlier in the year; incoming data indicate that loan expansion at large banks may have slackened in October. There are widespread reports that concerns about capital adequacy are leading large banks to pursue less aggressive lending and placement policies, with particular emphasis on limiting low margin assets. Business loan growth moderated in September, in part owing to an easing of merger-related lending. Consumer loan growth at banks slowed markedly, while real estate lending was little changed from the reduced pace of the previous two months. Security loans bounced back sharply from their August decline, apparently reflecting the demands of nonbank dealers for financing of their enlarged holdings of U.S. Treasury securities.

Business Finance

Business demands for bank loans and short-term market credit eased considerably in the third quarter as a whole, despite a widening of the gap between capital spending and internal sources of funds at nonfinancial corporations. In September, for the first time this year, growth in the total of nonfinancial commercial paper and business loans at domestic banking offices and foreign branches of U.S. banks dropped below a 10 percent annual rate; third-quarter growth was at about half the rate of the second quarter. Declines in corporate bond rates have encouraged businesses to shift to longer-term financing, both to support current business activity and to refinance short-term merger-related debt incurred earlier. Public bond offerings by nonfinancial firms were substantial both domestically and in the Eurodollar market during the third quarter.

COMMERCIAL BANK CREDIT AND SHORT- AND INTERMEDIATE-TERM BUSINESS CREDIT
(Percentage changes at annual rates, based on seasonally adjusted data)[1]

	1984[2] Q1	Q2	Q3	July	Aug.	Sept.[7]	Levels in bil. of dollars Sept.
	---------- Commercial Bank Credit ----------						
1. Total loans and securities at banks[3]	13.9	17.2	8.1	8.7	8.2	7.2	1688.8
2. Securities	4.4	-9.2	4.5	1.7	10.6	1.1	434.7
3. Treasury securities	-2.3	-11.1	4.4	7.3	13.1	-7.1	183.7
4. Other securities	9.5	-7.9	4.7	-2.4	9.2	7.2	251.0
5. Total loans[3]	17.5	13.1	9.3	11.0	7.4	9.3	1254.1
6. Business loans[3]	18.9	17.1	8.5	10.2	9.1	6.0	464.6
7. Security loans	-4.4	-38.5	19.7	9.8	-112.2	177.6	25.6
8. Real estate loans	14.5	14.5	11.3	11.4	11.6	11.5	369.6
9. Consumer loans	21.5	21.6	14.8	21.1	14.0	8.6	253.0
	---------- Short- and Intermediate-Term Business Credit ----------						
10. Business loans net of bankers acceptances	18.2	17.3	8.9	9.1	9.6	7.7	455.2
11. Commercial paper issued by nonfinancial firms[4]	22.8	67.1	43.8	55.4	39.2	32.3	64.9
12. Sum of lines 10 & 11	18.7	22.5	12.8	14.1	13.3	10.9	520.1
13. Line 12 plus loans at foreign branches[5]	18.4	22.6	12.5	13.4	14.3	9.4	540.1
14. Total bankers acceptances outstanding[6]	-22.2	45.4	-11.8	2.9	-11.8	-26.7	79.1
15. Line 13 plus total bankers acceptances outstanding	12.9	25.4	9.3	12.0	10.9	4.7	619.2
16. Finance company loans to business[6]	28.8	8.4	n.a.	10.6	14.[illegible]	n.a.	n.a.
17. Total short- and intermediate-term business credit (sum of lines 15 and 16)	15.1	22.9	n.a.	11.8	11.3	n.a.	n.a.

n.a.--not available.
1. Average of Wednesdays for domestically chartered banks and average of current and preceding ends of months for foreign-related institutions.
2. Growth rates beginning 1984 have been estimated after adjusting for major changes in reporting panels and definitions that caused breaks in series at the beginning of January. Data should be regarded as highly preliminary.
3. Loans include outstanding amounts of loans reported as sold outright to a bank's own foreign branches, unconsolidated nonbank affiliates of the bank, the bank's holding company (if not a bank), and unconsolidated nonbank subsidiaries of the holding company.
4. Average of Wednesdays.
5. Loans at foreign branches are loans made to U.S. firms by foreign branches of domestically chartered banks.
6. Based on average of current and preceding ends of month.
7. Beginning in September, growth rates for total loans and investments, total loans, business loans, and real estate loans have been adjusted to eliminate effects of loan reclassifications and of loan transfers from Continental Illinois National Bank to the FDIC.

The trend toward longer-term debt issues continued in October, even though commercial paper borrowing apparently picked up, too. The gross volume of bonds publicly offered in domestic markets by all types of businesses was $10 billion, well above the already strong monthly average for the third quarter. An additional $2.5 billion was offered abroad. Moreover, the average maturity of fixed-rate bonds issued by nonfinancial firms was much longer in October than in any other month this year, and the issuance of variable-rate and extendible notes moderated considerably during September and October from the preceding three months.

The volume of corporate bond issuance in the U.S. market in recent months has been buoyed by the sale of medium-term notes. Activity in this sector, which for years consisted almost exclusively of issues by auto finance companies, has gained momentum as smaller captive finance companies, other financial institutions, and even some industrial issuers have entered the market as an alternative to commercial paper issuance. Seventeen corporations have sold medium-term notes so far this year, compared with three in 1983. These notes are issued in a manner similar to commercial paper but at longer maturities. The notes are offered continuously on a best-efforts basis through dealers at maturities selected by the purchasers--from a minimum, usually, of nine months to a maximum of 3 to 10 years, with coupon rates varying with maturity. The volume of medium-term notes offered during the third quarter was about $2.7 billion, more than double the average issuance earlier in the year.

Stock prices have fluctuated since the last FOMC meeting, with most broader indexes ending up as much as 2 percent higher. An exception was the AMEX index, which declined 1-3/4 percent due mostly to the poor performance

GROSS OFFERINGS OF SECURITIES BY U.S. CORPORATIONS
(Monthly rates, not seasonally adjusted, billions of dollars)

		1984					
	1983	Q1	Q2	Q3p	Augp	Septp	Octp
Corporate securities - total[1]	8.91	8.36	6.85	10.77	12.79	11.40	14.80
Public offerings in U.S.	8.21	6.92	5.79	8.65	10.60	7.90	12.30
Stocks--total[2]	4.30	2.17	1.94	1.70	2.05	1.70	2.30
Nonfinancial	3.07	1.11	1.27	.90	1.00	1.00	1.30
Utility	.80	.22	.28	.15	.15	.20	.30
Industrial	2.27	.89	.99	.75	.80	.80	1.00
Financial	1.23	1.06	.67	.80	1.10	.70	1.00
Bonds--total[1]	3.91	4.75	3.85	6.95	8.55	6.20	10.00
By industry							
Nonfinancial	2.03	1.49	1.91	3.30	4.20	3.10	5.50
Utility	.95	.64	.46	.90	.95	.95	1.50
Industrial	1.08	.85	1.45	2.40	3.25	2.15	4.00
Financial	1.88	3.26	1.94	3.65	4.35	3.10	4.50
By quality[3]							
Aaa and Aa	1.13	.93	1.19	2.20	2.60	2.55	1.40
A and Baa	1.57	1.59	1.34	2.75	3.45	1.45	5.10
Less than Baa	.48	.61	.75	1.20	1.85	1.10	2.40
No rating (or unknown)	.37	.36	.15	.20	.30	.50	.30
Memo items:							
Equity based bonds[4]	.75	.28	.34	.55	.61	1.01	1.85
Mortgage-backed bonds	.38	1.26	.42	.59	.34	.61	.80
Floating rate or extendible notes	.46	.58	1.35	1.77	2.24	.91	.70
Bonds sold abroad - total	.70	1.44	1.06	2.12	2.19	3.50	2.50
Nonfinancial	.33	.86	.42	.88	.53	1.80	.60
Financial	.37	.58	.64	1.24	1.66	1.70	1.90

p--preliminary.
1. Securities issued in the private placement market are not included. Total reflects gross proceeds rather than par value of original discount bonds.
2. Includes equity issues associated with debt/equity swaps.
3. Bonds categorized according to Moody's bond ratings. Excludes mortgage-backed bonds.
4. Includes bonds convertible into equity and bonds with warrants attached where the warrants entitle the holder to purchase equity in the future.

of oil stocks. Market values of S&L stocks outperformed the broader indexes during this same period, as their earnings prospects improved with recent declines in interest rates. The estimated $2.3 billion volume of new stock issued during the month was about unchanged from the monthly average so far this year, and was sluggish compared with the monthly average of $4.3 billion for 1983.

Government Finance

Federal sector. The staff at present is projecting a combined (on- and off-budget) deficit of $71 billion for the current calendar quarter. The Treasury is expected to reduce its cash balance by about $14 billion during the quarter, and to borrow about $58 billion, net, from the public. Net bill financing could well total $20 billion, accounting for its largest share of marketable borrowing since the last quarter of 1982, when financing needs had reached a peak. Although gross issuance of bills is expected to rise just slightly, a reduced volume of maturing bills (which were issued under debt-ceiling constraints last spring) should result in an enlarged net volume.

During the intermeeting period, the Treasury operated under a restrictive statutory debt ceiling. The normal end-of-quarter auctions of 4- and 7-year notes and 20-year bonds, originally scheduled for late September, were postponed twice. Finally, on October 13 the ceiling was raised by $251 billion to $1,824 billion. The disruption forced the Treasury to insert the postponed auctions into an already heavy calendar; as a result, the Board staff estimates that the Treasury will sell more than $80 billion, gross, of coupon securities over the period from mid-October to the end of the year.

In conjunction with the domestic auction of 4-year notes, the Treasury

TREASURY AND AGENCY FINANCING[1]
(Total for period; billions of dollars)

	1984				
	Q3	Q4[f]	Aug.	Sept.	Oct.[f]
Treasury financing					
Combined surplus/deficit(-)	-37.9	-70.8	-34.7	14.9	-27.7
Means of financing deficit:					
Net cash borrowing from the public	53.8	57.7	25.5	4.1	19.6
Marketable borrowings/ repayments(-)	51.0	55.9	24.8	2.8	18.7
Bills	13.5	20.1	13.0	-3.6	2.3
Coupons	37.5	35.8	11.8	6.4	16.4
Nonmarketable	2.8	1.8	.7	1.3	.9
Decrease in the cash balance	-16.8	13.6	5.0	-19.1	7.4
Memo: Cash balance at end of period	30.4	16.8	11.3	30.4	23.0
Other[2]	.9	- .5	4.2	.1	.7
Federally sponsored credit agencies, net cash borrowing[3]	12.5	6.0	4.8	4.3	1.9
FHLB	11.3	3.0	4.2	4.0	.6
FNMA	.3	2.0	-.8	.2	.8
Farm Credit Banks	.1	--	.1	-.2	.1
FHLMC	.2	0.5	1.2	.2	.2
SLMA	.6	0.5	.1	.1	.2

f--staff forecast.
1. Data reported on a not seasonally adjusted, payment basis.
2. Includes checks issued less checks paid, accrued items and other transactions.
3. Excludes mortgage pass-through securities issued by FNMA and FHLMC.

has auctioned for the first time $1 billion of 4-year notes specially targeted to foreign buyers. Investment bankers submitted bids totaling four times the amount auctioned, and the average effective annual yield was nearly 35 basis points below that of the domestic issue; retail demand for the notes appears moderate, with the most recent quotes on the targeted issue maintaining about the initial yield spread relative to the companion domestic note.

Borrowing by the federally sponsored credit agencies slowed sharply in October, owing largely to a cutback by the Federal Home Loan Bank System. Its reduced borrowing needs reflected a lighter volume of advances to S&Ls generally, and the renewed ability of the Financial Corporation of America to raise some funds directly in the credit markets. Borrowing by the other sponsored agencies continued its moderate third-quarter pace into October.

The Federal National Mortgage Association recently announced an after-tax loss of $43 million for the third quarter. The loss was the result of a negative interest margin totaling $56 million and an addition of $35 million to the allowance for loan losses. The addition to the loan loss reserve followed upon an increase in FNMA's foreclosure rate during the first three quarters. Most of the loans foreclosed have been long-term, fixed-rate mortgages.

State and local sector. Gross offerings of long-term municipal securities have continued strong in recent weeks. Offerings in October are estimated at about $8.3 billion, seasonally adjusted, roughly equaling the third-quarter average. The October offerings included several large utility issues, as well as bonds earmarked for work on highways, schools, and medical facilities. In the short-term tax-exempt market, volume has fallen off as HUD recently ceased offering project notes amid confusion regarding arbitrage restrictions contained in the Deficit Reduction Act.

The volume of tax-exempt bonds for single-family housing is estimated to have totaled around $1.2 billion in October. The legislated state-by-state ceilings for 1984 imply a maximum volume of about $15 billion of such issues, should every state reach its limit. Thus far, more than $10 billion have been sold.

GROSS OFFERINGS OF SECURITIES BY STATE AND LOCAL GOVERNMENTS
(Monthly totals or monthly averages; billions of dollars)

	1983	1984 Q1	1984 Q2	1984 Q3[e]	1984 Sept.[e]	1984 Oct.[p]
	Seasonally adjusted					
Total	10.39	9.42	8.99	10.40	8.50	10.00
Long-term	7.20	5.84	5.75	8.40	6.60	8.30
Short-term[1]	3.19	3.58	3.24	2.00[2]	1.90[2]	1.70[2]
	Not seasonally adjusted					
Total	10.39	7.82	10.57	9.72	8.20	10.20
Long-term	7.20	5.04	6.38	7.62	6.20	8.50
Refundings	1.17	.80	.93	.79	.50	.90
Single-family housing[3]	.92	.12	.29	2.70	1.90	1.20
Short-term[1]	3.19	2.78	4.19	2.10[2]	2.00[2]	1.70[2]

e--estimate. p--preliminary.
1. These figures exclude tax-exempt commercial paper.
2. Excludes HUD cancellations.
3. Data from the Department of Housing and Urban Development.

Interest rates on municipal bonds rose during the first few weeks after the last FOMC meeting, but reversed direction in mid-October. The Bond Buyer revenue and general obligation bond indexes are both down about 10 basis points since the last FOMC meeting. At the same time, though, rates on taxable securities dropped appreciably more, and the ratio of tax-exempt to taxable yields thus has increased sharply further, reaching its highest level since June 1983.

Mortgage Markets

Interest rates in the primary mortgage market continued to decline during the intermeeting period. Average contract rates on new commitments for conventional fixed-rate mortgages at S&Ls had slipped 21 basis points to 14.05 percent by late October. The effective yield on commitments for FHA-insured loans at mortgage companies retreated about 45 basis points; in light of market developments, the ceiling rate on VA-guaranteed loans was cut 1/2 percentage point to 13 percent in late October.

On adjustable-rate home mortgages, the commitment rate on conventional 1-year ARMs at S&Ls has dipped about 10 basis points to 11.90 percent since the October FOMC meeting. The spread favoring 1-year ARMs over fixed-rate mortgages at S&Ls has narrowed about 60 basis points since June, when the Treasury yield curve was especially steep. Nevertheless, ARMs apparently have remained the dominant instrument in the conventional home loan market--in September, two-thirds of conventional loans closed at major originators carried adjustable-rate features.

In secondary markets, yields on fixed-rate instruments have fallen about 55 basis points since the previous FOMC meeting. For adjustable-rate loans, required yields posted by FNMA under its standard purchase program moved down 70 basis points on contracts that permit annual interest rate adjustments.

New mortgage commitments at federally insured S&Ls were down in September for the fourth consecutive month, leaving mortgage commitments outstanding about 5 percent below the June peak of $67 billion. With

MORTGAGE ACTIVITY AT FEDERALLY INSURED SAVINGS AND LOAN ASSOCIATIONS[1]
(Billions of dollars, seasonally adjusted)

	Mortgage commitments		Net change in mortgage assets		
	New	Outstanding[2]	Total	Mortgage loans	Mortgage-backed securities
	(1)	(2)	(3)	(4)	(5)
1983-Aug.	15.3	48.5	8.8	5.6	3.2
Sept.	15.8	49.8	8.0	5.5	2.5
Oct.	14.0	51.0	6.4	3.7	2.7
Nov.	15.2	53.8	6.5	5.6	1.0
Dec.	15.0	56.5	6.0	5.7	.3
1984-Jan.	17.2	58.0	5.8	4.9	.9
Feb.	18.1	60.4	6.1	6.0	.1
Mar.	17.0	62.8	10.0	5.9	4.1
Apr.	16.8	63.0	10.0	7.5	2.6
May	19.5	66.1	10.6	8.4	2.2
June	18.1	66.9	10.7	7.9	2.8
July	17.8	66.6	8.7	8.1	.6
Aug.	14.8	65.4	8.4	5.7	2.6
Sept. p	13.6	63.5	5.7	5.1	.6

p--preliminary.
1. Insured S&Ls account for approximately 98 percent of the assets of all operating S&Ls. Net changes in mortgage assets reflect adjustments to account for conversions of S&Ls to savings banks.
2. End of month. Includes loans in process.

NEW ISSUES OF FEDERALLY GUARANTEED MORTGAGE PASS-THROUGH SECURITIES
(Monthly averages, millions of dollars, n.s.a.)

Period	All issues	GNMAs	FHLMCs	FNMAs	Memo: FNMA and FHLMC swap issues
1983-Q1	7122	3841	1955	1326	2204
Q2	7368	4753	1392	1223	1880
Q3	7619	4835	1544	1240	2115
Q4	5733	3403	1673	657	1954
1984-Q1	4892	2745	886	1261	1745
Q2	4020	2343	1133	545	1492
Q3 p	5130	2206	1428	1496	2659
July	5438	2325	1580	1533	2576
Aug.	5799	2373	1564	1862	3317
Sept. p	4153	1921	1140	1092	2085

p--preliminary.

mortgage swap activity and mortgage acquisitions both subsiding, the net growth in S&L mortgage assets diminished to $5.7 billion--about half the record increase attained in June.

New issues of federally guaranteed mortgage pass-through securities declined in September from the 1984 high reached in the prior month.[1] FHLMC- and FNMA-underwritten pass-through issues, which had increased in July and August on the strength of vigorous swap activity, tapered off in September. Issuance of GNMA-guaranteed mortgage-backed securities fell further during the third quarter in response to the earlier rise in interest rates as well as to the unusually low FHA/VA share of home mortgage originations, attributable to stiff competition from conventional ARMs.

The rate of expansion in residential mortgage debt outstanding was apparently trimmed a percentage point or so in September from the nearly 11 percent rate of the previous three months. That rate, in turn, was about 1-1/2 points below the high reached in May.

Consumer Credit

Growth in consumer installment credit has moderated from the unusually rapid pace of the first half, although remaining strong relative to past economic recovery periods. Installment debt outstanding increased at a 16-1/2 percent annual rate in August, compared with nearly 20 percent in July and 24 percent during the second quarter. Preliminary data--based primarily on commercial banks and retail stores--suggest some further

1. Private sector pass-through securities have comprised a scant 2.5 percent share of total new issue volume. However, the Secondary Mortgage Market Enhancement Act, signed October 3, is designed to encourage an expansion of private issues of mortgage-backed securities. The Act exempts certain of these issues from state securities and investment laws, and permits limited forward trading.

CONSUMER INSTALLMENT CREDIT

	1983	1984 Q1	1984 Q2	1984 July	1984 Aug.	1984 Sept.
	----- Percent rate of growth, SAAR -----					
Change in outstandings--total	11.3	17.4	24.1	19.8	16.5	12.5p
By type:						
Automobile credit	8.7	14.8	23.8	26.3	13.4	n.a.
Revolving credit	15.5	25.1	31.2	8.9	18.1	n.a.
All other[1]	10.1	16.3	21.3	19.5	18.3	n.a.
	------- Billions of dollars, SAAR ------					
Change in outstandings--total	48.3	67.8	97.9	85.3	72.0	55.2p
By type:						
Automobile credit	13.6	20.9	35.0	41.1	21.3	n.a.
Revolving credit	12.9	19.0	25.0	7.7	15.8	n.a.
All other[1]	21.7	27.9	37.9	36.5	34.9	n.a.
By major holder:						
Commercial banks	23.4	41.5	55.7	38.3	31.6	15.7p
Finance companies	5.0	0	9.2	16.8	13.3	n.a.
All other	19.9	26.3	33.0	30.1	27.1	n.a.
	-------- Annual percentage rate --------					
Interest rates						
At commercial banks[2]						
New cars, 48 mos.	13.92	13.32	13.53	n.a.	14.08	n.a.
Personal, 24 mos.	16.50	16.16	16.35	n.a.	16.75	n.a.
Credit cards	18.78	18.73	18.71	n.a.	18.81	n.a.
At auto finance companies[3]						
New cars	12.58	14.11	14.15	14.68	15.01	15.16
Used cars	18.74	17.55	17.61	17.77	17.99	18.10

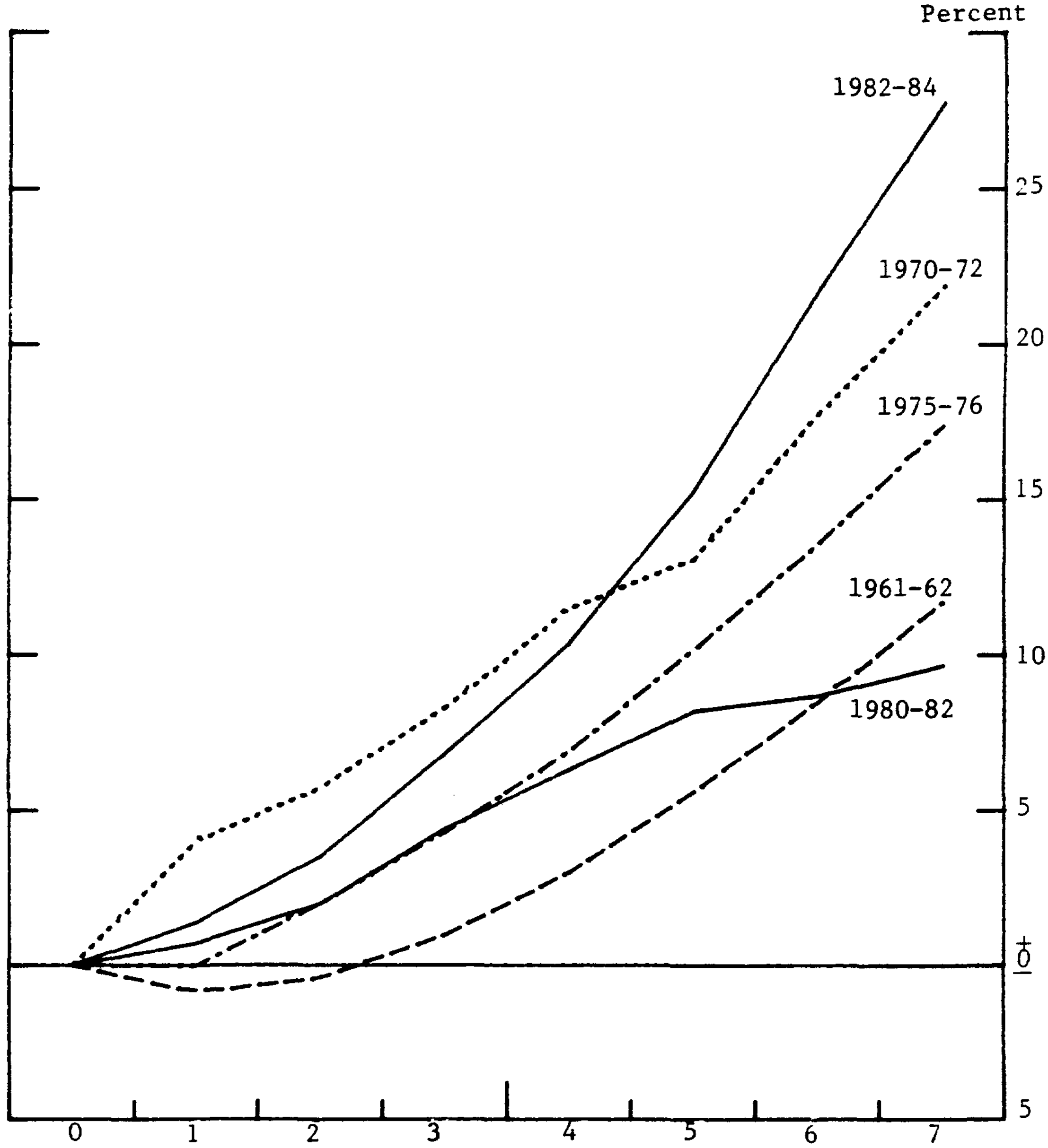
1. Includes primarily personal cash loans, home improvement loans, mobile home loans, and sales finance contracts for non-automotive consumer durable goods.
2. Average of "most common" rates charged, on loans of specified type and maturity, during the first week in the middle month of each quarter.
3. Average rate for all loans of each type made during the period, regardless of maturity.
n.a.--not available.
p--preliminary.

slackening of growth in September. During the 21 months of economic recovery from the trough in November 1982 through August 1984, the cumulative expansion in consumer credit totaled 28 percent, 6 percentage points more than in the most rapid of the four previous recoveries (see chart on page III-18), and nearly double the average for the four earlier periods.

The unusual strength in consumer credit during the current business advance likely reflects both stronger than normal increases in new lending and weaker than normal growth in repayments on outstanding loans. The robust pace of spending on consumer durables has generated a heavy volume of new borrowing. At the same time, the extended period of sluggish credit growth prior to the business recovery set the stage for a relatively light volume of repayments for several quarters into the recovery. More recently, however, with loan repayments becoming more reflective of credit extended during the recovery rather than before, repayments are no doubt accelerating, thereby imposing more of a drag on net credit expansion. Together, the slowdown in consumer spending during the third quarter and the probable swelling of repayments have begun to squeeze the growth rate of consumer debt after its explosive advance.

After modest increases between May and August, interest rates on consumer loans at banks apparently have been stable to slightly higher. According to an informal survey, a few banks have raised their offering rates by 50 basis points or less since the end of August, while others have made no change. Some banks noted that they expect to reduce rates in November; in cases where loans are made with adjustable rates tied to the prime rate, automatic reductions in offering rates will occur at the next adjustment period in response to the recent drop in the prime.

CONSUMER INSTALLMENT CREDIT
CUMULATIVE GROWTH FROM CYCLICAL TROUGHS



Number of Quarters Past Trough
in Business Cycle

At the automobile finance companies, new-car loan rates climbed another 15 basis points in September, and have now risen more than 100 basis points since early spring. (An increase of 100 basis points would add about $4 to the monthly payment on a typical auto loan.) The rise in rates at auto finance companies this year has restored the customary positive spread between finance company and bank auto loan interest rates, following a period in which the auto finance companies had supported the car market with cut-rate financing.

Foreign Exchange Markets

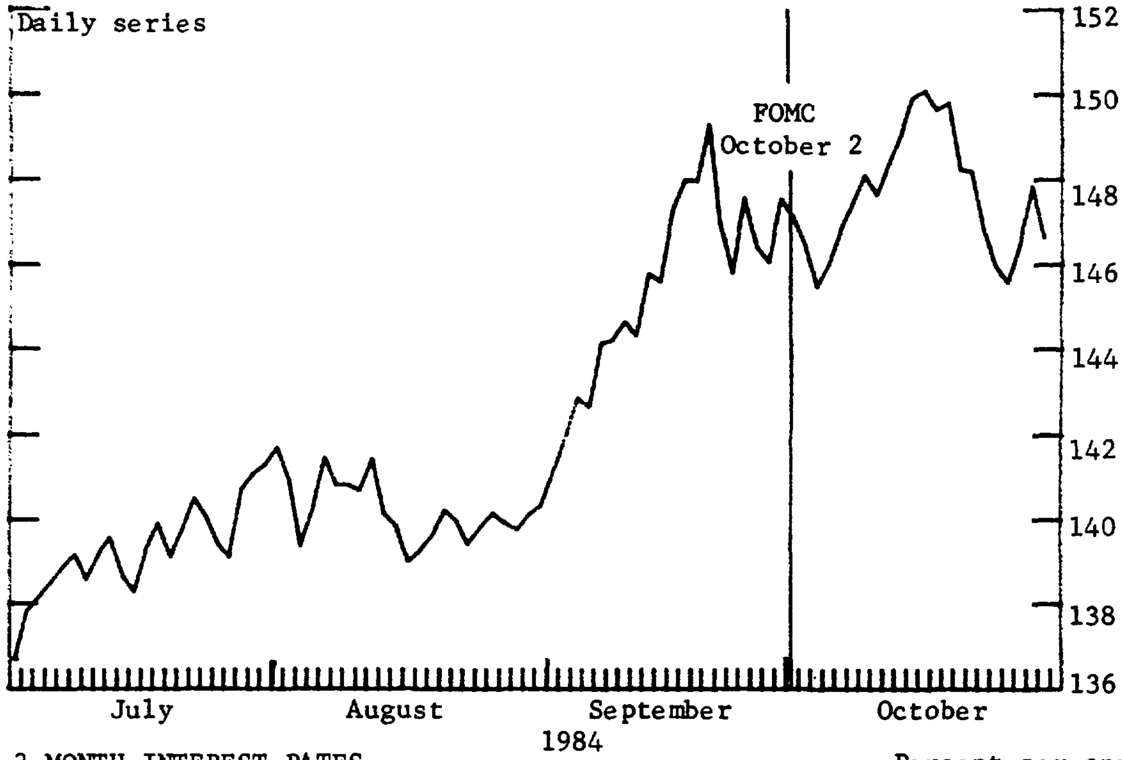
The trade-weighted average value of the dollar is little changed from its level at the time of the last FOMC meeting. The dollar has exhibited considerable movement in the intermeeting period, however, amid shifting opinion about the strength of U.S. economic activity, about the implications of weakness in oil prices for different currencies, and about Federal Reserve policy in the near term.

During the first half of the intermeeting period, the weighted-average dollar rose to a new record level even as U.S.-foreign interest-rate differentials continued to narrow (see chart). Market commentary suggests that demand for dollars may have been sustained by some further downward revision in expectations of U.S. inflation and by a belief that economic growth in the United States would continue to outpace growth elsewhere, particularly in Europe. Emerging weakness in world oil prices also appeared initially to generate support for the dollar, although the implications of oil price changes for the dollar are not unambiguous.

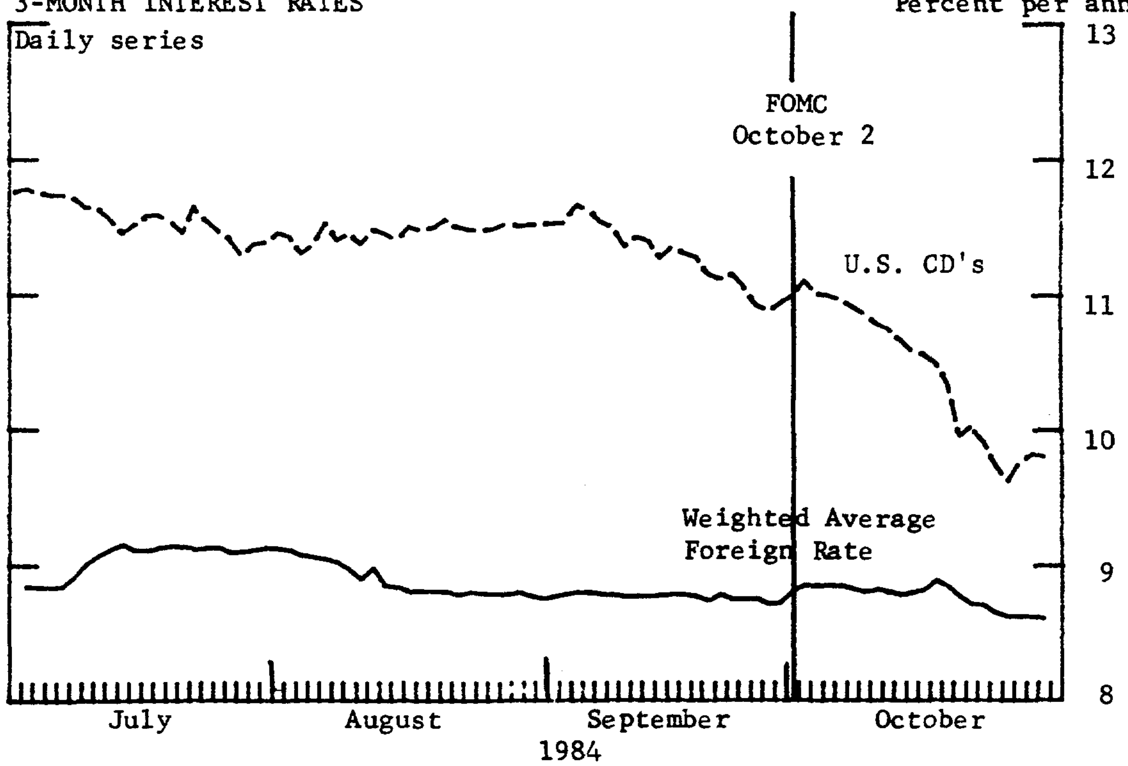
Since mid-October, however, the dollar has fallen 2-2/3 percent from its peak as U.S.-foreign short-term interest-rate differentials have declined sharply further. (Longer-term differentials, though also narrowing, showed much less change than short-term differentials.) Factors in the dollar's drop appear to have included a reassessment of the strength of U.S. economic activity, a backing away from initial

Chart 1 10/31/84

WEIGHTED AVERAGE EXCHANGE VALUE OF THE U.S. DOLLAR March 1973=100



3-MONTH INTEREST RATES Percent per annum



judgments of the likely magnitude and effects of oil price declines, and a market perception that the Federal Reserve might be easing reserve conditions more than had previously been thought. In addition, intervention by the Desk, may have provided some impetus to the dollar's decline.

While the dollar depreciated somewhat, on balance, against most major currencies, it changed little against the Canadian dollar and appreciated 1-3/4 percent against sterling. Canadian interest rates moved somewhat lower along with U.S. rates in the intermeeting period, and major banks in Canada reduced their prime rates from 13 to 12-1/2 percent late in the period. Sterling meanwhile was depressed by ongoing labor problems and by the prospect of a reduction in British oil revenues.

. The Bundesbank sold a moderate amount of dollars, concentrated in several actions visible to the market; perhaps because its sales were reminiscent of the very large sales of late September, they had a substantial, though temporary, effect on the mark/dollar rate.

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The Desk sold dollars against marks on October 17. The Desk's sales on that day totalled $95 million and were detected in the market. The Desk acted as the mark/dollar rate rebounded from the low reached after the Bundesbank's intervention.

U.S. International Financial Transactions

Data that were not available when the Commerce Department released second-quarter balance of payments figures in mid-September reveal that U.S. nonbank residents once again reported a sharp increase in their net financial liabilities to foreigners in that quarter. A large portion of this $5.5 billion net inflow appeared to be related to merger financing, just as it was in the first quarter. Based on these data, the estimated statistical discrepancy for the second quarter would be revised downward to $7.8 billion from the $13.3 billion previously reported. (See line 10 of the Summary of U.S. International Transactions.)

In August, recorded capital inflows exceeded the $9 billion merchandise trade deficit, although net inflows recorded over the two month span of July and August totalled only a little more than 50 percent of the trade deficit over the same period. Banks recorded a moderate net capital inflow in August, a significant portion of which appears to be associated with a reduction of bankers' acceptance claims on residents of Japan. Private foreign net purchases of U.S. Treasury obligations were quite large in August, totalling more than $6 billion (line 3). Nearly $2 billion of net purchases can be attributed to the World Bank, which actively manages its portfolio but is not expected to add much to its net holdings of U.S. Treasury securities over the rest of the year. About $3 billion of the remaining $4 billion of securities purchases is accounted for by net purchases by residents in the United Kingdom. A large part of this figure reflects a $1.7 billion purchase of 30 year Treasury bonds by a group of securities firms led by Salomon Brothers. The bonds, held in custody in the United Kingdom, were used to support the issue of CATS

SUMMARY OF U.S. INTERNATIONAL TRANSACTIONS
(Billions of dollars)

	1982	1983	1983	1984				
	Year	Year	Q4	Q1	Q2	June	July	Aug.
Private Capital								
Banks								
1. Change in net foreign positions of banking offices in the U.S. (+ = inflow)	-39.5	15.3	11.4	13.0	-2.6	-6.6	-3.0	4.0
a) with own foreign offices	-8.9	8.1	8.7	*	0.1	-1.2	-7.1	0.8
b) all other	-30.6	7.8	2.6	13.0	-2.7	-5.4	4.1	3.3
Securities								
2. Private securities transactions, net	-1.6	1.2	*	2.2	-0.2	0.6	0.2	0.4
a) foreign net purchases (+) of U.S. corporate bonds	2.8	2.2	0.7	0.3	0.5	0.5	0.4	0.9
b) foreign net purchases (+) of U.S. corporate stocks	3.6	6.4	0.4	1.2	*	-0.1	-0.5	0.1
c) U.S. net purchases (-) of foreign securities	-8.0	-7.4	-1.1	0.6	-0.8	0.2	0.3	-0.7
3. Foreign net purchases (+) of U.S. Treasury obligations 1/	6.5	8.3	1.7	1.4	6.6	1.5	2.4	6.1
Official Capital								
4. Changes in foreign official reserve assets in U.S. (+ = increase)	2.9	5.2	6.4	-3.0	-0.7	2.2	0.5	2.5
a) By area								
G-10 countries (incl. Switz.)	-12.7	6.4	1.7	2.3	-0.7	-1.3	-0.8	2.3
OPEC	6.9	-8.5	-1.5	-2.8	-2.4	0.5	1.6	-1.3
All other countries	8.8	7.3	6.1	-2.5	2.3	3.1	-0.3	1.6
b) By type								
U.S. Treasury securities	5.7	7.0	2.6	-0.2	-0.3	2.1	-1.8	2.6
Other 2/	-2.7	-1.8	3.8	-2.7	-0.5	0.1	2.3	-0.1
5. Changes in U.S. official reserve assets (+ = decrease)	-5.0	-1.2	-1.0	-0.7	-0.6	-0.1	-0.4	-0.3
Other transactions (Quarterly data)								
6. U.S. direct investment (-) abroad	4.8	-4.9	-1.6	-3.5	1.9	n.a.	n.a.	n.a.
7. Foreign direct investment (+) in U.S.	14.9	11.3	2.3	2.4	7.7	n.a	n.a.	n.a.
8. Other capital flows (+ = inflow) 3/ 4/	-6.7	-2.9	-0.3	1.9	-4.5e	n.a.	n.a.	n.a.
9. U.S. current account balance 4/	-9.2	-41.6	-17.2	-19.7	-24.4	n.a.	n.a.	n.a.
10. Statistical discrepancy 4/	32.9	9.3	-1.7	6.0	7.8e	n.a.	n.a.	n.a.
MEMO: U.S. merchandise trade balance -- part of line 9 (Balance of payments basis, seasonally adjusted)	-36.5	-61.1	-19.4	-25.9	-25.7	-7.5	-14.0	-9.0

1. Includes U.S. Treasury notes publicly issued to private foreign residents.
2. Includes deposits in banks, commercial paper, acceptances, & borrowing under repurchase agreements.
3. Includes U.S. government assets other than official reserves, transactions by nonbanking concerns, and other banking and official transactions not shown elsewhere.
4. Includes seasonal adjustment for quarterly data.
* Less than $50 million.
e/ Estimated.
NOTE: Details may not add to total because of rounding.

(Certificates of Accrual on Treasury Securities) that were marketed to non U.S. residents in bearer form through Salomon Brothers' U.K. affiliate.

It is widely believed that investors are especially attracted to securities issued in bearer form. The large August volume of CATS issued with Treasury obligations as backing tends to confirm this view, but may exaggerate it, because investors may have purchased these particular securities with unusual intensity in anticipation of imminent restrictions on such issues. In any event, bearer CATS are unlikely to figure prominently among U.S. Treasury obligations purchased by foreigners after August, because on September 7 the Treasury did issue regulations prohibiting further issuance of bearer instruments backed more than 50 percent by U.S. government securities. It remains to be seen if the Treasury issues targeted for foreigners, which seek to preserve some of the anonymity of investors, are given a vigorous reception.

Foreign private net purchases of U.S. corporate securities increased slightly in August. The increase in foreign net purchases of U.S. corporate bonds in part reflects the increased issuance of bonds in the Euromarket by U.S. corporations through their domestic offices rather than through finance affiliates in the Netherlands Antilles after the repeal of withholding tax on interest paid to foreigners and the concomitant legal changes. Prior to the repeal, finance affiliates in the Netherlands Antilles were active in acquiring funds for U.S. corporations, and these funds were recorded in the balance of payments statistics as direct investment inflows when transferred to domestic offices. By contrast, Eurobonds issued directly from the domestic office of a U.S. corporation are recorded as private foreign purchases of U.S. securities. Evidence for September shows that U.S. corporations are electing to offer an even greater proportion of their Eurobond issues through their domestic offices.

Data on foreign official capital flows for August show a moderate increase in G-10 dollar holdings in the United States. On the whole, OPEC members decreased their dollar holdings in August, approximately counterbalancing their buildup of dollar holdings in July. Other countries collectively increased their holdings very little in August

. Partial information for September shows that official holdings at the New York Federal Reserve Bank declined moderately,

.

INTERNATIONAL BANKING DATA
(Billions of dollars)

	1981	1982	1983				1984				
	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June	July	August	Sept. 3/
1. Net Claims of U.S. Banking Offices (excluding IBFs) on Own Foreign Offices	7.8	32.9	49.2	43.6	44.1	39.3	35.3	32.2	27.6	30.3	30.1
2. Net Claims of U.S. Banking Offices on Own IBFs 1/	11.8	16.2	14.6	12.8	10.5	5.2	4.1	4.4	8.1	6.8	6.3
3. Sum of lines 1 and 2 of which:	19.6	49.1	63.8	56.4	54.6	44.5	39.4	36.6	35.7	37.1	36.4
(a) U.S.-chartered banks	22.3	40.0	53.7	49.9	48.7	40.8	36.9	34.7	33.7	35.6	35.7
(b) Foreign-chartered banks	-2.6	9.1	10.0	6.5	5.9	3.6	2.5	1.9	2.0	1.5	.8
4. Credit Extended to U.S. Nonbank Residents by Foreign Branches of U.S. Banks	13.2	15.8	16.9	17.3	17.3	18.7	18.5	19.9	19.7	20.6	20.2
5. Eurodollar Holdings of U.S. Nonbank Residents 2/	95.5	112.6	116.4	120.4	121.3	126.4	128.0	123.1	122.5	119.5	119.4

1. Corresponds to net claims of international banking facilities (IBFs) on all foreign residents, including all banks whether related or not, and all nonbanks.
2. Includes term and overnight Eurodollars held by money market mutual funds.
3. Through September 30.

Note: These data differ in coverage and timing from the overall banking data incorporated in the international transactions accounts. Line 1 is an estimate constructed as the residual of line 3 minus line 2. Line 2 is data for the last Wednesday of the month for the sample of monthly IBF reporters. Line 3 is an average of daily data reported to the Federal Reserve by U.S. banking offices. Line 4 is an average of daily data. Line 5 is the month-end value for data through September 1983. For dates after September 1983, the overnight portion is an average of daily data and the term portion is an average of Wednesday data.

U.S. Merchandise Trade

In September, the U.S. merchandise trade deficit was larger than in August but less than the record July level. For the third quarter as a whole, the trade deficit was more than $30 billion larger, at an annual rate, than in either the first or second quarters. Data for September and the third quarter are not yet available on an international transactions or GNP basis. Some preliminary assessments were made for this Greenbook; the data and further discussion will be included in the Greenbook supplement.

Imports in the third quarter increased sharply from the second-quarter level. Despite sharp month-to-month volatility, the rate of imports in all three months exceeded that recorded in the second quarter. The increase for the third quarter as a whole was spread

U.S. MERCHANDISE TRADE[1/]

	1983 Year	1984 8 mo.	1984 Q1	Q2	J/A	Aug.
Value (Bil. $, SAAR)						
Exports	200.3	218.3	215.7	218.4	221.4	220.7
Agricultural	36.6	38.8	41.2	37.1	35.9	35.0
Nonagricultural	163.6	179.8	174.5	181.3	185.6	185.7
Imports	261.3	329.9	319.2	321.3	359.0	328.4
Oil	53.8	58.1	55.4	59.6	60.0	56.8
Non-oil	207.5	271.8	263.8	261.7	299.0	271.6
Trade Balance	-61.1	-111.8	-103.5	-102.9	-137.6	-107.7
Volume (Bil 72$, SAAR)						
Exports						
Agricultural	16.3	15.8	17.0	15.1	15.0	14.9
Nonagricultural	57.3	62.4	60.6	62.7	64.6	64.7
Imports						
Oil	4.9	5.4	5.1	5.5	5.6	5.3
Non-oil	81.9	104.6	102.3	100.3	114.4	103.5

International transactions and GNP basis.

among a wide range of commodity categories, particularly industrial supplies and machinery. Among individual items, strong increases were recorded for steel, chemicals, electronic equipment and parts, clothing and textiles, and passenger car imports from Canada and Japan.

Oil imports declined slightly in the third quarter. The volume imported decreased steadily during the period; a rate of about 5.3 million barrels per day (mbd) in September brought the quarterly average to about 5.7 mbd. The price of imported oil dropped to about $27.30 per barrel in September and reflected weak spot prices during the summer; the average for the third quarter was about $27.80 per barrel. From the summer until early October spot prices strengthened as OPEC reduced its level of crude oil production. Recent cuts in prices by Norway, the United Kingdom and Nigeria reflect a weakness in the price of light crude oil relative to heavy crude oil.

OIL IMPORTS

	1983		1984			
	Year	Q4	Q1	Q2	J/A	Aug.
Volume (mbd, SA)	5.20	5.53	5.40	5.76	5.85	5.59
Price ($/BBL)	28.42	28.30	28.05	28.26	28.02	27.77
Value (Bil. $, SAAR)	53.80	57.14	55.41	59.61	59.98	56.78

The value of exports in the third quarter was slightly higher than in the second quarter. The increase was largely in manufactured goods (especially machinery and industrial supplies). The value of agricultural exports in the third quarter was maintained at the second-quarter rate because a sharp increase in wheat shipments (largely to the Soviet Union) offset declines in other commodities (particularly soybeans and corn).

Foreign Economic Developments. Economic expansion in major foreign industrial economies is continuing, except in the United Kingdom, where the coal miners' strike continues to depress industrial production. Although industrial production in Germany also declined somewhat in August, after a substantial post-strike recovery in July, other indicators suggest a continuing expansion. In Japan, industrial production has decelerated in the last year but in the third quarter was about 11 percent above its year-earlier level. Industrial production during the summer rose in Canada, France, and Italy, although the pace of the advance in each country was uneven. The most recent unemployment rate in each of the major foreign countries is above the level at the beginning of this year.

Inflation rates remained low or have continued to decline in the major foreign countries. In September, the year-on-year increase of the trade-weighted average of consumer price indices in the foreign G-10 countries was 4-1/4 percent, the lowest since the early 1970s and 1-1/2 percentage points below the rate of a year earlier.

The cumulative current account surplus for Japan through the third quarter was $31 billion (s.a.a.r.), an increase of $11 billion from the corresponding period of last year. The external position of the United Kingdom deteriorated further in the third quarter while the French trade balance continued to improve.

Individual Country Notes. Industrial production in Japan rose in the third quarter by 1.6 percent (s.a.), the slowest rate of advance since early 1983. This deceleration was widely expected and coincides with the government forecast of a slowing of activity from the rapid

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REAL GNP AND INDUSTRIAL PRODUCTION IN MAJOR INDUSTRIAL COUNTRIES
(PERCENTAGE CHANGE FROM PREVIOUS PERIOD, SEASONALLY ADJUSTED)

	Q4/Q4 1982	Q4/Q4 1983	1983 Q4	1984 Q1	1984 Q2	1984 Q3	1984 MAY	1984 JUNE	1984 JULY	1984 AUG.	1984 SEP.	LATEST 3 MONTHS FROM YEAR AGO+
CANADA												
GNP	-4.9	7.1	1.2	.7	.7	N.A.	*	*	*	*	*	4.6
IP	-10.8	16.1	3.7	.6	.9	N.A.	.7	.7	3.5	-.5	N.A.	9.7
FRANCE												
GDP	1.4	.6	.6	.9	-.4	N.A.	*	*	*	*	*	1.0
IP	-1.8	1.8	.0	1.3	-1.0	N.A.	3.1	-2.3	(4.6)		N.A.	2.3
GERMANY												
GNP	-1.6	2.9	1.3	1.5	-2.1	N.A.	*	*	*	*	*	.6
IP	-5.4	5.9	2.2	1.1	-5.0	N.A.	2.1	-9.6	14.1	-2.2	N.A.	-.3
ITALY												
GDP	-2.3	1.2	1.0	.8	.7	N.A.	*	*	*	*	*	3.7
IP	-6.7	1.7	.5	1.0	.5	N.A.	3.7	.8	-1.3	1.4	N.A.	4.3
JAPAN												
GNP	3.8	3.6	.8	1.9	1.6	N.A.	*	*	*	*	*	5.9
IP	-2.7	8.6	2.9	3.2	2.8	1.6	2.4	.5	.3	.7	-.7	10.9
UNITED KINGDOM												
GDP	1.6	4.1	1.4	.8	-.9	N.A.	*	*	*	*	*	2.6
IP	.1	4.8	1.3	.0	-2.6	N.A.	-1.1	.8	-1.1	-.2	N.A.	-1.1
UNITED STATES												
GNP	-1.5	6.3	1.5	2.4	1.7	.7	*	*	*	*	*	6.4
IP	-7.5	15.0	2.5	2.7	2.1	1.6	.4	1.0	.9	.1	-.6	9.2

* DATA NOT AVAILABLE ON A MONTHLY OR QUARTERLY BASIS.

+ IF QUARTERLY DATA, LATEST QUARTER FROM YEAR AGO.

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CONSUMER AND WHOLESALE PRICES IN MAJOR INDUSTRIAL COUNTRIES
(PERCENTAGE CHANGE FROM PREVIOUS PERIOD)

	Q4/Q4 1982	Q4/Q4 1983	1983 Q2	1983 Q3	1983 Q4	1984 Q1	1984 Q2	1984 Q3	1984 JULY	1984 AUG.	1984 SEP.	1984 OCT.	LATEST 3 MONTHS FROM YEAR AGO
CANADA													
CPI	9.7	4.6	1.4	1.6	.9	1.2	.9	.9	.6	.0	.1	N.A.	3.9
WPI	4.5	3.5	1.5	.9	.4	1.6	1.2	N.A.	.5	-.0	N.A.	N.A.	3.8
FRANCE													
CPI	9.5	9.8	2.8	2.1	1.9	1.7	1.8	1.7	.7	.5	.5	N.A.	7.3
WPI	8.5	14.6	4.0	3.7	3.6	3.4	2.9	N.A.	1.1	.2	N.A.	N.A.	13.2
GERMANY													
CPI	4.7	2.7	.5	1.0	.5	.9	.5	.0	-.2	-.2	.1	.6	1.8
WPI	3.1	.9	.8	.9	1.2	1.7	.8	N.A.	-.9	-1.4	N.A.	N.A.	3.3
ITALY													
CPI	16.6	12.8	2.9	2.3	3.5	2.9	2.1	1.2	.3	.3	.7	N.A.	10.1
WPI	12.4	9.1	1.6	2.3	3.3	3.2	2.2	N.A.	.1	.6	N.A.	N.A.	10.9
JAPAN													
CPI	2.9	1.9	.9	-.2	1.4	.9	.6	-.2	.3	-.8	1.6	.7	2.5
WPI	1.6	-3.3	-1.0	.2	-.6	.1	-.1	.8	.6	.0	.2	N.A.	.2
UNITED KINGDOM													
CPI	6.2	5.1	2.0	1.3	1.1	.6	2.3	.9	-.1	1.0	.2	N.A.	4.7
WPI	6.5	5.6	2.0	.8	1.3	1.8	2.4	.6	.2	.2	.5	N.A.	6.2
UNITED STATES													
CPI (SA)	4.4	3.2	1.1	1.0	1.1	1.2	.9	.9	.3	.5	.4	N.A.	4.2
WPI (SA)	3.6	.9	.2	.6	.4	1.1	.4	.2	.3	-.1	-.2	N.A.	2.0

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TRADE AND CURRENT ACCOUNT BALANCES OF MAJOR INDUSTRIAL COUNTRIES 1/
(BILLIONS OF U.S. DOLLARS; SEASONALLY ADJUSTED)

			1983			1984			1984			
	1982	1983	Q2	Q3	Q4	Q1	Q2	Q3	JUNE	JULY	AUG.	SEP.
CANADA												
TRADE	14.4	14.4	4.3	3.1	3.5	3.6	4.1	N.A.	1.5	1.6	1.1	N.A.
CURRENT ACCOUNT	2.1	1.4	1.1	-.2	.0	.0	.5	N.A.	*	*	*	*
FRANCE												
TRADE 2/	-14.0	-5.9	-1.7	-.6	-.2	-1.5	-1.1	.4	-.6	-.1	.4	.1
CURRENT ACCOUNT 2/	-12.1	-4.2	-.9	.3	.3	-.5	-1.0	N.A.	*	*	*	*
GERMANY												
TRADE	20.9	16.4	4.1	3.7	3.4	4.3	3.2	N.A.	.5	1.4	N.A.	N.A.
CURRENT ACCOUNT (NSA)	3.5	4.1	.6	-2.3	3.7	.7	-.2	-.6	-1.2	-.1	-.5	.0
ITALY												
TRADE	-12.8	-7.8	-1.4	-2.1	-1.3	-2.5	-3.0	N.A.	-1.1	-.1	-.9	N.A.
CURRENT ACCOUNT (NSA)	-5.7	.6	1.1	1.5	-.1	-1.7	N.A.	N.A.	*	*	*	*
JAPAN												
TRADE 2/	18.8	31.2	7.8	8.5	8.2	10.0	11.1	10.1	3.6	3.4	2.8	3.9
CURRENT ACCOUNT	6.9	21.0	6.1	5.7	5.5	7.2	9.2	7.4	3.1	2.5	1.8	3.0
UNITED KINGDOM												
TRADE	4.1	-.8	-.7	-.4	-.0	-.1	-1.7	-1.9	-.1	-.2	-.7	-1.0
CURRENT ACCOUNT 2/	9.6	4.4	-.1	1.2	.9	1.2	-.6	-.9	.2	.1	-.4	-.6
UNITED STATES												
TRADE	-36.5	-61.1	-14.9	-17.5	-19.4	-25.9	-25.7	-30.0	-7.5	-14.0	-9.0	-7.1
CURRENT ACCOUNT	-9.2	-41.6	-9.6	-11.8	-17.2	-19.7	-24.4	N.A.	*	*	*	*

1/ THE CURRENT ACCOUNT INCLUDES GOODS, SERVICES AND PRIVATE AND OFFICIAL TRANSFERS.
2/ QUARTERLY DATA ARE SUBJECT TO REVISION AND ARE NOT CONSISTENT WITH ANNUAL DATA.

* COMPARABLE MONTHLY OR QUARTERLY CURRENT ACCOUNT DATA ARE NOT PUBLISHED.

rate of the first half of this year. In August, new housing starts rose by 2.6 percent (s.a.), following a 4.4 percent gain in July, while new construction orders advanced significantly in both months. Retail sales rose by more than 5 percent (s.a.) in September following an over 3 percent drop in August. Abnormally hot summer weather is said to explain in part this pattern of sales. Labor market conditions improved somewhat during the summer: unemployment declined marginally from June's record level of 2.81 percent and overtime work picked up in August. The sizeable increases in consumer prices in September and October are believed to reflect mainly seasonal factors; year-on-year increases remain low.

Both the trade and current account surpluses rose in September. The cumulative trade surplus through September was $42 billion (s.a.a.r.), compared with a surplus for the same period of last year of $31 billion.

Negotiations within the government are continuing over the budget for FY 1985 (beginning April 1). Prime Minister Nakasone, who was re-elected to a second two-year term on October 31, remains committed to a reduction of the government deficit, while Finance Minister Takeshita has mentioned that proposals are being considered for a tax cut to stimulate domestic demand. A draft of the FY 1985 budget is expected in late December or early January. The Finance Ministry has also floated proposals aimed at reducing tax evasion associated with the establishment of multiple tax-free savings accounts. At present, an individual can legally exempt from taxation interest received on holdings of up to 3 million yen each (or a total of approximately

$37,000) in bank savings deposits, postal savings accounts, and government bonds. On October 29 the long-term prime rate was lowered from 7.9 percent to 7.6 percent in line with declines in government bond rates.

Industrial production in Germany has rebounded from the strike-induced losses incurred in June. The index for July-August was 3 percent above its pre-strike level in April-May. Compared with last year, July-August was up by 4.6 percent. Data on orders and business climate surveys point toward further expansion. The rate of unemployment, however, has remained high at 9.3 percent (s.a.) through September.

Consumer price inflation continues to be moderate: consumer prices in October were about 2 percent above the year-earlier level. Wages and salaries in July were 2.5 percent above July of last year. Negotiations continue between the government and Germany's largest union, the public service employees. The government recently made an offer of a 2.5 percent increase in compensation, while the union wants a 5 percent raise plus an increase in paid annual leave from 30 to 40 days.

The cumulative current account through September was in balance, compared with a $0.5 billion (a.r.) surplus for the same period of last year. Similarly, the trade surplus so far this year is less than $2 billion (a.r.) smaller than last year's comparable figure.

The government's plan for a large tax cut scheduled for 1986 (DM 10 billion) and 1988 (DM 10 billion) remains officially unchanged despite statements by the Economics Minister that the first cut should be advanced to 1985 in order to stimulate the economy.

Industrial production in the United Kingdom continued to decline in August and its three-month average fell to 1 percent below its year-earlier level. This weakness is in part the result of the ongoing coal miners' strike. To date the effect of this strike on other industries has been limited despite the substantial drop in coal output. About three-fourths of the miners have remained away from work. Negotiations to end the eight-month strike have made little progress; however, a strike by the pit supervisors, which would have halted virtually all coal production, has been avoided.

The U.K. unemployment rate rose 0.1 percent to 12.9 percent (s.a.) in September. Retail prices rose slightly in September but the year-over-year inflation rate fell to 4.7 percent.

The U.K.'s external position deteriorated sharply in the second and third quarters. The trade deficit was $7.5 billion (s.a.a.r.) in the third quarter, bringing the total deficit for the first nine months of 1984 to $4.9 billion (s.a.a.r.), from $1.1 billion for the comparable period in 1983. Although the U.K. oil account remains in substantial surplus, future growth of this surplus is expected to be tempered by the $1.35/barrel reduction in the price of British North Sea oil, announced on October 17 in response to Norwegian price cuts. The cumulative current account deficit for the first three quarters equalled $440 million (s.a.a.r.), compared with a $4.7 billion surplus for the comparable period in 1983. Fourth-quarter figures, however, are expected to benefit by the release from the European Community of the 1983 budget refund amounting to about $550 million.

On Monday, October 1, the Bank of England purchased Johnson Matthey Bankers (JMB), one of five members participating in the London fix, for £1 in order to prevent the possible widespread effects of its insolvency. The parent company (Johnson Matthey group) agreed to contribute £50 million in new capital to JMB prior to its sale and the leading U.K. financial institutions have supplied the Bank of England with sizable indemnities in case the losses on JMB's commercial loan portfolio exceed its (recently augmented) capital. To shore up the parent company, the largest shareholders agreed to invest a further £25 million in the Johnson Matthey group and a consortium of banks have provided the group with a £250 million line of credit.

Industrial production in France rose by 4.6 percent (s.a.) in the July-August period. However, this increase may reflect unusual seasonal production patterns over the summer holiday period. Other recent data continue to suggest weak economic activity. Real GDP data for the second quarter were revised downward slightly, showing a 0.4 percent (s.a.) decline in the quarter and a year-over-year increase of only 1 percent. The unemployment rate in September was unchanged at 10.1 percent (s.a.) following increases in nine of the previous ten months. Inflation has continued to moderate with the year-over-year consumer price inflation rate easing to 7.1 percent in September.

On October 29 the French government announced that its 1985 monetary target would be a growth rate of M2R in the range of 4 to 6 percent, down slightly from the 1984 target range of 5-1/2 to 6-1/2 percent. (M2R in June was 9.2 percent above its year-earlier level and was up by 6.7 percent (s.a.a.r.) compared with its base period centered in December 1983.) The government also announced that the current monetary control technique of placing ceilings on commercial bank credit expansion will be removed at the end of this year and replaced by a credit control system relying on commercial banks holding required reserves at the Bank of France. Details of the new system remain to be worked out.

There was a small trade surplus in September. For the first nine months of this year, the cumulative trade deficit was $3 billion (s.a.a.r.), less than half the deficit recorded in the same period last year.

The latest industrial production data indicate that the economic recovery in Italy is continuing; the average level of industrial production was 2.5 percent higher in July and August than in the same two months of 1983. Also, the unemployment rate fell from 10.4 percent in the second quarter to 10.1 percent in the third quarter of 1984. The official September household survey shows that consumers' outlooks remain positive, with more families likely to buy consumer durables than was the case in July. Consumers are also more confident that inflation has moderated, and they expect this trend to continue. At the end of September, the year-on-year inflation rate was 9.5 percent, the lowest such rate since March 1973.

The government's proposed budget for next year calls for a deficit equivalent to 15.7 percent of GDP in 1985, down from the latest projection of 16.5 percent for 1984. Details of the budget proposals are not yet available. Despite labor opposition, the government appears to be counting on holding wage increases for government workers to 7 percent as a way to encourage wage restraint in the private sector and to reduce inflationary expectations. If the rate of inflation is brought down to 7 percent, Prime Minister Craxi has proposed that a new "heavy" lira be issued in 1985 or later, worth 1000 of the current lire.

The trade deficit for the first seven months of this year was $9.8 billion (s.a.a.r.), compared with $8.7 billion in the same period in 1983.

Economic expansion in Canada continues at a moderate pace. Industrial production declined slightly in August following a sharp jump in July; the July increase was associated with a pickup in the automotive sector and an across-the-board increase in U.S. imports. On October 29, Canadian U.A.W. members ratified a three-year contract, ending the 13-day strike against General Motors. The contract includes a larger increase in hourly wages and more paid time off than the recent settlement with U.S. workers, but does not contain the job security and training provisions of the latter. If inflation in both countries were to average 5 percent over the next three years, average wage rates for G.M.'s Canadian workers would rise about 20 percent, compared with a 17 percent rise for U.S. workers. The unemployment rate in August increased 0.6 percent from July to 11.8 percent (s.a.), the highest rate in a year. The rise is associated with an increase in the labor force rather than a decline in employment.

In September, the consumer price index stood only 3.8 percent (s.a.) above its year-earlier level. The cumulative trade surplus through August reached $15.6 billion (s.a.a.r.), somewhat higher than in the same period last year. An increasing service account deficit, however, helped hold the current account surplus to $1 billion (s.a.a.r.) in the first half of 1984, compared with $3.2 billion in the comparable period last year.

In early October a Swedish government-appointed committee formally recommended that a limited number of foreign banks be allowed to establish subsidiaries in Sweden. Changes in the existing banking laws, which prohibit foreign banking operations in Sweden, should take place in July 1985 with foreign banks beginning operations in early 1986. Foreign banks would be required to provide the same range of banking activities as domestic banks and would be regulated in the same manner. Other restrictions include the prohibition of foreign banks owning shares of any domestic banks or of any non-bank financial institutions. In their first year of operations, foreign bank's equity capital would be limited to a maximum of $9 million and a minimum of $3 million.

Debt Situation in Selected Developing Countries

The Philippines and Venezuela recently reached agreements in principle with their bank creditors on multi-year reschedulings, and Argentina, Brazil and Chile have begun or are about to begin discussions with bank creditors on financing packages for 1985 and subsequent years. Argentina and the Philippines are taking measures prerequisite to the approval of IMF programs. Mexico, Brazil and Chile continue to operate successfully under their IMF programs, although Brazilian inflation remains high, and Chile has had to take additional measures to meet its fiscal targets. Peru's external arrears continue to accumulate.

New lending to non-OPEC developing countries by banks in the BIS reporting area continued at a relatively low level in the second quarter, according to the BIS' latest quarterly report. The second-quarter data show an increase in outstanding claims on non-OPEC developing countries of $4.7 billion, after adjustment for the effects of exchange rate changes. This brings the net increase for the first half to about $ 6 billion, close to the rate of net bank lending last year. (Coverage in the quarterly series is less broad than in the semiannual series and has usually shown a smaller volume of new lending.) Increases (unadjusted) in claims on Mexico, Brazil and Chile reflected primarily drawings on loans arranged earlier as part of financing packages, and accounted for more than one-half of the total, but there seems also to have been an increase in voluntary lending to Mexico. Much of the rest was accounted for by new lending to Egypt and Israel.

Following the IMF Managing Director's acceptance of a letter of intent, Argentina and its bank creditors opened discussions on a new medium-term credit and restructuring. By late October, Argentina had eliminated interest arrears on public sector debts to bank through May 2 and repaid the $100 million short-term credit obtained from banks as part of the March 30 package. The banks on the Working Committee have agreed to another postponement of the repayment of the $750 million balance due on the 1982 bridge loan; it is now scheduled for January 15. Inflation intensified in September when the CPI rose by 27.5 percent to a level 687 percent higher than a year earlier. The peso price of the dollar rose only by 23.4 percent in September; since the end of 1983, it has risen about 26 percent less than the CPI. Another compensatory wage adjustment was announced at the beginning of October to achieve a 6 percent increase in real wages in the first nine months of the year. It is payable half at the end of October and half at the end of November. Another wage adjustment has been promised early next year to bring real wages in December 1984 to a level 8 percent above a year earlier. By delaying payment of these increases, the authorities hope to reconcile their promises to the Argentine people with the commitments recently made to the IMF on wage policies and the public sector deficit.

Brazil registered a trade surplus of $9.7 billion during the first nine months of the year, exceeding the target of $9 billion for the entire year. The current account deficit for 1984 is now expected to be $2 billion, substantially below the IMF projection of $5.3 billion. The general price index increased by 10.3 percent in September, not significantly different from the average during the first eight months of the year. The monetary base and M_1 increased substantially in September as the regulations passed in mid-September to restrict the growth of credit do not appear to have been entirely successful in slowing such growth.

Negotiations with creditor banks on a possible multi-year rescheduling are expected to begin on November 14. Brazil is expected to have about $8 billion in cash reserves by year-end and may not seek new credits from banks in 1985.

Mexico's current account surplus in the first half of 1984 was $3.3 billion, $1 billion higher than in the first half of 1983. The surplus is likely to narrow in the second half, reflecting some rise in imports as the economy begins to recover and the lagged effect of the increase in dollar interest rates in the second quarter. Nevertheless, the surplus for the year is likely to reach about $4.5 billion, some $2 billion more than previously projected, unless there is a significant decline in world oil prices in coming days. The annual rate of increase in the CPI in the first three quarters was 61 percent, down from 85 percent in the same period of 1983. In the third quarter, the annual rate was 43.1 percent. There continue to be indications that economic activity began to pick up in the third quarter.

Chile would like to negotiate a rescheduling of debt due bank creditors over 1985-90 and some reduction in interest charges. A request to banks for about $800 million in new money for 1985 also looks likely. Negotiations are expected to begin in November. Chilean authorities have begun discussions with the IMF on a new arrangement to follow the stand-by that expires at the end of this year. Chile has complied with that program, but additional adjustment measures were taken in September in order to remain in compliance through the end of the year.

Peru's external arrears continue to mount and are now about $300 million. Banks have discussed the possibility of disbursing $100 million (held over from a 1983 agreement) in return for an equivalent drawdown of Peru's reserves and payment of interest arrears, but are divided on whether to do this in the absence of a viable IMF program. The Peruvian government is also divided on the proposal.

Venezuela's private sector interest arrears now exceed $1 billion. Final approval of the rescheduling agreement reached last month is contingent on the government making substantial progress in reducing those arrears.

On October 11, the Managing Director of the IMF accepted the Philippines' letter of intent for an 18-month stand-by arrangement. If certain prior actions are taken, and if the Managing Director receives assurances that adequate financing will be forthcoming, the program will be sent to the Executive Board in early November. At that point, the United States, Japan and Korea will provide bridge financing of $80 million until the Philippines is able to draw on the stand-by. In mid-October, the peso was allowed to "float" and soon depreciated by about 10 percent. Later in October, the government raised petroleum product prices and various retail prices, touching off public disturbances. The exchange rate and price measures fulfill some of the prior actions required by the IMF. On October 9, the Philippines was granted a fourth 90-day extension of the moratorium on the payment of principal to banks on non-trade debt. On October 17 the advisory committee of creditor banks announced it had reached agreement to reschedule over a 10-year period about $5 billion in Philippine loans maturing between October 1983 and December 1986, to provide $925 million in new money, and also to provide a revolving short-term trade facility of about $3 billion.