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Confidential (FR) Class III FOMC

December 12, 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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INTERNATIONAL DEVELOPMENTS IV

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SELECTED DOMESTIC NONFINANCIAL DATA
(Seasonally adjusted)

	Latest data			Percent change from		
	Period	Release date	Data	Preceding period	Three periods earlier	Year earlier
				(At annual rates)		
Civilian labor force	Nov.	12-07-84	114.0	.1	1.9	1.8
Unemployment rate (%) 1/	Nov.	12-07-84	7.2	7.4	7.5	8.4
Insured unemployment rate (%) 1/	Sept.	12-06-84	2.7	2.7	2.7	3.4
Nonfarm employment, payroll (mil.)	Nov.	12-07-84	95.5	3.8	3.9	4.1
Manufacturing	Nov.	12-07-84	19.7	1.4	-.4	3.6
Nonmanufacturing	Nov.	12-07-84	75.7	4.5	5.1	4.2
Private nonfarm:						
Average weekly hours (hr.) 1/	Nov.	12-07-84	35.2	35.1	35.2	35.2
Hourly earnings ($) 1/	Nov.	12-07-84	8.43	8.38	8.34	8.14
Manufacturing:						
Average weekly hours (hr.) 1/	Nov.	12-07-84	40.5	40.4	40.5	40.6
Unit labor cost (1967=100)	Oct.	11-29-84	82.8	-4.3	-3.8	-6.9
Industrial production (1967=100)	Oct.	11-15-84	165.2	.0	-1.7	6.6
Consumer goods	Oct.	11-15-84	161.9	2.2	-4.6	3.2
Business equipment	Oct.	11-15-84	188.5	3.2	6.5	16.9
Defense & space equipment	Oct.	11-15-84	139.0	8.7	8.8	13.1
Materials	Oct.	11-15-84	162.1	-5.2	-3.4	5.3
Consumer prices all items (1967=100)	Oct.	11-21-84	314.6	4.2	4.6	4.1
All items, excluding food & energy	Oct.	11-21-84	305.4	3.9	4.9	4.9
Food	Oct.	11-21-84	304.9	4.3	3.6	3.9
Producer prices: (1967=100)						
Finished goods	Oct.	11-09-84	290.9	-2.1	-1.8	1.3
Intermediate materials, nonfood	Oct.	11-09-84	326.2	2.2	.1	1.7
Crude foodstuffs & feedstuffs	Oct.	11-09-84	249.4	-13.3	-11.5	-3.4
Personal income ($ bil.) 2/	Oct.	11-19-84	3,085.5	6.9	7.7	9.6
				(Not at annual rates)		
Mfgrs. new orders dur. goods ($ bil.)	Oct.	12-04-84	95.2	-3.5	-6.4	.5
Capital goods industries	Oct.	12-04-84	29.8	-13.3	-14.4	-7.0
Nondefense	Oct.	12-04-84	25.3	-9.3	-8.7	-1.0
Defense	Oct.	12-04-84	4.6	-30.5	-36.6	-30.3
Inventories to sales ratio: 1/						
Manufacturing and trade, total	Sept.	12-11-84	1.37	1.35	1.32	1.34
Manufacturing	Oct.	12-04-84	1.51	1.50	1.47	1.46
Trade	Sept.	12-11-84	1.25	1.25	1.20	1.23
Ratio: Mfgrs.' durable goods inventories to unfilled orders 1/	Oct.	12-04-84	.554	.542	.530	.546
Retail sales, total ($ bil.)	Oct.	11-14-84	107.7	-.1	.3	6.7
GAF 3/	Oct.	11-14-84	23.0	-1.8	2.2	8.6
Auto sales, total (mil. units.) 2/	Nov.	12-04-84	10.0	.5	.9	3.4
Domestic models	Nov.	12-04-84	7.2	1.1	4.2	2.9
Foreign models	Nov.	12-04-84	2.8	-1.0	17.1	4.9
Capital Appropriations, mfg.	1984-Q3	12-10-84	27,548	-22.8	—	36.2
Housing starts, private (thous.) 2/	Oct.	11-20-84	1,515	-9.8	-13.6	-9.4
Leading indicators (1967=100)	Oct.	11-29-84	163.8	-.7	-.1	.9

1. Actual data used in lieu of percent changes for earlier periods.
2. At annual rates.
3. Excludes mail order houses.

Economic growth remained slow in the autumn. Consumer outlays and capital goods orders have been weak since mid-year, leading to downward production adjustments and a reduced pace of inventory investment in the manufacturing sector. In addition, residential construction activity has been subdued, although home sales have firmed. Despite the sluggishness in goods output, however, employment—particularly in trade and services--posted further gains in November. With little pressure on resource utilization, wage and price inflation has maintained the relatively moderate pace observed earlier this year.

Industrial Production and Capacity Utilization

Industrial production increased somewhat in November, but the rise was primarily the result of a rebound of auto production from strike-affected levels. Auto assemblies in November reached almost 8 million units at an annual rate, sharply higher than the October pace of 7 million units. In addition, more complete data for October suggest weaker industrial activity than estimated initially. Capacity utilization in the industrial sector was about unchanged in November, and remained about 1 percentage point below the peak of 82.7 percent in the current cycle in July. (A more complete discussion of industrial production in November will be included in the Greenbook supplement, distributed December 14.)

Employment and Unemployment

Although factory hiring remained slow, total nonfarm payroll employment rose 300,000 last month, after rising 345,000 in October. The bulk of the new jobs in both months occurred in the services industry and at trade

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

		1984					
	1983	Q1	Q2	Q3	Sept.	Oct.	Nov.
		-Average monthly changes-					
Nonfarm payroll employment[2]	282	344	359	224	284	343	303
Strike adjusted	282	339	366	216	210	350	308
Manufacturing	92	108	54	-4	-109	65	23
Durable	70	82	46	15	-62	52	24
Nondurable	22	25	8	-19	-47	13	-1
Construction	22	22	64	10	18	10	30
Trade	69	88	85	61	91	162	132
Finance and services	96	105	122	63	118	127	106
Total government	3	1	7	72	152	-26	-13
Private nonfarm production workers	249	259	307	115	92	288	287
Manufacturing production workers	84	81	35	-15	-110	45	8
Total employment[3]	330	400	536	-170	270	347	286
Nonagricultural	336	425	495	-140	179	549	47

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)

		1984					
	1983	Q1	Q2	Q3	Sept.	Oct.	Nov.
Civilian, 16 years and older	9.6	7.9	7.5	7.5	7.4	7.4	7.2
Teenagers	22.4	19.6	18.7	18.7	19.3	18.8	17.5
20-24 years old	14.4	11.9	11.5	11.5	11.5	11.1	10.9
Men, 25 years and older	7.8	6.1	5.7	5.6	5.5	5.5	5.4
Women, 25 years and older	7.2	6.1	5.9	6.1	5.9	6.1	5.7
White	8.4	6.8	6.4	6.4	6.4	6.4	6.1
Black	19.5	16.5	15.9	16.0	15.1	15.4	15.0
Fulltime workers	9.5	7.6	7.2	7.2	7.1	7.1	6.9
Memo:							
Total national[1]	9.5	7.8	7.4	7.4	7.3	7.3	7.0

1. Includes resident Armed Forces as employed.

establishments. In manufacturing, automakers boosted employment in November after several months in which activity was depressed by strikes and production problems. But the employment gains in auto and related industries were partially offset by small losses in primary metals, nonelectrical machinery, textile and apparel--industries that have been particularly vulnerable to competition from imports. The overall factory workweek edged up 0.1 hour in November to 40.5 hours, about the level reported since last spring.

The civilian unemployment rate fell 0.2 percentage point in November to 7.2 percent, after four months of virtually no change. Throughout the summer and early autumn, long-term joblessness continued to edge down, but an increasing number of workers reported short spells of unemployment as activity slowed. There were indications from both the household survey results and data on initial claims for unemployment insurance that new layoffs subsided somewhat during November.

Personal Income and Consumption

Growth in income has been fairly well maintained in recent months, although the pace has been moderating as economic activity has slowed. Personal income increased $18 billion in October, somewhat less than the $21 billion advance in the third quarter and the average increase of $24 billion during the first half of this year. The slower income growth in October primarily reflected smaller gains in wages and salaries, but employment and hourly earnings information for November suggests that wage and salary disbursements may have picked up somewhat last month. Interest income continued to grow rapidly in October and has accounted for

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

	1984 Q1	1984 Q2	1984 Q3	1984 Aug.	1984 Sept.	1984 Oct.
Total sales	3.5	2.9	-1.0	-.8	1.2	-.1
(Real)[1]	2.7	3.0	-1.4	-1.0	.9	-.5
Total, less automotive, gasoline and nonconsumer stores	3.0	2.5	.5	.0	2.0	-1.1
GAF[2]	3.2	3.9	-.7	.3	3.7	-1.8
Durable	5.1	4.3	-2.8	-1.8	-.3	2.6
Automotive group	5.7	4.6	-4.7	-3.8	-.4	3.5[4]
Furniture & appliances	3.5	3.8	.8	1.3	3.0	-.9
Nondurable	2.7	2.1	.0	-.2	2.0	-1.6
Apparel	2.4	6.3	-3.1	-2.5	4.9	-2.3
Food	2.2	2.3	1.1	-1.6	2.8	-1.6
General merchandise[3]	3.4	3.0	-.2	1.0	3.6	-1.9
Gasoline stations	.3	1.4	-3.5	.5	.4	-1.1

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.
4. Sales of the automotive group frequently differ from sales of cars on a unit basis because of broader coverage (e.g. parts) and sampling.

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

	1984 Q1	1984 Q2	1984 Q3	1984 Sept.	1984 Oct.	1984 Nov.
Total sales[1]	10.5	10.6	10.3	10.2	10.0	10.0
Imports	2.3	2.4	2.4	2.4	2.8	2.8
Domestic	8.2	8.2	7.9	7.8	7.2	7.2
Small	3.7	3.7	3.7	3.8	3.3	3.5
Intermediate & standard	4.5	4.5	4.2	4.1	3.9	3.7
Domestic production	8.2	7.7	7.5	6.9	7.0	7.9
Small	3.9	3.8	3.6	3.5	3.3	3.7
Intermediate & standard	4.2	3.9	3.9	3.5	3.7	4.2
Domestic inventories	1.49	1.41	1.32	1.32	1.32	1.43
Days' supply[2]	56	53	51	52	57	61

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

PERSONAL INCOME AND EXPENDITURES
(Based on seasonally adjusted data)

	1984 Q1	1984 Q2	1984 Q3	1984 Aug.	1984 Sept.	1984 Oct.
	--Percent change from previous quarter[1]--			--Percent change from previous month--		
Total personal income						
Nominal	12.4	9.1	8.6	.6	.7	.6
Real[2]	8.3	6.8	4.1	.0	.5	--
Disposable personal income						
Nominal	12.7	8.6	8.4	.7	.8	.6
Real[2]	8.6	6.3	3.9	.0	.5	--
Personal consumption expenditures						
Nominal	8.6	10.2	4.9	.0	1.7	-.1
Real[2]	4.6	7.9	.6	-.6	1.5	--
	--Changes in billions of dollars from previous quarter--			--Changes in billions of dollars from previous month--		
Total expenditures	46.3	56.2	28.1	.4	40.4	-1.7
Durables	11.1	9.8	-2.2	-7.7	10.2	-3.0
New autos	4.4	1.5	-2.8	-4.4	2.4	-3.9
Furniture & appliances	3.2	3.6	-.2	1.3	4.1	-1.7
Nondurables	18.3	17.0	2.8	-5.7	17.1	-4.3
Food	8.8	8.2	6.3	-7.2	7.3	-1.5
Apparel	3.6	6.1	-2.9	-.3	5.6	-.7
Services	16.9	29.3	27.5	13.8	13.2	5.6
Total personal income	84.0	64.1	62.1	18.4	22.5	17.6
Disposable personal income	73.6	52.1	51.8	17.0	19.6	15.3
Wage and salary disbursements	40.3	37.4	26.4	4.5	12.3	4.2
Personal interest income	15.7	21.7	22.4	7.5	7.1	6.8
Addendum:						
Personal saving rate (percent)	6.1	5.7	6.3	6.8	5.9	6.5

1. Changes from previous quarter are at compound rates; monthly changes are not at annual rates.
2. Deflated by the implicit price deflator for personal consumption expenditures.

an unusually large share of the rise in total personal income so far this year.

Personal consumption outlays declined a little in October after a sharp rise in the preceding month. Purchases of both durable and nondurable goods fell, and spending on consumer services posted only a small increase. Domestic car sales in November were unchanged from the relatively low 7.2 million unit annual rate reported in October. Sales of imported cars in November continued at the strong 2.8 million unit pace of October, the highest selling rate since early 1980.

Growth in personal consumption expenditures in the past several months has been well below that of disposable personal income, and the personal saving rate since mid-year has averaged around 6.5 percent, compared with the rate of 5.9 percent during the first half of this year.

Consumer confidence in November reportedly remained at a relatively robust level. The Michigan index edged down a little in November as households were a little more concerned about buying conditions for large household durables and about prospects for business conditions in the next 12 months. The Conference Board index of confidence, in contrast, increased to the highest level since June with all questions on present and expected economic conditions contributing to the advance.

Business Fixed Investment

Business investment spending has decelerated considerably in the past several months. Growth in nonresidential construction slowed sharply in the third quarter. Although spending on structures rose in October, the increase was still well below the very rapid rate of expansion posted earlier this year. On the equipment side, shipments from domestic capital

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

	1984			1984		
	Q1	Q2	Q3	Aug.	Sept.	Oct.
Producers' durable equipment						
Nondefense capital goods						
Shipments	1.1	5.6	2.7	.7	6.5	-4.7
Orders	5.2	4.9	-1.1	-4.2	5.0	-9.3
Unfilled orders	4.4	4.1	1.7	.3	.1	-.9
Imports of capital goods excluding autos	25.3	-2.1	22.0	-19.0	9.8	-15.2
Sales of heavy-weight trucks (thousands of units, A.R.)	232	267	252	262	208	255
Nonresidential structures						
Nonresidential construction	8.0	8.7	.1	1.0	1.0	1.7
Commercial building	13.7	13.7	1.7	2.5	2.6	3.5
Value of nonresidential building						
Permits	16.0	.8	-1.0	7.1	-18.6	19.3
Contracts	-8.6	19.7	2.9	5.8	-17.8	19.3

goods producers declined substantially in October across a wide range of categories and imports of capital goods fell after rising sharply from July to September.

Recent indicators of near-term investment spending have been weak. New orders for nondefense capital goods slackened notably through the summer and early autumn; by October the level of orders in this category was about 6 percent below that in the first half of this year. In addition, the value of new permits for nonresidential construction has been flat since early this year, and the value of new contracts increased only 2.9 percent in the third quarter, considerably slower than the 8 percent rise in the first half of 1984.

Nevertheless, business spending plans for 1985 as a whole still appear relatively strong. Both the Merrill-Lynch and McGraw-Hill surveys report that businesses plan to increase nominal plant and equipment spending by around 10 percent next year. The Conference Board also reported that newly-approved capital appropriations (net of cancellations) of the nation's 1,000 largest manufacturers excluding auto makers rose 15 percent in the second quarter and 4 percent in the third quarter of this year, to a level 37 percent above that a year ago. On average, appropriations tend to precede expenditures by about three to four quarters. These indicators point to continued, but moderating, growth in outlays in the first half of next year.

Business Inventories

Business inventory accumulation slowed in September, as overall manufacturing and trade stocks rose at an annual rate of $19 billion in

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

	1984			1984		
	Q1	Q2	Q3	Aug.	Sept.[r]	Oct.[p]
Book value basis						
Total	73.7	56.3	55.1	61.8	49.2	--
Manufacturing	27.8	40.4	31.6	42.1	22.2	14.6
Wholesale trade	13.6	10.1	16.8	5.4	18.3	19.6
Retail trade	32.3	5.8	6.7	14.4	8.7	--
Automotive	10.5	-4.3	1.7	5.5	9.0	--
Ex. auto	21.8	10.1	5.0	8.9	-.3	--
Constant dollar basis						
Total	24.4	19.7	23.6	26.4	19.2	--
Manufacturing	9.1	13.8	12.6	15.2	10.8	--
Wholesale trade	3.9	4.1	7.9	8.0	4.4	--
Retail trade	11.4	1.7	3.1	3.3	3.9	--
Automotive	3.8	-3.0	.2	-.1	2.7	--
Ex. auto	7.7	4.7	2.9	3.3	1.2	--

r--revised estimates.
p--preliminary estimates.

INVENTORIES RELATIVE TO SALES[1]

	Cyclical Reference Points[2]		1984			1984		
	1981 Low	1982 High	Q1	Q2	Q3	Aug.	Sept.[r]	Oct.[p]
Book value basis								
Total	1.39	1.53	1.33	1.33	1.36	1.35	1.37	--
Manufacturing	1.60	1.77	1.44	1.47	1.49	1.48	1.50	1.51
Wholesale trade	1.06	1.28	1.11	1.09	1.14	1.13	1.14	1.15
Retail trade	1.36	1.44	1.37	1.34	1.37	1.37	1.36	--
Automotive	1.59	1.88	1.49	1.37	1.46	1.44	1.48	--
Ex. auto	1.29	1.36	1.34	1.33	1.35	1.36	1.33	--
Constant dollar basis								
Total	1.62	1.75	1.52	1.51	1.55	1.53	1.55	--
Manufacturing	1.91	2.11	1.73	1.76	1.79	1.76	1.80	--
Wholesale trade	1.34	1.52	1.33	1.30	1.36	1.34	1.37	--
Retail trade	1.34	1.44	1.34	1.31	1.34	1.34	1.33	--
Automotive	1.49	1.81	1.38	1.27	1.32	1.30	1.33	--
Ex. auto	1.28	1.37	1.33	1.33	1.35	1.36	1.33	--

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.

constant-dollar terms, compared with the $23 billion pace during the first eight months of this year. The moderation appears to have continued in October in the manufacturing sector.

Faced with heavy competition from imports, manufacturers have moved quickly to forestall inventory imbalances. As orders and shipments weakened in recent months, producers in many industries began to trim their output, although their inventory-to-shipments ratios often were still quite low by historical standards. As a result, the growth in factory stocks has slowed sharply since August. In September and October, the book value of manufacturers' inventories rose at an average annual rate of $18.5 billion, considerably slower than the $39 billion rate of investment maintained from February to August.

Inventories at nonauto retail establishments, especially general merchandisers and apparel stores, were quite high going into early autumn; and with sales remaining flat into the fourth quarter, many establishments appear to have adjusted their ordering policies and stepped up sales promotion efforts in an attempt to pare their excess stocks. Auto dealers' stocks expanded in November as strikes at General Motors plants ended and auto production rose to nearly 8 million units at an annual rate. With sales of only 7.2 million units, dealers reported a 61 days' supply at the end of November.

<u>Housing Markets</u>

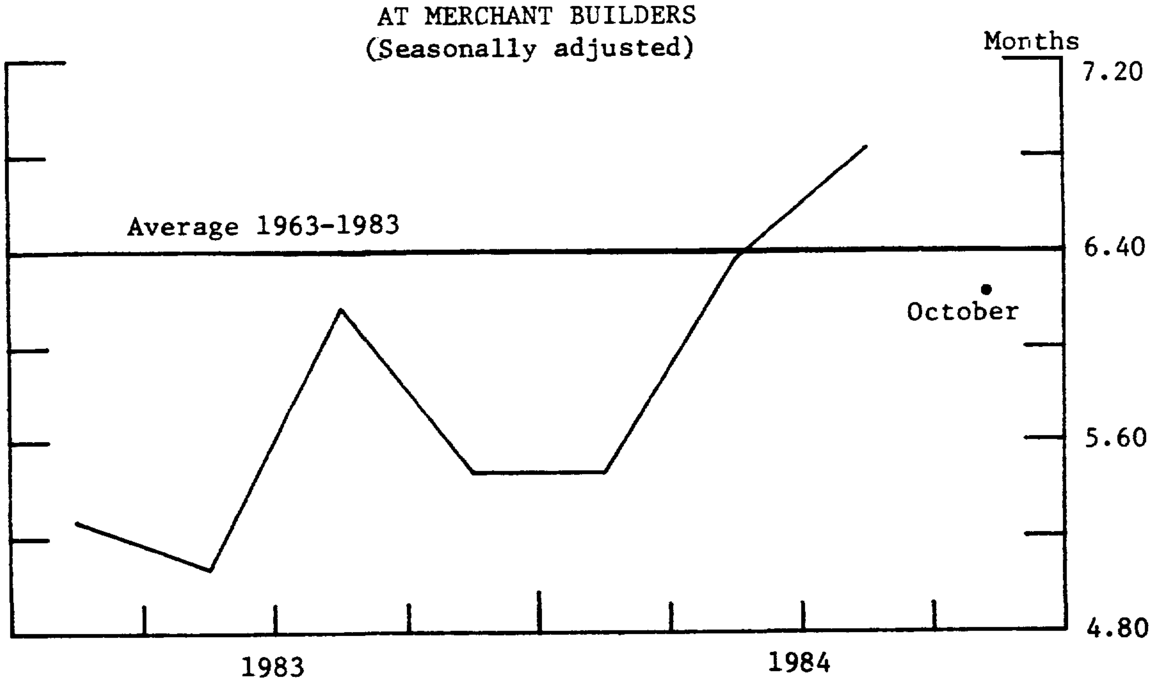
Residential construction remained sluggish through October, but home sales appear to have begun to respond to the reduction in mortgage rates since the summer. In October, sales of new single-family homes rose 2

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

	1983	1984					
	Annual	Q1	Q2	Q3	Aug.	Sept.	Oct.[1]
All units							
Permits	1.61	1.81	1.76	1.50	1.51	1.44	1.41
Starts	1.70	1.97	1.90	1.66	1.55	1.68	1.52
Single-family units							
Permits	.90	1.02	.93	.82	.80	.84	.78
Starts	1.07	1.28	1.14	.98	.93	1.02	.93
Sales							
New homes	.62	.69	.63	.62	.56	.67	.68
Existing homes	2.72	2.94	3.04	2.71	2.70	2.67	2.67
Multifamily units							
Permits	.70	.79	.83	.68	.70	.60	.63
Starts	.64	.69	.76	.68	.62	.66	.59
Mobile home shipments	.30	.30	.29	.29	.30	.28	n.a.

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

MONTHS' SUPPLY OF UNSOLD HOUSING UNITS
AT MERCHANT BUILDERS
(Seasonally adjusted)



percent after an 18 percent jump in September, bringing new home sales to their highest level since March. Sales of existing homes, after a five-month decline, leveled off in October.

On the construction side, total private housing starts fell almost 10 percent in October, to an annual rate of 1.5 million units; newly-issued permits also posted a 2 percent drop. Both measures of new residential construction activity were at their lowest point in nearly two years. The lag in the response of residential construction to firmer sales figures may, in part, reflect builders' desire to prevent further buildups in the stock of unsold homes. Builders' inventories, while not extremely high in historical perspective, increased noticeably during the first 10 months of this year (chart).

In line with the generally favorable inflation environment, price and cost increases remain moderate in the housing sector. Construction costs for new units, measured by the fixed-weighted price index for residential construction, were 4.2 percent above a year earlier in the third quarter. Nationally, the average price of existing homes sold in October was about 4 percent above a year earlier—only slightly more than the average increase during the preceding two years.

Federal Government

Federal unified budget outlays rose sharply in October from the third-quarter pace, but the rise was largely attributable to a number of special factors. October outlays included $3.1 billion of loans for low-income housing projects—lending that was previously handled by the issuance of guaranteed notes by local authorities. In addition, Federal outlays were boosted by the makeup of a delay in September of periodic hospital reimbursements under medicare and by normal seasonal influences.

Defense spending, which was about unchanged in the third quarter, increased somewhat in October, primarily in the operations and maintenance category. Defense procurement outlays declined, suggesting that the recent pattern of defense shortfalls is continuing.

The Treasury released a tax reform study on November 27. The study proposes a substantial broadening of the individual and corporate income tax bases through the elimination of many tax preferences and loopholes, with concurrent reductions in marginal tax rates. The Treasury study is currently being reviewed within the administration and could form the basis for an official legislative proposal presented at the time of the State of the Union address or Budget Message in late January or early February.

State and Local Government

Real outlays for goods and services by state and local governments have continued to increase this fall after a sharp advance in the third quarter. In October, real spending for construction stood well above its third-quarter average. Moreover, in November, employment in the sector was 80,000 above its third-quarter level.

The overall fiscal position of the sector has weakened lately. The sharp economic slowdown reduced corporate tax receipts in the third quarter, and federal grants to state and local governments also declined. With rising outlays, the combined operating and capital budget surplus in the state and local sector dwindled to just $2.5 billion in the third quarter from an average of nearly $12 billion over the preceding year. In the November elections, citizens defeated a variety of referenda aimed primarily at restricting spending and reducing taxes in many states.

Exports and Imports

The merchandise trade deficit in October was substantially reduced from the level in the third quarter. The narrower trade gap resulted from a marked decline in imports; exports in October were at about the same level as the third-quarter average. Although imports eased across a wide range of commodity categories—machinery, industrial supplies, consumer goods and agricultural products--the level of imports in October was still quite high, reflecting the continued high value of the dollar and the substantial demand for goods produced abroad.

Prices of non-oil imports in October were up only slightly from their third-quarter average, as the rise in exchange rate continued to moderate foreign price increases. The price of imported oil was about the same as in September but was about 25 cents per barrel less than the average for the third quarter. (Further discussion of international economic developments is included in Section IV.)

Prices

Recent price reports indicate little evidence of a change in the underlying rate of inflation. In October, the consumer price index for all urban consumers rose 0.4 percent for the second month--only slightly above the average pace earlier this year—while the producer price index for finished goods fell 0.2 percent in both months.

Food prices at the consumer level rose 0.4 percent in October after a small decline in September. So far this year, the food index has increased at an average annual rate of nearly 4 percent, not much below the overall

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

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.

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 Sept.	1984 Oct.
				--Annual rate--			--Monthly rate--	
Finished goods	100.0	3.7	.6	5.7	-.4	.4	-.2	-.2
Consumer foods	24.0	2.1	2.3	16.9	-8.5	3.3	-.4	.1
Consumer energy	12.0	-.1	-9.2	-8.1	7.5	-16.7	-.8	1.5
Other consumer goods	41.9	5.3	1.9	4.5	1.3	2.5	.0	-.5
Capital equipment	22.2	3.9	1.9	3.8	2.3	2.9	.0	-.6
Intermediate materials[2]	94.8	.2	1.4	2.9	3.3	-1.0	.0	.2
Exc. energy	79.5	.6	3.0	3.8	2.0	.4	.0	.2
Crude food materials	52.8	1.5	8.0	12.5	-21.7	-4.9	.0	-1.1
Crude energy	31.3	2.6	-4.6	-1.6	4.0	1.0	-.8	-.3
Other crude materials	15.9	-7.6	15.5	-9.7	31.6	-14.0	1.2	-1.5

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

CPI. In 1982 and 1983, by contrast, significantly smaller increases in food prices played a more important role in holding down the advance in the CPI total. At the producer level, prices in October edged down for finished foods and fell for crude foods. Although spot prices for livestock have rebounded since mid-October, futures prices for cattle and hogs have not changed in the past few weeks.

Consumer energy prices were up 0.3 percent in October, less than in September, as large increases for gasoline and fuel oil were partly offset by declines for electricity and natural gas. In contrast to food, the energy component has risen so far this year at an average annual rate well below the CPI total--only 3/4 percent--thus contributing importantly to a lower CPI for the third successive year. Moreover, the near-term outlook for prices of petroleum-based products appears to be little changed, as spot prices of gasoline and fuel oil have weakened again since late September.

Aside from the food and energy sectors, consumer prices rose 0.3 percent in October, somewhat below the average pace of 5 percent at an annual rate maintained since the end of 1982. Prices of services were up 0.5 percent, about the average rate so far this year, but prices of consumer commodities advanced only 0.2 percent after a large September increase. Prices of new cars rose 0.2 percent in October, and used car prices posted their third recent monthly decline after rising rapidly over the first half of this year and most of 1982 and 1983. If used cars were excluded, this year's rise in prices of CPI commodities less food and energy would be around 2-1/2 percent, not much higher than the comparable PPI component.

At the producer level, declines in the prices of new cars and trucks were responsible for most of the October reduction in the PPI index for finished goods less food and energy.[1] However, producer prices also were down for some other items in the finished consumer goods and capital equipment categories. At an earlier stage of processing, prices of intermediate materials less food and energy rose 0.2 percent in October, about the average rate so far this year.

Wages and Labor Costs

Wage inflation has continued to moderate this year, slowing to the lowest rate of increase in the past 20 years. In November, the hourly earnings index was only about 3 percent above the level of a year earlier, compared with the 4 percent rise in 1983. Most of the deceleration in wage inflation has been associated with smaller wage adjustments in the service-producing sector of the economy.

In the nonfarm business sector, hourly compensation, which includes wages, fringe benefits, and employers' contributions for social insurance, rose at a 3-3/4 percent annual rate in the third quarter--the same as in the preceding quarter. With inflation remaining fairly stable in recent years and compensation increases getting smaller, gains in real hourly compensation

1. The October PPI indexes for new cars and trucks compare manufacturers' prices for new models, after adjustment for quality changes, with September prices for old models. The CPI differs in a number of ways, notably because the prices of new models are phased in over several months in accordance with the mix of sales and because the sample, which includes imports, is broader.

HOURLY EARNINGS INDEX[1]
(Percentage change; based on seasonally adjusted data)[2]

	1983	1984 Q1	1984 Q2	1984 Q3	1984 Sept.	1984 Oct.	1984 Nov.	Nov. 1983 to Nov. 1984
			--Annual rate--		--Monthly rate--			
Total private nonfarm	3.9	3.5	3.2	2.7	.6	-.1	.4	3.1
Manufacturing	2.7	3.8	3.0	3.1	.1	.2	.5	3.2
Durable	2.1	3.8	2.7	2.8	.0	.1	.4	3.0
Nondurable	3.9	3.6	3.5	3.8	.2	.4	.5	3.7
Contract construction	1.5	2.3	1.9	-.7	.1	-.3	.3	1.1
Transportation and public utilities	4.3	3.7	3.1	2.7	.7	-.1	.1	2.8
Total trade	4.7	2.7	2.5	2.0	.6	-.1	.5	2.6
Services	4.9	3.3	4.9	3.9	1.2	-.3	.3	3.9

1. Excludes the effect of interindustry shifts in employment and fluctuations in overtime hours in manufacturing.
2. Changes over periods longer than one quarter are measured from final quarter of preceding period to final quarter of period indicated. Quarterly changes are compounded annual rates.

have slowed from around 2 percent in 1982 to less than 1 percent over the past four quarters.

Output per hour in the nonfarm business sector fell 0.7 percent at an annual rate in the third quarter. Declines in measured productivity are not unusual in quarters when output growth slows sharply, as it did last quarter, and the latest data still appear consistent with a trend growth rate in productivity of around 1-1/4 percent annually.

SELECTED FINANCIAL MARKET QUOTATIONS[1]
(Percent)

	1982/1983 Cyclical low	1984 highs	1984 FOMC Oct. 2	1984 FOMC Nov. 7	1984 Inter-meeting low	1984 Dec.11	Change from: 1984 highs	Change from: FOMC Nov. 7
Short-term rates								
Federal funds[2]	8.42	11.63	10.60	9.80	--	8.92	-2.71	-.88
Treasury bills								
3-month	7.08	10.67	10.25	8.55	--	8.35	-2.32	-.20
6-month	7.62	10.77	10.35	8.86	8.45	8.52	-2.25	-.34
1-year	7.73	11.13	10.39	9.11	8.67	8.80	-2.33	-.31
Commercial paper								
1-month	8.00	11.42	10.83	8.99	8.52	8.71	-2.71	-.28
3-month	7.97	11.35	10.79	9.05	8.58	8.77	-2.58	-.28
Large negotiable CDs[3]								
1-month	8.08	11.52	10.94	9.13	8.61	8.76	-2.76	-.37
3-month	8.13	11.79	11.11	9.23	8.72	8.90	-2.89	-.33
6-month	8.20	12.30	11.29	9.39	8.88	9.18	-3.12	-.21
Eurodollar deposits[4]								
1-month	8.68	11.89	11.09	9.60	8.84	8.88	-3.01	-.72
3-month	8.71	12.20	11.41	9.75	--	9.14	-3.06	-.61
Bank prime rate	10.50	13.00	12.75	12.00	--	11.25	-1.75	-.75
Treasury bill futures								
Mar. 1985 contract	9.05	12.57	10.59	9.16	8.56	8.69	-3.88	-.47
Dec. 1985 contract	10.86	13.20	11.43	10.23	9.67	9.86	-3.34	-.37
ermediate- and long-term rates								
U.S. Treasury (constant maturity)								
3-year	9.33	13.49	12.29	11.05	10.56	10.75	-2.74	-.30
10-year	10.12	13.99	12.54	11.72	11.24	11.57	-2.42	-.15
30-year	10.27	13.94	12.35	11.63	11.32	11.59	-2.35	-.04
Municipal revenue (Bond Buyer index)	9.21	11.44	10.65[5]	10.62	--	10.47[5]	-.97	-.15
Corporate--A utility Recently offered	11.64	15.30	13.90e	13.09e	12.77	12.93e	-2.37	-.16
Home mortgage rates								
S&L fixed-rate	12.55	14.68	14.26[6]	13.74	--	13.20[6]	-1.48	-.54
FNMA ARM, 1-yr.	10.49	13.70	12.90[6]	11.55	--	11.05[6]	-2.65	-.50

	1982 Lows	1983 Highs	1984 FOMC Oct. 2	1984 FOMC Nov. 7	1984 Dec. 11	Percent change from: FOMC Oct. 2.	Percent change from: FOMC Nov. 7
Stock prices							
Dow-Jones Industrial	776.92	1287.20	1191.36	1233.22	1178.33	-1.1	-4.5
NYSE Composite	58.80	99.63	94.38	97.46	94.00	-.4	-3.6
AMEX Composite	118.65	249.03	212.77	212.29	202.55	-4.8	-4.6
NASDAQ (OTC)	159.14	328.91	246.10	249.75	238.79	-3.0	-4.4

1. One-day quotes except as noted.
2. Averages for two-week reserve maintenance period closest to date shown. Last observation is for
tenance period ended December 5, 1984.
econdary market.
4. Averages for statement week closest to date shown.
5. One-day quotes for preceding Thursday.
6. One-day quotes for preceding Friday.
e--estimated.

Most interest rates have declined further on balance since the November FOMC meeting, as the System has eased reserve availability and cut the discount rate 1/2 point to 8-1/2 percent against a backdrop of sluggish economic activity and subdued inflation. Federal funds, which had been trading in a 9-1/2 to 10 percent range in early November, have been below 9 percent most recently. Yields on other market instruments have registered much smaller declines than this, especially in the longer maturity area. Market sentiment was adversely affected by upward revisions in estimates of the federal deficit, stronger-than-anticipated employment figures and the large M1 increase published in the latter part of November.

All the monetary aggregates surged in November. Owing to the earlier weakness, M1 remained in the lower part of its annual target range, but M2, reflecting not only the rebound in M1 but also continued acceleration in its nontransaction component, jumped to around the midpoint of its range. M3 also accelerated in November and has moved farther above the upper end of its target range.

Credit market borrowing has picked up on balance thus far in the fourth quarter. Business credit demands have been massive in both short- and long-term markets, partly because of heavy merger activity but also because of the sizable gap between internal funds and capital outlays. In addition, mortgage borrowing appears to be firming, and a moderate pickup in consumer borrowing in October may have carried into November. Tax-exempt bond issuance has been kept at high levels by efforts to market debt before new statutory restraints take effect.

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

	1983	1984					Growth from Q4 1983 to Nov. 1984pe
	Q4	Q1	Q2	Q3	Oct.	Nov.pe	
	------- Percentage change at annual rates ------						
						(Rounded)	(Rounded)
1. M1	4.8	7.2	6.2	4.5	-7.4	9	5
2. M2	8.5	6.9	6.9	6.2	5.9	15	7.5
3. M3	9.9	8.9	10.3	8.2	10.6	16	10
							Levels in billions of dollars Oct. 1984
Selected components							
4. Currency	9.7	8.7	7.2	7.6	3.8	3	157.2
5. Demand deposits	-0.5	1.2	3.4	0.2	-12.7	10	243.8
6. Other checkable deposits	9.6	16.2	9.9	8.8	-10.2	16	139.6
7. M2 minus M1[2]	9.7	6.8	7.1	6.8	10.2	16	1771.8
8. Overnight RPs and Eurodollars, NSA[3]	23.4	19.3	-7.5	-1.4	0.0	15	56.8
9. General purpose and broker/dealer money market mutual fund shares, NSA	-1.2	9.8	15.5	10.6	28.4	51	155.5
10. Commercial banks	12.4	5.4	6.7	7.3	7.7	16	756.8
11. Savings deposits, SA, plus MMDAs, NSA[4]	5.9	6.5	4.9	-3.4	8.8	27	372.4
12. Small time deposits	19.3	4.4	8.6	18.4	6.6	5	384.4
13. Thrift institutions	7.3	6.4	6.2	7.8	11.2	8	812.4
14. Savings deposits, SA, plus MMDAs, NSA[4]	-7.0	-0.9	2.5	-13.2	-2.7	4	311.9
15. Small time deposits	18.8	11.8	8.9	22.7	20.2	11	500.6
16. M3 minus M2[5]	15.9	17.5	24.7	16.2	29.1	20	598.9
17. Large time deposits	15.7	25.0	31.6	26.3	24.4	10	400.9
18. At commercial banks, net[6]	-0.4	10.2	24.3	21.6	20.0	-6	262.1
19. At thrift institutions	58.1	59.0	46.4	35.7	32.0	40	138.7
20. Institution-only money market mutual fund shares, NSA	17.4	11.1	8.1	9.7	135.6	140	52.2
21. Term RPs, NSA	50.0	18.4	41.8	15.3	31.5	45	66.4
22. Term Eurodollars, NSA	-4.4	4.9	-0.4	-29.3	-53.3	32	79.6
	-- Average monthly change in billions of dollars --						
MEMORANDA:							
23. Managed liabilities at commercial banks (24+25)	5.3	4.6	7.0	2.5	8.1	4	433.7
24. Large time deposits, gross	0.1	2.0	7.9	0.0	5.1	0	317.9
25. Nondeposit funds	5.2	2.6	-0.9	2.5	3.0	4	115.8
26. Net due to related foreign institutions, NSA	3.2	1.9	0.9	-0.4	2.2	0	-33.0
27. Other[7]	2.1	0.6	-1.8	2.9	0.8	4	148.8
28. U.S. government deposits at commercial banks[8]	-1.2	1.2	-1.3	1.2	-8.2	8	8.3

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 October and November at rates of 6.7 and 5 percent respectively. At thrift institutions, savings deposits excluding MMDAs decreased in October and November at rates of 5.5 and 4 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.
pe--preliminary estimate.

Meanwhile, the Treasury has been financing a huge quarterly deficit that was enlarged by the need to redeem maturing HUD project notes.

Monetary Aggregates and Bank Credit

A sharp rebound in M1 in November more than offset the contraction in October.[1] The expansion of M1, at roughly a 9 percent annual rate, was attributable to a resurgence in demand and other checkable deposit categories; currency growth remained sluggish.

M2 registered its strongest growth yet this year, increasing at a 15 percent annual rate in November. Its nontransaction component accelerated to a 16 percent rate of growth with surges in overnight RPs, MMDA balances, and assets of money market mutual funds. In addition, the runoff of savings deposits slowed to a 4 percent rate.

The increase in RPs last month likely was related to the uptick in bank holdings of Treasuries--primarily in trading accounts. The strong inflows to money market funds and MMDAs occurred as yields on these investments continued to lag the decline in market rates.[2] Growth in small time deposits, at around an 8 percent annual rate, was by far the slowest increase since the spring; unlike MMDA rates, offering rates on small time deposits declined roughly in line with those on market instruments during November.

The acceleration in M3 in November--to a 16 percent annual rate of growth--primarily reflected expansion of its M2 component.

1. A review of 1984 developments in monetary and credit aggregates is presented in Appendix A.
2. The lag in MMDA rates, which mirrored the earlier sluggishness on the upside when market rates rose, was a pricing decision of depository institutions. In the case of money funds, however, the lag in recorded returns was simply a consequence of the way capital gains are reflected under conventional accounting practices.

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	Sept.[7]	Oct.[7]	Nov.p	Levels in bil. of dollars Nov.p
	Commercial Bank Credit						
1. Total loans and securities at banks[3]	13.9	7.2	8.1	7.3	7.4	11.4	1711.6
2. Securities	4.4	-9.2	4.4	0.8	-2.5	2.8	434.4
3. Treasury securities	-2.3	-11.1	4.4	-7.1	-5.9	1.3	183.0
4. Other securities	9.5	-7.9	4.5	6.7	-0.5	2.9	251.4
5. Total loans[3]	17.5	13.1	9.4	9.5	10.9	14.5	1277.2
6. Business loans[3]	18.9	17.1	7.7	3.5	10.1	9.5	470.7
7. Security loans	-4.4	-38.5	19.7	177.6	89.1	39.3	28.4
8. Real estate loans	13.4	14.5	11.3	11.1	11.0	11.6	376.5
9. Consumer loans	21.5	21.6	14.8	8.6	10.0	16.9	258.7
	Short- and Intermediate-Term Business Credit						
10. Business loans net of bankers acceptances	18.2	17.3	8.0	5.1	10.0	10.4	461.5
11. Commercial paper issued by nonfinancial firms[4]	22.8	67.1	43.8	32.3	70.3	52.4	71.7
12. Sum of lines 10 & 11	18.7	22.5	12.0	8.6	17.1	15.8	533.2
13. Line 12 plus loans at foreign branches[5]	18.5	22.5	11.7	7.0	15.6	17.3	553.8
14. Total bankers acceptances outstanding[6]	-22.2	45.4	-11.8	-26.7	-36.4[8]	n.a.	n.a.
15. Line 13 plus total bankers acceptances outstanding	12.9	25.3	8.6	2.8	9.1[8]	n.a.	n.a.
16. Finance company loans to business[6]	28.8	8.4	12.9	13.8	n.a.	n.a.	n.a.
17. Total short- and intermediate-term business credit (sum of lines 15 and 16)	15.1	22.9	9.2	4.2	n.a.	n.a.	n.a.

n.a.--not available. p--preliminary.
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. 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.
8. Reporting panel change in October 1984 reduced reported acceptances by $400 million. Growth rates have been adjusted to eliminate this break in series.

Growth of the non-M2 component, although remaining strong, "slowed" to a 20 percent annual rate, down from the 29 percent pace in October. This deceleration was entirely due to a drop in net large time deposits at commercial banks. The needs of banks for managed liabilities were lessened by the strength in core deposits and a large buildup in Treasury balances. Thrift institutions, on the other hand, showed continued reliance on large time deposits, which accelerated to about a 40 percent annual rate of increase.

Other non-M2 components contributed to the growth of M3 last month. Institution-only money market funds soared again--by $6 billion, up a bit from the strong gain in October--reflecting favorable yield relationships. Term RPs continued to expand, in keeping with the buildup of securities in bank trading accounts, and term Eurodollars increased for the first time since March.

Bank credit is estimated to have expanded at an 11-1/2 percent annual rate in November, the largest monthly increase since May. Both increased loan growth and a resumption of net securities acquisition contributed to the faster growth. Consumer credit accounted for a good bit of the step-up in loan growth; real estate loans grew just a shade faster than in October and expansion in business loans slowed a little to 9-1/2 percent. Growth in business loans, adjusted to eliminate the effects of merger-related financing, was a little under 8 percent last month, or slightly less than in the third quarter and October.

Despite a sequence of cuts that moved the prime rate down from 12 to 11-1/4 percent at major banks, it remained well above market rates, and prime-based bank loans generally remained less attractive than open market

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

		1984						
	1983	Q1	Q2	Q3	Sept.	Oct.p	Nov.p	Dec.f
Corporate securities - total[1]	8.94	8.37	6.86	10.90	11.38	15.30	15.20	11.50
Public offerings in U.S.	8.24	6.93	5.80	8.74	7.73	12.80	11.60	8.00
Stocks--total[2]	4.30	2.17	1.94	1.64	1.53	2.30	2.30	2.00
Nonfinancial	3.07	1.11	1.27	.84	.78	1.30	1.30	--
Utility	.80	.22	.28	.17	.19	.30	.50	--
Industrial	2.27	.89	.99	.67	.59	1.00	.80	--
Financial	1.23	1.06	.67	.80	.75	1.00	1.00	--
Bonds--total[1]	3.94	4.76	3.86	7.10	6.20	10.50	9.30	6.00
By industry								
Nonfinancial	2.04	1.49	1.91	3.29	3.13	5.50	4.70	--
Utility	.95	.64	.46	.88	.96	1.50	2.10	--
Industrial	1.08	.85	1.45	2.41	2.17	4.10	2.60	--
Financial	1.90	3.27	1.95	3.81	3.07	4.90	4.60	--
By quality[3]								
Aaa and Aa	1.15	.94	1.20	2.23	2.63	2.20	3.20	--
A and Baa	1.58	1.59	1.34	2.76	1.51	4.80	1.85	
Less than Baa	.49	.61	.75	1.19	1.10	2.00	2.15	-
No rating (or unknown)	.37	.36	.15	.32	.35	.70	.25	--
Memo items:								
Equity based bonds[4]	.75	.28	.34	.55	1.01	1.90	1.55	--
Mortgage-backed bonds	.36	1.26	.42	.60	.61	.80	1.85	--
Floating rate or extendible notes	.46	.58	1.35	1.77	.91	.70	1.50	--
Bonds sold abroad - total	.70	1.44	1.06	2.16	3.65	2.50	3.60	3.50
Nonfinancial	.33	.86	.42	.88	1.81	.75	1.80	--
Financial	.37	.58	.64	1.28	1.84	1.75	1.80	--

p--preliminary. f--staff forecast.
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.

paper. Paced by the rapid expansion of outstanding commercial paper, the sum of business loans at domestic offices and foreign branches of U.S. banks plus paper increased at more than a 17 percent annual rate, close to the rapid rate of expansion in the first half of the year.

Business Finance

Although short-term market rates have posted the more sizable declines over the past couple of months, bond yields led the rally earlier and now are more than two percentage points below their 1984 highs. Corporations have responded to the rate decline with a record volume of bond offerings, earmarked in some cases for repayment of short-term debt and in others to meet needs for external funds. Both financial and nonfinancial firms have sharply increased their bond offerings, and the markets have been receptive to higher- and lower-rated firms alike. Corporate bond offerings totaled $12.9 billion in November, almost matching the volume of the preceding month; a backup in bond rates most recently, as well as the normal year-end hiatus, likely will leave December issuance lower, but still sizable.

The market rally has prompted some increase in the proportion of bond offerings with maturities in the 20-year plus category, but many firms still prefer intermediate-term financings. The Euromarket has been especially attractive for such deals. Despite foreign investor concerns that the repeal of the U.S. withholding tax could at some point be reversed, U.S. firms have been able to borrow abroad at favorable rates by including in their issues indemnification clauses promising compensation for any potential drop in interest income due to reintroduction of this tax.

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

	1984			
	Q4[f]	Oct.	Nov.[p]	Dec.[f]
Treasury financing				
Combined surplus/deficit(-)	-74.9	-28.0	-28.4	-18.5
Means of financing deficit:				
Net cash borrowing from the public	60.5	20.8	19.3	20.4
Marketable borrowings/ repayments(-)	58.2	20.3	17.4	20.5
Bills	17.1	2.3	6.1	8.7
Coupons	41.1	18.0	11.3	11.8
Nonmarketable	2.3	.5	1.9	-.1
Decrease in the cash balance	18.2	8.1	16.7	-6.6
Memo: Cash balance at end of period	12.2	22.3	5.6	12.2
Other[2]	-3.8	-.9	-7.6	4.7
Federally sponsored credit agencies, net cash borrowing[3]	5.0	.6	3.1	1.3
FHLB	1.5	.5	.5	.5
FNMA	1.7	.2	.6	.9
Farm Credit Banks	.7	-.3	1.3	-.3
FHLMC	.5	.0	.5	.0
SLMA	.6	.2	.2	.2

p--preliminary. 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.

Although stock prices have declined recently and generally have remained below their 1984 highs, new equity issues have picked up this fall. Nonfinancial firms sold about $1.3 billion during each of the past two months, and financial firms likewise raised substantial amounts in the equity markets. Even so, because of the redemption of outstanding shares associated with merger activity, net equity issuance by nonfinancial firms likely will again be negative in the fourth quarter.

Government Finance

Federal sector. The staff projects a combined deficit of $75 billion in the current quarter, of which about $6-1/2 billion reflects the need to refund HUD project notes.[1] Treasury financing during the quarter is expected to include an $18 billion reduction in cash balances and $61 billion net borrowing from the public. As usual, the majority of new funds will be raised in auctions of marketable coupon issues, although net bill financing could reach almost 30 percent of total new funds raised in the quarter.

On November 28 the Treasury conducted its second $1 billion auction of notes especially targeted to foreign investors. Dealer interest in these securities, offered in conjunction with the domestic 5-year 2-month notes, was not as keen as in the earlier targeted 4-year note offering.

1. The Deficit Reduction Act of 1984 removed the authority to issue tax-exempt project notes from the 1937 Housing Act and placed it under the Internal Revenue Code. Because of confusion surrounding the tax status of the notes, HUD suspended their issuance and was forced to borrow funds directly from the Treasury in order to fulfill its guarantee behind the outstanding project notes. These transactions add to the size of the deficit and alter the composition of government sector debt, by transferring borrowing from local governments to the federal government. Aside from this change, there is no direct effect on credit markets. If the IRS rules that the project notes are tax-exempt, the transactions will be unwound and the federal deficit total in a later period will be reduced accordingly.

The average yield on the latest foreign offering was only 7 basis points (on a comparable basis) below that on the companion domestic issue, whereas the earlier auction produced a 32 basis point saving. In addition, in early November, FNMA offered $300 million of 7-year debentures similar to the foreign-targeted Treasury issues. FNMA estimates that its targeted offering was sold at an average yield 18 basis points below what it would have paid in the domestic market. (See section IV for further discussion of targeted issues and related subjects.)

Borrowing by federally sponsored credit agencies has eased in the fourth quarter as the financing needs of the Federal Home Loan Bank System have diminished. Financial Corporation of America's improved funding situation and strong deposit growth at other S&Ls' have reduced the need for advances. In contrast, FNMA has stepped up its borrowing in the fourth quarter in anticipation of a bulge in its mortgage purchase program that is partly seasonal and also partly a result of S&Ls' attempting to realize capital gains on their mortgage portfolios as long-term rates decline.

State and local sector. Rates on long-term municipal securities have come down significantly less from their 1984 highs than have yields on taxable bonds, and the ratio of tax-exempt to taxable yields is now at its highest level in about 18 months. This evidently is attributable to the unusually heavy issuance of long-term municipal bonds in recent months; in November, gross offerings totaled around $9.5 billion, following a volume almost as large in October. Issuance in the first half of the year averaged $5.8 billion per month. By contrast, offerings of short-term municipals were sharply reduced in November, owing to the

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 Oct.[e]	1984 Nov.[e]	1984 Dec.[f]
	Seasonally adjusted						
Total	10.39	9.43	9.05	10.98	10.55	9.50	9.40
Long-term	7.20	5.86	5.81	8.96	8.80	8.70	8.50
Short-term[1]	3.19	3.57	3.24	2.02	1.75	.80	.90
	Not seasonally adjusted						
Total	10.39	7.84	10.64	10.22	10.70	10.20	10.20
Long-term	7.20	5.06	6.45	8.12	9.00	9.50	9.50
Refundings	1.17	.80	.93	.79	.70	.30	--
Single-family housing[2]	.92	.12	.29	2.69	1.55	1.20	--
Short-term[1]	3.19	2.78	4.19	2.10	1.70	.70	.70

e--estimate. f--staff forecast.
1. These figures do not include tax-exempt commercial paper.
2. Data from the Department of Housing and Urban Development.

absence of HUD project notes and a falloff in issuance of tax and revenue anticipation notes.

In the long-term market, single-family housing bonds have continued to boost issue volume since their reauthorization in June under the Deficit Reduction Act. After soaring to more than $3 billion in July and August, issuance has trended down to a still sizable $1.2 billion in November. There also has been a rush to market industrial development bonds because of impending volume restrictions on most IDBs. Other issuers of IDBs may be coming to market before the end of the year in an effort to avoid more severe arbitrage requirements that go into effect January 1.[1]

1. Under the old law, the proceeds of capital improvement bonds could be reinvested for a period of three years. After year-end, however, the arbitrage period will be shortened to six months for all IDBs, except multifamily housing bonds.

Short-term municipal markets also have been affected by a number of new influences recently. As noted previously, the Department of Housing and Urban Development has not sold project notes--which typically have maturities between 3 and 13 months--since August. At the same time, investors in short-term municipals may have shifted away from more traditional instruments in this market towards variable-rate demand bonds. These bonds technically are long-term, but their yields are adjusted regularly to some index of shorter-term securities, and they have the feature that they can be put sold back ("put") to the bond trustee at prestated intervals, which typically correspond to the interest rate adjustment period, ranging from a day to a quarter. One estimate suggests that such bonds may total close to $14 billion this year. Much of the reduction in supply of short-term tax-exempt securities resulting from the cancellation of HUD project notes seems to have been offset by the surge in "puttable" bonds. The increased supply of these issues helps explain why yields on shorter-term tax and revenue anticipation notes, with 3- and 6-month maturities, have fallen only 25 to 35 basis points since early summer. Unable to buy HUD notes, investors have not had to purchase these TANs and RANs for short-term placements, but rather have been able to pick up the variable-rate bonds.

It is not clear whether uncertainties about tax reforms are having a significant effect on the municipal bond market. One Treasury proposal that might reduce the demand for tax-exempt bonds is a cut in the top marginal tax rate. Other elements of the Treasury plan, including the elimination of alternative tax shelters and restrictions on eligible issuers of tax-exempt debt, might work in the opposite direction.

Mortgage Markets

Interest rates have dropped further since early November on borrowing secured by home mortgages, as well as on short-term construction funds. In the primary market for permanent financing, average contract interest rates on new commitments at S&Ls for conventional fixed-rate home mortgages declined 65 basis points during November; the decrease from the early August high has cumulated to 1-1/2 percentage points. The nominal interest rate on this dominant type of fixed-rate mortgage instrument--averaging 13.2 percent during the week ending December 7--was equal to its 1984 low, registered in February.

On FHA-insured fixed-rate home mortgages, the effective yield on new commitments at mortgage companies also has retreated. With price discounts on GNMA-guaranteed securities issued against pools of FHA/VA loans falling to minimal levels, the Administration cut the ceiling rate on VA-guaranteed loans by 1/2 percentage point, effective November 21, the second such action within a month. On VA-guaranteed loans bearing the new 12-1/2 percent coupon rate applicable to level-payment mortgages, discounts have recently averaged around 3 points.

At S&Ls, initial interest rates on conventional adjustable-rate mortgages (ARMs) have declined during the past four weeks about as much as average costs of fixed-rate credit. The average interest rate differential favoring one-year ARMs over fixed-rate loans at these institutions thus has continued to exceed 200 basis points since early November. At that time, ARMs were accounting for 61 percent of all conventional home loans closed at major originators--down somewhat from the high in

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

	Mortgage commitments		Net change in mortgage assets		
	New (1)	Outstanding[2] (2)	Total (3)	Mortgage loans (4)	Mortgage-backed securities (5)
1983-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. r	14.3	65.2	5.0	5.0	*
Oct. p	14.6	64.4	4.8	4.8	*

p--preliminary. r--revised.
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.
* Less than .1.

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	1638
Q2	4020	2343	1133	545	1497
Q3	5130	2206	1428	1496	2659
July	5438	2325	1580	1533	2576
Aug.	5799	2373	1564	1862	3317
Sept.	4153	1921	1140	1092	2085
Oct.	6144	2473	2560	1111	3392
Nov. p	5154	1432	2322	1400	2913

p--preliminary.

early August, when the ARM initial interest rate differential was wider, a larger share of ARMs was being discounted, and ARM credit and insurance standards were less stringent.

Because of the recent cuts in the bank prime rate, credit costs have declined on many new and outstanding residential construction loans. More than two-thirds of construction and land development loan extensions by insured commercial banks during the week of November 5 to 9 carried floating rates, according to the latest quarterly survey of terms of bank lending.

Mortgage credit demand appears to be firming in response to lower interest rates. During October, new commitments at S&Ls--which had declined during each of the preceding four months--rose nearly 2 percent to $14.6 billion, according to preliminary data for insured institutions. With mortgage closings rising, commitments outstanding dipped further, to about 4 percent below the June high.

New issues of federally guaranteed mortgage pass-through securities--typically backed by fixed-rate loans--climbed in October to more than $6 billion, the largest volume in a year. Preliminary data show somewhat less strength in November, owing to a sharp drop in new GNMA issues.[1] Issuance associated with mortgage swapping--usually with S&Ls and banks--strengthened at FNMA and FHLMC in both months.

Consumer Credit

Consumer installment credit outstanding rose at an estimated 16-3/4 percent seasonally adjusted annual rate in October, the first

1. Of the three federally sponsored housing credit agencies, only FNMA so far has issued large amounts of ARM pass-through securities. The GNMA ARM pass-through security program has been slow in evolving; several applications for GNMA guaranty have been filed, and a small amount of securities was issued in November.

CONSUMER INSTALLMENT CREDIT

	1983	1984 Q2	1984 Q3	1984 Aug.	1984 Sept.	1984 Oct.
	----- Percent rate of growth, SAAR -----					
Change in outstandings--total	11.3	24.1	16.2	16.5	11.6	16.8p
By type:						
Automobile credit	8.7	23.8	16.7	13.4	9.8	17.4p
Revolving credit	15.5	31.2	15.2	18.1	18.0	20.0p
All other[1]	10.1	21.3	16.2	18.3	10.2	15.2p
	------- Billions of dollars, SAAR ------					
Change in outstandings--total	48.3	97.9	69.5	72.0	51.4	75.3p
By type:						
Automobile credit	13.6	35.0	26.1	21.3	15.8	28.3p
Revolving credit	12.9	25.0	13.1	15.8	15.9	18.0p
All other[1]	21.7	37.9	30.4	34.9	19.7	29.0p
By major holder:						
Commercial banks	23.4	55.7	28.8	31.6	16.6	25.9p
Finance companies	5.0	9.2	14.9	13.3	14.4	20.5p
All other	19.9	33.0	25.9	27.1	20.3	28.9p
	-------- Annual percentage rate --------					
Interest rates						
At commercial banks[2]						
New cars, 48 mos.	13.92	13.53	13.91	14.08	n.a.	13.91[4]
Personal, 24 mos.	16.50	16.35	16.63	16.75	n.a.	16.63[4]
Credit cards	18.78	18.71	18.82	18.81	n.a.	18.82[4]
At auto finance companies[3]						
New cars	12.58	14.15	14.95	15.01	15.16	15.18
Used cars	18.74	17.61	17.95	17.99	18.10	18.19

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.
4. Data shown are for November 1984.
n.a.--not available.
p--preliminary.

acceleration after four straight months of slowing growth. Commercial bank data suggest further strength in November.

By early November, consumer interest rates at commercial banks had turned down a bit from their August levels, but they remained substantially above a year earlier. On new cars, the most common rate on 48-month loans, 13.91 percent, was down 17 basis points from August but still 45 basis points above the November 1983 rate. At finance companies, by comparison, interest rates edged up a trifle to 15.18 percent in October--also well above the year-earlier levels. As a result, rate relationships between banks and finance companies for this type of credit have been returning to a more normal spread. In the 1970s bank rates often were about 200 basis points below those at finance companies, but from 1980 through mid-1983 they were generally higher, as auto finance companies offered occasional interest rate rebate/reduction programs and banks were scarcely competing in this area. Since mid-1983, however, banks have been aggressively pushing auto loans and the earlier rate relationship has been re-emerging. The most recent Federal Reserve survey of senior loan officers, taken in November, showed banks again reporting an increased willingness to make consumer loans.

There also has been a widening of spreads between various consumer loan rates and market interest rates recently. Compared with the rate on three-year Treasury notes, for example, new-car loans at banks carried a 3 percentage point markup in November, larger than last spring or a year earlier. Apparently, the recent widening of these spreads is the result of a tendency toward a more normal relationship; over the 1972-83 period the average auto loan spread was 360 basis points.

APPENDIX A*

MONEY AND CREDIT GROWTH IN 1984

The monetary and credit aggregates have grown at substantially disparate rates in 1984, with M1 and M2 increasing much less rapidly than M3 and domestic nonfinancial debt. Money and credit expansion occurred against a backdrop of a very brisk increase in economic activity over the first half of the year followed by a marked slowing, and rising money market rates of interest through much of the spring and summer preceding sharp declines. In addition, the surge in merger activity in 1984 boosted debt growth and bank issuance of managed liabilities. Unlike 1983 and some other recent years, there were no major deregulation measures and thus distortions from this source likely diminished.

M1 and M2 through November have expanded within their target ranges of 4 to 8 percent and 6 to 9 percent, respectively. Through the first half of the year M1 was mostly in the upper half of its range, but growth since June has been sluggish, leaving it at the lowest quartile.[1] M2 has generally been in the lower half of its range, with the November surge pulling this measure near the midpoint. In contrast, M3 and debt have run consistently above the upper ends of their ranges.

M1

The path of transactions balances has been influenced by swings in output growth and interest rates over the year. The rapid growth of output boosted M1 growth over the first half of the year, while the rise in interest rates through mid-summer and the slowdown in economic activity tended to damp expansion in this measure into the fall. Over the first three quarters of the year, M1 demand was in line with predictions of standard money demand models, but more recently it appears to be well below model predictions. For the year as a whole, M1 velocity is likely to rise about 4 percent.

The growth rates of the components of M1 have followed patterns similar to the aggregate, weakening in the second half of the year. OCD has continued to be the strongest component, but it has not dominated overall M1 growth to the extent seen in 1982 or 1983. Growth of the number of ATS/NOW accounts outside the Northeast slowed to an 8 percent annual pace through the third quarter, consistent with the end of significant net shifting into these accounts. The OCD component has increased from 17 percent of M1 in December 1981 to 21 percent in December 1982, and to 25 percent in December 1983, but its share has since risen only slightly. Demand deposits expanded at about a 4 percent annual rate in the first half of the year but, on balance, have declined a bit since June.

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* Prepared by Paul O'Brien, Economist, Banking Section, Division of Research and Statistics.

1. Concurrent seasonal adjustment using the X-11 ARIMA procedure suggests that underlying growth may have been in the neighborhood of 1/2 percentage points slower in the first half of the year and 1/2 percentage point faster in the second half, mainly in the fourth quarter.

M2

The growth of M2 was, until recently, much steadier. Its nontransactions components grew at about a 7 percent annual rate in each of the first three quarters of this year, but likely will expand more rapidly in the fourth quarter. M2 velocity expanded briskly during the first half of the year--at about a 5 percent annual rate--but it was roughly unchanged in the third quarter. The sluggishness of M2 in the first half of the year, despite higher growth in nominal income and credit, may have reflected both the observed reluctance of depository institutions to match rising market rates with comparably higher rates on retail deposits and inflows to IRA/Keogh accounts, which are excluded from the monetary aggregates. The rebound of M2 growth in the fourth quarter is in part due to relatively more favorable yields on M2 deposits and money market mutual funds as such yields have lagged market rate declines.

There have been substantial variations in growth of the various nontransactions M2 components over the year, reflecting rate relationships. Nontransactions M2 deposits were much weaker when bank and thrift offering rates lagged market rate increases during the spring, but they recovered when market rates declined more swiftly after mid-summer. Another effect seems to stem from the slope of the bank deposit yield curve. During the January through March period, the yield curve of commercial bank offering rates was relatively flat, and commercial bank MMDAs surged more than $14 billion while commercial bank small time deposits--after adjustment for IRA/Keogh deposits--stagnated. Yet in those months the bank rate-market rate gap favored longer-term deposits. Between June and August, the yield curve of bank offering rates steepened considerably, small time deposits rose rapidly, and MMDAs declined. At that time, however, the gap between market rates and bank offering rates was much greater for small time deposits than for MMDAs. Thrift institutions have generally set a steeper yield curve with their offering rates, stimulating relatively stronger growth of small time deposits and net runoffs of MMDAs.

M3

The much more rapid expansion of M3--at a 10 percent annual rate from the fourth quarter of 1983 through November--reflected very rapid credit growth at depository institutions and heavy issuance of large time deposits. Credit growth has been especially strong at thrift institutions and their issuance of large time deposits exceeded 30 percent at an annual rate in nine of the first eleven months of the year. The outstanding volume of thrift large time deposits declined in September, owing to a runoff of large CDs at the troubled American Savings and Loan subsidiary of the Financial Corporation of America, but resumed rapid growth in October and November. In response to record levels of mortgage lending in the spring and summer, thrift institutions supplemented core deposit growth with other managed liabilities as well, particularly term RPs and FHLB advances.

Commercial bank credit was especially strong in the first half of the year, but issuance of large time deposits was primarily concentrated in the March to July period. Bank CD issuance in the early part of the year probably was restrained by borrowings from foreign offices. About $15 billion was raised over the first five months; however, some of this inflow was reversed shortly thereafter--the result of large advances by Continental Illinois Bank to its foreign offices and an easing of borrowings by other commercial banks. Bank credit growth tapered off after June as did large time deposit growth. More recent fluctuations in bank large CD issuance have stemmed to some extent from swings in Treasury balances.

Institution-only money market mutual funds grew slowly through much of the year, but have risen sharply in October and November as their dividend rates declined less than money market rates. Term RPs have shown a net increase of about $13 billion through November; about $9 billion of this has been by thrift institutions. Term Eurodollars, which had grown rapidly in recent years, were flat through May but then began to decline. Rate premiums on Eurodollar deposits had dropped in late 1983, and Continental-inspired concerns about the banking system may have introduced doubts about the relative safety of offshore deposits.

Total Credit

Domestic nonfinancial sector debt has grown at a 13 percent annual rate through October, keeping this aggregate consistently above its monitoring range. While growth of nonfinancial debt has certainly been supported by very heavy federal borrowing, many private debt components also have shown significant strength. Business borrowing was boosted by the wave of corporate mergers and acquisitions. Net retirement of corporate equities during 1984 has been about $70 billion. Allowance for this amount would imply debt growth closer to the 11 percent upper end of its monitoring range.

MONETARY AND CREDIT AGGREGATES
(Q4 to Q4 averages, seasonally adjusted unless noted otherwise)

Growth rates or flows	1980	1981	1982	1983	1984[1]	Levels in billions of dollars Oct. 1984
Growth rates (percent)						
M1	7.4	5.1[2]	8.7	10.0	5	545.5
M2	9.0	9.3	9.5	12.1	7.5	2317.2
M3	9.6	12.4	10.6	9.7	10	2916.2
Domestic nonfinancial debt[3]	9.5	10.0	9.1	10.8	13.1	5795.4
Bank credit[4]	8.0	8.8	7.8	10.3	10.6	1696.8
Thrift credit[5,6]	7.4	4.2	2.3	16.8	16.2	1108.5
Flows ($ billions)						
M1	28.3	21.3	38.0	47.4	26	
Currency	10.0	7.0	10.3	13.9	12	157.2
Demand deposits	8.3	-33.9	2.4	5.6	1	243.8
Other checkable deposits	10.0	48.2	25.3	27.9	13	139.6
M2	134.2	151.4	169.5	235.2	163	
Nontransactions-M2	105.5	130.0	131.2	187.7	137	1771.8
MMDAs (NSA)[7]			14.3	358.8	24	386.8
Savings deposits	-18.5	-66.9	18.5	-47.2	-19	297.4
Small time deposits	88.2	110.6	44.2	-86.2	107	885.0
General purpose and broker/dealer money market mutual fund assets (NSA)	31.0	81.4	44.5	-49.4	24	155.5
Overnight RPs and Eurodollars (NSA)	5.7	5.7	10.8	11.2	1	56.8
M3	172.9	244.2	233.8	236.7	268	
Non-M2 component	38.7	92.8	64.4	1.4	105	598.9
Institution-only money market mutual fund assets (NSA)	7.1	19.3	16.5	-8.6	15	52.2
Large time deposits (NSA)	28.0	52.2	31.1	-11.8	84	400.9
Term RPs (NSA)	2.3	2.5	3.3	12.8	17	66.4

1. Monetary aggregates and bank credit data for 1984 are through November, domestic nonfinancial debt data are through October, and thrift credit data are through the third quarter.
2. The rate of M1 growth in 1981 adjusted for shifts of non-M1 funds into NOW accounts was 2.5 percent.
3. Based on month average data.
4. Bank credit data for 1981 and after are adjusted for shifts of assets into IBFs.
5. Based on end-of-period data.
6. Level for the end of September.
7. MMDAs were authorized on December 14, 1982.

Foreign Exchange Markets

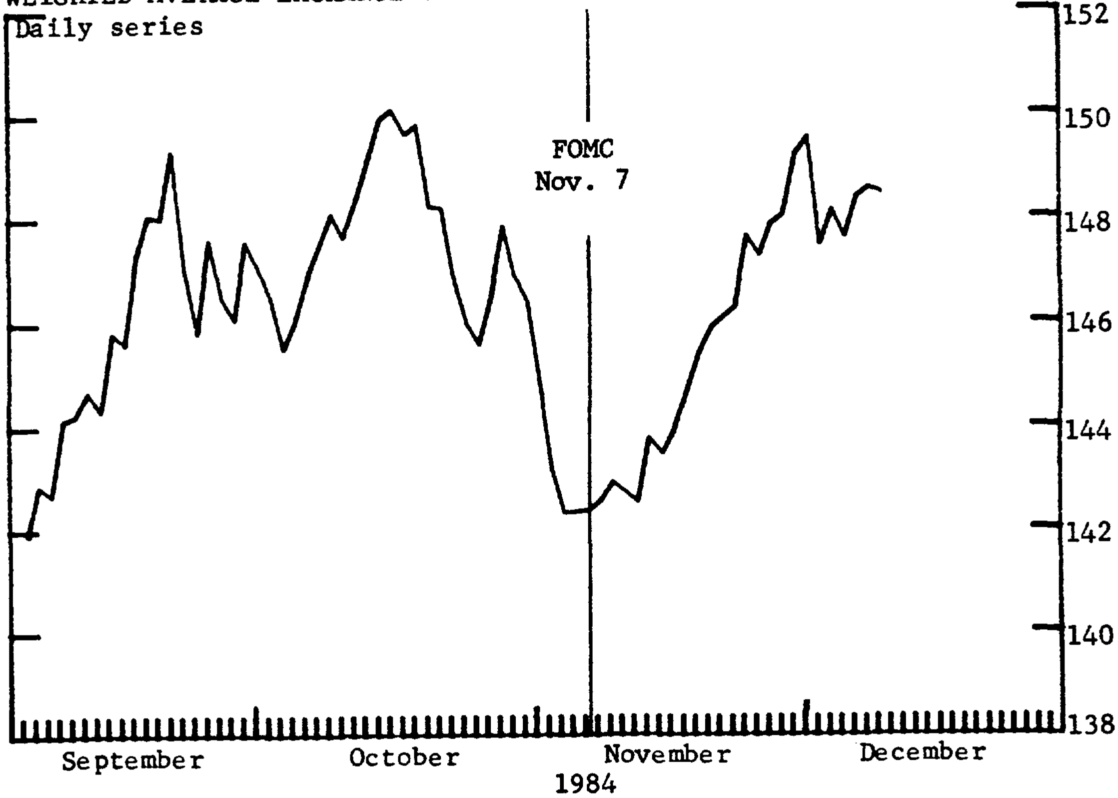
Since the last FOMC meeting, the trade-weighted value of the dollar has rebounded by nearly 4-1/2 percent. It now stands only 1 percent below its mid-October peak. The dollar's strength has been surprising in light of economic developments in the intermeeting period. Incoming data on U.S. economic activity have until very recently proven weaker than most market participants expected, while reports on foreign activity have perhaps been stronger than expected. Dollar interest rates have registered some further decline relative to foreign rates.

The improvement in the U.S. trade balance in October appeared to provide some support to the dollar. In addition, market commentary on the dollar's rise noted an emerging belief that dollar interest rates may have bottomed out and might be headed upward. This view is consistent with the recent steepening of the Treasury yield curve. Furthermore, market participants expressed the expectation that foreign interest rates would come down if dollar interest rates maintained or extended their declines.

Interest rates in Canada and in most European markets did ease somewhat during the intermeeting period. Central bank actions included three cuts totalling 1 percent in the Bank of England's money-market dealing rates. Around mid-November, the Bundesbank provided liquidity to the German market at a reduced rate of interest in what was perceived in the market as a tentative move toward ease. However, an easing came into doubt as the mark continued to weaken and as the Bundesbank's next domestic operation proved less generous than the market expected,

Chart 1 12/12/84

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



whereupon German domestic short-term interest rates retraced a portion of their earlier declines.

Italian money-market interest rates did not move lower until late in the intermeeting period and did so then without an active push from the Bank of Italy. The Bank's discount rate remains at the higher level established early in September. Comparatively firm interest rates, favorable inflation news, strong third-quarter growth, and ongoing economic reform likely account for the lira's gains of about 1-1/2 percent vis-a-vis the other EMS currencies over the intermeeting period.

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. Visible Bundesbank sales of dollars have on several occasions induced sharp but transient declines in the mark/dollar rate.

U.S. banks' foreign lending in the third quarter. Gross claims of U.S.-chartered banks on foreigners declined by nearly $22 billion (five percent) between end-June and end-September. It appears that as much as about $9 billion of the decrease may have reflected the effect of the appreciation of the dollar during the quarter (more than eight percent on a weighted average basis) on the $110 billion end-June stock of nondollar-denominated claims at foreign branches. The overall decline in claims can be ascribed largely to U.S. banks' desire to improve capital/assets ratios. Three-fourths of the total decrease was in claims on G-10 countries and offshore banking centers, principally interbank placements. Reductions in claims on other areas were relatively small; claims on non-OPEC developing countries fell $1.9 billion.

Large declines in total claims on foreigners were recorded at both the U.S. offices and the foreign branches. Claims on banks (excluding intrabank claims) held by the foreign branches were drawn down by nearly $7 billion, while foreign branch claims on nonbank foreigners fell another $7 billion; at the U.S. offices the decline in foreign claims was largely in the interbank area.

The $1.9 billion drop in claims on non-OPEC developing countries can be fully accounted for by reductions in claims on Korea, Taiwan and the Philippines. Claims on Latin America as a whole were little changed. Claims on Brazil rose $0.9 billion, more than can be accounted for by the U.S. banks' share (about $0.3 billion) of Brazil's September drawing of $875 million on the bank term loan signed in February. Claims on Mexico decreased $0.6 billion even though they tended to be increased by the U.S. banks' share (about $350 million) of Mexico's September drawing

TABLE 1. CLAIMS ON FOREIGNERS OF U.S.-CHARTERED BANKS
(Billions of dollars)

Claims on:	Change (no sign = increase) 1983 Year	1983 Q3	1983 Q4	1984 Q1	1984 Q2	1984 Q3	Outstanding 9/30/84
Total, all countries	-0.7	-7.9	6.0	-4.0	-3.7	-21.7	408.6
Non-OPEC developing countries	4.4	1.0	-1.7	0.5	1.8	-1.9	111.9
OPEC countries	1.5	-1.1	1.7	-0.3	-1.9	-1.8	24.9
Eastern Europe	-0.9	-0.5	..	-0.1	..	-0.3	4.6
Smaller developed countries	2.4	-0.2	1.8	-0.4	1.4	-0.8	36.3
G-10 countries	-11.5	-8.2	-0.9	-2.5	-7.9	-9.2	148.6
Offshore banking centers	4.3	0.3	1.7	-0.4	2.1	-7.2	65.6
Miscellaneous	-0.9	0.7	0.1	-0.6	0.9	-0.5	16.8

TABLE 2. CLAIMS OF U.S.-CHARTERED BANKS ON NON-OPEC DEVELOPING COUNRIES
(Billions of dollars)

Claims on:	Change (no sign = increase) 1983 Year	1983 Q3	1983 Q4	1984 Q1	1984 Q2	1984 Q3	Outstanding 9/30/84
Latin America	2.6	1.3	0.3	1.5	0.9	0.3	77.6
Argentina	0.6	0.1	..	..	-0.3	-0.1	9.1
Brazil	0.2	0.4	..	2.0	0.3	0.9	26.3
Chile	0.1	0.5	0.1	0.1	0.2	0.4	7.1
Colombia	0.1	..	..	-0.1	-0.1	-0.1	2.9
Mexico	1.6	0.6	0.2	-0.5	1.1	-0.6	26.1
Peru	-0.2	-0.2	..	-0.1	..	-0.1	2.2
Others	0.2	-0.1	..	0.1	-0.3	-0.1	3.9
Asia and Africa	1.8	-0.3	-2.0	-1.0	0.9	-2.2	34.3
Korea	0.5	..	0.5	-0.3	0.1	-1.1	10.1
Philippines	-0.1	-0.2	..	0.5	-0.4	-0.4	5.9
Taiwan	..	0.1	0.1	-0.4	0.9	-0.6	5.2
Others	1.4	-0.2	-2.6	-0.8	0.3	-0.1	13.1
Total	4.4	1.0	-1.7	0.5	1.8	-1.9	111.9

of $950 million on the bank term loan signed in April. The fall in claims on Mexico may have resulted from repayments or bank write-offs of debts of private Mexican borrowers. Of the $1.8 billion decrease in claims on OPEC countries, $1 billion was in claims on Middle Eastern countries and $0.5 billion in claims on Venezuela.

U.S. Capital Accounts

Since late October, four issues of U.S. government or agency foreign-targeted notes (FTNs) have been introduced into the Eurobond market -- two $1 billion auctions by the U.S. Treasury, a $300 million issue by FNMA and a $200 million issue by FHLB. The annualized rate differential between the U.S. Treasury FTN and the companion domestic bond was 32 basis points in the first issue, but only 7 basis points in the second issue. For the FNMA and FHLB issues there are no domestic companion issues from which to calculate interest savings.

The FTNs are designed to tap the Euromarket funding source by preserving anonymity for foreign investors while making the bond unattractive to U.S. tax evaders via the certification requirement. However, unlike standard Eurobonds, the FTNs are not true bearer instruments, nor do they indemnify the bond holder against changes in U.S. tax law. A greater market appreciation of these negative characteristics may explain the smaller rate differential and the lower degree of oversubscription distinguishing the second foreign-targeted Treasury auction. Part of the explanation however may reflect timing; evidence from the corporate bond market suggests that the degree to which Euromarket financing is advantageous varies over time with changes in the LIBOR-Treasury bill spread and with the changes in exchange rate expectations that can influence the relative value of annual versus semi-annual coupons. The Treasury's simultaneous auction of domestic and foreign-targeted notes that is decided well in advance prevents the Treasury from taking advantage of such timing windows. In addition the Euromarket's increased familiarity with the Treasury yield-auction technique probably reduced the skew in the distribution of accepted bids, thus lowering the average spread over the interest rate on the domestic bonds.

Guidance from the corporate bond market on where rate differentials between domestic and Euro-Treasuries are likely to equilibrate over time is limited by the narrowing range of comparable domestic and Euromarket instruments and by the falling percentage of corporate Euromarket instruments that are conventional fixed-rate bonds. From September to November, the percentage of fixed-rate issues (by value) in the Eurobond market fell from 45 to 6 percent, compared with a November figure of 47 percent for the domestic market. U.S. firms increasingly issue Eurobonds with novel features designed to exploit the foreign currency and interest rate preferences of Euromarket participants.

Among these new instruments are Savings and Loan collateralized Eurobonds. This debt has been issued in two distinct phases distinguished by the characteristics of the instruments and corresponding to changes in the regulatory environment. The U.S. Treasury caused the hiatus when, in advance of its own auction of foreign-targeted notes, it disallowed the bearer form for instruments collateralized by U.S. government securities or agency obligations. Prior to that August ruling, the Netherlands Antilles affiliates of six S&Ls and one state agency raised $875 million via fixed-rate, bearer, tax-indemnified notes collateralized by mortgages guaranteed by GNMA, FNMA, FHLMC or by U.S. Treasury bonds. Since August, S&L issues in the Euromarket comprise three types of foreign-targeted notes (a fixed-rate bond, a zero-coupon bond, and a floating-rate note) all with tax indemnification and collateralized by U.S. securities or GNMA, FNMA, or FHLMC obligations; in addition, a bearer, fixed-rate, tax-indemnified instrument was issued with a collateral pool of mortgage bonds, CDs, BAs, and cash. The volume of debt since August totals $475 million, bringing outstanding collateralized S&L Eurodebt to $1.4 billion as of November.

Apparently the institutional investor, predominant in the floating rate market, is attracted by the collateral and the quasi U.S. government guarantee and is not dissuaded by the foreign-targeted (as opposed to bearer) form of the instrument. S&Ls therefore find it cheaper to raise long-term funds by issuing LIBOR based floating-rate obligations in the Euromarket and using interest rate swap contracts to hedge against both the maturity risk and the rate risk associated with the mismatching of the term structure and interest rate basis of their assets and liabilities.

Another development in the Eurobond market is the increased use of floating rate notes (FRNs) for bank funding -- $3.5 billion in the five months July through November compared with $0.4 billion in the first six months of 1984; bank Euronotes issued in 1984 total $7.9 billion. Over 50 percent of the FRN proceeds raised by banks or bank holding companies is in the form of bank equity commitment notes or equity contract notes. Both instruments augment banking organizations' primary capital under current Federal Reserve and Comptroller capital guidelines, although there is a maximum percent of primary capital that can be held in this form.

The first non-dollar bond issue has just been introduced into the U.S. domestic financial market. (The U.S. Treasury, in a 1982 statement, opened the domestic market to foreign currency issues.) The European Economic Community floated the fixed rate, 12 year, 200 million ECU bond. While the ECU is well established in the Eurobond market, the recent Euromarket funding of ECU-denominated loans and the successful issue in the U.S. domestic market signals both a wider acceptance of the ECU and a demand by investors for registered foreign currency issues.

The Summary Table on U.S. International Transactions shows that U.S. banking offices reported a $14 billion net capital inflow in the third quarter vis-a-vis unaffiliated foreigners in contrast to a $2 billion net outflow in the second quarter (line 1b). The bulk of the inflow ($12 billion) represents a reduction in net claims on unaffiliated foreign banks in significant part by U.S.-chartered banks. The Euro-interbank deposit rundown was associated with a narrowing of the interest differential favoring Euromarket deposits over Treasury bills.

As shown in the International Banking Data Table, net inflows have also been occurring through reductions in U.S. non-bank holdings of Eurodollar deposits (line 5) which fell $4.8 billion further in October to a level of $115.2 billion. Heightened concerns about bank failures, along with oil-merger financing and cash management, account for some of the downward trend in these deposits. However, notably in contrast to the net inflows induced by the relative strength of economic activity and credit demands in the United States, some of the reduction in non-bank holdings of Eurodollars appears to reflect deposit withdrawal by sectors of the U.S. economy facing relatively weak product demand, in particular the oil and gas extraction, primary metals, and non-electric machinery industries.

September data show net private foreign sales of U.S. Treasury obligations of $3.4 billion. (See the Summary Table, line 3.) Active World Bank portfolio managers sold $3.2 billion of U.S. Treasury bills, accounting for the bulk of the amount. The September data contrast sharply with large August net purchases associated with bearer Euro-CATS (since disallowed by the Treasury regulations on bearer instruments).

Foreign official reserve holdings in the United States (line 4) declined by $3.8 billion in September. Substantial outflows from the accounts of Germany, the Netherlands, and OPEC outweighed net inflows for Italy. Official dollar sales by the Bundesbank, combined with the oil glut's effect on OPEC holdings help explain the September data. Over the third quarter as a whole, net foreign official reserve holdings in the United States were essentially unchanged. Preliminary data for October covering official holdings at the FRBNY show an increase of $2.2 billion, primarily in OPEC RPs.

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

	1982 Year	1983 Year	1984 Q1	1984 Q2	1984 Q3	1984 July	1984 Aug.	1984 Sept.
Private Capital								
Banks								
1. Change in net foreign positions of banking offices in the U.S. (+ = inflow)	-39.5	13.3	13.0	-0.6	9.1	-2.2	4.1	7.3
a) with own foreign offices	-8.9	7.0	*	1.3	-4.9	-7.0	1.0	1.1
b) all other	-30.6	6.4	13.0	-1.8	14.1	4.8	3.1	6.2
Securities								
2. Private securities transactions, net	-1.6	1.7	2.2	-0.2	0.4	0.2	0.2	*
a) foreign net purchases (+) of U.S. corporate bonds	2.8	2.2	0.3	0.6	2.7	0.4	0.9	1.4
b) foreign net purchases (+) of U.S. corporate stocks	3.6	6.4	1.2	*	-1.0	-0.5	0.1	-0.6
c) U.S. net purchases (-) of foreign securities	-8.0	-6.9	0.6	-0.8	-1.3	0.3	-0.8	-0.8
3. Foreign net purchases (+) of U.S. Treasury obligations 1/	6.5	8.3	1.4	6.6	5.1	2.5	6.1	-3.4
Official Capital								
4. Changes in foreign official reserve assets in U.S. (+ = increase)	2.9	5.2	-3.0	-0.7	-0.8	0.2	2.8	-3.8
a) By area								
G-10 countries (incl. Switz.)	-12.7	6.4	2.3	-0.7	-0.6	-0.9	2.4	-2.1
OPEC	6.9	-8.5	-2.8	-2.4	-0.7	1.6	-1.4	-0.[illegible]
All other countries	8.8	7.3	-2.5	2.3	0.5	-0.5	1.7	-0.7
b) By type								
U.S. Treasury securities	5.7	7.0	-0.2	-0.3	-0.6	-1.8	2.6	-1.4
Other 2/	-2.7	-1.8	-2.7	-0.5	-0.2	2.0	-0.2	5.1
5. Changes in U.S. official reserve assets (+ = decrease)	-5.0	-1.2	-0.7	-0.6	-0.8	-0.4	-0.3	-0.1
Other transactions (Quarterly data)								
6. U.S. direct investment (-) abroad	4.8	-4.9	-3.5	1.9	n.a.	n.a.	n.a.	n.a.
7. Foreign direct investment (+) in U.S.	14.9	11.3	2.4	7.7	n.a.	n.a.	n.a.	n.a.
8. Other capital flows (+ = inflow) 3/ 4/	-6.7	-2.9	1.9	-4.5e	n.a.	n.a.	n.a.	n.a.
9. U.S. current account balance 4/	-9.2	-41.6	-19.7	-24.4	n.a.	n.a.	n.a.	n.a.
10. Statistical discrepancy 4/	32.9	9.3	6.0	7.8e	n.a.	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	-25.9	-25.7	-32.9	-13.9	-8.5	-10.5

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 a 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.

INTERNATIONAL BANKING DATA
(Billions of dollars)

	1981	1982	1983				1984				
	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Oct.	Nov. 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	30.2	23.3	27.4
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	6.3	11.0	7.1
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	36.5	34.3	34.5
(a) U.S.-chartered banks	22.3	40.0	53.7	49.9	48.7	40.8	36.9	34.7	35.7	34.6	33.8
(b) Foreign-chartered banks	-2.6	9.1	10.0	6.5	5.9	3.7	2.5	1.9	.7	-.3	.7
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	20.2	19.8	20.9
5. Eurodollar Holdings of U.S. Nonbank Residents 2/	95.5	112.6	116.4	120.4	121.3	126.4	128.0	123.2	120.0	115.2	113.1

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 November 26.

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 October, the U.S. merchandise trade deficit was substantially less than in September and considerably smaller than the deficit for the third quarter as a whole, largely because of a reduction in imports.

Imports in October dropped back to a level well below the average for the third quarter. There were declines from third-quarter levels in a wide range of machinery items and industrial supplies (including steel). Decreases were also recorded for new passenger cars from Japan, consumer goods (especially clothing and footwear) and agricultural imports. Nonetheless, the level of imports in October was still substantially higher than recorded a year ago, reflecting the strong expansion of economic activity in the United States and the continued appreciation of the dollar.

U.S. MERCHANDISE TRADE[1/]

	1983	1984	1984				
	Year	10 mos.	Q1	Q2	Q3r	Sept.r	Oct.
Value (Bil. $, SAAR)							
Exports	200.3	218.7	215.7	218.4	221.5	218.9	219.9
Agricultural	36.6	37.7	41.2	37.1	35.9	37.4	34.5
Nonagricultural	163.6	181.0	174.5	181.3	185.6	181.5	185.3
Imports	261.3	329.8	319.2	321.3	353.1	344.4	317.4
Oil	53.8	57.8	55.4	59.6	57.9	53.6	59.2
Non-oil	207.5	272.0	263.8	261.7	295.2	290.8	258.3
Trade Balance	-61.1	-111.1	-103.5	-102.9	-131.6	-125.5	-97.5
Volume (Bil 72$, SAAR)							
Exports							
Agricultural	16.3	15.8	17.0	15.1	15.3	16.3	15.4
Nonagricultural	57.3	62.7	60.6	62.7	64.4	62.7	63.6
Imports							
Oil	4.9	5.4	5.1	5.5	5.4	5.0	5.6
Non-oil	81.9	104.4	102.3	100.3	112.7	110.7	98.1

r/ Revised.
1/ International transactions and GNP basis.

The only major category of imports that did not decline in October from its third-quarter level was oil. The volume imported was marginally higher than the average rates for both the second and third quarters; domestic consumption of crude oil has increased steadily during the year, and inventories, after being drawn down in the third quarter, were boosted a little in October. While the average price of oil imports in October was about the same as in September, the price was about 25 cents per barrel less than in the third quarter. After firming in September and early October, spot market prices dropped sharply in mid-October, primarily for light crude oil; during November and early December, part of the decline was reversed.

OIL IMPORTS

	1983		1984				
	Year	Q4	Q1	Q2	Q3	Sept.	Oct.
Volume (mbd, SA)	5.20	5.53	5.40	5.76	5.66	5.31	5.85
Price ($/BBL)	28.42	28.30	28.05	28.26	27.91	27.62	27.64
Value (Bil. $, SAAR)	53.80	57.14	55.41	59.61	57.85	53.64	59.16

Exports in October were close to the average for the third quarter as a whole. An increase in machinery exports in October from third-quarter levels was offset by declines in exports of passenger cars to Canada, aircraft, industrial supplies (especially coal) and agricultural commodities. For the entire July-October period, the volume of nonagricultural exports expanded to a rate that was 5 percent higher than that recorded in the first half of the year; this increase largely reflected a gradual strengthening of economic activity in major trading partners.

The volume of agricultural exports in the July-October period continued to be influenced by strong shipments of wheat and feedgrains to the USSR, which had a very poor grain harvest. However, demand for U.S. products from the rest of the world remained weak, as many foreign buyers awaited the results of their own harvests (which turned out to be very good) and as the high value of the dollar continued to make it difficult for U.S. agricultural producers to remain price-competitive with foreign producers.

Foreign Economic Developments. Economic expansion in the major foreign industrial countries has been continuing at a moderate, though uneven, pace. Real activity in Germany has recovered strongly following the strike-related slump of the summer, with real GNP growing by just over 10 percent (s.a.a.r.) in the third quarter. Part of the increase in third quarter Canadian real GNP growth, to nearly 8 percent (s.a.a.r.), reflected a temporary increase in production in advance of the September and October auto strikes. In both France and Italy real GDP growth in the third quarter increased to about 4 percent (s.a.a.r.) while the pace of real GNP growth in Japan slowed to 3 percent (s.a.a.r.). Activity in the United Kingdom has continued to be depressed by the coal strike, with real activity virtually flat in the third quarter. Unemployment rates have on balance held steady in recent months, remaining at or near record-high levels in Europe.

There continues to be no indication that expansion abroad has led to a rekindling of inflationary pressures. Indeed, inflation rates in recent months have either remained steady at low levels (in Japan and Germany) or shown further declines (in Italy, France and Canada).

Japan's cumulative current account surplus through October increased to $32 billion (s.a.a.r.), well above the record-high rate of last year. France's external deficits have continued to decrease while those of the United Kingdom have expanded in recent months, reflecting in large part the impact of the coal strike.

Individual Country Notes. Real GNP growth in Japan slowed to 3 percent (s.a.a.r.) in the third quarter from an upward revised 7.6 percent increase in the second quarter. Plant and equipment spending

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

	Q4/Q4	Q4/Q4	1983	1984			1984					LATEST 3 MONTHS
	1982	1983	Q4	Q1	Q2	Q3	JUNE	JULY	AUG.	SEP.	OCT.	FROM YEAR AGO+
CANADA												
GNP	-4.9	7.1	1.2	.8	.8	1.9	*	*	*	*	*	4.8
IP	-10.8	16.1	3.7	.6	.8	3.3	.6	3.6	-.6	-1.9	N.A.	8.5
FRANCE												
GDP	1.4	.6	.6	.9	-.5	1.0	*	*	*	*	*	2.0
IP	-1.8	1.8	.0	1.3	-1.0	2.8	-2.3	(4.6)		-3.7	N.A.	3.1
GERMANY												
GNP	-1.6	3.2	1.4	1.2	-2.1	2.5	*	*	*	*	*	3.0
IP	-5.4	6.0	3.0	.6	-4.7	5.6	-9.6	13.8	-1.8	-.4	2.3	3.4
ITALY												
GDP	-2.3	1.0	.6	.9	.7	1.1	*	*	*	*	*	3.3
IP	-6.7	1.7	.5	1.0	.5	1.9	.8	-1.2	1.5	1.1	N.A.	4.0
JAPAN												
GNP	3.8	3.6	.8	2.1	1.8	.7	*	*	*	*	*	5.5
IP	-2.7	8.6	2.9	3.2	2.8	1.5	.5	.3	.7	-1.0	2.9	10.4
UNITED KINGDOM												
GDP	1.8	4.1	1.4	.8	-.9	N.A.	*	*	*	*	*	2.6
IP	.1	4.8	1.3	.0	-2.6	-.4	.8	-1.1	.1	1.4	N.A.	-1.7
UNITED STATES												
GNP	-1.5	6.3	1.5	2.4	1.7	.5	*	*	*	*	*	6.2
IP	-7.5	15.0	2.5	2.7	2.1	1.6	1.0	.9	.1	-.5	.0	7.8

* 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 AUG.	1984 SEP.	1984 OCT.	1984 NOV.	LATEST 3 MONTHS FROM YEAR AGO
CANADA													
CPI	9.7	4.6	1.4	1.6	.9	1.2	.9	.9	.0	.1	.2	N.A.	3.6
WPI	4.5	3.5	1.5	.9	.4	1.6	1.2	.5	-.1	-.1	.1	N.A.	3.6
FRANCE													
CPI	9.5	9.8	2.8	2.1	1.9	1.7	1.8	1.7	.5	.5	.7	N.A.	7.1
WPI	8.5	14.6	4.0	3.7	3.6	3.4	2.9	2.1	.1	1.4	.2	N.A.	11.9
GERMANY													
CPI	4.7	2.7	.5	1.0	.5	.9	.5	.0	-.2	.1	.6	.1	1.9
WPI	3.1	.9	.8	.9	1.2	1.7	.8	-1.4	-1.4	.0	.9	N.A.	1.6
ITALY													
CPI	16.6	12.8	2.9	2.3	3.5	2.9	2.1	1.2	.3	.7	1.0	.6	9.0
WPI	12.4	9.1	1.6	2.3	3.3	3.2	2.2	1.2	.6	.9	N.A.	N.A.	10.3
JAPAN													
CPI	2.9	1.9	.9	-.2	1.4	.9	.6	-.2	-.8	1.6	.7	N.A.	2.5
WPI	1.6	-3.3	-1.0	.2	-.6	.1	-.1	.8	.0	.2	-.3	-.2	.5
UNITED KINGDOM													
CPI	6.2	5.1	2.0	1.3	1.1	.6	2.0	.9	.9	.2	.6	N.A.	4.9
WPI	6.5	5.6	2.0	.8	1.3	1.8	2.3	.6	.1	.5	.5	.3	6.1
UNITED STATES													
CPI (SA)	4.4	3.2	1.1	1.0	1.1	1.2	.9	.9	.5	.4	.4	N.A.	4.2
WPI (SA)	3.6	.9	.2	.6	.4	1.1	.3	.2	-.1	-.2	-.2	N.A.	1.7

December 12, 1984

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

	1982	1983	1983 Q2	1983 Q3	1983 Q4	1984 Q1	1984 Q2	1984 Q3	1984 JULY	1984 AUG.	1984 SEP.	1984 OCT.
CANADA												
TRADE	14.4	14.4	4.3	3.1	3.5	3.6	4.2	4.1	1.5	1.1	1.5	1.7
CURRENT ACCOUNT	2.1	1.4	1.1	-.2	.0	.0	.5	.5	*	*	*	*
FRANCE												
TRADE 2/	-14.0	-5.9	-1.7	-.6	-.2	-1.5	-1.1	.4	-.1	.4	.1	-.4
CURRENT ACCOUNT 2/	-12.1	-4.2	-.9	.3	.3	-.5	-1.0	.7	*	*	*	*
GERMANY												
TRADE	20.9	16.4	4.1	3.7	3.4	4.3	3.2	5.0	1.4	1.9	1.7	N.A.
CURRENT ACCOUNT (NSA)	3.5	4.1	.6	-2.3	3.7	.7	-.2	-.6	-.1	-.5	.0	2.1
ITALY												
TRADE	-12.8	-7.8	-1.4	-2.1	-1.3	-2.5	-3.0	-1.6	-.1	-.9	-.6	N.A.
CURRENT ACCOUNT (NSA)	-5.7	.6	1.1	1.5	-.1	-1.7	-1.0	N.A.	*	*	*	*
JAPAN												
TRADE 2/	18.8	31.2	7.8	8.5	8.2	10.0	11.1	10.1	3.4	2.8	3.9	4.0
CURRENT ACCOUNT	6.9	21.0	6.1	5.7	5.5	7.2	9.2	7.4	2.5	1.8	3.0	3.4
UNITED KINGDOM												
TRADE	4.1	-.8	-.7	-.4	-.0	-.2	-1.8	-2.1	-.3	-.8	-1.0	-1.0
CURRENT ACCOUNT 2/	9.6	4.4	-.1	1.2	.9	.5	-.5	-1.2	.1	-.5	-.7	-.1
UNITED STATES												
TRADE	-36.5	-61.1	-14.9	-17.5	-19.4	-25.9	-25.7	-32.9	-13.9	-8.5	-10.5	-8.1
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.

continued its rapid advance, rising by almost 10 percent (s.a.a.r.) in the third quarter. The rate of growth of private consumption rose to 3 percent, double the rate in the second quarter. However, the rate of growth of exports decelerated sharply, falling to 7 percent after a 21 percent rate of increase in the second quarter. Import growth surged to a 31 percent rate, compared with an 11 percent rate of advance in the second quarter, in part as a result of accelerated petroleum purchases ahead of a September increase in the tax on petroleum. Thus net exports made their first negative contribution to GNP since late 1981. Other indicators point to a continued healthy expansion. Industrial production jumped in October by 2.9 percent (s.a.) after a revised 1 percent drop in September. New construction orders in the third quarter rose by more than 18 percent (s.a.) on the strength of overseas and private domestic orders.

Wholesale price inflation remains close to zero. Most of the pickup of consumer price inflation in September and October reflects seasonal influences; consumer prices in October were 2.2 percent above their year-earlier level.

The cumulative trade surplus in the first ten months of this year was $42 billion (s.a.a.r.), compared with a surplus in the same period last year of $31 billion. This increase is reflected in a higher current account surplus, which rose from $21 billion (s.a.a.r.) in the first ten months of 1983 to $32 billion through October of this year.

The draft budget for FY 1985 (beginning April 1) is scheduled to be submitted to the cabinet on December 24. The outline of the budget calls for a 4 percent increase in both general account spending and in total revenue. The Finance Ministry has also concluded its outline of the Fiscal Loan and Investment Program; total outlays under this program in FY 1985 are slated to be unchanged in nominal terms from this fiscal year.

The Euroyen CD market was launched December 1 as expected. The maturity of Euroyen CD's is restricted to six months or less, and they may not be sold to Japanese residents.

Satoshi Sumita, the current Deputy Governor of the Bank of Japan, has been selected by the Prime Minister to be the Bank's new Governor. Following expected cabinet approval, Sumita will replace Governor Mayekawa, who is retiring, on December 16.

Industrial production in Germany increased by 2.3 percent (s.a.) in October after having retreated somewhat in August and September from the relatively high level associated with the rebound from the early summer metal workers' strike. The October level of industrial production was 4 percent above its year-earlier value. Real GNP growth in the third quarter was 10.3 percent (s.a.a.r.), also reflecting the rebound from the strike. This put third-quarter GNP about 3 percent above its level a year ago. Surveys on the business climate and data on order volumes suggest continuing strength, particularly in the export sector. The rate of unemployment, however, has remained unchanged at 9.2 percent (s.a.) through November.

The monthly rate of consumer price inflation was 0.1 percent (n.s.a.) in November after very low monthly advances during the preceding months. The November consumer price index was 2 percent above its level of November last year. There has, however, been a pickup in the pace of wholesale price inflation, particularly for imported goods, partly caused by the strength of the U.S. dollar.

The cumulative current account through October was in surplus by about $2 billion (n.s.a.), little different than in the same period last year.

Industrial production in the United Kingdom declined slightly in the third quarter and was 1.7 percent below its year-earlier level. The output measure of real GDP increased by only 0.8 percent (s.a.a.r.) in the third quarter. This weakness is in part the result of the ongoing coal miners' strike, now in its ninth month. To date, the effect of the strike on coal-using industries has been limited although coal production has been substantially reduced. The U.K. unemployment rate was 12.9 percent (s.a.) in November, the same as in the previous two months. The year-over-year increase in the retail price index was 5 percent in October, similar to that at the beginning of the year.

The U.K. trade deficit exceeded $12 billion (s.a.a.r.) in both September and October reflecting, in part, increased oil imports as a consequence of the coal strike and the front-loading of imports prior to the November 1 change in VAT procedures which advanced the collection of VAT on imports from time of sale to time of import. The cumulative current account deficit has widened to $1.5 billion (s.a.a.r.) for the first ten months of 1984, compared with a $4.4 billion surplus for all of 1983.

The Bank of England lowered all four of its money-market dealing rates by 1 percentage point in three steps in November, the last cut taking place one day after the Federal Reserve Board announced a lowering of the discount rate. The shortest-term dealing rate is now 9-1/2 percent. A general outline of the government's 1985/86 budget was provided by Chancellor of the Exchequer Nigel Lawson in his Autumn Statement to Parliament on November 12. Real public expenditures are scheduled to be held constant and a net tax cut equivalent to 0.4 percent of GDP is envisioned. Reductions in the contingency reserve and increased asset sales (which count as negative expenditure) allow for a small increase in actual real expenditures despite the stated target of zero percent real growth. The Public Sector Borrowing Requirement is forecast to fall to 2 percent of GDP (from 2-1/2 percent in 1984/85).

On December 11 the London clearing house announced that Citibank is to become the first overseas bank to receive settlement privileges in the U.K. clearing house system. Citibank is expected to participate in both the same day clearing of high value checks (town clearing) and in the bulk electronic clearing system (CHAPS).

Economic activity in France has remained weak in recent months. Industrial production in September fell by 3.7 percent (s.a.), almost entirely reversing a 4.6 percent rise recorded for the July-August period which seems to have reflected an abnormal seasonal production pattern over the summer holiday period. On a year-over-year basis, September's industrial production figure showed an increase of only 1.6 percent. Real GDP in the third quarter rose by 4 percent (s.a.a.r.), following a 2 percent decline in the second quarter. Third-quarter real GDP was only 2 percent above its year-earlier level. The unemployment rate in October remained at the record-high level of 10.1

percent (s.a.) for the third consecutive month.

Consumer prices in October increased by 0.7 percent (n.s.a.) as the year-over-year inflation rate eased slightly further to 7 percent. The government has officially admitted that its original consumer price inflation target for 1984 of 5 percent (December-over-December) will not be achieved. A new target for 1985 of 4-1/2 percent has been announced.

The current account was in surplus by $740 million (s.a.) in the third quarter. For the first three quarters of this year, the current account was in deficit by only $800 million (s.a.a.r.), a sharp reduction from the $4.5 billion current account deficit rate recorded in the same period last year. Comparing the same periods, the trade deficit was reduced to $2.2 billion (s.a.a.r.) this year from $5.7 billion last year.

On November 14 it was announced that Michel Camdessus was replacing Renaud de la Geniere as governor of the Bank of France. Mr. Camdessus had been first deputy governor of the Bank since August and before that had headed the treasury department at the Ministry of Finance.

The recovery in Italy appears to be continuing. Real GDP increased by 4.5 percent (s.a.a.r.) in the third quarter. Industrial production increased by 1.1 percent (s.a.) in September. For the third quarter as a whole, industrial production was 1.9 percent above its level in the previous quarter and showed a year-over-year increase of 4 percent. At the end of November, the year-over-year rate of consumer price inflation in Italy was down to 8.5 percent. The recent unexpectedly rapid progress in lowering the rate of growth of consumer prices suggests that the government may achieve its goal of attaining a 7 percent rate of inflation in 1985.

The trade deficit in September declined slightly to $610 million (s.a.). For the first nine months of 1984, the cumulative trade deficit was $9.5 billion (s.a.a.r.), somewhat greater than the $8.6 billion deficit rate in the same period last year.

Finance Minister Visentini has proposed a tax reform package, designed to make tax evasion by the self-employed more difficult, which would raise tax collections by an amount equivalent to approximately 13 percent of this year's projected budget deficit. On November 30, the government announced a reduction in the non-interest bearing deposit requirement on Italians' direct foreign investments from 50 to 40 percent for investments outside the European Community and to 30 percent for investments within the Community.

Economic expansion picked up in Canada in the third quarter with real GNP increasing by 7.6 percent (s.a.a.r.) mostly due to an increase in net exports. Private fixed investment increased slightly, but remained well below previous peaks. Both consumption and inventory investment were about unchanged. About half of the third-quarter increase in net exports appears to have been related to an increase in auto production in anticipation of the September and October strikes. Industrial production declined by 1.9 percent (s.a.) in September and its year-over-year rate of increase fell to 5.2 percent. The unemployment rate was unchanged in October at 11.3 percent (s.a.) after a drop of 0.5 of a percentage point in September which reversed most of the rise in unemployment in August. Inflation has continued to moderate. In October, the consumer price index was 3.4 percent above its year-earlier level, the lowest inflation rate since the summer of 1971.

The trade surplus increased to $1.7 billion (s.a.) in October. This brought the cumulative trade surplus so far this year to more than $16 billion (s.a.a.r.), about $2 billion higher than the surplus rate in the same period last year. The current account was in surplus by $520 million (s.a.) in the third quarter. For the first three quarters of this year, the current account surplus of $1.8 billion (s.a.a.r.) was somewhat below the $2.2 billion surplus rate in the comparable period last year.

Although the budget for 1985/86 will not be submitted until April 1985, there are strong indications that Canada, under its recently elected Conservative government, is heading for a period of fiscal austerity. On November 5, Brian Mulroney, Canada's new Prime Minister, delivered a speech to Parliament calling for fiscal austerity, deregulation, and new incentives to increase investment and to improve productivity and international competitiveness. On November 8, Finance Minister Michael Wilson provided some details regarding proposed budget cuts. These cuts, along with other new initiatives, are expected to reduce next fiscal year's budget deficit to 7.8 percent of GNP, compared with a previously estimated deficit of 8.3 percent of GNP. No tax increases were outlined, although tax reform was proposed. On December 7 the government introduced a bill in Parliament which would substantially reduce restrictions on foreign investment in Canada.

Debt Situation in Selected Developing Countries

Argentina and its bank advisory committee reached an agreement on December 2 under which Argentina will receive $4.2 billion in new credits in 1985 and a multi-year debt restructuring of a reported $13.4 billion in public and private sector debts now in arrears as to principal and debts maturing in 1985. In return, Argentina will pay at least $750 million to reduce public sector interest arrears to the banks before the end of 1984 and eliminate both public and private sector interest arrears by June 30, 1985. Argentina has also agreed to repay during the first quarter of 1985 the long-overdue $750 million balance of the 1982 bridge loan. The agreement must now be approved by an estimated 320 participating banks. The IMF Executive Board will consider a 15-month, SDR 1.42 billion standby agreement and an SDR 275 million compensatory financing facility drawing for Argentina on December 28, assuming the IMF receives assurances that a "critical mass" (85 percent) of the bank financing is available. The U.S. Treasury has said that it would provide a $500 million bridge loan when the bulk of the bank lenders agree to participate in the financing. The U.S. Treasury will be repaid from the first IMF disbursements. Argentine inflation (measured by the CPI) abated somewhat in October to 19 percent and further in November to 15 percent. The November rate was the lowest monthly rate since last January, but prices were still 675 percent higher than a year earlier. The peso price of the dollar rose substantially faster than domestic prices in October and November. Since the end of 1982, it has risen by about 13 percent less than the CPI. Two months ago, this discrepancy was about twice as large.

The rate of crawl of the Mexican peso was raised from 13 to 17 centavos per day, effective December 6. This is the first change in the rate of crawl since the crawl was adopted in December 1982. On December 5, the controlled peso price of the dollar was 34 percent higher than a year earlier, but the Mexican CPI in December is expected to be about 60 percent higher. As a result, the undervaluation of the peso that remained at the beginning of 1984 has been virtually eliminated. If the new rate of crawl is maintained until the end of 1985, the resulting depreciation of the peso will be about the same in percentage terms as that recorded this year and the controlled peso price of the dollar will be some 30 percent higher than in December 1984. Price inflation, however, may well exceed 40 percent next year. The budget submitted to the Mexican Congress late last month calls for a public sector deficit of 5.1 percent of GDP in 1985. The IMF, in negotiations over its EFF program for 1985, reportedly is pressing for a smaller fiscal deficit and significant steps toward relaxing trade restrictions. The 1984 public sector deficit is expected to exceed its target, partly because inflation did not abate as much as anticipated, causing spending and, to a lesser extent, receipts to exceed original plans. In particular, the stubborn inflation led the Bank of Mexico to keep interest rates higher than originally expected, causing interest payments on the internal public debt to exceed original projections. The 1984 fiscal deficit was also swollen by the decision to spend a contingency reserve earmarked to stimulate economic activity if it did not show signs of recovering by mid-year. Signs of an upturn began to appear in the second half, prompting Finance Secretary Silva-Herzog to tell the Mexican Congress in

October that he expected real GDP growth of 2-3 percent this year. (Earlier forecasts had been for only 1 percent real growth in 1984.) Real GDP growth of 3-4 percent is forecast for 1985.

Colombia is continuing to lose reserves. Between the end of 1983 and the end of November 1984, foreign exchange reserves declined by about $1.1 billion and gold holdings were reduced by 2.45 million ounces (equivalent to about $800 million at current prices). Much of the remaining foreign exchange reserves is not in liquid form and the remaining gold holdings (1.78 million ounces on November 30, equivalent to about $585 million at current prices) probably will not last through the first half of 1985, if reserves continue to decline at the rate experienced in 1984. The authorities would like to obtain foreign commercial bank financing, but the banks are likely to insist that Colombia negotiate a formal stand-by arrangement with the IMF. The Colombian authorities are hoping to avoid the policy constraints of an IMF-approved program and would prefer to work instead with the World Bank. Colombia has initiated, but not yet fully implemented, policy adjustments such as the IMF might recommend. However, the IMF staff does not consider these steps to be of sufficient magnitude. The financial difficulties of the country's commercial banks have complicated Colombia's external funding problems. In November, agreement in principle was announced on the refinancing of $530-$550 million in short-term external debts owed to banks by the Banco de Colombia, the country's largest commercial bank. While this potentially removes an important obstacle to foreign bank lending to the government, one or two other commerical banks in Colombia are reported to be in difficulties, and their problems have yet to be addressed.

Brazil registered a trade surplus of almost $12 billion during the first eleven months of the year, compared with a surplus of about $6 billion in the same period last year. The current account in 1984 is now expected to either be in balance or register a small deficit, perhaps $500 million (excluding $700 million of re-invested profits), substantially below the projection of $5.3 billion made by the IMF at the end of 1983. The general price index increased by over 12 percent in October, but increased at a 9.9 percent rate in November, slightly less than the average monthly rate of a little over 10 percent through the first 10 months of the year. Economic activity has shown continued signs of strength and real GDP is expected to grow by 3 percent this year. Negotiations with creditor banks on a possible multi-year rescheduling are expected to continue in mid-December after the IMF and Brazil have agreed on 1985 performance criteria under the current EFF. Brazil is not expected to need new money from banks in 1985, in part because its cash reserves at the end of this year are now expected to be approximately $9 billion.

Venezuela's bank advisory committee has continued to express concern about the lack of progress in the payment of private sector interest arrears, which now are estimated to exceed $1 billion. Substantial progress in the registration of this debt and the reduction of the interest arrears is necessary for the country's multi-year debt rescheduling agreement--negotiated in September--to be put in a form that can be circulated to banks. Recently some changes have been made in the registration procedures, but it is not clear how much of a contribution these changes will make. Real GDP is expected to show slightly negative growth again this year. At the same time, the inflation rate has increased (to about 16 percent in the 12 months through October), although the lifting of some price controls in September has distorted these figures somewhat. The public sector deficit, which was 4.7 percent of GDP in 1983, is expected to show a surplus of 4-5 percent of GDP this year. Venezuela's 1984 current account surplus is expected to be about $3 billion, not much different from the surplus registered in 1983.

On November 23, Chile announced that its bank creditors will allow the country to postpone until the end of June 1985 $2.2 billion in principal payments coming due by the end of the year and during the first quarter of next year. The postponement will give Chile time to implement a new IMF program--not expected to be agreed upon until March or April--and negotiate a debt rescheduling agreement with the banks. Chile is expected to ask for about $1 billion in new money for next year but is likely to receive less than that, perhaps $800 million.

In Peru, there has been no movement toward a resolution of the country's fiscal problems, which are the major obstacle to reaching agreement with the IMF. Mounting arrears are also straining Peru's relations with banks. Peru's central bank has continued to refuse to release foreign exchange reserves, which as of September totaled $1.5 billion (excluding gold), to the government except in exchange for an equivalent amount of domestic currency. Thus, the government's fiscal problems have continued to contribute to the accumulation of external arrears. There are indications that the government is contemplating changes in economic policy that would help its relations with the IMF.

The government is also discussing with its bank advisory committee possible arrangements to bring interest payments current.

On November 2, the IMF Managing Director approved and sent to the Board an 18-month, SDR 615 million stand-by arrangement for the Philippines. The Board is currently scheduled to consider the proposal on December 14. Consideration as scheduled will depend largely on whether the Philippine authorities will have arranged pledges for about 90 percent of the $925 million in new money needed from the commercial banks in 1985. On November 7, the United States, Japan, and Korea provided $80 million in bridge financing for the Philippines until the country can draw on the stand-by arrangement. This credit was to have expired on November 30, but was extended by the three countries until December 28--the date when the IMF is expected to disburse funds to the Philippines. Philippine officials on December 17 will meet with the Paris Club to reschedule debt owed to official lenders.

Yugoslavia's bank advisory committee reportedly has offered the country a four-year serial debt restructuring for 1985-88 involving the setting in advance of terms and conditions. Each year's restructuring will be activated if the country complies with certain specified conditions, including successful negotiation of a parallel arrangement with official creditors. Yugoslavia is to arrange for another IMF stand-by for 1985; in subsequent years relations with the IMF will be determined by monitoring through the Article IV consultation process. The banks have granted Yugoslavia a 90-day extension of principal payments due in the first quarter of next year in order to allow time to work on the details of the restructuring arrangement. The next meeting between Yugoslavia and the banks is scheduled for January 7.