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May 15, 1987

SUPPLEMENT
CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Prepared for the
Federal Open Market Committee

By the Staff
Board of Governors
of the Federal Reserve System

TABLE OF CONTENTS

	Page
THE DOMESTIC NONFINANCIAL ECONOMY	
Industrial production	1
Producer price index	1
Manufacturing and trade inventories	2
Tables	
Industrial production	4
Recent changes in producer prices	5
Changes in manufacturing and trade inventories	6
Inventories relative to sales	6
THE FINANCIAL ECONOMY	
Tables	
Monetary aggregates	7
Commercial bank credit and short- and intermediate- term business credit	8
Selected financial market quotations	9
INTERNATIONAL DEVELOPMENTS	
U.S. Merchandise trade	10

SUPPLEMENTAL NOTES

THE DOMESTIC NONFINANCIAL ECONOMY

Industrial Production

Industrial production declined an estimated 0.4 percent in April, after falling 0.2 percent in March. Much of the April decline in total production was related to sharp cuts in the output of motor vehicles; however, smaller declines were widespread elsewhere. Output of consumer goods declined 0.9 percent in April after decreasing 0.4 percent in March. A sharp reduction in auto assemblies—from a 7.9 million unit rate in March to a 7.2 million unit pace—accounted for a large part of the decline in production of consumer goods. Moreover, output of home goods and nondurable consumer goods, both of which advanced in the last quarter of 1986, fell again in April. Business equipment production decreased 0.4 percent, led by weakness in transit equipment (particularly motor vehicles); and output of defense and space equipment was about flat for a second month. The production of both construction and business supplies, which was quite strong during the second half of last year, has been, on average, little changed since December. Output of materials was about unchanged in April as declines in durable and nondurable goods materials offset a small rise in energy materials.

Producer Price Index

The producer price index rose 0.7 percent in April. Consumer food prices jumped 1.5 percent as a pickup in livestock prices was translated into higher finished food prices. Moreover, large increases in the prices of cattle, hogs, and poultry pushed the index for crude foods up 4.3 percent, and recent commodity prices suggest a further rise in May. However, supply

indicators point to increased meat production as the year progresses, and futures prices of cattle and hogs show a sharp reversal of the recent runup. Consumer energy prices also rose in April after leveling off in March, as gasoline, fuel oil, and natural gas all posted sizable increases; and wellhead prices of crude petroleum turned up again last month.

Apart from food and energy, price increases, on average, were more moderate than in March. The PPI for other consumer goods was up 0.2 percent, and capital equipment prices rose 0.3 percent. Both these indexes were influenced importantly by an uptick in manufacturers' prices for automobiles and light trucks. Elsewhere, prices, on average, for other consumer durables were up slightly, and prices of other types of capital equipment were little changed. Prices of nondurable consumer goods (excluding food and energy) fell last month, after a particularly sharp rise a month earlier. At the intermediate stage of processing, the index for intermediate materials rose another 0.3 percent last month, as prices rose rapidly for various petroleum-derived materials.

Manufacturing and Trade Inventories

The market value of retail inventories rose at an annual rate of \$38.4 billion in March. With a 0.8 percent gain in sales, the retailers' inventory-sales ratio rose from 1.53 to 1.55. As in the previous several months, the March retail inventory change was heavily influenced by movements in auto dealers' stocks. But several other categories of stores—apparel, lumber, food, and general merchandise—also reported relatively sizable stock accumulations. With the exception of general merchandisers, most of these stores also posted some gain in sales in March, and their inventory-

sales ratios were still below the most recent highs reached last year.

For all manufacturing and trade, inventory accumulation expanded at an annual rate of \$28 billion in March and \$40.5 billion for the first quarter as a whole. With a 0.8 percent rise in total shipments and sales, the overall inventory-sales ratio for all manufacturing and trade edged down from 1.49 to 1.48.

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

	1986	1987	1987		
	Q4	Q1	Feb.	Mar.	Apr.
	--Annual rate--		--Monthly rate--		
Total Index	3.2	2.7	.4	-.2	-.4
Products	3.4	2.8	.8	-.3	-.5
Final products	2.8	3.5	1.0	-.5	-.6
Consumer goods	3.2	4.0	.6	-.4	-.9
Durable consumer goods	7.9	8.7	1.9	-.9	-2.5
Nondurable consumer goods	1.7	2.5	.2	-.3	-.3
Equipment	2.2	3.0	1.5	-.5	-.4
Business	-1.6	3.4	1.9	-.8	-.4
Defense and space	9.8	2.2	.7	.1	-.1
Oil and gas drilling	48.8	3.2	-.6	3.2	-1.5
Intermediate products	5.5	.5	.2	.3	-.1
Construction supplies	6.2	3.4	-.3	.2	-.2
Materials	3.0	2.5	-.2	-.1	-.1
Durable goods	4.3	2.9	.7	-.3	-.2
Nondurable goods	5.2	6.0	-.4	.3	-.2
Energy materials	-1.8	-1.9	-1.7	-.3	.2

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

	Relative Importance Dec. 1986	1986	1986		1987	1987	
			03	04	01	Mar.	Apr.
			-Annual rate-			-Monthly rate-	
Finished goods	100.0	-2.3	-.4	1.8	3.9	.4	.7
Consumer foods	26.3	2.9	11.2	1.1	-6.7	-.5	1.5
Consumer energy	8.6	-38.0	-42.7	-12.5	57.6	-.2	2.1
Other consumer goods	40.6	3.0	2.3	4.4	3.4	.8	.2
Capital equipment	24.5	2.1	2.0	3.4	.1	.1	.3
Intermediate materials ²	95.0	-4.5	-1.5	-1.2	8.0	.4	.3
Exc. energy	82.9	.1	1.5	1.2	3.3	.3	.2
Crude food materials	42.5	-1.4	18.1	-2.7	-11.3	.4	4.3
Crude energy	40.9	-27.5	-19.6	-.5	41.2	-.9	1.7
Other crude materials	16.6	1.7	-24.1	8.5	16.3	-.9	.7

1. Changes are from final month of preceding period to final month of period indicated.

2. Excludes materials for food manufacturing and animal feeds.

BUSINESS INVENTORIES
(Billions of dollars, current cost basis,
seasonally adjusted annual rate)

	1986			1987	1986	1987		
	Q2	Q3	Q4	Q1	Dec.	Jan.	Feb. ^r	Mar. ^p
Manufacturing and trade (Previous)	-.5	-4.4	-1.1	40.4	-41.8	76.0	17.2	28.1
							13.8	
Manufacturing	-10.8	-11.7	-.7	5.7	-6.6	30.2	-1.8	-11.3
Trade, total	10.2	7.3	-.4	34.8	-35.2	45.8	19.1	39.5
Wholesale	5.9	5.9	-4.9	8.5	-9.9	23.7	.7	1.1
Retail	4.3	1.4	4.5	26.3	-25.3	22.1	18.3	38.4
Durable	2.9	-5.4	2.4	19.5	-25.3	20.1	14.7	23.9
Auto	.3	-11.3	5.2	20.2	-15.5	25.4	17.9	17.2
Nondurable	1.4	6.8	2.1	6.7	.0	2.1	3.6	14.5

totals may not add because of rounding.

INVENTORY/SALES RATIOS
(Current-cost basis)

	1986			1987	1986		1987	
	Q2	Q3	Q4	Q1	Dec.	Jan.	Feb. ^r	Mar. ^p
Manufacturing and trade	1.56	1.53	1.50	1.51	1.47	1.55	1.49	1.48
Manufacturing	1.70	1.69	1.65	1.64	1.61	1.69	1.64	1.62
Trade, total	1.43	1.40	1.38	1.41	1.36	1.44	1.37	1.38
Wholesale	1.30	1.28	1.25	1.23	1.24	1.28	1.21	1.21
Retail	1.56	1.50	1.51	1.58	1.47	1.59	1.53	1.55

r—Revised.

p—Preliminary.

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

May 15, 1987

	1985:Q4 to 1986:Q4		1987				Growth from Q4 1986 to Apr. 1987P
	1986:Q4	1986:Q4	Q1	Feb.	Mar.	Apr. P	
----- Percentage change at annual rates -----							
1. M1	15.3	17.0	13.0	-0.7	3.3	17.9	11.9
2. M2	8.9	9.2	6.4	-0.2	1.8	5.9	5.3
3. M3	8.8	8.0	6.5	1.2	1.9	5.8	5.4
Levels in billions of dollars Apr. 1987P							
<u>Selected components</u>							
4. Currency	7.5	8.1	10.1	7.7	3.8	7.0	188.9
5. Demand deposits	11.6	12.8	2.4	-17.3	-6.4	19.3	303.9
6. Other checkable deposits	28.6	31.1	29.4	13.0	13.8	24.9	250.6
7. M2 minus M1 ²	6.9	6.6	4.1	-0.1	1.3	1.7	2089.4
8. Overnight RPs and Eurodollars, NSA	14.7	21.9	16.6	-57.3	-39.1	-1.6	77.1
9. General purpose and broker/dealer money market mutual fund shares, NSA	17.3	12.7	6.2	9.8	5.1	1.1	211.8
10. Commercial banks	6.8	6.4	5.9	-1.1	1.2	-1.6	905.1
11. Savings deposits, SA, plus MMDAs, NSA ³	16.0	19.2	13.3	2.9	7.7	2.6	547.5
12. Small time deposits	-4.2	-10.7	-4.9	-7.2	-8.3	-8.0	357.6
13. Thrift institutions	4.3	3.1	3.9	5.6	7.6	4.4	909.1
14. Savings deposits, SA, plus MMDAs, NSA ³	12.0	15.5	14.5	16.7	15.6	10.0	424.0
15. Small time deposits	-1.2	-6.4	-4.8	-3.9	0.7	-0.5	485.1
6. M3 minus M2 ⁴	8.3	3.4	7.1	7.1	2.2	5.2	701.7
17. Large time deposits	3.0	-2.2	2.7	-4.3	5.4	12.3	454.6
18. At commercial banks, net ⁵	2.8	0.4	9.5	0.4	12.6	28.1	306.1
19. At thrift institutions	3.3	-7.3	-10.0	-14.0	-8.7	-18.3	148.6
20. Institution-only money market mutual fund shares, NSA	30.3	16.8	0.9	10.0	2.8	-25.4	83.1
21. Term RPs, NSA	28.3	26.4	5.9	38.7	-15.9	80.4	87.6
22. Term Eurodollars, NSA	2.3	5.1	49.4	51.5	20.0	-40.7	88.3

-- Average monthly change in billions of dollars --

MEMORANDA:

23. Managed liabilities at commercial banks (24+25)	2.0	1.3	8.8	4.9	7.9	2.4	519.5
24. Large time deposits, gross	0.6	0.5	2.8	0.9	3.0	5.7	359.8
25. Nondeposit funds	1.4	0.8	6.0	4.0	4.9	-3.3	159.7
26. Net due to related foreign institutions, NSA	0.6	1.7	4.3	3.0	6.0	-3.6	-9.7
27. Other ⁶	0.8	-1.0	1.7	0.9	-1.0	0.3	169.4
28. U.S. government deposits at commercial banks ⁷	0.4	1.6	-1.2	1.9	-5.5	2.8	20.5

1. Dollar amounts shown under memoranda are calculated on an end-month-of-quarter basis.

2. Nontransactions M2 is seasonally adjusted as a whole.

3. Growth rates are for savings deposits, seasonally adjusted, plus money market deposit accounts (MMDAs), not seasonally adjusted. Commercial bank savings deposits excluding MMDAs increased during March and April 1987 at rates of 27.7 percent and 27.8 percent, respectively. At thrift institutions, savings deposits excluding MMDAs increased during March and April 1987 at rates of 29.1 percent and 30.5 percent, respectively.

4. The non-M2 component of M3 is seasonally adjusted as a whole.

5. Net of large-denomination time deposits held by money market mutual funds and thrift institutions.

6. 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, loan RPs and other minor items). Data are partially estimated.

7. Consists of Treasury demand deposits and note balances at commercial banks.

p--preliminary

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

May 15, 1987

	1986		1987				Levels in bil. of dollars April ^p
	03	04	01	Feb.	Mar.	Apr. ^p	
----- Commercial Bank Credit -----							
1. Total loans and securities at banks	13.4	8.4	7.0	0.9	3.8	11.9	2147.2
2. Securities	31.5	6.0	2.4	5.9	1.9	7.0	512.8
3. U.S. government securities	27.8	20.2	5.7	-4.2	-3.4	5.0	315.6
4. Other securities	36.8	-14.5	-2.8	23.3	9.9	10.4	197.2
5. Total loans	7.8	9.1	8.4	-0.7	4.4	13.4	1634.5
6. Business loans	3.4	18.5	7.6	-0.6	-4.6	5.0	554.0
7. Security loans	14.5	-39.3	-3.1	25.5	-6.2	159.8	43.4
8. Real estate loans	13.6	16.3	17.9	11.8	17.1	16.2	517.9
9. Consumer loans	6.2	5.4	1.9	1.1	1.9	3.8	316.7
10. Other loans	7.9	-20.5	0.0	-39.0	3.0	16.8	202.5
----- Short- and Intermediate-Term Business Credit -----							
11. Business loans net of bankers acceptances	3.4	18.8	8.1	-0.2	-3.1	4.2	548.9
12. Loans at foreign branches ²	0.0	-22.5	-7.1	60.8	-7.2	7.3	16.6
13. Sum of lines 11 & 12	3.3	17.4	7.7	1.3	-3.0	4.3	565.5
14. Commercial paper issued by nonfinancial firms	7.3	-19.1	-13.0	-42.1	0.0	40.5	79.7
15. Sums of lines 13 & 14	3.8	12.5	5.1	-4.1	-2.6	8.6	645.2
16. Bankers acceptances: U.S. trade related ^{3,4}	0.0	-16.9	-2.5	-3.8	7.7	n.a.	31.5 (Mar)
17. Line 15 plus bankers acceptances: U.S. trade related	3.6	11.0	4.8	-4.1	-2.0	n.a.	672.2 (Mar)
18. Finance company loans to business ³	3.4	11.2	14.7	15.1	12.2	n.a.	178.3 (Mar)
19. Total short- and intermediate- term business credit (sum of lines 17 & 18)	3.5	11.0	n.a.	-0.1	0.7	n.a.	850.4 (Mar)

n.a.--not available.

p--preliminary

1. Average of Wednesdays.

2. Loans at foreign branches are loans made to U.S. firms by foreign branches of domestically chartered banks.

3. Based on average of current and preceding ends of month.

4. Consists of acceptances that finance U.S. imports, U.S. exports and domestic shipment and storage of goods.

III-T-1
SELECTED FINANCIAL MARKET QUOTATIONS 1/
(percent)

	1984	1985	1986	1987		Change from:	
	Highs	March highs	June highs	FOMC Mar 31	May 14	June highs	FOMC Mar 31
Short-term rates							
Federal funds 2/	11.63	8.58	6.90	6.11	6.75	-0.15	0.64
Treasury bills 3/							
3-month	10.67	8.80	6.52	5.61	5.73	-0.79	0.12
6-month	10.77	9.13	6.57	5.74	5.96	-0.61	0.22
1-year	11.13	9.25	6.62	5.78	6.55	-0.07	0.77
Commercial paper							
1-month	11.42	8.04	6.87	6.39	6.80	-0.07	0.41
3-month	11.35	9.12	6.81	6.31	6.85	0.04	0.54
Large negotiable CD's 3/							
1-month	11.52	8.89	6.88	6.30	6.72	-0.16	0.42
3-month	11.79	9.29	6.91	6.30	6.89	-0.02	0.59
6-month	12.30	9.92	6.97	6.31	7.12	0.15	0.81
Eurodollar deposits 4/							
1-month	11.89	8.89	7.01	6.38	6.81	-0.20	0.43
3-month	12.20	9.58	7.01	6.36	7.10	0.09	0.74
Bank prime rate	13.00	10.50	8.50	7.50	8.00	-0.50	0.50
Intermediate- and long-term rates							
U.S. Treasury (constant maturity)							
3-year	13.49	11.22	7.86	6.79	7.95	0.09	1.16
10-year	13.99	12.02	8.39	7.51	8.57	0.18	1.06
30-year	13.94	11.97	7.93	7.81	8.73	0.80	0.92
Municipal revenue 5/ (Bond Buyer Index)	11.44	10.25	8.57	7.11	8.20	-0.37	1.09
Corporate—A utility recently offered	15.30	13.23	9.70	9.05	9.93	0.23	0.88
Home mortgage rates 6/							
S&L fixed-rate	14.68	13.29	10.76	9.07	10.52	-0.24	1.45
S&L ARM, 1-yr.	12.31	11.14	8.65	7.53	7.85	-0.80	0.32
	1984	1985	1986	1987		Percent change from:	
	Lows	March lows	Highs	FOMC Mar 31	May 14	1986 highs	FOMC Mar 31
Stock prices							
Dow-Jones Industrial	1086.57	1247.35	1955.57	2304.69	2325.49	18.92	0.90
NYSE Composite	85.13	102.46	145.75	165.89	165.76	13.73	-0.08
AMEX Composite	187.16	222.28	285.19	332.66	336.93	18.14	1.28
NASDAQ (OTC)	225.30	276.18	411.16	430.05	422.65	2.79	-1.72

1/ One-day quotes except as noted.

2/ Averages for two-week reserve maintenance period closest to date shown. Last observation is the average to date for the maintenance period ending May 20, 1987.

3/ Secondary market.

4/ Averages for statement week closest to date shown.

5/ Thursday quotes.

6/ Friday quotes.

e—estimate

Merchandise Trade through March.

The March merchandise trade deficit was \$13.6 billion (\$164 billion at an annual rate), the same as the average deficit for January-February. (See the table below.) The value of both exports and imports rose in March although, on this basis, not in the first quarter as a whole. These data are not seasonally adjusted and the value of imports includes insurance and freight charges (CIF). The chart on the next page illustrates that monthly data are very volatile; the Commerce Department advised that because of late documents, the reported January deficit was understated and the February deficit was overstated.

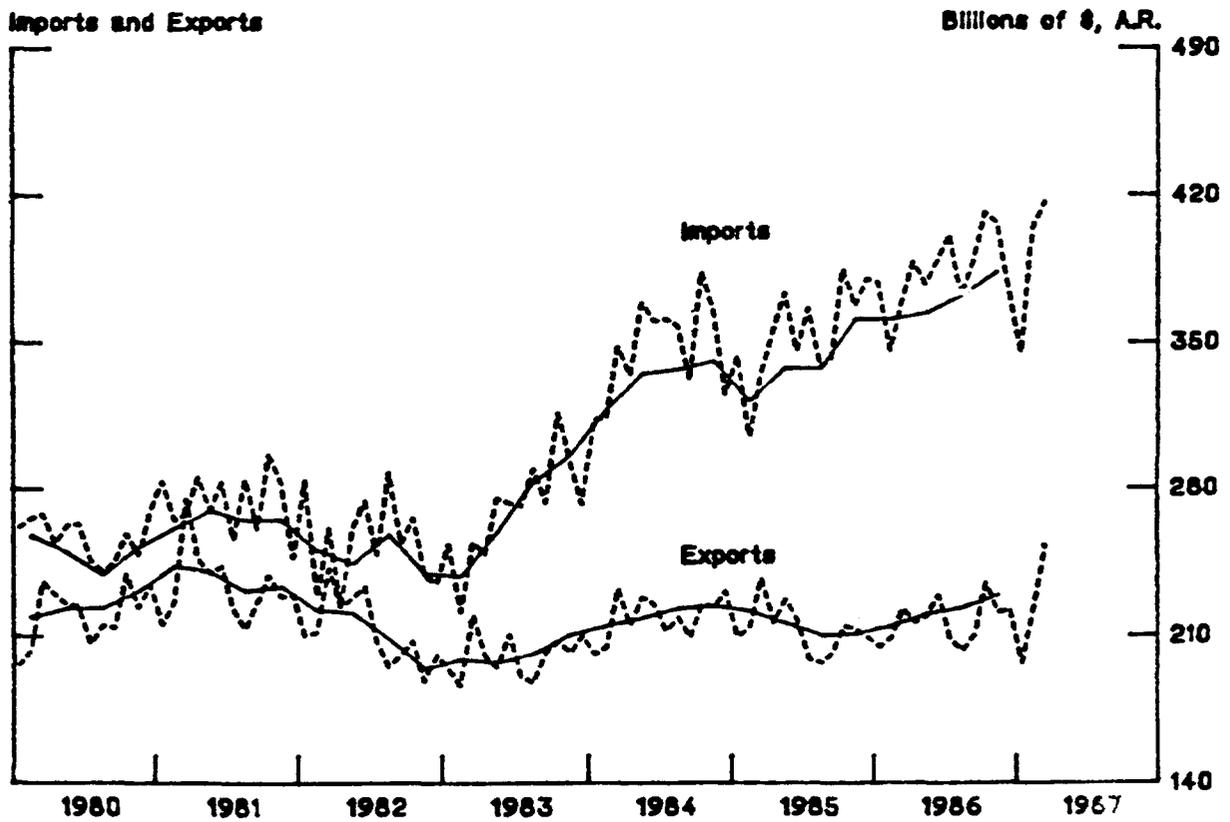
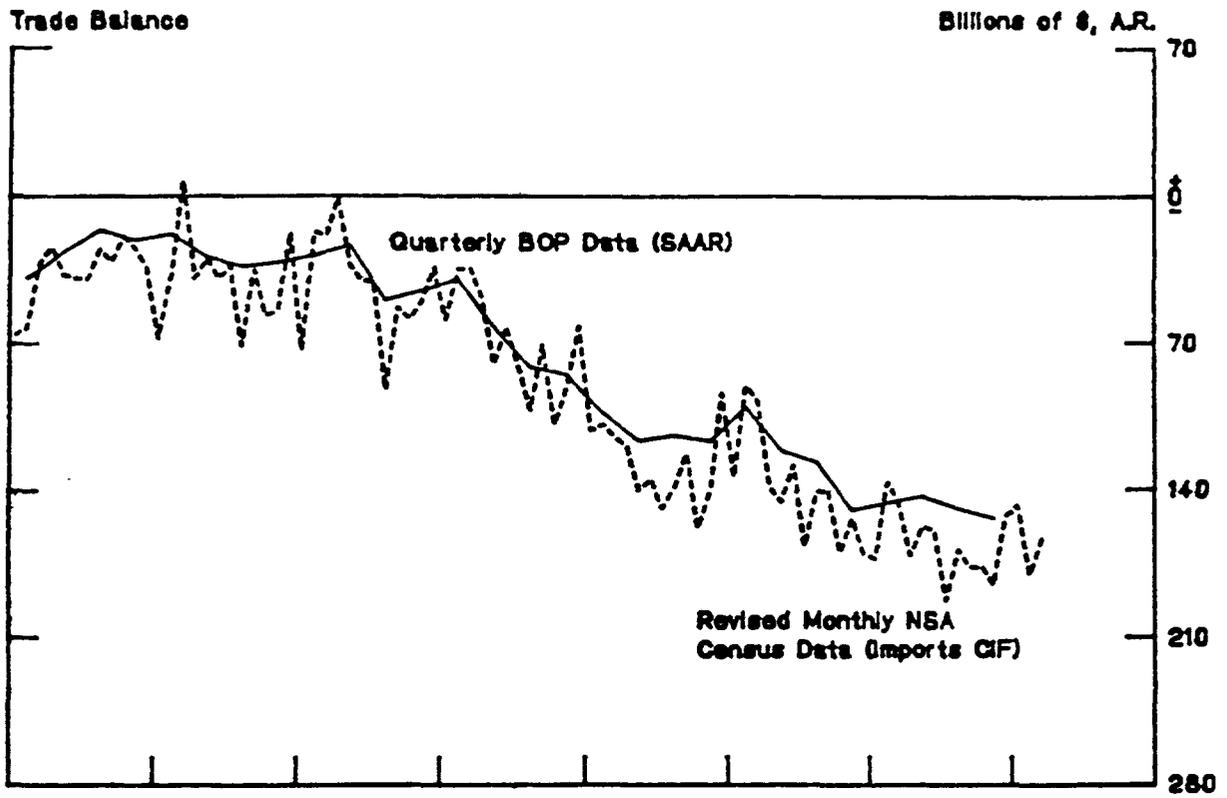
MONTHLY TRADE DATA
(Billions of dollars, annual rates)

	<u>Revised Census Basis, NSA</u>		
	<u>Exports</u>	<u>Imports</u>	<u>Balance</u>
		CIF	CIF
<u>Months</u>			
1986 - Oct.	235	411	-176
Nov.	221	406	-185
Dec.	222	375	-153
1987 - Jan.	197	344	-147
Feb.	224	405	-181
Mar.	252	416	-164
<u>Quarters</u>			
1986 - Q4	226	398	-172
1987 - Q1	225	388	-164

SOURCE: U.S. Department of Commerce, Bureau of the Census.

On a seasonally adjusted basis, the staff estimates that the merchandise trade deficit in the first quarter will be about the same as the deficit in the fourth quarter of last year (balance-of-payments basis). (See the table below.) The Commerce Department will release revised seasonally adjusted quarterly data on May 27.

U.S. MERCHANDISE TRADE



Exports in the first quarter increased by an estimated 1 percent from the fourth-quarter level. Much of the increase was in industrial supplies (especially paper and chemicals), in consumer goods and in exports of automotive parts to Mexico and other non-Canadian destinations. Exports of machinery continued at about the same elevated rate as in the fourth quarter (about 5 percent above previous 1986 levels). While the value of aircraft exports declined for the second quarter in a row, the level of those exports was still above rates recorded throughout the first half of last year. Over the past four quarters, the value of nonagricultural exports rose about 10 percent, largely in volume.

Agricultural exports declined somewhat in 1987-Q1 from strong fourth-quarter levels, particularly the volume of soybeans and cotton. While the value of agricultural exports was about the same in 1987-Q1 as it was a year earlier, a decline in prices was largely offset by an increased volume of shipments.

Imports increased slightly in the first quarter. Part of the increase was in the value of oil imports, which rose an estimated 5 percent. The price of imported oil rose by nearly 25 percent in the first quarter (by about \$3 per barrel) as OPEC countries acted to limit oil production and raise prices. The volume of U.S. oil imports declined by an estimated 1 million barrels per day, reflecting in part a drawdown in stocks of petroleum from unusually high fourth-quarter levels; U.S. domestic consumption was essentially flat. There was also a small increase in the value of non-oil imports, most of which appears to have been in manufactured goods, particularly machinery. Prices of imported machinery (other than computers) rose strongly in the first

quarter, as did prices of imported consumer goods. More detailed information about imports will be available next week.

U.S. MERCHANDISE TRADE
(Billions of dollars, annual rates)

	<u>Balance-of-payments basis, seasonally adjusted</u>						<u>Balance</u>
	<u>Exports</u>			<u>Imports</u>			
	<u>Total</u>	<u>Ag.</u>	<u>Nonag.</u>	<u>Total</u>	<u>Oil</u>	<u>Non-oil</u>	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
<u>Years</u>							
1984	220	38	182	332	57	275	-112
1985	214	30	185	339	51	288	-124
1986	222	27	195	370	34	336	-148
<u>Quarters</u>							
1985-4	211	29	182	360	57	304	-149
1986-1	214	29	186	360	40	320	-146
2	220	25	196	363	31	332	-143
3	223	26	197	372	32	340	-149
4	229	28	201	383	32	351	-154
1987-1e	232	27	205	387	34	353	-155

e/ FR staff estimate.

SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis.