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CONFIDENTIAL (FR)

CURRENT ECONOMIC and FINANCIAL CONDITIONS

**Prepared for the
Federal Open Market Committee**

By the Staff

BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM

January 6, 1965

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IN BROAD REVIEW

As the new year begins, the U.S. economy is continuing to move forward with each monthly step carrying it further into uncharted areas beyond the guides of earlier peacetime cyclical comparisons. Although the economy is now in the 46th month of this expansion period, there are few signs of imbalance--except for the precautionary buildup of steel stocks--of the sort that in the past preceded cyclical downturn. "Sustained moderation" still seems to be an accurate description of the mood and the performance of the domestic economy.

Industrial production and employment expanded further at year-end and unemployment apparently was little changed around its reduced November level. Capacity utilization was higher than earlier in the year, but new capacity was coming on stream in large volume and was serving, along with competition from at home and abroad, to maintain general price stability, with some increases but largely of a selective nature. After advancing in October and November, prices of industrial commodities at wholesale showed only a little further increase in December. Consumer prices have given no indication of accelerating their slow upward pace. Stock market prices were below peak levels reached last autumn.

Meanwhile, the statistical information now available for the fourth quarter as a whole underscores the effects of strikes and strike threats. GNP, despite substantial increase in the rate of inventory investment, was up much less than in preceding quarters. Retail sales were somewhat disappointing and the personal saving rate

rose to about the high second quarter rate reached immediately following the tax cut. Industrial production for the quarter was probably only half a per cent above the third quarter level, although in December the index rose to a new high, 7 per cent above a year earlier.

The labor market strengthened further in late 1964 but hourly earnings in manufacturing did not show signs of accelerating their earlier moderate rate of increase. Fringe benefits rose more than cash wages, but unit labor costs in manufacturing were still within the narrow range of the past year as productivity continued to increase rapidly.

In the financial area, markets for corporate, municipal and U.S. Government bonds withstood with minimum effects the sterling crisis, the consequent discount rate and Regulation Q actions and the very large Treasury advance refunding announced at the end of December. Initial market reception of the Treasury refunding was favorable, and yields on Treasury bonds in early January were only a little above a year earlier. Bill and other short-term yields remained below the level reached immediately after the change in the discount rate, but were considerably above a year earlier.

Bank credit and monetary growth moderated in December. Total bank credit growth in 1964 was about 8 per cent, the same as in 1963. The money supply was estimated to be up \$400 million in December, somewhat less than in other recent months, while growth for the year was placed at 4.1 per cent as compared with 3.8 per cent

in 1963. Time and savings deposits rose substantially in December, but the increase for the year was less than in 1963.

The U.S. balance of payments deficit totalled about \$2.5 billion in 1964. The rate of deficit increased during the year from a low \$1 billion in the first quarter to about \$4 billion in the final quarter when the deficit was swollen by a bunching of foreign security issues and by the British waiver of its service payments on the 1947 sterling loan. These somewhat exceptional factors nearly doubled the rate of deficit in the fourth quarter.

Abroad, the pound has remained under heavy pressure pending the impact of the import surcharges and other recent measures to improve Britain's payments position. In general, the economies of the other industrial countries of Europe entered 1965 with aggregate demand still strong and rising, although less buoyant than a year earlier. Restrictive economic policies were being continued except in Italy and Japan. Canadian economic activity by late autumn had begun to advance again.

SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally Adjusted)

| | Latest Period | Amount | | | Per cent change | |
|--|------------------|------------------|-------------------|-------------|-----------------|------------------|
| | | Latest Period | Precedg Period | Year Ago | Year Ago/1 | 2 years Ago/1 |
| Civilian labor force (mil.) | Nov. '64 | 74.4 | 74.2 | 73.6 | 1.2 | 3.3 |
| Unemployment (mil.) | " | 3.7 | 3.9 | 4.4 | -14.3 | -11.2 |
| Unemployment (per cent) | " | 5.0 | 5.2 | 5.9 | - | - |
| Nonfarm employment, payroll (mil.) | " | 58.8 | 58.4 | 57.1 | 3.0 | 5.2 |
| Manufacturing | " | 17.5 | 17.2 | 17.1 | 2.4 | 3.5 |
| Other industrial | " | 7.8 | 7.7 | 7.6 | 2.7 | 4.3 |
| Nonindustrial | " | 33.5 | 33.5 | 32.5 | 3.3 | 6.4 |
| Industrial production (57-59=100) | " | 134.9 | 131.7 | 126.1 | 7.0 | 12.6 |
| Final products | " | 134.5 | 130.7 | 127.0 | 5.9 | 10.5 |
| Materials | " | 135.4 | 132.5 | 125.7 | 7.7 | 14.8 |
| Wholesale prices (57-59=100) ^{2/} | " | 100.7 | 100.8 | 100.7 | 0.0 | 0.0 |
| Industrial commodities | " | 101.3 | 101.1 | 100.6 | 0.7 | 0.9 |
| Sensitive materials | " | 100.8 | 100.4 | 97.4 | 3.5 | 4.5 |
| Farm products and foods | " | 97.8 | 98.2 | 99.7 | -1.9 | -2.6 |
| Consumer prices (57-59=100) ^{2/} | " | 108.7 | 108.5 | 107.4 | 1.2 | 2.5 |
| Commodities except food | " | 104.8 | 104.6 | 104.5 | 0.3 | 1.4 |
| Food | " | 106.8 | 106.9 | 105.1 | 1.6 | 2.6 |
| Services | " | 116.0 | 115.7 | 113.9 | 1.8 | 4.0 |
| Hourly earnings, mfg. (\$) | " | 2.56 | 2.54 | 2.49 | 2.8 | 6.2 |
| Weekly earnings, mfg. (\$) | " | 104.70 | 102.97 | 100.85 | 3.8 | 7.5 |
| Personal income (\$ bil.) ^{3/} | " | 502.0 | 498.7 | 473.8 | 6.0 | 11.7 |
| Retail sales, total (\$ bil.) | " | 21.3 | 21.4 | 20.6 | 3.4 | 5.7 |
| Autos (million units) ^{3/} | " | 6.878 | 5.963 | 7.320 | -6.0 | -5.0 |
| GAF (\$ bil.) | " | 5.1 | 5.1 | 4.5 | 11.4 | 12.5 |
| Selected leading indicators | | | | | | |
| Housing starts, pvt. (thous.) ^{3/} | " | 1,420 | 1,599 | 1,577 | -10.0 | -10.1 |
| Factory workweek (hours) | " | 40.9 | 40.5 | 40.5 | 1.0 | 1.2 |
| New orders, dur. goods (\$ bil.) | " | 19.4 | 19.6 | 18.1 | 7.2 | 16.1 |
| New orders, nonel. mach. (\$ bil.) | " | 3.0 | 3.0 | 2.6 | 14.3 | 28.2 |
| Common stock prices (1941-43=10) | Dec. '64 | 83.96 | 85.44 | 74.17 | 13.2 | 34.0 |
| Inventories, book val. (\$ bil.) | Oct. '64 | 107.3 | 107.3 | 103.7 | 3.5 | 7.6 |
| Gross national product (\$ bil.) ^{3/} | QIII-64 | 628.4 | 618.6 | 587.2 | 7.0 | 12.4 |
| Real GNP (\$ bil., 1963 prices) ^{3/} | " | 614.9 | 608.5 | 586.6 | 4.8 | 8.4 |

^{1/} Based on unrounded data. ^{2/} Not seasonally adjusted. ^{3/} Annual rates.

SELECTED DOMESTIC FINANCIAL SERIES

| | Week ended Jan. 1 | Four-Week Average | Last six months | |
|---|----------------------|----------------------|------------------------------------|------------------------------|
| | | | High | Low |
| <u>Money Market^{1/} (N.S.A.)</u> | | | | |
| Federal funds rate (per cent) | 4.00 | 3.83 | 4.00 | 1.00 |
| U.S. Treas. bills, 3-mo., yield (per cent) | 3.84 | 3.84 | 3.86 | 3.43 |
| Net free reserves ^{2/} (mil. \$) | 105 | 170 | 254 | -60 |
| Member bank borrowings ^{2/} (mil. \$) | 504 | 254 | 590 | 122 |
| <u>Security Markets (N.S.A.)</u> | | | | |
| Market yields ^{1/} (per cent) | | | | |
| 5-year U.S. Treas. bonds | 4.09 | 4.08 | 4.13 | 4.00 |
| 20-year U. S. Treas. bonds | 4.20 | 4.18 | 4.22 | 4.15 |
| Corporate new bond issues, Aaa | -- | -- | 4.52 | 4.37 |
| Corporate seasoned bonds, Aaa | 4.43 | 4.44 | 4.45 | 4.40 |
| Municipal seasoned bonds, Aaa | 2.99 | 3.00 | 3.12 | 2.99 |
| FHA home mortgages, 30-year ^{3/} | 5.45 | 5.45 | 5.46 | 5.45 |
| Common stocks S&P composite index ^{4/} | | | | |
| Prices, closing (1941-43=10) | 84.75 | 84.21 | 86.28 | 81.86 |
| Dividend yield (per cent) | 3.02 | 3.04 | 3.05 | 2.93 |
| | | | | |
| | | | | |
| | | Change in Nov. | Average change-- last 3 mas. | Annual rate of change (%) |
| | | | 3 mos. | 1 year |
| <u>Banking (S.A., mil. \$)</u> | | | | |
| Total reserves | ^{5/} 37 | 20 | 1.1 | 4.1 |
| Bank loans and investments: | | | | |
| Total | 4,100 | 2,100 | 9.6 | 8.5 |
| Business loans | 500 | 400 | 9.4 | 10.3 |
| Other loans | 1,600 | 800 | 9.1 | 11.9 |
| U. S. Government securities | 1,400 | 400 | 7.3 | -0.2 |
| Other securities | 600 | 500 | 15.1 | 11.6 |
| Money and liquid assets: | | | | |
| Demand dep. & currency | ^{5/} 400 | 500 | 3.8 | 4.1 |
| Time and savings dep. | ^{5/} 1,400 | 1,600 | 15.8 | 12.6 |
| Nonbank liquid assets | 1,300 | 1,400 | 6.8 | 6.2 |

N.S.A.--not seasonally adjusted. S.A.--seasonally adjusted. n.a.--not available.

^{1/} Average of daily figures. ^{2/} Averages for statement week ending December 30.^{3/} Latest figure indicated is for month of November. ^{4/} Data are for weekly closing prices. ^{5/} Change in December.

U.S. BALANCE OF PAYMENTS

| | 1964 | | | | | | 1963 |
|--|--------|--------|--------|--------|--------|--------|-------|
| | Nov. | Oct. | Sept. | QIII | QII | QI | Year |
| Seasonally adjusted annual rates, in billions of dollars | | | | | | | |
| Balance on regular trans. | | | | 2.3 | 2.8 | 1.0 | - 3.3 |
| Exports <u>1/</u> | 25.2 | 26.8 | 25.4 | 24.1 | 24.4 | 21.9 | |
| Imports <u>1/</u> | - 18.6 | - 18.6 | - 18.9 | - 18.3 | - 17.5 | - 16.9 | |
| Trade balance <u>1/</u> | 6.6 | 8.2 | 6.5 | 5.8 | 6.9 | 5.0 | |
| Unadjusted monthly averages, in millions of dollars | | | | | | | |
| Balance on regular trans. | -289 | - 825 | - 63 | - 339 | - 196 | 23 | - 272 |
| Trade balance <u>1/</u> | | 626 | 506 | 421 | 565 | 587 | 416 |
| Securities transactions | - 160 | - 73 | - 36 | - 69 | - 15 | - 70 | |
| Bank-reported claims <u>2/</u> | -250 | - 219 | - 137 | - 48 | - 199 | - 212 | - 123 |
| Other | - 1072 | - 359 | - 676 | - 493 | - 337 | - 495 | |
| Financing, total | 289 | 825 | 63 | 339 | 196 | - 23 | 272 |
| Special receipts <u>3/</u> | 0 | 0 | 0 | 2 | - 10 | 68 | 55 |
| Liabilities increase | | | | | | | |
| To nonofficial <u>4/</u> | 540 | 678 | - 141 | 187 | 36 | 77 | 49 |
| To official | 378 | 12 | 35 | 127 | 69 | - 151 | 136 |
| Monetary reserves decrease | -629 | 135 | 169 | 23 | 101 | - 17 | 32 |
| of which: Gold sales | (40) | (37) | (14) | (-7) | (-24) | (15) | (38) |

1/ Balance of payments basis; differs a little from Census basis.

2/ Adjusted for changes in coverage and for long-term claims taken over from nonfinancial concerns.

3/ Other than nonmarketable bonds, which are included in liabilities to official. Advances on military exports are assumed as zero for individual months in absence of information.

4/ Including international institutions (except IMF), commercial banks and private nonbank.

Most recently prospects have improved for a lessening of upward pressures on prices in nonferrous metal markets. Tin prices fell back more than half way from the October high after announcement of an increase in the amount of the metal available from the stockpile. More importantly, copper production has recovered from the strikes and other disturbances of last summer, and recently prices in the "free" markets have fallen sharply.

As the pressures lessen in some nonferrous metal markets, steel producers have increased prices of galvanized products 2 to 3 per cent. The effect on the index for steel mill products is likely to be less than .3 per cent. Steel mill products account for about 5 per cent of all industrial commodities. The important question is whether this increase signals the beginning of a series of increases for steel. There is no doubt that temporarily the market is strong enough to support higher prices, owing partly to inventory demand arising from the threat of a strike. The extent to which price increases effected now will hold after the strike threat is over is uncertain. It will depend importantly on market demand conditions but also on the amount of increase in wages and fringe benefits provided in the new contract, the extent of cost reduction being effected gradually by introduction of new equipment, and the nature of foreign competition.

In 1963, prices were raised for most steel products, in two stages, with an impact on the index for steel products of 2 per cent. Prices of some products eased last summer, however, and even with the latest rise, the index now is little more than 1 per cent higher than

early in 1963. In the three years 1955 through 1957, steel prices rose at a rate of 8 per cent per year.

The consumer price index rose .2 per cent in November and for the third consecutive month was 1.2 per cent higher than a year earlier. According to BLS, early figures indicate no change in December. If the final figure is unchanged from November, the 1964 rise in the index will be 1.0 per cent--the smallest increase since 1961.

Much of the November rise was attributable to autos. Prices after discounts were seasonally higher for the new models; prices of used cars increased contraseasonally because of fewer trade-ins during the period when sales of new cars were limited by strikes; insurance premiums for the new autos were up substantially. Apparel and fuel increased about seasonally and foods changed little.

CONSUMER PRICES

| | Per cent increase to November from: | |
|--------------------|-------------------------------------|---------------|
| | October 1964 | November 1963 |
| All items | .2 | 1.2 |
| Food | -.1 | 1.6 |
| Apparel | .3 | .3 |
| Other nondurables | 0 | .3 |
| New cars | 1.2 | -.7 |
| Used cars | .8 | 1.6 |
| Household durables | 0 | -.8 |
| Rent | .1 | 1.0 |
| Other services | .3 | 2.1 |

Labor market. Strength in trade and manufacturing apparently pushed nonfarm employment up to new record levels in December. With

the labor force continuing to rise, however, unemployment probably showed little change from the November rate of 5.0 per cent; the rate in December 1963 was 5.5 per cent.

For 1964, as a whole, employment rose somewhat more than the labor force and unemployment declined from 5.7 per cent to an average of 5.2 per cent, the lowest for any year since 1957, when it was 4.3 per cent. Much of the decline this year was among adult male workers, reflecting substantial increases in industrial employment during the year, with demands for labor buttressed at year-end by inventory accumulation in the metal producing and using industries. For adult males the unemployment rate averaged about 3.8 per cent in 1964, compared with 4.5 per cent in 1963. At year-end, the rate was below the average for the year. Rising activity and higher employment, however, had little impact on the unemployment rate of younger workers. Teenage employment was up some 300,000 in 1964, but about 15 per cent of the teenagers in the labor force was unemployed, the same percentage as in 1963, and a rate sharply higher than the 10.8 per cent in 1957.

**LABOR FORCE, EMPLOYMENT AND UNEMPLOYMENT
(Annual averages)**

| | 1964* | 1963 | Change |
|----------------------------|-------|------|--------|
| <u>Millions of persons</u> | | | |
| Civilian labor force | 74.2 | 73.0 | 1.2 |
| Employment | 70.3 | 68.8 | 1.5 |
| Nonagricultural | 65.6 | 63.9 | 1.7 |
| Agricultural | 4.7 | 4.9 | -0.2 |
| Unemployment | 3.9 | 4.2 | -0.3 |
| <u>Per cent</u> | | | |
| Unemployment rate | 5.2 | 5.7 | -- |

*--preliminary

In contrast to labor force increases of 1.1 million in 1963 and 1.2 million in 1964, the projected rise for 1965 is about 1.5 million. If this projection is realized, an increase in employment this year comparable to the large gain of 1964 would not result in a further reduction in unemployment, assuming continuation of current productivity trends and hours of work. The expected sharper rise in the labor force in 1965 mainly reflects an extremely large increase in high school graduates entering the labor force.

Earnings and unit labor costs. The rise in hourly earnings in manufacturing has shown no tendency to accelerate. In November, at \$2.56 an hour, earnings were about the same as in September; over the 12 months from November 1963, hourly earnings increased 7 cents or 2.8 per cent, about the same percentage as over the previous 12-month period. Fringe benefits in manufacturing, represented by employer contributions to social security, pension and other funds, have continued to rise somewhat more rapidly than hourly earnings. Such benefits increased 4.3 per cent per employee over the year.

Combining wages and salaries and fringes, total compensation per employee increased about 3.3 per cent, close to the guidepost target and somewhat less than the rise in productivity in manufacturing. Output per manhour in manufacturing continued to rise in 1964 at about a 4 per cent rate.

Labor costs per unit of output in manufacturing, which reflect changes in both productivity and total compensation, declined in November following a rise during the strike-affected months of September and October. In December, with automobile output increasing

further, another decline in unit labor costs seems likely, to a level not much different than that in late summer. On the whole, unit labor costs remained relatively stable in 1964, showing no significant trend.

Industrial relations. Although the New York Shipping Association and the Longshoremen's union reached agreement on a new 4-year contract, there is uncertainty as to whether the contract will be ratified by the union membership this weekend. In New York and other East Coast ports questions of interpretation of various contract clauses, especially those dealing with crew size have delayed ratification. In Galveston and Houston negotiations over the size of crews have not yet been completed. Members of the union in New York are to vote on the proposed agreement January 8, and ratification in other ports must be completed by January 11. If the union members fail to accept the contract, they would be free to strike.

The agreement over cargo gang size allows a reduction in the size of crews from 20 to 17 men by October 1967. In exchange, the contract provides for wage rate increases of 10 cents in both October 1964 and 1965; and of 8 cents in both October 1966 and 1967-- the basic wage rate currently is \$3.26 per hour. In addition, certain union members with seniority are guaranteed 1,600 hours of work or pay and an annual salary of \$5,792. Cost of this provision will depend on future employment conditions in the industry. Employers also agreed to increase payments into the pension, health, and welfare funds from 32 cents to 46-1/2 cents per hour. Paid holidays are increased to 12 from 9, and workers with more than 12 years of service receive a fourth week of vacation.

Consumers. Seasonally adjusted retail sales in December (based on data for four weeks) rose sharply from the reduced October-November level and may have exceeded the high reached last summer. The sharp December increase in retail sales, like the preceding decline was mainly attributable to autos, as supplies increased substantially. Furniture and appliance sales apparently were up from November and were near their June-July peak. Nondurable goods sales were up moderately from the reduced November level, mainly reflecting gains at gasoline and general merchandise outlets, and they were about at the high of last summer.

Preliminary reports of sales for December by the three largest producers of domestic autos were 13 per cent above a year earlier, setting a record seasonally adjusted annual rate of over 9.0 million units. Despite the autumn strike, a record 7.6 million domestic cars were sold in 1964, and at year-end dealer stocks were not far from a year earlier. Adding the half-million imported vehicles total sales will set a historic mark of 8.1 million new cars for 1964.

For the fourth quarter as a whole, the increase in consumer spending was quite small, the smallest of this long expansion period. Purchases of goods apparently were down somewhat on balance, while outlays for services continued their steady rise.

The failure of consumer spending to expand more last quarter was primarily--but not entirely--attributable to limited availability of autos for which expenditures were down substantially. Thus,

furniture and appliance sales were little changed from the preceding quarter. Sales of nondurable goods were up only a little, in contrast to sharp increases in the preceding quarters of 1964.

Meanwhile, personal income showed another substantial increase in the fourth quarter notwithstanding loss of income because of the auto strikes, and exceeded an annual rate of \$500 billion.

With consumer after-tax income up \$6 billion or so and spending up only a little, the personal saving rate rose sharply from 7.1 per cent in the third quarter to around 8 per cent. This was about the same as the high second quarter rate when the tax cut was first effective for an entire quarter.

Orders for durable goods. New orders for durable goods declined 1 per cent in November, as orders for defense products declined sharply. New orders for civilian products showed a substantial rise but remained below earlier highs because strikes continued to limit activity in the auto industry. New orders for machinery and equipment (a special Census classification of producers' equipment industries) rose further in November recovering to about the record May-June level. New orders for primary metals remained at advanced levels.

The level of new orders remained somewhat above shipments in November and the backlog of unfilled orders continued the expansion that began last January.

Business inventories. Changes in inventory investment are of key cyclical significance and for this reason the recent acceleration in accumulation of stocks is of special interest. Inventory accumulation has accelerated at manufacturers since mid-1964--owing in part to the emerging steel stock build-up--but distributors' inventories were about unchanged from June to September and then dropped sharply in October because of the General Motors' strike. The October decline at distributors was enough to offset an extraordinarily large rise at manufacturers. Thus, total business inventory accumulation was quite small in the summer and early fall,

In November, the pace of over-all inventory accumulation was stepped up sharply, as manufacturers' stocks continued to rise rapidly and as auto stock rebuilding at dealers began. Present indications suggest continuation of a high rate of accumulation in December and in early 1965 as the build-up of steel and auto stocks proceeds. Moreover, recent inventory data suggest that manufacturers generally have stepped up accumulation--at least through the fourth quarter--in part as a make-up for the very low rates in the first half of 1964, when stock-sales ratios declined.

The book value increase at manufacturers in November totaled \$500 million. This amount, on top of a \$750 million increase in October (revised upward \$200 million from the preliminary figure) resulted in an exceptionally large two-month increase. Manufacturers in the November survey had reported expectations of only a \$1.2 billion accumulation for the fourth quarter as a whole and this has now been exceeded in October and November alone.

CHANGE IN BOOK VALUE OF BUSINESS INVENTORIES
(Millions of dollars, seasonally adjusted)

| | Total | Manufacturers | | Distribu- tors |
|---------------------------|-------|---------------|------------------|-------------------|
| | | Total | Durable goods | |
| <u>Quarterly changes:</u> | | | | |
| 1963 - IVQ | 1,987 | 1,060 | 492 | 568 |
| 1964 - IQ | 594 | 179 | 51 | 128 |
| IIQ | 900 | 72 | 413 | -341 |
| IIIQ | 702 | 621 | 545 | 76 |
| <u>Monthly changes:</u> | | | | |
| October | -12 | 758 | 480 | 278 |
| November | n.a. | 510 | 421 | 89 |

The auto strikes contributed significantly to the unusually large October increase at manufacturers; in that month inventories in the auto industry increased abruptly by about \$200 million as parts accumulated and auto plants took delivery of steel even when auto assemblies were shut down. Some reversal of this rise may have occurred in December and the rate of total accumulation by manufacturers may have slowed somewhat. Nevertheless, it now appears likely that the fourth quarter increase appreciably exceeded manufacturers' anticipations.

Over two-thirds of the rise in manufacturers' inventories during October and November occurred in durable goods industries, and within these industries, materials, work-in-process, and finished goods shared about equally. However, the increase in stocks of materials represented a pronounced step-up from earlier rates of gain and reflected in part a speed-up in accumulation of steel.

Stocks held by nondurable goods producers increased \$350 million from the end of September to the end of November. This increase was about in line with producers' anticipations and brought the book

value of such inventories from a level slightly below, to a level still only moderately higher than at the end of 1963.

Manufacturers' sales rose in November, following a decline in October, and were somewhat above September. The rise in inventories considerably exceeded the sales increase from September to November, however, and the over-all stock-sales ratio rose from 1.64 to 1.66. At 1.66 the ratio was back close to last winter's levels before the decline last spring and summer, but the November ratio was still below the average levels in 1963 and 1962.

Residential building. Seasonally adjusted housing starts, which had advanced sharply in the two preceding months, dropped in November to a new low for 1964. On a three-month moving average, however, the annual rate in September-November, at nearly 1.5 million was unchanged from the preceding period, but appreciably below the recent high reached in the autumn of 1963.

In contrast to starts, seasonally adjusted residential permits rose in November with permits for 1-to-4 family buildings accounting for all of the rise. Permits for 5-or-more-family structures, which had been moving toward a record peak at this time in 1963, declined further.

PRIVATE HOUSING STARTS AND PERMITS

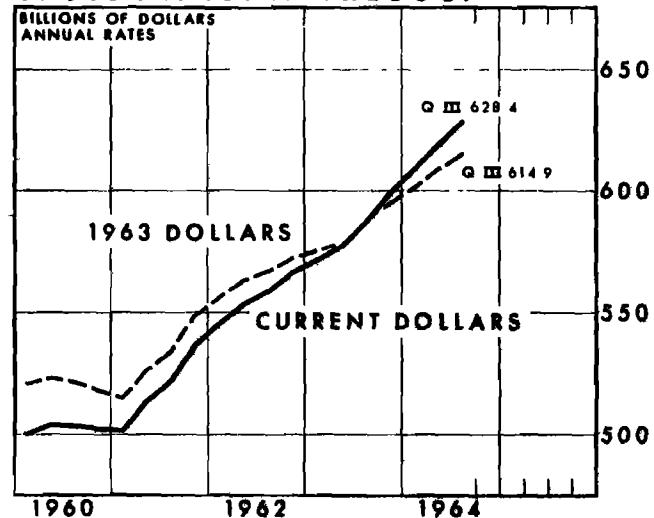
| | November (thousands of units) 1/ | Per cent change from: | |
|-----------------|--|-----------------------|----------|
| | | Month ago | Year ago |
| Starts (total) | 1,420 | -11 | -10 |
| Permits (total) | 1,257 | +3 | -8 |
| 1 - family | 744 | +8 | +1 |
| 2-4 - family | 106 | +14 | -17 |
| 5 or more | 407 | -7 | -17 |

1/ Seasonally adjusted annual rate; preliminary.

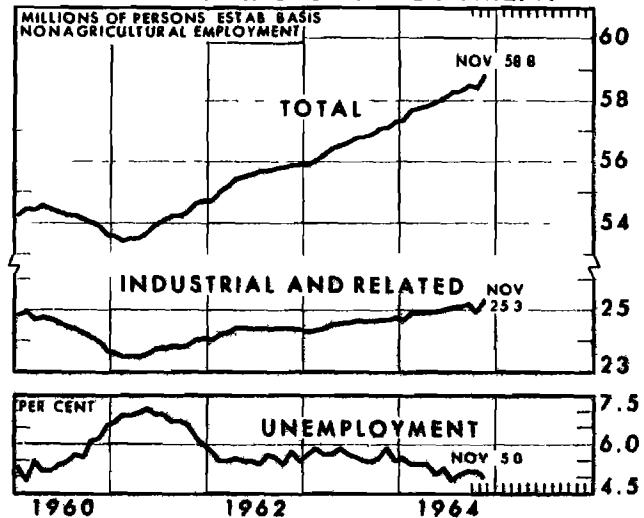
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

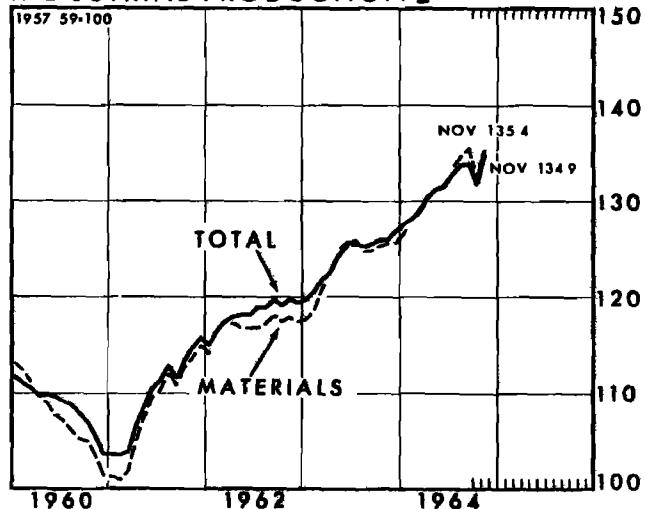
GROSS NATIONAL PRODUCT



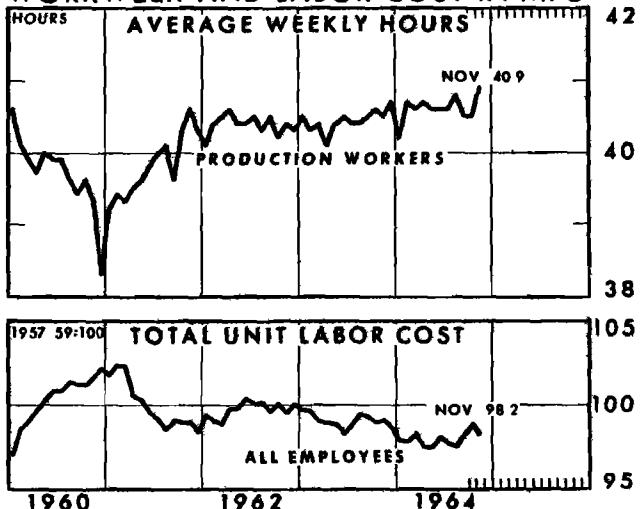
EMPLOYMENT AND UNEMPLOYMENT



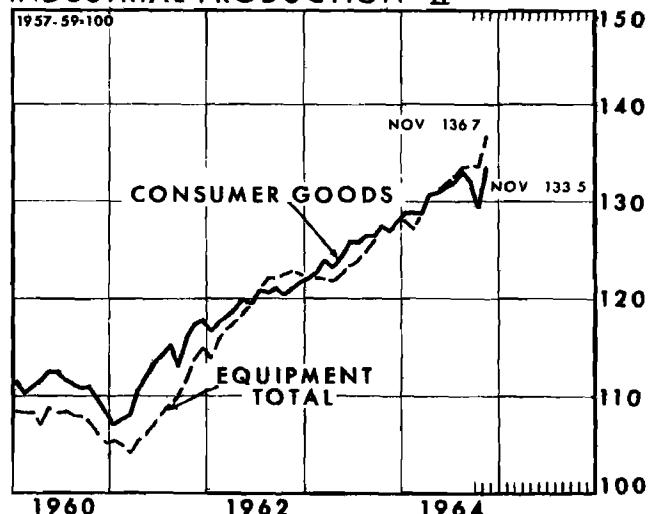
INDUSTRIAL PRODUCTION-I



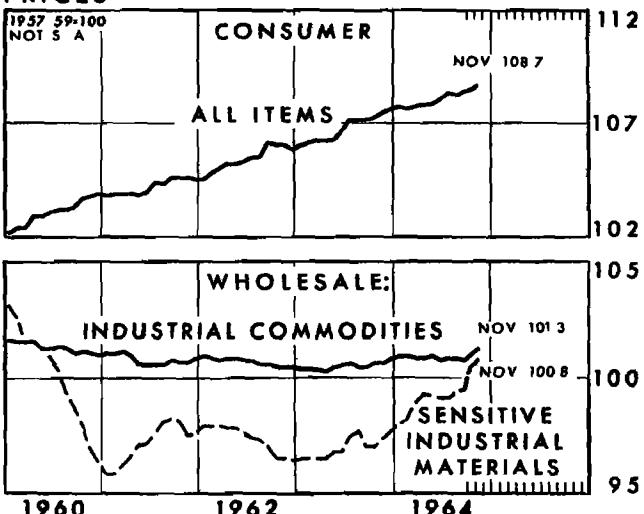
WORKWEEK AND LABOR COST IN MFG



INDUSTRIAL PRODUCTION-II



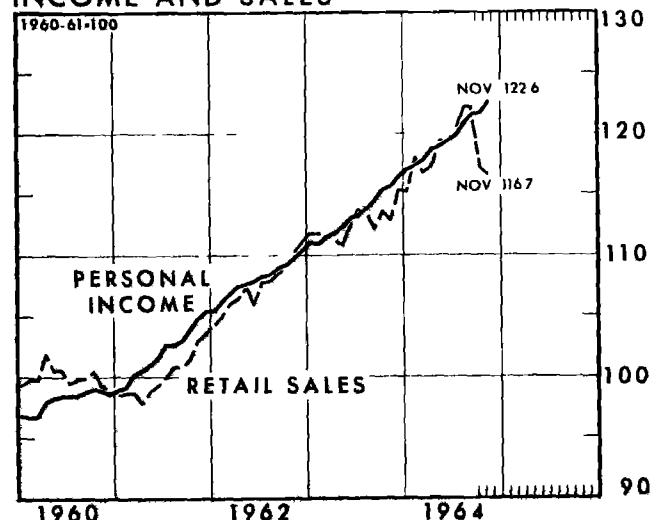
PRICES



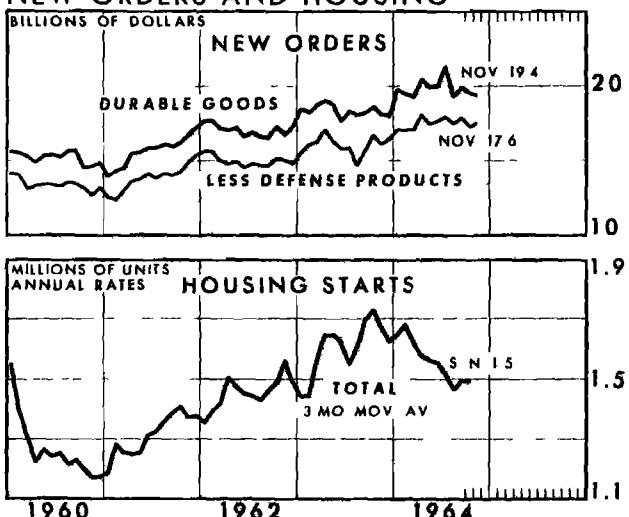
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

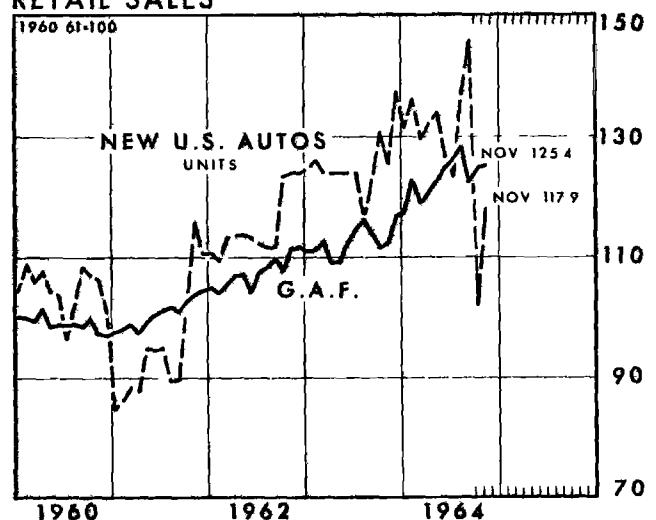
INCOME AND SALES



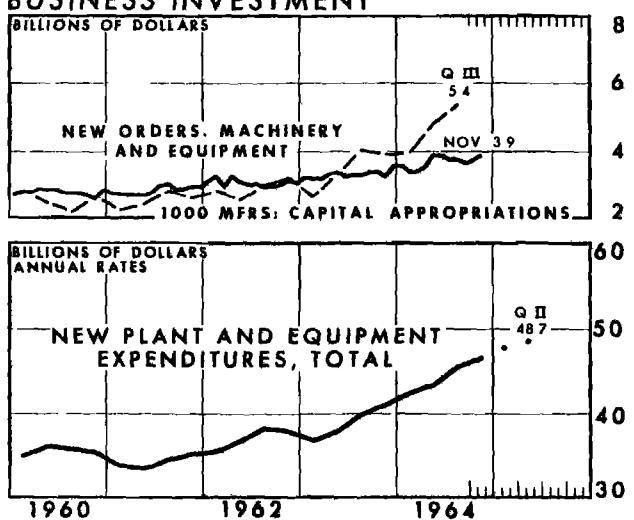
NEW ORDERS AND HOUSING



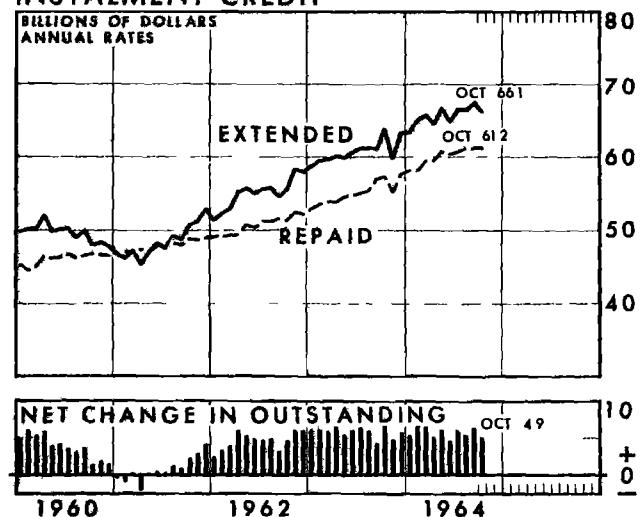
RETAIL SALES



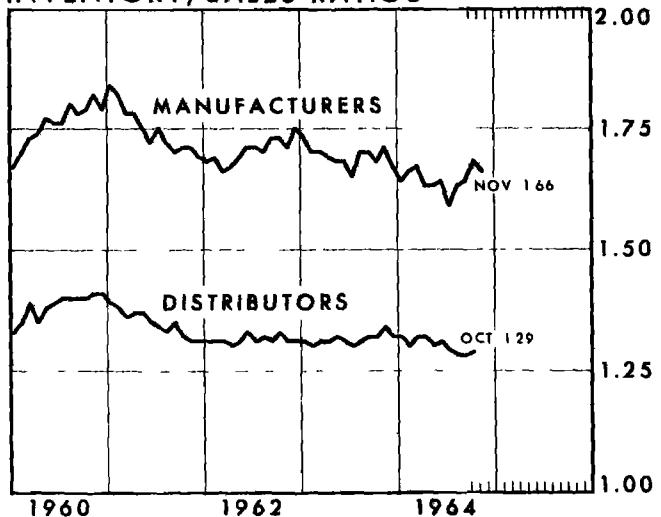
BUSINESS INVESTMENT



INSTALMENT CREDIT



INVENTORY/SALES RATIOS



DOMESTIC FINANCIAL SITUATION

U. S. Government securities market. Prior to the Treasury advance refunding announcement on December 30, yields were edging higher in the Treasury bond market, as the market reflected discussion of Treasury financing possibilities involving longer-term issues and also continuing concern over the international position of sterling. By December 30, yields on issues with 5 years or more to maturity had returned close to the levels reached shortly after the November discount rate action, but yields on shorter-term coupon issues remained below such levels. This rate pattern resulted in part from dealer efforts to work down their holdings of Treasury bonds due in more than 5 years, which declined from \$225 million on December 15 to \$135 million on December 30, and to increase their holdings of shorter-term coupon obligations. By the end of 1964 yields on Treasury securities were generally above year-earlier levels; the yield curve had flattened further, however, as yield increases over the year varied from 31 basis points for the 3-month bill to just one basis point on 20-year bonds.

YIELDS ON U. S. GOVERNMENT SECURITIES

| Date (closing bids) | 3-month bills | 6-month bills | 3 years | 5 years | 10 years | 20 years |
|-----------------------------|------------------|------------------|---------|---------|----------|----------|
| <u>Year-end comparisons</u> | | | | | | |
| 1962, December 31 | 2.92 | 2.96 | 3.40 | 3.56 | 3.85 | 3.92 |
| 1963, December 31 | 3.51 | 3.64 | 4.01 | 4.04 | 4.13 | 4.19 |
| 1964, December 31 | 3.82 | 3.92 | 4.06 | 4.11 | 4.20 | 4.20 |
| <u>1964-65</u> | | | | | | |
| November 20 | 3.62 | 3.80 | 4.02 | 4.01 | 4.13 | 4.15 |
| December 1 | 3.88 | 4.03 | 4.14 | 4.13 | 4.21 | 4.21 |
| December 15 | 3.87 | 3.96 | 4.06 | 4.07 | 4.17 | 4.16 |
| December 30 | 3.84 | 3.93 | 4.07 | 4.09 | 4.20 | 4.21 |
| January 5 | 3.82 | 3.92 | 4.06 | 4.12 | 4.20 | 4.20 |

The demand for intermediate- and long-term Treasury securities that kept longer-term yields relatively stable in 1964 has continued in evidence in the first trading days of 1965, contributing to the favorable initial market reception accorded the Treasury's advance refunding. In that offering, a total of \$33.1 billion of securities due from February 1965 to November 1967, including \$22.1 billion held by private investors, was made eligible for exchange into new 4's of February 1970, new 4-1/8's of February 1974, or the reopened 4-1/4's of August 1987-92. Downward price adjustments on the outstanding bonds surrounding the new issues were relatively small following the announcement, partly because the financing had been anticipated and largely discounted.

One question raised by an advance refunding of this magnitude is the likely downward impact on short-term interest rates stemming from reinvestment demand by sellers of the "rights." After the announcement, it became more attractive to sell the "rights" as they generally rose in price by around 4/32 or 5/32 by Tuesday. As a result, an associated demand for bills began to appear, but it was seemingly of moderate proportions.

The usual seasonal demand for bills also began to develop following the mid-December tax date, contributing to the subsequent reduction in yields on Treasury bills. Bill rates declined despite a tighter Federal funds market and higher dealer borrowing costs at money market banks; the latter were partly offset, however, by the large volume of repurchase agreements made by the System during the second half of December and in early January at 3-7/8 per cent. In the January 4 auction the average issuing rate on 3- and 6-month bills fell to 3.83 and

3.92 per cent respectively, after having been around 3.87 and 3.96 per cent in the previous three auctions.

The Treasury's announcement that it would shortly be offering \$1.5 to \$2.0 billion of June tax anticipation bills should help to maintain upward pressure on bill rates in coming weeks. The Treasury may also raise additional cash by adding to the regular weekly auctions of bills. In total, the Treasury may need to raise around \$2.5 billion in cash by mid-February, but thereafter it should be in a position to retire debt out of the first half year seasonal surplus.

The next regularly scheduled Treasury financing will involve the balance of the February maturities that are not exchanged in the advance refunding. This refinancing will probably be announced in late January and will no doubt involve a short-term coupon offering so as not to interfere with market absorption of the advance refunding issues.

Corporate and municipal bond markets. Corporate and municipal bond markets have remained steady since mid-December. Forces tending to increase yields--such as the anticipation and subsequent announcement of the Treasury advance refunding, the unusually heavy volume of municipal offerings in December, and the unexpected addition of \$200 million World Bank bonds to the January calendar--have apparently been fairly well balanced by offsetting forces--such as the continued paucity of corporate bond offerings, the usual turn-of-the-year pickup in flows of investment funds, and some lessening of the crisis atmosphere regarding the British financial situation.

At the start of the new year, yields on high grade municipal bonds are at the lowest level since May 1963, 10 basis points below the

sterling crisis high of late November and some 12 basis points below a year ago. With yields on U. S. Treasury and high grade corporate bonds at levels close to or above a year ago, spreads within the structure of long-term yields have widened, particularly the one between high grade municipals and U. S. Governments. This latter differential has grown to more than 1-1/8 percentage points; in absolute size this is slightly larger than the previous peak spread that prevailed between these two series in early 1951, shortly after the Korean War excess profits tax was introduced. At that time, however, all bond yields were at considerably lower levels.

The further decline of yields on municipals relative to other types of bonds since the sterling crisis apparently reflects market expectations that bank interest in municipal issues will be stronger--as a result of the late November change in Regulation Q. Recent increases of rates paid on commercial bank time and savings deposits have improved the competitive position of many banks vis a vis other savings institutions and are expected to encourage bank investment in assets that provide more favorable returns.

BOND YIELDS
 (Weekly averages - per cent per annum)

| | Corporate | | State and local government | |
|--------------------|--------------------|-------------|----------------------------|---------------------------------|
| | New | Seasoned | Moody's Aaa | Bond buyer (mixed qualities) |
| 1962 - Year-end | 4.24 | 4.23 | 2.94 | 3.05 |
| 1963 - " | 4.54 | 4.37 | 3.11 | 3.26 |
| 1964 - " | 4.47 ^{1/} | 4.43 | 2.99 | 3.12 |
| 1964 - High | 4.54(8/8) | 4.45(12/11) | 3.16(3/26) | 3.32(4/21) |
| Low | 4.30(2/21) | 4.35(7/28) | 2.99(12/31) | 3.12(12/31) |
| <u>Week ending</u> | | | | |
| 1964 - Nov. 27 | n.a. | 4.44 | 3.09 | 3.21 |
| Dec. 18 | n.a. | 4.43 | 2.99 | 3.12 |
| 1965 - Jan. 1 | n.a. | 4.43 | 2.99 | 3.12 |

1/ Week ending December 4.

Firmness persisted in municipal bond prices during December, even though the supply of new offerings totaled over \$1 billion, a record for any December and the second largest monthly total in 1964. New supply is expected to drop back to about \$850 million in January, with the bulk of offerings concentrated in the latter half of the month. Anticipation of this January financing pattern, in combination with turn-of-the-year reinvestment demands, apparently encouraged dealers to take on December offerings. Although the blue list of dealers' advertised inventories swelled to nearly \$730 million late in December, it has since fallen below \$700 million.

BOND OFFERINGS ^{1/}
 (millions of dollars)

| | Corporate | | State & local government | |
|-----------------------|---------------------|-----------------------|--------------------------|------------------|
| | Public offerings | Private placements | Current period | Previous year |
| 1964 - Jan.-Oct. avg. | 328 | 390 | 494 | 486 |
| November | 30e/ | 183 | 600e/ | 549 |
| December | 305e/ | 626 | 800e/ | 751 |
| 1965 - January | 200e/ | 338 | 500e/ | 526 |
| | | | 915e/ | 929 |
| | | | | |

1/ Includes refundings--data are gross proceeds for corporate offerings and principal amounts for State and local government issues.

Continued stability in the corporate bond market has reflected chiefly the scarcity of new publicly-offered issues. In the final quarter of 1964 the monthly volume of such offerings averaged only \$170 million, roughly half the monthly average for the preceding 9 months; and the January supply is expected to remain quite light. While the volume of private placements appears to have been at record levels recently--and for the year may have accounted for more than five-eighths of total new corporate bond offerings--the supply of publicly-offered issues seems to exert the major impact on published bond market yields.

Stock market. Common stock prices, after approaching their lows for the month, staged an active two-day rally at the very end of 1964, as investors sought to reinvest funds accumulated from earlier "year-end" selling. On the first trading day of 1965, prices turned down again on low volume, but after the President's State of the Union message most of this first day decline was recovered.

Standard and Poor's composite index of 500 stocks closed at 84.63 on January 5, up from the December low of 83.22, but 2 per cent below the record November 20 high of 86.28. In addition to concern about the future prospects of sterling, the general hesitancy of stock prices in recent weeks has apparently reflected continued uncertainty about the likely course of wage costs and corporate profit margins in 1965.

During 1964 the Standard and Poor's index rose 13 per cent, which compares with gains of 19 per cent in 1963 and 24 per cent in 1961. Roughly nine-tenths of the 1964 advance occurred in the first 6-1/2 months. The limited further rise in the latter half of the year was accompanied by more erratic swings in prices.

Mortgage markets. Mortgage markets continued little changed in the latter part of 1964 and, with mortgage funds remaining ample, trade expectations are for maintenance of this trend into 1965. In November, secondary market yields on FHA-insured mortgages remained at 5.45 per cent, an average which--with slight exception--has prevailed for nearly two years. Contract interest rates for conventional home mortgages also held at earlier reduced levels--5.80 per cent for loans on new homes and 5.85 per cent for loans on existing houses.

Foreclosures on nonfarm real estate--mainly homes--dipped slightly from the second to the third quarter of 1964, reflecting a drop in foreclosures of government-underwritten mortgages and a moderate further rise in foreclosures on conventional mortgages. These shifts appeared to be largely seasonal, however. On a year-to-year basis, third-quarter foreclosures on government-underwritten and conventional mortgages combined were 13 per cent higher than in 1963 when they were also 13 per cent higher than in 1962. But in the preceding years, rates of increase had been higher, as the table shows.

NONFARM MORTGAGE FORECLOSURES

| | Number (In thousands) <u>1/</u> | Year over year increase (per cent) | Rate per thousand mortgaged homes |
|--------------------|------------------------------------|--|--------------------------------------|
| 1964 Third quarter | 112.0 | + 13 | 4.8 |
| 1963 " " | 98.8 | + 13 | 4.5 |
| 1962 " " | 87.2 | + 18 | 4.2 |
| 1961 " " | 74.0 | + 38 | 3.7 |
| 1960 " " | 53.8 | + 26 | 2.8 |

1/ Annual rate.

Bank credit. Growth in city bank credit over the four weeks ending December 23 was somewhat smaller than in the corresponding weeks of most other recent years, as a larger-than-usual loan rise was offset in part by a contra-seasonal reduction in holdings of U.S. Government securities. These holdings declined substantially in early December, reflecting in part secondary distribution of Treasury issues acquired in the late November financings, but they subsequently rose somewhat as is usual.

NET CHANGE IN CITY BANK CREDIT
FIRST FOUR REPORTING WEEKS OF DECEMBER
(In millions of dollars)

| | 1964 | 1963 | 1962 | 1961 | 1960 |
|---------------------------|-------|-------|-------|-------|-------|
| Total loans & investments | 3,191 | 3,633 | 4,468 | 3,106 | 3,524 |
| Loans | 2,985 | 2,457 | 3,450 | 2,068 | 2,201 |
| U.S. Govt. securities | -198 | 650 | 684 | 634 | 790 |
| Other securities | 404 | 526 | 334 | 404 | 533 |
| Type of loan: | | | | | |
| Business | 1,120 | 604 | 486 | 709 | 441 |
| Real estate | 119 | 75 | 105 | 81 | -20 |
| Security | 97 | 389 | 1,664 | 334 | 1,017 |
| Nonbank financial | 858 | 919 | 926 | 636 | 638 |
| "Other" | 675 | 301 | 191 | 223 | 79 |

While the credit rise reported through December 23 was relatively moderate and the usual temporary year-end credit bulge was probably similar to other years, there may have been an additional short-lived increase on December 31, when \$3.2 billion maturing Treasury bills were exchanged for new bills. Net bank acquisitions of these bills along with associated borrowing by security dealers may

have resulted in a larger year-end credit rise than in other years when bill financing was not concentrated on the year-end date. Based on these assumptions, the December increase in seasonally adjusted total credit at all commercial banks is tentatively estimated at \$1.5-2.0 billion, bringing the total growth for the year to about 8 per cent, the same as in 1963.

Business loans at city banks over the four weeks ending December 23 increased \$1.1 billion, almost twice as much as the substantial rise in the corresponding weeks last year. Borrowing was unusually heavy in the week of December 2, presumably in part to cover anticipated tax and dividend period needs in advance of a possible increase in the prime rate, and again in the week of the 16th, which included both the dividend and tax payment dates. Both corporate tax and dividend payments were larger this year than a year ago, and there were no maturing tax securities in either year.

Borrowing over the four weeks by public utilities, metals companies, and petroleum and chemicals companies was larger than in the comparable weeks of any other year following some slackening during the autumn. Bank purchases of bankers' acceptances and loans to the service industries also were unusually large. On the other hand, borrowing by food processors and repayments by commodity dealers and trade concerns appeared to be about seasonal proportions.

Security loans, which had been high at the time of the Treasury financing in late November, rose less in the four weeks ending December 23 than in the corresponding weeks of other recent years. Dealer loans on

U.S. Government securities showed a small contra-seasonal decline while other security loans rose somewhat less than usual. Loans to nonbank financial institutions rose about in line with the large December increases of other recent years. An unusually large increase in "other loans" reflected city bank purchases of practically the entire \$450 million Export-Import Bank participation certificates sold in late November.

Money supply, turnover, and time deposits. The seasonally adjusted money supply increased \$400 million in December, or at a somewhat slower rate than in the August-November period. Expansion was substantial in early December, but slackened in the second half of the month. U.S. Government deposits at commercial banks showed little change on a seasonally adjusted basis. Over the year, the money supply rose 4.1 per cent compared with 3.8 per cent in 1963.

Turnover of demand deposits at 343 centers outside New York averaged 35.5 in November, the same as in October but 5.7 per cent above a year earlier. Since the April peak, turnover has fluctuated within a relatively narrow range and has shown no discernible trend.

Seasonally adjusted time and savings deposits at all commercial banks increased \$1.4 billion in December, well below the sharp \$2 billion November rise but somewhat above the substantial rates of gain in the August-October period. Most of the increase occurred in the first half of the month, reflecting in part an unusually large inflow of State and local government funds in the New York and San Francisco Districts; growth moderated in the second half. Since July, expansion has been at an annual rate of 14.3 per cent, considerably

faster than earlier in the year. Over the entire year, time and savings deposits increased 12.6 per cent compared with 14.7 per cent in 1963.

At weekly reporting banks growth in savings deposits in December exceeded last year's expansion by a wider margin than in the three preceding months. Time deposits, contrary to the recent trend, also rose more than in the corresponding weeks last year, but this reflected the sharp rise in deposits of State and local governments referred to above. Outstanding CD's have been showing divergent movements since early November--declining rather steadily at New York City banks and, except for a temporary tax-period decline, expanding at banks outside. Outstanding unsecured notes of banks have declined in recent weeks to a total of \$92 million on December 30 from a high of \$123 million on November 25, just after the Regulation Q ceilings were revised.

Bank reserves. Free reserves averaged \$139 million in December compared with a nominal level in November and an \$86 million average in September and October.^{1/} Member bank borrowings at \$278 million in December were down substantially from their temporarily high \$413 million average in November and were also somewhat below levels of the two previous months. Meanwhile, excess reserves at \$417 million in December were close to the average of other recent months. In the last statement week of the month, both borrowings and excess reserves were temporarily high as is usual at this time of year.

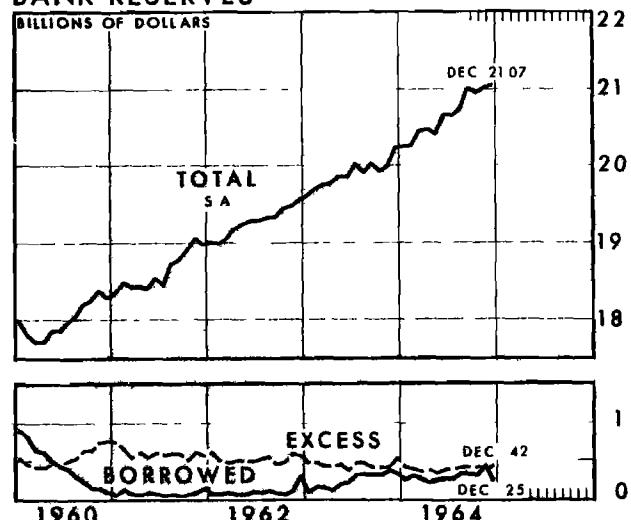
1/ Based on the average of daily figures for all of the reserve weeks ending in the month as used in the reserve memorandum to the FOMC.

Except for five days in early December, the effective rate on Federal funds was consistently at 4 per cent in the December reserve period. Some transactions took place below the 4 per cent rate on 11 days of that period, all prior to December 17.

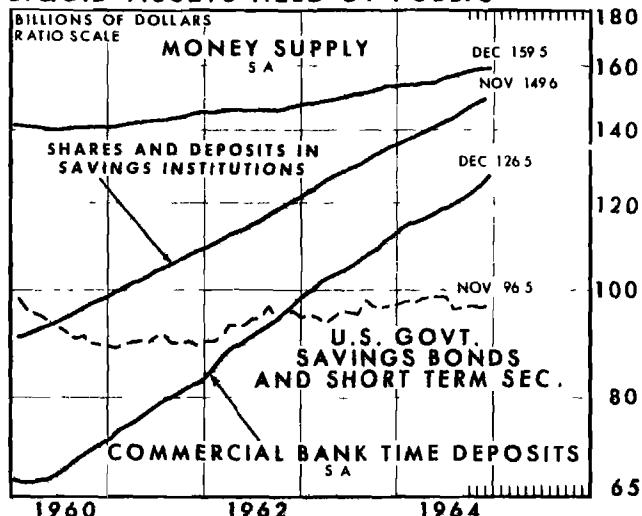
Seasonally adjusted reserves required against private demand deposits rose at an annual rate of over 5 per cent in December, about the same as in October and in contrast with a small decline in November.

FINANCIAL DEVELOPMENTS - UNITED STATES

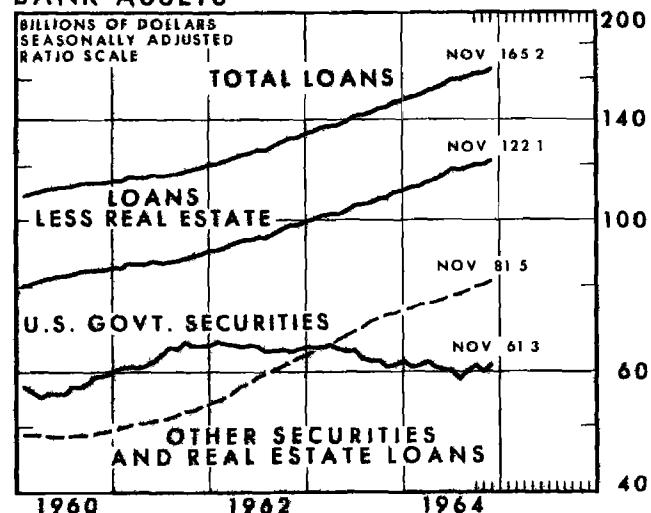
BANK RESERVES



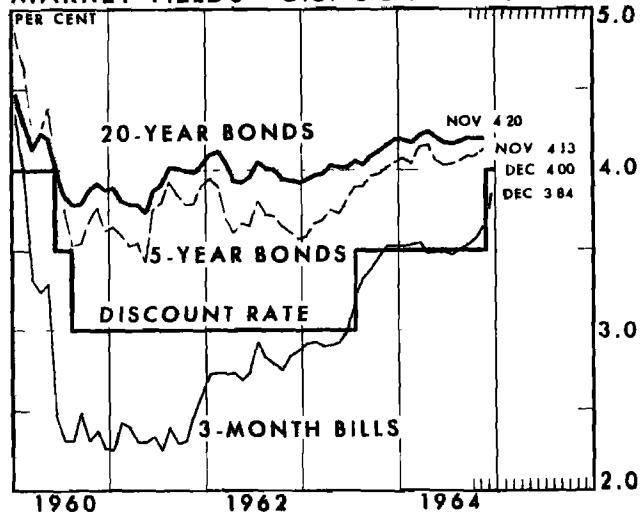
LIQUID ASSETS HELD BY PUBLIC



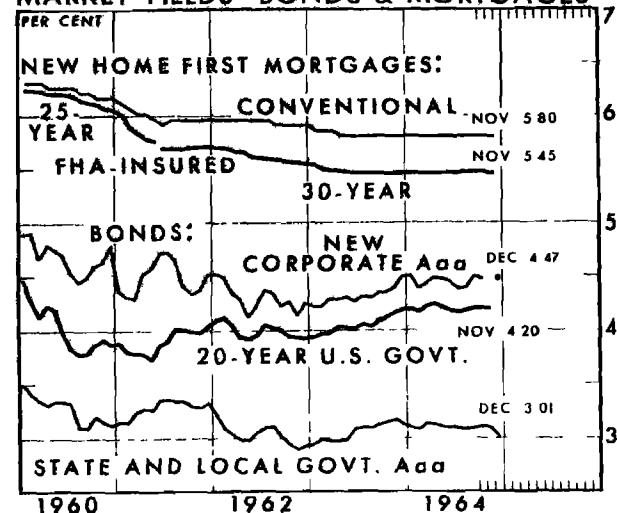
BANK ASSETS



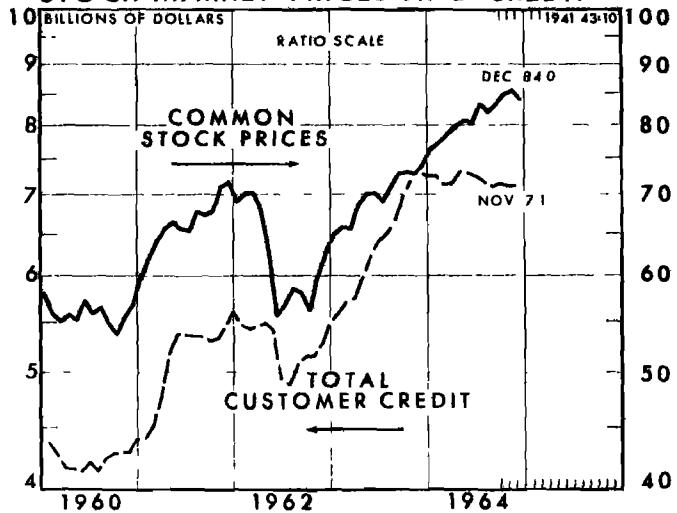
MARKET YIELDS - U.S. GOVT. SEC.



MARKET YIELDS - BONDS & MORTGAGES



STOCK MARKET PRICES AND CREDIT



INTERNATIONAL DEVELOPMENTS

U.S. balance of payments. The over-all deficit on regular transaction in the balance of payments in 1964 now appears to have totaled \$2.5 billion. Preliminary estimates of the major elements in this outcome, which compares with a \$3.3 billion deficit in 1963, are shown in the following tabulation together with the corresponding figures for 1963 (in billions of dollars):

| | <u>1964</u> | <u>1963</u> |
|---------------------------------|-------------|-------------|
| Exports | 24.8 | 22.0 |
| Imports | <u>18.6</u> | <u>17.0</u> |
| Trade Surplus | <u>+6.2</u> | <u>+5.0</u> |
| Net services, etc. | +0.8 | -0.1 |
| Balance on above | +7.0 | +4.9 |
| Government grants & loans (net) | -3.7 | -3.9 |
| U.S. private capital (net) | -5.8 | -4.3 |
| Foreign non-liquid capital | +0.4 | +0.4 |
| Errors & omissions | -0.4 | -0.3 |
| Balance on regular transactions | -2.5 | -3.3 |

As is shown in the table, there was a marked expansion of net receipts from goods and services transactions to a record total of \$7 billion but also a very large rise in the outflow of U.S. private capital. The resulting deficit was financed to a much greater extent than in 1963 by a rise in liabilities to foreign commercial banks and other non-official holders: the rise in these liabilities totaled approximately \$1.5 billion and was perhaps in considerable part directly related to the

increase in capital outflows. The balance financed by changes in reserves and in liabilities to foreign official holders and by special transactions was about \$1 billion, compared to \$2.7 billion in 1963. The gold stock declined \$125 million in 1964.

The further expansion of the trade surplus in 1964 reflected a continuation during the year of the high rate of exports to Europe and Canada attained at the end of 1963, a rise for the first time in several years in exports to Latin America and a continued increase in shipments to other nonindustrial countries. These gains outpaced a rise in imports of about 10 per cent for the year as a whole. These trends appeared to be continuing throughout 1964 with perhaps some renewed advance in exports to Europe and Canada towards the end of the year. There was also in 1964 a very large increase (\$600 million) in net income from foreign investments, which accounted for most of the improvement on service transactions.

The outflow of private capital was at record or near-record levels throughout the year. The increased outflows of the first half of the year were mainly of short-term capital -- bank credit and liquid funds. Outflows of short-term capital diminished in the second half of the year, while out-flows of long-term bank loans and on foreign security issues increased. The higher level of new foreign security issues was concentrated in the fourth quarter and consisted mainly of Canadian issues; many of these issues had apparently been postponed until uncertainties about the passage and application of the interest equalization tax were resolved. The outflow of long-term bank loans to

foreigners totaled over \$800 million in 1964, up nearly \$300 million from 1963; available information indicates a significant step-up in commitments on these loans after mid-year.

Data on the fourth quarter are still incomplete, but on the basis of the information available, the over-all deficit is estimated at roughly \$1 billion for the quarter, or \$4 billion at an annual rate. This annual rate would represent an increase of nearly \$2 billion from the \$2.3 billion deficit in the third quarter. About \$1-1/2 billion of this increase (in annual rate terms) results from the bulge in new foreign security issues and another \$1/2 billion from Britain's failure to make its usual end-of-year payments (the amount actually involved is \$138 million). Excluding these exceptional factors, the deficit would have been of the order of \$2-1/2 billion in the fourth quarter, or about the same rate as for the year as a whole.

The British position. The Bank of England gave substantial support to both the spot and the forward exchange rates throughout December. The rate for spot sterling was maintained slightly above \$2.79 and the discount on 3-months forward sterling was prevented from widening beyond 2.7 per cent per annum except on 2 or 3 days. To provide a measure of relief to the reserve position, the British Government exercised its right to waive its end-of-year payments of \$174 million of interest and principal on the U.S. and Canadian loans. This together with substantial utilization of the facilities made available under the \$3 billion international assistance package allowed official reserve losses in December to be limited to only \$28 million.

British financial markets during December were affected by the continued movements out of sterling, further adjustments to the rise in Bank rate, continued uncertainties about prospective taxation of capital gains and company profits, and indications of a credit squeeze by the Bank of England. On December 9, the Bank of England addressed a letter to the commercial banks which requested the banks to exercise more selectivity in granting advances; lending for real estate development and for consumer finance were singled out for curtailment. Moral suasion of this sort has worked with indifferent success on previous occasions, except when coupled with measures to reduce over-all bank liquidity. In the December 9th letter, it was suggested that the Bank of England would not provide much relief to the banks' liquidity positions during the period of seasonal strain in February and March. As of mid-December, the liquid asset ratio of the banks was 30.6 per cent, a relatively low ratio for that time of year. During the preceding month the banks had been net sellers of long-term government securities and of Treasury bills to improve their cash position and to increase their loans; clearing bank advances as of mid-December were up nearly 15 per cent from a year earlier.

In mid-December, prices of long-term government securities began to fall sharply, after showing fairly modest declines in the two weeks following the rise in Bank rate. Markets became disorderly and on December 17 the Government broker announced that all maturities of government bonds would be supported at the then existing prices; this policy is apparently still largely in effect as bond prices have

changed little since then. Over the two-week period ending December 18, yields on long-term government bonds rose by 10 to 35 basis points, the largest increases being for the shorter maturities. In part, the fall in bond prices resulted from bank selling and from movements of funds out of sterling, but also purchases by institutional investors have reportedly been restrained by uncertainty about the application of the proposed capital gains tax to government securities. Other interest rates also moved up in December: rates on automobile loans by finance houses from 8 to 9 per cent, and building society rates on home loans by 1/4 per cent. On the other hand, the Treasury bill rate remained at 6.41 per cent throughout December and has since moved up only 3 basis points. In view of the recent Bank of England support of the government securities market, it is not clear how severe the credit squeeze has been so far.

The Government is evidently pinning much of its hopes of solving Britain's economic problems on its "incomes" policy. On December 16, representatives of labor and management agreed to a government-sponsored "declaration of intent" to keep increases in wages and other money incomes in line with productivity gains, to keep prices stable, and to increase industrial efficiency. However, wage settlements in the last two months have generally exceeded the expected guideline of 3 to 3-1/2 per cent per annum; the most important of these has been the settlement with the 3 million workers in engineering industries which provides for a 4 per cent per annum increase in wages over the next three years. This was the lowest such settlement since the war but

is still likely to raise costs; however, the agreement does provide for the first time the possibility of reducing restrictive labor practices in these industries.

Economic indicators released during the past month confirm the earlier picture of an economy operating at high levels of resource utilization with upward pressures on prices accompanied by severe balance of payments difficulties. In October, the index of industrial production (preliminary) moved up 2 percentage points after showing no change for ten months. In November, the unemployment rate remained at 1.5 per cent; imports and the trade deficit continued at record rates; and prices increased further to levels around 4 per cent higher than a year earlier. The balance of payments deficit in the third quarter on current and long-term capital transactions totaled nearly \$800 million bringing the deficit for the first nine-months to \$1.7 billion.

Selected developments elsewhere. The German economic situation continues to be characterized by gradually increasing production, heavy pressures on resources and prices, and a declining trade surplus. Industrial production in September-October was up 2 per cent from the second quarter and up 6 per cent from a year earlier. In the same two months, new industrial orders remained on the average at the same high level as in the previous six months. Despite the easing of order backlog, heavy pressures on productive facilities persist: in November, job vacancies fell less than seasonally and were still 4.5 times the number of unemployed; producer prices of industrial products rose a further 0.3 per cent and were 2.4 per cent above a year earlier. The

seasonally adjusted trade surplus disappeared in November as imports rose further whereas exports were no higher than last spring; compared with a year earlier, imports were up by 25 per cent while exports were up by only 5 per cent.

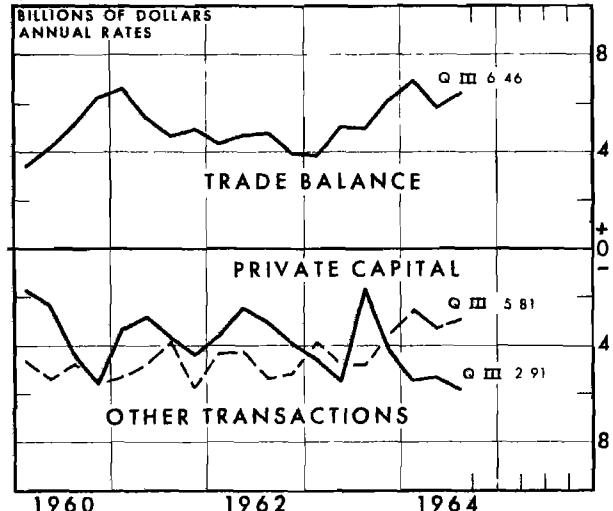
French industrial production in October was again unchanged from the levels attained in the spring. Among the elements in the leveling of output has been a decline in automobile production; demand for automobiles has been limited by the consumer credit restrictions adopted in the fall of 1963 and an apparent increase in the saving rate of the consumer sector. Another element in the slackening of activity has been the sluggishness of exports: in September-October, exports were no higher than the rate reached very early in the year. The labor market also continued to ease in October, with unemployment rising and job vacancies declining.

In Canada, seasonally adjusted indicators of employment, construction activity, and retail sales point to a continued rise in economic activity in October and November. Employment in mid-October slightly exceeded the previous peak reached in April and was 2 per cent above year-earlier levels while unemployment declined in November to 4.3 per cent of the labor force, the lowest rate since mid-1957. Residential construction starts in October were 40 per cent above March-April levels and the number of dwellings under construction was up 9 per cent. Retail sales in September, spurred by heavy demands for automobiles, reached a new record and were 6 per cent higher than a year earlier.

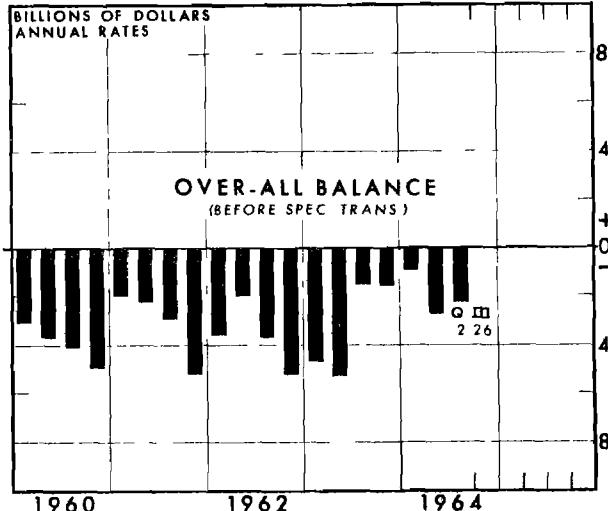
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED

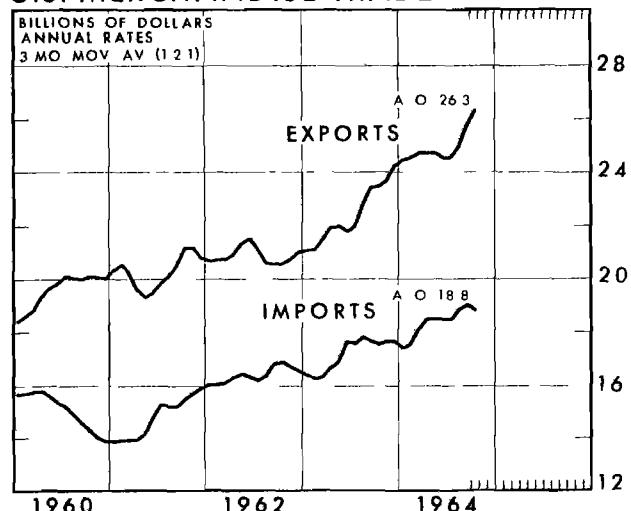
U.S. BALANCE OF PAYMENTS



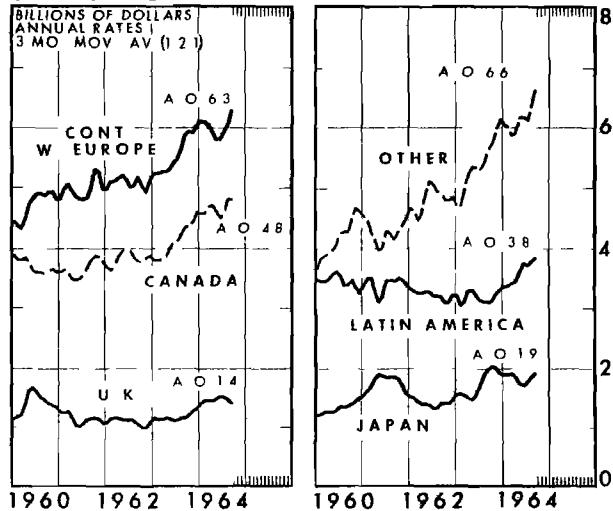
U.S. BALANCE OF PAYMENTS-CONT.



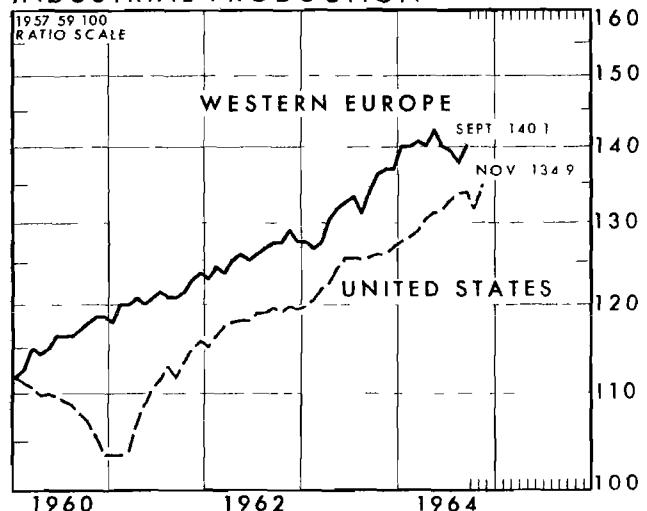
U.S. MERCHANDISE TRADE



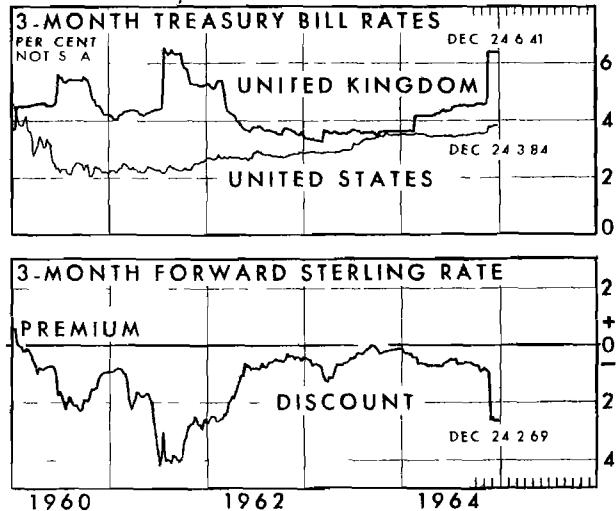
U.S. EXPORTS BY AREA



INDUSTRIAL PRODUCTION



BILL YIELDS, FORWARD STERLING



APPENDIX A: REVISION IN NONFARM PAYROLL DATA*

The Bureau of Labor Statistics has revised its nonfarm payroll estimates for employment, hours, earnings, and labor turnover. The revision reflects: (1) the adjustment to March 1963 employment benchmarks provided by employer reports to the State Unemployment Compensation Insurance programs, supplemented by data for small firms and nonprofit organizations from the Old Age and Survivors Insurance program; and (2) the adjustment to the October 1962 Census of Governments for State and local government employment; and (3) revision of seasonal factors.

The new benchmark lowered the estimated level of nonfarm employment by 530,000 (Table 1), or 1 per cent, for March 1963. The major change was in State and local government where the 1962 benchmark data were the first available since 1957. The level of employment in this sector was decreased by nearly 5 per cent. A reduction of 1-1/2 per cent occurred in construction. In manufacturing the revision was negligible--less than 0.1 per cent. For all industries, except for State and local government, revisions were carried back to 1962. Figures for State and local government and, therefore, for total nonfarm employment were revised back to 1957. In the new series the gain in nonfarm employment between 1957 and 1963 was reduced to 3.7 million from the earlier published 4.3 million, or to an annual rise of about 600,000 rather than 700,000.

Nonfarm employment in October 1964 in the new series was 59.2 million (unadjusted) or 630,000 lower than in the old series (Table 1). Manufacturing and construction accounted for 150,000 of the reduction, trade and service for 140,000 and State and local government for 360,000. The benchmark revisions had very little effect on the level of average weekly hours, average hourly and weekly earnings.

The revision of the seasonal factors had relatively little effect on monthly changes in total nonfarm employment, as may be seen in the chart.^{1/} The new seasonal factors mainly affected the pattern of increase in manufacturing employment. In the new series, manufacturing employment increased only 1.2 per cent from January to July 1964 compared with a 1.7 per cent rise reported in the old series.

*--Prepared by Jane Moore, Economist in National Income, Labor and Trade Section.

^{1/} The revisions for the seasonally adjusted employment series have been carried back to 1953. Revised back data will appear in the December Employment and Earnings publication of the Bureau of Labor Statistics. The November 1964 data released in December were on the revised basis.

In contrast a larger increase occurred between July 1963 and January 1964 in the new series, reflecting a revision in the seasonal factors for this period (Table 2). As a result the revised series shows a somewhat stronger upward trend in the last half of 1963 than previously, and not quite as sharp a rise earlier in the year.

Table 1

REVISION IN NONFARM EMPLOYMENT
 (In thousands of persons)

| | March 1963 | | October 1964 | |
|--------------------------------|------------------|-----------------------------|---------------|---------------|
| | New benchmark | Change from old estimate | New | Old |
| Total | <u>55,184</u> | <u>-530</u> | <u>59,154</u> | <u>59,783</u> |
| Manufacturing | 16,731 | -25 | 17,421 | 17,515 |
| Construction | 2,518 | -38 | 3,372 | 3,429 |
| Other industrial ^{1/} | 4,461 | -2 | 4,671 | 4,669 |
| Trade | 11,434 | -63 | 12,340 | 12,399 |
| Finance | 2,832 | 7 | 2,962 | 2,954 |
| Service | 8,014 | -62 | 8,678 | 8,757 |
| Government | | | | |
| Federal | 2,334 | 0 | 2,329 | 2,320 |
| State and local | 6,860 | -347 | 7,381 | 7,740 |

Table 2

CHANGES IN SEASONALLY ADJUSTED NONFARM EMPLOYMENT
 (In thousands of persons)

| | Jan. 1963- July 1963 | | July 1963- Jan. 1964 | | Jan. 1964- July 1964 | |
|--------------------------------|-------------------------|-------|-------------------------|-----|-------------------------|-------|
| | New | Old | New | Old | New | Old |
| Total | 863 | 1,007 | 571 | 510 | 922 | 1,062 |
| Manufacturing | 160 | 232 | 73 | 16 | 213 | 290 |
| Construction | 92 | 102 | -65 | 52 | 166 | 170 |
| Other industrial ^{1/} | 129 | 124 | -5 | -30 | 54 | 82 |
| Trade and services | 387 | 474 | 379 | 347 | 399 | 449 |
| Government | | | | | | |
| Federal | -4 | -2 | 0 | -2 | -20 | -17 |
| State and local | 99 | 77 | 189 | 231 | 110 | 88 |

1/ Mining, transportation and public utilities.

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EMPLOYMENT IN NONFARM ESTABLISHMENTS

