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CONFIDENTIAL (FR)

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

October 1, 1969

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SUMMARY AND OUTLOOK

Outlook for Economic Activity

While expansion of GNP in the third quarter is apparently somewhat greater than in the preceding quarter, there have been continued signs of easing in indicators of economic activity and growth is expected to moderate in the fourth quarter. Industrial production dipped in August and is expected to show little or no improvement in September. New and unfilled orders for machinery and equipment have declined. Housing starts have already fallen substantially this year, and are expected to drop further in coming months. Retail sales have continued sluggish despite higher auto sales in September.

The large gain in current dollar GNP now estimated for the third quarter reflects a greater increase in inventory accumulation than had earlier been anticipated and also the sizable Federal pay raise. Despite the relatively large rise in disposable income in the third quarter, growth in consumer expenditures moderated and the saving rate rose substantially. The slowing in consumer spending would seem to be in line with the recent Michigan survey, which indicated a sharp decline in its index of consumer sentiment.

The major sectors accounting for the relative strength in GNP growth last quarter seem likely to provide less stimulation to the economy in the current and the next few quarters. Federal government purchases are expected to decline as defense expenditures resume their downward

trend. While inventory investment will probably continue large this quarter because of involuntary stock building, the rate of accumulation is not expected to be any greater than last quarter. Declines in new orders for machinery and equipment and likely declines in profits suggest that gains in business fixed investment are not expected to continue at their recent pace in coming quarters and may fall short of the increases forecast by the latest private surveys. Finally, reduced availability of funds for mortgage lending should act to curtail new housing starts further.

If final sales slow as much as we anticipate, some downward adjustment in the rate of inventory accumulation should be under way by the turn of the year. With final demands sluggish and an inventory adjustment under way, no further growth in real GNP is expected in the first half of 1970. This outlook assumes that the surcharge will be retained at 5 per cent and that the investment tax credit will be repealed.

Outlook for resource use and prices

The rate of capacity utilization in manufacturing is estimated to have declined in the third quarter. With production projected to increase only a little further in the current quarter and to decline somewhat in the first half of next year, it appears likely that the capacity utilization rate will fall appreciably further by mid-1970.

Demand for labor is showing some signs of abating. Growth in nonfarm employment has slowed in recent months, and the manufacturing workweek has come down a little. With expansion in real GNP projected to

slow in the current quarter and to halt in the first half of next year, we are expecting little, if any, further increase in employment after year-end. The unemployment rate is likely to edge up in the fourth quarter, and to rise further in the first half of next year.

The heavy calendar of contract negotiations scheduled for the first half of 1970--in contrast to the light schedule this year--will be a factor exerting upward pressure on wage rates. Nevertheless, we anticipate some slowing in the upward pace of average hourly earnings, as weakening demand for labor leads to some reduction in the average work-week and in overtime pay.

Average prices of industrial commodities have continued to increase fairly rapidly, with rising labor and materials costs putting pressure on prices of finished goods. But with demands weakening and resources in more ample supply, prices of industrial commodities over the next three quarters are unlikely to continue to rise as rapidly as over the past year.

Some easing of the rapid advance in consumer prices is also in prospect. Sluggish demands are likely to exert a slowing influence on prices of nonfood commodities. With respect to food, the extraordinarily sharp rise in meat prices from August 1968 to August 1969 is most unlikely to be approached. Prices of services will generally continue to rise rapidly, but any leveling off of the rise in mortgage interest rates would contribute to a slower increase in the overall index.

Prospective supplies of funds

Recent increases in interest rates have developed in large measure because lendable funds available from banks and other types of financial intermediaries have become severely limited by the cumulative effects of monetary restraint. Given no change in prevailing tight money market conditions or existing regulatory rate ceilings at depositary institutions, there appears to be little relief in sight with respect to these supply constraints. Depositary-type institutions can be expected to experience continued heavy pressures on their savings flows during the fourth quarter. Funds available from life insurance companies should continue to be restricted by policy loan increases and the slowing of repayment flows. And even pension funds, where flows are more assured, may continue to show considerable caution in committing funds to long-term markets until they see clearer evidence of slower economic activity and a peaking in interest rates.

Nonbank thrift institutions are expected to experience sizable net losses of savings during the current October reinvestment period. Thereafter, industry spokesmen anticipate little if any net resumption of seasonal inflows over the remaining weeks of the quarter. And they fear that net savings attrition in January will again become heavy, following year-end interest crediting. In short, thrift institutions are likely to have to continue cutting into their reduced liquidity, to step-up borrowing at Federal Home Loan and commercial banks, and to

cut back still further on their new mortgage loan commitments. This outlook for the savings industry and, in consequence, the mortgage market is buttressed by results of the recent Federal Reserve and Federal Home Loan Banks survey of selected mortgage lenders.

At commercial banks, also, net attrition in time and savings accounts is expected to continue during the fourth quarter. Some moderation in the volume of CD attrition may develop as the level of outstandings approaches hard core levels. Also, a few major banks have recently shown a willingness to bid for foreign official CD's at rates not far below those available on Euro-dollars. But attrition in consumer-type time and savings deposits will be resumed in October--following quarterly interest crediting--and weakness in these accounts is likely to persist over the rest of the year.

Banks have reduced their reliance on nondeposit sources of funds recently. Their future attitudes toward such funds will undoubtedly be considerably influenced by the strength of fall loan demands.

Demands for funds

With no relief in sight for institutional lenders, pressures on mortgage markets are likely to continue in the months ahead and lead to further general advances in mortgage interest rates. Although there has been some evidence that rising interest rates and building costs have begun to limit current demands for housing, effective demands for

mortgage funds reportedly still greatly exceed supplies. In these circumstances FNMA and FHLBB can be expected to continue their efforts to support the mortgage market. Taken together their combined demands for net new money may total as much as $2.5 billion during the fourth quarter.

Business takings of external funds in the fourth quarter would seem more likely to expand than to contract from recent levels. In the third quarter reduced bank credit availability and high corporate bond yields apparently led business corporations to meet a sizable share of their needs for funds through liquidation of assets. While some further draw down of liquid assets can probably also be expected into the fall, the large prospective gap between corporate uses and internal sources suggests that businesses may attempt to make more active use of credit lines at banks in addition to maintaining a relatively heavy volume of borrowing in capital markets.

Limitations imposed by inflexible rate ceilings have sharply reduced the effective demands of State and local governments on capital markets over the past two months. In fact, the extremely small calendar of offerings in September caused municipal yields to recede from their earlier highs. Yields are not expected to decline sufficiently further, however, to permit any large increase in municipal bond volume, since any tendency to step-up demand would quickly reassert upward pressures on yields. A firm Congressional assurance that the tax exempt status of municipal bonds would remain unchanged would, of course, help to moderate these pressures.

If recent tendencies evident in Federal receipts and outlays should persist, Treasury cash needs over the fall months might be as much as $1 billion larger than the $5 billion previously indicated by Treasury spokesmen. This need would most likely be met in the bill area, and there would be no further refinancing requirements.

Given the prospective continuing constraints on the supply of lendable funds from financial intermediaries, prospective demands for funds suggest that intermediate- and long-term interest rates may remain under upward pressure in the period immediately ahead. However, some part of prospective supply-demand developments has undoubtedly already been discounted by recent rate advances, and longer-term interest rates may peak out as the fourth quarter progresses, assuming enough substantiating evidence of an economic slowdown.

Balance of payments outlook

If an upward revaluation of the German mark emerges from the present situation, it may prove more significant in paving the way psychologically and politically for later actions by Germany and other surplus countries to adjust their payments positions than for any early effects--apart from checking or reversing the recent speculative flows of funds. In the short run the degree of stimulus a mark revaluation will give German imports, and its damping effect on German exports, will depend not only on the magnitude of the rate change, which may be small, but also on whether offsetting border tax changes are made, on

whether German monetary policy is then tightened a few more notches to help bring Germany's domestic boom under better control, and on whether German producers adjust their DM prices and accept a shrinkage of present wide profit margins. Moreover, any reduction in the German trade surplus will benefit primarily the trade balances of other countries within continental Europe, Germany's major trade partners.

With or without a mark revaluation in the near future, a moderate trend of improvement in the U.S. trade balance is probably beginning to emerge. Both exports and imports in August were above expected levels. Imports, however, may ease off in the course of the next six months if present projections of U.S. demand for materials and for inventories in general prove valid. Exports, on the other hand, will be sustained--and may advance appreciably from 1969 to 1970, even though less rapidly than over the past two years--if demand in continental Europe, in Japan, and in many of the less industrialized countries holds up as we expect it will. In Germany the margin of labor force expansibility--mainly with foreign labor--has already become narrower than in the previous peak year 1965, and the pressures of rising disposable income are beginning to push the German price level up perceptibly. A mark revaluation would help relieve the inflationary pressures within the country--which, of course, is its main virtue in German domestic political thinking--but even with that help

the end of the present boom in Germany will still be many months away, at the least.

Despite the expected improvement in the U.S. export surplus, it is highly probable that the overall balance of payments, exclusive of flows to and from the Euro-dollar market and speculative flows to or from other currencies, will still be severely in deficit in the next several quarters. Though the July-August statistics support a belief that some inflows of foreign capital to the U.S. stock market may still be obtained, and though a pick-up in European flotations of securities by U.S. corporations may be in the offing, an offsetting tendency for U.S. direct investment outflows to grow is indicated both by companies' plans for plant and equipment expenditures abroad and by the way the Administration seems to be leaning toward easing the OFDI controls.

Little net change has occurred since July in the outstanding liabilities of U.S. banks to their foreign branches. The official settlements balance is therefore tending to come into line with the liquidity balance. The deficit in August and September was large on either basis, apparently averaging more than half a billion dollars a month. In coming quarters the liquidity balance may show some improvement. Because some net repayment of Euro-dollar borrowings by U.S. banks may occur, continuation of very large deficits on the official settlements basis is not unlikely.

SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally adjusted)

	Latest Period	Amount			Per Cent Change	
		Latest Period	Preced'g Period	Year Ago	Year Ago*	2 Yrs. Ago*
Civilian labor force (mil.)	Aug'69	81.1	80.8	78.7	2.9	4.4
Unemployment (mil.)	"	2.9	2.9	2.8	3.3	-2.8
Unemployment (per cent)	"	3.5	3.6	3.5	--	--
Nonfarm employment, payroll (mil.)	"	70.4	70.3	68.1	3.4	6.7
Manufacturing	"	20.3	20.2	19.8	2.6	4.5
Other industrial	"	8.5	8.5	8.2	3.2	5.0
Nonindustrial	"	41.6	41.6	40.1	3.9	8.2
Industrial production (57-59=100)	"	174.3	174.6	164.6	5.9	10.1
Final products	"	172.8	172.5	164.8	4.9	9.0
Materials	"	175.8	176.4	164.2	7.1	11.2
Wholesale prices (57-59=100)1/	"	113.4	113.3	108.7	4.3	6.9
Industrial commodities (FR)	"	111.8	111.4	108.1	3.4	6.1
Sensitive materials (FR)	"	112.5	111.6	106.6	5.5	12.3
Farm products, foods & feeds	"	114.6	115.5	107.7	6.4	8.9
Consumer prices (57-59=100)1/	"	128.7	128.2	121.9	5.6	10.1
Commodities except food	"	118.2	118.1	113.5	4.1	8.0
Food	"	127.4	126.7	120.5	5.7	9.3
Services	"	145.0	144.0	135.5	7.0	13.1
Hourly earnings, mfg. ($)	"	3.24	3.20	3.03	6.9	13.3
Weekly earnings, mfg. ($)	"	131.63	130.37	123.28	6.8	13.2
Personal income ($ bil.)2/	"	756.6	751.4	696.1	8.7	19.1
Corporate profits before tax ($ bil.)2/	QII'69	95.4	95.5	90.7	5.2	20.6
Retail sales, total ($ bil.)	Aug'69	29.3	29.2	28.8	2.0	11.5
Autos (million units)2/	"	8.1	8.1	8.9	-9.2	15.3
GAF ($ bil.)	"	8.0	8.1	7.7	3.7	14.6
Selected leading indicators:						
Housing starts, pvt. (thous.)2/	"	1,336	1,358	1,518	-12.0	-5.0
Factory workweek (hours)	"	40.6	40.7	40.7	-0.2	-0.2
New orders, dur. goods ($ bil.)	"	29.9	30.6	27.3	9.4	15.6
New orders, nonel. mach. ($ bil.)	"	5.4	5.4	4.8	14.1	22.1
Common stock prices (1941-43=10)	"	94.18	94.81	98.11	-4.0	-0.3
Manufacturers' inventories, book val. ($ bil.)	"	93.6	93.2	86.7	8.0	14.4
Gross national product ($ bil.)2/	QII'69	924.8	908.7	858.7	7.7	18.0
Real GNP ($ bil., 1958 prices)2/	"	726.7	723.1	705.8	3.0	8.4

* Based on unrounded data. 1/ Not seasonally adjusted. 2/ Annual rates.

SELECTED DOMESTIC FINANCIAL DATA

	Week ended September 27, 1969	4-week average	Last 6 months High	Last 6 months Low
Money Market 1/ (N.S.A.)				
Federal funds rate (per cent) 9/	9.46	9.17	10.18	6.80
U.S. Treas. bills, 3-mo., yield (per cent)	7.10	7.09	7.12	5.93
U.S. Treas. bills, 1-yr., yield (per cent)	7.37	7.35	7.37	5.96
Net free reserves 2/ ($ millions)	-960	-781	-405	-1,242
Member bank borrowings 2/ ($ millions)	1,106	1,026	1,634	740
Capital Market (N.S.A.)				
Market yields (per cent)				
5-year U.S. Treas. bonds 1/	7.77	7.52	7.77	6.25
20-year U.S. Treas. bonds 1/	6.64	6.52	6.64	5.93
Corporate new bond issues, Aaa adj. 8/	8.13	8.02	8.13	7.02
Corporate seasoned bonds, Aaa 1/	7.19	7.13	7.19	6.75
Municipal seasoned bonds, Aaa 1/	5.82	5.83	5.85	4.95
FHA home mortgages, 30-year 3/	--	8.36	8.36	8.05
Common stocks, S&P composite series 4/				
Prices, closing (1941-43=10)	94.16	94.34	105.94	91.96
Dividend yield (per cent)	3.38	3.36	3.39	2.99

	Latest month	Amount	3-month average	Change from year earlier: Latest month	Change from year earlier: 3-month average
New Security Issues (N.S.A., $ millions)					
Corporate public offerings 5/	Oct. '69e	1,800	1,610	266	380
State & local govt. public offerings	"	600	638	-1,630	-1,153
Comm. & fin. co. paper (net change in outstandings) 6/	Aug. '69	+1,285	+1,390	+297	+618

	Latest month	Outstandings Latest month	Change: Latest month	Change: 3-month average	Annual rate of change from: Preceding month	3 months ago	12 months ago
Banking (S.A.)		($ billions)			(per cent)		
Total reserves 1/	Aug. '69	27.40	-0.13	-0.28	- 5.8	-11.9	+ 0.7
Credit proxy 1/ 10/	"	285.3	-2.7	-3.3	-11.3	-13.3	- 0.4
Bank credit, total 6/	"	395.4	-0.3	-0.1	- 0.9	- 0.2	+ 5.4
Business loans	"	103.7	+1.1	+0.4	+12.9	+ 4.3	+13.1
Other loans	"	165.5	-0.7	-0.1	- 5.1	- 0.5	+ 7.2
U.S. Govt. sec.	"	56.6	--	+0.2	--	+ 4.3	-11.4
Other securities	"	69.6	-0.7	-0.6	-12.0	- 9.5	+ 6.6
Total liquid assets 1/ 6/ 11/ 12/	"	716.0	-2.0	-1.4	- 3.3	- 2.3	+ 4.3
Demand dep. & currency 1/ 12/	"	199.1	-0.3	+0.3	- 1.8	+ 1.6	+ 4.2
Time & sav. dep., comm. banks 1/ 12/	"	194.5	-3.2	-2.4	-19.4	-14.3	+ 0.4
Savings, other thrift instit. 6/	"	200.5	+1.1	+0.3	+ 6.6	+ 1.6	+ 4.9
Other 6/ 7/ 11/	"	121.9	+0.4	+0.5	+ 4.0	+ 4.6	+10.5

N.S.A. - Not seasonally adjusted. S.A. - Seasonally adjusted. e - Estimated.
1/ Average of daily figures. 2/ Average for statement week ending September 24. 3/ Latest figure is monthly average for August. 4/ End-of-week closing prices; yields are for Friday. 5/ Corporate security offerings include both bonds and stocks. 6/ Month-end data. 7/ U.S. savings bonds and U.S. Government securities maturing within 1 year. 8/ Adjusted to Aaa basis. 9/ Federal funds data are 7-day averages for week ending Sunday: latest figure is for week ending September 28. 10/ Reflects $400 million reduction in member bank deposits resulting from withdrawal of a large country bank from System membership in January 1969. Percentage annual rates are adjusted to eliminate this break in series. 11/ Reflects $1.7 billion increase beginning January 1969 in U.S. Government securities maturing within 1 year to conform to the new Budget concept. Percentage annual rates are adjusted where necessary. 12/ Money supply and time deposits on revised basis.

U S BALANCE OF PAYMENTS
(In millions of dollars)

	1968				1969			
	Year r/	II r/	III r/	IV r/	I	II p/	July p/	August p/
Goods and services, net 1/	2,516	841	909	301	363	283	n.a.	n.a
Trade balance 2/	626	264	313	-75	-103	-7	54	75
Exports 2/	33,598	8,395	8,879	8,383	7,469	9,588	3,100	3,235
Imports 2/	-32,972	-8,131	-8,566	-8,458	-7,572	-9,595	-3,046	-3,160
Service balance	1,890	577	596	376	466	290		
Remittances and pensions	-1,159	-274	-325	-285	-271	-286		
Govt. grants & capital, net	-3,955	-1,055	-968	-835	-793	-1,103		
U.S. private capital	-5,157	-1,537	-1,868	-947	-1,345	-1,971		
Direct investment	-3,025	-1,009	-1,262	-283	-928	-1,101		
Foreign securities	-1,266	-164	-337	-455	-323	-426		
Banking claims	269	243	-90	-120	78	-482	*345	*30
Other	-1,134	-607	-179	-89	-172	38		
Foreign capital	9,277	2,645	2,515	2,902	3,334	4,213		
Official foreign, nonliquid	2,407	937	433	709	-42	-272		
Official foreign, liquid	-3,099	-2,186	-55	22	-1,132	-578		
Int'l and reg., liq. & nonliq. 3/	235	-97	78	273	96	28		
Foreign private non-bank, liq.	374	103	44	223	-23	-147		
Foreign commercial banks, liq.	3,382	2,297	702	-74	2,944	4,653		
New direct invest. issues 4/	2,129	585	586	378	401	145		
Other	3,849	1,006	727	1,371	1,090	384		
Errors and omissions	-642	-480	309	-60	-1,239	-838		
	Balances, with and without seasonal adjustment (deficit -)							
Official settlements balance, S.A.		1,553	97	367	1,143	1,243		
Seasonal component		-3	-25	-442	567	-29		
Balance, N.S.A. 5/	1,638	1,550	72	-75	1,710	1,214	278	-657
Liquidity balance, S.A.		9	-139	862	-1,653	-3,711		
Seasonal component		96	-269	-124	395	64		
Balance, N.S.A.	168	105	-408	738	-1,258	-3,647	-1,178	-1,126
Adjusted over-all balance, S.A. 6/		-751	-613	464	-1,809	-3,417		
Seasonal component		96	-269	-124	395	64		
Balance, N.S.A.	-1,744	-655	-882	340	-1,414	-3,353	-1,153	e/ -973
Financed by: Liab. to comm. banks abroad, N.S.A. (decrease -)	3,382	2,205	954	-415	3,124	4,567	1,431	e/ 316
Official settlements, N.S.A. 7/	-1,638	-1,550	-72	75	-1,710	-1,214	-278	657
	Reserve changes, N.S.A. (decrease -)							
Total monetary reserves	880	137	571	1,076	48	299	-121	259
Gold stock	-1,173	-22	74	137	-56	317	-9	10
Covertible currencies	1,183	-267	474	575	73	-246	-189	233
IMF gold tranche	870	426	23	364	31	228	77	16

1/ Equals "net exports" in the GNP, except for latest revisions.
2/ Balance of payments basis which differs a little from Census basis
3/ Long-term deposits and Agency securities
4/ New issues sold abroad by U S direct investors
5/ Differs from liquidity balance by counting as receipts (+) increase in liquid liabilities to commercial banks, private nonbanks, and international institutions (except IMF) and by not counting as receipts (+) increases in certain nonliquid liabilities to foreign official institutions.
6/ Represents the net result of all international transactions of the U S other than changes in reserve assets, in all liabilities to foreign monetary authorities and in liabilities to commercial banks abroad (including U S bank branches) reported by banks in the U.S
7/ Minus sign indicates decrease in net liabilities.

* Not seasonally adjusted

THE ECONOMIC PICTURE IN DETAIL

Domestic Nonfinancial Scene

Gross national product. Recent developments lend support to our projections of a further easing of final demands and GNP growth in the next several quarters. The sharp decline in construction activity since last spring has begun to affect supplier industries, as well as to reduce demands for appliances and furniture. Consumer demand for goods in general has shown little or no growth in recent months. In addition, Federal purchases of defense goods are being cut further and new orders for machinery and equipment have turned down. Growth of industrial production has leveled off, but there are signs, nevertheless, of growing imbalances between output and consumption with an associated increase in inventory accumulation. However, there are also indications of some further rise in business fixed investment in the next few quarters, and although employment growth has slowed, income flows are still large and inflationary pressures continue strong.

Gross national product in the third quarter is expected to increase by $17 billion, $1 billion more than in the second quarter, and slightly more than we had anticipated last month. However, final demands appear to be weaker than we had earlier thought. Growth in private final sales is expected to be $5 billion less than in the second quarter, although there was some offset from a rise in Government purchases as a result of the Federal pay raise in July. However, a larger rise in inventory accumulation is estimated to have added about $3 billion to GNP growth.

Some of this additional inventory accumulation appears to have been involuntary. Consumer demand has been perceptibly weaker in the past few months, despite an exceptionally large increase in disposable income, reflecting the Federal pay raise and the completion of payments in the second quarter on 1968 income tax liabilities. This suggests an increase in the saving rate to about 6.7 per cent from 5.3 per cent in the second quarter--an unusually sharp change. Retail sales have shown little or no increase recently and in real terms were below the year ago level for the quarter as a whole. Nondurable goods sales have continued sluggish and durable goods sales have declined. Unit sales of new domestic autos apparently declined somewhat from the 8.5 million rate of the second quarter, and appliance sales also turned down. Only service expenditures maintained their upward momentum.

In addition to the weaker consumption picture, residential construction activity dipped further in the increasingly taut monetary atmosphere, and business fixed investment expenditures were estimated to have grown at a somewhat slower pace in the third quarter.

These developments suggest that a substantially smaller rise in GNP--about $12 billion--should be evident in the fourth quarter as Federal spending resumes its downward course, residential construction activity weakens further, and growth of business investment spending continues to taper off.

Housing activity may have fallen slightly less in the third quarter than we had earlier anticipated, starts dropping to an annual rate of 1.34 million. However, with availability of funds very tight

and some buyer resistance to higher interest rates apparently developing, a further reduction in starts to a 1.2 million rate is anticipated in the fourth quarter, with expenditures expected to drop by an additional $1.4 billion. Barring a significant shift in monetary policy toward ease in the near future, we expect starts to fall further in early 1970, dropping to about a 1.1 million rate in the second quarter.

Growth of business fixed investment spending is still expected to slow during the next several quarters, but not quite as rapidly as we had thought earlier. We had adjusted up our projections slightly last month to reflect newly available information, including the results of the NICB appropriations survey which suggested that capital spending by manufacturers would continue to rise into early 1970. We have made another slight upward adjustment this month in the expected pattern of capital spending, in response to the investment plans for 1970 reported in recent private surveys. But our projections still call for a distinct tapering off of growth. Continued tight credit conditions with high interest rates are likely to exert a retarding influence. The expected further slowing of GNP growth is likely to reduce profits further and, along with a reduced rate of manufacturing capacity utilization, result in substantial downward adjustment of investment plans. The significant reduction in new orders for machinery and equipment in the past few months suggests that this process may have already begun.

Despite larger than expected Federal outlays in the third quarter, recent official announcements of substantial cuts in defense spending and the planned curtailment of Federal construction activities

appear to assure a decline in Federal purchases in the next several quarters. At the State and local level, some increases in Federal grants-in-aid are probable and this should support growth in expenditures for some programs, but serious financing difficulties in capital markets appear likely to curb State and local capital spending and more than offset increases in the Federally aided programs. As a result, growth in spending at these levels of government is likely to be smaller than earlier this year.

With income having substantially outrun consumption in recent months, and a sharp rise in the saving rate probable in the quarter just completed, some recovery in the growth of consumption expenditures--particularly for nondurables--would seem likely in the fourth quarter with an accompanying decline in the saving rate. But with every other major sector of demand apparently either declining or showing distinctly less ebullience, growth of total final demands is expected to ease somewhat further. We have projected inventory accumulation in the fourth quarter to continue at about the relatively high third quarter rate, but a larger portion is likely to be unintended.

But inventory accumulation is unlikely to continue strong in the face of a further weakening of growth of final demands, and downward adjustments in production should accompany a reduced rate of inventory accumulation in the first half of next year. Under these conditions, GNP increases would be significantly smaller, with virtually no growth in real GNP, or possibly some decline, in the first half of next year. We still expect that a moderation of price increases would accompany

such reduced pressure on resources, with the GNP deflator dropping to under a 3-1/2 per cent rate of increase in the second quarter of next year.

These projections assume that the tax surcharge will be extended at a 5 per cent rate for the first half of 1970, that the investment tax credit will be dropped, and that a 10 per cent increase in Social Security benefits will take effect on April 1. Elimination of the tax surcharge entirely on January 1 would raise disposable income, consumption and corporate profits significantly.

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income figures are billions of dollars, with quarterly figures at annual rates.)

	1967	1968	1969 Proj.	1969 I	1969 II	1969 III	1969 IV	1970 I	1970 II
						Projected			
Gross National Product	793.5	865.7	932.3	908.7	924.8	941.8	953.8	961.8	968.8
Final sales	786.2	858.4	923.7	902.1	917.9	931.3	943.4	954.4	964.4
Private	606.1	658.1	708.1	692.1	705.0	712.6	722.8	732.3	740.6
Excluding net exports	600.9	655.6	706.2	690.6	703.4	710.4	720.5	729.0	737.5
Personal consumption expenditures	492.3	536.6	575.9	562.0	572.8	579.4	589.4	598.9	607.8
Durable goods	73.0	83.3	89.4	88.4	90.6	89.3	89.4	88.8	88.0
Nondurable goods	215.1	230.6	243.9	238.6	242.1	245.0	250.0	255.1	259.8
Services	204.2	222.8	242.6	235.0	240.1	245.1	250.0	255.0	260.0
Gross private domestic investment	116.0	126.3	138.9	135.2	137.4	141.5	141.5	137.5	134.1
Residential construction	25.0	30.2	31.8	33.3	32.7	31.2	29.8	27.8	26.9
Business fixed investment	83.7	88.8	98.6	95.3	97.8	99.8	101.3	102.3	102.8
Change in business inventories	7.4	7.3	8.6	6.6	6.9	10.5	10.4	7.4	4.4
Nonfarm	6.8	7.4	8.4	6.6	6.7	10.2	10.2	7.2	4.2
Net exports of goods and services	5.2	2.5	1.9	1.5	1.6	2.2	2.3	3.3	3.1
Gov't. purchases of goods & services	180.1	200.3	215.6	210.0	212.9	218.7	220.6	222.1	223.8
Federal	90.7	99.5	101.9	101.6	100.6	103.2	102.1	100.6	99.3
Defense	72.4	78.0	79.3	79.0	78.5	80.5	79.0	77.0	75.5
Other	18.4	21.5	22.6	22.6	22.1	22.7	23.1	23.6	23.8
State & local	89.3	100.7	113.7	108.5	112.3	115.5	118.5	121.5	124.5
Gross national product in constant (1958) dollars	674.6	707.6	728.3	723.1	726.7	730.5	732.9	732.6	732.1
GNP implicit deflator (1958=100)	117.6	122.3	128.0	125.7	127.3	128.9	130.1	131.3	132.3
Personal income	629.4	687.9	747.0	724.4	740.5	756.1	767.0	777.0	787.9
Wages and salaries	423.5	465.0	510.0	493.3	504.3	516.7	525.5	533.0	539.2
Disposable income	546.5	590.0	629.3	610.2	622.0	638.2	646.6	659.1	667.6
Personal saving	40.4	38.4	37.3	32.5	33.3	42.7	40.8	43.5	42.8
Saving rate (per cent)	7.4	6.5	5.9	5.3	5.3	6.7	6.3	6.6	6.4
Corporate profits before tax	80.3	91.1	93.1	95.5	95.4	92.0	89.5	84.5	80.0
Federal government receipts and expenditures (N.I.A. basis)									
Receipts	151.1	176.3	200.9	198.1	202.3	200.9	202.4	198.3	198.6
Expenditures	163.8	181.5	191.7	188.5	189.3	193.9	195.0	195.8	198.6
Surplus or deficit (-)	-12.7	-5.2	9.2	9.6	13.0	7.0	7.4	2.5	0.0
Total labor force (millions)	80.8	82.3	84.2	83.7	83.8	84.5	84.7	85.0	85.2
Armed forces "	3.4	3.5	3.5	3.5	3.5	3.5	3.5	3.4	3.3
Civilian labor force "	77.2	78.7	80.7	80.2	80.3	81.0	81.2	81.6	81.9
Unemployment rate (per cent)	3.8	3.6	3.6	3.3	3.5	3.7	3.9	4.2	4.5
Nonfarm payroll employment (millions)	65.9	67.9	70.1	69.5	70.0	70.4	70.7	70.8	70.7
Manufacturing	19.4	19.8	20.1	20.1	20.1	20.2	20.1	20.0	19.8
Industrial production (1957-59=100)	158.1	165.4	173.2	170.2	172.7	174.4	175.5	175.0	174.5
Capacity utilization, manufacturing (per cent)	85.3	84.5	84.2	84.5	84.6	84.2	83.6	82.4	81.2
Housing starts, private (millions A.R.)	1.29	1.51	1.44	1.72	1.51	1.34	1.20	1.18	1.13
Sales new domestic autos (millions, A.R.)	7.57	8.62	8.39	8.37	8.54	8.40	8.25	8.15	8.10

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1967	1968	1969 Proj.	1969 I	1969 II	1969 III	1969 IV	1970 I	1970 II
						Projected			
	In Billions of Dollars								
Gross National Product	43.6	72.2	66.6	16.2	16.1	17.0	12.0	8.0	7.0
Inventory change	-7.4	-0.1	1.3	-3.9	0.3	3.6	-0.1	-3.0	-3.0
Final sales	51.1	72.2	65.3	20.1	15.8	13.4	12.1	11.0	10.0
Private	27.8	52.0	50.0	16.8	12.9	7.6	10.2	9.5	8.3
Excluding net exports	27.9	54.7	50.6	16.5	12.8	7.0	10.1	8.5	8.5
Net exports	-0.1	-2.7	-0.6	0.3	0.1	0.6	0.1	1.0	-0.2
Government	23.3	20.2	15.3	3.3	2.9	5.8	1.9	1.5	1.7
GNP in constant (1958) dollars	16.5	33.0	20.7	4.6	3.6	3.8	2.4	-0.3	-0.5
Final sales	23.5	33.3	19.9	8.2	3.5	1.1	2.1	1.7	2.4
Private	10.0	24.9	17.9	7.8	3.9	0.5	3.0	1.8	3.1
	In Per Cent Per Year								
Gross National Product	5.8	9.1	7.7	7.3	7.1	7.4	5.1	3.4	2.9
Final sales	7.0	9.2	7.6	9.1	7.0	5.8	5.2	4.7	4.2
Private	6.1	8.5	7.6	9.9	7.5	4.3	5.7	5.3	4.5
Personal consumption expenditures	5.6	9.0	7.3	8.2	7.7	4.6	6.9	6.4	5.9
Durable goods	3.1	14.1	7.3	9.7	10.0	-5.7	0.4	-2.7	-3.6
Nondurable goods	4.0	7.2	5.8	7.3	5.9	4.8	8.2	8.2	7.4
Services	8.3	9.1	8.9	8.5	8.7	8.3	8.0	8.0	7.8
Gross private domestic investment	-4.4	8.9	10.0	3.9	6.5	11.9	0.0	-11.3	-9.9
Residential construction	0.0	20.8	5.3	17.6	-7.2	-18.3	-17.9	-26.8	-12.9
Business fixed investment	2.6	6.1	11.0	16.6	10.5	8.2	6.0	3.9	2.0
Gov't. purchases of goods & services	14.9	11.2	7.6	6.4	5.5	10.9	3.5	2.7	3.1
Federal	16.6	9.7	2.4	-1.2	-3.9	10.3	-4.3	-5.9	-5.2
Defense	19.3	7.7	1.7	-1.5	-2.5	10.2	-7.5	-10.1	-7.8
Other	7.6	16.8	5.1	1.8	-8.9	10.9	7.0	8.7	3.4
State & local	13.0	12.8	12.9	14.1	14.0	11.4	10.4	10.1	9.9
GNP in constant (1958) dollars	2.5	4.9	2.9	2.5	2.0	2.1	1.3	-0.1	-0.3
Final sales	3.6	5.0	2.8	4.6	2.0	0.6	1.2	0.9	1.3
Private	1.9	4.7	3.2	5.6	2.8	0.4	2.1	1.3	2.2
GNP implicit deflator	3.2	4.0	4.7	4.7	5.1	5.2*	3.8	3.5	3.2
Personal income	7.2	9.3	8.6	7.4	8.9	8.4	5.8	5.2	5.6
Wages and salaries	7.4	9.8	9.7	9.3	8.9	9.8	6.8	5.7	4.7
Disposable income	6.8	8.0	6.7	3.9	7.7	10.4	5.3	7.7	5.2
Corporate profits before tax	-4.6	13.4	2.2	4.2	-0.4	-14.3	-10.9	-22.3	-21.3
Federal government receipts and expenditures (N.I.A. basis)									
Receipts	6.0	16.7	14.0	23.1	8.5	-2.8	3.0	-8.1	0.6
Expenditures	14.7	10.8	5.6	2.3	1.7	9.7	2.3	1.6	5.7
Nonfarm payroll employment	3.0	3.0	3.3	4.7	2.9	2.3	1.7	0.6	-0.6
Manufacturing	1.0	2.1	1.6	4.0	0.0	2.0	-2.0	-2.0	-4.0
Industrial production	1.2	4.6	4.7	6.7	5.9	3.9	2.5	-1.1	-1.1
Housing starts, private	10.9	16.7	-4.3	28.2	-48.3	-45.0	-41.8	-6.7	-16.9
Sales new domestic autos	-9.7	14.0	-2.7	-20.4	8.4	-6.6	-7.1	-4.8	-2.5

* Excluding Federal pay increase 4.0 per cent.

Industrial production. Industrial production in September is tentatively estimated to have changed little from the July-August level. This estimate is consistent with such physical volume data as are now available. If this expectation is realized, the third quarter average would show an annual rate of growth of about 4.0 per cent from the second quarter, compared to 6.0 per cent from the first to the second quarter, and 6.8 per cent from the fourth to the first quarter.

The revised July and preliminary August figures indicated some decline in output of business equipment and of industrial materials. These two sectors accounted for the rapidity of the growth in industrial production from January to June of 1969, as shown in the table.

INDUSTRIAL PRODUCTION
(Per cent change at annual rates)

	January to June	June to August
Total index	6.6	1.7
Consumer goods	1.8	6.6
Auto products	3.4	8.2
Home goods and apparel	0.0	-.6
Consumer staples	2.4	3.4
Business equipment	7.0	-2.0
Industrial equipment	16.0	-12.6
Commercial equipment	12.5	- 1.2
Materials	6.8	-.9
Durable materials	9.1	0.0
Nondurable materials	9.4	-1.9

The rise in consumer goods from June to August reflected high levels of auto production that are usually associated with the model

changeover period, and are more or less independent of the sales rate in order to build up dealers' inventories of new models. In September, auto assemblies were maintained at the July-August annual rate of 9.0 million units. Production schedules for the fourth quarter are presently set at about an 8.5 million rate, 7 per cent below a year earlier.

Output of home goods and apparel has changed little since the beginning of the year and the July-August figures showed some declines. Considering the weakness in retail sales and the high level of inventories, production of such goods probably eased off further in September.

Overall production of business equipment in September was probably maintained at about the August level. The sharp decline in output of industrial equipment from June to August is not likely to be repeated in the near future. Output of defense equipment has changed little since March, and in August was about 6 per cent below the July-August 1968 peak.

Among materials, output of raw steel leveled off in September at the reduced August rate. It is unlikely that production of other industrial materials turned up in September in view of the lack of growth in output of final products, the sustained decline in new housing starts, and the high cost of further increasing current record inventories of these materials.

Retail sales. Figures for three weeks ending September 20 suggest that retail sales for the month may show little change from the August level. As a result, this may be the fourth consecutive month in which real retail sales have been below year-earlier levels.

Sales of the automotive group, however, were very strong--particularly in the last week available--and if it were not for this, total retail sales for the month might be down by at least 1 per cent. As noted below, however, the earlier introduction date for the 1970 autos makes it difficult to determine seasonal factors at this time. The continued decline in housing starts is apparently affecting furniture and appliance sales, as well as those of the lumber, building material and hardware group, and sales of these two durable goods categories are tentatively estimated to have declined for the third consecutive month. Sales of all the major types of nondurable goods stores also apparently declined in September, with the largest drops at apparel and department stores.

Introduction of 1970 model autos in mid-September by General Motors and Ford resulted in a surge in sales in the September 10-20 period. On a daily average basis, sales were about one-half larger than a year earlier when new models had not yet been introduced. A rough allowance for the seasonal influence suggests the possibility of a seasonally adjusted annual rate of 9 or more million units in this 10-day interval. Prior to the latest figure, sales had been running at an annual rate of about 8 million units. A more reliable specification of the seasonal factors in the intervals containing and surrounding the model introduction dates cannot be made for some time. So far as gauging the strength of consumer demand for autos is concerned, the situation is further complicated by the fact that fleet purchases are normally made in large volume early in the new model period. Stocks of new cars remained at an advanced level, 12 per cent above a year earlier.

Consumer credit. Growth of consumer instalment credit apparently slackened further in August. Incomplete reports suggest that the seasonally adjusted increase in outstandings will total approximately $7.3 billion at an annual rate, the smallest monthly advance since January 1968. Instalment credit expanded by $7.5 billion in July and $9 billion in the first half of 1969.

Extensions of auto credit contracted sharply during July and August, reflecting mainly the decline in new car sales. The decline was tempered somewhat by continued strong sales of used cars and higher average notes on used car contracts. With repayments well maintained, auto credit outstanding increased at only a $1.3 billion annual rate in July-August, less than one-half the rate in the first half of this year.

The seasonally adjusted proportion of new cars sold on credit has changed little; in July 67.3 per cent of the new cars sold were financed, about one percentage point less than both the first half average and the July 1968 figure. Used car financing eased to 76 per cent of the units sold by franchised dealers in July, from 79 per cent in the first half of the year and 81 per cent last July.

Extensions and repayments for "other consumer goods" eased slightly this summer but the increase in outstandings exceeded the first-half average, and also the average for the full year 1968. This strong performance may be due to the surge in mobile home sales (and the large instalment contracts for these units) which more than offset the summer softness in furniture and appliance sales that was probably associated with the sustained decline in conventional housing starts.

NET CHANGE IN CONSUMER INSTALMENT CREDIT OUTSTANDING
(Billions of dollars, seasonally adjusted annual rates)

	Total	Automobile	Other consumer goods	Personal loans	Home repair and modernization
1968 - QI	$ 7.0	$2.8	$1.9	$2.4	$ 0
QII	8.4	3.0	2.8	2.4	.1
QIII	10.0	3.9	2.6	3.3	.2
QIV	10.2	3.8	2.7	3.5	.2
1969 - QI	8.3	2.7	2.5	3.0	.2
QII	9.6	3.1	2.9	3.2	.4
e July-Aug.	7.3	1.3	3.2	2.8	0

Michigan survey of consumer demand. The August-September index of consumer sentiment declined sharply to the lowest level since 1958. Responses to all five attitudinal questions were lower for the second consecutive quarter. Unlike the previous deterioration in sentiment, which occurred primarily among lower income families, the latest downward shift was among the upper income families.

Families' evaluation of their likely personal financial situations a year from now has apparently been seriously affected by inflation. The proportion expecting to be worse off jumped from 6 per cent in May-June to 14 per cent in the third quarter--the highest proportion since the question was first asked in 1953. The reason was clearly higher prices rather than lower income.

Explanation of "worse off"	February 1969	May-June 1969	August-September 1969
		(Per cent of families)	
Lower income	9	7	10
Higher prices	13	22	24

Responses to other questions (not included in the index) were also pessimistic. Families thought that unemployment was more likely to increase, and the number planning to buy a new car was lower than a year ago although used car purchase plans were higher. Less than half of the respondents thought that the government was trying to slow inflation and only 42 per cent of these (18 per cent of all respondents) also thought that the government would be successful in its efforts.

The most frequently mentioned item of "bad news" was "tight credit" and "high interest rates." This was cited as a problem more frequently than the decline in the stock market, and the table below suggests that some consumers may be postponing purchases of cars, household durables, and homes because of monetary restraint.

	November-December 1968	February 1969	May-June 1969	August-September 1969
	(Per cent of all families)			
Bad time to buy because credit is tight; interest rates high:				
Cars	3	7	10	11
Large household goods	3	6	8	11
Houses	19	24	36	45

Cyclical indicators. The preliminary Census composite leading indicator declined slightly in August after rising in July and is still less than 1 per cent below its April-May high. The coincident composite continued to increase. Based on the current performance, it would be

difficult to conclude that an upper turning point has already been reached. The behavior of the leading composite would not, however, be inconsistent with a turning point in the next few months.

(The leading indicator composite has been revised by the substitution of an unemployment claims series for the nonagricultural placements series. The revision does not much change the recent movements of the series.)

COMPOSITE CYCLICAL INDICATORS
1963 = 100

		12 Leading Indicators	5 Coincident Indicators	6 Lagging Indicators
1969:	April	152.8	167.7	182.8
	May	152.8	168.9	184.7
	June	151.7	170.9	187.3
	July	152.0	170.7	189.9
	August (prel.)	151.6	171.9	193.6

The July leading composite was revised upwards with the inclusion of net business formation and July's high inventory change figure. In August, series decreasing included the manufacturing workweek, durable new orders, contracts and orders for plant and equipment, housing permits, common stock prices, and the ratio of price to unit labor cost. Industrial materials prices continued to rise and there was a slight improvement (i.e. decline) in unemployment claims. The preliminary September materials and common stock price indexes were up.

Manufacturers' orders. New orders at durable goods manufacturers declined 2 per cent in August, with most industry and market categories lower. Shipments rose, backlogs fell, and the ratio of backlog to shipments declined. Unfilled orders at machinery and equipment manufacturers dropped for the first time since last November.

Orders had been strong in July and the July-August average is still above the second-quarter average for the total and for most categories. New orders for machinery and equipment, however, have fallen off from their April high and are well below the second-quarter average. Defense orders had rebounded in July from a low second quarter but are below last winter's levels.

NEW ORDERS FOR DURABLE GOODS
(Per cent changes in monthly averages, seasonally adjusted)

	1969		
	Second quarter from first	July-August average from second quarter	August from July
Total durable goods	0.3	0.7	-2.2
Primary metals	3.2	5.2	-4.4
Iron and steel	8.8	6.9	-5.3
Motor vehicles	-1.9	0.9	8.0
Consumer durables, exc. autos	-2.4	2.7	-13.0
Machinery & equipment industries	4.8	-6.2	-2.3
Defense products industries	-12.5	9.3	-7.5
All other durable goods	3.1	-0.6	-0.1

Business inventories. In August, manufacturers' stocks rose much less than the high July rate, but the July-August average increase still exceeded the average for the preceding two quarters. Trade inventories jumped in July. With retail sales continuing weak for the rest of the third quarter and auto production running well ahead of sales, further increases in trade stocks seem likely. With the slowing of the quarter-over-quarter rise in wholesale prices, meaning that relatively more of the book value increase represents an increase in physical volume of inventories than has been the case recently; it seems probable that the corporate inventory valuation adjustment (IVA) will drop appreciably from the $6 billion annual rate in the first half. Both the available data on book values and the smaller IVA support over projections of an increase in inventory investment on a GNP basis in the third quarter.

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

	1969			
	QI Average	QII Average	July	August
Manufacturing & trade, total	877	954	1,357	n.a.
Manufacturing, total	579	633	951	483
Durable	518	501	962	265
Nondurable	61	132	-11	218
Trade, total	298	321	406	n.a.
Wholesale	182	176	-30	n.a.
Retail	116	145	436	n.a.
Durable	27	-59	-7	n.a.
Nondurable	89	204	443	n.a.

Durable goods retail stocks changed little in July; the buildup in nondurable retail stocks, on the other hand, was very large. All nondurable categories increased in July, with the largest part of the rise at general, drug, and other retailers. The major retail inventory-sales ratios were up from the lows of April to late-1966 levels.

INVENTORY-SALES RATIOS

	1966		1969		
	Sept.	Dec.	April	July	Aug.
Manufacturing & trade, total	1.50	1.56	1.54	1.55	n.a.
Manufacturing, total	1.65	1.72	1.71	1.70	1.71
Durable	1.89	2.00	2.00	2.04	2.03
Nondurable	1.35	1.37	1.34	1.28	1.31
Trade, total	1.34	1.39	1.36	1.38	n.a.
Wholesale	1.15	1.22	1.19	1.20	n.a.
Retail	1.46	1.51	1.46	1.50	n.a.
Durable	2.01	2.10	2.04	2.11	n.a.
Nondurable	1.19	1.23	1.19	1.23	n.a.

In August, the durable goods manufacturers' inventory-shipments ratio dropped slightly, but there was a further rise in their ratio of inventories to unfilled orders.

Residential construction and real estate. Seasonally adjusted private housing starts continued to decline in August for the seventh consecutive month. Unlike the drop in July, the August decline was moderate and was concentrated entirely in single-family starts. Regionally, the movement was quite mixed, with a sharp upturn in the North Central states from a particularly low rate and a slight rise in the Northeast offsetting most of the decline in the West and South.

PRIVATE HOUSING STARTS AND PERMITS

	August 1969 (Thousands of units) 1/	Per cent change from July 1969	Per cent change from August 1968
Starts	1,336	- 2	-12
1-family	732	- 9	-16
2-or-more family	604	--	- 7
Northeast	189	+ 2	-26
North Central	354	+25	+ 3
South	518	- 6	-17
West	275	-20	- 6
Permits	1,193	- 3	- 8
1-family	577	+ 1	-14
2-or-more-family	616	- 6	--

1/ Seasonally adjusted annual rates; preliminary.

Given the minor further decline in permits in August, the relatively large backlog of commitments--including FNMA commitments--still available, and technical measurement considerations, starts in September may at least have leveled off at the reduced August rate. If so, this would yield a third quarter average of 1.34 million units, seasonally adjusted annual rate. This would be 17 per cent below the average in the first half year, though still appreciably above the 1.08 million rate in the third quarter of 1966 when multifamily starts were considerably lower than has been the case this year. Moreover, further reductions are clearly indicated for the period ahead by the sustained downward pressures on flows to financial intermediaries this year and the evidence now available from the latest FRB-FHLBB Lender Survey which is discussed in a special attachment to the Green Book.

Based on data now available, indications are that upward pressures on home prices mounted further this summer. In July, for example, median prices of existing homes actually sold were 11 per cent above a year earlier, according to the National Association of Real Estate Boards. This compared with an average year-to-year increase of about 7 per cent during the first half of 1969. Sales of such homes, meanwhile, edged below the advanced year-earlier level for the first time this year.

Labor market. Employment growth eased in most major industries this summer and the manufacturing workweek drifted down slowly from March through August. The slowing of growth was associated with some increases in insured unemployment claims in late August and early September. An increase in total joblessness probably occurred in September.

A major element in the slowing of overall employment growth was the reduction in construction employment, which was due partly to strikes and partly to reduced residential building. Construction-related manufacturing industries also showed slight declines. Restraints on Federal spending and hiring resulted in small employment reductions in government and in defense-related manufacturing industries, while State and local governments added relatively few employees between May and August.

NONFARM PAYROLL EMPLOYMENT
(Average monthly change in thousands, seasonally adjusted)

	December-March	March-June	June-August
Total	278	197	92
Government	33	42	-7
Private industry	245	154	99
Construction	15	31	-32
Manufacturing	55	25	73
All others	175	98	58

Job gains continued in the capital-goods and primary metals industries, but here too, some slowing appeared to be developing. Changes in other sectors were also more moderate, in part reflecting the sluggishness of consumer buying. The only sizable increase this summer occurred in August in the transportation equipment sector of manufacturing, where an early model changeover in the auto industry boosted the employment figure by 150,000 from July and by about the same amount from the average level over the prior 12 months. The bulk of this increase was due to the timing of the changeover and a sizable decline is anticipated for this industry in September.

Income and wages. Although employment growth slowed this summer, personal income gains amounted to a $5 billion each in July and August. However, income flows were supplemented in both months by special factors. The most important of these was the Federal pay raise which added about $2-1/2 billion to growth in July and $1/2 billion in

August. The August figure was also inflated to some extent by the early model changeover in the auto industry. Exclusive of these one-time stimulants, the growth rate of income in the past few months was slower than in the prior six months and slower than in 1968.

PERSONAL INCOME
(Average monthly increase, billions of dollars, seasonally adjusted)

	1968	1969			
	Year	QI	QII	July	Aug.
Personal income	5.2	4.9	5.1	5.3	5.2
Wage & salary disbursements	3.5	4.0	3.5	4.3	4.2
Government	0.5	0.5	0.5	3.0	1.0
Private	3.0	3.5	3.0	1.3	3.2
Manufacturing	1.0	1.0	1.0	0.7	1.7
Nonmanufacturing	1.9	2.5	2.0	0.6	1.5
Other sources of income	1.8	0.8	1.7	1.0	1.0

The moderate employment advances expected in the next few months should serve to restrain the growth of wage and salary payments; sizable advances in hourly earnings, however, will keep the total growing. Average hourly earnings continued to rise strongly in July and August, with the momentum being maintained in part by very large wage increases in recently negotiated construction industry contracts. Increases in hourly earnings from a year ago averaged 6.8 per cent in July and August for production and nonsupervisory workers on private nonfarm payrolls, with construction workers showing an increase of nearly 9 per cent. Any slowing in the rise of hourly earnings would likely be attributable to employer cutbacks of overtime and the comparatively low level of collective bargaining activity through year end. In 1970,

a series of large, important contracts--including the railroad, trucking, rubber, construction and auto industries--are scheduled for renegotiation. Unions in these industries will demand catch-up wage increases, and given the accelerated price increases of 1968-1969, it is doubtful that large boosts in basic wage rates can be prevented, even in the presence of an easing labor market and reduced profit margins.

Wholesale prices. Wholesale prices in September rose at about the same 1 per cent annual rate as in August, according to preliminary BLS estimates, but the rise in industrial commodity prices edged down to an annual rate of 4 per cent following the upward revised 5 per cent of August. The somewhat smaller rate of rise in September was not unexpected in view of the concentration of price increases for steel mill products in August, and does not diminish the impression that pressures on industrial prices have not moderated appreciably as yet. In fact, the September rise was about the same as the average monthly increase over the past year. Preliminary estimates also indicate that nearly one-half of industrial product classes showed increases in September--a substantially higher proportion than in August and close to the level of June and July.

Prices of metals accounted for about half the increase in the industrial commodity average in September, following a rise of 6.7 per cent in the first eight months of the year. Non-ferrous metals increased about 13.0 per cent over the same period and in September zinc, copper, steel, and aluminum products prices were raised by some producers. A

substantial increase in nickel prices is expected to follow the settlement of a prolonged strike at major Canadian producers which normally supply most of the U.S. market; stainless steel prices have already been increased to reflect nickel shortages.

Other industrial commodity price increases in September included apparel, footwear, electric power, paperboard, and concrete. The increase in machinery prices accelerated.

Increases in price for 1970 autos have been announced, but it cannot yet be determined whether they will be larger or smaller than in 1968. Judging from manufacturers' announcements, major appliance prices will rise this fall, and this may also be true for television sets.

Cattle prices have been declining since early summer, and hog prices are below August peaks; these accounted for most of the 0.6 per cent decline in the farm products index in September. Meat prices are reflecting these declines, but may not fall much further since the fourth quarter supply of meats is expected to rise less than seasonally. At present, it looks as though any decline in meat prices may be temporary.

WHOLESALE PRICES IN SEPTEMBER
(1957-59-100)

Commodity group	Prelim. Estimate Sept. 1969	Per cent change to Sept. 1969 from: 1 month ago	3 months ago	1 year ago
All commodities	113.5	0.1	0.3	4.0
Farm products, and processed foods and feeds	114.3	-.3	-1.0	5.2
Industrial commodities	113.1	.3	.8	3.6

Consumer prices. Consumer prices increased at an annual rate of about 5 per cent in August, a smaller rise than in the preceding several months. As in recent months, food and services contributed most to the increase. The index was 5.6 per cent above a year earlier.

Food prices in August rose less sharply than in the preceding two months. Beef prices fell, for the first time in eight months, but the price of pork and other meats rose sufficiently to offset the drop. Eggs rose particularly sharply as consumers shifted from meat to eggs, and fruits and vegetables declined less than seasonally.

On the other hand, the increase in the cost of services accelerated in August. Home and automobile repair costs rose at a fast pace and gas and electric utility rates increased. Rents rose at a rate of about 5 per cent, but this was less than half the rate of rise in the services and costs connected with homeownership.

Among nonfood commodities, apparel declined in price in August for the first time in 4 years, reflecting in part late summer sales. However, in view of rising wholesale prices of apparel, this is probably no more than a temporary remission in the rise in apparel prices, which in August were over 5 per cent above a year earlier.

CONSUMER PRICE INDEX

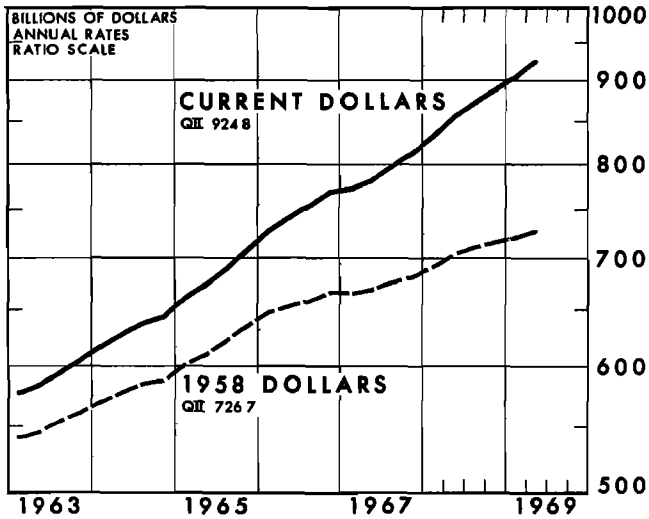
	Per cent change at annual rates to August 1969 from:		
	August 1968	May 1969	July 1969
All items, (unadjusted)	5.6	6.0	4.8
Commodities--(unadjusted)	4.7	6.0	3.6
Food	5.7	12.0	7.2
Apparel & upkeep	5.2	0.0	-2.4
Commodities--(seasonally adjusted)	4.7	5.2	1.2
Food	5.7	7.2	6.0
Apparel & upkeep	5.2	3.6	-2.4
Services, (unadjusted)	7.0	6.4	8.4
Insurance and finance 1/	10.7	9.2	13.2
Other services	4.9	4.8	6.0

1/ Includes mortgage interest, taxes and insurance, auto insurance, other auto expenses.

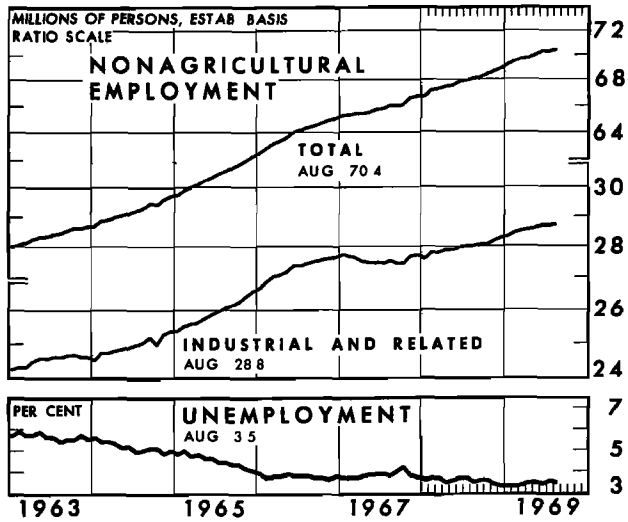
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

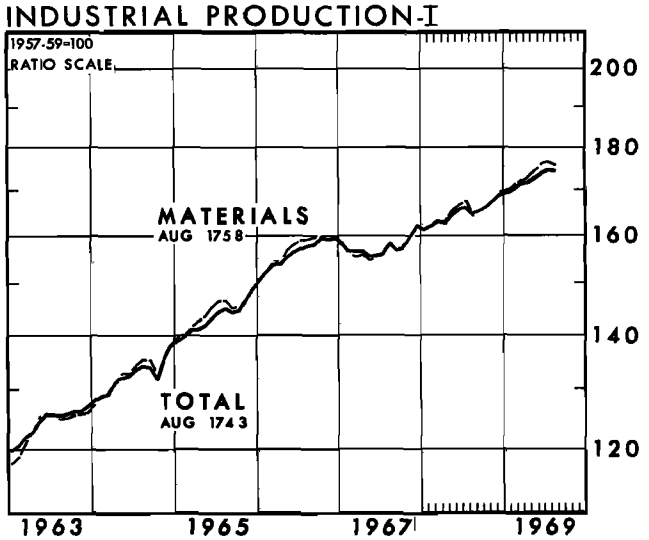
GROSS NATIONAL PRODUCT



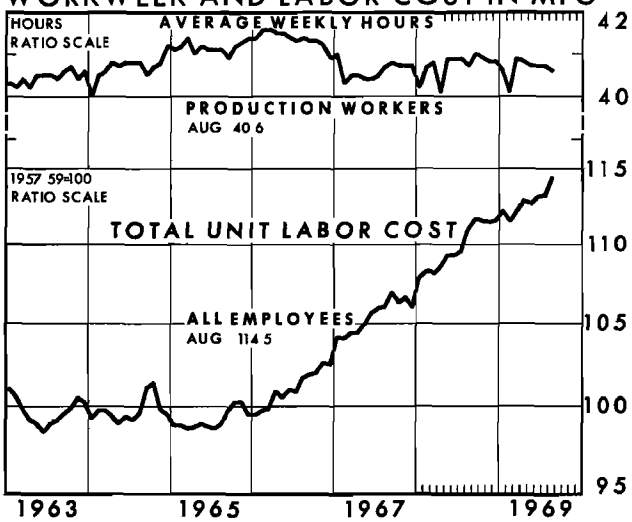
EMPLOYMENT AND UNEMPLOYMENT



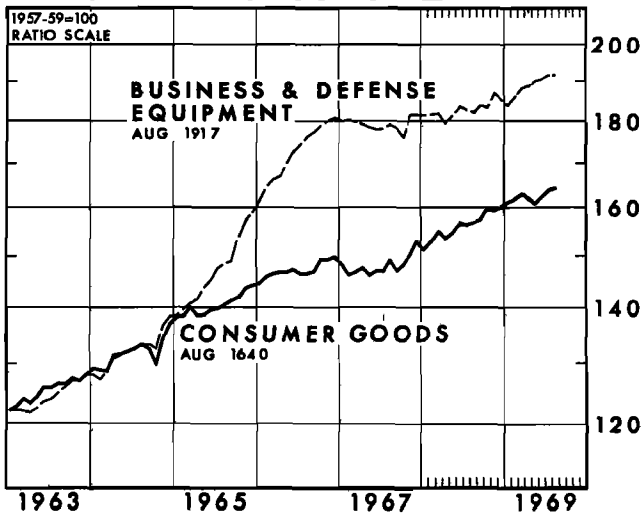
INDUSTRIAL PRODUCTION-I



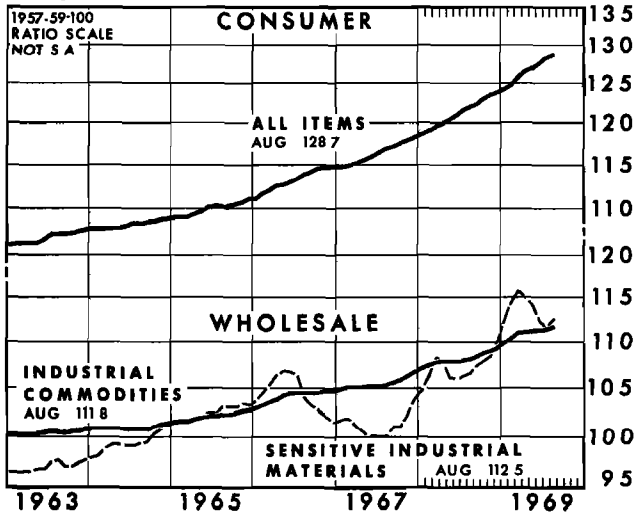
WORKWEEK AND LABOR COST IN MFG



INDUSTRIAL PRODUCTION-II



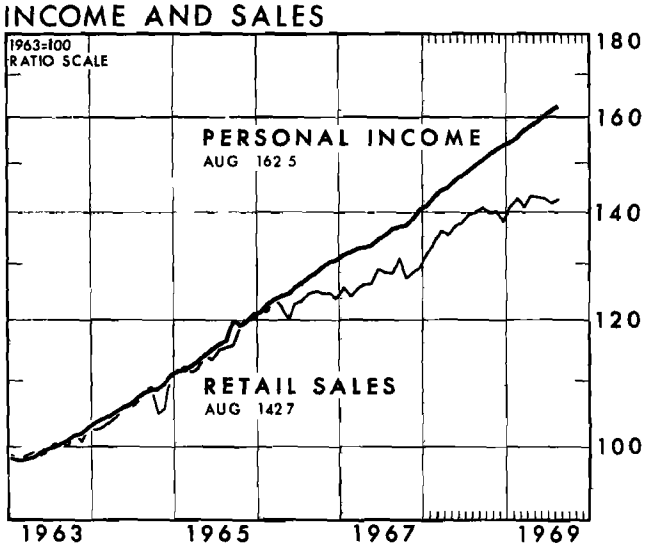
PRICES



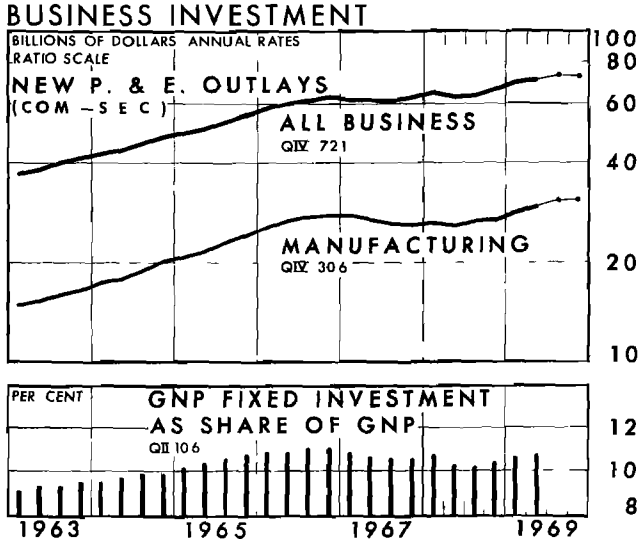
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

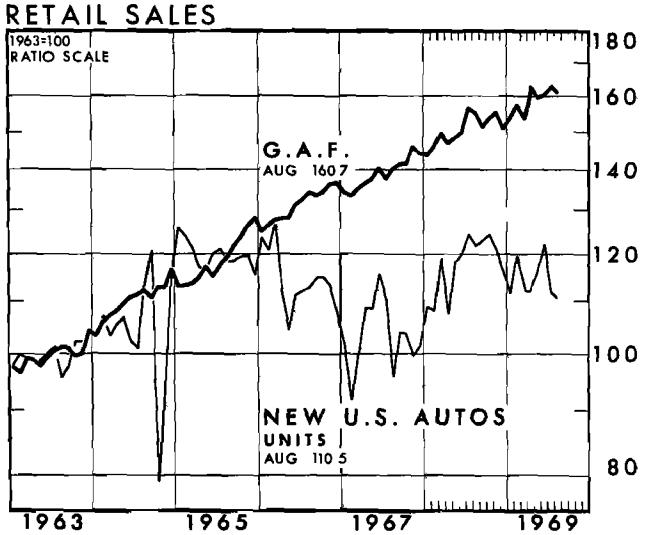
INCOME AND SALES



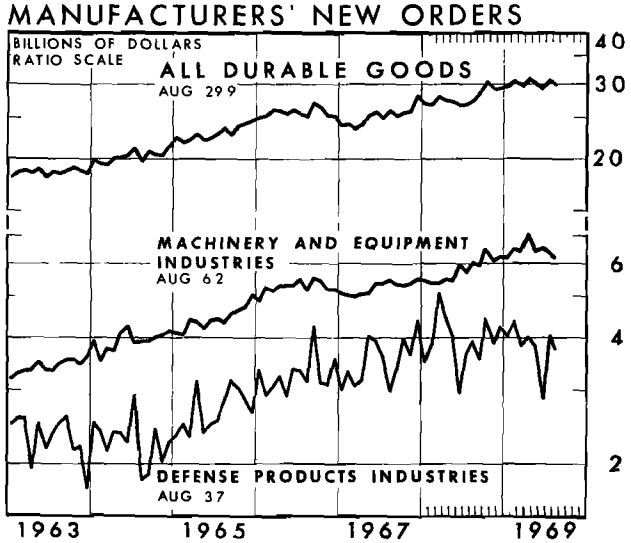
BUSINESS INVESTMENT



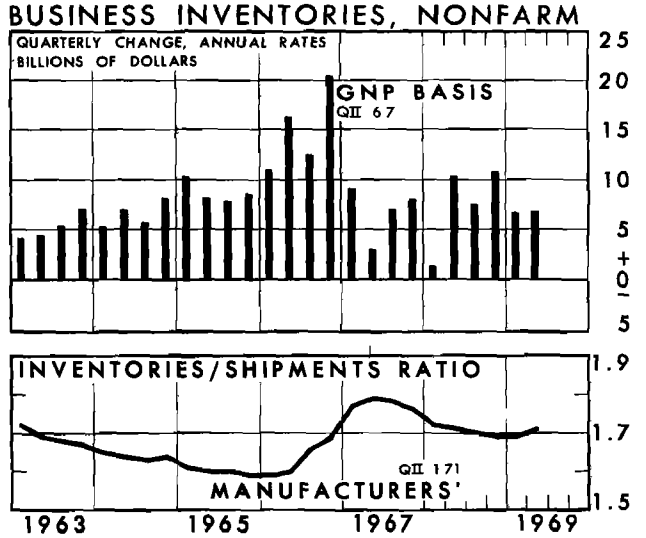
RETAIL SALES



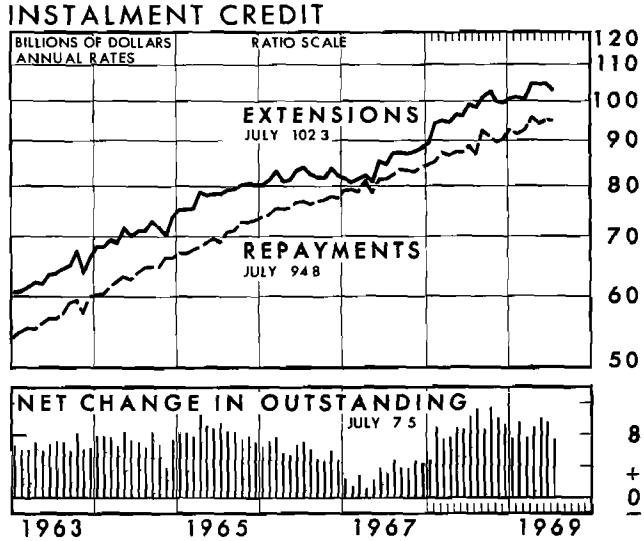
MANUFACTURERS' NEW ORDERS



BUSINESS INVENTORIES, NONFARM



INSTALMENT CREDIT



THE ECONOMIC PICTURE IN DETAIL

Domestic Financial Situation

Bank credit. Commercial bank credit is estimated to have declined slightly in September as a sharp drop in holdings of U.S. Treasury securities more than offset moderate increases in loans and holdings of other securities. Bank credit has now remained virtually unchanged for four months, with declines in investments approximately offsetting a moderate advance in loans. Credit extended through the banking system has risen moderately over this period, however, if the net increase in commercial paper issued by affiliates of banks is taken into account.

NET CHANGE IN BANK CREDIT
All Commercial Banks
(Seasonally adjusted percentage change, at annual rates)

	1968	1969		
	Year	1st 5 months	June-September	September
Total loans & investments[1/]	11.0	3.9	-0.2	- 0.3
U.S. Gov't. securities	3.0	-21.5	-3.8	- 27.6
Other securities	16.4	--	-6.3	3.4
Total loans	11.6	11.2	2.1	4.5
Business loans	11.1	16.8	4.1	3.5
All other loans	11.9	7.7	0.9	5.1

1/ Last Wednesday of the month series. Data for September are preliminary estimates and are subject to revision.

The sharp decrease in holdings of U.S. Treasury securities in September was confined primarily to short-term bills apparently reflecting bank distribution of the Treasury strip bills acquired in the late August financing. The increase in other security holdings, the first monthly advance since March, presumably reflected in large part underwriting by New York City banks of the $450 million of short-term notes sold by the State of New York on September 12. There was also a small rise in holdings of other securities at nonweekly reporting banks in early September, following a small decline over the summer, but holdings at large banks outside New York City continued to decline.

The September advance in total loans was scattered among a number of categories with small gains recorded in all major classes except loans to nonbank financial institutions. Consumer loans increased at the reduced rate of recent months, while real estate loans rose somewhat faster reflecting in part a sizable loan reclassification in one District.

Despite large tax payments, business loans are estimated to have increased only $300 million in September or slightly less than the average monthly rise over the preceding three months. Compared with earlier in the year, recent growth has slowed considerably. Even after adjustment for outright sale of loans, business loan expansion in recent months has been well below its pace earlier this year. Judging from scattered reports of bankers and the probable

trend of inventory investment this summer, this moderation in business loan growth seems to be attributable predominantly to reduced willingness and ability of banks to lend.

Bank sources of funds. Member bank deposit balances, measured on a daily average basis, increased moderately in September. A sharp build-up in U.S. Treasury deposits around the mid-September tax date was mainly responsible for this expansion, which represents the first month-to-month increase in total deposits since April. Private demand balances also rose slightly, and time deposits continued to fall but at a considerably slower pace than in recent months.

NET CHANGE IN TIME AND SAVINGS DEPOSITS
Weekly Reporting Banks
(Millions of dollars, not seasonally adjusted)

	Dec. 11 - Aug. 27			Aug. 27 - Sept. 17		
	1967	1968	1969	1967	1968	1969
Total time & savings	+13,067	+4,866	-13,639	-413	-215	-1,006
Consumer deposits	+ 6,679	+3,496	- 925	+474	+447	- 2
Savings	+ 971	- 307	- 2,084	+152	+ 46	- 130
IPC time deposits	+ 5,708	+3,802	+ 1,159	+322	+401	+ 128
Negotiable CD's	+ 5,335	+1,189	-11,643	-845	-471	- 795
All other time	+ 1,053	+ 181	- 1,071	- 42	-191	- 209
Memorandum:						
Euro-dollar borrowing	- 373	+2,370	+ 7,306	- 46	+574	- 159

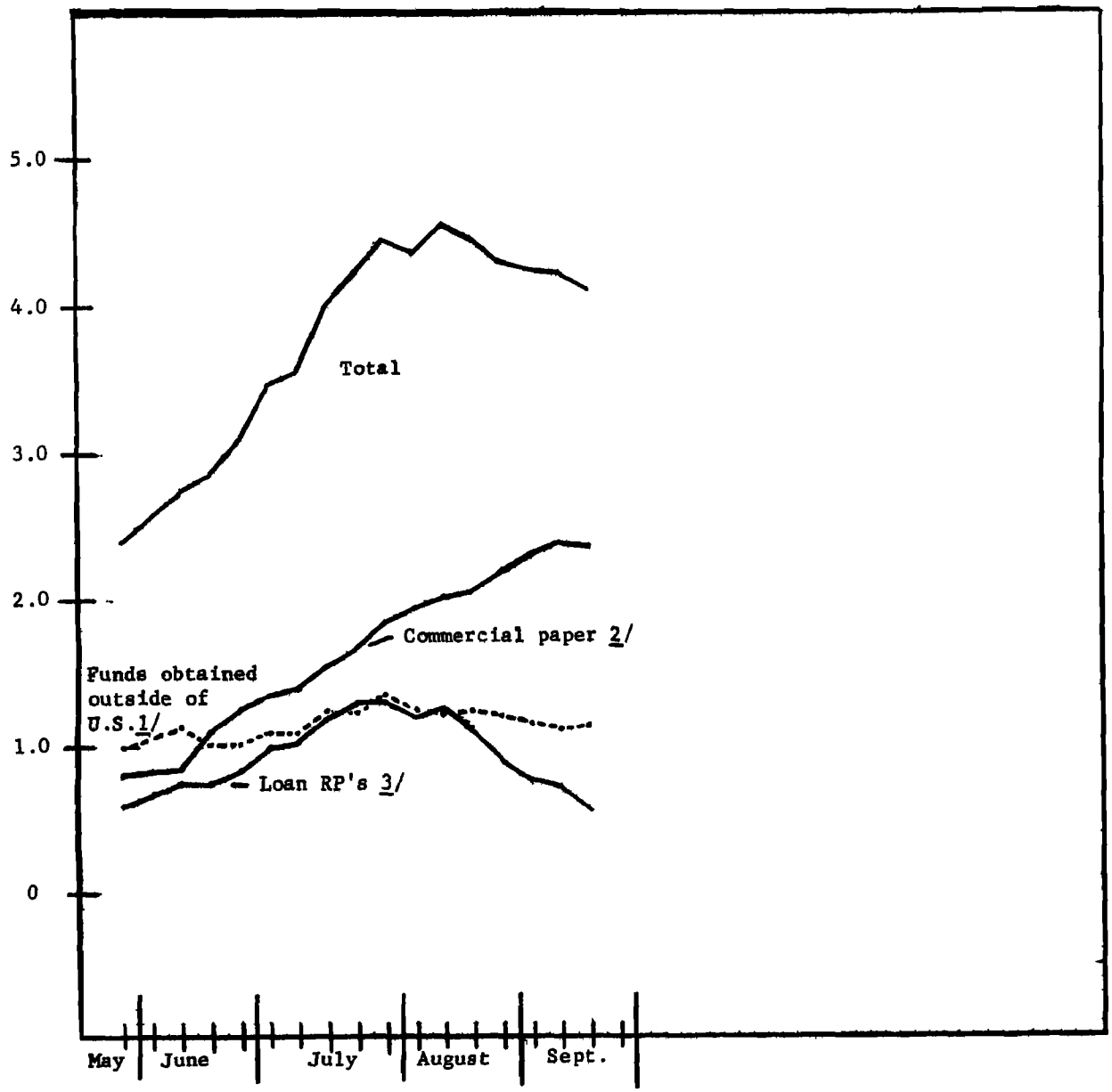
Continued heavy runoff of large CD's was again responsible for a major part of the drop in total time deposits. Substantial CD attrition has been usual during September in recent years, but this year's decline was quite large, particularly when measured in relation to the sharply reduced level of outstandings. A large portion of the decline in CD's took place over the two weeks encompassing the corporate tax and dividend dates, when attrition on maturing CD's was nearly 80 per cent. As in other recent months, a considerable proportion of the CD attrition occurred at banks outside New York City.

Consumer-type time and savings deposits continued to decline in September but at a much reduced rate. While savings deposits declined further, this drop was offset in part by a small rise in time certificates and open account deposits.

Net acquisition of funds from nondeposit sources, which had diminished considerably in recent months, turned into net outflows in September as slight declines occurred in both Euro-dollar borrowings and other nondeposit liabilities. Loan RP's continued to runoff sharply and Euro-dollar borrowings from sources other than foreign branches trailed off. Continued growth in commercial paper issued by bank holding companies or affiliates, although at a somewhat slower pace, partly offset the reduction in bank nondeposit sources. An analysis of individual bank data suggests that for the most part, there has been little correlation between changes in the two types of

SELECTED NONDEPOSIT SOURCES OF FUNDS

(Outstandings in billions of dollars)



1/ Euro-dollars borrowed directly or through brokers or dealers, and liabilities to bank's own branches in U.S. territories and possessions. Does not include liabilities to own foreign branches.

2/ Issued by a bank holding company or other bank affiliate.

3/ Loans or participations in pools of loans sold under repurchase agreement to other than banks and other than banks' own affiliates or subsidiaries.

financing, with only a few banks using commercial paper issues of their affiliates to offset declines in the banks' sources of nondeposit funds.

Further revisions in the money supply data--made necessary by new benchmark data and the updating of seasonal factors--have resulted in some further changes in the magnitude and timing of money supply growth this year, but the changes were relatively minor as compared with the August revision for Euro-dollar float. Based on averages of daily figures for the last month of each quarter, the money supply increased at a 4.1 per cent annual rate in the first quarter and at a 4.5 per cent annual rate in the second quarter instead of at the annual rates of 2.9 per cent and 4.7 per cent, respectively, indicated by the August revisions.[1/]

In September, the money supply rose at an annual rate of only about 1 per cent, reflecting in part the substantial rise in U.S. Government deposits. The annual rate of growth for the third quarter appears to be working out to less than 1 per cent on the revised basis.

1/ For a discussion of the revisions and back data, see Appendix A.

Nonbank depositary intermediaries. Pressure on savings flows has been continuous since July. At the sensitive New York savings banks and west coast S&Ls large year-to-year shortfalls continued at least through early September. In the aggregate, seasonally adjusted

SAVINGS FLOWS - NEW YORK SAVINGS BANKS AND SAN FRANCISCO DISTRICT S&L's

(Not seasonally adjusted, millions of dollars)

	Net "Adjusted" Inflow 1/ New York State MSBs			Net New Money San Francisco District S&Ls		
	July	August	September 2/	July	August	September 3/
1966	158	67	20	-152	63	n.a.
1967	185	132	40	89	151	97
1968	53	76	25	-105	79	77
1969	-265	- 48	2	-310	- 79	15

1/ Adjusted to exclude passbook loans as well as interest credited.

2/ First 15 days of September, for the 15 largest savings banks in New York City.

3/ First 10 days of September.

savings growth slowed further during July and August from the modest second quarter pace. On an unadjusted basis, through the first eight months of this year, there was a loss of deposits, excluding interest credited, from both types of institutions. The recent developments suggest that a further sizeable outflow can be expected during the current reinvestment period.

SAVINGS GROWTH AT NONBANK THRIFT INSTITUTIONS*
(Seasonally adjusted per cent changes, at annual rates)

	MSB's	S&L's	BOTH
1968 - IV	7.1	6.2	6.5
1969 - I	6.2	6.1	6.1
II	4.3	3.5	3.8
June	3.3	4.4	4.0
July	-0.9	-0.4	-0.5
August	3.6	2.5	2.8
Memorandum:			
1968 July & August	6.1	5.3	5.6
1969 July & August	1.4	1.1	1.2

* Because of seasonal adjustment difficulties, monthly patterns may not be significant.

NET NEW MONEY FLOWS[1/]

(Not seasonally adjusted, millions of dollars)

	Monthly Average				First
	QI	QII	July	August	8 months
Insured S&Ls					
1966	228	-215	-1,495	121	-1,337
1967	606	668	34	623	4,479
1968	276	186	- 606	366	1,148
1969	306	- 19	-1,122	- 15	- 278
Mutual Savings Banks					
1966	95	-188	108	120	- 41
1967	292	197	222	283	1,973
1968	193	0	64	181	825
1969	150	-126	- 295	30	- 193

1/ Deposits minus withdrawals, excluding interest credited.

Takedowns of previous commitments have maintained net mortgage lending of the thrift institutions. With reduced inflows, these institutions have not been able to rebuild their liquidity since the July interest-crediting period and will have to rely more heavily on other sources of funds to meet expected withdrawals.

In October, as in other recent months, S&Ls can be expected to draw extensively on FHLB advances. The FHLB System is entering the current reinvestment period with a fairly high $1.1 billion in liquid funds available for advances, including $500 million of new money received from its September financing. So far this year, the FHLB System has raised $2.4 billion of new money from the market, and in the remaining months of this year it is expected to raise additional large amounts to maintain its support of the mortgage market.

NET CHANGE IN FHLB ADVANCES TO SAVINGS AND LOAN ASSOCIATIONS
(Millions of dollars)

	Q I	Q II	Q III
1966	-301	1,093	394
1967	-1,737	- 874	-178
1968	-114	652	145
1969	50	1,076	1,524*

* Includes $200 million of the special 5-year advances.

Liquidity of mutual savings banks has also been greatly reduced. Heavy outflows during the current reinvestment period are thus likely to place many of these institutinns under considerable strain. To meet their commitments, MSB's may have to activate bank credit lines and/or take sizeable losses in the liquidation of some of their less marketable Agency and corporate securities.

Mortgage market. With savings inflows at thrift institutions off sharply and overall prospects for the current reinvestment period bleak, the residential mortgage market continued to tighten during September. The latest FHA and FNMA field office reports, as well as the recently conducted FRB-FHLBB survey, indicate that the demand for mortgage funds continues to exceed supply in most areas. Furthermore, the FRB-FHLBB survey results (being distributed with this Greenbook) suggest that the supply of short-term and long-term credit was more limited in early September than at any other time this year.

Reflecting the low level of liquidity and the concern of thrift institutions about future savings flows, the seasonally adjusted dollar volume of new commitments at all savings and loan associations and New York State mutual savings banks apparently fell further in August, to the lowest level since November 1966. The backlog of outstanding commitments fell again, but still remains unusually high relative to earlier years. The size of this backlog, in the context of the severe liquidity pressures faced by the institutions, suggests further constraint on new commitment activity. Although policy loan

pressures have continued quite strong, the most recent life insurance company data (July) suggest that new mortgage commitments have not declined further from their modest year ago pace, but the share accounted for by 1-4 family residential mortgages declined to extremely low levels. High yields and "equity kickers" on income properties continue to make such mortgages much more attractive.

OUTSTANDING RESIDENTIAL MORTGAGE COMMITMENTS

	All Savings & Loan Associations	Mutual Savings Banks (N.Y. State)
	($ millions, seasonally adjusted)	
1966		
High	5,465 (Mar.)	2,731 (Jan.)
Low	3,261 (Nov.)	2,073 (Nov.)
1967		
High	5,825 (Dec.)	2,685 (Nov.)
Low	3,358 (Jan.)	2,164 (Jan.)
1968		
High	6,606 (Dec.)	3,203 (Nov.)
Low	5,822 (Jan.)	2,520 (Feb.)
1969		
High	7,184 (Apr.)	3,291 (Apr.)
Low	6,507 (Aug.)	2,977 (Aug.)
1969		
June	7,036	3,161
July	6,830	3,083
August	6,507	2,977

Note: Data from Federal Home Loan Bank Board and Savings Banks Association of New York State. Reporting savings banks account for about 70 per cent of total mortgage lending in the industry. Data for savings banks and S&L's include a minor amount of nonresidential commitments. S&L commitments include loans in process.

The scarcity of funds available for residential mortgage investment continued to increase pressures on mortgage interest rates in September. Average secondary market yields in FNMA's forward commitment auction of Government-underwritten loans advanced each week during September, despite the large volume of FNMA commitments accepted, and by the September 29 auction the average yield on 6-month commitments had risen above the previous high reached early in July.

FNMA WEEKLY AUCTION

		Amount of total offers		Implicit private market yield
		Received	Accepted	6-month commitments
		(Millions of dollars)		(per cent)
Highs				
1968		$232(6/3)	$ 89(7/1)	7.71(6/10)
1969		410(6/16)	152(9/8)	8.48(9/29)
Sept.	2	253	151	8.34
	8	243	152	8.36
	15	242	145	8.40
	22	247	145	8.44
	29	258	144	8.48

Note: Average secondary market yield after allowance for commitment fee and required purchase and holding of FNMA stock, assuming prepayment period of 15 years for 30-year Government-underwritten mortgages. Yields shown are gross, before deduction of 50 basis point fee paid by investors to servicers. The first auction date was May 6, 1968.

In the primary home mortgage market, the average contract rate on conventional first mortgages rose again in August, as usury ceilings were relaxed somewhat in the North Central region. However,

low usury ceilings in a number of states continued to blunt the rise of mortgage interest rates and to disrupt the potential flow of funds into mortgages. Due in part to the unwillingness of sellers to absorb deeper discounts, average secondary market yields on Government-underwritten home loans remained unchanged in August.

AVERAGE RATES AND YIELDS ON SELECTED NEW-HOME MORTGAGES

	Primary Market: Conventional loans		Secondary Market: FHA-insured loans		
	Level (per cent)	Yield spread (basis points)	Level (per cent)	Yield spread (basis points)	Discount (points)
1968					
Low	6.75(Jan.Feb.)	23(Mar.)	6.78(Feb.)	26(Mar.)	4.4(Sept.)
High	7.40(Dec.)	115(Aug.)	7.52(Aug.)	120(Aug.)	7.9(April)
1969					
January	7.55	63	7.85e	93e	2.8e
February	7.60	69	7.99	108	3.9
March	7.65	28	8.05	68	4.4
April	7.75	58	8.06	89	4.5
May	7.75	53	8.06	84	4.5
June	8.00	42	8.35	77	6.7
July	8.10	47	8.36	73	6.8
August	8.20	55	8.36	71	6.8

Note: FHA series: Interest rates on conventional first mortgages (excluding additional fees and charges) are rounded to the nearest 5 basis points. Data for FHA loans in January 1969 estimated by Federal Reserve for 7-1/2 per cent regulatory interest rate, on which a change of 1.0 points in discount is associated with a change of 12 to 14 basis points in yield. Gross yield spread is average mortgage return, before deducting service fees, minus average yield on new issues of high grade corporate bonds with 5-year call protection.

e/ Estimated.

Corporate security and municipal bond markets. While stock prices have changed little on balance in moderate trading throughout September, corporate bond prices have declined substantially. At month-end, yields on new issues of corporate bonds were at new highs, nearly 25 basis points above the peaks a month earlier. Even at these higher yields, a sizeable number of new issues have received lukewarm responses from investors and remain largely unsold. In contrast, municipal bond yields have declined about 30 basis points over the month, associated with a sharply reduced volume of new offerings and possibly hopes that the ultimate tax reform bill will be less restrictive than the House Bill regarding tax-exempt bond income.

STOCK PRICES AND BOND YIELDS

1968				
Low	48.66(3/4)	21.58(3/5)	6.13(8/30)	4.07(8/9)
High	61.27(11/29)	33.25(12/20)	6.92(12.13)	4.85(12/29)
1969				
Low	49.31(7/29)	25.02(7/29)	6.90(1/10)	4.82(12.24)
High	59.32(5/14)	32.91(1/3)	8.13(9/26)	6.37(9.5)
Week of:				
Sept. 5	51.80	26.33	7.90	6.37
12	52.19	26.42	8.02	6.33
19	52.84	26.77	8.04	6.25
26	52.23	26.63	8.13	6.08

1/ Prices as of the day shown. NYSE is New York Stock Exchange. AMEX is the American Stock Exchange.
2/ With call protection (includes some issues with 10-year call protection).
3/ Bond Buyer (mixed qualities.)

The recent run-up in corporate yields reflects not only mounting bond volume, but also the limited demand from institutional investors. Furthermore, there appears to be increasing investor hesitancy to commit funds at long-term because of expectations of a continued strong economy and restrictive monetary policy. Life insurance companies and mutual savings banks have virtually withdrawn from the public bond market as their cash positions have come under increasingly severe pressure. State and local pension funds--the largest single buyers of public corporate debt--are reportedly buying new issues quite selectively, allocating most of their cash to the money and equity markets. Managers of these funds appear to be expecting further upward yield movements and/or to be awaiting a clarification of underlying trends before returning more fully to the bond market. Individuals thus appear to be among the current major buyers of bonds.

The September volume of corporate new issues was sizable and contributed to the upward pressure of yields. Public bond issues aggregated $1.2 billion, a more than seasonal rise from the $0.7 billion offered in August. Stock offerings also exhibited an advance from the month earlier, owing to the clustering of several large preferred stock issues by utility companies. Thus, total corporate security offerings in September, including private placements, amounted to nearly $2.5 billion, significantly above the pace earlier in the year.

CORPORATE SECURITY OFFERINGS[1/]
Monthly or Monthly Averages
(Millions of Dollars)

	Public Bond Offerings		Private Bond Offerings		Stocks		Total	
	1968	1969	1968	1969	1968	1969	1968	1969
Year	894	--	554	--	382	--	1,830	--
Q I	821	886	574	513	330	674	1,726	2,073
Q II	1,035	1,136	548	526	319	709	1,902	2,371
Q III	869	1,063e	454	517e	389	533e	1,711	2,113e
August	637	700e	400	500e	396	400e	1,433	1,600e
September	727	1,230e	433	550e	398	700e	1,556	2,480e
October	1,009	1,200e	595	500e	525	600e	2,129	2,300e

e/ Estimated.
1/ Data are gross proceeds.

Corporate security offerings in October are estimated to decline somewhat in total from the September pace, due largely to a lighter schedule of stock issues. However, total new offerings in October would still be significantly above the average monthly volume during the third quarter. Public corporate bond offerings are expected to remain at September's $1.2 billion volume. The large financing requirements of public utility firms are again reflected in a heavy slate of utility offerings. It is assumed that convertible bond financing will continue to be somewhat discouraged by the level of stock prices, so that many such issues postponed earlier this year will not be marketed in October.

State and local government bond issues have been reduced sharply. The volume of long-term offerings in September is estimated at $525 million, less than one-half of the average volume for the first half of this year. While short-term issues continue to represent an alternative source of funds, these offerings have not been of sufficient volume to offset fully the shortfall in long-term financing, For the third quarter, as a whole, long-term issues of about $2.5 billion were less than one-half of the amount planned by governmental units--according to our recent survey of borrowing anticipations, and pressure to cut-back capital outlays should be increasing markedly. This situation is expected to continue as October bond volume is estimated at only $600 million, a level which assumes that municipal interest rates will not decline much further.

STATE AND LOCAL GOVERNMENT OFFERINGS
Monthly or Monthly Averages
(Millions of dollars)

	Gross Long-Term 1/		Net Short-Term2/		Total 3/	
	1968	1969	1968	1969	1968	1969
Year	1,381	--	- 38	n.a.	1,343	n.a.
Q I	1,246	930	- 56	328	1,190	1,258
Q II	1,285	1,208	5	375e	1,290	1,583e
Q III	1,537	792e	- 58	285e	1,499	1,070e
August	1,699	790	204	490e	1,963	1,280e
September	1,444	525e	-902	80e	542	605e
October	2,230	600e	252	n.a.	2,482	n.a.

e/ Estimated.
1/ Data are for principal amounts of new issues.
2/ EXCLUDES note offerings of Housing Assistance Administration and Renewal Assistance Administration.
3/ Combines GROSS long-term and NET short-term issues.

Corporate Finance. The slowdown in corporate financing in credit and capital markets during the summer occurred at a time when the flow of internal funds showed little change and total outlays for plant and equipment and inventories spurted again. Despite the step-up in corporate security offerings in September, net funds raised from this source in the quarter as a whole were at a seasonally adjusted rate one-eighth below either the first or second quarter, and short-term borrowing from banks and other lenders also declined. As these and other data have become available for the third quarter, it has become increasingly clear that corporations must have reduced their holdings of liquid assets considerably since midyear.

Moreover, rough projections for the fourth quarter suggest that the nonfinancial corporate universe will need to raise, from some combination of new borrowing and further reduction in liquid assets, as large a volume of funds as in the third quarter. In the table below, it is assumed that financing in credit and equity markets will increase somewhat, but will remain below the volume of the first half of the year, and that liquid assets will again be reduced, though not by as much as in the third quarter.

FLOW OF FUNDS, NONFINANCIAL CORPORATE BUSINESS

Seasonally adjusted annual rates, in billions of dollars

	1968		1969			
	H1	H2	I	II (prel.)	III (est.)	IV (proj.)
Sources						
Internal funds	61.5	64.7	63.0	63.3	63.5	63.8
Credit & equity market Instr.	22.1	30.0	38.9	32.5	26.5	30.0
Security issues & mortgages	16.4	15.4	18.8	18.2	16.0	17.5
Bank & other loans	5.7	14.6	20.1	14.3	10.5	12.5
Other sources	11.5	9.9	11.9	5.8	9.0	10.0
Uses						
Capital expenditures	76.8	81.3	86.7	87.0	91.5	92.6
Liquid assets	9.7	8.2	5.7	.2	-10.0	- 6.3
Other uses	8.3	12.3	16.6	10.1	13.0	13.0
Discrepancy	.3	2.8	4.9	4.4	4.5	4.5
Memo: Int. funds less cap. exp.	-15.3	-16.6	-23.7	-23.7	-28.0	-28.8

Note: "Other"sources comprise profit tax and miscellaneous liabilities; "other" uses comprise net trade credit, consumer credit, State and local securities, and miscellaneous financial assets.

The assumption that corporations will continue to reduce their holdings of liquid assets over the final quarter of the year, rather than to accelerate the volume of their new borrowing, reflects not only the level of interest rates and reduced credit availability but also new estimates of corporate financial flows in the second quarter. In particular, more complete data for that quarter suggest that holdings of liquid assets, rather than having been substantially reduced, remained about unchanged from the first quarter level.

However, the reduction in liquid assets shown in the table for the third and fourth quarters of this year would leave the relative liquidity position of corporations as a whole at the end of the year well below its level of a year earlier, following a decline of only seasonal proportions in the first half of 1969. Thus, it seems likely that corporations will be under pressure to increase the volume of their net long-term financing at the earliest opportunity to levels above those apparent in the third quarter and presently projected for the final quarter. Moreover, it is conceivable that the increase could come before the end of the year, although there is as yet no evidence which would support such a projection.

Government securities market. The U. S. Government securities market--except in the bill area--continued persistently weak during the last three weeks and price declines accelerated in the final days of September. Consequently, yields again have reached new highs, and are now generally up about 30 to 60 basis points in the note and bond area since the last FOMC meeting. The composite yields on intermediate and long-term securities have reached recent peaks of 7.91 and 6.57 per cent, respectively.

In contrast, short-term Treasury bill rates have declined recently, after reaching their highs in the third week of September when the 3-month rate closed at a record level of 7.16 per cent. Taking the last three weeks as a whole, short-dated bills have declined by 10 to 20 basis points, while the one-year bill is unchanged on balance.

MARKET YIELDS ON U.S. GOVERNMENT SECURITIES[1/]
(Per cent)

	Lows	Highs	Sept. 8	Sept. 22	Sept. 29
Bills					
1-month	5.30(3/25)	7.20(9/22)	7.14	7.20	7.02
3-month	5.87(4/30)	7.16(9/19)	7.09	7.14	6.91
6-month	5.96(4/30)	7.39(9/9)	7.37	7.32	7.31
1-year	5.86(1/16)	7.47(7/1)	7.41	7.38	7.41
Coupons					
3-year	6.02(1/20)	8.07(9.29)	7.68	7.87	8.07
5-year	6.11(1/20)	7.96(9/29)	7.39	7.72	7.96
7-year	6.09(1/16)	7.71(9/29)	7.20	7.51	7.71
10-year	5.95(1/20)	7.45(9/29)	7.03	7.26	7.45
20-year	5.91(5/5)	6.80(9/29)	6.48	6.58	6.80

1/ Latest dates of high or low rates in parentheses.

The advances in note and bond yields reflected the continued effects of a tight credit policy. Special factors contributing to the weak market atmosphere were the sizable buildup of new corporate financings, the prospect of heavy fourth quarter borrowing in the Federal agency market, and difficulty in finding investors for the new Treasury notes offered in the recent refunding.

Yields in the Treasury coupon market adjusted upwards partly in anticipation of the refunding. The Government offered three new notes in exchange for the $8.9 billion of securities maturing on October 1 and in mid-December, $7.6 billion of which were held by the public. Preliminary results from the Treasury indicate that around $3.4 billion of rights were exchanged for the new 8 percent 19-month note, while about $1.0 billion and $1.5 billion, respectively, were

turned in for the 3-1/2 year 7-3/4's and the 6 year 10 month 7-1/2's. This gives an over-all attrition rate of about 24 per cent of the publicly held rights.

The initial market reaction to the refunding was generally favorable, and the new notes moved quickly to premiums on a when-issued basis. Dealers took substantial positions in these issues, aggregating about $900 million just after the books closed on September 24. Most recently, the weight of the positions, together with some floating supply in the hands of trading banks and other temporary holders, has exerted downward pressure on new issue prices. By Monday, September 29, the new issues had fallen 6/32 to 1/2 point below their initial offering price, and dealers had reduced their positions by about $150 million.

DEALER POSITIONS IN GOVERNMENT SECURITIES
(In millions of dollars)

	Sept. 8	Sept. 22	Sept. 29
Total	2,024	1,732	1,773
Treasury bills (total)	1,567	960	790
Due in 92 days or less	322	132	44
93 days or over	1,245	828	834
Treasury notes and bonds (Total)	458	772	983
Due within 1 year	256	680	70
1-5 years	32	49	518
over 5 years	170	44	396

Bill rates increased through the middle of September. Since then, however, the market has been helped by a fair-sized amount of demand, including sizable buying by the System for foreign cccounts. The Desk bought almost $1.0 billion of bills for such accounts in the last half of September. Actual and anticipated bill demand also resulted from the refunding-- from attrition money as well as selling of rights.

Other short-term credit markets. During September, short-term interest rates outside the Treasury bill market have increased for some instruments while remaining constant for others. Rates on 3-month commercial paper have shown the greatest advances--about 50 basis points--to 8.75 percent, thus climbing higher than the prime rate. On the other hand, rates on finance paper have remained steady at 7.63 per cent. With Treasury bill rates declining slightly recently, the spread between bill rates and other short-term market rates widened.

Table 1

NEW FUNDS OBTAINED FROM THE PUBLIC IN THE FEDERAL AGENCY MARKET

	1966	1967	1968	1969
June	1,151	275	1,107	1,247
July	494	272	822	755
August	234	- 28	- 145	1,101
September	- 306	- 83	111	393
October	- 123	- 53	354	

Short-term rates in the agency market fluctuated within a narrow range during the month, but yields in the 9 to 12-month area--in which the new cash financing was concentrated--did move moderately higher. Thus the August 20, 9-month FICB offering had carried a yield of 8.12 per cent whereas a comparable September 19 offering yielded 8.20 per cent. The amount of new cash raised in the agency market was substantially lower in September than the exceptionally large August volume but cash borrowing did remain larger than usual for the month--with the Federal Home Loan Banks raising a sizable amount of new cash.

SELECTED SHORT-TERM INTEREST RATES
(Wednesday Quotation--Discount Basis)

	August 27	September 10	September 24
3-month			
Commercial paper	8.25	8.50	8.75
Finance paper	7.63	7.63	7.63
Bankers' acceptances	8.00	8.13	8.25
Federal agencies (secondary market)	7.73	7.67	7.69
Treasury bill	7.15	7.12	7.10
6-month			
Commercial paper	8.25	8.50	8.63
Finance paper	7.63	7.63	7.63
Bankers' acceptances	8.00	8.13	8.25
Federal agencies	7.93	7.89	7.88
Treasury bill	7.36	7.34	7.31
12-month			
Prime municipals 1/	5.75	5.85	5.75
Treasury bill	7.37	7.31	7.36

1/ Bond yield basis.

Federal finance. Data on outlays early in fiscal 1970 suggest that the Administration may have difficulty holding the year's total to $192.9 billion. September spending alone could be almost $2 billion higher than projected in the last Greenbook, implying a third quarter total $4 billion larger than a year earlier. Heavy defense expenditures account for some of the recent surge in outlays, but contract awards, usually a reliable leading indicator of defense spending, foreshadow lower expenditures for the rest of the year. On the other hand, the high level of outlays this quarter by the Commodity Credit Corporation may be maintained for the rest of the year. On balance, it is too early to estimate the total size of offsetting expenditure cuts that could take place later during the fiscal year, and the staff continues to project total outlays in the amount of $192.9 billion (See Appendix B for further details).

The large expenditures have led to a smaller increase in the Treasury cash balance in September than projected earlier. An additional $600 million drain on the balance is expected during October and November from the Housing Assistance Administration and the Renewal Assistance Administration. These agencies cannot finance their activities in the usual way by selling in the municipal bond market because of a 6 per cent ceiling imposed by Congress on their debt issues; consequently, the Treasury must provide operating funds until HAA and RAA can repay these funds, presumably before the end of the fiscal year.

Despite the Treasury expectations that the large September outflow will be offset later in the fiscal year, $5 to $6 billion new cash appears to be needed before the end of this calendar year. Presumably this would be raised through tax anticipation bills, part of them issued in October and the remainder in November. Even so the end-of-year cash balance would still be on the low side and thus would require additional borrowing early in January to cover the usual seasonal drain in that period.

The current Staff estimate of the fiscal 1970 surplus is $3.7 billion. In evaluating the degree of fiscal restraint implied, however, it should be recalled that five government sponsored agencies--FNMA, FICB, Banks for Coops, FLB, and FHLB--whose operations were included under the old cash budget concepts have now been dropped from the budget data. If agency lending during fiscal 1970 were included in the budget, the staff would estimate a fair-sized deficit--in the order of $5 to $6 billion. The Federal sector in the NIA accounts, however, which excludes all Federal lending operations, continue to show a sizable estimated surplus for fiscal year 1970.

FEDERAL SURPLUS OR DEFICIT (-)
(In billions of dollars)

Fiscal Year	Unified Budget	Unified Budget plus Agency Lending	In NIA Accounts
1964	-5.9	-8.0	-2.1
1965	-1.6	-2.3	2.0
1966	-3.8	-5.2	.9
1967	-8.8	-12.4	-7.2
1968	-25.2	-26.7	-11.5
1969	3.1	- .9	4.8
1970	3.7	-5.6	3.4

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	Sept.	Oct.	Nov.	Dec.
Borrowing operations				
New cash raised:				
Weekly and monthly bills	--	--	--	--
Tax bills	--	3.0	3.0	--
Coupon issues	--	--	--	--
Other (agency, debt repayment, etc.)	--	-1.0	--	-2.4
Total net borrowing from public	--	2.0	3.0	-2.4
Plus: Other net financial sources[b/]	-.3	1.0	-.8	--
Plus: Budget surplus or deficit (-)	2.9	-5.4	-1.5	2.0
Equals: Change in cash balance	2.6	-2.4	0.7	-.4
Memoranda: Level of cash balance end of period	6.6[a/]	4.2	4.9	4.5
Derivation of budget surplus or deficit				
Budget receipts	21.0	12.0	14.7	17.5
Budget outlays	18.1	17.4	16.2	15.5

a/ Actual
b/ Checks issued less checks paid and other accrual items.

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

	FY 1969 Actual	Calendar year 1969e/	Fiscal 1970 Summer Budg. Review	Fiscal 1970 F.R. Board	Calendar quarter 1969 I	1969 II	1969 III e/	1969 IV e/	1970 I e/	1970 II e/
Quarterly data, unadjusted										
New budget:										
Surplus/deficit	3.1	6.0	5.9	3.7	-2.0	15.3	-2.4	-4.9	-3.3	14.3
Receipts	187.8	197.6	198.8	196.6	44.1	60.8	48.5	44.2	44.0	59.9
Total expenditures and net lending	184.8	191.6	192.9	192.9	46.1	45.5	50.9	49.1	47.3	45.6
Means of financing:										
Total borrowing from the public	-1.4 1/	-6.2		-2.8	.2	-12.6	3.6 2/	2.6	4.1	-13.1
Decrease in cash operating balance	- .6	.2		- .1	-.1	-1.1	-.7	2.1	-1.5	--
Other 2/	-1.1	- .1	n.a.	- .8	1.9	-1.7	-.5	.2	.7	- 1.2
Cash operating balance, end of period	5.9	4.5		6.0	4.8	5.9	6.6*	4.5	6.0	6.0
Seasonally adjusted annual rate										
Federal surplus/deficit in national income accounts 3/	4.8	9.3	n.a.	3.4	9.6	13.0	7.0	7.4	0.9	-1.6
Receipts	192.2	200.9	n.a.	199.3	198.1	202.3	200.9	202.4	196.7	197.0
Expenditures	187.4	191.7	195.8	195.8	188.5	189.3	193.9	195.0	195.8	198.6

*--Actual

e--Projected. Assumes extension of surcharge at 10 per cent through end of calendar year 1969 and at 5 per cent for January to June 1970. Also assumes repeal of investment tax credit.

n.a. - Not available.

1/ Excludes effect of conversion of agencies to private ownership.

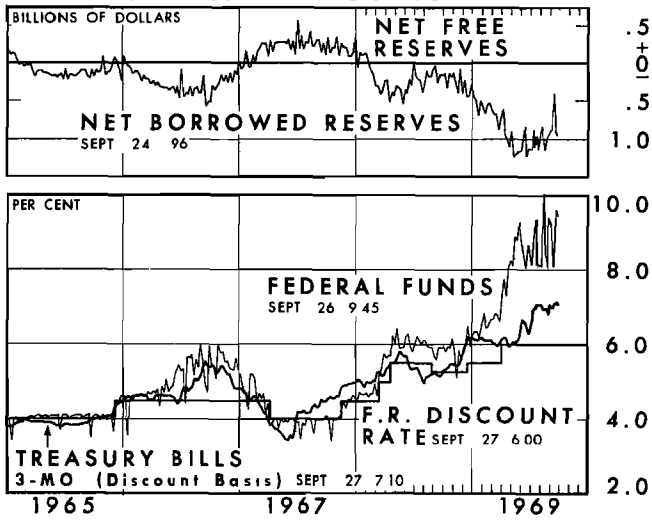
2/ Excludes effect of reclassification of $1.6 billion of CC certificates of interest from Budget transactions to borrowing from the public.

3/ Includes various accrual items, such as deposit fund accounts and clearing accounts.

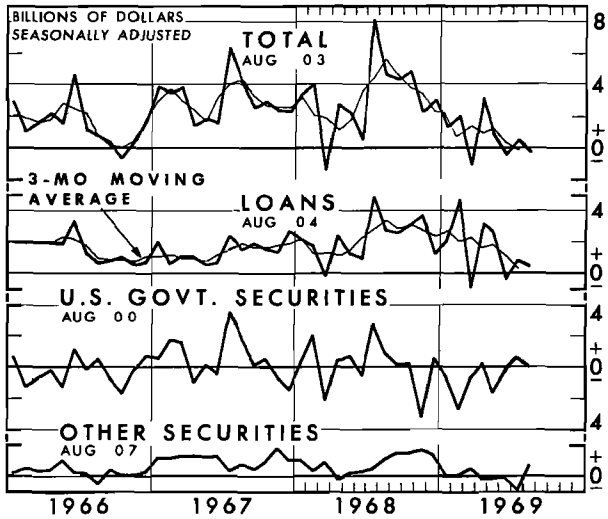
4/ National Income account translation estimated by Federal Reserve staff.

FINANCIAL DEVELOPMENTS - UNITED STATES

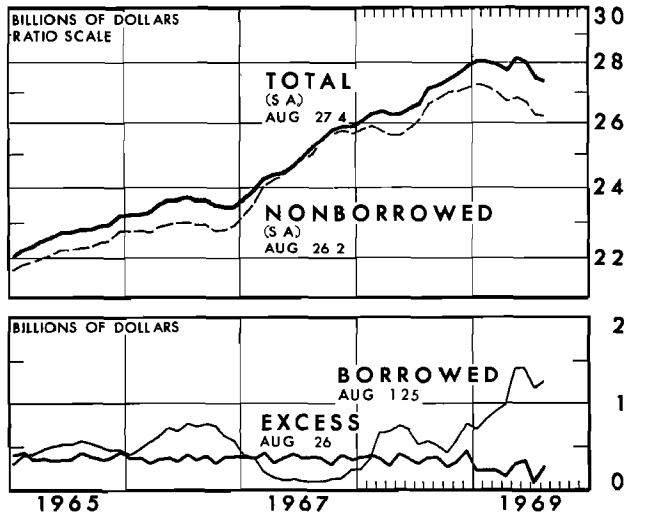
FREE RESERVES AND COSTS



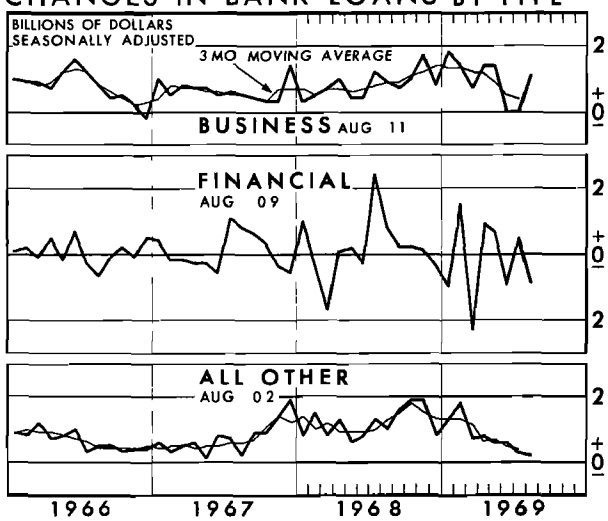
CHANGES IN BANK CREDIT



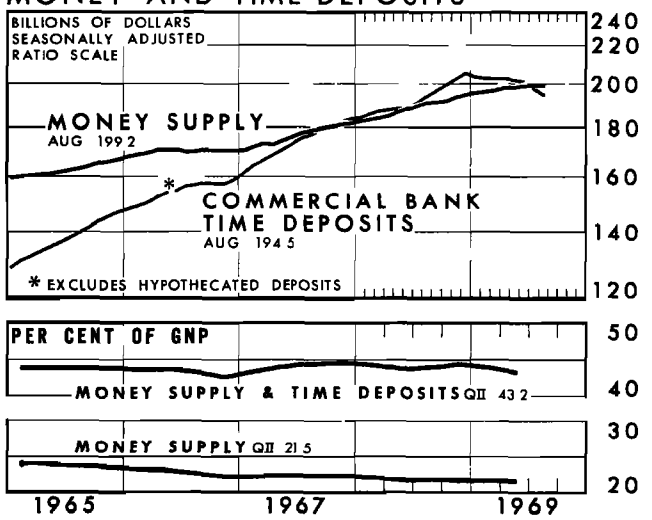
BANK RESERVES



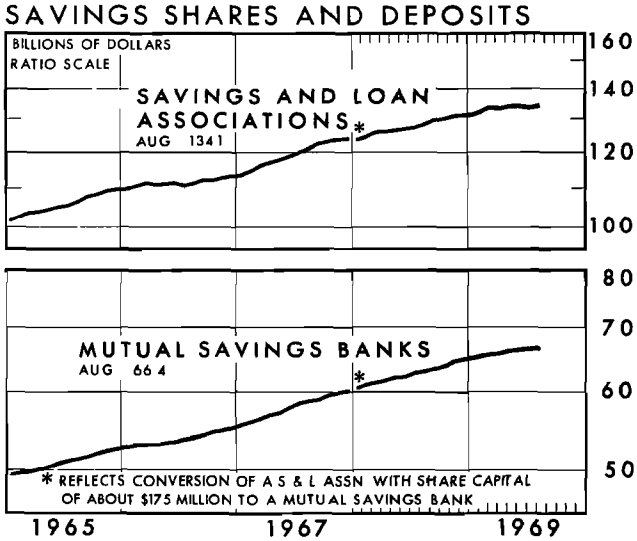
CHANGES IN BANK LOANS-BY TYPE



MONEY AND TIME DEPOSITS

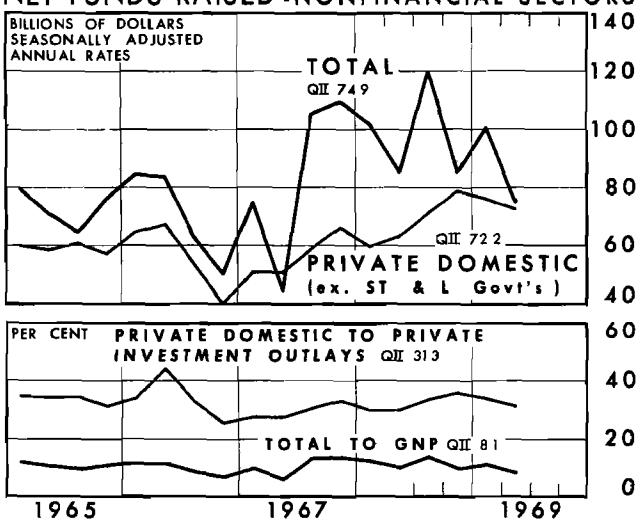


SAVINGS SHARES AND DEPOSITS

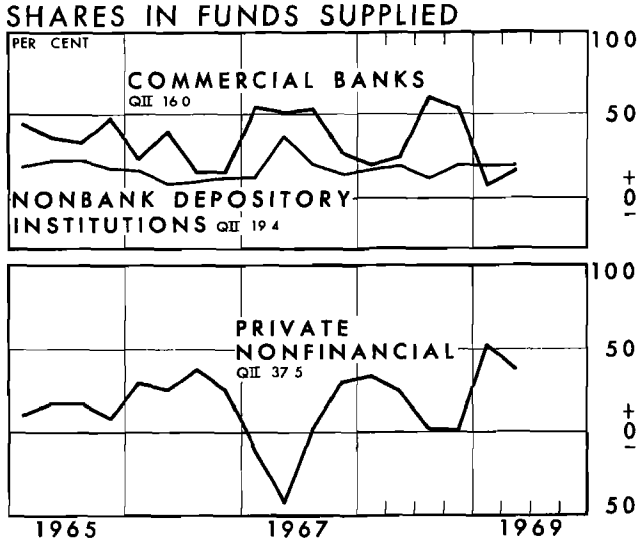


FINANCIAL DEVELOPMENTS - UNITED STATES

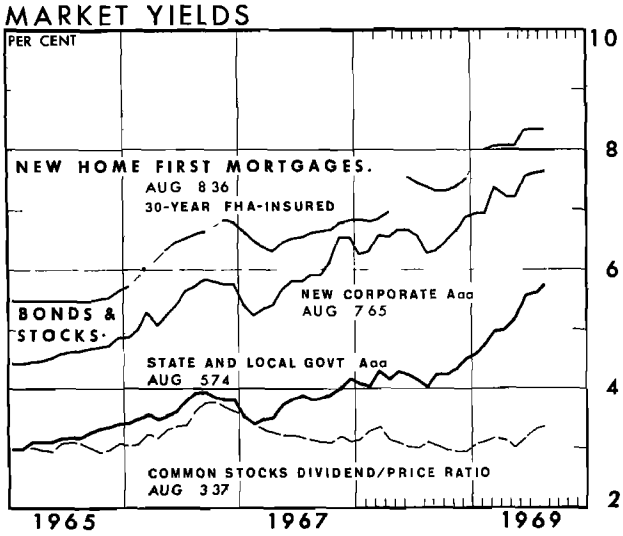
NET FUNDS RAISED - NONFINANCIAL SECTORS



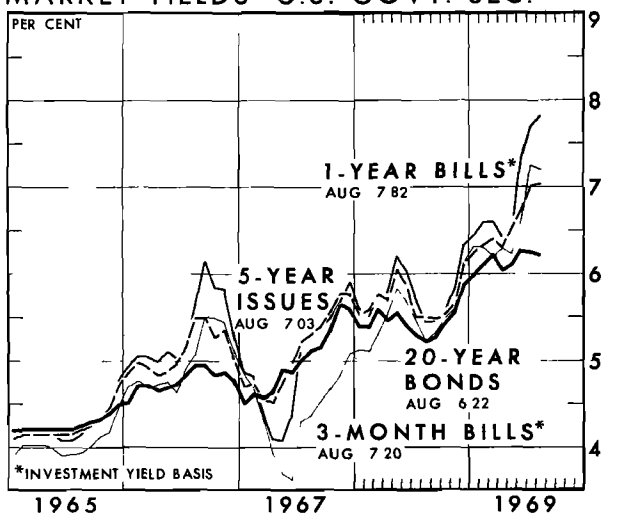
SHARES IN FUNDS SUPPLIED



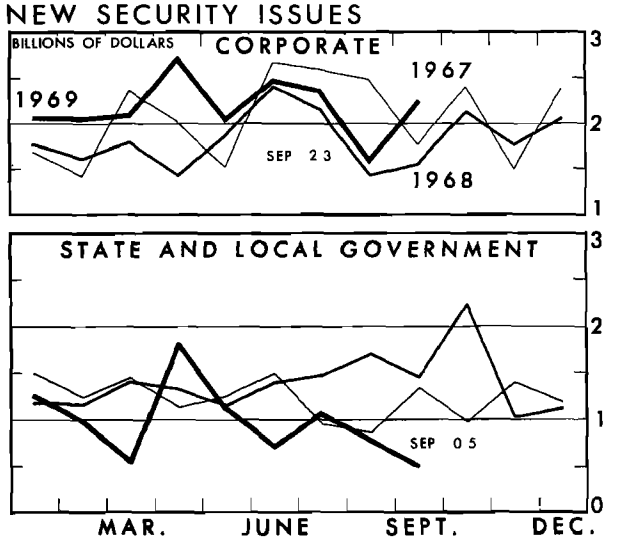
MARKET YIELDS



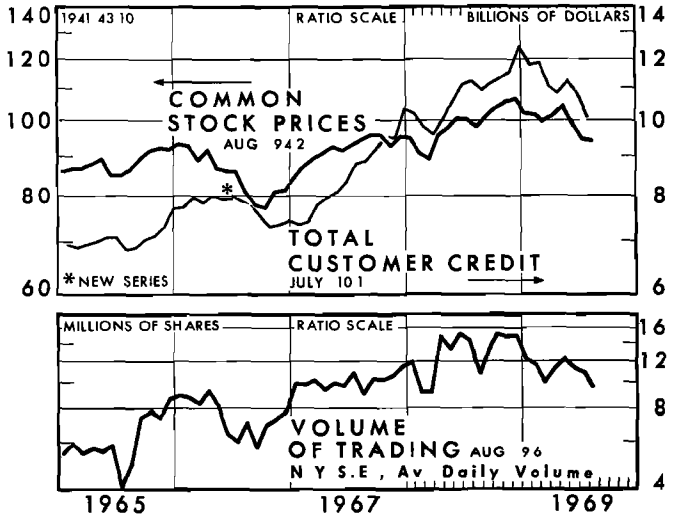
MARKET YIELDS—U.S. GOVT. SEC.



NEW SECURITY ISSUES



STOCK MARKET



THE ECONOMIC PICTURE IN DETAIL

International Developments

Foreign exchange markets. The major development in exchange markets during September was the build-up of speculation on a mark revaluation and finally the German government's decision to allow the mark exchange rate to "float" for a while, at least until a new government is formed. The large movement of funds into German marks, which tended to accelerate the week before the German elections, was halted when the Bundesbank stopped operating in exchange markets Thursday and Friday. (This suspension continued for most of the trading day Monday after the elections.) Between the beginning of September and the suspension of its exchange operations the Bundesbank purchased $1.4 billion spot. Its swap business -- new and maturing swap transactions -- resulted in net payments of about $230 million, so that Bundesbank reserves increased from these transactions a little less than $1.2 billion in September.

Trading in the mark on Tuesday, September 30 -- the first day of dealings under the new floating arrangement -- was orderly although the volume of trading was generally considered to be below its normal level. The exchange rate climbed to a peak of 26.10 cents/mark -- a little more than 4 per cent above the mark's current par value. Trading continued very orderly on Wednesday and the mark rate pushed to 26.43 cents/mark -- about 5.7 per cent above par.

The market for sterling was relatively firm during most of September although the pound did suffer in the week prior to the German elections from selling pressures, which abated after the Bundesbank's withdrawal from the market. The announcement of the favorable trade results for August at mid-month gave a short-lived boost to the demand for sterling. The Bank of England was able to purchase net $120 million during September. The market's more favorable view of sterling was also reflected in the substantial narrowing of the discount on forward sterling. The 3-month discount narrowed to 3.2 per cent per annum at the end of the month from about 9 per cent at the beginning of the month.

The Italian lira and French franc, in September, were under selling pressure which tended to get heavier toward the end of the month. The lira rate stayed at its lower limit most of the time and the Bank of Italy sold about $450 million during the month. The Bank of France lowered its support level for the franc several times during the month and held its losses to an estimated $150 million. At the end of the month the franc rate was at its lowest level since devaluation, 17.95 cents/franc compared with its lower limit of 17.87.

Demand for the Dutch guilder and Swiss franc was strong in September. The Swiss National Bank purchased about $300 million, which largely reflected the repatriation of dollars by Swiss commercial banks for quarter-end liquidity needs.

Euro-dollar market. After advancing steadily during August and the first few days of September, Euro-dollar interest rates peaked out, and subsequently declined moderately. For deposits with maturities from one month to one year the highs were about 11 to 11-1/2 per cent per annum. The three-month deposit rate declined to a low for the month of 10-5/8 per cent on September 24, and since then has advanced by about 5/8 per cent to around 11-1/4 per cent. Rates in most other maturities have increased since September 24 by 1/8 to 1/4 per cent.

U.S. bank takings of Euro-dollar funds through their branches increased fairly steadily from the end of August through the second week of September -- rising by about $600 million. These borrowings then declined by a roughly equal amount in the two weeks ending September 24. This easing of U.S. bank demand helps to explain the rate decline. Assuming that the usual month-end downward adjustment in these borrowings (often $300-$500 million) occurs in the last few days of September, there may be a sizable decline in U.S. banks' liabilities to branches for the month as a whole.

A variety of foreign developments may have influenced the Euro-dollar market in September. September saw another round of bank rate increases: the Belgian National Bank raised its discount rate by 1/2 per cent to 7-1/2 per cent -- its fifth discount rate increase this year; the Swiss National Bank raised its rate by 3/4 per cent to 3-3/4 per cent -- its first discount rate increase since July of 1967; the Bundesbank raised its rate by 1 per cent to 6 per cent -- the third

German discount rate increase this year; the Austrian National Bank raised its bank rate a full percentage point to 4-3/4 per cent; and the Bank of Norway raised its rate from 3-1/2 to 4-1/2 per cent. Thus major national money markets tightened further during September. Certain other foreign developments may help to explain the moderate easing of Euro-dollar rates during most of the month. Most notable were the sizable flows of speculative capital from the Italian lira and, perhaps to a lesser extent, from the French franc; a large part of these flows no doubt reflected demand for German marks but some may have gone into Euro-dollar deposits or to repay outstanding Euro-dollar loans. Furthermore, we understand that Japanese banks were reducing their borrowings of Euro-dollars during September and turning to lower cost (mainly yen) sources of financing. Finally, though the Bundesbank purchased a very large amount of dollars while holding the mark at its upper limit in September, its swap activities with German banks supplied about a $250 million net increase in forward cover potentially available for German bank placements in Euro-dollars.

SELECTED EURO-DOLLAR AND U.S. MONEY MARKET RATES
(weekly average of daily figures)

Average for week ending Wednesday	(1) Call Euro-$ Deposit	(2) Federal Funds	(3) =(1)-(2) Differ-ential	(4) 3-month Euro-$ Deposit	(5) 3-month Treasury Bill	(6) =(4)-(5) Differ-ential
Aug. 6	8.98	9.57	-0.59	10.25	6.99	3.26
13	9.88	9.18	0.70	10.55	7.04	3.51
20	9.66	8.79	0.87	10.83	6.86	3.97
27	9.13	8.82	0.31	10.91	7.04	3.87
Sept. 3	10.35	9.57	0.78	11.25	7.01	4.23
10	9.45	8.57	0.88	11.34	7.09	4.25
17	8.85	9.07	-0.22	11.14	7.11	4.03
24	9.00	9.61	-0.61	10.68	7.13	3.55
Oct. 1	10.00	9.25	0.75	11.08	7.07	4.01

U.S. balance of payments. The early and very partial data on balance of payments transactions in August and September show improvement in some sectors though the over-all results for the third quarter were still very poor. The merchandise trade accounts in August appear to have begun their hoped-for strengthening; foreigners returned to net purchases of U.S. equity securities during the month, and U.S. banks reduced their outstanding claims on foreigners, though by only a small amount.

On the liquidity basis the July and August deficits (with a rough allowance for adverse seasonality) were a little under $1 billion each. In September, unless there was a surge of outflows in the final week of the month (for which data are not available) related to DM speculation, the liquidity deficit was probably much lower. This would result in a quarterly deficit (seasonally adjusted) of somewhat less than $3 billion, compared to the $3.7 billion deficit of the second quarter. Moreover, of this more than $500 million is accounted for by negative "special" transactions in the third quarter, compared to around $360 million in the second.

In addition to the gain in the trade accounts (discussed below) the outflow of U.S. private capital was probably much smaller in the third quarter. Banking claims on foreigners were reduced by $375 million in July and August, indicating that even after allowance for the usual large seasonal inflow in the third quarter there was a major shift from the outflow of nearly $1/2 billion (seasonally adjusted) in the second quarter. Inflows were widely dispersed, with the largest

amounts reported for Europe, but there were outflows to Canada and a sizable loan was extended to Venezuela. Direct investment outflows can reasonably be expected to have been lower than the very large second-quarter rate, and to have contained a larger component of foreign-source funds -- i.e., U.S. corporations would be making more use of the proceeds of new issues previously sold abroad. U.S. investors purchased a much larger amount of new foreign bonds in the third quarter than in the second -- mainly Canadian issues -- but this change was offset (according to figures for July and August) by a shift from sizable net U.S. purchases to small net sales of foreign equity securities.

Following a net sell-off of $155 million in June-July, foreign investors purchased about $85 million of U.S. equity securities in August, despite the unsettled market and high Euro-dollar interest rates.

Since July there has been a marked change in the behavior of private foreign liquid claims on the United States. In July such claims increased by $1.3 billion, but the increase in August was only about $300 million, and in September the change was probably not significant either way. The largest component of these changes in claims is borrowings by U.S. banks from their foreign branches; such borrowings advanced by almost $900 million in July, but by only about $300 million in August, and there probably was some net repayment in September.

As a result of the declining inflows of private foreign short-term funds the balance on official settlements shifted to a deficit of $650 million in August, and showed a deficit of roughly $500 million for September, through the 24th. Thus, the third quarter official settlements balance was a deficit probably approaching $1 billion (the seasonal element on this basis is minor).

U.S. foreign trade. The export surplus increased in August as exports rose more than imports. For July-August combined, the trade balance (balance of payments basis) was in surplus by about $3/4 billion at an annual rate, still low, but a marked improvement over the small deficit recorded in the first half of the year, and slightly above the $1/2 billion annual rate in the second half of 1968. Both exports and imports in July-August were up sharply over the January-June rates; exports by 12 per cent and imports by 9 per cent. How much of the improvement in the trade balance and the acceleration in trade movements in July-August is an aftermath of the dock strike and how much represents the beginning of the long awaited improvement in our basic trade position is still difficult to determine.

Exports of both agricultural and nonagricultural commodities advanced in July-August. The value of shipments of agricultural products was well above the strike-depressed rate of the first half, and about equal to the rate in the second half of 1968. July agricultural exports were very strong, possibly reflecting the reopening of West Gulf ports (through which about 25 per cent of agricultural exports move) which

occurred in April, about 6 weeks later than for other ports. August agricultural shipments, however, were again down sharply. The effects of price-cutting in wheat are not yet discernible in the August trade figures. These lower wheat prices -- 15 to 20 per cent below the minimum stipulated by the International Grains Arrangement -- may reduce exports by $100 million in the current crop year ending June 1970.

In contrast, shipments in nonagricultural commodities advanced sharply in August, the first real rise since March, when most Atlantic coast ports were in full operation for the first time following the ending of the strike.

For July-August together, exports of nonagricultural products were considerably greater than in the first half of this year and the last half of 1968. Machinery and chemicals rose very sharply, while shipments of steel -- mainly to Europe but also to Latin America and Canada -- expanded at an even faster rate. Shipments of automotive vehicles and parts to Canada fell, possibly reflecting the earlier than usual changeover to production of 1970 models. Deliveries of commercial aircraft, which had dipped in the first half, were about unchanged in July-August.

By areas, total exports to all major markets, except Canada, were substantially higher in July-August than in the first six months of the year. Particularly encouraging was the strong upturn in sales to Western Europe, which had slumped badly in January-June. Shipments to Japan, already at a high rate, advanced further while exports to the

less-developed countries, particularly Latin America, also increased. The drop in shipments to Canada reflected lower deliveries of automotive vehicles and parts; exports of other commodities to Canada showed little change from that of the first half.

The import expansion in July-August appears to have been more broadly-based than in the small advance from the second half of 1968 to the first half of this year. Purchases of foreign nonfood consumer goods other than automobiles, and of foreign machinery, which had increased in the first half over those in the preceding half-year despite the strike, were at a considerably higher rate in July-August than in the first half. Imports of foodstuffs and industrial materials, which in the first half of the year had fallen below the rates in the second half of 1968, also rose in July-August. Imports of iron and steel, particularly from Europe, increased sharply from their low levels in the first half of the year. Imports of other materials associated with manufacturing of durable goods were also much larger. Partially offsetting these gains in July-August was a sizable decline in the value of imports of building materials, reflecting lower prices for lumber and an easing in demand as housing starts here declined from the very high rate in the first part of this year.

Arrivals of automobiles increased in July-August over those of the first half. The recent expansion was in cars from Europe and Japan whereas the growth in the first half of the year over the last six months of 1968 was entirely in automobiles from Canada.

Reserve changes and the Euro-dollar market. An inference that central banks have become direct suppliers of funds on a considerable scale to the Euro-dollar market may be drawn from available data on official reserve positions. A large discrepancy exists between the aggregate increase in reserve assets other than gold and the aggregate increase in reserve liabilities reflected in the data of the table below.

During the year and a half through mid-1969, when the U.S. balance of payments on the official settlements basis showed a $4.6 billion surplus, U.S. liabilities to foreign official reserve holders fell by $3.3 billion while U.S. official holdings of other currencies rose by $1.0 billion. Meanwhile the U.S. reserve position in the IMF increased by somewhat more than the amount ($0.9 billion) by which U.S. gold reserves declined.

CHANGES IN NET OFFICIAL RESERVES
(in billions of dollars)

	1967	1st 3 Q's 1968	1968 Q-4 & 1969 Q-1	1969 Q-2
U.S. 1/	-3.4	1.7	1.6	1.2
U.K. & France 2/	-.3	-5.7	-.5	-1.0
Other Group of Ten 2/ 3/	1.0	.8	-1.0	1.8
Other Developed Countries 4/	-.2	1.0	.5	-.2
LDC's 4/	.8	.3	.8	.2
Total net change	-2.2	-1.4	1.5	2.0
Official gold	-1.6	-.9	.3	-.1
Discrepancy	-.6	-.5	1.2	2.1

1/ Official reserves transactions balance, not seasonally adjusted.
2/ Confidential BIS data.
3/ Switzerland is included.
4/ Gross reserves (IFS) and IMF credit tranche position.

During this period Britain and France suffered net drains of net official reserves (assets less liabilities) exceeding $7 billion. Substantial gains in net official reserves occurred for many other countries. In the aggregate, net reserve gains of the United States and others (as reflected in the table) exceeded net reserve losses by a large amount. In 1967 there had been a negative discrepancy, and this continued through the first three quarters of 1968. For the next three quarters, over $3 billion of the increase in world gross reserves (other than gold) is not matched by known changes in official liabilities, and the discrepancy becomes especially large for the second quarter of 1969.

Reasons for the discrepancy are under study. Some considerable part may reflect statistical difficulties. Some part can probably be ascribed to "recycling" actions and increased holdings by some European central banks at the BIS, while that institution increased its Euro-dollar investments (claims against commercial banks rather than central banks). In addition it seems possible that high Euro-dollar interest rates have attracted investments directly from some central banks. The success of U.S. banks in expanding their borrowings from their foreign branches by more than $6-1/2 billion between September 30 of last year and June 30, 1969, is to be explained, it seems, not only by massive shifts by foreign commerical banks and nonbank investors out of other currencies into Euro-dollars, and by a considerable movement (of uncertain size) on the part of U.S. investors, but also by some redirection of foreign official reserve accruals into Euro-dollar deposits.

Reserves and balance of payments of other industrial countries

Reserve movements in industrial countries outside the U.S. were quite large in the second and third quarters, reflecting continuing disequilibria in basic balances of payments and the speculative capital flows associated with the lack of adjustment.

The current account surpluses of Germany, Italy and Japan continued to be large, but of the three only Germany showed large gains in official reserves. Intense speculation on a revaluation of the German mark in late April and early May led to a second quarter increase in German official reserves of $1.9 billion. After a summer lull, speculation in the mark again became heavy with the approach of the German elections. The Bundesbank suspended operation in German exchange markets September 25-26 because of the heavy inflow of dollars, and on September 29 the decision was made to temporarily allow the mark to float. Domestic political uncertainty and speculation on a DM revaluation led to huge capital outflows from Italy, and only the forced reduction of commercial bank net foreign positions prevented official reserves from declining sharply in the second quarter. Japanese official reserves declined as a result of a switch to yen financing of international transactions by Japanese banks in the second quarter.

For France, continuing large balance of payments deficits and official reserve losses ($1.2 billion in the second quarter) culminated in a devaluation of the franc on August 8. Immediately after devaluation,

the Bank of France had significant reserve gains, but domestic labor unrest and the revival of DM speculation in September led to renewed French losses.

Britain's net reserve gains--which took the form mainly of repayments of official assistance--were substantial in the first quarter. There were further gains in the second quarter when there was a surplus on the basic balance of payments, but as a result of DM speculation the reserve gains were smaller than in the first quarter. Greatly improved trade figures for August led to some reserve gains in mid-September, but renewed speculation in marks led to some reserve losses in the week before the German elections.

Taken together, the members of the Group of Ten other than the United States but including Switzerland had a combined balance of payments deficit on non-monetary transactions of $1.2 billion in the

COMBINED OFFICIAL AND COMMERCIAL
BANK NET EXTERNAL MONETARY POSITIONS
(millions of dollars)

	Net position as of Dec. 1968	Changes in net position, 1969		
		I	II	July
Germany	10,566	-635	1,841	-318
France	3,208	-559	-1,216	n.a.
Italy	6,275	-357	- 515	+ 15
Belgium	1,722	- 50	100	n.a.
Netherlands	2,361	89	- 112	- 73
United Kingdom	-10,003	497	304	469
Switzerland	4,995	-327	511	n.a.
Sweden	1,074	-132	- 150	3
Japan	2,072	278	637	120
Canada	3,801	23	235	n.a.

Source: Confidential BIS data.

first quarter of 1969. In the second quarter the position changed to a surplus amounting to $1.6 billion. Within the Common Market, the second-quarter surplus of Germany was almost fully offset by the French and Italian deficits but among the others, Japan, Switzerland, Britain and Canada all had surpluses in the second quarter. (Balances calculated on this basis include not only the current account and long-term capital, but also any short-term capital movements that do not take the form of a change in the country's commercial banks' external assets or liabilities. Thus some, but not all, of the speculative movements into marks are counted in the German surplus on this basis.)

The overall German balance of payments deficit of $635 million in the first quarter was, predictably, only a temporary phenomenon. In the second quarter speculation on a mark revaluation together with more fundamental factors combined to produce a surplus of over $1.8 billion. The third quarter will undoubtedly also show a huge surplus.

Heavy speculative flows in May and again in September were a major factor in throwing the balance of payments from deficit into substantial surplus. But there also was a more important reversion to a larger basic payments position: the trade surplus, which in the first quarter had been adversely affected by German tax measures that induced a bulge in exports at the end of 1968, and by strikes abroad, was not reduced by cyclical factors, and increased substantially in subsequent months. Currently, at the height of the boom, it is at about the same level ($4 billion, annual rate) as in the recession year 1967.

NET EXTERNAL MONETARY POSITIONS OF
OFFICIAL INSTITUTIONS AND COMMERCIAL BANKS
(millions of dollars)

		Net position as of Dec. 1968	Changes in net positions, 1969			
			I	II	July	Aug.
Germany:	Official	10,331	-1,814	1,932	--	508
	Banks	235	1,179	- 91	-318	n.a.
France:	Official	3,269	185	-1,218	-115	119
	Banks	- 61	- 744	2	n.a.	n.a.
Italy:	Official	5,538	- 381	16	60	- 31
	Banks	737	24	- 531	- 45	+ 68
Belgium:	Official	2,458	- 106	82	30	-174
	Banks	- 736	56	18	32	n.a.
Netherlands:	Official	2,449	- 58	- 127	- 47	44
	Banks	- 88	147	15	- 26	n.a.
U.K.:	Official	-9,380	454	195	355	-400[e]
	Banks	- 623	43	109	114	n.a.
Switzerland:	Official	4,485	- 778	215	-280	13
	Banks	510	451	296	n.a.	n.a.
Sweden:	Official	800	- 68	- 165	- 37	33
	Banks	274	- 64	15	40	n.a.
Japan:	Official	2,861	319	- 94	- 82	117
	Banks	- 789	- 41	731	202	n.a.
Canada:	Official	2,843	- 38	- 45	- 24	34
	Banks	958	61	280	n.a.	n.a.
Total EEC:	Official	24,045	-2,174	685	- 72	466
	Banks	87	662	- 587	n.a.	n.a.
Other:	Official	1,609	- 111	106	- 68	-203
	Banks	300	450	1,431	n.a.	n.a.

e - Estimated.
Source: Confidential BIS data.

In addition, net long-term capital outflows, $1.5 billion in the first quarter, fell to $1 billion in the second quarter. The basic deficit of $1.1 billion in the first quarter was thus reduced to $0.4 billion in the second.

That the basic balance was still in deficit in the second quarter is misleading, however, since a large part of the long-term capital export was financed by the huge inflow of non-bank short-term capital ($2-1/4 billion in the second quarter). The Bundesbank, in its August report, points out that the present level of long-term capital export (roughly $4 billion, annual rate) would not be sustainable solely from domestic savings. Nor would domestic savings sustain a rate of capital export sufficient to offset the current account surplus, now running at an annual rate of about $2.5 billion.

Despite various measures taken by the Bundesbank to hold down net short-term capital inflows, including encouraging banks to place funds in the Euro-dollar market through the use of preferential dollar-mark swap rates, net official reserves increased $500 million in August on top of a $1.9 billion gain in the second quarter. Before the Bundesbank ceased support operations on September 25, the central bank had intervention gains of about $1.4 billion for the month. The September 29 decision to let the mark float temporarily, and the consequent upward movement of the price of the mark should substantially reduce the short-term capital inflow as well as cut into the large current account surplus.

During the second quarter and in July and August, Italy's balance of payments continued to show a severe deterioration from the previous year because of increased capital outflows. For the first eight months of the year, Italy incurred an overall deficit of $826 million this year as against a surplus of $454 million last year. In September to date, there has been a large reduction in official reserves that has probably reflected, in addition to underlying factors, renewed speculation on a mark revaluation by Italian traders and investors. The prospect now is for a large deficit in 1969 in excess of $1 billion.

The current account has remained strong; the January-July current account surplus of $951 million was nearly identical with that of a year earlier. The net capital outflow over the first seven months, however, increased to $1,820 million compared with $769 million a year earlier. The outflow has become larger in recent months and was slightly in excess of $300 million in both June and July. The higher capital outflow reflects anxiety among business and investors, created by political uncertainty and fears of student and labor unrest, as well as the much higher rates of interest prevailing in foreign financial markets.

The reduction of Italian commercial banks' net foreign assets by $531 million in the second quarter--which kept the decline in official reserves to negligible dimensions--was in response to the directive given the banks at the end of March that by end-June they repatriate a sum equal to their net foreign assets on March 31. Later, some exceptions were granted which allowed $230 million of net foreign assets to be

outstanding on June 30. In June, foreign depositors withdrew funds from lira bank accounts, and further withdrawals have since occurred, presumably in reflection of some nervousness about the lira. Banks' net foreign assets rose by $23 million in July-August.

In Japan, the balance of payments as a whole remained in heavy surplus through August. In July-August, the current account surplus was $475 million, compared with $279 million in the same period a year earlier.

In recent months, however, export growth has slackened and import growth has accelerated. This has narrowed the seasonally adjusted trade surplus substantially. From a peak of $178 million in March this year, the seasonally adjusted trade surplus (imports c.i.f.) has declined steadily, and in August there was a $7 million deficit on trade account. With the recent tightening of monetary policy on September 1, however, this deteriorating trend may be arrested.

Through March of this year, the balance of payments surpluses were reflected in large gains in official reserves. In the year ending March 1969, official reserves increased $1-1/4 billion to reach $3,213 million. During the April-July period, however, official reserves declined as the foreign exchange banks repaid substantial amounts of their short-term indebtedness and sharply improved their net foreign exchange position. During the second quarter alone, the foreign exchange banks reduced their net foreign indebtedness from $830 million to $99 million. This reflected a shift from foreign currency financing to yen financing of Japanese

business--a shift induced by much higher foreign interest rates, and permitted by the Japanese authorities in view of Japan's strong payments position.

The overall balance of payments surpluses are likely to continue in the coming months; however, somewhat smaller surpluses appear likely.

In France, a huge current account deficit and an adverse movement of leads and lags combined to produce an overall deficit of $1.2 billion in the second quarter, and eventually led to the devaluation of the franc on August 8. Moderate reserve gains in August, after devaluation, were probably a result of some reversal in leads and lags. It is most improbable that any other capital inflows occurred, since exchange controls are still in force and constitute a very strong deterrent against capital return.

The current account, seasonally adjusted, was in deficit by about $1.9 billion annual rate in the first eight months, and little improvement is expected before year-end. With a current account deficit at this rate, it is expected that French reserve losses will continue in coming months. It is also extremely doubtful that France can achieve her target of current account balance by mid-1970.

The combination of renewed speculation on a mark revaluation, and the generally poor reception of the austerity program and the attendant labor unrest in France may have again shifted leads and lags adversely.

In the two weeks prior to the German elections the Bank of France had intervention losses of some $130 million. On September 26, the French drew $500 from the IMF to repay some outstanding short-term assistance from other central banks.

The British basic balance of payments (current account and long-term capital) registered a surplus of $456 million in the second quarter, a marked improvement over the $187 million deficit in the previous quarter. On a seasonally adjusted basis, the improvement was smaller, but still substantial--a deficit of $124 million in the first quarter gave way to a surplus of $240 million in the second.

While part of the swing in the seasonally adjusted balance arose from a $144 million reduction in the trade deficit, the bulk of the improvement stemmed from a $228 million increase in net long-term capital inflow, an account which typically shows very erratic quarterly movements. Much of the long-term capital inflow was accounted for by a $75 million borrowing in Germany by the U.K. Gas Council and by heavy foreign purchases of British Petroleum Company equities in connection with BP's participation in Alaskan oil development.

Movements in net official reserves and commercial banks' net position have deviated from changes in the basic balance, because there have been large short-term capital flows other than those through the banks. Receipts under the import deposit system were significantly reduced in the second quarter, and there was a large reversal of leads

and lags against Britain, undoubtedly connected with speculation on a mark revaluation and the uncertainty over the viability of the current parity of the pound. The net position of commercial banks in the U.K., including branches of U.S. banks, increased by only $109 million in the second quarter as both foreign assets and foreign liabilities increased by nearly $6 billion.

After increasing by $454 million in the first quarter, net official reserves increased by only $195 million in the second quarter. A sharp increase in July was followed by an even larger decline in August as speculative capital outflows resumed in the wake of the franc devaluation. Following the publication of very favorable August trade results ($115 million surplus), the Bank of England had significant intervention gains until the week preceding the German elections, at which time it incurred small losses.

Though the trade surplus diminished, Canada's overall balance of payments was in surplus by $235 million in the second quarter, as long-term capital inflow continued strong. The unadjusted trade surplus for the first eight months of the year was $410 million less than for the same period a year ago, as exports rose at a much slower rate than imports. For the year as a whole, the trade surplus will probably be less than half of last year's $1.1 billion.

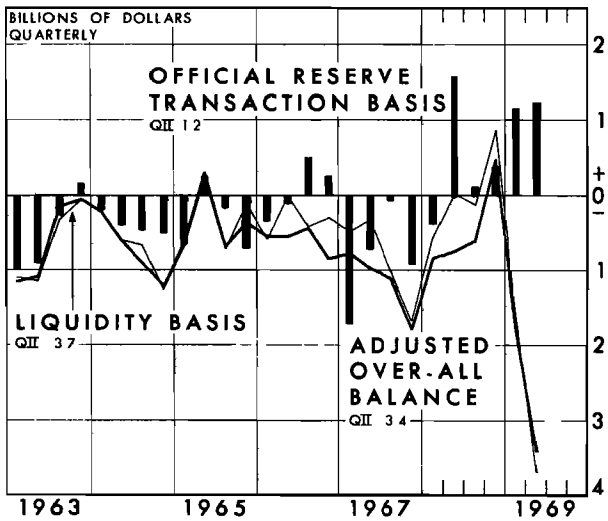
Official net reserves fell by $45 million in the second quarter, but the net foreign position of Canadian banks increased by $280 million as they sharply increased their lending to New York banks with funds

raised from "swapped" deposits by Canadian residents. The banking capital outflow apparently has slowed considerably since mid-July when the Bank of Canada imposed a temporary ceiling on swapped deposits of the banks and further tightened domestic money market conditions.

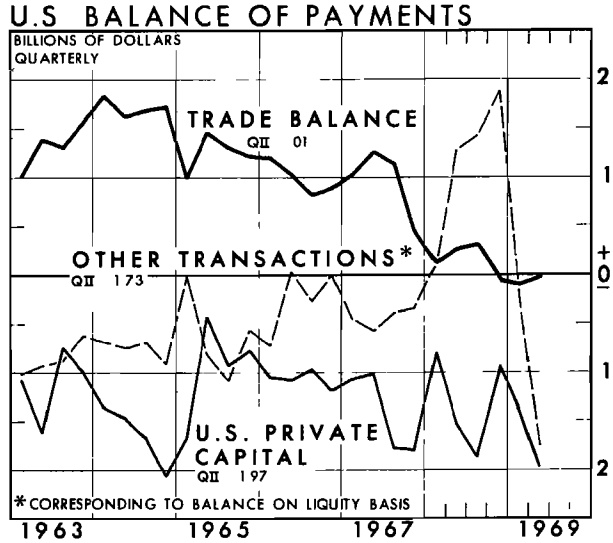
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED

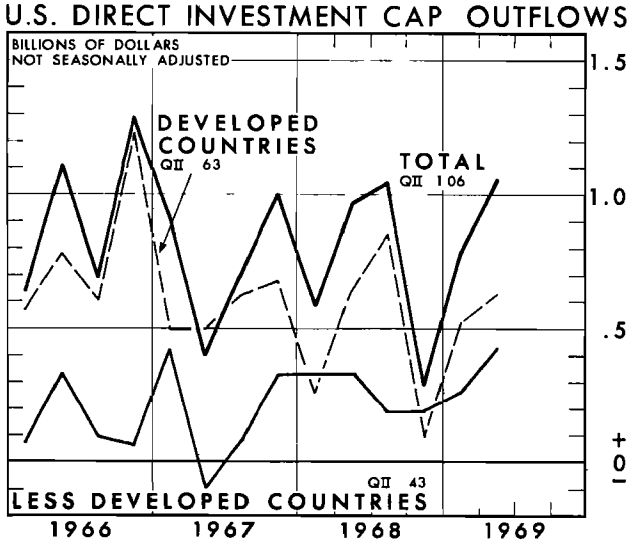
U S BALANCE OF PAYMENTS



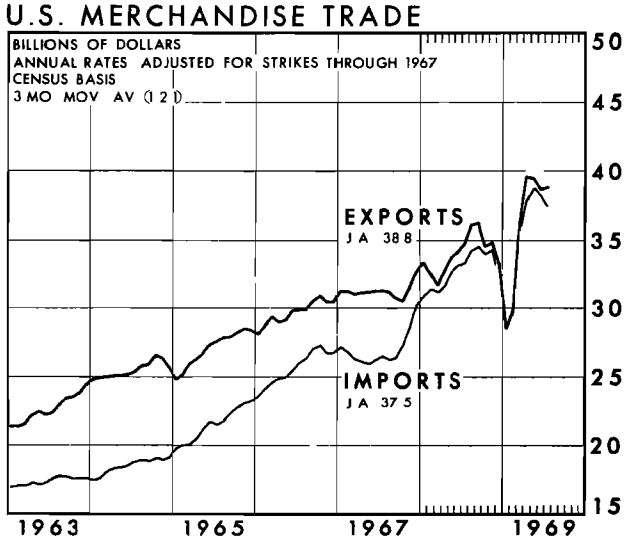
U.S BALANCE OF PAYMENTS



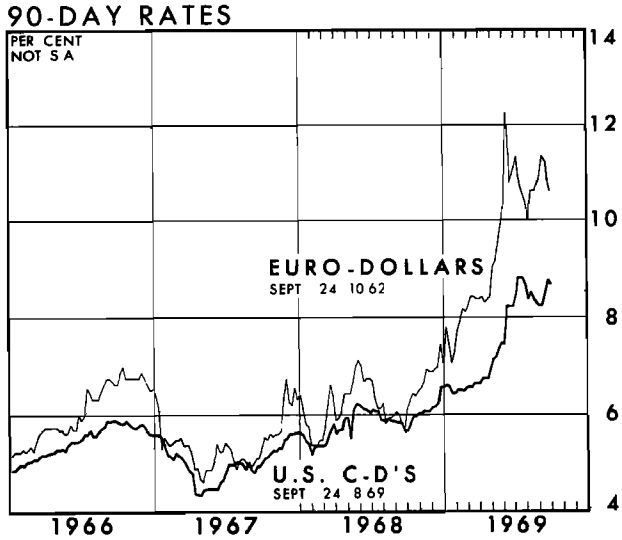
U.S. DIRECT INVESTMENT CAP OUTFLOWS



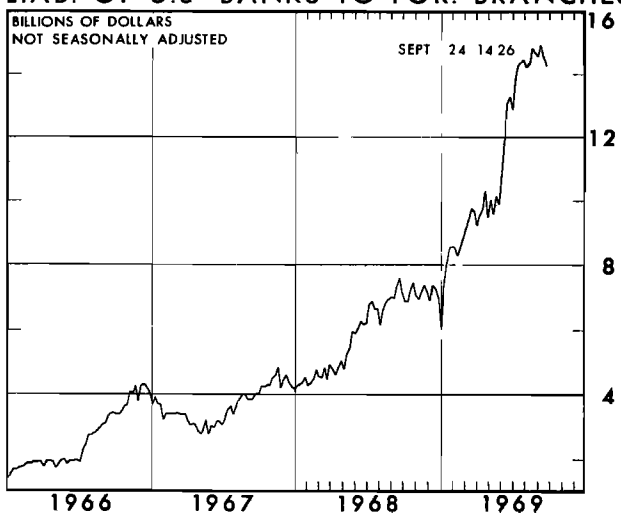
U.S. MERCHANDISE TRADE



90-DAY RATES



LIAB. OF U.S BANKS TO FOR. BRANCHES



APPENDIX A: REVISION OF MONEY SUPPLY AND COMMERCIAL BANK TIME DEPOSITS ADJUSTED*

Annual benchmark and seasonal factor revisions were published September 25 with the regular money supply release. As explained below, the benchmark corrections raised the levels of both money supply and time deposits in 1968 and 1969, and seasonal factor changes smoothed the series over a somewhat longer period. In addition to publication of revised data from 1967 to date, data for earlier periods will be published in the October Bulletin, including some minor seasonal changes for other recent years.

The accompanying charts and tables compare the revised data with the series published before and after the August correction for downward bias connected with Euro-dollar float. As may be seen on the charts, the Euro-dollar float revision in August accounted for most of the change in level of the money supply, with the benchmark revision adding another 1/2 percentage point to the growth rate for the first half of 1969. The revised series still indicates noticeably slower expansion after April. Slower expansion in recent months is most evident in the weekly series (chart 2), which has shown little change since mid-May following wide fluctuations in April.

The decline in time deposits is now estimated at a 4 per cent annual rate in the first half of 1969, about 1 percentage point less than before the revisions. Since June, the rate of contraction in the revised series is at a 19 per cent average annual rate, about 1 percentage point greater than estimated earlier. Additional information on the various adjustments is provided below.

Euro-dollar float adjustment (published in August)

To briefly recap the general effects of the Euro-dollar float adjustment: the money supply level was increased in 1969 by amounts ranging from $1.8 billion in January to $3.3 billion in July, with a sharp spurt in the amount of correction occurring in the second quarter. Levels were increased by smaller amounts prior to 1969 beginning with data for June 1967. Annual growth rates were increased by 0.2 percentage points over the year 1967, by 1/2 percentage point over 1968, and by 1-1/2 percentage points over the first half of 1969.

Benchmark corrections

The table below indicates the amounts of change in currently published levels of money supply and time deposits for the three benchmark dates that are being incorporated in this revision. Effects of benchmarks on semiannual changes in the series would be reflected in differences between benchmarks for succeeding dates--e.g., $400 million additional growth in money supply in the first half of 1969 due to benchmark corrections, $800 million additional growth in nonmember time deposits.

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* Prepared by Edward Fry, Darwin Beck, and Frances Weaver, Banking Section, Division of Research and Statistics.

CHANGES FROM PUBLISHED LEVELS
(In billions of dollars)

	Benchmark dates		
	June 30, 1968	Dec. 31, 1968	June 30, 1969
Total money supply	+ 0.2	+ 0.4	+ 0.8
Demand deposit component	+ 0.3	+ 0.4	+ 0.9
Nonmember demand adjusted	(+ 0.3)	(+ 0.3)	(+ 0.8)
Nonmember due to foreign and mutual savings banks	(1/)	(+ 0.1)	(1/)
Nonweekly reporting member due to foreign, mutual and banks in territories and possessions	(1/)	(1/)	(+ 0.1)
Currency component	- 0.1	1/	- 0.1
Nonmember vault cash	(+ 0.1)	(1/)	(+ 0.1)
Time deposits adjusted (nonmember time & savings)	+ 0.3	+ 0.6	+ 1.4

1/ Less than $50 million.

Implications of benchmarks for current estimates

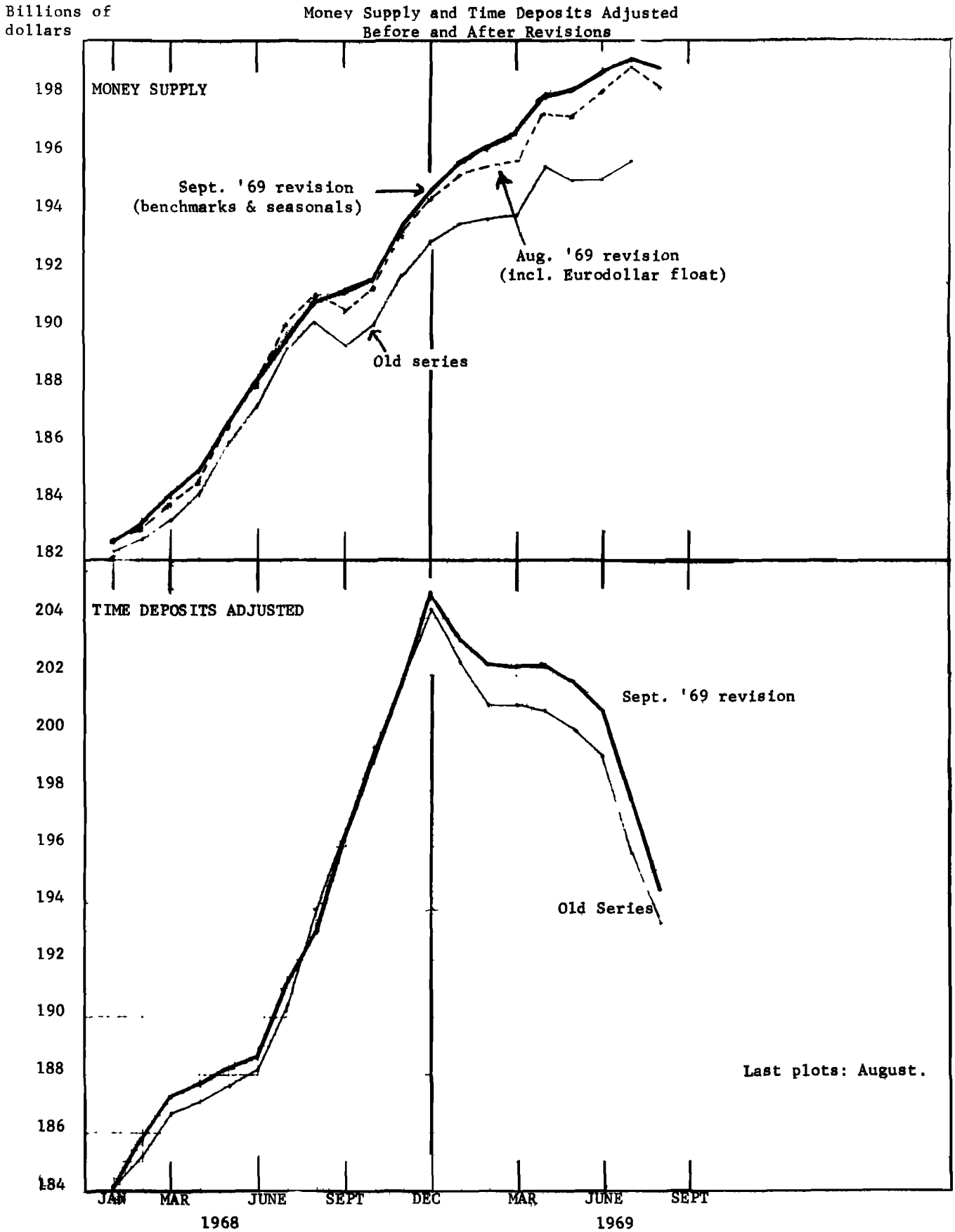
These benchmark corrections were relatively large by past standards, suggesting a change in the behavior of nonmember deposits in relation to country member bank deposits from which the nonmember estimates are derived. Changes in banking structure do not account for the major part of the estimating error; indeed, the cumulative effects of bank structure changes on the estimates were insignificant in relation to the total benchmark corrections. The explanation for the abnormal behavior of nonmember/country growth rates seems to be that country bank deposit growth was restricted relative to nonmembers in the first half of 1969 due to differences in depositor characteristics. With a greater concentration of fairly large urban banks in the country group, the interest-sensitivity of depositors in country banks probably is greater than for nonmembers. This explanation would seem consistent with the relative size of benchmark corrections for time and demand deposits as well as with the abnormally faster total deposit growth of nonmembers relative to country banks.

In view of the continuation of monetary restraint since June, it would seem that estimated changes in nonmember deposits probably were understated during the third quarter before the revision. The revised data include increased allowances for nonmember growth relative to the country bank data on which current estimates are based. Such allowances will be carried forward also as estimates are made in the fourth quarter in order to reduce the likelihood of further upward revision when December benchmarks become available.

Seasonal factor revisions

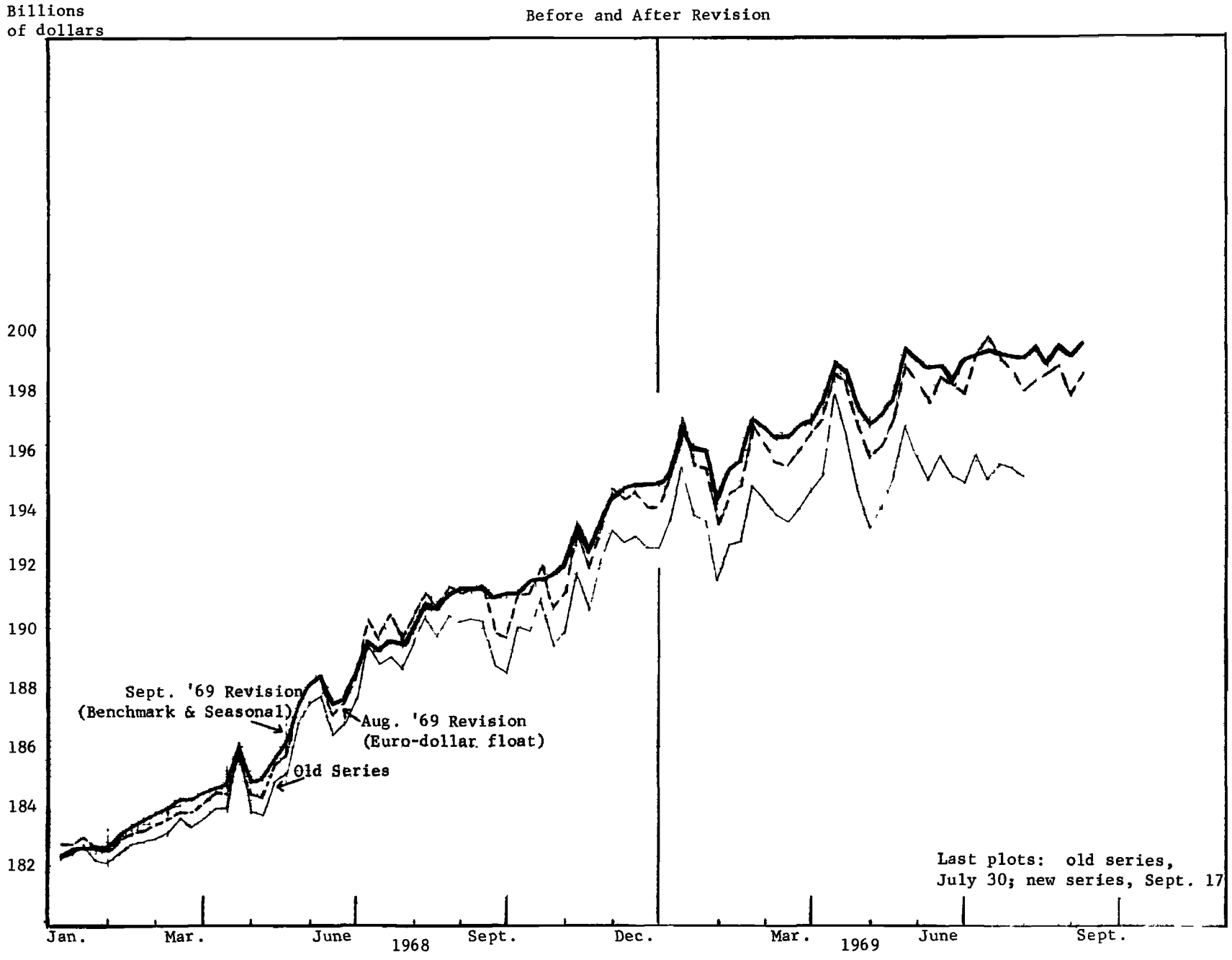
Seasonal factor revisions affect the series mainly in the period from 1967 to date, with the principal changes in the demand deposit component of money supply. Seasonal factors for July, August, and November have been raised and those for March, April, and September lowered. The result of these changes is to smooth out the monthly and quarterly pattern of change in demand deposits and the money supply, with the first and second quarters now showing similar growth rates in 1969. These changes also reduce the tendency for the seasonally adjusted money supply figures to show large increases in July and August.

Time deposits seasonal factors have been lowered slightly over the months from February through July, raising the level of the series in these months, and factors for the August through November period have been raised with opposite effects on seasonally adjusted levels.


Billions of dollars
Money Supply and Time Deposits Adjusted
Before and After Revisions
MONEY SUPPLY
198
196
194
192
190
188
186
184
182
Sept. '69 revision
(benchmarks & seasonals)
Aug. '69 revision
(incl. Eurodollar float)
Old series
TIME DEPOSITS ADJUSTED
204
202
200
198
196
194
192
190
188
186
184
Sept. '69 revision
Old Series
Last plots: August.
JAN
MAR
JUNE
SEPT
DEC
MAR
JUNE
SEPT
1968
1969

Money Supply

Before and After Revision



MONEY SUPPLY--CHANGES BEFORE AND AFTER
1969 REVISIONS

	Seasonally adjusted annual rates of change, in %		
		1969 Revisions	
Monthly:	Old series	August (corrected for Euro-dollar float)	September (benchmark and seasonal factor corrections)
	(1)	(2)	(3)
1968--January	6.6	6.6	5.9
February	2.6	2.6	4.6
March	4.6	5.2	5.9
April	5.9	5.2	5.9
May	11.7	13.0	11.0
June	8.4	9.0	9.0
July	12.8	13.4	8.9
August	5.7	6.3	8.9
September	- 5.0	- 3.8	2.5
October	4.4	5.7	2.5
November	10.7	11.3	11.3
December	7.5	7.4	7.4
1969--January	3.7	5.6	6.2
February	0.6	1.8	3.1
March	1.2	1.2	3.1
April	10.5	9.8	7.9
May	- 3.1	- 0.6	1.2
June	--	4.9	4.2
July	3.7	5.4	2.4
August		- 4.8	- 1.8
Quarterly--based on averages of daily figures for last month of each quarter.			
1968--I	4.6	4.8	5.5
II	8.7	9.1	8.7
III	4.5	5.3	6.8
IV	7.6	8.2	7.1
1969--I	1.9	2.9	4.1
II	2.5	4.7	4.5
July-August		0.3	0.3

TIME DEPOSITS ADJUSTED--CHANGES BEFORE AND AFTER 1969 REVISION

	Seasonally adjusted annual rates of change, in %	
Monthly:	Old series	1969 revision (benchmark and seasonal factor corrections)
	(1)	(2)
1968--January	3.9	2.6
February	7.2	11.1
March	9.7	9.0
April	2.6	3.2
May	3.2	3.2
June	3.8	2.6
July	14.0	15.9
August	21.4	17.0
September	17.3	16.1
October	17.7	18.3
November	14.4	16.2
December	14.3	16.6
1969--January	-10.6	-10.0
February	- 8.9	- 4.7
March	--	- 0.6
April	- 1.2	--
May	- 4.2	- 3.6
June	- 5.4	- 5.4
July	-20.5	-18.5
August	-15.3	-19.4
Quarterly--based on averages of daily figures for last month of each quarter.		
1968--I	7.0	7.6
II	3.2	3.0
III	17.9	16.5
IV	15.7	17.3
1969--I	- 6.5	- 5.1
II	- 3.6	- 3.0
July-August	-17.8	-18.8

APPENDIX B: SUMMER BUDGET REVIEW

The Summer Budget Review, released by the Bureau of the Budget on September 17, indicates no change in the earlier estimate of total outlays for fiscal 1970. The Administration's current forecast of receipts, $198.8 billion, is $.4 billion less than its May 20 estimate, but above the $196.6 billion in receipts presently being projected by the Board Staff for fiscal 1970.

UNIFIED BUDGET RECEIPTS & OUTLAYS
(Billions of dollars)

	Fiscal 1969 Actual	Fiscal 1970 Estimate		
		Budget Bureau May 20	Budget Bureau Sept. 17	Current Board Staff
Total Receipts	187.8	199.2	198.8	196.6
Total Outlays	184.8	192.9	192.9	192.9
Surplus	3.1	6.3	5.9	3.7

At present the legal ceiling on budget outlays stands higher than the Administration's estimate of $192.9 billion for fiscal 1970. Congress established a $191.9 billion limit with provision for two types of adjustments. The ceiling adjusts automatically if Congressional action or inaction has a net effect on spending. The President may also adjust the ceiling by as much as $2 billion for increases in certain administratively uncontrollable items specified in the Act. As of August 31, the President specified increases of $1.5 billion under the latter provision, thereby raising the legal ceiling to $193.4 billion. Congressional action may raise the ceiling further.

The Administration remains committed to holding total outlays to the $192.9 billion announced earlier, despite the higher legal ceiling. However, substantial adjustments have been made in individual items. The table below shows that increased outlays for several programs are intended to be offset primarily by decreases in defense spending.

* Prepared by William Beeman, Economist, Government Finance Section, Division of Research and Statistics.

CHANGES IN UNIFIED BUDGET OUTLAYS
(Fiscal 1970, billions of dollars)

April 15 Estimate of Outlays			192.9
Budget increases		3.7	
Agriculture	.4		
Health Education and Welfare	.6		
Interior	.3		
Post Office	.4		
Treasury (mostly interest)	.9		
Veterans Administration	.4		
Other	.7		
Budget decreases		3.7	
Defense	3.0		
Housing and Urban Development	.2		
Transportation	.2		
Other	.3		
September 17 Estimate of Outlays			192.9

The Administration attributes most of the increased spending by HEW to Medicare and Medicaid programs and to increases in assistance payments. However, the recently proposed 10 per cent hike in Social Security benefits (involving more than $.6 billion in fiscal 1970) is scheduled to go into effect only in April 1970 and thus does not require more funds than the 7 per cent hike that had been budgeted previously. Most of the increases in Agriculture expenditures is said to arise because Congress is unlikely to eliminate the special milk and agriculture conservation programs and from the Administration's proposed expansion of the food stamp program. The Administration seems to be anticipating less than a $100 million increase in its estimate of CCC outlays, though present crop yields suggest an increase of perhaps $900 million.

The Budget Review indicates that about $2.5 billion of the $3.7 billion increases shown in the above table result from "uncontrollable" items. Congressional action or inaction to date accounts for at least an additional $1 billion in spending increases. To offset these increases the Administration indicates it has directed agency heads to reduce

spending for other items by $3.5 billion, including the $3 billion cut previously announced by Defense Secretary Laird. However, recent action by the House involving appropriations for education would provide nearly $1 billion above that recommended by the Administration. Senate action in the area of housing also exceeds Administration requests. In view of the apparent low estimates for agriculture and possible Congressional action in various areas, it would appear that further budget cuts by the Administration will become necessary if outlays are going to be held to the $192.9 billion level.

The Budget Bureau estimate of receipts for fiscal 1970 includes about $4 billion dependent upon action not yet taken by Congress. The Bureau assumes retroactive repeal of the investment tax credit ($1.3 billion), extension of the tax surcharge through June 1970 at the 5 per cent rate ($2.0 billion) and extension or imposition of certain excise and user charges ($.7 billion). The presumed enactment of the administration's tax reform proposal is expected to have no net effect on the total budget for fiscal 1970.

Most of the $2.2 billion difference between the Budget Bureau and Board Staff estimates of total receipts for fiscal 1970 involves estimates of corporate income tax receipts. The Staff forecast assumes lower corporate profits, especially in the second half of fiscal 1970.

As customary the Summer Budget Review does not go beyond the current fiscal year and official estimates cannot be expected before the January Budget. In preparing the Budget Document the administration will face the expiration of the surtax which at the recommended 7.5 per cent average for this fiscal year, would yield an estimated $8 billion. Thus, even with the usual growth in the tax base, total net receipts would not increase sufficiently to offset large expenditures increases. The recent Administration proposals on increases in social security benefits would add $3.5 billion to outlays in fiscal 1971. A partially offsetting social security tax increase is now scheduled for January 1971. The final budget outcome for fiscal 1971, of course, will depend heavily on developments in defense spending.