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CONFIDENTIAL (FR)

CURRENT ECONOMIC and FINANCIAL CONDITIONS

**Prepared for the
Federal Open Market Committee**

By the Staff

**BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM**

July 12, 1967

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SUMMARY AND OUTLOOK

Outlook for economic activity

The third quarter has begun on a firm tone as consumers appear to be buying more durable goods, especially autos, than anticipated and the inventory adjustment has become much less of a downward drag on economic expansion than earlier. Gains in GNP in both the second and third quarter are now expected to be somewhat larger than previously anticipated. Real GNP growth this quarter could increase to an annual rate of over 4 per cent although the price deflator is also expected to rise more rapidly than previously estimated, mainly because of rising prices of farm products and foods. These projections would need to be modified if there is a lengthy or widespread auto strike; contracts are scheduled to expire in early September.

Inventories continue to move into a more favorable balance with sales. In May there was little further accumulation in total business inventories. Additions to stocks of manufacturing fell to a relatively low level as shipments increased and output declined somewhat further. At the same time, there was additional liquidation of distributors' inventories. New orders and employment in manufacturing have begun to rise and, with the inventory situation improving, production should also turn up in this quarter.

Gains in retail sales in the second quarter were the major factor lifting private final outlays above expected levels. Domestic automobile sales increased to an 8.4 million annual rate in June, sharply above the April and May rate; sales of department and other general merchandise stores also showed significant improvement. Services, meanwhile, continued their upward trend,

The outlook for total consumer expenditures, therefore, appears to be strengthening. Along with improved consumer sentiment, which has also been reflected in recent surveys, wages and employment will be advancing faster and the savings rate, which fell in the second quarter, should decline further.

Final demands are also being augmented in the third quarter by a further rise in expenditures for residential construction. Housing starts have responded to the greater availability of mortgage credit over recent months, and the number of new building permits issued implies a continuation of the upward trend in expenditures even though interest costs on mortgages have risen somewhat recently.

In line with latest Commerce-SEC survey, our expectation is still for some moderate rise in business fixed investment this quarter. New orders for machinery and equipment have strengthened and, although the evidence is still incomplete, reinstatement of the 7 per cent tax credit seems to be having a positive effect on business expectations and on expenditures for plant and equipment.

The Government sector, meanwhile, will also provide important support to rising final sales in the third quarter. Defense expenditures are projected to continue to rise and to exceed Budget estimates. Exactly how huge this extra spending may be should become clearer in the next few weeks, when the Budget Bureau is scheduled to present revised estimates of Federal expenditures and receipts for fiscal year 1968.

Resource use and prices

Demand for workers strengthened somewhat in June, even though the unemployment rate rose to 4.0 per cent from 3.8 in May. Nonfarm employment turned up after declining since March, including a small rise in manufacturing and construction. Gains in employment are expected to increase faster in coming months. The labor force, which had been declining recently, recovered sharply as the inflow of workers in June, particularly teenagers, sharply exceeded seasonal expectations. Most of these new workers found jobs although the added supply of women seeking seasonal jobs somewhat exceeded demands and their unemployment rose. The higher rate of unemployment in June is not expected to continue beyond the summer.

Industrial production is estimated to have declined somewhat further in June, and possibly into July, reflecting attempts by both manufacturers and distributors to reduce inventories of materials and of consumer goods, as well as some further downward adjustment in production of business equipment.

The rate of capacity utilization by manufacturers continued downward from the estimated level of 85.0 per cent in May. Excess capacity now exists in many manufacturing industries--especially those producing industrial materials. Among the major groups, only manufactures of aircraft and electrical generating equipment continue to operate at peak rates of utilization.

Industrial commodity prices have continued stable as the overhang of inventories and the level of unutilized capacity have provided some offset to the further increase in business costs. Recent and anticipated increases in negotiated wage contracts are likely to produce a renewed rise in unit labor costs, but output and productivity also should rise and help keep the rise in labor costs from being as sharp as last year.

The expansion in market supplies of consumer food products, which resulted in lower food prices earlier, has come to an end. With food prices increasing again, the consumer price index increases of 0.3 per cent in April and May may be followed by a larger rise in June. This would add further to upward pressure on wage rates.

Outlook for banking

While distribution of the \$4 billion of new tax bills is currently a principal influence on bank credit, expansion will probably be sustained as the summer progresses by continued active public demand for time and savings deposits, by growth in private demand deposits, and late in the summer probably by further Treasury cash borrowing. Barring substantial additional increases in short- and intermediate-term yields inflows into passbook savings and time deposits other than negotiable CD's are likely to continue at near recent rates. Meanwhile, net increases in outstanding CD's may continue to be relatively small, as banks face increasing competition from new issues of Treasury and Federal Agency securities bearing relatively attractive yields. Private demand deposits are likely to expand over the months ahead in view of the accelerated pace of economic activity,

but the rate of expansion may be slower than in recent months when Treasury deposits had been declining.

During the summer, business loan demands on banks are expected to be quite moderate, as inventory financing needs are minimal and as corporations no longer have to deal with large accelerated tax payments. With loan demands moderate and deposit inflows continuing in volume, bank investments in State and local, Federal Agency, and U.S. Government securities are likely to be fairly sizable.

Current interest rate relationships between the cost of time and savings deposits and the return on marketable securities make intermediate-term securities an attractive investment outlet for banks. But banks are also likely to emphasize short-term securities in an effort further to restock their liquidity against the prospect of sizable fall loan demands. And the recent rise in Treasury bill yields has made them attractive to banks, but does not appear to have attracted individuals' savings away from banks.

Capital markets outlook

Yields on new and recently offered corporate bond issues have dropped back from the record highs registered two weeks ago, but prospects for further rate declines will depend on market psychology and the forthcoming volume of new offerings. Thusfar, this volume shows little sign of abatement over the near-term. The amount of public bond offerings in July is expected to surpass the record June level, and the amount of public flotations already scheduled for August is unusually large. In the municipal market, too, the forward calendar

indicates near-term continuation of demand pressures--with July sales of issues ultimately expected to total more than \$1 billion. The August municipal volume now appears to be relatively light, however, and may represent the first month this year in which offerings fall short of \$1 billion.

In late July, the Treasury will announce the terms of its mid-August refunding, which will involve \$3.6 billion of publicly held maturing issues. The sharp yield increases in the intermediate-term sector of the Government securities market toward the end of June probably reflected some expectation that the Treasury might take this opportunity to use its new authority to issue securities with maturities as long as seven years free of the interest rate ceiling. The market is in a good technical position to absorb such issues, with dealers having a small net short position in securities maturing in over 5 years. But over-all investor demand for such issues will be strongly influenced by interest rate expectations, which in turn will depend heavily on market evaluation of prospects for a tax increase.

The results of the official re-evaluation of the Federal Government's budgetary position over the next few weeks will be a critical factor influencing capital markets as a whole. If such a review is accompanied by a strongly worded request for a tax increase, it will be more likely that investor and borrower attitudes as to the likelihood of future credit stringency will shift and that intermediate- and long-term interest rates will decline further. The

sustainability of such declines, should they develop, will be tested by how readily the Treasury financing and private borrowings are absorbed in the market and by the gathering evidence of Congressional attitudes towards any tax proposal.

The earlier increases in market interest rates have led to some tightening in mortgage markets in May and June, and to a renewal of uncertainty about credit costs, if not mortgage availability, over the period ahead. Nevertheless, savings flows to depositary-type financial intermediaries do not appear to have been seriously affected by the recent increases in short- and intermediate-term rates, although only fragmentary data for the July reinvestment period are currently available. However, there does appear to be some outflow of funds from California S&L's as a result of the reduction in the maximum permissible rate from 5.25 to 5.00 per cent on their passbook savings; these funds may be being diverted to depositary institutions in other regions.

While short- and intermediate-term market rates have risen dramatically, they still do not appear to be at the levels necessary to trigger significant disintermediation. Should the upward rate trend continue, however, in the wake of Treasury refundings and cash financings later in the summer, there would be a real risk of a significant impact on depositary flows in the months ahead.

The balance of payments

With half the year over, projections of the deficit in the 1967 balance of payments are being revised upward, by observers outside the Government as well as within. On the liquidity basis, but before counting the effect of net acquisitions of near-liquid assets by foreign official and international bodies, the deficit in the first half-year is now tentatively estimated at about \$2 billion, seasonally adjusted, and the full-year deficit may exceed \$3-1/2 billion. After counting the special transactions, the half-year deficit was only about \$1 billion.

Evaluation of prospects for the full year 1967 is hampered by lack of complete information as to the particular elements of receipts and payments that produced so large a deficit in the first half. Insofar as these receipts and payments are known, or can be roughly inferred from statistics covering the first quarter of 1967 and the final quarter of 1966, it appears that military expenditures abroad may be increasing more than was expected a few months ago and that U.S. receipts of investment income from abroad (especially on direct investments) have not been coming up to expectations. Also, it now seems likely that U.S. merchandise exports--recently well above late-1966 levels--will not rise as much during the rest of this year as was formerly anticipated. The changes in expectations regarding receipts of investment income and export earnings reflect, in part, a more pessimistic appraisal than before of prospects for an early upturn in European economic activity.

Despite these shifts toward more pessimistic appraisals, the projections imply a smaller deficit (before special transactions) in the second half of the year than in the first half. With imports declining in recent months and not expected to advance rapidly in the next few months, the trade surplus is likely to increase somewhat further--though less than if Europe's demand were growing at a normal pace. Apart from this, much of the projected improvement depends on unidentified items, the balance of which ("errors and omissions") was more adverse in late 1966 and early 1967 than in most other recent periods.

Although the liquidity deficit computed without counting certain kinds of special transactions may reach or exceed \$3-1/2 billion for the year 1967, the generally publicized official figure for the deficit (which is reduced by such transactions) will be much smaller. Tentative indications are that during the first half of 1967 net placements of foreign official and international funds in near-liquid assets amounted to about \$1 billion. It is assumed that during the second half of the year holdings of time deposits and Agency securities with original maturities over 12 months coming due will be rolled over into similar assets. In addition, some moderate amount of debt prepayment receipts is looked for.

On the official settlements basis, the deficits is predictable only with a wide margin of possible error. If net changes over the year in liquid and near-liquid liabilities to others than foreign monetary authorities--i.e., to commercial banks, other private foreign residents,

and international institutions--should turn out small, the deficit on this basis would be about the same as the liquidity deficit without benefit of special receipts--i.e., \$3-1/2 billion or more. During the first half of 1967, according to very tentative estimates, the net run-down in U.S. liabilities to commercial banks abroad (including U.S. bank branches) exceeded the increase in other liquid and near-liquid liabilities to non-official holders, by some \$500 million. Accordingly, the official settlements deficit during that period, now estimated at about \$2-1/2 billion, seasonally adjusted, was considerably larger than the first half-year liquidity deficit as measured without giving effect to special transactions of the kinds that have been mentioned.

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.)	June '67	77.2	76.2	75.7	2.1	3.7
Unemployment (mil.)	"	3.1	2.9	2.9	5.2	-10.5
Unemployment (per cent)	"	4.0	3.8	3.9	--	--
Nonfarm employment, payroll (mil.)	"	65.6	65.4	64.0	2.5	8.2
Manufacturing	"	19.2	19.1	19.2	-0.1	6.5
Other industrial	"	8.0	8.0	8.1	-0.8	2.3
Nonindustrial	"	38.4	38.3	36.7	4.5	10.3
Industrial production (57-59=100)	"	155.2	155.5	156.5	-0.8	8.5
Final products	"	155.9	156.3	154.9	0.6	10.3
Materials	"	154.9	155.1	158.0	-2.0	6.7
Wholesale prices (57-59=100) ^{1/}	"	105.8	105.3	105.6	0.2	3.6
Industrial commodities	"	105.2	105.1	104.3	0.9	3.1
Sensitive materials	"	100.1	100.7	106.8	-6.3	-2.2
Farm products, foods & feeds	"	105.0	103.4	107.9	-2.7	3.9
Consumer prices (57-59=100) ^{1/}	"	115.6	115.3	112.6	2.7	5.5
Commodities except food	"	108.7	108.4	106.3	2.3	3.3
Food	"	113.9	113.7	113.5	0.4	5.6
Services	"	127.0	126.6	121.5	4.5	8.1
Hourly earnings, mfg. (\$)	June '67	2.81	2.80	2.71	3.7	7.7
Weekly earnings, mfg. (\$)	"	112.91	113.00	111.85	0.9	5.6
Personal income (\$ bil.) ^{2/}	May '67	616.9	614.1	573.0	7.7	16.8
Corporate profits before tax (\$ bil.) ^{2/}	QI '67	77.4	81.8	82.7	-6.4	3.9
Retail sales, total (\$ bil.)	June '67	26.1	26.0	25.4	2.6	11.7
Autos (million units) ^{2/}	"	8.4	7.5	8.3	1.1	-6.0
GAF (\$ bil.)	"	6.3	6.3	6.0	4.3	19.1
Selected leading indicators:						
Housing starts, pvt. (thous.) ^{2/}	May '67	1,310	1,173	1,318	-0.6	-13.6
Factory workweek (hours)	June '67	40.2	40.4	41.3	-2.7	-2.0
New orders, dur. goods (\$ bil.)	May '67	23.9	22.2	24.3	-1.5	13.9
New orders, nonel. mach. (\$ bil.)	"	3.5	3.4	3.6	-1.1	13.1
Common stock prices (1941-43=10)	June '67	91.43	92.59	86.06	6.2	7.5
Inventories, book val. (\$ bil.)	May '67	137.4	137.3	126.2	8.9	19.4
Gross national product (\$ bil.) ^{2/}	QI '67	763.7	759.3	721.2	5.9	15.6
Real GNP (\$ bil., 1958 prices) ^{2/}	"	656.7	657.2	640.5	2.5	9.4

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

SELECTED DOMESTIC FINANCIAL DATA

	Week ended	Four-Week	Last six months				
	July 8	Average	High	Low			
Money Market <u>1/</u> (N.S.A.)							
Federal funds rate (per cent)	3.91	3.97	5.75	2.50			
U.S. Treas. bills, 3-mo., yield (per cent)	4.20	3.79	4.83	3.33			
U.S. Treas. bills, 1-yr., yield (per cent)	4.84	4.61	4.84	3.80			
Net free reserves <u>2/</u> (mil. \$)	152	231	324	-170			
Member bank borrowings <u>2/</u> (mil. \$)	353	157	585	43			
Capital Market (N.S.A.)							
Market yields <u>1/</u> (per cent)							
5-year U.S. Treas. bonds	5.30	5.17	5.36	4.38			
20-year U.S. Treas. bonds	5.02	5.04	5.11	4.44			
Corporate new bond issues, Aaa	5.86	5.83	5.92	5.11			
Corporate seasoned bonds, Aaa	5.59	5.50	5.59	4.99			
Municipal seasoned bonds, Aaa	3.85	3.83	3.85	3.25			
FHA home mortgages, 30-year <u>3/</u>	6.44	6.44	6.77	6.29			
Common stocks S&P composite index <u>4/</u>							
Prices, closing (1941-43=10)	91.32	91.78	94.44	86.46			
Dividend yield (per cent)	3.20	3.18	3.12	3.36			
New Security Issues							
Corporate public offerings	July '67	1.9 ^e	1.6 ^e	236.4	76.1		
State & local gov. public offerings	"	1.1 ^e	1.2 ^e	56.9	33.9		
Comm. & Fin. co. paper, change in outstandings	May '67	17.1	16.5	49.2	47.7		
Banking (S.A.)							
Total reserves <u>1/</u>	June '67	24.46	0.16	0.05	7.7	2.6	4.1
Credit Proxy <u>1/</u>	"	259.2	2.0	1.8	9.3	8.3	6.3
Bank Credit, Total <u>5/</u>	"	326.7	0.3	1.6	1.1	6.0	6.2
Business loans	"	82.6	1.2	0.7	17.7	10.9	8.4
Other loans	"	131.7	-0.7	0.1	-6.4	0.9	3.1
U.S. Gov't. sec.	"	56.5	-1.1	-0.4	-22.9	-9.0	2.5
Other securities	"	55.9	0.8	1.2	17.4	27.5	15.0
Money and other liquid assets							
Total <u>1/</u> <u>5/</u>	May '67	618.7	2.9	4.0	5.7	7.8	4.8
Demand deposits & currency <u>1/</u>	June '67	176.0	1.9	1.1	13.1	7.4	2.9
Time and savings deposits, comm. banks <u>1/</u>	"	171.7	2.4	2.1	17.0	15.5	11.8
Savings accounts, other institutions <u>5/</u>	May '67	175.0	1.1	1.5	7.6	10.3	6.4
Other <u>5/</u> <u>6/</u>	"	100.3	-2.2	-0.8	-25.8	-9.0	-3.3

N.S.A. -- not seasonally adjusted. S.A. -- Seasonally adjusted.

1/ Average of daily figures. 2/ Averages for statement week ending July 5.

3/ Latest figure indicated is for month of May. 4/ Data are for weekly closing prices. 5/ Month-end data.

6/ U.S. Savings bonds and U.S. Government securities maturing within 1 year.

NOTE: Where necessary, changes have been adjusted to take account of conceptual and definitional changes in data.

U. S. BALANCE OF PAYMENTS
(In millions of dollars)

	1 9 6 7			1 9 6 6				1966
	May	Apr.	QI	QIV	QIII	QII	QI	Year
	(billions)							
	Seasonally adjusted							
Current account balance			1,078	838	873	1,108	1,273	4.1
Trade balance <u>1/</u>	390	400	1,001	722	802	956	1,178	3.7
Exports <u>1/</u>	2,510	2,625	7,690	7,402	7,382	7,181	7,203	29.2
Imports <u>1/</u>	-2,120	-2,225	-6,689	-6,680	-6,580	-6,225	-6,025	-25.5
Services, etc., net			77	116	71	152	95	0.4
Capital account balance			-1,416	-1,028	-1,315	-1,032	-1,691	-5.1
Govt. grants & capital <u>2/</u>			-1,205	-724	-759	-988	-975	-3.4
U.S. private direct investment			-695	-922	-900	-1,006	-634	-3.5
U.S. priv. long-term portfolio			-154	69	-5	-69	-252	-0.3
U.S. priv. short-term			-157	-231	-27	-60	-95	-0.4
Foreign nonliquid			795	780	376	1,091	265	2.5
Errors and omissions			-206	-229	277	-198	-233	-0.4
	Balances, with and without seasonal adjustment (- = deficit)							
Liquidity bal., S.A.			-544	-419	-165	-122	-651	-1.4
Seasonal component			301	-47	-530	-27	604	--
Balance, N.S.A.	-166	-336	-243	-466	-695	-149	-47	-1.4
Official settlements bal.			-1,822	-18	861	-175	-443	0.2
Seasonal component			543	-180	-456	-210	846	--
Balance, N.S.A. <u>3/</u>	-249	-622	-1,279	-198	405	-385	403	0.2
Memo items:								
Monetary reserves (decrease -)	37	51	-1,027	6	-82	-68	-424	-0.6
Gold purchases or sales (-)	-20	50	-51	-121	-173	-209	-68	-0.6

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

2/ Net of loan repayments.

3/ Differs from liquidity balance by counting as receipts (+) increases in liquid liabilities to commercial banks, private nonbanks, and international institutions (except IMF) and by not counting as receipts (+) increase in certain nonliquid liabilities to foreign official institutions.

THE ECONOMIC PICTURE IN DETAIL

Gross national product.^{1/} Latest data available tend to support staff projections of a month ago calling for a moderate rise in GNP in the second quarter and a larger rise in the third quarter. Indeed, the present staff projection indicates slightly larger increases in current dollar GNP than projected in both quarters before. Increases in GNP of \$11.6 billion and \$15.2 billion, annual rates, are now estimated for the second and third quarters. However, the estimated GNP deflator has been raised largely because of higher food prices. The increases in real GNP of 2.9 per cent and 4.4 per cent, respectively, are not much different than the previous estimates.

The faster rate of expansion also reflects the further substantial rise in final sales (\$17 billion a quarter) while the downdrag from inventory adjustment diminishes sharply. Declines in the rate of inventory investment, which offset \$11 billion of final sales in the first quarter, and \$5 billion in the second quarter, are projected to call for only a \$ 2 billion additional offset in the third quarter. Within final sales the contribution of the private sector increases appreciably after the first quarter.

^{1/} Revised estimates of gross national product and income for the period since the end of 1963 will be available shortly, and these, with staff projections of the third quarter adjusted to the new Commerce figures will be incorporated in a supplement and sent to the Committee as soon as possible. This Commerce annual revision is not expected to change significantly the quarter-to-quarter pattern of economic activity depicted by the presently available figures, but it may show a higher level of GNP in recent quarters and a slightly faster rate of expansion over the three-year period as a whole.

The bulk of the increase in private final sales is now expected to be in consumer spending. New car sales figures suggest larger second quarter gains in consumption expenditures than were indicated a month ago. Sales of new U.S.-made autos rose sharply in June to an annual rate of about 8.4 million units, in contrast to an April-May rate of 7.6 million. The higher sales rate accounts for much of the \$1 billion second quarter upward revision in consumer outlays for durable goods. Sales of domestic autos in the third quarter have been raised to an estimated annual rate of 8-1/4 million from the 8 million indicated a month ago and sales of other durables also have been increased. Nondurable consumption expenditures have been raised, partly because of the expected continuation of higher food prices.

Income in the third quarter is now projected to be bolstered by larger employment increases than estimated earlier. Consumer spending is still expected to rise more rapidly than income, reflecting recent evidences of greater willingness of consumers to spend more freely including recent surveys which report strengthening of consumer intentions to buy. The ratio of personal saving to disposable income is projected to drop to 6.2 per cent in the second quarter and to 5.9 per cent in the third, from the unusually high rate of 6.5 per cent in the first quarter.

Residential construction is predicted to rise sharply in both the second and third quarters based on evidence of higher starts and permits recently and later availability of credit. Housing starts in May were somewhat higher than earlier anticipated and second quarter outlays therefore will also be slightly higher. For the third quarter, starts are still expected to amount to about a 1,350,000 annual rate. Estimated business fixed investment in the second quarter has been

raised to about the first quarter rate because of higher new car sales a portion of which are used for business purposes. A modest further gain is expected for the third quarter, not only because of the latest Commerce-SEC survey but also because of recent increases in new orders for machinery and equipment at the restoration of the investment tax credit and accelerated depreciation.

Government purchases should rise about \$5 billion in each quarter. State and local government purchases are expected to maintain their steady upward trend. While Federal defense outlays are likely to be up less in the third quarter than in the second, this may well offset by a more rapid rise in other Federal purchases. The estimated increase of \$2.8 billion annual rate in defense outlays in the second quarter reflects actual spending as shown by the April and May monthly Treasury statements; the critical June Treasury statement, however, is not yet available. Total defense spending for fiscal 1967 now appears to be about \$1.3 billion larger than estimated in the Budget last January.

Recent information shows business efforts to bring excessive inventories into line with sales are meeting with success. A further marked slowing in the rate of accumulation of inventories occurred in April and May at both durable and nondurable goods manufacturers. Both retail and wholesale establishments, meanwhile, liquidated stocks. Although inventories-shipments ratios in most manufacturing lines are still high, the ratios appear to be declining. Prospectively stronger final sales suggest a further reduction in the rate of accumulation in manufacturing and continued liquidation at trade establishments which should further reduce stock-sales ratios in the months ahead.

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GROSS NATIONAL PRODUCT AND RELATED ITEMS ^{1/}
 (Quarterly figures are seasonally adjusted. Expenditures and income
 figures are billions of dollars, with quarterly figures at annual rates)

	1965	1966	1966			1967		
						Projected		
			II	III	IV	I	II	III
Gross National Product	681.2	739.6	732.3	745.3	759.3	763.7	775.3	790.5
Final sales	672.1	727.7	720.0	735.4	742.9	758.1	775.3	792.5
Private	535.9	574.7	571.0	579.2	581.8	589.0	601.0	613.2
Personal consumption expenditures	431.5	464.9	460.1	469.9	474.1	479.9	488.9	498.3
Durable goods	66.1	69.3	67.1	70.2	69.6	68.4	70.0	71.5
Nondurable goods	190.6	206.2	205.6	208.1	209.2	212.5	216.2	220.4
Services	174.8	189.4	187.4	191.5	195.3	199.1	202.7	206.4
Gross private domestic investment	106.6	117.0	118.5	115.0	120.0	109.3	106.1	106.6
Residential construction	27.8	25.8	28.0	24.8	21.9	22.1	24.1	25.9
Business fixed investment	69.7	79.3	78.2	80.3	81.6	81.6	81.5	82.2
Change in business inventories	9.1	11.9	12.3	9.9	16.4	5.6	.5	-1.5
Nonfarm	8.1	12.2	12.1	10.4	17.6	6.0	.5	-1.5
Net Exports	7.0	4.8	4.7	4.2	4.1	5.4	6.0	6.3
Gov't purchases of goods & services	136.2	153.0	149.0	156.2	161.1	169.1	174.3	179.3
Federal	66.8	76.9	74.0	79.0	81.7	87.0	90.0	92.8
Defense	50.1	60.0	57.1	62.0	65.5	69.7	72.5	75.0
Other	16.7	16.9	16.9	17.0	16.2	17.2	17.5	17.8
State & local	69.4	76.2	75.0	77.2	79.4	82.1	84.3	86.5
Gross National Product in constant (1958) dollars	614.4	647.8	643.5	649.9	657.2	656.7	661.5	668.8
GNP Implicit deflator (1958=100)	110.9	114.2	113.8	114.7	115.5	116.3	117.2	118.2
Personal income	535.1	580.4	573.5	585.2	598.3	609.7	617.5	630.0
Wage and salaries	358.4	392.3	387.4	396.7	405.0	411.8	418.5	428.0
Disposable income	469.1	505.3	499.9	507.8	518.4	528.5	536.5	545.3
Personal saving	25.7	27.0	26.6	24.5	30.4	34.4	33.1	32.1
Saving rate (per cent)	5.5	5.3	5.3	4.8	5.9	6.5	6.2	5.9
Total labor force (millions)	77.2	78.9	78.4	79.1	79.8	80.3	80.2	80.7
Armed forces "	2.7	3.1	3.1	3.2	3.3	3.4	3.5	3.5
Civilian labor force "	74.5	75.8	75.4	76.0	76.5	76.9	76.7	77.2
Unemployment rate (per cent)	4.5	3.8	3.8	3.8	3.7	3.7	3.8	3.9
Nonfarm payroll employment (millions)	60.8	63.9	63.6	64.1	64.8	65.5	65.5	65.8
Manufacturing	18.0	19.1	19.0	19.2	19.4	19.4	19.2	19.3
Industrial production (1957-59=100)	143.4	156.3	155.2	157.6	158.8	157.0	155.6	157.5
Capacity utilization, manufacturing (per cent)	89	91	91	91	90	87	85	85
Housing starts, private (millions, A.R.)	1.51	1.22	1.37	1.09	.98	1.21	1.26	1.36
Sales new U.S.-made autos (millions, A.R.)	8.76	8.38	7.81	8.47	8.13	7.33	7.83	8.25

^{1/} GNP revised figures will be available by July 17th.

CONFIDENTIAL -- FR

July 12, 1967

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS ^{1/}
(Quarterly changes are at annual rates)

	1965	1966	1966			1967		
			II	III	IV	I	Projected	
							II	III
	(Billions of Dollars)							
Gross National Product	49.5	58.4	11.1	13.0	14.0	4.4	11.6	15.2
Final sales	45.1	55.6	7.7	15.4	7.5	15.2	17.2	17.2
Private	37.8	38.8	3.7	8.2	2.6	7.2	12.0	12.2
GNP in constant (1958) dollars	34.4	33.4	3.0	6.4	7.3	-0.5	4.8	7.3
Final sales	30.2	31.1	-0.1	8.9	1.2	9.5	9.9	9.4
Private	27.4	22.0	-2.2	4.4	-2.2	4.2	6.3	6.2
	(Per Cent)							
Gross National Product	7.8	8.6	6.2	7.1	7.5	2.3	6.1	7.8
Final sales	7.2	8.3	4.3	8.6	4.1	8.2	9.1	8.9
Private	7.6	7.2	2.6	5.7	1.8	4.9	8.1	8.1
Personal consumption expenditures	7.5	7.7	3.9	8.5	3.6	4.9	7.5	7.7
Durable goods	11.3	4.8	-18.2	18.5	-3.4	-6.9	9.4	8.6
Nondurable goods	6.5	8.2	7.3	4.9	2.1	6.3	7.0	7.8
Services	7.2	8.4	8.7	8.7	7.9	7.8	7.2	7.3
Gross private domestic investment	14.6	9.8	14.0	-11.8	17.4	-35.7	-11.7	1.9
Residential construction	0.7	-7.2	-8.4	-45.7	-46.8	3.7	36.2	29.9
Business fixed investment	14.8	13.8	6.2	10.7	6.5	0.0	-0.5	3.4
Gov't purchases of goods & services	5.7	12.3	11.0	19.3	12.5	19.9	12.3	11.5
Federal	2.5	15.1	11.7	27.0	13.7	25.9	13.8	12.4
Defense	0.2	19.8	18.3	34.3	22.6	25.6	16.1	13.8
Other	9.9	1.2	-11.5	2.4	-18.8	24.7	7.0	6.9
State & local	8.9	9.8	10.4	11.7	11.4	13.6	10.7	10.4
GNP in constant (1958) dollars	5.9	5.4	1.9	4.0	4.5	-0.3	2.9	4.4
Final sales	5.2	5.1	-0.1	5.6	0.7	5.9	6.1	5.7
Private	5.9	4.5	-1.7	3.4	-1.7	3.3	4.9	4.7
GNP Implicit deflator	1.8	3.0	4.3	3.2	2.8	2.8	3.1	3.4
Personal Income	7.9	8.5	6.3	8.2	9.0	7.6	5.1	8.1
Wage and salaries	7.4	9.5	7.8	9.6	8.4	6.7	6.5	9.1
Disposable income	7.4	7.7	3.9	6.3	8.3	7.8	6.1	6.6
Nonfarm payroll employment	4.2	5.1	4.9	3.3	4.0	4.3	0.0	1.8
Manufacturing	4.4	5.8	6.9	3.5	4.0	0.0	-4.1	2.1
Industrial production	8.4	9.0	7.9	6.2	3.0	-4.5	-3.6	4.9
Housing starts, private	-3.3	-18.9	-39.5	-81.3	-39.3	88.4	16.5	31.7
Sales new U.S.-made autos	15.0	-4.4	-62.8	33.6	-15.8	-39.6	27.3	21.5

^{1/} GNP revised figures will be available by July 17th.

Industrial production. Industrial production in June was 155.2 per cent as compared to 155.5 in May, and was 1 per cent below a year earlier. The June decline was primarily in manufacturing industries.

Auto assemblies increased in June and were at an annual rate of 8.0 million units as compared with 7.8 billion in May. Schedules for the third quarter are somewhat above the June rate, after allowance for the earlier and shorter model changeover period this year. Production schedules may not be met, however, as the continuing strike in the tire industry, which started April 21, may begin to affect auto assemblies and, in addition, a strike in the auto industry in early September is not unlikely.

Among the limited production data available for June, the only increases other than for autos were shown by output of crude petroleum, as a result of the Mid-East situation, and by defense equipment. Steel ingot production declined 4 per cent and output of steel mills products apparently also declined further as mill inventories of these goods reached a record level at the end of May. Production of trucks and paperboard continued to decline and were below year ago levels. Output of appliances declined and television and radio production was sharply curtailed by a strike at RCA.

The decline of 2.4 per cent in total industrial production in the 6 months since the high last December has been much smaller than in corresponding postwar periods of production curtailment, as

shown in the table. While decreases in some industries have been sharp--autos, appliances, television sets, lumber, and steel--the timing of the cutbacks in output have been staggered.

INDUSTRIAL PRODUCTION
Per cent decline from 6 months earlier to:

June 1967	November 1960	February 1958	January 1954	April 1949
2.4	4.1	11.9	9.3	6.5

The current contraction has been quite different from those in 1957 and 1953 when output readjustments occurred almost simultaneously in most cyclical industries. Another major difference this time has been the continuing sharp advance in output of defense equipment which has almost offset the reduction in output of other business equipment.

Auto markets. Sales of new domestic automobiles in the month of June strengthened considerably to a seasonally adjusted annual rate of 8.4 million units, 11 per cent above the May rate. It was the first month since last November that the sales rate exceeded 8 million units. The higher June figure raised sales for the second quarter to an average rate of 7.8 million units, up from 7.3 million in the first quarter and was the same rate as in the second quarter of last year.

With auto assemblies at a seasonally adjusted annual rate of about 8 million units, new car inventories at the end of June were down to 1.4 million, a level substantially below the record 1.73 million a year earlier. As a consequence of the higher sales, and the improved inventory situation, the model year sales clean-up should pose no problems. On the contrary, in the face of continued strong consumer demand there may be some supply shortages prior to the introduction of the 1968 models in September. Used car prices (seasonally adjusted) as reported in the Consumer Price Index continued to show unusual strength, rising 2 per cent further in May. In June, however, used car auction prices moved irregularly.

Consumer credit. Expansion in consumer instalment credit apparently slowed further in the second quarter. In May the seasonally adjusted increase in outstandings was \$193 million, down from \$213 million in April, and the smallest monthly rise in more than five years. Data for June are incomplete but even assuming an acceleration in credit use because of the improvement in new car and other retail sales, the net increase in outstandings for the second quarter as a whole would still not reach that in the first quarter--itself a relatively sluggish period.

INCREASES IN CONSUMER INSTALMENT CREDIT
(Billions of dollars, seasonally adjusted annual rate)

Period	Increases in Outstandings
1966 Q1	7.1
Q2	6.3
Q3	6.6
Q4	4.6
1967 Q1	3.0
Q2 (est.)	2.6

The importance of the repayments pattern should be noted in evaluating recent changes in outstandings. New credit extensions actually rose \$100 million in April, the largest monthly rise since last November, and while extensions turned down again in May, they were still the second highest month of the year. But a rise in repayments overshadowed the improvement in extensions. In April, for example, the \$100 million rise in extensions more than counter-balanced an increase of \$150 million in the rate of repayments.

Credit demands this spring have been closely tied to developments in consumer spending. But there is some indication that credit also has been used less intensively than usual. For both new and used cars, the proportions bought on credit trailed off in April and May from both first quarter and year-earlier levels.

Meanwhile, lending standards on autos--in such nonprice terms as maturities and downpayments--are showing little further change after a noticeable easing late last year by sales finance companies. Perhaps the major exception to that easing was in used-car maturities, and finance companies have continued to maintain relatively tight controls in this area. Indeed, the proportion of used-car contracts in the "over-30-months" category has tended to decline since early 1966.

Retail sales. Retail sales in June, according to advance estimates based on a partial sample, were about unchanged from the April-May level. A rise at durable goods stores, mostly at automotive stores, was almost offset by a decline at nondurable goods stores. For the second quarter, total retail sales were 1.4 per cent higher than in the first quarter.

Sales at durable goods stores in June rose 1.9 per cent, following a rise of 1.1 per cent in May. Both of these increases reflected relatively large gains in sales reported by automotive stores. Furniture and appliance stores sales were indicated to be off about 3 per cent in June, following a rise of 1.6 per cent in May. For the second quarter as a whole, furniture and appliance sales were down from the first quarter but were higher than in the final quarter of last year.

Sales at nondurable goods stores were off .5 per cent in June, after changing little in May (preliminary figures revised out the 1 per cent rise shown earlier by the advance figures.) Sales at general merchandise stores rose in June with sales at department stores up 2 per cent. Sales at food stores were about unchanged and sales at other types of nondurable goods stores were down from 1 to 2 per cent. Nondurable goods sales in the April-June quarter were 1.4 per cent higher than in the first quarter.

QUARTERLY CHANGES IN RETAIL SALES
(Per Cent)

	1966	1967	
	IV	I	II
All retail stores	- .1	.5	1.4
Durable goods stores	-1.1	-1.1	1.4
Furniture and appliances	- .5	2.0	-1.1
Nondurable goods stores	.3	1.2	1.4
Apparel and general merchandise	- .1	.6	3.6

Construction activity. Value of new construction activity edged up further in June and was only slightly below the declining rate a year earlier, based on confidential projections now available from the Census Bureau and on revised data back to January 1963, which will be published shortly.^{1/}

^{1/} The revisions affect virtually all component series, but their effect on the level and general pattern of movement of the annual data was minor both for the total and the major groups. For the year 1966--where the revision was most pronounced--residential construction expenditures were reduced by 3 per cent from the already low level estimated earlier, but private nonresidential and public construction outlays were raised by 2 and 1 per cent, respectively.

As in other recent months, a feature of the rise in June was a further recovery in outlays for residential construction, reflecting in part the sharply higher rate of starts registered in May. Nonresidential construction expenditures, already appreciably below earlier peaks, changed little. Public construction, which was under special administrative as well as other restraint at this time last year, apparently moved higher.

NEW CONSTRUCTION PUT IN PLACE
(Confidential FRB)

	June 1967 (\$ Billions) ^{1/}	Per cent change from	
		May 1967	June 1966
Total	73.2	+1	- 2
Private	46.5	+1	-10
Residential	22.3	+2	-10
Nonresidential	24.1	--	- 9
Public	26.8	+1	+16

^{1/} Seasonally adjusted annual rates; preliminary. Data for the most recent month (June) are available under a confidential arrangement with the Census Bureau. Under no circumstances should any public reference be made to them.

Data on housing starts for June are not yet available; and, according to present Census plans, the June data will be accompanied by revisions, back to 1960 for the seasonally adjusted series. In terms of the currently published series, however, starts in June are expected to hold fairly near the sharply improved annual rate of 1.31 million units reached in May. This would bring the second quarter average moderately above the 1.21 million rate in the first quarter and would leave the

rate for the first half as a whole at or slightly above the current Census total of 1.22 million for the year 1966.

The ability of builders to raise unadjusted starts through the spring months at or above a normal seasonal pace indicates that a substantial amount of momentum in housing activity has been regained. Furthermore, figures available through May indicate that commitments from lenders also have increased significantly. This suggests that the recent further tightening in financial markets, discussed in the section on mortgage market developments and elsewhere, may not appreciably moderate further expansion in starts during the current quarter.

New and unfilled orders. Manufacturers' new and unfilled orders, shipments, and inventories all rose in May. New orders for durable goods rose 7.5 per cent, following a rise of .7 per cent in April; they are now only 5 per cent below their peak last September, just before suspension of the investment tax credit and accelerated depreciation.

For steel, motor vehicles and aircraft, the May gains were very sharp. Also significant was the continued rise in machinery and equipment orders which were 8.5 per cent above their February low.

The rise in new orders in May was accompanied for the first time this year by a rise in unfilled orders. Most of the May increase was for aircraft and parts and this raised their backlogs to a new high. For defense products, which includes aircraft and parts, unfilled orders were higher in May than at any time since the series began in 1952. Backlogs for iron and steel also increased appreciably.

Inventories. Inventory building in manufacturing in May was sharply reduced as stocks rose only \$250 million (book value). This increase, equivalent to an annual rate of \$3.0 billion, compares with a rate of \$7.2 billion in the first quarter and a high of \$12.1 billion in the final quarter of last year. Defense products accounted for a substantial proportion of the addition to durable goods inventories. For nondurable goods, the May increase was quite small, amounting to only \$50 million.

Stronger demands were also reflected in increased shipments in May. Especially large gains occurred in durable goods industries. In nondurable goods industries shipments rose slightly. With shipments up more than inventories, stock-sales ratios declined, although stock-sales ratios continued high for nearly all durable goods and most nondurable goods industries.

Inventories held by distributors declined nearly \$200 million in book value in May, following a decline of \$370 million in April. In May stocks were liquidated at both durable and nondurable goods wholesalers and at durable goods retailers, but were increased at nondurable goods retailers. The combined April-May reduction in distributors' stocks was more than twice as large as the total reduction in the first three months of the year. In the earlier period nearly all of the liquidation occurred at auto dealers, while in the more recent months wholesale establishments participated in the reduction. At wholesale establishments in both durable and nondurable goods lines, inventories continue high relative to sales. But at the retail level, inventories-sales ratios for both durable and nondurable goods are not out of line with those of other recent years.

Labor market. After declining for two months, employment turned around in June and gains should accelerate further in the current quarter as the pace of real output steps up. A rise of 150,000 in non-farm employment in June brought the level almost back to the March peak. Especially significant were the increases--although small--reported in

manufacturing and construction employment, which had been declining earlier this year. Hours of work in manufacturing, however, declined somewhat further; in contrast, the workweek in construction rose substantially, in part reflecting improved weather conditions in June.

As expected, there was an exceptionally large influx of workers into the labor force in June. The seasonally adjusted increase of 900,000 in the month, reversed the downward tendencies which were reported in previous months and brought the civilian labor force up to 77.2 million, about 1.6 million more than a year ago. In addition, the armed forces have absorbed about 350,000 young people, so that the total labor force is now 1.9 million larger than last June. This is a much larger increase than would be anticipated solely from population growth in the working age groups.

Almost all of the large June increase in the labor force was absorbed into gainful employment. However, the unemployment rate rose to 4.0 per cent, slightly above the May level of 3.8 but still close to the narrow range of the past year and a half. The rise during the month was almost entirely accounted for by an increase in unemployment among adult women looking for seasonal work. Among adult men, there was also a slight rise in unemployment in June and their rate is somewhat higher than earlier this year, with a rise among semi-skilled and unskilled workers in manufacturing and construction accounting for the higher levels. Youths (students and graduates) entering the labor force at the end of the school year generally found jobs, and the unemployment rate for the group showed little change. This marks the third successive

year that the very large number of young people entering the labor market in the summer have, on the whole, successfully found jobs, attesting to the continued underlying strength in demand for labor. (On an unadjusted basis, almost 2-1/2 million youths 16-19 entered the labor force and found jobs in June.)

Nonfarm employment. With reductions in manufacturing and construction employment is no longer offsetting the continuing substantial gains in services and government activities, total nonfarm employment rose in June. In manufacturing, employment increased by 30,000 in June but was still 300,000 below the January peak level. The relatively moderate June increase occurred despite a strike in the electrical equipment industry which reduced employment by 40,000. Moreover, some 50,000 rubber workers continued on strike. The decline from the January peak thus includes at least 90,000 workers on strike.

In the durable goods industries, autos, aircraft, fabricated metals and machinery showed some strength in June, but employment continued to ease in primary metals, lumber and furniture. In nondurable goods lines, increased demands for workers appeared to be more widespread with almost all industries showing gains. Employment even rose in the textiles and chemicals industries, which have a substantial inventory overhang.

Although manufacturing employment expanded somewhat, the workweek eased further to 40.2 hours and was about an hour below a year ago. The apparent contradictory performance of hours and employment can be explained in part by: (a) further attempts of employers to cut costs by reducing overtime at premium pay while at the same time rehiring laid-off workers; (b) an inadequate seasonal adjustment--the seasonally adjusted workweek has declined by .2 hours in June of each of the past three years; (c) industries reporting lower hours of work were mainly in durable goods industries where inventory adjustments are still underway.

CHANGES IN NONAGRICULTURAL EMPLOYMENT
(In thousands)

	June 1966 to June 1967	June 1966 to Dec. 1966	Dec. 1966 to June 1967
Total	1,582	1,093	489
Industrial	-78	318	-396
Manufacturing	-14	278	-292
Mining	-12	-6	-6
Construction	-145	-7	-138
Transportation and public utilities	93	53	40
Nonindustrial	1,660	775	885
Trade	379	175	204
Service	602	303	299
Government	679	297	382
Federal	159	58	101
State and local	520	239	281

Notwithstanding the easing in industrial employment over the past half year, demands for labor have continued strong in the service and government sector. While industrial employment was falling by about 400,000, gains in nonindustrial activities totaled almost 900,000. In fact, the increase in the latter group was somewhat larger than over the previous half year. Recent gains in trade and service employment were about in line with earlier trends but expansion in government employment accelerated.

The expansion of close to 1.7 million in nonindustrial employment over the past year was about equal to the growth in the civilian labor force. Taken together with demands of the armed forces in the period, it becomes clear why sluggishness in industrial employment has had relatively little impact on aggregate unemployment.

 DOMESTIC FINANCIAL SITUATION

Bank credit. Bank credit expansion during June was moderated by sizable bank liquidation of Treasury securities during the last statement week of the month. As a result, the all commercial bank credit series, calculated from last Wednesday to last Wednesday of the month, showed an increase of only about 1 per cent annual rate. The credit proxy for member banks, based on daily average figures and adjusted to include borrowing from foreign branches, is less influenced by end-of-month developments and showed a rate of growth of almost 10 per cent.

The disparity between these two series in any one month is reduced when a longer time span is considered. As indicated in the table, both series show about an 11 per cent rate of growth of bank credit during the first half of 1967, with much slower growth in the second quarter when Treasury deposits were declining.

COMMERCIAL BANK CREDIT
Seasonally adjusted annual rate
(per cent)

	1967			
	June	1st Half	2nd Qtr.	1st Qtr.
Adjusted credit proxy ^{1/}	9.7	11.0	7.6	14.1
All commercial bank ^{2/}	1.1	10.6	6.0	15.1

^{1/} Daily average of total member bank deposits plus change in liabilities to overseas branches.

^{2/} All commercial banks, last Wednesday of month series.

Substantially all of the \$1.1 billion liquidation of Treasury securities by banks during June reflected reduced holdings of Treasury bills, presumably for the most part tax bills maturing on June 22. Bank acquisitions of other securities, while sizable in June, were considerably less than those of other recent months.

COMPONENTS OF COMMERCIAL BANK CREDIT
 Seasonally adjusted annual rate
 End-of-month series
 (per cent)

	1967			
	June	1st Half	2nd Qtr.	1st Qtr.
Total loans & investments	1.1	10.6	6.0	15.1
U.S. Gov't. securities	-22.9	8.1	-9.0	25.8
Other securities	17.4	29.6	27.5	29.6
Total loans	2.8	6.9	4.7	8.9
Business loans	17.7	11.5	10.9	11.8

The reason for the slower pace of acquisitions is not clear, but may be related to bank expectations of further rate increases. Moreover, in May many banks lengthened their portfolios by acquiring Treasury securities in a refinancing. If, as a result, they temporarily moderated this purchase of municipals, June deliveries of such securities would have been reduced.

Business loans expanded by \$1.2 billion in June, with virtually every industry category showing heavy loan demands over the tax and dividend period. An unusually small share of tax bills was turned in for tax payments, suggesting that the build-up of corporate

liquid assets over the spring was neither large nor broadly distributed among firms. Thus, the record June corporate income tax payments of \$9.2 billion were translated into substantial, but probably temporary, demands for bank loans by nonfinancial businesses.

Loans to nonbank financial institutions showed only modest increases in June--either because of small tax period maturities of finance company paper or the ease with which such maturing paper could be quickly refunded. Loans to security dealers declined, mainly as the result of a sizable reduction in Government security dealer positions in June. Consumer and real estate loans continued to increase by modest amounts.

Bank deposits. Net inflows of time and savings deposits in June, on a daily average basis, were at an annual rate of over 16 per cent--somewhat more than in May. As in other recent months, the combined inflows to passbook savings accounts and time deposits other than

TIME AND SAVINGS DEPOSIT INFLOWS, WEEKLY REPORTING BANKS
(Millions of dollars, not seasonally adjusted)

	June <u>1/</u>			
	1967	1966	1965	1964
Total time and savings deposits	+1,019	+573	+882	+ 12
Negotiable CD's	+ 84	- 4	+270	-244
Other time <u>2/</u>	+ 481	+566	- 39	- 71
Savings	+ 454	+ 11	+591	+327
Memo: Other time <u>2/</u> plus savings	+ 925	+577	+552	+256

1/ Four weeks ended June 28, 1967; June 29, 1966; June 30, 1965; July 1, 1964.

2/ Other than large negotiable CD's.

negotiable CD's for weekly reporting banks--shown in the last line of the table--were very large. By late June and early July, when most banks credit interest payments, there had as yet been no indications of shifts out of such deposits into market securities.

Heavy loan demands and efforts of banks to obtain funds before the anticipated rise in short-term interest rates, led to increases of offering rates on negotiable CD's of $1/8$ to $3/8$ of a percentage point in June. These increases carried typical CD rates 12 to 75 basis points above their April lows. With yields on most money market assets unchanged to only somewhat higher until late in June, the yield advantage of newly issued negotiable CD's rose to record levels, a dramatic change from the generally noncompetitive rates posted in April.

These attractive offering rates permitted banks not only to replace very large CD maturities in June, but also to increase outstandings by about \$85 million--a good performance for a month with large tax and dividend maturities. The increase in outstandings was particularly sharp when consideration is given to the tax payments that have apparently limited corporate funds available for short-term investment. Indeed, the difficulty in obtaining corporate time deposits probably was a major factor in the increase in CD rates since April. During the spring, essentially all of the increase in outstanding CD's has occurred among holders other than individuals, partnerships, and corporations. Earlier in the spring, the increase of "other" holders was thought to be mainly among States and political subdivisions; more recently it has probably been centered in acquisitions of foreign government.

Despite record tax inflows in June, Treasury balances at banks continued to decline sharply, particularly in the last reporting week of the month when \$3.5 billion of tax bills were turned in for cash. These declining balances contributed to a sharp June increase in the money stock, which for the second consecutive month, expanded at an annual rate of more than 13 per cent. Although these increases brought the first half annual rate of growth in money balances to 6.7 per cent, the money stock in June was only about 3 per cent above year-ago levels. Much of the expansion since late last year has reflected rebuilding of cash balances from the very low levels to which they were drawn down in the summer and fall of 1966.

Corporate and municipal bond markets. During the latter part of June, yields on new corporate bonds rose to their highest level in over 45 years, slightly above the August 1966 peak. The corporate new issue series does not reflect this peak, however, due to a shift in the characteristics of the issues included in the series. But issues offered at these record yield levels experienced an excellent reception, and most recently corporate new issue yields have dropped back from their highs. In the municipal market, on the other hand, new issue yields advanced less sharply in June and have not shared in the recent yield declines of other bond markets,

BOND YIELDS
(Weekly averages, per cent per annum)

	Corporate Aaa		State and local Government	
	New With call protection	Seasoned	Moody's Aaa	Bond buyer's (mixed qualities)
<u>1965</u>				
End of July ^{1/}	4.58	4.48	3.16	3.25
Early December ^{2/}	4.79	4.60	3.37	3.50
<u>1966</u>				
Late summer high	5.98*	5.44	4.04	4.24
<u>Weeks ending:</u>				
February 3 ^{3/}	--	5.02	3.25	3.40
March 31	5.21*	5.12	3.46	3.54
June 9	5.70*	5.37	3.76	3.90
June 30	5.92*	5.57	3.85	4.06
July 7	5.86*	5.59	3.85	4.07

^{1/} Week prior to President's announcement of increased U.S. involvement in Vietnam.

^{2/} Week preceding Federal Reserve discount rate increase.

^{3/} 1967 low.

* Some issues included carry 10-year call protection.

The decline in corporate yields over the past two weeks has occurred in both recently offered issues and new issues. Among the recently offered issues, two Aaa-rated utility issues with 5-year call protection--Boston Edison Company and Illinois Bell Telephone Company initially offered to yield investors 6 per cent in late June--are now trading at more than 20 basis points below their reoffering yields. Similarly, an Aa-rated gas company issue last week was priced 20 basis points below a comparable issue brought to market only two weeks ago. The sharp advance in yields appears to have been an over-discounting of market pressures, and the recent turnaround, in part, constitutes a realization of this by market participants.

Accompanying the sharp corporate yield advance in June were record-breaking offerings. Estimated public bond offerings totaled \$1.65 billion in June, slightly exceeding the previous record established in March. (Not included in this June estimate are two large rights offerings which expire in July, and account for the larger June total shown in other published data.) The volume of public bond offerings during the first half advanced to more than \$7.2 billion, an all-time high and nearly double the previous record volume of such issues offered during the first half of 1966. While total bond and stock offerings in June, and for the first half, showed a smaller margin of increase over a year ago--with both private placements and stocks in smaller volume--gross funds raised with bonds and stocks of all types aggregated an estimated \$11.7 billion in the first half, \$1.5 billion more than in the like period of 1966.

The June record for public debt offerings will most likely be short-lived, as July offerings are now estimated at \$1,750 million, \$100 million more than in June. Included in this total are convertible offerings aggregating \$500 million. Even though private placements and stock offerings in July are projected in lower volume than a year earlier, total bond and stock offerings still are expected to amount to \$2,300 million--more than double the July 1966 volume. And public bond offerings for August may ultimately reach \$1,300 million, exceeding the previous record August calendar of last year.

CORPORATE SECURITY OFFERINGS^{1/}
(Millions of dollars)

	Bonds				Total bonds and stocks	
	Public offerings ^{2/}		Private placements		1967	1966
	1967	1966	1967	1966	1967	1966
1st Quarter	3,263	1,774	1,811	2,586	5,464	5,094
2nd Quarter	3,975e	1,941	1,750e	2,083	6,250e	5,115
June	1,650e	832	550e	784	2,475e	2,427
July	1,750e	440	450e	535	2,300e	1,085
August	1,300e	1,140	450e	435	1,850e	1,712

^{1/} Data are gross proceeds.

^{2/} Includes refundings.

The volume of municipal security offerings in June ranked with the other \$1.4 billion months of January and March of this year. This volume raised gross municipal issues during the first half to an estimated \$7.6 billion, more than 20 per cent above the like period of 1966. It now appears that July will be the seventh consecutive month in which municipal offerings will exceed \$1 billion. And since new issues in the latter half of June did not generally experience an enthusiastic reception, dealers entered July with some excess inventories. New issue volume in August will probably be under the \$1.0 billion mark, however, reflecting a tendency toward seasonal lull and the fact that a number of large and frequent borrowers--such as the State of California, New York City, and the Public Housing Administration--will already have been in the market in either June or July.

STATE AND LOCAL GOVERNMENT BOND OFFERINGS
(Millions of dollars) 1/

	1967	1966
1st Quarter	4,112	2,964
2nd Quarter	3,529e	3,256
June	1,400e	1,143
July	1,100e	702
August	950e	775

1/ Data are for principal amounts of new issues.

Flows to nonbank intermediaries. Savings flows to nonbank depositary-type intermediaries continued in record volume during June, as the table shows. While the rate of growth in net inflows slackened a bit relative to preceding months, for all three months of the second quarter the rate of growth (at a seasonally adjusted annual rate) was 11 per cent at both S&L's and mutual savings banks, which compares with growth rates of 2.0 per cent and 2.4 per cent, respectively, for the second quarter of 1966.

SAVINGS FLOWS TO NONBANK INTERMEDIARIES
(Millions of dollars) 1/

	S&L's	Savings Banks
<u>June</u>		
1967	\$1,821	600 ^{2/}
1966	1,184	224
1965	1,603	436
1964	1,751	478
1963	1,631	395
<u>Year to date</u>		
1967	5,862	2,707
1966	2,088	784
1965	4,190	1,684
1964	5,410	1,934
1963	6,143	1,537

1/ Data include interest credited which typically amounts to about 75 per cent of the total.

2/ Federal Reserve estimate.

As they moved into the July reinvestment period, spokesmen for the thrift industry were generally not anticipating any serious increase in gross withdrawals, despite the high level of long-term market rates and the rapid recent advance of short-term rates. Officials at California S&L's were less sanguine about this outlook, however, because of the recent Home Loan Bank Board action which reduced the California passbook rate to 5 per cent from 5-1/4 per cent, and eliminated the 5-1/4 per cent certificate option for any S&L's paying the 5 per cent passbook rate. Preliminary reports from the California State chartered S&L's for the first week of July indicate that this concern was probably well founded although details on the size of the net outflow is not yet available. Thus far, the only data available from other parts of the country are for the 15 largest savings banks in New York City, which continued to experience a record net inflow during the first 10 days (5 business days) of July as indicated in the table.

EARLY JULY SAVINGS FLOWS AT NEW YORK CITY'S
15 LARGEST MUTUAL SAVINGS BANKS
(Millions of dollars)

First 5 business days of July	Savings Deposits
1967	+56.0
1966	-31.1
1965	- 9.5
1964	+ 7.4

Mortgage market developments. With further increases in bond yields in June, there were widespread additional price reductions in the secondary market for Federally-underwritten mortgages, accompanied in numerous areas by somewhat more restrictive rate and nonrate terms in the primary market, according to reports from FNMA and VA field offices. These developments imply that the sensitive official secondary-market yield series on FHA home mortgages will show a rise for the second consecutive month when it becomes available for June. In May these had turned up by 15 basis points, after 5 months of decline and this had been associated with an upturn of about 5 basis points for the FHA series on conventional loans.

Yields on FHA loans, however, undoubtedly increased less during June than yields on corporate bonds. Competition from some conventional-mortgage lenders, such as savings and loan associations, has apparently continued to limit the rise in yields required by lenders on Federally-underwritten mortgages. The yield spread favoring home mortgages over bonds thus has remained unusually low, and has contributed to some further reduction in the availability of home mortgage credit and to growing market uncertainty in an increasing number of areas.

The reduced relative attractiveness in recent months of home mortgages in general--which are subject to more restrictive Federal and State interest-rate ceilings than are higher-yielding business-type mortgages secured by multifamily and commercial properties--has accounted in part for lessened interest of diversified lenders in these investments, and has further dampened the longer-run outlook for 1- to 4-family construction.

As secondary-market prices for FHA and VA loans declined again last month, there was a sharp increase in offerings of these mortgages to FNMA for purchase under its unchanged price schedule. Offerings of about \$200 million--the largest monthly volume since early last year--were reportedly bolstered by market anticipations that FNMA would soon announce a cut in its buying prices.

Stock market. The Standard & Poor's composite index of 500 stocks traded on the New York Stock Exchange closed at 92.48 on July 11, two per cent below its early May peak. The decline took place in May, and the index subsequently has been fluctuating within a narrow range. The composite index, however, has not reflected the speculative interest which seems to have developed. One indication of such interest is that Standard & Poor's index of low priced stocks has advanced to a new record high recently, sixty per cent above its 1967 low. On the American Stock Exchange, average prices also have risen recently to an all-time high.

Moreover, on the American Exchange, monthly share volume in June exceeded 100 million for the first time in history. Although the New York Stock Exchange monthly volume--at 228 million shares--was also high in June, trading on the American Exchange was almost as large a proportion of New York Stock Exchange volume as at the April 1966 speculative peak.

Between mid-May and the end of June, 100 per cent margin requirements were imposed by the American Exchange on 11 separate issues.

Of these, 6 issues were added to the list during the last week in June, and 15 more issues have been added thus far in July, making the total number now affected 26. On 17 occasions in June, openings were delayed on the American Exchange, and 9 times trading in certain issues had to be halted to preserve an orderly market.

Although margin panel data are not available for June, May statistics showed an increase of \$59 million in customer credit extended by banks and New York Stock Exchange member firms--the fourth increase in as many months. Over the four months, total customer credit rose \$334 million, an increase cancelling about three-fourths of the July-October decline.

U. S. Government securities market. Treasury bill rates rose very sharply in late June and early July, moving above the discount rate for the first time since February. Yields on Treasury notes and bonds advanced further in the second half of June, but subsequently declined as the market rallied.

YIELDS ON U. S. GOVERNMENT SECURITIES
(Per cent)

Date (closing bids)	3-month bills	6-month bills	3 years	5 years	10 years	20 years
<u>1966</u>						
High	5.59	5.94	6.22	5.89	5.51	5.12
<u>1967</u>						
High	4.85	4.92	5.12	5.36	5.22	5.11
Low	3.33	3.71	4.27	4.38	4.45	4.44
June 1	3.40	3.73	4.57	4.72	4.81	4.83
20	3.55	3.83	5.07	5.17	5.14	5.08
23	3.33	3.83	5.00	5.15	5.14	5.08
July 3	4.10	4.50	5.12	5.36	5.22	5.07
11	4.22	4.69	5.00	5.22	5.09	4.95

The recent upsurge in Treasury bill rates was triggered in late June by the announcement of large Treasury cash financings totaling \$6.2 billion, including the auction of \$4.0 billion of March and April tax bills on July 5. The financing "package" also included \$100 million additions to weekly 3-month and to monthly 1-year bill auctions and was recognized to be but a beginning towards meeting the Treasury's very large second half cash needs. Close market observers generally expect the Treasury's total cash requirements to range from \$15 billion to \$20 billion over the second half of the year, up from \$10 billion in the second half of 1966 and much smaller amounts in other recent years. Our own projections indicate a gross cash need of around \$18 billion in the second half of 1967.

At the higher yield levels, sizable market demand for bills developed and this demand was supplemented by large System purchases to help meet seasonal reserve needs around the turn of the month. Higher bill rates also stimulated bank bidding for the new tax bills, which were being offered with 100 per cent Treasury tax and loan account privilege, and bank sales of the new bills following the auction have been relatively light thus far. As a result of these developments, dealer bill inventories were reduced to quite low levels, especially in bills maturing in three months or less.

The steadier tone which developed in the Treasury bond market in early July seemed to be related in part to the improved atmosphere in the corporate bond market where high yields on recent new issues attracted good investor interest. In addition, sizable buying

of coupon issues by official accounts in recent weeks, especially by the System, has served to reduce dealer inventories in notes and bonds to very low levels. As of July 10, dealers as a group actually had net short positions of \$9 million in bonds maturing after 5-years and a relatively light \$106 million of securities maturing in 1 to 5 years.

Yields on short-term market instruments other than Treasury bills have been under upward pressure for several weeks, but over the last two weeks have risen much less than bill rates.

SELECTED SHORT-TERM INTEREST RATES

	1967		July 10
	High	Low	
Commercial paper 4-6 months	6.00(1/16)	4.63(6/26)	4.75
Finance company paper 30-89 days	5.88(1/5)	4.25(5/24)	4.75
Bankers' Acceptances 1-90 days	5.50(1/10)	4.25(6/6)	4.50
Certificates of deposit (prime NYC)			
Most often quoted new issue:			
3-months	5.50(1/20)	4.13(5/5)	4.75
6-months	5.50(1/13)	4.13(4/28)	5.00
1-year	5.50(1/13)	4.13(4/14)	5.13
Secondary market:			
3-months	5.59(1/13)	4.35(4/28)	4.90
6-months	5.68(1/6)	4.36(4/14)	5.20
Federal Agencies (Secondary Market):			
3-months	5.05(1/6)	3.82(5/26)	4.50*
6-months	5.19(1/13)	4.11(5/19)	4.85*
1-year	5.20(7/7)	4.18(4/7)	5.20*
Prime Municipals 1-year	3.45(1/6)	2.40(4/14)	3.00*

N.B. Latest dates on which high or low rates occurred are indicated in parentheses.

* Rates on July 7.

Treasury finance. With the completion of the \$4.0 billion tax bill financing, the Treasury's next major financing will be the regular August refunding. The terms of this refunding are expected to be announced on July 26. Public holdings of the issues maturing in mid-August are a moderate \$3.6 billion. Given favorable market conditions, many market participants expect the Treasury to offer an issue in the intermediate-term maturity area in this refunding. Under recently enacted legislation, the Treasury could bring to market a note with a maturity as long as 7 years which would be exempt from the 4-1/4 per cent interest rate ceiling.

It is currently anticipated that the Treasury will need to re-enter the market very shortly after the August refunding to raise additional new cash, perhaps as much as \$3 billion to \$4 billion. The payment date for this financing will have to be scheduled to meet a seasonal low in Treasury balances around the second week of September.

Federal budget. Fiscal 1967 budgetary figures shown on the accompanying table are still preliminary and final figures will not be reported until later this month. Revised fiscal 1968 budget projections are expected to be released by the Bureau of the Budget within two or three weeks in keeping with a request of the Joint Economic Committee. These figures will indicate larger deficits than those shown in the table below for fiscal 1968 taken from the January budget document. (Our projection for the July-September 1967 quarter shown in the table is consistent with a considerably larger fiscal 1968 cash deficit than that indicated in the January Budget document.)

VARIOUS FEDERAL BUDGETS
(In billions of dollars)

	Calendar 1966				Calendar 1967			Fiscal Year		Jan. Budget Document	
	I	II	III	IV	I	II E	III E	1966	1967 E	Fy1967	Fy1968
<u>Quarterly data, unadjusted</u>											
Cash surplus/deficit (-)	- 1.3	10.0	- 6.7	- 7.7	1.4	9.2	- 6.2	- 3.3	- 3.9	- 6.2	- 4.3
Cash receipts	33.3	46.2	34.6	31.1	38.0	49.4	36.3	134.5	153.1	154.7	168.1
Cash payments	34.6	36.2	41.3	38.8	36.7	40.2	42.5	137.8	157.0	160.9	172.4
Change in total cash balances	- .1	+6.6	- 4.1	- 2.5	+ .7	+ .3	3.4	- .1	- 5.6	- 3.4	--
Net cash borrowing (+)	+1.0	-3.7	+ 2.4	+ 5.1	- .9	- 9.1	8.2	+ 2.6	- 2.5	+ 1.7	+ 3.8
(Pool sales to public) <u>1/</u>	.4	1.8	--	--	1.1	1.9	.6	3.1	3.0	3.1	5.0
<u>Seasonally adjusted annual rate</u>											
Federal surplus/deficit (-) in national income accounts	2.3	3.8	- .5	- 3.6	-10.3	-13.5	-11.4	+ 0.3	- 7.0	- 3.8	- 2.1
Receipts	136.0	141.0	145.3	147.9	149.2	148.3	154.2	132.6	147.7	149.8	167.1
Expenditures	133.7	137.1	145.8	151.5	159.5	161.8	165.6	132.3	154.7	153.6	169.2
High employment surplus/deficit (-) <u>2/</u>	1.5	4.1	- .2	- .6	- 8.3	- 9.1	- 8.7	2.1	- 4.6	n.a.	n.a.

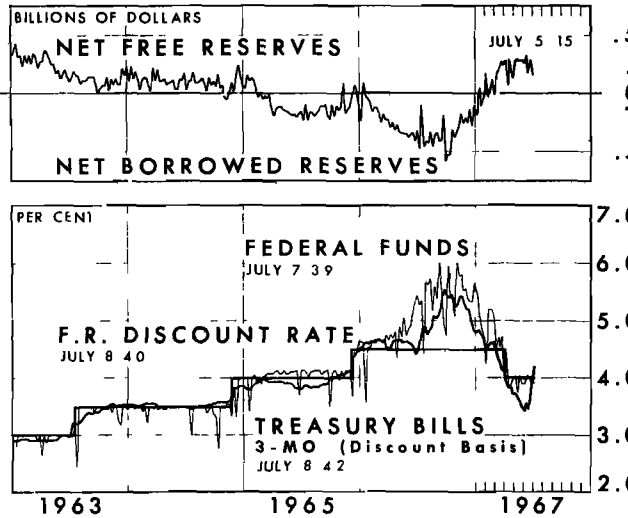
E - staff projections.

1/ Not included in net cash borrowing.

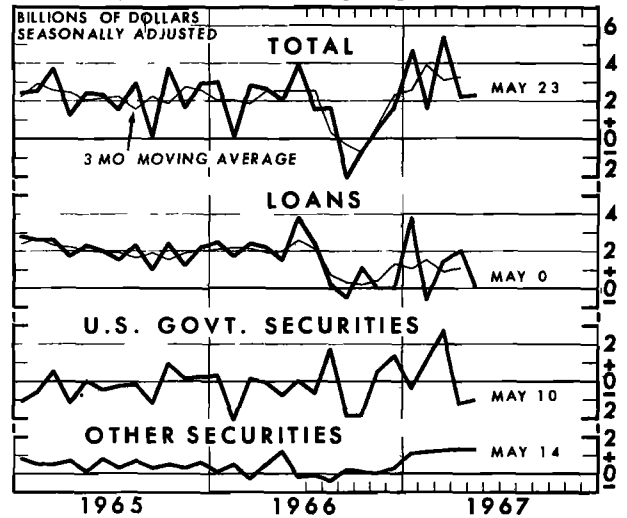
2/ Uses 1966 IVQ as a high employment base.

FINANCIAL DEVELOPMENTS - UNITED STATES

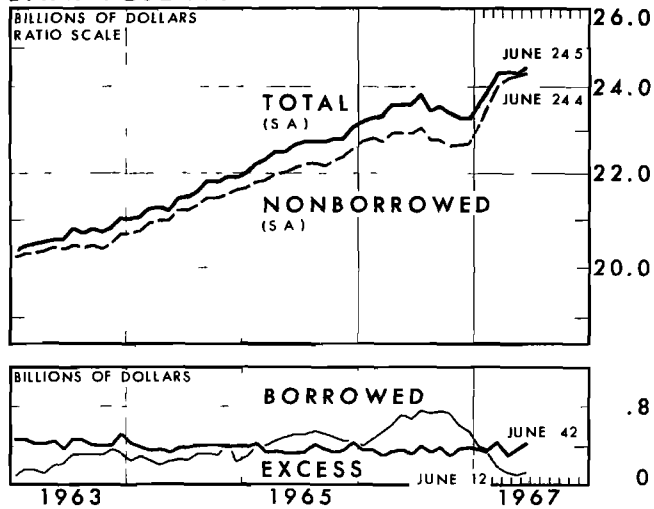
FREE RESERVES AND COSTS



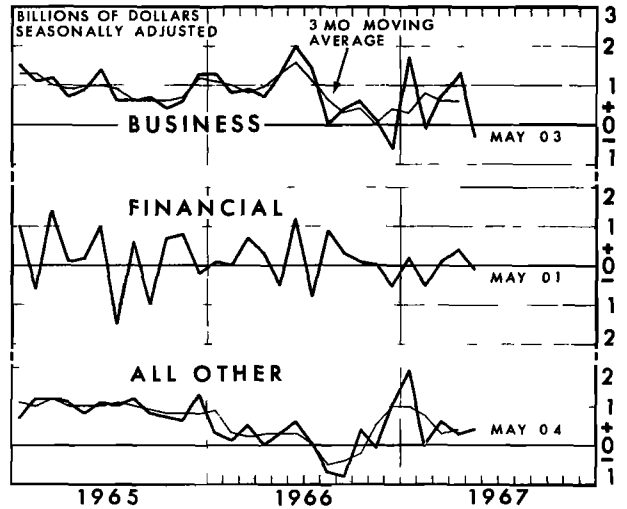
CHANGES IN BANK CREDIT



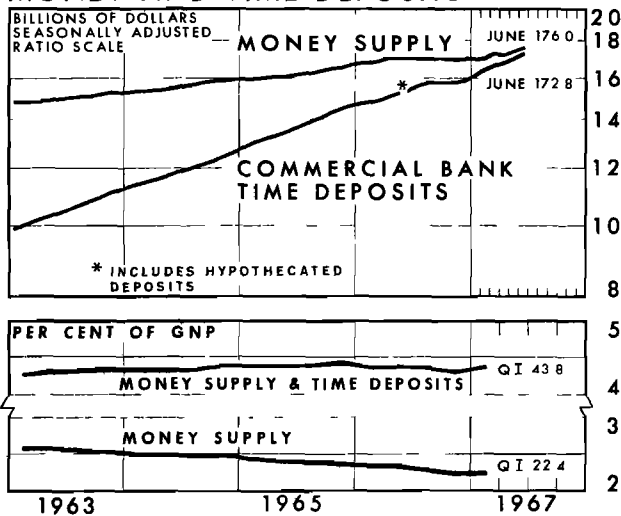
BANK RESERVES



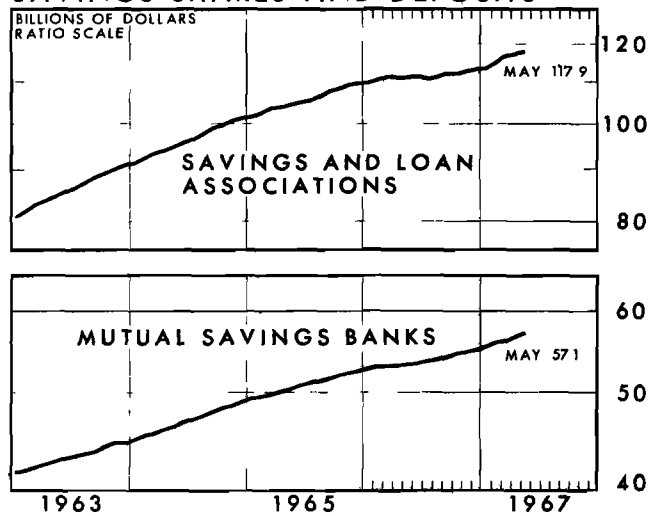
CHANGES IN BANK LOANS-BY TYPE



MONEY AND TIME DEPOSITS

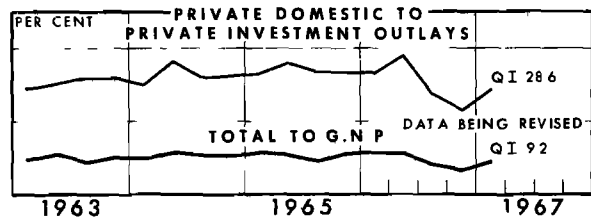
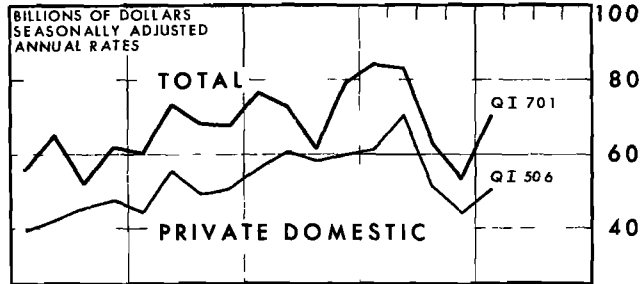


SAVINGS SHARES AND DEPOSITS

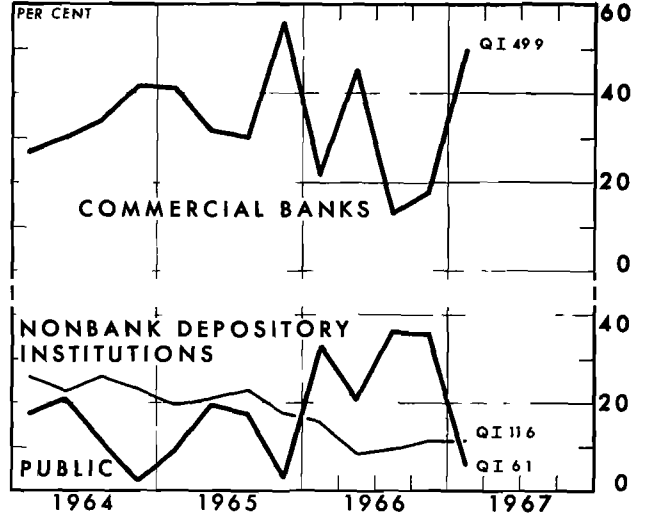


FINANCIAL DEVELOPMENTS - UNITED STATES

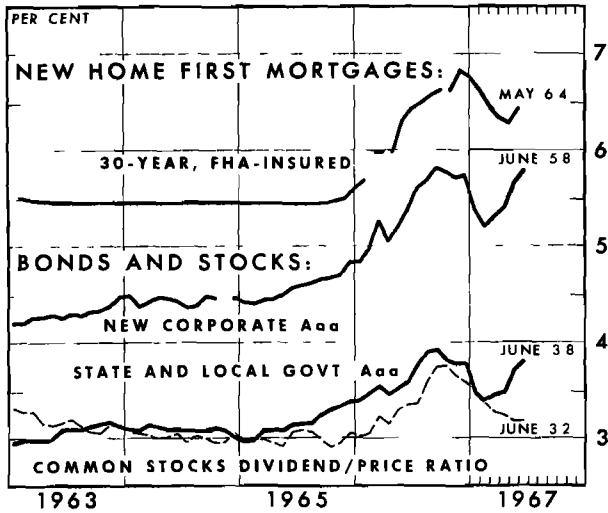
NET FUNDS RAISED - NONFINANCIAL SECTORS



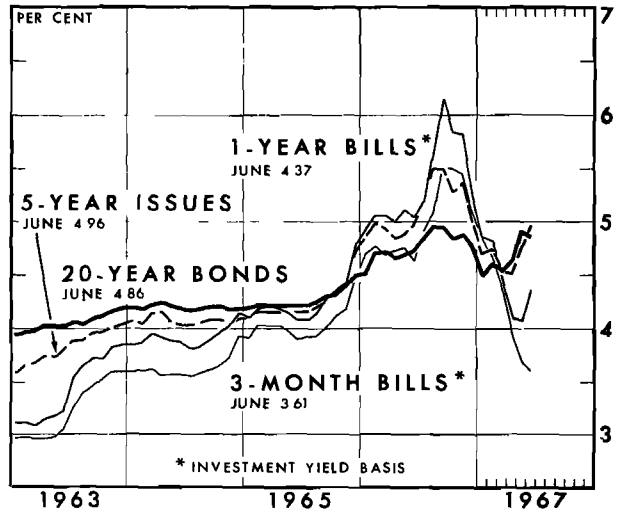
SHARES IN TOTAL CREDIT



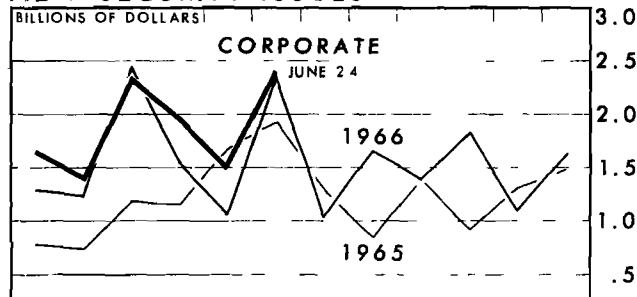
MARKET YIELDS



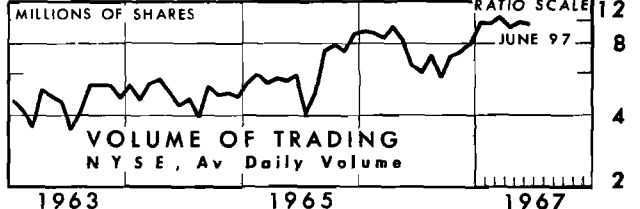
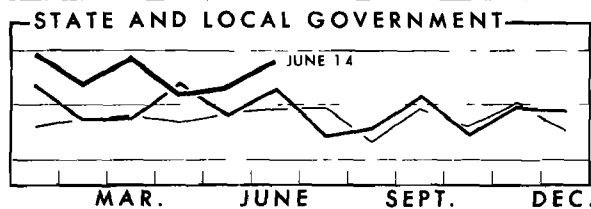
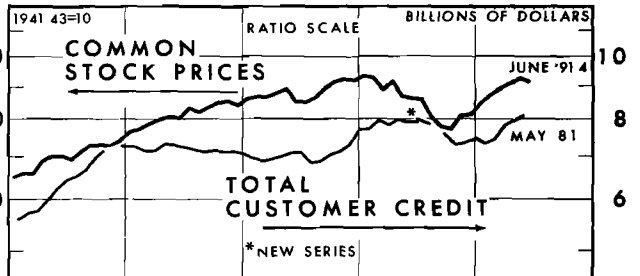
MARKET YIELDS—U.S. GOVT. SEC.



NEW SECURITY ISSUES



STOCK MARKET



INTERNATIONAL DEVELOPMENTS

U.S. balance of payments. Data for the second quarter (still partial for June) show a continued heavy liquidity deficit, greatly exceeding the large first-quarter deficit when both are adjusted to eliminate the effects of special receipts. Such U.S. receipts, primarily from official foreign purchases of long-term CD's and other non-liquid obligations, were especially large at the end of June, and will greatly reduce the published liquidity deficit for the quarter.

In April and May combined the liquidity deficit was \$502 million (before seasonal adjustment), after counting receipts of \$160 million from the sale of long-term CD's and about \$85 million from purchases of bonds of U.S. Government agencies by international institutions. It now appears that very large receipts at the end of June may have resulted in a surplus on the liquidity basis for the month on the order of \$200-300 million. Special receipts of about \$450 million which contributed to this result are shown in Table 1. In addition, there were receipts on military account from Germany totaling over \$200 million in May and June, part of which would be matched by current deliveries.

The estimate of the June surplus is highly tentative since at present only incomplete weekly figures are available and they include a reported surplus of over \$500 million in the week ended July 5, which has to be distributed between June and July.

If special receipts of the types shown in table 1 are not counted, the liquidity deficit appears to have deteriorated sharply

Table 1. Measures of the balance on international transactions, and special receipts, Jan.-June 1967
(in millions of dollars)

	1 9 6 7				Total Q-2, est.
	Q-1	Apr.	May	June (est.)	
Liquidity deficit (-), N.S.A.	-243	-336	-166	+300	-202
Seasonal adjustment	-301	--	--	--	-270
Liquidity deficit, S.A.	-544	n.a.	n.a.	n.a.	-472
Special receipts <u>1/</u>					
Investments by foreign official agencies in long- term deposits and CD's	+306	+124	+39	+440 ^{3/}	+603
Investments by international organizations in long-term deposits or U.S. Govt. agency bonds <u>2/</u>	+57	+70	+15	n.a.	+85
Advance retirement of Canadian bonds	--	--	--	+31	+31
Net U.K. transactions in U.S. securities (other Treasury issues)	-23	-3	+66	n.a.	+63
Total	+340	+191	+120	+471	+782
Liquidity deficit not reduced by special receipts, N.S.A.	-583	-527	-286	-171	-984
" ", S.A.	-884	n.a.	n.a.	n.a.	-1,254
Official settlements deficit(-), N.S.A.	-1,279	-622	-249	+100	-770
Seasonal adjustment	-543				-100
Official settlements deficit, S.A.	-1,822	n.a.	n.a.	n.a.	-870
Special receipts affecting official settlements balance	-23	-3	+66	+31	+94
Adjusted official settlements balance	-1,799	n.a.	n.a.	n.a.	-964

1/ As in Table A, p. 18, Survey of Current Business, June 1967, except as noted in footnote 2 below.

2/ Before netting out sales of bonds of international organizations in the U.S. amounting to: Q-1, \$52 million; Q-2, \$100.

3/ Includes \$200 million of U.S. Treasury obligations acquired by the Canadian Government.

from \$900 million in the first quarter to \$1-1/4 billion in the second quarter. The major known changes in transactions between quarters were an improvement in the trade surplus from an annual rate of about \$4.0 billion in the first quarter to \$4.8 billion in April-May, more than offset by a shift in bank-reported lending from an inflow of \$70 million in the first quarter to an outflow of about \$175 million in April-May. U.S. purchases of foreign securities appear to have continued at the relatively high first quarter rate. Foreign transactions in U.S. securities, apart from the official transactions mentioned above and dealings in bonds of the special Delaware financing affiliates, showed a larger inflow into corporate stocks in April and May than in the first quarter, but there appears to have been some liquidation of corporate bonds. These securities transactions are discussed in Appendix C.

Very little is known about major factors in the balance of payments for June. Sales of new Canadian bond issues in the U.S. market were relatively high, and transfers of funds to Israel as remittances or bond purchases were probably substantial.

The deficit on the official settlements basis was reduced from \$1.8 billion in the first quarter to probably somewhat less than \$1 billion in the second quarter (this estimate is highly tentative). The major difference in the behavior of the two balances was a large contraseasonal shift in movements of liabilities to foreign commercial banks (including branches of U.S. banks) from a decline of \$750 million (not seasonally adjusted) in the first quarter to a small increase in the second quarter. There is normally a sizable seasonal inflow of

foreign commercial bank funds in the first quarter, and outflow in the second, with a swing of over \$400 million between the quarters. It now appears that this outflow was relatively small in April-May and net borrowing was resumed in June.

U.S. foreign trade. The merchandise trade surplus in May held at the high April rate, as both exports and imports fell off. For April and May combined, the trade surplus (on the balance of payments basis) was at an annual rate of \$4.8 billion, compared with \$4.0 billion in the first quarter and \$2.8 billion in the second half of 1966.

Exports in April-May averaged about \$30.8 billion at an annual rate (balance of payments basis), about the same as in the first quarter, but higher than in the fourth quarter of 1966. In contrast to this leveling off in exports, imports in April-May skidded further to an annual rate of \$26.1 billion, 3 per cent below the average of the preceding two quarters.

Both the agricultural and nonagricultural components of exports in April-May showed only minor changes in totals from the first quarter. Shifts occurred, however, in the area distribution of exports. Exports to Western Europe and Japan expanded sharply, while shipments to Latin America and Asia, which had been unusually large in the first quarter, declined. Increased deliveries of automobiles and parts to Canada were instrumental in sustaining total exports to that country at the first quarter rate as other types of exports declined.

The further rise in exports to Japan -- some wheat but largely industrial materials -- probably reflects the strong advance in economic activity there, and continued growth in sales can be expected. The bulk of the recent increase in shipments to Western Europe consisted of machinery and aircraft. Improved supply conditions and shortened delivery schedules in the United States may have facilitated the delivery of equipment ordered previously. In view of current demand conditions in Europe, further substantial gains in exports are unlikely in the months ahead.

Imports of four of the five major categories declined in April-May. Only automotive vehicles and parts increased, buoyed by the continued expansion in arrivals of passenger cars from Canada, which consist, to a considerable extent, of components made in the U.S. Our net export balance on automotive trade with Canada in the first five months of this year was about \$90 million, compared with nearly \$175 million in the corresponding period of 1966.

The downturn in imports of industrial materials has been especially marked for nonferrous metals, reflecting the slowdown in domestic output. Imports of iron and steel products, however, rebounded from the first quarter low to almost the peak levels of the last half of 1966. In contrast, domestic steel output edged downward in April-May.

Imports of machinery, after stabilizing in the first quarter, declined in April-May, possibly reflecting the suspension of the investment tax credit last fall and the general easing in domestic investment outlays. The strong upward movement of the past several

years in nonfood consumer goods (excluding autos) was interrupted in April-May, with imports falling below those of the first quarter. Purchases of imported foodstuffs also slipped in April-May as sugar refiners drew down stocks previously accumulated.

Bank credit. Outflows of short-term bank credit (loans and acceptances) in April and May rose sharply to \$185 million. This is a considerable shift from a net return flow of about \$30 million in the first quarter (before seasonal adjustment), which would probably correspond to a small net outflow, seasonally adjusted. Japan alone accounted for a \$200 million outflow in April-May, presumably representing the major part of the borrowing from U.S. banks anticipated by Japanese officials earlier this year to cover an expected balance of payments deficit. Credit flows to other areas in April-May were small and irregular, and changes in foreign-currency assets and collections were insignificant.

Longer term bank credits registered a small net inflow of \$27 million in April and May, following a net liquidation of over \$150 million in the first quarter. Information on new loan commitments through May does not suggest any increase over the 1966 rate, while the large volume of credits extended from early in 1963 through the first quarter of 1965 is continuing to mature. On balance, it seems likely that net return flows on long-term bank credits will continue, though the movements will be irregular. Most of the reduction in outstanding credits has been in claims on Europe, with lesser but substantial reductions for Japan. In June there was a \$100 million bank loan to Argentina, the proceeds of which were invested in long-term CD's.

Economic activity in industrial countries abroad.

Businessmen's opinions during the last two or three months about the chances of early upturns in activity have been pessimistic. Only in Italy and Japan was expansion continuing during the first half of 1967.

Except in Italy and Japan, unemployment was generally increasing through April or May. In June, unemployment rose further in Britain. commonly expressed opinion in many countries was that no real improvement could be looked for until 1968. However, there have been relatively few signs of cumulative deterioration in the situation. The declines in industrial production in Britain and Germany appear to have ended. In those countries inventories do not seem to be abnormally large in relation to sales. However, since early this year there have been declines in import demand in many industrial countries, and this has contributed to a spreading of the slowdown in growth. Thus, after several months of little change, French industrial production declined noticeably in April and May.

Declines in private business investment have been a prominent feature of the sluggish performance in most Western European economies this year. In Britain and Germany, for instance, business capital outlays will be down sharply in 1967 as compared with 1966.

European governments have moved only cautiously to spur economic revival. In Britain, the priority given to the defense of the pound is the obvious explanation for the restraint shown by the authorities. However, in June the government did announce various steps to encourage consumer spending.

In Germany, monetary policy has been eased very considerably, but long-term interest rates remain fairly high, even by German standards. A break with tradition has been made by the planning of substantial Federal government deficits, not only for 1967 but also for 1968. However, disbursements under this year's "contingency budget" have been slow. In France, too, the authorities have adopted only mild reflationary measures. The cautious attitude toward recovery measures in these two countries reflects the emphasis their governments place on checking inflation, and in the case of France, on avoiding a balance of payments deficit.

INDUSTRIAL PRODUCTION
(1st quarter 1966 = 100)

	^{a/} U.K.	EEC	Germany	France	Italy	Nether- lands	Canada	Japan
<u>1966</u>								
Q-1	100	100	100	100	100	100	100	100
Q-2	99	102	101	101.5	104	101	101	104.5
Q-3	100	101+	98.5	104	107	102	101	110.5
Q-4	97	101+	97	104.5	107	105	103	115
<u>1967</u>								
Q-1	98	101-	94	104.5	110	104	102	120
Jan.	98	101-	96	104.5	107	104	103	120
Feb.	98	101+	95	104.5	111	105	102	118
Mar.	98	101-	93	104.5	111	104	102	121.5
Apr.	97	...	97	103	...	...	...	124
May	...	...	94	102	...	...	...	...

a/ Manufacturing.

In Germany, economic indicators for April and May gave mixed readings. Industrial production turned up in April after many months

of decline; one important factor in the turn was a pickup in auto output. But in various industries new orders fell off after rising in earlier months, and in May industrial production fell back somewhat.

Business investment plans, according to an April survey, call for fixed capital expenditures this year 12 per cent below those of 1966. German industry is currently operating at an average of 75 per cent of capacity. Spending on equipment was already 11 or 12 per cent smaller in January-April than in the corresponding period a year earlier.

Inventory policies of industry and trade have been very cautious, influenced by the expectation that inventories on hand when the value-added tax is introduced January 1, 1968, would suffer double taxation. Last week the Cabinet announced a measure of tax relief, with maximum relief in cases where purchased inventories are at least as large as at the end of 1966.

Consumer demand still showed some expansion in the first quarter of 1967. As compared with early 1966, growth was mainly in the area of services, including housing and travel. Retail sales rose in January from their fourth-quarter low, but subsequently fell off somewhat; in April and May they showed little change.

With foreign demand weakening, Germany's new export orders were no higher in the first four months of 1967 than in the last four months of 1966.

Apparently, developments in the German economy in the next few months will depend greatly on the stimulus to production and incomes to be provided by government expenditures. Since April the

placing of contracts under the Federal Government's "contingency budget" has accelerated. Earlier in the year, despite easier borrowing conditions, expenditures by Federal, State, and local authorities were only about in line with past trends of increase. At State and local levels, revenue shortages and legal debt ceilings have reportedly caused widespread budgetary problems.

Economic policy differences within the Federal Government were resolved last week by a compromise under which a second contingency budget will provide for placing of orders this autumn and a substantial budget deficit will be planned for 1968, but taxes will be increased next year to keep that deficit within acceptable limits.

The Bundesbank made a further move toward easier money with an additional cut of 8 per cent in the banks' reserve requirements effective July 1.

In Britain, industrial production registered no net rise from December through April. Retail sales, covering about half of total consumer expenditures, rose a little to March, dropped off in April, and were unchanged (in volume terms) in May.

The continuing rise in unemployment appears to have been a major consideration in the Government's decision, announced June 7, to ease restrictions on installment purchases of automobiles. A sharp decline in automobile sales played a large role in the decrease of consumer expenditures which took place in the last half of 1966, and despite a pick-up early this year car sales have remained depressed.

Other expansionary measures announced in June will take effect later. Payment of regional employment premiums will begin in

September, and increases in social security benefits in November. The government announced that it will also speed up payments of investment grants to private industry.

Price rises since the beginning of the year -- when the so-called freeze on wages and prices ended -- have been relatively moderate. But average hourly wage rates have increased about 2 per cent since the beginning of the year, and with the ending of the period of "severe restraint" at midyear the wage rise is now expected to accelerate.

So far, the impact of the war in the Middle East on the British economy has been limited. The principal effect has been in the foreign exchange markets. The Arab countries have switched only small amounts of their sterling holdings into other currencies, but the threat that they might withdraw larger amounts, coupled with general uneasiness over the Middle Eastern situation, contributed to heavy selling of sterling in recent weeks.

U.K. prices of all petroleum products were raised slightly at the end of June because of increased transportation costs, but no shortage of oil has yet developed in the United Kingdom. It is estimated that at the beginning of the war the United Kingdom had oil inventories sufficient to meet her needs for three to four months. As long as production in the Middle East remains at more or less normal levels, Britain can circumvent the Arab embargo on shipments to her by increasing purchases from other nations. However, continuation of the embargo and of the shutdown of the Suez Canal will adversely affect

Britain's foreign exchange reserves, since some alternative oil suppliers are less likely to accept payment in sterling than is, for example, Kuwait. Furthermore, only part of the increased shipping costs can be paid for in sterling.

Economic activity in France was moving on a plateau in the early months of 1967, with key economic indicators generally showing little change from late 1966 levels. A sharp dip in industrial production in April was associated with strikes in several industries, but in May output fell further and unemployment increased further.

As in other European countries, both lower foreign demand and a levelling off in domestic consumer expenditures have contributed to the sluggishness of activity.

According to surveys taken in May and June, French businessmen have become progressively more pessimistic about the prospects for resumed expansion later this year. Inventories are regarded as excessively large by many. With regard to counter-cyclical policy, the official view reportedly has been that it is better to await business recovery in France's main trading partners than to risk acceleration of inflation through vigorous domestic action. Long-term interest rates remain high, and the bond market is very tight.

Expansion continues in Italy, with the rise in industrial production accelerating again this year after slowing in late 1966. Italian exports to areas outside Europe re-emerged as a growth factor in the first quarter. Domestic demand for equipment and for semi-manufactured materials has been strong. An April survey, however, showed that while optimism still prevailed it was somewhat less buoyant than before.

The expansion has been making significant inroads into unemployment. Nevertheless, the pace of wage rate increases has slowed since the signing of new labor contracts in many industries in late 1966.

In Japan, industrial production has been rising at a rate of about 1-1/2 per cent a month since October of 1965, and in May it was 20 per cent higher than a year earlier. A survey of 330 large enterprises for the six months ending with March indicated that profits were up 22 per cent, after rising by 20 per cent in the previous six months.

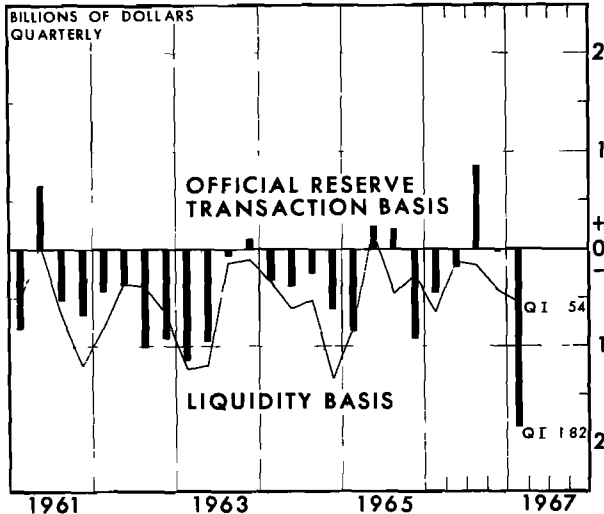
On the other hand, producers' shipments tended to level off in the first four months of this year, with the result that there was an increase in producers' inventories in March and April. The increase in both wholesale and consumer prices, seasonally adjusted, slackened substantially in the first five months of 1967, despite the generally buoyant economic conditions. A decline in iron and steel prices and weakness in non-ferrous metals were partly responsible.

In line with the general rise in economic activity and imports, and as a result of the lowering of interest rates elsewhere, Japanese businesses have increased their foreign borrowing. Much of this has been in the form of acceptance financing, largely in the United States, but Euro-dollar borrowing has also increased substantially.

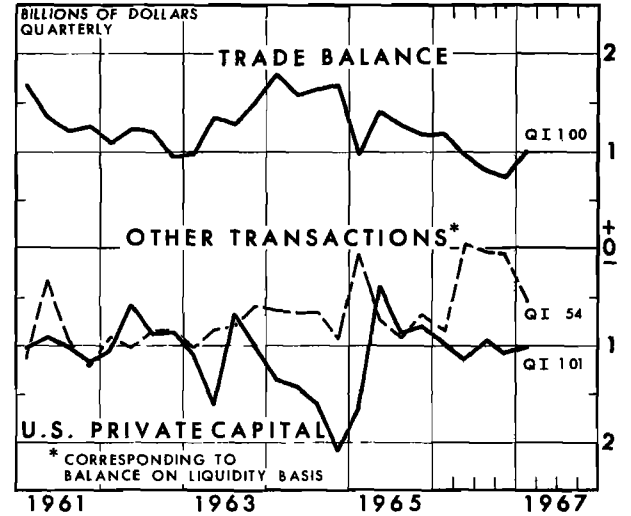
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED

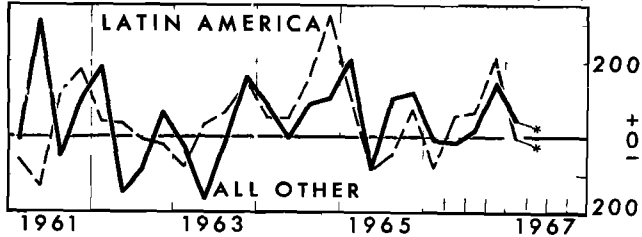
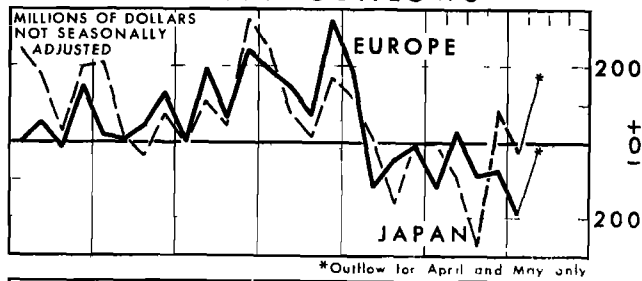
U.S. BALANCE OF PAYMENTS



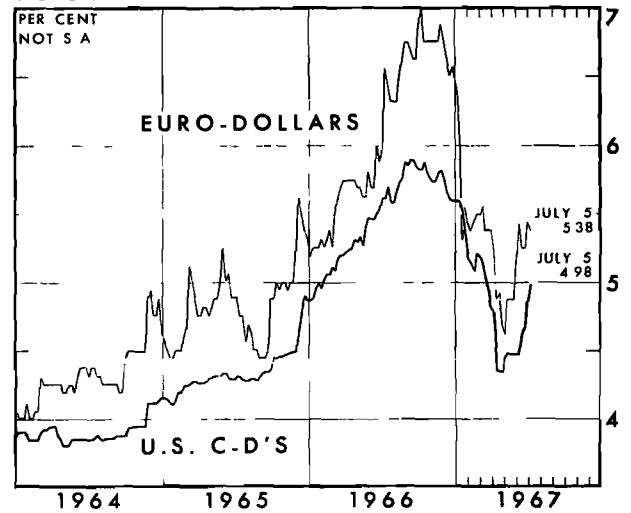
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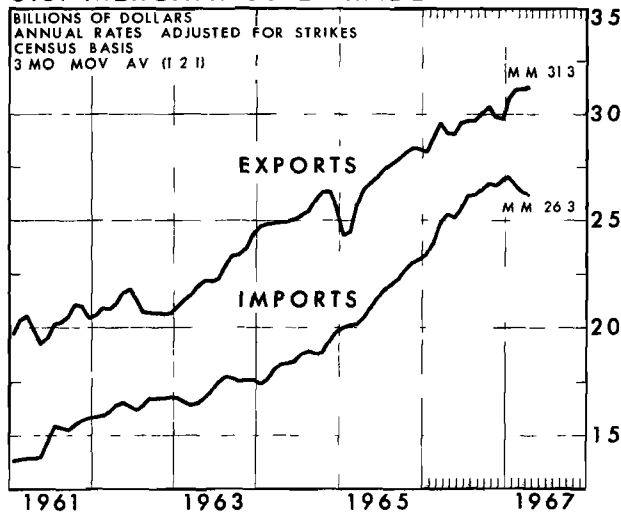
U.S. BANK CREDIT OUTFLOWS



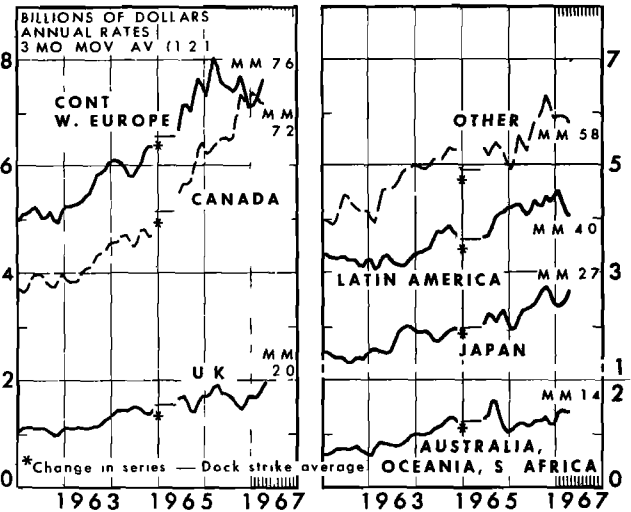
90-DAY RATES



U.S. MERCHANDISE TRADE



U.S. EXPORTS BY AREA



APPENDIX A: RESULTS OF THE APRIL 28 SURVEY OF TIME AND SAVINGS DEPOSIT RATES

This Appendix summarizes some of the major findings of the April 28 survey of time and savings deposit rates at member banks, and comments on some of the salient developments during the three months following the previous survey made at the end of January. A detailed report on the April survey will appear in the July Bulletin.

The increase of 3.4 per cent in total time and savings deposits at member banks in the 3 months ending April 28, as shown in Table 1, was the composite result of a relatively rapid rate of growth in consumer-type time deposits (defined here as all time deposits in denominations under \$100,000), a slow rate of growth in passbook savings, and a slight decline in business-type time deposits (that is, denominations of \$100,000 and over). Consumer-type time deposits became more attractive relative to market instruments during this period following the sharp decline in market rates in late 1966 and early 1967. They expanded at an annual rate of more than 40 per cent, although this was much less rapid than during the year 1966, when there were large transfers into those instruments out of savings deposits. Passbook savings, after declining since early 1966, bottomed out in mid-February and then began to expand. Over the entire January-April period, they rose on balance at only a 5 per cent annual rate. The decline in business-type deposits was due mainly to the heavy runs-off of corporate holdings in April to meet tax payments and the temporary decline in bank interest in competing for CD's at that time because of their large inflows of consumer savings.

Perhaps the most eye-catching figure in Table 1 is the large rate of growth which banks experienced in their new 90-day notice open-account passbook deposits, which rose 33 per cent in the 3-month period. Since it applies to a small base, the significance of this large growth rate is limited. Nevertheless, aggressive promotion of these deposits appears quite widespread since all except four Districts--Philadelphia, Richmond, Kansas City, and San Francisco--showed increases for this period of 18 per cent or more.

Rates of growth in total time and savings deposits were fairly uniform in the January-April period among all bank size groups, except those with total deposits of \$500 million or more, as shown in Table 2. The slower growth at large banks reflects the previously mentioned attrition in business-type time deposits, which are relatively

important at these banks. For consumer-type instruments, rapid growth prevailed among all bank-size groups. As might be expected in view of the greater interest sensitivity of depositors at large than at small banks, passbook savings at the largest banks rose less rapidly, and other consumer-type time deposits rose more rapidly, than at smaller banks.

Of particular interest in this table are the rapid rates of growth that occurred in large denomination business-type time deposits at smaller banks. Here, also, the amounts outstanding are relatively small. These rapid growth rates also occurred between the May 1966 and January 1967 surveys. One factor accounting for this expansion was a sizable increase in the number of issuing banks, which rose between January and April by more than 10 per cent. One possible explanation for this development is that small banks also are beginning to encounter higher loan/deposit ratios and lower liquidity positions and are finding it necessary to reach out for additional funds to accommodate their loan demand.

Among Federal Reserve Districts, growth rates in total time and savings deposits over the 3-month period varied considerably from a low of 0.5 per cent in the New York District, where business-type deposits showed a sizable decline, to a high of 5.7 per cent in the Boston District. These differences reflect wide variations in growth rates not only on business-type deposits but on consumer-type deposits as well.

Rate developments between late January and late April are summarized in Table 3. In general, these data confirm the special telephone survey information reported by the Presidents at the FOMC meeting on May 2 that some banks, mainly large ones, were attempting to moderate the rapid inflow of consumer CD's by rate reductions and other means. Close to 5 per cent of all member banks reduced the maximum rate paid on consumer-type time deposits between January and April. Among large banks with total deposits of \$100 million or more, 16 per cent took such action. On the other hand, another 4 per cent of all member banks raised rates during this period and another 1 per cent introduced an instrument of this kind.

The heaviest concentration of rate changes on consumer-type time deposits, both increases and decreases, was at 1/2 of 1 per cent, but changes of 1/4 per cent also were common. Among banks raising rates, however, more raised by a full percentage point than by 1/4 per cent. These were mainly smaller banks previously having relatively low rates. Among large banks, the principal actions were to reduce rates on consumer-type time deposits from the 5 per cent ceiling to either 4-3/4 or 4-1/2 per cent as shown in the bottom panel of column (3).

As might be expected rate reductions were far more widespread among business-type deposits, which are issued in competition with other money market instruments, than among consumer-type deposits. On passbook accounts, there was little rate activity, most of it upward.

Table 4 provides a rather detailed picture of the structure of offering rates on various types of instruments, as of both the January 31 and April 28 Survey dates. As shown in columns (1) and (2), about half of all member banks were paying 5 per cent on at least one consumer-type time deposit on both survey dates, but the proportion fell slightly between these two dates. Smaller banks were less generally at ceiling than large banks, but the difference between them was smaller in April than in January. Banks paying the 5 per cent ceiling held nearly 80 per cent of all consumer-type time deposits on January 31, but by April 28, they held only 71 per cent, reflecting the rate reductions at large banks.

On passbook savings, less than two-thirds of all member banks were at the 4 per cent ceiling at the end of April, but these included over 90 per cent of all large banks. Reflecting this concentration of large banks at the ceiling, banks paying the ceiling held nearly 90 per cent of all passbook deposits.

An analysis of time and savings deposit flows over the 3-month period relative to the level and change in offering rates suggests that rate was an important factor governing behavior of these deposits. Banks paying the higher rates tended to have the larger inflows. Also, banks raising rates experienced larger inflows than those leaving rates unchanged, while banks lowering rates tended to lose deposits. In all cases, of course, the experience of the individual bank reflected not only its own rate action, but also the relationship between its rates and those on alternative outlets for funds.

There was little change between January and April in the minimum denomination or minimum maturity associated with the maximum offering rate. Thus, there is no indication that any appreciable number of banks raised their minimum denomination in order to moderate inflows of consumer-type time deposits. Some are reported to have shortened their maximum maturities for this purpose, but the survey does not cover this characteristic.

TABLE 1

Types of Time and Savings Deposits of Individuals, Partnerships, and Corporations
(IPC) Held by Member Banks on January 31 and April 28, 1967

Type of deposit	Number of issuing banks		Amount			
	Jan. 31, 1967	Apr. 28, 1967	Millions of dollars		Increase or decrease (-)	
			Jan. 31, 1967	Apr. 28, 1967	Jan. 31-Apr. 28, 1967	
	(1)	(2)	(3)	(4)	millions of dollars	per cent
Total time and savings			116,890	120,824	3,934	3.4
Savings	5,850	5,835	70,701	71,600	899	1.3
Consumer-type time deposits--less than \$100,000:						
Total			25,081	27,749	2,668	10.6
Savings bonds	174	179	1,409	1,643	234	16.6
Savings certificates	1,593	1,558	8,033	8,647	614	7.6
Other nonnegotiable CD's	2,932	2,986	9,402	10,434	1,032	11.0
Negotiable CD's	1,885	1,923	4,381	4,561	180	4.1
Time deposits, open account	977	1,008	1,856	2,465	609	32.8
Business-type time deposits-- \$100,000 or more:						
Total			17,658	17,646	-12	-0.1
Negotiable CD's	828	907	13,018	12,786	-232	-1.8
Nonnegotiable CD's	882	993	2,814	3,188	374	13.3
Time deposits, open account	284	322	1,826	1,671	-155	-8.5
Christmas savings and other special accounts	4,084	4,201	3,450	3,828	378	11.0

NOTE: Includes a small amount of deposits outstanding in a relatively few banks that no longer issue these types of deposits and are not included in the number of issuing banks. Dollar amounts may not add to totals because of rounding.

TABLE 2

Percentage Changes in Time and Savings Deposits, IPC, at Member Banks from January 31 to April 28, 1967
by Type of Deposits and by Size of Bank and Federal Reserve District

Group	Total time & savings deposits	Business-type time	Consumer-type deposits		
			Total	Savings	Consumer-type time
All Banks	2.9	-0.1	3.4	1.0	10.3
Size of bank (total deposits, in millions of dollars):					
Under 10	3.9	33.3	3.6	1.0	7.3
10 - 50	3.9	16.7	3.6	1.2	8.8
50 - 100	4.5	21.3	3.6	1.5	9.3
100 - 500	4.1	12.2	3.3	1.4	10.3
500 and over	1.6	-3.1	3.3	0.7	12.4
Federal Reserve District:					
Boston	5.7	1.2	6.8	3.4	25.2
New York	0.5	-6.8	3.9	1.3	16.9
Philadelphia	3.9	-2.9	4.5	1.2	13.0
Cleveland	1.9	-3.4	2.5	1.1	8.0
Richmond	4.6	5.3	4.5	2.3	12.0
Atlanta	4.1	12.6	3.3	1.8	6.8
Chicago	4.9	12.9	4.0	0.5	12.5
St. Louis	4.4	10.9	3.8	2.3	5.6
Minneapolis	5.1	10.2	4.6	0.5	6.9
Kansas City	5.2	13.7	4.4	0.9	9.2
Dallas	3.2	1.6	3.8	-0.4	11.3
San Francisco	1.4	2.2	1.2	0.2	5.4

NOTE: Consumer-type time deposits are the following instruments issued in denominations of less than \$100,000: savings certificates, savings bonds, other nonnegotiable and negotiable CD's and time deposits, open account. Business-type time deposits include the following instruments issued in denominations of \$100,000 and over: negotiable and nonnegotiable CD's and time deposits, open account.

TABLE 3

Member Banks Changing the Maximum Rate Paid or Introducing New Time and Savings Deposit Instruments
between January 31 and April 28, 1967

Group	Consumer-type time			Business-type time			Saving deposits		
	All sizes	Size of bank, (total deposits in mil. of \$)		All sizes	Size of bank, (total deposits in mil. of \$)		All sizes	Size of bank, (total deposits in mil. of \$)	
		Less than 100	100 & over		Less than 100	100 & over		Less than 100	100 & over
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Number of issuing banks, Apr. 28, 1967	5,714	5,345	369	1,775	1,414	361	5,803	5,430	373
Percentage distribution of number of banks in group									
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
No change in rate, Jan. 31-Apr. 28	90.3	90.8	81.6	55.2	57.9	44.9	98.3	98.3	98.4
Banks raising rate	3.7	3.9	1.9	4.8	5.3	2.5	1.0	1.1	0.3
New maximum rate (per cent)									
3.50 or less	--	--	--	0.2	0.1	--	0.1	0.1	--
3.51-4.00	0.1	0.2	--	0.1	0.1	--	0.9	1.0	0.3
4.01-4.25	--	--	--	0.1	0.1	--	--	--	--
4.26-4.50	1.3	1.2	0.3	0.6	0.5	0.5	--	--	--
4.51-4.75	0.2	0.2	--	0.5	0.5	0.5	--	--	--
4.76-5.00	2.1	2.2	1.0	1.4	1.7	--	--	--	--
5.01-5.25	--	--	--	0.2	0.3	--	--	--	--
5.26-5.50	--	--	--	1.8	2.0	1.4	--	--	--
Banks reducing rate	4.6	3.8	16.2	20.6	13.3	49.3	0.5	0.4	1.3
New maximum rate (per cent)									
3.50 or less	1/	1/	--	0.2	0.2	--	0.5	0.4	1.3
3.51-4.00	0.5	0.5	--	0.7	0.6	1.1	--	--	--
4.01-4.25	0.4	0.4	1.6	1.8	1.0	5.0	--	--	--
4.26-4.50	2.5	2.1	7.6	5.5	3.5	13.3	--	--	--
4.51-4.75	1.2	0.8	7.0	3.2	1.9	8.3	--	--	--
4.76-5.00	--	--	--	7.8	5.2	18.3	--	--	--
5.01-5.25	--	--	--	1.4	0.8	3.3	--	--	--
Banks introducing new instruments 2/	1.4	1.5	0.3	19.4	23.5	3.3	0.2	0.2	--
New maximum rate (per cent)									
3.50 or less	0.2	0.2	--	0.8	1.1	--	0.1	0.1	--
3.51-4.00	0.4	0.4	0.3	2.8	3.4	0.5	0.1	0.1	--
4.01-4.25	0.1	0.1	--	0.4	0.5	--	--	--	--
4.26-4.50	0.3	0.4	--	5.0	5.9	1.7	--	--	--
4.51-4.75	1/	1/	--	0.9	1.1	--	--	--	--
4.76-5.00	0.4	0.4	--	7.4	9.1	0.8	--	--	--
5.01-5.25	--	--	--	0.3	0.3	0.3	--	--	--
5.26-5.50	--	--	--	1.7	2.1	--	--	--	--

NOTE: Consumer-type time deposits are the following instruments issued in denominations of less than \$100,000: savings certificates, savings bonds, other nonnegotiable and negotiable CD's and time deposits, open account. Business-type time deposits include the following instruments issued in denominations of \$100,000 and over. Negotiable and nonnegotiable CD's and time deposits, open account.

1/ Less than 0.05 per cent.

2/ Between January 31 and April 28, 44 banks discontinued issuance of consumer-type deposits and 61 banks discontinued issuance of business-type deposits. Since these banks had no offering rate on those instruments as of April 28, they are excluded from this table.

TABLE 4

Time and Savings Deposits, IPC, Held by Member Banks on January 31 and April 28, 1967, by Type of Deposit
by Maximum Rate Paid on any Instrument in Each Category and by Size of Bank

Group	All banks		Size of bank (total dep. in mil. of \$)				All banks		Size of bank (total dep. in mil. of \$)			
			Less than 100		100 & over				Less than 100		100 & over	
	Jan. 31	Apr. 28	Jan. 31	Apr. 28	Jan. 31	Apr. 28	Jan. 31	Apr. 28	Jan. 31	Apr. 28	Jan. 31	Apr. 28
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
	Number of banks						Amount of deposits (in millions of dollars)					
Consumer-type time deposits												
No. of issuing banks	5,726	5,744	5,365	5,371	361	373	25,080	27,733	11,288	12,168	13,792	15,565
Per cent distribution by maximum rate paid												
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
4.50 or less	46.7	47.7	48.9	49.4	15.0	22.5	20.0	23.1	38.8	39.4	4.6	10.3
4.51-4.75	1.8	2.7	1.8	2.4	1.1	8.1	1.1	5.9	1.7	2.2	0.6	8.9
4.76-5.00	51.5	49.6	49.3	48.2	83.9	69.4	78.9	71.0	59.5	58.4	94.8	80.8
Business-type time deposits												
No. of issuing banks	1,602	1,786	1,258	1,422	344	364	17,657	17,636	936	1,084	16,721	16,552
Per cent distribution by maximum rate paid												
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
4.50 or less	28.5	35.4	32.8	36.1	12.8	32.7	1.9	31.8	17.7	23.6	1.0	32.3
4.51-4.75	1.6	5.3	1.9	4.4	0.6	9.1	0.1	16.5	1.3	4.9	0.1	17.2
4.76-5.00	32.7	37.1	35.7	38.4	21.5	32.4	22.8	28.9	30.3	34.3	22.4	28.6
5.01-5.25	5.7	3.7	4.0	3.2	12.2	5.5	26.8	1.8	4.5	4.2	28.0	1.7
5.26-5.50	31.5	18.4	25.6	17.9	52.9	20.3	48.4	21.0	46.2	33.0	48.5	20.2
Savings deposits												
No. of issuing banks	5,830	5,835	5,482	5,458	368	377	70,698	71,595	23,130	23,154	47,568	48,441
Per cent distribution by maximum rate paid												
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
3.50 or less	36.0	34.4	36.7	36.1	9.2	9.8	10.3	10.4	24.8	24.2	3.3	3.7
3.51-4.00	65.0	65.6	63.3	63.9	90.8	90.2	89.7	89.6	75.2	75.8	96.7	96.3

NOTE: Consumer-type time deposits are the following instruments issued in denominations of less than \$100,000: savs. certs., savs. bonds, other nonnegotiable and negotiable CD's and time deposits, open account. Business-type time deposits include the following instruments issued in denominations of \$100,000 and over: negotiable and nonnegotiable CD's and time deposits, open account. Dollar amounts may not add to totals because of rounding.

APPENDIX B: IMPORTANCE OF CERTAIN FACTORS IN RECENT AND PROSPECTIVE VOLUME OF CORPORATE SECURITY ISSUES*

Two special and partly related factors that appear to have contributed to the record volume of corporate financing in capital markets this year have been (1) the bunching of flotations by very large companies, a number of whom have come to market for the first time in many years, and (2) numerous efforts to rebuild liquidity positions which had declined persistently over a long period and in some industries had dropped precipitously. In assessing the underlying strength of corporate capital market demand in coming months, it is appropriate to ask whether there is still a significant number of large companies that appear to be long overdue for long-term financing and whether rebuilding of liquidity still has a long way to go. The answer would seem to be a qualified yes to both questions.

Capital market financing by very large companies

Out of a group of about 200 very large companies (comprising the 50 largest public utilities and all manufacturing, railroad, and other transportation companies with end-of-1966 assets of \$500 million or more), 71 are known to have undertaken or announced prospective capital market financing this year. They comprise (with some double-counting): 43 with public offerings or private placements in the first quarter (vs. 30 in 1966); 21 with public offerings in the second quarter (vs. 22 in 1966); and 14 that, as of midyear, had announced prospective public offerings. (Information on individual company private placements, it should be noted, is not yet available beyond the first quarter of this year.)

It may be more meaningful to base 1966-67 comparisons on financing by manufacturing companies only. The major public utility and transportation companies come to the capital market frequently, and usually for only moderately large amounts each time. Most giant manufacturers, on the other hand, come infrequently and, when they do, their issues tend to be very large.

In each of the last 10 years, for example, at least 40 per cent--and as many as 70 per cent--of the largest public utilities have raised new capital through sale of long-term debt or equity securities, and all but 10 of these 50 largest utilities have come to market at

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least once in the last 2-1/2 years. Similarly, over the last decade the proportion of large transportation companies raising funds in the capital market has ranged between 50 and 80 per cent each year, and all but 4 of the 24 largest companies have done so at least once since 1964.

But large manufacturers undertake capital market financing much less frequently. In 1958, and again in 1966, about 30 per cent of the 123 largest companies raised new capital in the long-term securities markets; in each of the intervening years, when internally generated funds were large relative to investment outlays, the proportion ranged between 10 and 20 per cent. The peak years of 1958 and 1966 have been about matched already this year, and the 1967 count includes only private placements in the first quarter and public offerings sold or scheduled by midyear.

Among the giant manufacturers that have sold issues for the first time in many years are 11 that did their first post-1958 financing in 1966 and another 9 that have either sold or scheduled offerings thus far in 1967. But there are still 31 (or one-fourth of the group tallied) that have done no capital market financing since at least 1958. It is of course impossible to say how many of these 31 may currently be contemplating such financing or how many are likely to come to market in the foreseeable future. The fact that 73 of these 123 companies have obtained capital market funds quite recently, i.e., since 1964, suggests that the backlog of urgent demands, at least among giant concerns, may be less than many had thought.

It should be noted, however, that the present tally did not cover manufacturers below the \$500 million asset class, and hence did not include all companies that may be not only in need of long-term funds but also large enough to swell total capital market demands with issues of \$50 million or more. Of the 28 public offerings of this size by manufacturers in the first half of 1967, 8 were sold by companies with end-of-1966 assets of less than \$500 million and ranging down to \$170 million.

Rebuilding corporate liquidity

Despite the substantial volume of corporate capital market financing in the first quarter of this year, corporate liquidity declined about as much as in other recent years and reached another new low. At the end of the first quarter, according to the latest available SEC data, corporations held only \$24.60 of cash, bank deposits and U. S. Government securities for each \$100 of total current liabilities, compared with \$34.10 three years earlier and \$36.80 in the first quarter of 1962. If the definition of liquid assets is broadened to include "other" current assets (the item which, in the SEC series on corporate working capital, includes such additional liquidity investments as finance company paper), the story is about the same, as may be seen from Table 1.

Table 1

CORPORATE LIQUIDITY RATIOS, END OF FIRST QUARTERS

Year	Cash and Governments/Total		Cash, Governments and "other"/	
	Current Liabilities		Total Current Liabilities	
	Level (per cent)	Change from preced- ing (4th) quarter (points)	Level (per cent)	Change from preced- ing (4th) quarter (points)
1962	36.8	-1.6	45.8	- .9
1963	35.0	-2.0	44.3	-1.3
1964	34.1	-1.3	44.1	- .7
1965	30.9	-2.0	41.0	-1.2
1966	28.0	-1.4	38.3	- .9
1967	24.6	-1.5	34.6	- .8

In almost every industry, liquidity showed no improvement in the first quarter of 1967 after allowance for usual seasonal changes, and at the end of the quarter was substantially lower than three years ago, when the year-to-year decline began to accelerate. Data for selected industries are shown in Table 2.

Table 2

CORPORATE LIQUIDITY RATIOS, SELECTED INDUSTRIES

Industry	Cash, Governments and "other"/		
	Total Current Liabilities		
	1964-Q1 (per cent)	1967-Q1 (per cent)	Percentage Change 1964-67
Total	44.1	34.6	-22
Manufacturing	59.8	40.7	-32
Motor vehicles	84.4	42.9	-49
Elec. machinery	44.4	25.3	-43
Other machinery	56.5	37.6	-34
Primary metals	96.8	75.6	-22
Food and kindred	50.8	39.8	-22
Chemicals	77.8	56.5	-27
Petroleum	87.6	60.7	-31
Retail trade	35.9	29.9	-17
Electric utilities	44.1	32.5	-26
Gas utilities	45.5	31.6	-31
Railroads	76.1	48.8	-36
Communication	82.5	57.6	-30

Some observers have attributed the absence of liquidity improvement in the first quarter to the fact that the bulk of the security issues sold to provide funds to repay bank debt or otherwise rebuild liquidity were offered so late in the quarter that proceeds would not have been received by the corporation until after the close of the quarter; further, they suggest, proceeds may have been used initially for other purposes, such as tax payments; or the bank loans repaid in the first quarter may have been primarily term loans, only the current portion of which enters into the calculation of conventional liquidity ratios. These kinds of explanations would lead one to expect the liquidity improvement effect of the first quarter, and still larger second quarter, capital market financing to show up later this year (though not necessarily in the second quarter, because of the large drains on liquid assets then to meet tax payments).

It seems more likely, however, that it will not show up at all--in aggregate figures, over the relatively short-run future. The persistent decline in corporate liquidity over the past decade has reflected relatively small additions to aggregate liquid asset holdings in the face of much larger increases in aggregate corporate needs for day-to-day funds (measured here by total current liabilities). The decline could be halted--though not reversed--with an annual growth in liquid assets about twice what is has averaged over the past five years. But massive amounts of new long-term funds would be required to reduce dependence on short-term funds and/or accelerate the growth in liquid assets enough to return the all-corporate ratio to its level of even one year ago. Table 3 illustrates the point.

Table 3

CHANGES IN CORPORATE LIQUIDITY

First quarter	Changes from first quarter of preceding year:		
	In total current liabilities (Billions of dollars)	In liquid assets, including "other" (Billions of dollars)	In the liquidity ratio (points)
1963	+15	+4.5	-1.5
1964	+14	+5.6	- .2
1965	+17	+1.2	-3.1
1966	+24	+3.8	-2.7
1967	+20	-1.8	-3.7
1968 ^{1/}			
a	+20	+7.2	0
b	+15	+14.8	+3.7
c	+20	+16.8	+3.7

^{1/} The examples a, b, and c show the growth in liquid assets (from Q1 1967 to Q1 1968) which would need to accompany three hypothetical patterns of change in total current liabilities and in the liquidity ratio. In a, total current liabilities grow by the same amount as over the past year, and the liquidity ratio remains at the Q1 1967 level. In b, liabilities grow more slowly (as new long-term funds are used to repay bank debt or otherwise reduce dependence on short-term funds), and the ratio rises to the Q1 1966 level. Example c uses the liability hypothesis of a and the ratio hypothesis of b.

Individual companies, of course, by undertaking major long-term financing, can rebuild their liquidity quickly, though it seems out of the question for corporations as a whole to do so. If success in reversing, or at least slowing down, the prolonged decline in liquidity is attained selectively, it is not likely to affect aggregate statistics significantly, and one must look beyond the aggregate statistics--perhaps to the financial statements of individual corporations--for clues to the extent of satisfied vs. still unsatisfied needs for additional liquidity.

APPENDIX C: INTERNATIONAL TRANSACTIONS IN SECURITIES

In the first half of this year there has been a larger flow of U.S. capital into foreign securities than in the same period of 1966. Last year the net outflow for the year was about \$480 million, and \$360 million of that occurred in the first quarter, largely because the sale of \$150 million of new Canadian bonds originally scheduled for the end of 1965 was delayed by agreement until early 1966. After the first quarter, net outflows were comparatively small as the amount of new foreign bond issues dropped, the Canadian Government made advance repurchase of Canadian bonds outstanding in the U.S. (such repurchases totaled \$139 million for the year), and sizable liquidations by U.S. investors of their holdings of foreign equity securities were resumed. In the last three quarters of 1966, net purchases of foreign securities of all types averaged only about \$40 million per quarter.

This year the amount of new issues sold through June was probably about \$750 million, including an allowance of \$50 million for extra sales of bonds of Israel. This was about as large as sales in the first half of 1966, even though there was no carryover this year. The first half figure includes about \$150 million of purchases of bonds of international institutions, which were approximately offset by investments by those institutions in bonds of U.S. Government agencies. Redemptions have been lower, mainly because Canadian advance purchases were only \$31 million -- which came at the end of June -- whereas they amounted to \$109 million in the first half of last year.

Transactions in foreign equity securities through May still appear to reflect net liquidations by Americans, but at a rate of only \$25-30 million per quarter compared to \$50 million per quarter in 1966. Although net transactions with Canada continue to show net sales by U.S. investors, data for Europe indicate that liquidations ceased in the early months of this year.

Foreign transactions in U.S. securities other than Treasury issues have been dominated since 1965 by purchases of debt obligations of U.S. corporations specially organized to finance direct foreign investments (usually Delaware corporations), purchases of obligations of U.S. Government Agencies by international organizations, and the liquidation of the British Treasury portfolio of U.S. corporate stocks. Apart from these transactions, the principal regular feature of foreign dealings in U.S. securities has been a steady inflow from Canada to purchase U.S. stocks. These Canadian purchases amounted to \$230 million in 1966, and have continued this year, though on a somewhat reduced scale. Dealings by other countries in U.S. corporate stocks have been irregular; there was a small net liquidation overall in 1966, but an inflow of about \$60 million this year through May. Transactions in U.S. corporate bonds, other than the special types mentioned above, resulted in a net sale by foreigners of about \$50 million in 1966,

mainly early in the year when purchases of bonds of the special financing affiliates were large. In the first quarter this year such transactions were minor, but in April and May it appears that there has again been some foreign selling of U.S. corporate bonds, aside from U.K. dealings and bonds of the special financing affiliates. Sales of bonds by those affiliates reached \$422 million in 1966 (excluding one large transaction of \$178 million involving exchange of U.S. corporate bonds for stock in a foreign corporation); so far this year sales already made or announced total nearly \$300 million.

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These tables show details of U.S. transactions in securities with foreigners summarized in the discussion of the balance of payments in Section IV. Data are in millions of dollars, not seasonally adjusted. Outflows (-).

Table 1. U.S. Transactions in Foreign Securities

	<u>1965</u>	<u>1 9 6 6</u>					<u>1967</u>	
		<u>Total</u>	<u>Q-1</u>	<u>Q-2</u>	<u>Q-3</u>	<u>Q-4</u>	<u>Q-1</u>	<u>Apr. - May</u>
Total transactions in foreign securities	-758	-482	-357	-60	-11	-54	-239	-127
Foreign bonds, total	-1,051	-689	-325	-129	-101	-134	-272	-144
New issues, total	-1,201	-1,164	-432	-299	-235	-198	-332	-210 est.
Canada	-706	-888	-391	-235	-131	-131	-256	-104
Int'l. organ.	-179	-80	--	--	-62	-18	-52	-100
Other	-316	-196	-41	-64	-42	-49	-24	-6
Debt retirement	222	405	118	123	75	89	100	40 est
Other transactions in foreign bonds	-72	70	-11	47	59	-25	-40	26
Foreign stocks, total	293	207	-32	69	90	80	33	17
Canada	170	69	-60	14	62	51	42	17
Europe	132	134	24	62	24	23	-10	4
Other	-9	4	4	-7	4	6	1	-4

Table 2. Foreign Transactions in U.S. Securities

	<u>1965</u>	<u>1 9 6 6</u>					<u>1967</u>	
		<u>Total</u>	<u>Q-1</u>	<u>Q-2</u>	<u>Q-3</u>	<u>Q-4</u>	<u>Q-1</u>	<u>Apr. - May</u>
Total, all U.S. securities	-357	909	173	520	107	109	112	244
U.S. corporate stock	-400	-305	-33	-61	-51	-160	-50	72
United Kingdom	-396	-525	-61	-216	-93	-155	-96	-9
Canada	47	232	28	99	47	57	33	35
Other	-51	-12	--	56	-5	-62	13	46
U.S. bonds (other than Treasury issues)	43	1,214	205	581	158	269	162	172
United Kingdom	-123	424	--	170	74	180	73	72
Issues of Delaware Corporations <u>1/</u>	191	599	183	296	35	85	92	82 est.
U.S. agency bonds bought by int'l. organizations	--	244	73	139	27	5	-6	71
Other transactions in U.S. bonds	-25	-53	-51	-24	22	-1	3	-53 est.

1/ U.S. corporations specially organized to finance direct foreign investments.