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CONFIDENTIAL (FR)

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

September 5, 1968

SUMMARY AND OUTLOOK

Outlook for economic activity

The rise in over-all economic activity is expected to be considerably less vigorous this quarter than in April-June, largely as a result of a sharply lower rate of steel and other inventory accumulation. Retail sales, however, have been quite strong thus far this summer. In the fourth quarter, increases in both final sales and inventory building are likely to be smaller, with little rise in real GNP. Some deceleration in the rate of price advance also is anticipated by the fourth quarter.

The anticipated slackening in economic activity reflects the expected impact of fiscal restraint, as well as the lagged effects of tight monetary conditions, and the post-steel settlement inventory adjustments. The effects of the recent change in fiscal stance has not been apparent in most business indices as yet. While available data indicate strengthen consumer buying thus far, it is probable that by the fourth quarter several months of slower growth in disposable income will have dampened expansion in consumer demand. The recent fiscal package also will reduce the stimulus from rising Federal expenditures in the second half of this year. The deficit, NIA basis, was at rate of about $9.5 billion in the first half of the year; in the second half, the deficit should be reduced to about $6 billion by the increase in tax collections and further tapering off of the rise in Federal outlays.

Changes in other major sectors will contribute little to growth in the rest of this year: residential construction is expected to be maintained at about the rate of the last two quarters (as starts dip and begin to rise again) and figures from the new Commerce-SEC survey indicate that investment in plant and equipment will recover in the third quarter, but only to the first quarter level, and show little further increase in the fourth.

Outlook for resource use and prices

Liquidation is now underway in steel inventories and this is expected to continue into the fourth quarter. Over coming month,, expectations are that growth in private demands, production, incomes, and employment will slacken further and the unemployment rate is likely to rise gradually to about 4 per cent. In addition, the rate of capacity utilization in manufacturing is expected to be reduced further. Although the expansionary effects of new wage agreements for the remainder of the year will be more limited than earlier because of the smaller number of workers involved, the pattern of 7 per cent or more in first-year wage increases is likely to continue to exert strong upward pressure on unit labor costs and to curtail profit prospects.

The wholesale industrial price average was unchanged in August and the number of classes of products that were stable or showed declines remained large for the third month in a row. Selective advances in domestic steel mill products will contribute directly to a slight increase in September in the average level of wholesale commodity prices, and new

auto prices are also expected to be higher this autumn. On the other hand, actual and prospective increases both here and abroad in the supply of farm products and food are exerting downward pressure on the wholesale price level. These developments should also limit further increases in the consumer price index, which rose rapidly in June and July.

Demands for credit

The abatement of business credit demands appears to be having relatively more of an effect so far on capital markets than on banks. Business loan demands on banks may remain near their June-August pace in September, but moderate substantially thereafter. One factor bolstering loan demands is the recent tax legislation. Corporate income tax payments are expected to be much larger in September than in any earlier month of the year except June, and to exceed payments of September 1967 by about $1.5 billion. Apart from any such tax-related borrowing, however, the expected slower pace of business activity between now and year-end, including a reduced rate of inventory accumulation, is expected to lead to smaller short-term credit demands of business.

Expectations of declining long-term interest rates may have also contributed to maintenance of business loan demands on banks, while corporate bond offerings have been reduced. Corporate bond issues are expected to continue at around the recent moderate pace over the next few months. Not only will fund requirements probably drop

off, but, in view of their improved liquidity position and the availability of bank credit, corporations are also in a relatively good position to handle such needs without heavy reliance on bond markets.

In contrast to the corporate bond market, municipal offerings are likely to continue near their recent record pace, bolstered in part by sizable industrial revenue bond offerings. Some issuers may decide to postpone scheduled offerings, however, in view of the advanced level of rates and the congested near-term calendar.

These demand conditions in prospect suggest that corporate bond yields are likely to edge down over the months ahead. The major factor that could push such yields up would be development of expectations that interest rates were near their bottom; this could lead to some return of major industrial borrowers to the market. In contrast, technical conditions in the municipal market suggest the possibilities of some interest rate increases over the short run, although over the longer-run such yields may tend to decline, given no dramatic shifts in the business outlook. The potential weakness in the municipal market reflects substantial accumulated inventory of unsold securities combined with the continuing large volume of new offerings. This same potential exists in the Government market, though probably to a lesser degree, for the volume of coupon issues in dealer hands remains unusually large, and the cost of carry negative.

However, new Treasury cash borrowing is not expected until the last half of October (and will probably take the form of tax bills), and new coupon issues are not likely to come to market until announcement of the mid-November refunding.

Supply of funds

While net savings inflows to thrift institutions may pick up a bit in the period immediately ahead, it will likely remain below year-earlier levels. With mortgage portfolio repayments continuing to run modestly ahead of last year, total cash flows to savings and loan associations and savings banks could be large enough to encourage some further increases in new mortgage commitment activity particularly if thrift institutions remain interested in locking up the high prevailing mortgage yields.

Inflows of consumer-type time and savings deposits at banks are expected to continue at close to the recent moderate pace unless there should be a significant further drop in market yields. Negotiable CD's, which have been the major contributor to the July-August upsurge in commercial bank time deposits, are expected to show only a small further rise in the coming weeks unless loan demand should be unexpectedly strong. Outstanding CD's at New York and Chicago banks have shown little net change recently and the rate of growth at banks outside these cities has tapered off. While no substantial run-off is anticipated over the tax period, banks undoubtedly would be able to recoup any such attrition rapidly if it did develop.

Private demand deposits are expected to show relatively moderate growth in the weeks ahead, continuing the recent slowdown. In part, this would reflect the further unwinding of some of the temporary influences contributing to rapid monetary growth earlier--such as the surge in stock market activity, heavy bank financing of securities dealer inventories, and the decline in U.S. Government deposits--but moderation in the pace of economic expansion generally would also be a factor.

Thus, in contrast to the July-August period, changes in supplies of funds during the period just ahead would seem unlikely to contribute to any tendency to move market yields down further from their recent rather stable levels.

International developments

After three months of near balance on the liquidity basis (measured before special transactions) a large deficit in the balance of payments reoccurred in August; preliminary and partial weekly data indicate a deficit for that month of over $700 million, well in excess of the average for the month in recent years. We have not been able to explain the improvement in the May-July period on the basis of available data, nor are we now able to explain the reversal in August. Perhaps too much stress should not be put on this latest reversal, though it certainly puts a damper on optimism about the outcome for the year.

There was a modest improvement in the trade balance in July on a seasonally adjusted basis. A major improvement in the trade balance in the remaining months of the year is still a reasonable hope.

Imports should fall off as the anticipated tapering in the growth of domestic demand occurs, and because of the disappearance of certain special factors tending to produce abnormally high imports in the first six months. Exports in January-June were about 7.5 per cent above the rate of the last half of 1967 and hopefully will continue to increase at a healthy rate.

On the capital side it is difficult to see any overall improvement on the first-half performance. While direct investment outflows will probably decline, this could be more than offset by a swing in bank lending. Outstanding U.S. bank credit to foreigners was reduced about $800 million through July. Some of this reduction was seasonal but a fair-sized net outflow, seasonally adjusted, could occur during the last five months, without violating the guidelines. The change in net flows from the first to the last half of the year could therefore be substantial.

On direct investments, we apparently had a very considerable outflow in the first half of the year, and if the controls are effective, the last half should show a smaller use of funds from the United States. Recently released data on plant and equipment expenditures of foreign affiliates of U.S. companies are somewhat reassuring; the continuation of only small year-to-year increases is contemplated in 1968 and 1969, which would be entirely consistent with a continuing reduction in the amount of financing from U.S. sources.

So far this year the underlying balance of payments deficit has not involved a financing problem. In fact, there has been an official settlements surplus as U.S. banks increased their liabilities to foreign branches by over $3.0 billion. It seems highly unlikely that this flow will continue at this rate, if it continues at all. Thus, the problem of financing the U.S. deficit may come to the fore again.

To the foregoing uncertainties, which are probably apparent to most sophisticated market observers, has been added the speculation over possible revaluation of the mark. Although such a revaluation would strengthen weak currencies, anticipatory speculation inevitably drains reserves from countries whose payments position is weakest. It seems clearer than ever that continued close cooperation among monetary authorities will be needed to finance reserve changes brought about by speculative short-term capital flows in ways that will abate rather than increase the speculative fever.

September 3, 1968

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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.)	Jul'68	79.0	79.0	77.5	1.9	4.3
Unemployment (mil.)	"	2.9	3.0	3.0	-2.3	1.7
Unemployment (per cent)	"	3.7	3.8	3.9	--	--
Nonfarm employment, payroll (mil.)	"	68.2	68.0	65.9	3.4	6.0
Manufacturing	"	19.8	19.8	19.3	2.8	2.8
Other industrial	"	8.2	8.1	8.1	0.8	1.1
Nonindustrial	"	40.2	40.1	38.5	4.3	8.8
Industrial production (57-59=100)	"	165.3	164.7	156.6	5.6	5.2
Final products	"	164.3	164.3	157.1	4.6	5.8
Materials	"	166.5	165.7	156.1	6.7	4.8
Wholesale prices (57-59=100)1/	"	109.1	108.7	106.5	2.4	2.5
Industrial commodities (FR)	"	108.0	107.9	105.2	2.7	3.3
Sensitive materials (FR)	"	106.3	105.9	100.0	6.3	0.0
Farm products, foods & feeds	"	109.4	108.0	107.3	2.0	-0.5
Consumer prices (57-59=100)1/	"	121.5	120.9	116.5	4.3	7.2
Commodities except food	"	113.2	113.0	109.1	3.8	6.1
Food	"	120.0	119.1	116.0	3.4	5.0
Services	"	134.9	133.9	127.7	5.6	10.0
Hourly earnings, mfg. ($)	"	3.01	3.00	2.83	6.4	10.7
Weekly earnings, mfg. ($)	"	123.08	122.81	114.51	7.5	9.7
Personal income ($ bil.)2/	"	689.2	683.7	629.8	9.4	17.3
Corporate profits before tax ($ bil.)2/	QII'68	91.1p	88.9	80.3	13.4	6.4
Retail sales, total ($ bil.)	Jul'68	29.1	28.2	26.4	9.9	14.6
Autos (million units)2/	"	9.1	8.8	8.1	12.9	11.0
GAF ($ bil.)	"	7.2	6.9	6.3	13.6	18.3
Selected leading indicators:						
Housing starts, pvt. (thous.)2/	"	1,539	1,349	1,369	12.4	42.6
Factory workweek (hours)	"	40.9	40.9	40.5	1.0	-0.7
New orders, dur. goods ($ bil.)	"	24.7	24.6	23.7	4.3	1.5
New orders, nonel. mach. ($ bil.)	"	4.0	4.0	3.6	10.9	15.4
Common stock prices (1941-43=10)	Aug'68	98.11	100.30	94.49	3.8	21.6
Manufacturers'						
Inventories, book val. ($ bil.)	Jul'68	84.9	84.6	80.6	5.3	16.8
Gross national product ($ bil.)2/	QII'68	851.6	831.2	780.2	9.2	15.0
Real GNP ($ bil., 1958 prices)2/	"	702.3	692.7	669.2	4.9	7.5

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

SELECTED DOMESTIC FINANCIAL DATA

	Week ended Aug. 31, 1968	4-week average	Last 6 months High	Last 6 months Low
Money Market 1/ (N.S.A.)				
Federal funds rate (per cent)	5.90	6.02	6.42	4.62
U.S. Treas. bills, 3-mo., yield (per cent)	5.19	5.10	5.82	4.96
U.S. Treas. bills, 1-yr., yield (per cent)	5.17	5.16	5.99	5.10
Net free reserves 2/ ($ millions)	-234	-245	21	-551
Member bank borrowings 2/ ($ millions)	374	577	823	374
Capital Market (N.S.A.)				
Market yields (per cent)				
5-year U.S. Treas. bonds 1/	5.50	5.50	6.15	5.46
20-year U.S. Treas. bonds 1/	5.24	5.23	5.68	5.18
Corporate new bond issues, Aaa adj. 8/	6.36	6.29	6.83	6.14
Corporate seasoned bonds, Aaa 1/	5.97	6.01	6.29	5.97
Municipal seasoned bonds, Aaa 1/	4.25	4.03	4.42	3.80
FHA home mortgages, 30-year 3/	--	7.42	7.52	6.78
Common stocks, S&P composite series 4/				
Prices, closing (1941-43=10)	98.86	98.31	102.34	88.42
Dividend yield (per cent)	3.08	3.10	3.38	2.94

	Latest month	Amount	3-month average	Change from year earlier: Latest month	Change from year earlier: 3-month average
New Security Issues (N.S.A., $ millions)					
Corporate offerings 5/	Sept. '68 e/	1,725	1,833	2	-362
State & local govt. public offerings	Sept. '68 e/	1,500	1,533	170	490
Comm. & fin. co. paper (net change in outstandings) 6/	July '68	+948	+746	+54	+481

	Latest month	Out-standings Latest month	Change: Latest month	Change: 3-month average	Annual rate of change from: Preceding month	Annual rate of change from: 3 months ago	Annual rate of change from: 12 months ago
Banking (S.A.)		($ billions)			(per cent)		
Total reserves 1/	August '68 p	26.40	0.48	0.23	22.0	10.7	7.2
Credit proxy 1/	"	285.7	4.8	2.8	20.1	12.1	7.4
Bank credit, total 6/ 9/	July '68	364.6	7.3	3.4	24.5	11.5	9.7
Business loans	"	91.2	0.8	0.7	10.6	9.9	9.4
Other loans	"	146.5	3.5	1.5	29.4	13.0	10.1
U.S. Govt. sec.	"	62.6	2.1	0.9	41.7	17.3	5.4
Other securities	"	64.2	0.8	0.3	15.1	5.0	13.6
Total liquid assets 1/ 6/	"	677.3	6.2	3.3	11.1	5.9	7.7
Demand dep. & currency 1/	August '68 p	190.0	0.6	1.3	3.8	8.4	6.2
Time & sav. dep., comm. banks 1/	"	193.7	3.3	2.0	20.8	13.0	9.3
Savings, other thrift instit. 6/	July '68	190.2	1.0	0.8	6.3	5.3	7.8
Other 6/ 7/	"	107.3	0.8	-0.3	9.0	-3.7	9.5

N.S.A. -- not seasonally adjusted. S.A. -- seasonally adjusted. p - Preliminary
e. Estimated by F.R.B. 1/ Average of daily figures. 2/ Average for statement week ending August 28. 3/ Latest figure is monthly average for July. 4/ End of week closing prices; yields are for Friday. 5/ Corporate security offerings include both bonds and stocks. 6/ Month-end data. 7/ U.S. Savings bonds and U.S. Government securities maturing within 1 year. 8/ Adjusted to Aaa basis. 9/ Data for total bank credit and components are based on revised seasonal factors.

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

	1967				1968			
	I	II	III	IV	I	II	June[p]	July[p]
				Seasonally adjusted				
Goods and services, net 1/	1,293	1,269	1,359	848	374			
Trade balance 2/	975	1,098	1,085	319	84	13[r]	-112[r]	94
Exports 2/	7,661	7,703	7,626	7,478	7,924	8,323[r]	2,759[r]	2,778
Imports 2/	-6,686	-6,605	-6,541	-7,159	-7,840	-8,310[r]	-2,871[r]	-2,684
Services balance	318	171	274	529	290			
Remittances and pensions	-262	-392	-358	-263	-269			
Govt. grants & capital 3/	-1,176	-1,039	-988	-1,008	-1,163			
U.S. private capital	-975	-1,104	-1,788	-1,638	-716[r]			
Direct investments	-653	-651	-902	-815	-468			
Foreign securities	-259	-199	-476	-332	-406	-81		
Banking claims	79	-198	-435	95	360[r]	204		
Other	-142	-56	25	-586	-202			
Foreign capital, nonliquid	865	1,202	766	353	1,311			
Official foreign accts.	382	724	18	150	336			
Long-term deposits	304	584	-215	147	117	144	49	-126
U.S. Govt. liab.	78	140	233	3	219	763		
Int'l. institutions 4/	70	97	117	30	-92	-64		
Other 5/	413	381	631	173	1,067			
Errors and omissions	-250	-458	207	-34	-200[r]			
		Balances, with and without seasonal adjustment (- deficit)						
Liquidity balance, S.A.	-505	-522	-802	-1,742	-663[r]	-156[r]		
Seasonal component	267	302	-410	-159	412[r]	298[r]		
Balance, N.S.A.	-238	-220	-1,212	-1,901	-251	142[r]	317	-231
Official settlements balance, S.A.	-1,764	-806	247	-1,082	-530[r]	1,456[r]		
Seasonal component	485	101	-272	-314	630	97		
Balance, N.S.A. 6/	-1,279	-705	-25	-1,396	100	1,553	993	-73
			Reserve changes, N.S.A. (decrease -)					
Total monetary reserves	-1,027	419	375	181	-904	137	-285	303
Gold stock	-51	-15	-92	-1,012	-1,362	-22	213	-5
Convertible currencies	-1,007	424	462	1,145	401	-267	-907	294
IMF gold tranche	31	10	5	48	57	426	409	14

1/ Equals "net exports" in the GNP.
2/ Balance of payments basis which differs a little from Census basis.
3/ Net of scheduled and non-scheduled repayments.
4/ Long-term deposits and Agency securities.
5/ Includes some foreign official transactions in securities.
6/ Differs from liquidity balance by counting as receipts (+) increase in liquid liabilities to commercial banks, private nonbanks, and international institutions (except IMF) and by not counting as receipts (+) increases in certain nonliquid liabilities to foreign official institutions.

THE ECONOMIC PICTURE IN DETAIL

The Nonfinancial Scene

Gross national product. Although hard facts on recent and current economic activity are still scarce, staff estimates indicate that expansion in the economy is now slowing, and will slow further in the fourth quarter. The deceleration reflects the combined impact of reduced inventory investment, the tax surcharge and curtailed Federal expenditures. GNP in current dollars is expected to increase by $12 billion this quarter, and by about $9 billion in October-December. These changes correspond to annual rates of growth in real GNP of 1.3 per cent and 0.4 per cent, compared to about 6 per cent in the first half of the year. Prices in the private economy, as measured by the GNP deflator, are expected to rise somewhat less rapidly as the growth in economic activity eases.

The slowing this summer in total economic activity is not a reflection of the surtax, which took effect on withholdings in mid-July. Indeed, the rise in final demand this quarter is expected to be exceptionally strong, exceeding that of any recent quarter except the first. Consumption expenditures will increase substantially even if retail sales in August and September level off at the advanced July rate. In addition, increases in outlays for housing and for plant and equipment are likely. Diminished GNP growth for the quarter is thus largely attributable to an anticipated large downward swing

in inventory accumulation. Although business stocks as a whole are projected to continue to grow, accumulation is likely to be reduced by some $5 billion from the high rate of accumulation in April-June, when acceleration in inventory building reflected in part a large rise in steel stocks prior to the wage settlement.

In the fourth quarter, the income drain resulting from the surtax is likely to weaken growth in consumer expenditures appreciably, and, since little change is projected in either fixed investment or Federal spending, the rise in fnnal sales will be considerably reduced and inventory accumulation will be curtailed further. The large reduction in steel production following the contract settlement will adversely affect incomes directly. And secondary declines in production and income may well begin before the end of the year.

Retail sales rose very strongly in July--up 3 per cent from June, according to advance estimates--and have apparently continued at close to the July rate in August. Although unit sales of new U.S.- made cars slackened in August from their extremely high July rate, sales of new domestic autos in the quarter appear likely to average 8.6 million compared to an annual rate of 8.44 million in April-June. At the same time, the rise in nondurable goods expenditures appears to be one of the strongest since early 1966, compensating in part for the weak performance in the second quarter. These increases have taken place despite the fact that personal income is now advancing at a rate considerably below that of last quarter. The surtax began to reduce pay-checks in the second half of July, and

the increase in spendable income this quarter is expected to be one of the smallest in recent years. The saving rate in the third quarter is expected to average 6.6 per cent--down 1 percentage point from the very high second quarter rate.

The increase in personal income is likely to be further slowed in the fourth quarter and the rise in disposable income should just about match the small rise in the third quarter. Earnings of production workers in manufacturing are likely to be affected by cuts in hours and employment as inventory adjustments continue and many earners will be paying social security taxes in the fourth quarter of this year for the first time because of the higher statutory level of earnings subject to tax--a not inconsiderable bite out of spendable income; since the tax rate is now 4-1/2 per cent of taxable earnings. Some further reduction in the saving rate is anticipated for the fourth quarter, but on balance the slow growth of disposable income is likely to be more fully reflected than in the third quarter in a smaller rise in consumption expenditures.

A net reduction in inventories of steel and autos (which together accounted for about half of the investment in nonfarm inventories in the second quarter) is likely this quarter. Steel inventories are expected to decline modestly, since the liquidation of steel stocks did not begin until August, and the high level of auto sales should result in a larger than seasonal reduction of auto stocks. Inventories in other areas in general are expected to increase in line with final sales, but the recent strength in retail sales may

also reduce stocks at some retailers (such as apparel and general merchandise). In the fourth quarter, the run-down in steel inventories will be much larger than in the third quarter, so that even if stocks "back-up" in other lines as a result of weak sales, total accumulation should drop further.

Housing starts, according to revised estimates, have been rising somewhat faster in recent months than previously had been estimated. The revised second quarter starts rate, plus a sharp spurt in July, indicates that expenditures for residential construction in the current quarter will be somewhat above the previous period. However, the July starts apparently reflected some non-recurrent factors of strength, and a decline in starts in August and September is still expected to reduce the quaeterly rate somewhat below that in April-June. Improving credit conditions should result in a rising rate of starts before the end of the fourth quarter, but probably too late to raise the fourth quarter average rate significantly above the third quarter. Expenditures for housing construction in the fourth quarter should be maintained close to the level of the second and third quarters.

The recently released official survey of intentions to invest in new plant and equipment suggests a smaller rise in the second half of the year, and particularly in the fourth quarter, than the May survey had shown. A much sharper dip in outlays apparently took place in the second quarter than was indicated formerly (or is reflected in the current official estimates of GNP) but the decline is expected to be recovered in the third quarter. Both third and fourth quarter

fixed investment is now expected to increase little from the rate in the first quarter of the year. Outlays in both the manufacturing and commercial sectors are expected by business to be appreciably lower at the end of the year than previously reported.

No further rise after July (when the Federal pay-raise operated to increase spending) is anticipated for either defense or nondefense purchases of goods and services except for CCC commodity loans,which because of record crops are exceeding January Budget estimates. A leading indicator of defense expenditures--"gross national defense obligations incurred outside the Federal budget"-- leveled off several months ago, indicating that the peak may already have been reached in defense procurement. Total Federal expenditures (NIA basis) in the third quarter are estimated at a rate of about $185.0 billion, which is close to the rate now estimated for the entire fiscal year; a bulge in fourth quarter non-defense expenditures reflects CCC outlays.

The Federal deficit is expected to decline from a rate of over $10 billion in the second quarter to between $6 and $6.5 billion in the second half of the year. (The drop would be larger, except that declining corporate profits are projected to offset some of the increase in receipts that otherwise would result from the surtax.) Owing to the retroactive feature of the personal income surcharge and a rise in social security taxes, a substantial further increase in tax receipts will occur early next year.

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September 4, 1968

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

	1967	1968 Proj.	1967 III	1967 IV	1968 I	1968 II*	1968 Projected III	1968 Projected IV
Gross National Product	789.7	854.9	795.3	811.0	831.2	851.6	863.8	872.8
Final sales	783.6	849.8	789.9	802.7	829.1	841.6	859.3	869.3
Private	605.2	652.9	610.3	619.2	638.6	646.0	659.8	667.3
Personal consumption expenditures	492.2	532.7	495.5	502.2	519.4	527.6	538.5	545.1
Durable goods	72.6	80.4	73.1	74.2	79.0	80.9	81.4	80.2
Nondurable goods	215.8	231.8	216.4	218.4	226.5	228.2	234.4	237.9
Services	203.8	220.5	205.9	209.6	213.9	218.4	222.7	227.0
Gross Private domestic investment	114.3	123.1	114.7	121.8	119.7	127.4	123.2	122.1
Residential construction	24.6	29.5	26.0	28.5	29.1	29.5	29.9	29.6
Business fixed investment	83.6	88.6	83.3	85.0	88.6	87.9	88.8	89.0
Change in business inventories	6.1	5.0	5.3	8.3	2.1	10.0	4.5	3.5
Nonfarm	5.6	4.7	4.8	7.1	1.6	9.7	4.5	3.0
Net Exports	4.8	2.2	5.4	3.4	1.5	0.9	2.6	3.6
Gov't. purchases of goods & services	178.4	196.9	179.6	183.5	190.5	195.6	199.5	202.0
Federal	90.6	100.3	91.3	93.5	97.1	100.0	101.8	102.3
Defense	72.4	79.2	72.9	74.6	76.8	79.0	80.5	80.5
Other	18.2	21.1	18.4	19.0	20.3	21.0	21.3	21.8
State & local	87.8	96.6	88.4	90.0	93.4	95.6	97.7	99.7
Gross national product in constant (1958) dollars	673.1	701.2	675.6	681.8	692.7	702.3	704.6	705.3
GNP implicit deflator (1958=100)	117.3	121.9	117.7	118.9	120.0	121.2	122.6	123.7
Personal income	628.8	683.2	633.7	645.2	662.7	678.1	691.8	700.0
Wages and salaries	423.4	461.7	426.3	436.4	448.3	457.6	467.3	473.6
Disposable income	546.3	587.8	550.0	559.6	574.4	586.3	592.2	598.2
Personal saving	40.2	40.7	40.5	43.4	40.8	44.4	39.2	38.5
Saving rate (per cent)	7.4	6.9	7.4	7.8	7.1	7.6	6.6	6.4
Corporate profits before tax	81.6	88.6	80.8	85.4	88.9	91.1p	88.5	86.0
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	151.2	174.3	152.2	156.4	166.6	171.5p	178.9	180.0
Expenditures	163.6	182.1	165.1	168.6	175.1	181.7	185.1	186.5
Surplus or deficit (-)	-12.4	-7.8	-12.9	-12.2	-8.6	-10.2p	-6.2	-6.5
Total labor force (millions)	80.8	82.5	81.1	81.6	81.9	82.2	82.7	83.0
Armed forces "	3.4	3.6	3.5	3.5	3.5	3.5	3.6	3.6
Civilian labor force "	77.3	78.9	77.6	78.2	78.4	78.7	79.1	79.4
Unemployment rate (per cent)	3.8	3.8	3.9	3.9	3.6	3.6	3.7	4.0
Nonfarm payroll employment (millions)	66.0	67.9	66.1	66.7	67.4	67.8	68.1	68.2
Manufacturing	19.4	19.6	19.3	19.5	19.6	19.7	19.7	19.5
Industrial production (1957-59=100)	158.0	162.9	157.2	159.5	162.1	163.8	163.2	162.5
Capacity utilization, manufacturing (per cent)	85.3	83.5	84.3	84.7	84.9	84.5	83.0	81.5
Housing starts, total private (millions A.R.)	1.29	1.44	1.41	1.45	1.50	1.44	1.40	1.40
Sales new U.S.-made autos (millions, A.R.)	7.57	8.37	7.57	7.44	8.19	8.44	8.60	8.25

* Second quarter data subject to revision to lower plant and equipment expenditure levels from new Commerce-SEC survey. Third quarter projections for business fixed investment tied to first quarter estimates.

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1967	1968 Proj.	1967 III	1967 IV	1968 I	1968 II	1968 Projected III	1968 Projected IV
	--In billions of dollars--							
Gross National Product	42.1	65.2	15.1	15.7	20.2	20.4	12.2	9.0
Final sales	50.8	66.2	11.9	12.8	26.4	12.5	17.7	10.0
Private	28.6	47.7	9.6	8.9	19.4	7.4	13.8	7.5
GNP in constant (1958) dollars	16.0	28.1	6.4	6.2	10.9	9.6	2.3	0.7
Final sales	24.0	29.3	3.5	3.4	16.9	2.2	7.5	1.7
Private	9.8	21.1	3.1	2.8	12.4	-0.5	7.0	1.0
	--In Per Cent Per Year--							
Gross National Product	5.6	8.3	7.7	7.9	10.0	9.8	5.7	4.2
Final sales	6.9	8.4	6.1	6.5	13.2	6.0	8.4	4.7
Private	5.0	7.9	6.4	5.8	12.5	4.6	8.5	4.5
Personal consumption expenditures	5.7	8.2	4.2	5.4	13.7	6.3	8.3	4.9
Durable goods	3.0	10.7	-1.6	6.0	25.9	9.6	2.5	-5.9
Nondurable goods	4.4	7.4	2.0	3.7	14.8	3.0	10.9	6.0
Services	8.2	8.2	8.5	7.2	8.2	8.4	7.9	7.7
Gross private domestic investment	-5.4	7.7	26.4	24.8	-6.9	25.7	-13.2	-3.6
Residential construction	-0.8	19.9	58.1	38.5	8.4	5.5	5.4	-4.0
Business fixed investment	2.8	6.0	2.9	8.2	16.9	-3.2	4.1	0.9
Gov't purchases of goods & services	14.2	10.4	5.2	8.7	15.3	10.7	8.0	5.0
Federal	17.1	10.7	5.8	9.6	15.4	11.9	7.2	2.0
Defense	19.5	9.4	4.4	9.3	11.8	11.5	7.6	0.0
Other	8.3	15.9	11.2	13.0	27.4	13.8	5.7	9.4
State & local	11.4	10.0	5.5	7.2	15.1	9.4	8.8	8.2
GNP in constant (1958) dollars	2.4	4.2	3.8	3.7	6.4	5.5	1.3	0.4
Final sales	3.7	4.4	2.1	2.0	10.0	1.3	4.3	1.0
Private	1.9	4.0	2.4	2.1	9.3	-0.4	5.1	0.7
GNP implicit deflator	3.1	3.9	3.8	4.1	3.7	4.0	4.6*	3.6
Personal income	7.2	8.7	7.8	7.3	10.8	9.3	8.1	4.7
Wages and salaries	7.3	9.0	8.3	9.5	10.9	8.3	8.5	5.4
Disposable income	6.8	7.6	6.3	7.0	10.6	8.3	4.0	4.1
Corporate profits before tax	-4.7	8.6	2.5	22.8	16.4	9.9p	-11.4	-11.3
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	5.7	15.3	10.8	11.0	26.1	11.8p	17.3	2.5
Expenditures	14.9	11.3	8.9	8.5	15.4	15.1	7.5	3.0
Nonfarm payroll employment	3.1	2.9	2.4	3.6	4.2	2.4	1.8	0.6
Manufacturing	1.0	1.0	-2.1	4.1	2.0	2.0	0.0	-4.1
Industrial production	1.1	3.1	3.3	5.9	6.5	4.2	-1.5	-1.7
Housing starts, total private	10.3	11.6	66.1	11.3	13.8	-16.0	-11.1	0.0
Sales new U.S.-made autos	-9.7	10.6	-26.6	-6.9	40.3	12.2	7.6	-16.3

* Excluding the pay increase of Federal government military and civilian employees, the annual rate of increase is 4.0 per cent.

Industrial production. In August, industrial production is tentatively estimated to have declined about 2 points from the preliminary July level of 165.3, reflecting a 25 per cent cutback in steel output following the labor contract settlement. The August drop in steel was especially severe compared to contract settlements in 1963 and 1965, as shown in the table. In 1963 and 1965, the decline in steel production was spread over a four month period, and amounted to 1.7 points and 2.3 points, respectively, in the total index. The largest monthly decline in those periods was in September 1965 and amounted to 1 point in the total index. In both 1963 and 1965, industrial production excluding steel was rising (see table). In August 1968, however, there is little indication (on the basis of incomplete data) of any marked upward movement in other segments of the index.

CHANGES IN INDUSTRIAL PRODUCTION
FOLLOWING STEEL CONTRACT SETTLEMENTS
(1957-59=100, seasonally adjusted)

1963

	May	June	July	Aug.	Sept.	Per Cent Change May to September
Total index	124.4	125.6	125.6	125.4	125.6	1.0
Steel	129.3	126.1	117.1	102.6	100.0	-22.7
All Other	124.0	125.4	126.1	126.7	127.2	2.6

1965

	July	Aug.	Sept.	Oct.	Nov.	Per cent Change July to November
Total index	144.3	144.9	144.1	145.5	146.7	1.7
Steel	152.2	143.3	125.0	115.8	110.5	-27.4
All Other	142.8	145.0	145.2	147.2	148.8	4.2

With steel consuming industries working off inventories built up prior to the contract settlement, steel production in September will probably continue close to the reduced rate reached in the last week of August and for the month as a whole will be down about 7 per cent from August.

Recovery in industrial production from the June 1967 low was not limited to the steel industry, as shown in the table. Output increases were widespread among other industries. The .6 point estimated increase in the total index from June to July 1968 was the result of a further rise in output of materials including steel. In August auto assemblies, after allowance for the model changeover period, were about unchanged from the July rate. Output of other consumer goods and business equipment probably changed little, and, as mentioned earlier, there are no indications of any marked change either up or down to offset or accentuate the indicated decline in iron and steel output.

INDUSTRIAL PRODUCTION
POINTS IN THE TOTAL INDEX

	1967 Low		Change	
	June	July 1968	Index points	Per cent
Total index*	155.6	165.3	9.7	6.2
Consumer goods	47.5	50.3	2.8	5.9
Automotive products	4.8	5.7	.9	18.8
Home goods	7.2	7.8	.6	8.3
Apparel	7.2	7.6	.4	5.6
Staples	28.2	29.1	.9	3.2
Business equipment	21.2	21.4	.3	1.4
Defense equipment	5.7	6.2	.5	8.8
Durable materials	39.8	42.9	3.1	7.8
Steel	6.6	8.3	1.7	25.8
Nondurable materials	41.7	44.7	3.0	7.2

* Does not add to total because of rounding.

Capacity utilization. The August rate of manufacturing capacity utilization is now estimated to be about 83 per cent, down sharply from the 84.5 per cent recorded in July. The decline is the result of reduced steel production.

Most manufacturing industries appear to have considerable unused capacity. Aircraft, motor vehicle, petroleum and rubber industries are exceptions.

UTILIZATION RATES
(per cent)

Industry	1967		1968				
	QIII	QIV	Q I	Q II	June	July	Aug. (e)
Manufacturing	84.3	84.7	84.9	84.5	84.6	84.5	83.0
Primary processing industries	83.0	85.3	85.5	86.1	86.1	86.2	--
Advanced processing industries	85.2	84.3	84.4	83.4	83.6	83.3	--

e -- estimated.

Retail sales. August weekly retail figures suggest that sales last month continued at about the high July level. July had surged 3.0 per cent above June, for the largest month-to-month gain since mid-1966. In August there apparently was no net gain, but this in itself suggests strength since large month-to-month increases in this series are often followed by some decline in the next month.

The July gain had been greater for durables (4.8 per cent) than for nondurables (2.1 per cent), but within the nondurables group, general merchandise stores showed unusual strength (5.4 per cent). Weekly figures suggest that in August there continued to be greater strength in durables than in nondurables, which may have declined slightly. Stronger sales in the automotive group, despite the decline in unit auto sales, appear to have offset lower sales in other durable goods categories. (In July the automotive group had also moved ahead more strongly than other durable goods categories.) Among nondurable goods, the food group in August may have been about even with July while general merchandise may have declined somewhat.

SEASONALLY ADJUSTED RETAIL SALES
Month-to-Month Percentage Changes

	April	May	June	July
All retail	-1.8	1.4	0.8	3.0
Durable	-2.4	2.3	1.2	4.8
Automotive	-3.9	5.2	2.6	5.6
Furniture & appliances	-1.5	0.4	0.1	3.5
Nondurable	-1.5	0.9	0.6	2.1
Food group	0.3	1.3	-0.1	0.6
General merchandise	-2.7	0.0	3.3	5.4

Unit sales and stocks of autos. Dealer sales of new domestic autos in August were at a seasonally adjusted annual rate of 8.6 million units compared with 9.1 million in July and 7.0 million a year earlier. The August level of sales was about the same as the average for the first seven months of 1968. Stocks of new cars declined about seasonally from the advanced end of July level, but were about one-third above a year earlier. However, the supply of new cars is estimated to have been equal to about 48 days of sales, not much above the 45 days a year earlier. The larger dealer inventories, price cuts available at model change-over time, and anticipated price increases for the 1969 model have been sustaining forces in the auto market.

Consumer credit. The use of consumer instalment credit continued to increase in July. Extensions, that is credit granted during the month, reached an all time high of nearly $7.7 billion--a seasonally adjusted annual rate of $92 billion. This July spurt reflected increased borrowing for all major purposes: autos, other consumer durables, personal loans, and home repair and modernization.

Although repayments on consumer instalment debt also moved up to a new record level during July, the even stronger growth in extensions produced a net increase of $9.3 billion in outstandings (seasonally adjusted annual rate), the highest rate of increase for instalment credit outstanding in any month since November 1965. The present increase, however, is still well below the record rise of $8.9 billion (annual rate) in April 1965, a figure that was even larger relative to consumer expenditures than in the current period.

Consumer buying expectations. The Census Consumer Buying Expectations Survey, taken in early July after the passage of the surtax but before the increased withholdings took effect, suggests a continuation of the present high level of demand for durables and houses despite some deterioration in respondents' evaluation of their income situation.

The survey suggests that sales of all new automobiles (foreign and domestic) will be at an annual rate of 9.2 million units in the final quarter of this year and the first quarter of 1969. The fourth quarter forecast is below the current unusually high rate of sales but consistent with our projection of sales of 8.25 million U.S.-made automobiles in the final quarter of the year. Plans to buy used cars declined from April but are still slightly above a year ago.

The index of expected expenditures for houses, at 117.9, is up strongly both from April, 114.7, and a year ago, 106.6. Much of the increase reflects the expectation of paying more for a house. In addition, the probability of a household planning to purchase a house in the next 6 months was 5 per cent above the figure a year earlier. On the other hand, the index of expected expenditures for household durables showed no significant change from April, and was about 1 per cent above a year ago. This index has shown very little change in any of the 7 surveys for which it is available.

The index of family income expectations for the next year declined for the second survey in a row, as optimism decreased among families with incomes under $5,000. These families represent over one

third of the sample. Families considered their change in income from a year ago less favorable than a similar year-over-year comparison in the second quarter, but their income evaluation was still well avove the same comparison for the third quarter of 1967.

This new Census survey has yet to establish its usefulness as a leading indicator. Since the series was changed in January 1967, the widely followed component index for expected purchases of new cars--which had been the best component of the 1959-1966 survey--has incorrectly indicated the direction of movement in the quarter following the survey about half of the time. Apparently, the new procedure of asking respondents to assign a weight from 0 to 100 to their expenditures plans is not adding to the reliability of the series.

INDEXES OF CONSUMER PLANS TO PURCHASE
(Average of January 1967 and April 1967 = 100.0)

Date of survey	New Cars	Used Cars	Houses	Household Durables
1967				
January	101.0	98.7	98.1	100.8
April	99.0	101.3	101.9	99.2
July	104.7	101.0	106.6	100.9
Oct	102.2	101.6	102.5	99.4
1968				
January	103.9	103.4	105.7	100.1
April	104.3	103.9	114.7	101.6
July	106.4	102.0	117.9	101.7

Durable goods orders and shipments. Manufacturers new orders for durable good in July showed an increase of 0.5 per cent from the June level. But this rise resulted entirely from a sharp increase in aircraft orders and durable orders excluding aircraft declined. On the other hand, durable goods shipments increased by 3.1 per cent in July--to a record level.

Although there were offsets within each group, new orders declined for primary metals (iron and steel was down 13 per cent) and fabricated metals. A 25 per cent rise in aircraft orders resulted in an increase in the transportation and in the defense products groupings (which includes aircraft). Orders declined for consumer durables and for the machinery and equipment groupings, although orders for machinery and equipment remained above the level prevailing in early 1968.

Unfilled orders declined for the second straight month. Declines were widespread but the sharpest drop occurred at iron and steel manufacturers.

Manufacturers' inventories. In July the book value of inventories at manufacturers increased $295 million from a June level which had been revised up to show an increase of $113 million. The July increase was less than two-thirds of the average monthly increase in the second quarter.

Although stocks rose at both durable and nondurable manufacturers, the bulk of the increase occurred in the latter group. Food and chemical manufacturers showed the largest increases in the nondurable group. Among the durable goods, holdings in electrical machinery,

consumer durable goods and defense products increased. Inventories held by steel and machinery and equipment producers declined.

Both durable and nondurable goods shipments increased substantially in July. Consequently, the over-all inventory shipments ratio fell to 1.66, the lowest level since mid-1966.

Manufacturers' capital appropriations. The latest National Industrial Conference Board's survey indicates that in the second quarter manufacturers' net new appropriations increased 2 per cent from the first quarter level. However, the second quarter level of these appropriations remained below the average for 1967.

Since capital expenditures by manufacturers remained at the first quarter's level--the lowest since the first quarter of 1966--the backlog of unspent appropriations increased. At current levels, the backlog is the highest since the fourth quarter of 1966.

The increase in total appropriations resulted from offsetting movements at durable and nondurable manufacturers. Durable manufacturers increased their appropriations by 5 per cent while nondurable manufacturers appropriations showed a slight decline. Both groups, however, increased their backlogs of unspent appropriations.

Anticipated expenditures for plant and equipment. The August Commerce-SEC Survey indicates that firms have revised downward significantly their anticipated expenditures on plant and equipment from the levels indicated in the May survey. (These data are confidential until released, either September 6 or early the following week.) The

latest survey, the first since the enactment of the surtax, now reports the prospective increase in plant and equipment expenditures for the year 1968 at only 4.4 per cent; the May survey had indicated an increase of 6.7 per cent.

ANTICIPATED EXPENDITURES FOR NEW PLANT AND EQUIPMENT

(Annual Rate, $ billion)

Date of Survey	Year 1968	Quarter I	II	III	IV
			All Firms		
May	65.8	64.9	64.6	66.0	67.5
August	64.4	64.9	62.8	64.9	65.2
			Manufacturing firms		
May	27.6	26.4	27.6	28.3	28.0
August	26.5	26.4	25.8	26.8	27.2

The final estimate for the second quarter now indicates that actual outlays declined by $2.1 billion from the first quarter whereas the May survey had suggested a decline of only $0.3 billion. Declines by manufacturing firms accounted for almost all of this shortfall. Manufacturers had expected to increase their outlays in the second quarter, but these actually declined by more than $0.5 billion.

Both manufacturers and all firms, taken together, now anticipate that this shortfall will be recouped in the third quarter. However, for the total, indicated expenditures in the second half of the year will be only slightly above the first quarter; the fourth quarter increase is anticipated to be only $250 million.

Revision of plans to purchase new plant and equipment have not been substantial in the other sectors, except for the "commercial and other" group. Utilities still expect lower outlays in the second half while anticipated expenditures by railroads have been revised upward. However, anticipated outlays by the "commercial and other" group--a series which is subject to considerable revision--have been revised down almost $1 billion for the fourth quarter.

Construction and real estate. Seasonally adjusted new construction put in place--revised upward somewhat for both June and July--edged higher in August, but remained slightly below the peak reached last February. Private nonresidential construction expenditures, in a downtrend since February, apparently changed little in August. However, residential construction moved temporarily higher, reflecting in part a much greater than expected reversal in the rate of housing starts in July. Also, public construction outlays rose further to a new record in August.

NEW CONSTRUCTION PUT IN PLACE
(Confidential FRB)

	August 1968 ($ billions)1/	Per Cent Change from	
		July 1968	August 1967
Total	83.2	+ 1	+ 8
Private	54.2	+ 1	+ 5
Residential	27.6	+ 1	+ 10
Nonresidential	26.6	--	--
Public	29.0	+ 2	+ 15

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

Private housing starts, which had declined further in June, soared above the 1.5 million annual rate in July, reflecting mainly an advance of four-fifths in the Northeast states from a reduced rate in June. Particular strength was reported in the New York City area, where excavation was begun for a few exceptionally large apartment projects, some with building permits issued nearly a year ago.

A major factor in the surge in the Northeast states probably was the long-anticipated one-time increase in usury ceilings, effective July 1, in New York and New Jersey where builders were apparently held back pending clearance by lenders of loans under the higher permissible rates now in effect. Another factor was an unusual increase in the number of working days from 20 in June to 22 in July this year--just the opposite of the usual pattern--for which no direct adjustment is incorporated by the Census Bureau in the starts series.

While single-family units also participated in the July starts advance, the particularly volatile multifamily starts series about matched the record 1963 level and accounted for 42 per cent of total starts.

Seasonally adjusted residential building permits, which include an allowance for working days, declined 4 per cent in July. Multifamily permits slipped by 8 per cent from a relatively high rate. Single-family permits, after a three month decline, edged slightly higher. Unlike starts, among the individual regions only the West posted an advance over the June rate of permits.

PRIVATE HOUSING STARTS AND PERMITS

	July 1968 (thousands of units)1/	Per cent change from	
		June 1968	July 1967
Starts	1,539	+ 14	+ 12
1-family	898	+ 14	+ 4
2-or-more family	641	+ 14	+ 26
Northeast	348	+ 79	+ 14
North Central	356	+ 12	+ 6
South	595	+ 9	+ 21
West	240	- 17	+ 2
Permits	1,236	- 4	+ 9
1-family	648	+ 1	- 1
2-or-more family	588	- 8	+ 24

1/ Seasonally adjusted annual rates; preliminary.

During June, the latest month for which data are available, sales of new homes by speculative builders increased 5 per cent (seasonally adjusted annual rate). But in the second quarter as a whole, sales were down somewhat further from the first quarter owing to the still relatively limited supply of new houses available for sale under the conditions of gradually increasing restraint which had prevailed in the residential mortgage market for more than a year.

Indications since the mid-June passage of the fiscal package of possible easing in underlying mortgage market conditions have buoyed hopes of a sustained recovery in housing activity before the year end. These hopes have been strengthened recently by the brighter inflow expectations of some intermediaries, some reduction in liquidity requirements by the Federal Home Loan Bank Board, and other developments. In

the current quarter, however, given the low inflow of savings earlier this year, a declining rate of housing starts would appear to be indicated for August and especially September from the high July rate. Consequently, although demand pressures are strong, the third quarter average may run at a seasonally adjusted annual rate of 1.4 million--higher than originally projected, but still somewhat below the upward-revised second quarter.

The labor market. The employment situation appears to have continued firm in August. The level and rate of insured unemployment continued below year-earlier levels thouugh mid-August. But youngsters--generally not protected by unemployment insurance and, therefore, not reflected in these figures--have carried the burden of easing demand this summer. Some 1.8 million 16 to 21 year-olds were jobless this June and July, about 150,000 more than year earlier. It is probable that many of these youngsters withdrew from the labor force in August.

No August employment data are available yet, but easing of growth in July is even more clearly evident in the revised July figures. As revised, the preliminary employment increase of 63,000 in manufacturing in July is virtually eliminated, reflecting sizable downward adjustments in electrical equipment, apparel, fabricated metals, and food, along with smaller reductions in 10 other manufacturing industries. (These data are confidential until released September 11th.) The only large employment increase remaining in manufacturing--43,000 in transportation equipment--was mainly due to a later than

usual model changeover in the auto industry. Exclusive of transportation equipment, manufacturing employment declined by nearly 40,000 in July.

With demand still strong in August, employment is likely to show a further gain; however, later in the year easier demand for labor should weaken the employment picture. Increased tax withholdings and rising prices are likely to dampen consumption, particularly affecting industries such as television, recreation goods, clothing, and, autos. At the same time, the heavy-goods industries are entering a phase of comparatively slow growth. With capacity utilization rates likely to dip, and construction activity likely to remain fairly stable, demand for producers durables may rise only modestly in the last half. In addition, the defense industries are faced with a slow-down in purchases and the steel adjustment will likely last through year end. All these factors point to widespread but modest reductions in manufacturing employment.

In construction, unless there is an unexpected and substantial pickup in building activity, employment, after falling by 200,000 between February and July, is likely to stabilize at about 3.2 million for the remainder of the year. Service and trade employment is likely to continue up, but at a slightly slower pace. Federal government employment is expected to decline this fall and winter, while State and local government employment is likely to expand at a reduced pace.

With employment growth easing labor force increases are likely to fall somewhat below projected long-term "normal" growth of about 1.5 million a year. But the labor force is likely to rise by more than employment, and the total unemployment rate will move irregularly higher over the fall and winter months, and may average about 4.0 per cent for the fourth quarter.

Wage changes. Collective bargaining settlements in the first half of this year provided substantially higher first-year wage increases--7.5 per cent--than in contracts negotiated in 1967 or 1966. But wage rate increases provided for later years of the contract were substantially lower--about 4 per cent--so that the annual rate of increase when averaged over the life of the contract was little changed from the average for 1967. The spread of "front-loading" to settlements in nonmanufacturing industries this year has been an important factor in the upward pressure on wage rates. As these contracts mature, the smaller wage rate increases of second subsequent years will tend to moderate labor cost pressures somewhat.

WAGE CHANGES IN COLLECTIVE BARGAINING SITUATIONS

	Median percentage change		
	1966	1967	1st half 1968
First-year increases:	4.8	5.7	7.5
Manufacturing	4.2	6.4	7.7
Nonmanufacturing	5.0	5.0	7.5
Annual rate of increase during life of contract:	3.9	5.0	5.2
Manufacturing	3.8	5.1	5.2
Nonmanufacturing	3.9	5.0	5.3

Wholesale prices. Average prices of industrial commodities are estimated by the BLS to be unchanged in August, while prices of agricultural commodities have declined following a one month rise in July. The preliminary total wholesale price index declined 0.4 per cent to its June level of 108.7 per cent of the 1957-59 average.

It was expected that the general price increases first announced by the steel industry in early August would exert upward pressures on August figures, but the effective dates were later than the BLS pricing date of August 13th. Subsequently, additional selective price increases were announced and the average rise for all steel mill products is estimated to be about 2-1/2 per cent. This will be reflected in the September WPI and is likely to amount to an increase of about 0.1 per cent in the total index.

Most of the 0.4 per cent increase in the WPI for July was attributable to a temporary upturn in farm and food products, while grain prices continued to decline in July and August. Wheat prices have dropped 10 per cent since June and are 20 per cent below last season. Prices of other grains and soybeans have also declined in line with a worldwide easing in supplies of major farm commodities. Reduced domestic supplies of cotton, fruits, and vegetables last season had led to higher prices during the first half of this year, but larger crops of these products are being realized this season.

Prices of industrial commodities in July increased by only 0.1 per cent as higher prices for lumber, textiles, leather, and rubber products were nearly offset by declines in fuels, chemicals, and metals--

especially nonferrous metals. The largest price rise was in lumber and wood products partly reflecting increased demands by lumber dealers to rebuild inventories and a higher rate of housing construction. Excess capacity for liquified petroleum gas and an improvement in copper supplies resulted in lower prices. Among final products there was a slight decline in wholesale prices of new cars resulting from intensified dealer incentive programs. On the other hand, prices of furniture, appliances, and automobile tires registered increases.

The further easing in upward pressure on industrial commodity prices shown in the BLS preliminary data for July has been confirmed by the release of the revised data shown below. The reduction in the number of price increases since the past winter and spring, as well as the large jump in the number of decreases in July, is impressive.

MONTHLY CHANGES IN WHOLESALE PRICES OF
225 INDUSTRIAL PRODUCT CLASSES

	January	February	March	April	May	June	July
Increases	127	131	110	115	90	90	87r
Decreases	36	25	30	38	42	38	55r
Unchanged	62	69	85	72	93	97	83r

Consumer prices. The consumer price index rose 0.5 per cent in July for the second consecutive month--the sharpest two-month increase since June-July 1957. More than one-half of the July increase was due to the increase of 0.7 per cent in consumer services, primarily mortgage interest and medical care charges.

Mortgage interest charges increased by 4-1/2 per cent (they increased nearly 4 per cent in June) and were 13-1/2 per cent above a year earlier. Property taxes and insurance rose 0.8 per cent, and domestic services were up 0.5 per cent. Over-all homeowner costs rose 1.3 per cent in July. Medical care services increased 0.7 per cent as their steep climb was resumed following a moderate rise in June. Higher physician and dentist fees were mainly responsible for the increase, but hospital service charges also rose substantially.

Grocery-store prices advanced 0.8 per cent, a smaller increase than expected seasonally, and restaurant meals and between-meal snacks increased 0.6 per cent further. The rise in food prices at wholesale in July was followed by a decline in August which may limit the increase in retail food prices in August. Apparel prices declined less than expected seasonally in July, and footwear rose contraseasonally owing to increased demands and higher costs. Over-all, prices of commodities other than foods advanced 0.2 per cent instead of registering the slight decline that is usual for July.

Agricultural conditions. Based on August 1 conditions, crop production this year will top the record output of 1967 by 3 per cent and exceed the 1957-59 average by 21 per cent. Prior to the August 1 crop report, it had been assumed that crop output would about equal 1967.

CROP PRODUCTION
1957-59 = 100

	1965	1966	1967	1968 1/
All crops	115	111	117	121
Feed grains	111	110	124	123
Hay and forage	112	110	115	110
Food grains	117	118	134	145
Vegetables	108	109	112	115
Sugar crops	138	137	136	161
Cotton	121	78	62	89
Tobacco	107	109	116	105
Oil crops	153	164	171	185
Cropland used	94	93	96	95
Crop production per acre	122	119	122	127

1/ Based on August 1 conditions.

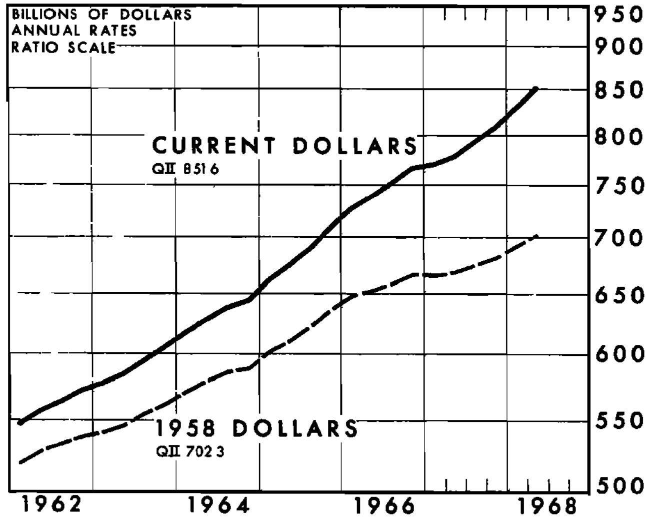
The new crop report has resulted in raising estimated CCC net expenditures for price supports this year $700 million above the January Document estimate of $2,859 million. The increase will go largely for price support loans on 1968 crops of feed grains, wheat, and soybeans.

Abroad, as well as at home, surplus production of farm commodities is in prospect in contrast to the critical shortages of two years ago. Even in India transportation and storage of the huge crops are a problem. Pressure on prices and on the price stabilization programs of the free world are great. The U.S. net expenditure for stabilization of farm prices, now estimated at $3.5 billion for 1968-69 compares with an estimated net expenditure in the EEC countries of $2.7 billion in 1968-69.

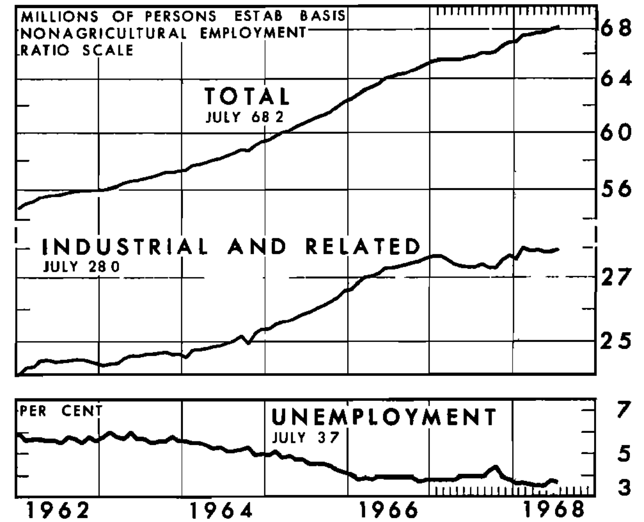
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED

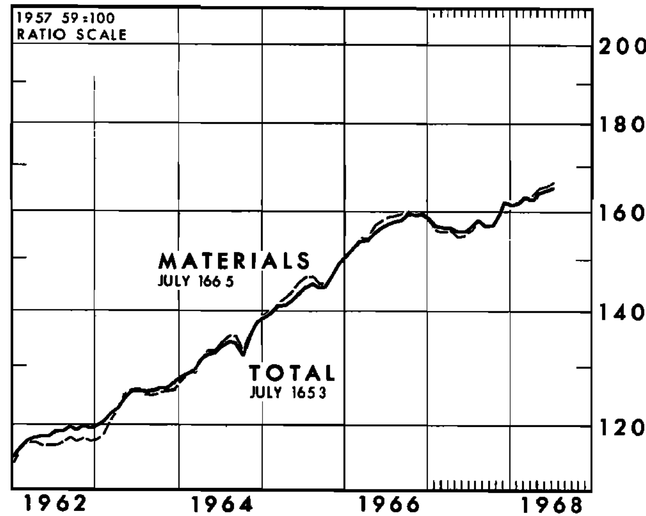
GROSS NATIONAL PRODUCT



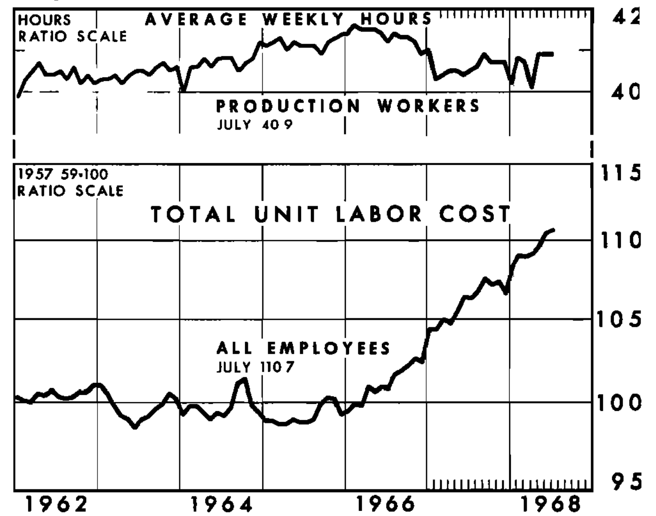
EMPLOYMENT AND UNEMPLOYMENT



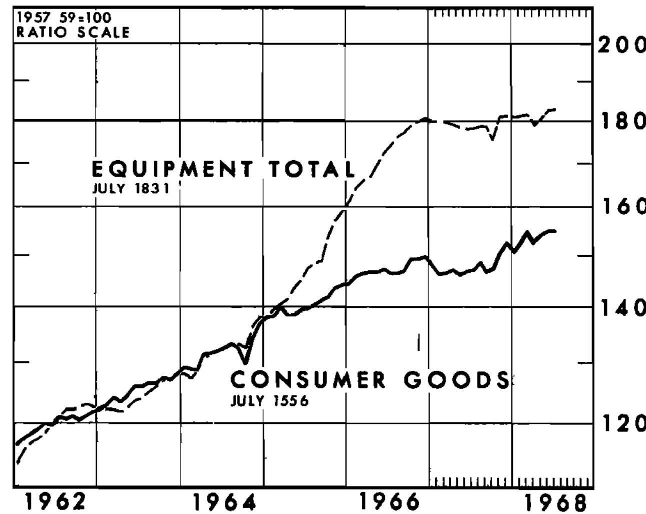
INDUSTRIAL PRODUCTION-I



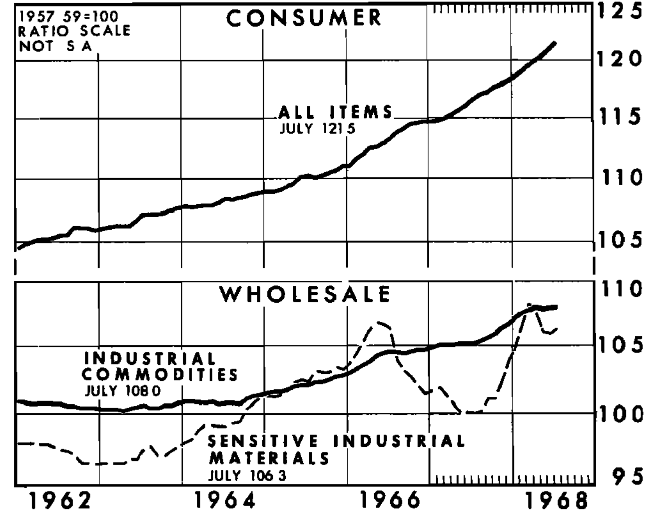
WORKWEEK AND LABOR COST IN MFG



INDUSTRIAL PRODUCTION-II



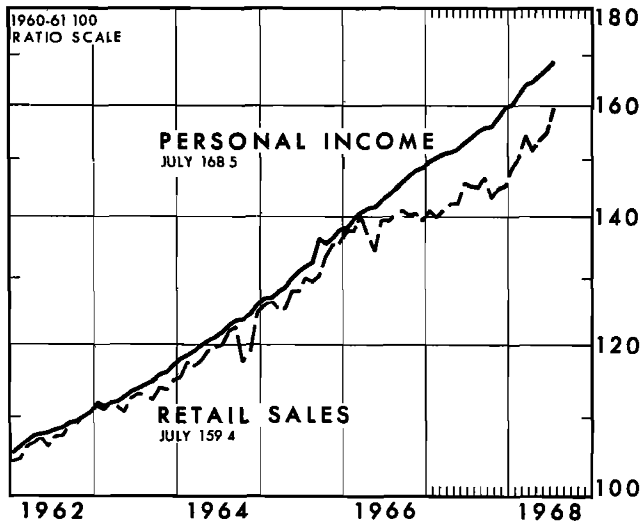
PRICES



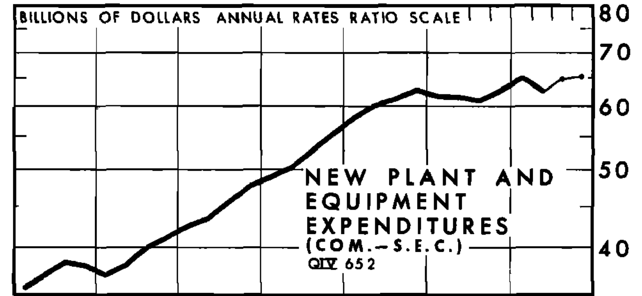
ECONOMIC DEVELOPMENTS - UNITED STATES

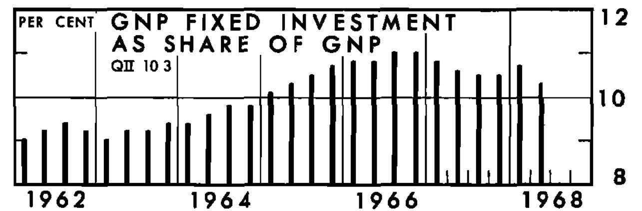
SEASONALLY ADJUSTED

INCOME AND SALES

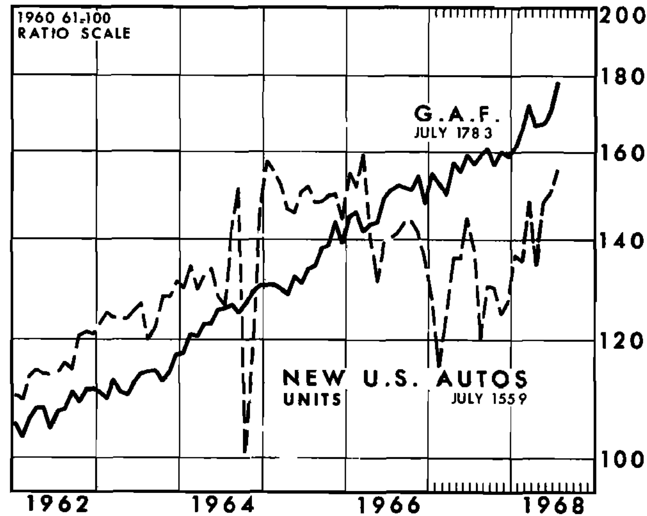


BUSINESS INVESTMENT

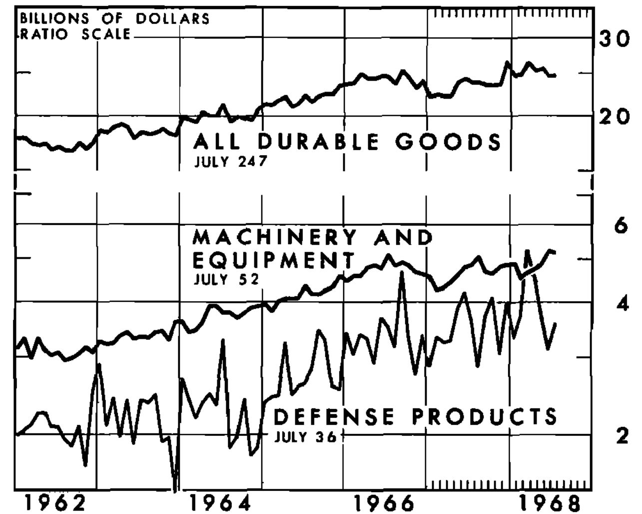




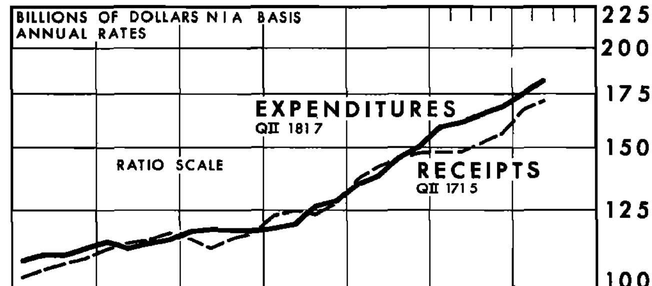
RETAIL SALES

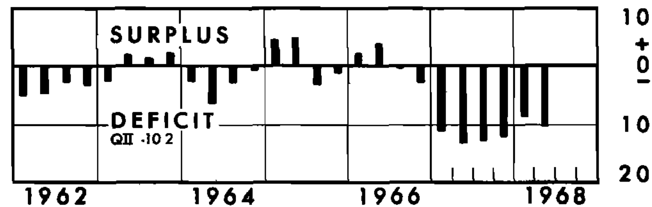


MANUFACTURERS' NEW ORDERS

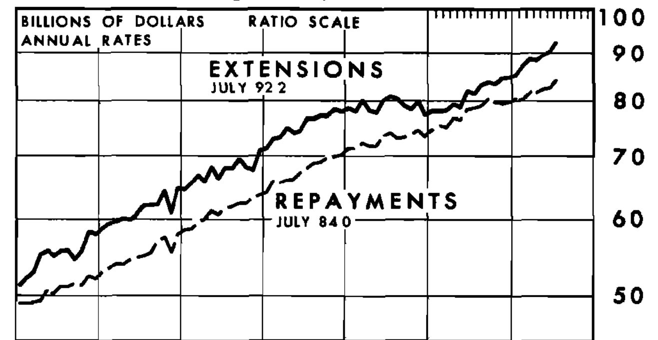


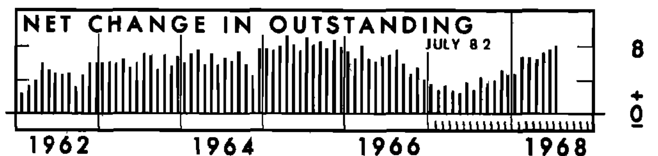
FEDERAL FINANCE—N.I. ACCOUNTS





INSTALMENT CREDIT





DOMESTIC FINANCIAL SITUATION

Bank credit. Total loans and investments at all commercial banks are estimated to have increased at approximately a 14 per cent annual rate in August, about half the exceptionally rapid July rate of growth. In July, a $4 billion Treasury cash financing in the latter part of the month contributed substantially to the increase in bank credit. In August, too, Treasury financings added to bank credit growth as the Treasury raised nearly $2 billion of new cash and refunded a sizable amount of maturing coupon issues. In addition to the effects of Treasury financing, bank credit expansion in August was augmented by large bank acquisitions of municipal and agency issues as well as further growth in virtually all major loan categories.

NET CHANGE IN BANK CREDIT
All Commercial Banks
(Seasonally adjusted annual rates in per cent)

	1967	1968			
		First half	First 8 mos.	July-Aug.	Aug.1/
Total loans & investments2/	11.6	6.2	9.7	19.5	14.1
U.S. Gov't. securities	11.4	2.7	9.5	29.8	17.3
Other securities	26.1	6.5	9.5	18.0	20.6
Total loans	8.3	7.1	9.8	17.2	12.1
Business loans	9.8	9.6	10.1	11.3	11.8
MEMO:					
Credit Proxy3/	11.6	5.5	8.2	15.6	20.4

1/ All August rates are preliminary estimates based on incomplete data and are subject to revision.
2/ Last Wednesday of the month series.
3/ Monthly average of daily figures, adjusted to include Euro-dollar borrowing.

Business loans, as measured by the end-of-month series, are estimated to have increased $900 million in August, or at about the pace of the previous two months. Weekly reporting bank data on business loans by industry, however, do not indicate any broad strength in loan demand. With the exception of some mild expansion in textiles, construction, and public utilities, bank loans to most industrial categories displayed about normal or somewhat less than normal growth over the first three weeks of the month. While a few banks indicated somewhat greater leniency in lending to established and local customers, the August Lending Practices Survey gave no indication that easier lending policies were a significant factor affecting the recent volume of business loan expansion. (See Appendix A.)

In spite of recent uncertainty as to the course of interest rates in the near future and the continued high cost of dealer financing, security loans in August showed a moderate further increase--following the July surge--as dealers apparently are maintaining their high level of speculative inventories in hopes that interest rates will decline. Consumer loans also continued to expand at the increased pace of recent months, associated in large part with financing of the high volume of automobile sales. Growth in real estate loans remained moderate, and may reflect hesitancy on the part of some banks to expand commitments to acquire mortgages while inflows of consumer-type time and savings deposits continue at the moderate pace of recent months.

With the availability of funds improved, banks acquired approximately $2.0 billion of securities in August in order to take

advantage of the relatively high yields still available. Since midyear--when the marked improvement in deposit inflows began--banks have taken nearly $5.0 billion of securities into portfolio. About 60 per cent of the July-August increase in bank security holdings represents Governments, most of which were acquired in the recent Treasury financings. (Net bank acquisitions of the new 6-year notes offered in the midmonth refunding accounting for most of the $900 million increase in Government security holdings in August.)

Moreover, banks also added approximately $1.1 billion of other securities to their portfolios in August bringing net acquisitions since midyear to almost $2.0 billion. While much of the August increase in these holdings was in short-term municipals, banks--as in July--acquired a significant amount of the relatively high yielding longer-term issues.

Bank deposits. Following an increase of almost $2.5 billion in July, time and savings deposits at all commercial banks in August are estimated to have increased by another $3.3 billion, on a daily average basis, or at about a 20.8 per cent annual rate. As in July, a large part of this rapid expansion was attributable to CD sales by banks, since August inflows of consumer-type time and savings deposits appear to have remained at the moderate pace of recent months. Time deposits held by state and local governments also rose more than usual, probably reflecting in part the temporary investment of funds obtained in recent capital market financings.

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

	1968				
	April	May	June	July	August
Total time & savings deposits	-226	-12	- 79	512	545
Consumer-type deposits	-125	90	101	102	121
Savings deposits	-175	10	47	-77	7
Time deposits, IPC (Other than CD's, IPC)	51	80	54	178	114
Negotiable CD's	-192	-49	- 68	436	267
All other time deposits	90	-54	-112	-26	157

Despite the recent back up in some market rates of interest, CD's still remain competitive with most other money market instruments, and large banks added another $800 million to their outstandings during the first three weeks in August--bringing this total to a new high of $22.3 billion. The increase in outstanding CD's occurred almost exclusively at banks outside of New York and Chicago, where loan demand for the most part has remained somewhat stronger. Banks in New York and Chicago have ready access to the Euro-dollar market and as the cost of these funds fell slightly below that of CD's during August, they relied more heavily on the Euro-dollar than on the CD market as a source of funds. (Over the four weeks ending August 28, banks in New York and Chicago account for all of the $900 million increase in head office liabilities to their foreign branches.) However, interest in CD's by outside banks also appears to be waning, as indicated by the successively smaller weekly increases in CD's outstanding at these banks during August.

With most market rates of interest unchanged to somewhat higher than early in the month, inflows of consumer-type time and savings deposits at large banks during the first three weeks in August remained at about the moderate pace prevailing since the end of April. Although the average weekly change in these deposits during August rose somewhat over that of recent months, much of this increase occurred at banks in New York during the week of the Treasury financing. Savings deposits at large banks, after declining in July, showed only nominal growth compared to most recent past years. Inflows of savings deposits at country banks, although much greater than those at large banks, also were below the comparable period of last year. Time certificates and open accounts at large banks, however, continued to expand fairly rapidly, matching the expansion in 1967.

Following the rapid July increase, the money stock, on a daily average basis, is estimated to have expanded at a much reduced 3.8 per cent annual rate in August. This slower rate of expansion may reflect some movement of private demand balances into U.S. Government deposits in response to the recent Treasury financing, although the reduced level of stock market activity in August probably also contributed to a lower transactions need for cash.

Nonbank depositary intermediaries. During the first half of August, savings appeared to be flowing into mutual savings banks at a more rapid rate than in July, as judged by data from the fifteen largest savings banks in New York City, the only institutions for which August

data are available.[1/] Moreover, although the increase in their passbook loans was sizable, it was considerably below that for May, the corresponding month in the reinvestment cycle.

SAVINGS INFLOWS: FIRST FIFTEEN DAYS OF THE MONTH
Fifteen Largest Savings Banks in New York City*
($ millions; seasonally adjusted)

	May	June	July	August
Savings inflow				
1965	31.9	39.5	40.3	32.1
1966	20.5	28.9	113.6	51.5
1967	78.3	73.6	58.1	56.6
1968	56.7	51.4	5.4	41.8
Increase in passbook loans				
1965	9.0	12.3	11.3	10.4
1966	15.3	16.3	12.6	13.8
1967	18.1	18.2	13.0	20.6
1968	30.3	34.6	13.1	19.4

* These banks account for 28 per cent of industry deposits.

During July, mutual savings banks' liquidity ratios[2/] continued to drift downward, while the net increase in mortgage holdings exceeded for the third consecutive month the continued large net acquisition of corporate securities. The savings and loan average liquidity ratio also dropped in July--from 10.0 per cent in June to 9.6 per cent, the lowest since November 1966. This reflected the FHLBB

1/ Savings and loan association and mutual savings bank data may be available around September 12.

2/ The liquidity ratio is U.S. Government plus cash holdings expressed as a per cent of total share capital.

regulatory change permitting a one-half percentage point decrease--to 6.5 per cent--in the required liquidity ratio to help stimulate mortgage lending. While the net increase in S&L mortgage holdings was not particularly large, it was presumably aided by the decrease in required liquidity.

Mortgage market developments. The residential mortgage market eased slightly further during August, judging from fragmentary reports received thus far. Weekly applications to FHA for insurance of existing-home mortgages, which usually fluctuate rather sensitively with general market conditions, tended higher through the week ended August 22, the latest available date. After changing little through mid-August, implicit yields in the FNMA weekly forward commitment auction of Government underwritten home loans available for future delivery to FNMA edged down in each of the three weeks following the initial reduction in the Federal Reserve discount rate effective August 16.

FNMA WEEKLY AUCTIONS
(6-month forward commitments)

Auction Date	Accepted bids ($ millions)	Implicit private market yield (per cent)
July 1	60.5	7.48
8	65.9	7.40
15	57.3	7.35
22	47.4	7.32
29	53.7	7.33
August 5	49.7	7.32
12	43.4	7.31
19	37.4	7.27
26	37.0	7.24
September 3	37.6	7.23

Note: Average secondary market yield after allowance for commitment fee and required FNMA stock purchase, assuming prepayment period of 15 years for 30-year mortgages. Yields shows are gross, before deduction of 50 basis point fee paid by investors to servicers.

During July as a whole, yields on certain FHA-insured mortgages traded in the private secondary market reversed their earlier uptrend and declined by as much as 10 basis points, according to the FHA series, affirming earlier indications of easing in this sensitive sector of the mortgage market. The decline was the first in 5 months, and the largest in more than a year and a half. Average discounts required by lenders on these loans dropped to 5-1/2 points--still large enough to inhibit some transactions financed with this type of credit but nevertheless the lowest in nearly a year.

In the more sluggish primary mortgage market, interest rates on conventional new-home loans increased less during July than in any of the 3 preceding months, based on the FHA series shown in the table. The Northeastern area again recorded the largest rise, reflecting further increases in usury ceilings in New Jersey and New York, both effective July 1, following an increase in Pennsylvania around mid-May.

During July, returns on Government underwritten as well as conventional mortgages again widened somewhat over yields on new issues of high-grade corporate bonds. The gross yield margin favoring these mortgages, while the most attractive in more than a year, continued considerably below spreads generally prevailing prior to 1965, even if some allowance is made for interim reductions in mortgage servicing costs.

AVERAGE RATES AND YIELDS ON SELECTED NEW-HOME MORTGAGES

	Primary Market: Conventional loans		Secondary Market: FHA-insured loans		
	Level (per cent)	Yield spread (basis points)	Level (per cent)	Yield spread (basis points)	Discount (points)
1967					
July	6.50	72	6.53	75	4.6
August	6.55	66	6.60	71	5.2
September	6.55	67	6.63	75	5.4
October	6.55	43	6.65	53	5.6
November	6.65	12	6.77	24	6.5
December	6.70	19	6.81	30	6.8
1968					
January	6.75	51	6.81	57	6.8
February	6.75	46	6.78	49	6.6
March	6.80	24	6.83	27	7.0
April	6.90	38	6.94	42	7.9
May	7.15	49	7.50e	84e	6.1e
June	7.25	60r	7.52	87r	6.3
July	7.30	76	7.42	88	5.5

Note: FHA series: interest rates on conventional first mortgages (excluding additional fees and charges) are rounded to the nearest 5 basis points; secondary market yields and discounts are for certain 6 per cent, FHA-insured Sec. 203 loans through April with data for May 1968 estimated by Federal Reserve based on the new 6-3/4 per cent regulatory rate. Gross yield spread is average mortgage return, before deducting servicing fees, minus average yield on new issues of high grade corporate bonds.

Confidential field reports from both FHA and VA indicated some improvement in the availability of mortgage funds by the end of July, particularly on long-term loans, as lenders apparently accelerated their new commitment approvals in order to lock up the high yields prevailing at the time. In view of this development, total outstanding

residential mortgage commitments of reporting thrift institutions rose in July for the first time in three months, according to the seasonally adjusted data shown in the table. At thrift institutions the backlog of mortgage commitments to be taken down in coming months remained quite high relative to their recent cash flow positions, undoubtedly also reflecting expectations of further improvement ahead in inflows.

RESIDENTIAL MORTGAGE COMMITMENTS OUTSTANDING
(Per cent increase from month to month)

	Thrift Institutions			Reporting life insurance companies	All reporting lenders
	All S&Ls	New York State savings banks	Total		
1967					
June	11.4	7.7	10.1	1.5	8.0
July	7.4	0.8	5.1	-1.2	3.7
August	6.2	-1.5	3.6	0.7	3.0
September	2.4	5.9	3.5	0.2	2.8
October	3.2	-0.5	2.0	-0.7	1.4
November	2.3	0.1	1.6	1.8	1.6
December	--	-3.2	-1.0	1.8	-0.5
1968					
January	0.4	-2.5	-0.5	5.3	0.7
February	0.9	-2.3	-0.1	5.2	1.0
March	3.8	0.8	2.9	-0.1	2.3
April	1.4	0.8	1.2	3.6	1.8
May	-1.6	1.3	-0.8	1.3	-0.3
June	-3.0	2.5	-1.3	0.5	-0.9
July p/	2.8	3.8	3.1	n.a.	n.a.

Note: Based on seasonally adjusted dollar volume which is confidential for life insurance companies. Reporting savings banks and life insurance companies account for about 70 per cent of total mortgage lending in the industry. Data for savings banks and S&Ls include a minor amount of nonresidential commitments.

The quality of outstanding mortgage debt generally improved again during the second quarter, judging from such after-the-fact measures as delinquency rates and foreclosure rates relating to loans closed mainly in earlier periods. Some improvement could have been expected in view of demand pressures for available housing, further increases in used-house prices, and the comparatively limited number of unseasoned risk-prone loans outstanding relative to the growing number of total mortgages in force. While the composite delinquency rate on home mortgages (MBA series) rose in the second quarter, the increase reflected a slight rise only in short-term delinquencies from a reduced level, as 60-day-and-over delinquencies showed further year-over-year improvement to the lowest rate in 8 years. The over-all foreclosure rate on nonfarm mortgages (FHLBB series) again declined, and reached the lowest level since 1961.

Corporate and municipal bond markets. Yields on corporate bonds on balance showed little change over the latter half of August, while municipal bond yields advanced significantly, returning to early July levels. In both markets, investor response accorded new issues notably lacked enthusiasm and the volume of unsold bonds in syndicate consequently rose. After the sharp yield decline in July, investors appeared to have second thoughts about their expectations as to the course or rapidity of monetary ease. But the recent cut in the discount rate seemed to be viewed by investors as some confirmation of their earlier expectations that monetary restraint was in the process of being relaxed. While this action did not drive yields down, it limited the extent of developing upward yield pressures.

BOND YIELDS
(Weekly averages, per cent per annum)

	Corporate Aaa		State and local Government	
	New	Seasoned		
	With call protection		S&P High Grade	Bond Buyer's (mixed qualities)
1968				
Low	6.12 (2/2)	5.97 (8/30)	4.15 (8/9)	4.07 (8/9)
High	6.83 (5/24)	6.29 (6/7)	4.68 (5/24)	4.71 (5/24)
Week ending:				
July 12	6.56*	6.27	4.44	4.36
19	6.51	6.26	4.41	4.33
26	6.40	6.22	4.27	4.16
Aug. 2	6.36	6.15	4.18	4.11
9	--	6.07	4.15	4.07
16	6.13	6.00	4.29	4.22
23	6.13	5.98	4.34	4.27
30	6.13	5.97	4.45	4.38

* Some issues included carry 10-year call protection.

The divergent path of corporate and municipal bond yields appears to be primarily a reflection of the substantially different volume of current and prospective new issues in these two markets. Public flotations of corporate bonds in August are estimated to have aggregated $675 million, about 45 per cent below July--a much larger than seasonal drop-off. This volume was below earlier expectations as several convertible bond offerings were pushed forward to the September calendar. Total corporate security offerings, including private placements and stock issues, are estimated at about $1.6 billion, which is also well below earlier months this year and the outsized August 1967 volume.

CORPORATE SECURITY OFFERINGS[1/]
(Millions of dollars)

	Bonds				Total bonds and stocks	
	Public Offerings[2/]		Private Placements			
	1967	1968	1967	1968	1967	1968
QI monthly avg.	1,088	822	604	575	1,821	1,726
QII monthly avg.	1,339	1,035	489	548	2,069	1,901
QIII monthly avg.	1,534	895e	517	633e	2,277	1,878e
July	1,889	1,260e	486	600e	2,589	2,310e
August	1,813	675e	412	600e	2,481	1,575e
September	902	750e	647	700e	1,763	1,750e

e/ Estimated.
1/ Data are gross proceeds.
2/ Includes refundings.

Moderation of corporate bond offerings is likely to continue in September, as the calendar now totals about $550 million and the ultimate volume may be no more than $750 million. While there are no sizable industrial issues currently scheduled, some such offerings may be placed on the market by corporations which deferred financing earlier in the hope of catching lower rates. But the total volume of corporate security offerings, nonetheless, will likely show at most a seasonal rise in September.

In contrast to the corporate market, the estimated volume of new municipal issues in August--at $1.7 billion--was a record for any month. This sharply enlarged volume included more than $200 million industrial aid bonds and a $286 million utility revenue issue--the largest single municipal offering in more than four years. Even though offering yields advanced throughout much of the month, a sizable volume

of these issues was not fully absorbed. As a consequence, the market is in a poor technical position with about $800 million of dealers' advertised inventories, a high for the year. Moreover, this overhang of unsold bonds is coincident with no respite from the unusually large volume of new offerings. The September volume is estimated at $1.5 billion--a record for the month--with more than $300 million industrial revunue bonds included.

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

	1967	1968
QI monthly average	1,391	1,240
QII monthly average	1,294	1,259
QIII monthly average	1,050	1,533e
July	950	1,400e
August	860	1,700e
September	1,340	1,500e

e/ Estimated.
1/ Data are for principal amounts of new issues.

Stock market. During August, common stock prices fluctuated within a narrow range somewhat below their all-time highs reached in mid-July. Trading volume remained moderate throughout the month. Apparently stemming the earlier decline and contributing to the market stability throughout August were somewhat improved investor expectations regarding monetary policy, profit prospects, and the economic outlook in general.

STOCK PRICES

	Dow-Jones Industrials	New York Stock Exchange Index	American Exchange Index
March 29	840.67	50.05	22.42
Mid-July high	923.72	57.69	30.08
Early August low	869.65	54.18	27.52
September 3	900.36	55.65	28.82

TRADING VOLUME

	New York Stock Exchange	American Exchange
March	9.2	3.6
June	15.1	7.4
July	14.3	6.6
August	10.8	4.8

Preliminary figures now available for July show that margin debt of brokers' customers dropped $240 million or 3.6 per cent to $6,450 million during the month. Over the same period the New York Stock Exchange composite price index fell 2.3 per cent. The decline in margin debt was the first since January 1968 and the largest in the two-and-one-half-year history of the series. In addition, the number of margin accounts declined by 5,000, the first decline since 1966. At banks, purpose loans to non-brokers continued to rise moderately--by $14 million--possibly because of borrowing to buy corporate or municipal bonds;[1/] indeed, during the first half of August such debt rose by an additional $50 million to $2,473 million.

1/ Since March 1968, the margin debt figure has not included debt associated with bond acquisitions; however, such debt continues to be included in bank purpose loans to others than brokers and dealers.

U. S. Government securities market. The market for Treasury securities has shown no clear trend since the last meeting of the Committee, with prices in both the bond and bill sectors fluctuating moderately in response to a number of diverse influences. The cut in the discount rate by the Minneapolis Federal Reserve Bank and the accompanying reduction in the repurchase agreement rate to 5-1/4 per cent on August 15 had a favorable, but very short-lived effect on yields. Thus, after yield declines of around 6 basis points on Treasury bills and of from 2 to 4 points on intermediate and long-term issues in trading immediately after the initial discount rate cut, market yields quickly rebounded and within a week were at or above the levels immediately preceding the discount rate action.

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

	1967	1968				
	Highs	Highs	July 15	Aug. 5	Aug. 12	Sept. 3
Bills						
1-month	4.75 (1/4)	5.70 (5/21)	5.40	4.95	5.00	5.05
3-month	5.07 (12/15)	5.92 (5/21)	5.42	4.89	5.05	5.18
6-month	5.60 (12/1)	6.08 (5/21)	5.53	5.12	5.25	5.20
1-year	5.71 (12/29)	6.03 (5/21)	5.50	5.04	5.19	5.14
Coupons						
3-years	5.87 (11/13)	6.36 (5/21)	5.64	5.41	5.47	5.33
5-years	5.91 (11/13)	6.21 (5/21)	5.68	5.48	5.52	5.46
10-years	5.87 (11/13)	6.02 (5/21)	5.56	5.37	5.42	5.42
20-years	5.81 (11/20)	5.77 (3/14)	5.33	5.16	5.22	5.22

Remarks by the President on the bombing of North Vietnam and the tensions caused by the Czech crisis had an adverse impact on the market because of their possible implications for Government spending. Moreover, there was apparently some adjustment in positions by dealers who had anticipated a larger discount rate reduction.

Most recently, prices of coupon issues have moved higher as market participants have interpreted recent System actions and reserve data as at least confirming that policy had taken an easier stance. In addition there has been a moderate net retail demand for Governments. The market also was buoyed by the anticipation that the Desk probably would buy coupon issues in preparation for the Labor Day weekend. On Thursday before the holiday the System did buy over $80 million of notes and bonds.

A hesitant tone has pervaded the market for Treasury bills in most sessions. Bill yields now stand about 10 basis points above the level reached about the time of the last Committee meeting.

The dealers' large bill positions, as well as relatively substantial coupon holdings, together with the higher cost of day-to-day financing, have in part been responsible for this back-up of rates as some dealers sought to reduce their positions from the record levels reached at midmonth. The reduction in the discount rate by 1/4 of a point, rather than the 1/2 many had expected, encouraged this movement. The occurrence of three regular auctions in the week of August 26 frustrated this action to some extent; and on September 3, dealer positions in bills stood at $3.7 billion, despite the fact that sizable sales to foreign accounts had eased some of the pressure on holdings.

DEALER BORROWINGS AND POSITIONS
(In millions of dollars)

	July 1	July 31	Aug. 15	Aug. 30	Sept. 3
Borrowings					
New York Banks	830	1,620	1,790	1,364	1,518
Other banks	646	1,216	1,558	1,470	1,429
Federal Reserve	--	237	311	--	--
Nonbank Lenders	1,571	2,220	2,363	2,441	2,426
Total	3,047	5,293	6,022	5,274	5,372
Positions					
Treasury Bills	1,580	3,920	3,479	3,293	3,720
Other within 1 year	417	763	327	426	421
1 to 5 years	139	169	313	222	215
5 to 10 years	231	183	813	822	834
Over 10 years	33	139	146	120	121
Total	2,400	5,175	5,079	4,883	5,311

As the accompanying table shows, dealer positions and borrowings rose markedly in July; borrowings continued upward in August and totaled $6 billion on August 15, the payment date for the Treasury financing. The increased demand for financing fell most heavily on banks. Of the $3 billion rise in borrowings from the beginning of July to mid-August, about two-thirds was accommodated at banks. This growing demand contributed to the relatively high dealer loan rates and large basic reserve deficits of the major banks throughout July and August.

Since August 15 dealer positions have risen by about $370 million. Daily financing needs have continued to be frequently near $1.5 million, but borrowings have been reduced $250 billion. Almost

all of the reduction has been at banks, with nonbank lenders--mainly corporations, who appear to be in relatively liquid position--now providing a somewhat higher proportion of these funds than at midmonth.

Rate movements on other short-term instruments in recent weeks have also fluctuated and, if anything, have been even less clear-cut as to a general trend than have short maturity Government yields. On balance, however, these yields--like those on Treasury bills--are generally higher than at midmonth, although in many instances the change has been negligible.

SELECTED SHORT-TERM RATES

	1966 Highs	1967 Highs	1968 Highs	1968 July 15	1968 Aug. 12	1968 Sept. 3
1-month						
CD's (prime NYC)						
Highest quoted new issue	5.50 (12/13)	5.50 (12/29)	5.50 (8/29)	5.50	5.50	5.50
Secondary market	5.75 (9/28)	5.50 (12/29)	6.20 (5/31)	5.90	5.80	5.75
3-month						
Bankers' acceptances	5.75 (10/25)	5.63 (12/29)	6.13 (5/24)	5.88	5.75	5.63
Federal agencies	5.76 (9/21)	5.30 (12/29)	6.11 (5/17)	5.65	5.45	5.59*
Finance paper	5.88 (12/31)	5.88 (1/6)	6.13 (6/25)	5.88	5.75	5.63
CD's (prime NYC)						
Highest quoted new issue	5.50 (12/31)	5.50 (12/29)	6.00 (7/18)	6.00	5.75	5.75
Secondary market	5.90 (9/21)	5.70 (12/29)	6.20 (5/31)	6.05	5.85	5.84
6-month						
Bankers' acceptances	6.00 (9/23)	5.75 (12/29)	6.25 (5/24)	6.00	5.88	5.75
Commercial paper	6.00 (12/31)	6.00 (1/6)	6.25 (7/25)	6.25	5.88	5.88
Federal agencies	6.04 (9/21)	5.55 (12/29)	6.25 (5/24)	5.80	5.49	5.59*
CD's (prime NYC)						
Highest quoted new issue	5.50 (12/31)	5.50 (12/29)	6.25 (7/11)	6.25	5.75	5.75
Secondary market	6.30 (9/28)	6.00 (12/29)	6.40 (5/31)	6.18	5.90	5.90
1-Year						
Federal agencies	6.13 (9/23)	5.95 (12/29)	6.01 (5/31)	5.88	5.55	5.65*
Prime municipals	4.25 (9/21)	4.00 (12/29)	3.90 (5/31)	3.30	2.75	2.90*

N.B. - Latest dates on which high rates occurred are indicated in parentheses.
* - August 30.

Federal finance. The Treasury's cash operating balance at the end of August totaled $4.6 billion, or $500 million less than projected in the last Greenbook, with the shortfall spread rather widely through a number of receipt and expenditure items. According to present projections, the balance will decline to a rather low level at mid-September, possibly requiring temporary overdrafts with the Federal Reserve, but thereafter as quarterly tax payments are deposited, it will rise substantially.

Looking beyond September to the fourth quarter, the Treasury will experience large, partly seasonal, cash drains, as shown in the table. Accordingly, a $3.0 billion borrowing operation is assumed for the second half of October. In view of the large Treasury cash surplus projected for next spring, and in line with previous Treasury statements, the October financing is likely to consist of tax bills.

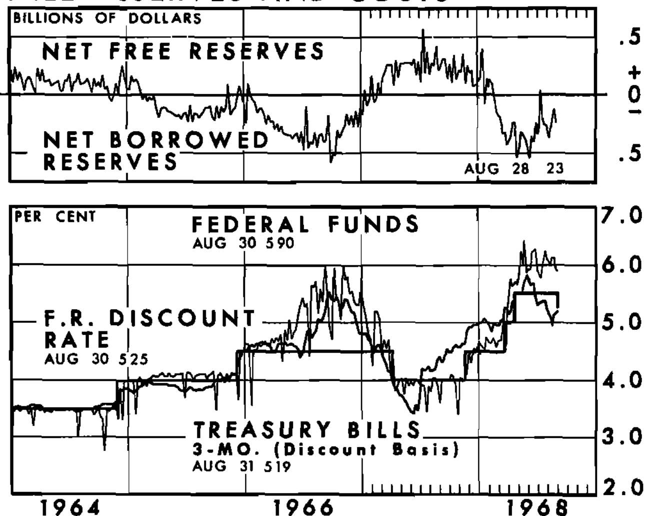
While trends in Federal spending for fiscal 1969 to date are difficult to interpret from the data now available, thus far they seem to be consistent with the assumptions underlying Greenbook projections. The Administration's problem of deciding which specific programs to cut is still complicated by the fact that Congress has not yet completed action on several major appropriation bills. Moreover, spending in two uncontrollable programs that fall within the area of the budget subject to the over-all expenditure ceiling is now expected to be about $1 billion larger than previously projected, necessitating a commensurately larger cut-back in other programs also subject to the ceiling. About $700 million of the expected overage is attributable to CCC crop purchases, and the other $300 million to Medicaid and other public assistance grants to states.

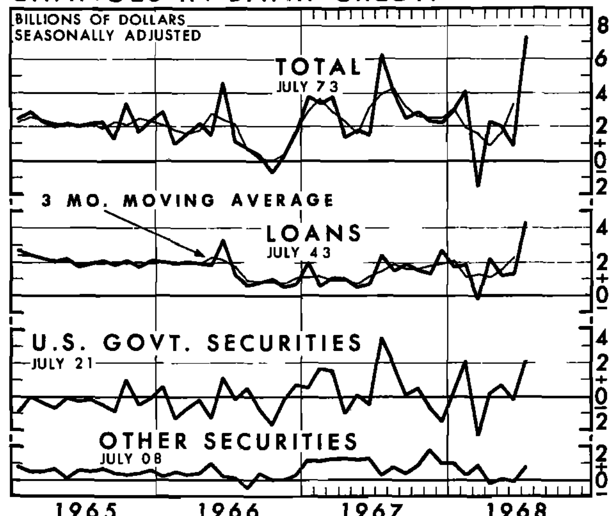
PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

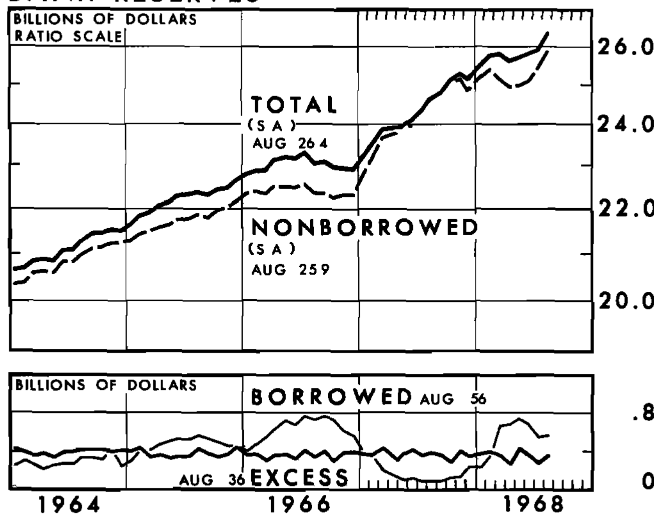
	Aug.[a]	Sept.	Oct.	Nov.-Dec.
Borrowing operations				
New cash raised				
Weekly bills	.5	.4	.2	--
Tax bills	--	--	3.0	3.0
Coupon issues	1.7	--	--	.5
PC's	.8	--	--	--
Debt repayment etc. (-)	- .1	--	- .1	- .2
Total net borrowing from public	2.9	.4	3.1	3.3
Plus: Other net fin'l. sources[b]	- .5	.9	.1	- .8
Plus: Budget surplus or deficit (-)	-3.8	1.9	-5.1	-3.5
Equals: Change in cash balance	-1.4	3.2	-1.9	-1.0
Memorandum: Level of cash balance end of period	4.6	7.8	5.9	4.9

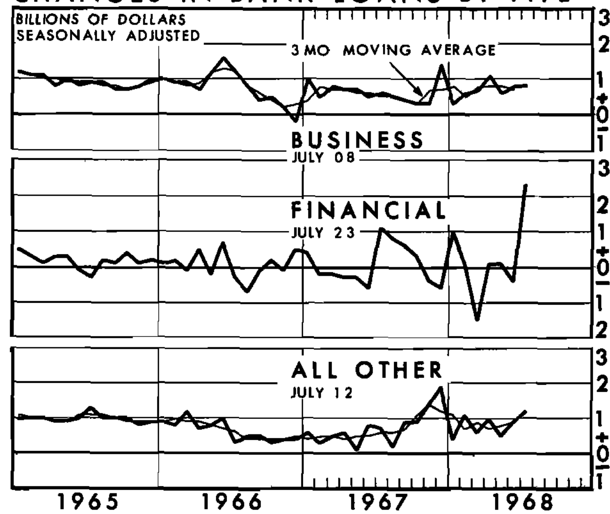
a/ Actual and estimated data.
b/ Checks issued less checks paid and other accrual items.

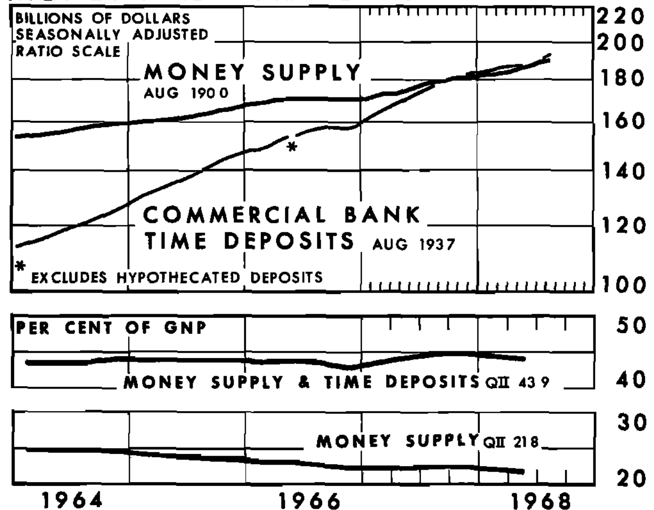
FINANCIAL DEVELOPMENTS - UNITED STATES

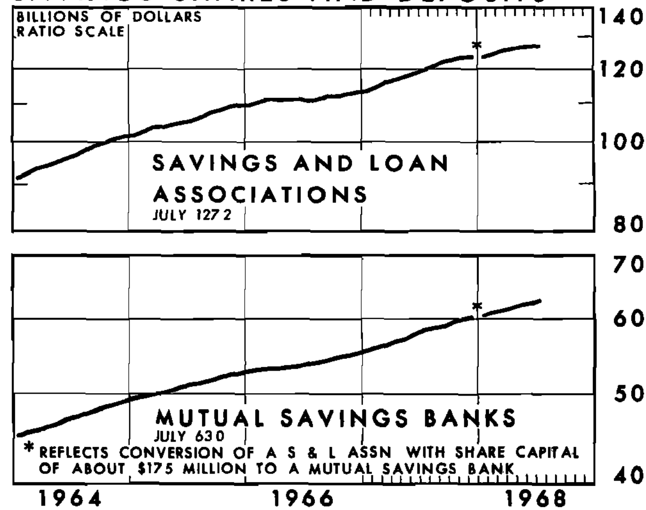




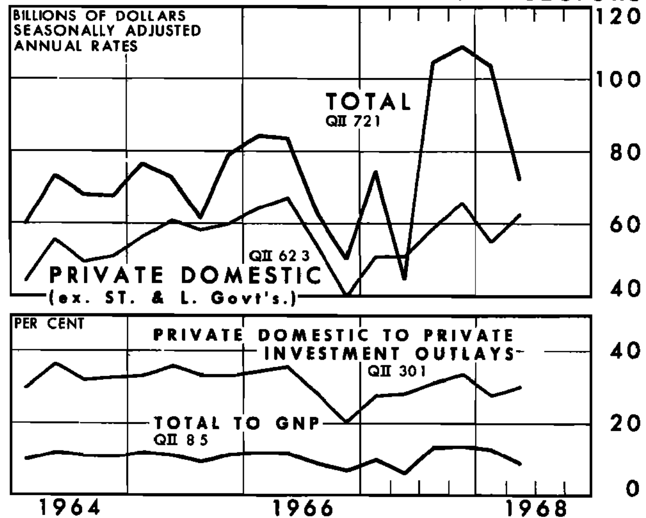


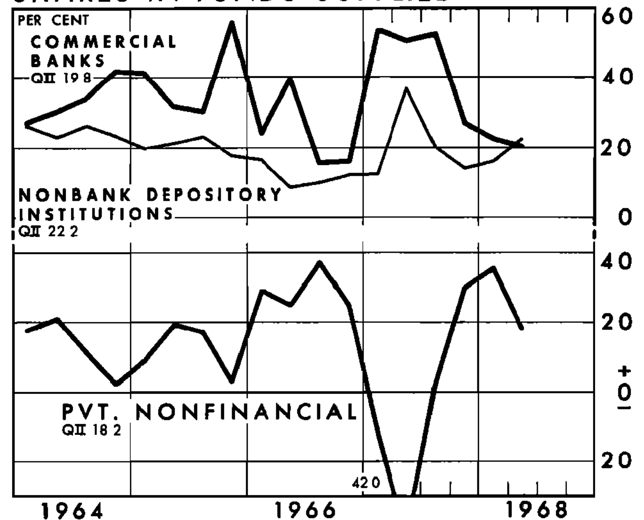


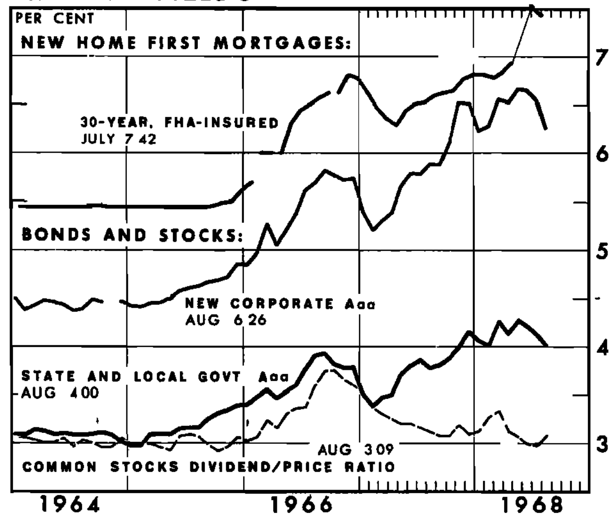


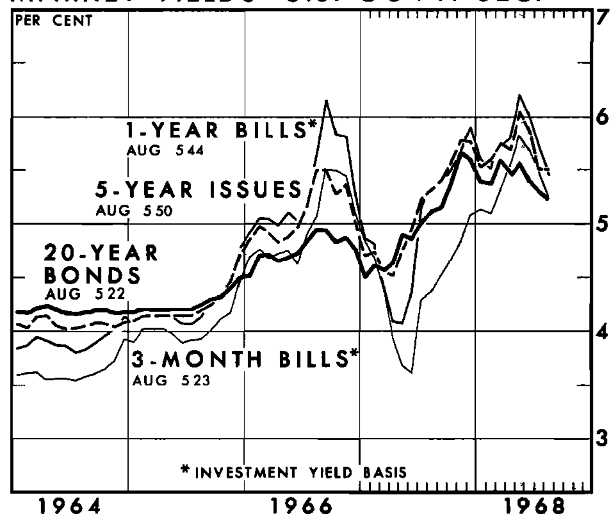


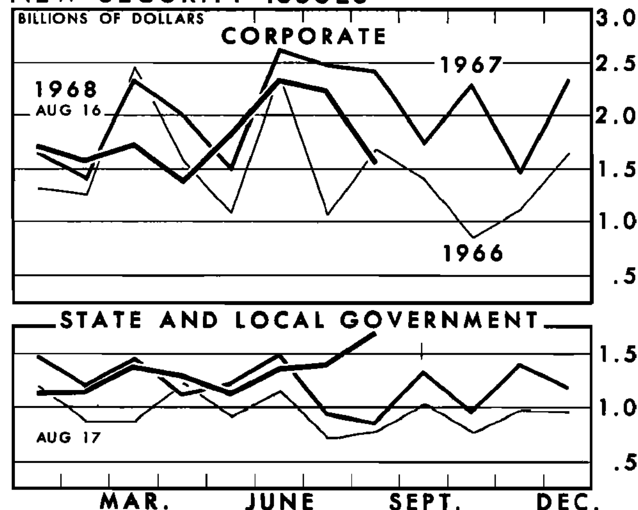
FINANCIAL DEVELOPMENTS - UNITED STATES

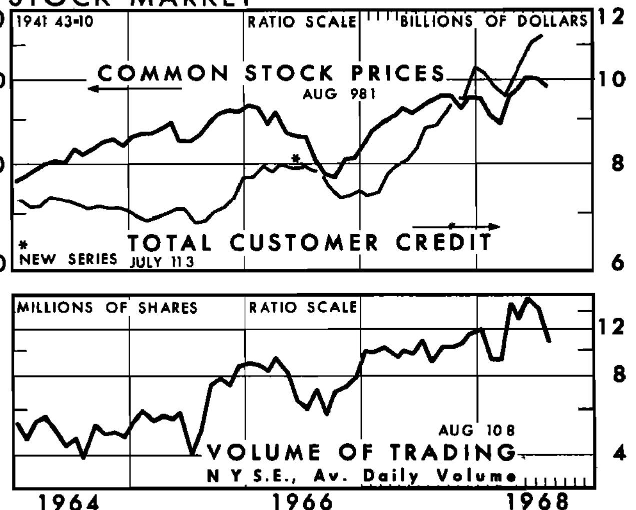












INTERNATIONAL DEVELOPMENTS

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Exchange market developments. Until the last week of August -- when rumors of a revaluation of the German mark thoroughly destabilized the exchange markets -- the pattern of developments for most foreign currencies had not been significantly different from that of July. In the first three weeks of August the French franc continued to be under selling pressure, although less severe than in July. The German mark (until August 27) continued to trade well below par as very easy money market conditions in Germany continued to encourage both short- and long-term capital outflows; the Canadian dollar remained quite firm with the Bank of Canada making sizeable purchases of dollars; the Italian lira continued to show seasonal strength; the other major currencies showed little tendency for significant pressures to develop in either direction.

The most notable exception to this approximate repetition of the July pattern of events was in the market for sterling. The pound had recovered quite well in July and the Bank of England purchased over $500 million in the market. Early in August sterling remained firm but its first setback of the month came on August 13 with the release of the British trade figures for July, which showed a deficit paralleling

those of April and May. A little more than one week later (on August 21) sterling experienced another setback as the Czech-Soviet confrontation emerged. Up to this point sterling had been quoted markedly lower than in the first two weeks of August but selling pressure was moderate and the Bank of England had provided only modest support for the rate.

The mark revaluation rumors which began on August 27 sharply accelerated pressures on both sterling and the French franc. During this final hectic week of the month the Bank of England and Bank of France each sold approximately $150 million in support of their respective currencies while the Bundesbank made spot market purchases in excess of $850 million. Furthermore, the Bundesbank intervened in the forward market, swapping $240 million (selling dollars spot against two and three-month forward repurchase); and the Federal Reserve Bank of New York sold $32 million equivalent of marks on an outright forward basis, half for System account and half for Treasury account.

The French franc began and ended the month at its floor; sterling's overall decline was from about 239.40, in the first two days of August, to its August 30 afternoon quotation of 238.38; during the last week of August the German mark moved nearly the full range between its lower and upper support levels.

The failure of the mark revaluation to materialize on the last weekend of August has not generated a major reflow of funds away from marks. The speculative atmosphere seemed to have subsided somewhat as of last Monday and Tuesday (September 2 and 3), but on Wednesday a

new wave of speculation hit the market -- possibly in response to Bundesbank President Blessing's statement late Tuesday that "some day" the mark might have to be revalued if Germany's trading partners continued to tolerate creeping inflation.

Between August 26 and September 4 the Bundesbank made gross spot market purchases of dollars totaling about $1 billion, while engaging in "swap" operations with German commercial banks totaling about $700 million. The resulting net increment to German reserves of about $300 million was roughly equal to the volume of intervention losses by other major central banks (principally the Bank of France and Bank of England).

Gold markets have been generally quiet in the past several weeks. During the month of August prices advanced from a level just under $39.00 to a level just under $40.00. Prices declined modestly early in the month but began to rise concurrent with the release of the British trade figures on August 13; they were marked up rather sharply (but temporarily) at the time of the Czech crisis, and advanced further during the week of German mark speculation.

Euro-dollar market. U.S. banks drew rather heavily on the Euro-dollar market for funds during the month of August. Between July 31 and August 28 liabilities to foreign branches increased $875 million to a new peak of $7,085 million. U.S. banks had reduced their use of Euro-dollar funds during the last three weeks of July by about $750 million; thus, the $7,085 million peak level of

outstanding liabilities on August 28 was only about $120 million more than the previous peak level of July 10.

The decrease in U.S. bank liabilities to overseas branches after July 10 is not readily explainable, especially in view of the fact that the cost of Euro-dollar funds to the banks was, generally speaking, lower than the cost of funds acquired in domestic financial markets during this period. Dollar advances to banks' head offices had, however, risen very sharply during the second quarter, and growing evidence of easier monetary conditions in the United States coupled with the fact that some banks may have felt overly dependent on Euro-dollar funds may have caused U.S. banks to reduce their liabilities to overseas branches. The volume of outstanding C/D's of New York banks increased by about $350 million between July 10 and July 31, coinciding with the reduction in Euro-dollar liabilities through overseas branches and indicating that U.S. banks again were able to compete more successfully for funds in domestic markets.

Even though supply conditions in the Euro-dollar market were less favorable than in June and early July, when there were massive flows of speculative funds from the French franc and sterling, Euro-dollar rates fell considerably in the last three weeks of July, probably reflecting the reduced demand for funds from U.S. banks. The rate for three-month funds fell from 6.69 per cent per annum on July 10 to 6.25 per cent by the end of July.

During August Euro-dollar rates have held relatively steady; the three-month deposit rate has ranged between 5.94 and 6.12 per cent per annum even in face of the relatively heavy demand for funds from U.S. banks. The supply of funds apparently came mainly from holders of sterling, French franc and (until the final week of August) German mark assets. There are two possible factors behind the recent increase in demand for Euro-dollar funds from U.S. banks. First, the cost of Euro-dollar funds -- particularly 3-month deposits -- has been lower than the cost of domestic U.S. funds. Second, it may be that U.S. banks, anticipating a further decline in domestic U.S. interest rates and hence being hesitant to issue long-term domestic C/D's, are acquiring very short-term deposits in the Euro-dollar market in lieu of longer-term domestic funds.

U.S. balance of payments. The third quarter opened with an unusually low liquidity deficit in July -- about $100 million before special transactions or seasonal adjustment. This relatively favorable outcome resulted in part from a net reduction of over $180 million in claims on foreigners reported by banks, and continued heavy purchases of U.S. corporate stocks by foreigners. According to the weekly figures for August, however, the liquidity balance has once more swung into heavy deficit. In the four weeks ended August 28 it amounted to $561 million, and about $775 million before special transactions. The special transactions in August included the latest $125 million installment under the German military offset agreement, and a conversion

of $100 million of official Argentine balances from liquid to non-liquid form. August, and the third quarter as a whole, are seasonally adverse because of tourism and other factors, but the average August deficit before special transactions has been about $400 million in the past few years. These early and partial figures for August suggest that the improvement in the overall balance registered in the May-July period has suffered at least a temporary setback.

The balance on the official settlements basis showed a deficit of $73 million in July but turned to a surplus of about $140 million in August through the 28th. The striking difference in the behavior of the two measures of the balance between July and August reflected primarily the fact that in July non-official foreign liquid dollar holdings rose by only about $50 million, whereas in the four weeks of August such accounts increased by some $900 million. Most of the activity in these accounts is reflected in liabilities to foreign branches of U.S. banks, which are discussed above.

Direct foreign investments. Much of the hope for improvement in the balance of payments this year was based on the new mandatory controls, which were to reduce direct investment (including reinvested earnings) by $1 billion from the 1967 amount. Many changes have already been made in the regulations governing the program, and some unexpected developments have occurred, including (a) a very large demand for special authorizations covering prior commitments or abnormal circumstances in the base period, and (b) a massive and successful effort by direct

investors to tap European capital markets. As far as can be judged by the not altogether satisfactory information gathered from OFDI (Office of Foreign Direct Investments) operations and projections at this time, a saving of $1 billion compared to 1967 is still possible, but it will depend in large part on companies that do not use their basic quotas in 1968 but carry them into 1969. This will occur either because investors -- especially those with large bases in less developed countries -- will not wish to invest as much as they could this year, or because of the requirement now in the regulations that companies with funds available out of foreign borrowings must use those funds prior to using their generally allowable investment quotas in the various scheduled areas. But if there is a large carry forward, it will, of course, complicate the operation of any 1969 program.

It is difficult to judge from the direct investment capital outflow figures given in the balance of payments accounts how much effect the restraint program had in the first half of the year, and whether a different result can be expected in the second.

DIRECT INVESTMENT CAPITAL FLOW
(in millions of dollars; outflow (-))

	1967					1968	
	Total	I	II	III	IV	I	II
All countries	-3,020	-899	-423	-719	-980	-589	-836
Canada	-392	-64	-52	-123	-153	26	-239
United Kingdom	-342	-41	-116	-74	-112	-9	-28
Other Europe	-1,100	-270	-244	-257	-330	-210	-219
Japan	-33	-29	-3	-7	7	-4	-7
Australia, New Zealand, and South Africa	-357	-70	-66	-164	-57	-27	-87
Other countries	-796	-425	+58	-94	-335	-365	-256

Note: not seasonally adjusted.

As indicated in the table, direct investment outflows rose in the second quarter (and show a considerably larger increase on a seasonally adjusted basis), though most of the upturn was in flows to Canada, which are exempt from the restrictions. However, these figures include amounts derived from foreign borrowing, which should be subtracted to arrive at the outflow of U.S. funds subject to the OFDI restrictions. For all of 1967 the Office of Business Economics tables show $278 million of foreign financing entering these outflows, reducing the net flow to about $2-3/4 billion. In the first half of 1968 the OBE tally shows that only about $150 million of foreign funds was included in the total. These figures on the use of foreign funds are probably low, since they exclude certain types of borrowing, but they are consistent for the two periods. On this basis, the net outflow of U.S. funds for direct investment in the first half of 1968 (excluding Canada but including some other outflows not covered by the OFDI program) was about the same as in the first half of 1967.

Data from OFDI reports for the second quarter will not be tabulated for several weeks, and important differences will perhaps appear because the regulations do not extend to all the outflows included in the balance of payments accounts. At the moment, however, the OBE estimates indicate that the drawdowns against proceeds of foreign financing will have to accelerate in the second half if investors are to stay within the program allowables. This would imply somewhat less pressure on the balance of payments in the

second half, since the balance of payments gain does not show up when these funds are borrowed and held abroad in liquid form, but occurs instead when these funds are drawn down and substituted for outflows of U.S. funds.

Income received from direct foreign investments was at an annual rate of $4.6 billion in the first half of the year, slightly above the $4.5 rate for all of last year. However, such returns had reached a $5 billion rate in the last half of 1967. The effect of OFDI limits on reinvested earnings in Schedule C (developed) countries, plus some improvement in earnings experience abroad, should be to raise income receipts in the second half to at least the level achieved at the end of last year.

The latest projections of expenditures for plant and equipment by foreign affiliates of U.S. firms indicate continued cooling off from the 20 per cent increases of 1964 and 1965 and the 16 per cent increase of 1966. In 1967 such expenditures increased by a relatively moderate 7 per cent, and for 1968 the increase is expected to drop to 5 per cent. For 1969 these early indicators suggest no more than another modest rise in capital expenditures abroad. The results of the new survey are summarized in the accompanying table. Year-to-year changes are measured by the OBE by comparing estimates made at the same period of each year. However, the control programs may be affecting the timing of company planning, and if the comparison is made based on the last two columns of the table -- which give the projections for both 1968

and 1969 as made by the companies in June this year -- some decline is suggested. In any case, expenditures in 1968 and in 1969 will be maintained at far higher levels than a few years ago, but will be financed to a much lesser extent by outflows from the United States.

PLANT AND EQUIPMENT EXPENDITURES BY
FOREIGN AFFILIATES OF U.S. COMPANIES
(millions of dollars)

	1965	1966	1967		1968		1969
	Final	Final	June[1/]	Final	June[2/]	June[1/]	June[2/]
Total	7,440	8,640	10,045	9,245	9,785	10,520	10,168
By industry							
Mining	629	789	931	902	761	1,101	969
Petroleum	2,277	2,526	3,295	3,018	3,432	3,595	3,385
Manufacturing	3,884	4,583	5,035	4,513	4,853	4,963	4,894
Other industries	650	741	783	812	739	861	921
By area							
Canada	1,847	2,357	2,360	2,208	2,053	2,244	2,206
Latin America	1,073	1,092	1,441	1,258	1,601	1,715	1,791
Europe	2,639	3,253	3,970	3,637	3,814	3,803	3,858
Other areas	1,880	1,938	2,274	2,142	2,317	2,759	2,313

1/ Estimated in June of current year.
2/ Estimated in June of previous year.

Other capital accounts. As mentioned earlier, bank-reported claims on foreigners were reduced by about $180 million in July, of which about $130 million was in banking claims covered by the restraint program. The inflow came mainly from Europe ($140 million) and Japan ($68 million), and was partly offset by outflows to Canada. In the seven months through July the net capital inflow from bank-reported claims totalled $800 million, accounted for mainly by a reduction of nearly $400 million in Europe and $200 million in Japan.

An additional effect of the controls on direct investments has been to force some liquidation of liquid balances abroad, apart from those consisting of the temporarily invested proceeds of foreign borrowing. The exact amount involved is uncertain because of the intermingling of these two kinds of liquid foreign assets, but as a rough order of magnitude the liquidation in the first half might have amounted to $200 million. By June 30 the reduction of balances required by OFDI regulations should have been accomplished.

Purchases of U.S. securities by foreigners continued on a substantial scale in July. Foreigners bought, net, about $160 million of U.S. corporate stocks, in line with the monthly average of the first half of the year, and also purchased approximately $150 million of convertible bonds issued by Delaware affiliates for use in financing direct foreign investments.

U.S. foreign trade. In July the merchandise trade balance (balance of payments basis) returned to an export surplus, following two successive monthly deficits, as exports increased slightly and imports fell sharply. But for the three months of May-July combined, the trade balance was in deficit by about $400 million, at an annual rate, compared with a surplus at a rate of nearly $900 million in January-April.

Comparing the first four months of the year to the May-July period, exports rose at an annual rate of about 7 per cent; average shipments in the latter period exceeded those in the early months by

a little less than 2 per cent. A gain of over 4 per cent in non-agricultural exports was largely offset by a steep decline in shipments of agricultural products, mainly P.L. 480 deliveries of wheat to India and Pakistan. The general abundance of crops in both foreign exporting and importing countries makes it uncertain whether exports of agricultural commodities in fiscal 1969 will be as large as they were in the last fiscal year.

The gains in shipments of nonagricultural products in May-July appear to be somewhat more widespread than they were earlier in the year. Exports of aircraft remained high, and sales of cars to Canada expanded further, while shipments of refined copper continued to rise following the resumption of operations by domestic copper refineries after the copper strike ended in March. In addition, exports of machinery, chemicals and logs and lumber also advanced in the more recent period.

By area, the greatest gain in exports in May-July over those in January-April was in shipments to the EEC countries. These increased by nearly 13 per cent over the rate in the first four months of the year, with much of the advance in commodities other than copper and aircraft. Exports to the U.K. and Latin America also expanded sharply. The more moderate rise in shipments to Japan consisted largely of greater deliveries of commercial aircraft. Despite the advance in deliveries of cars to Canada, total exports to that country fell substantially during May-July.

Imports in July declined by over 6 per cent from the record rate of the preceding month. The drop, however, was concentrated in a few commodities -- nonferrous metals, mainly copper, and cars from Canada, and does not appear to signal any general weakening in imports from the very high rates of the first six months of the year.

The decline in arrivals of cars from Canada was exceptionally large, apparently greater than seasonal. It is not expected that this low rate will be sustained. Continued growth in such imports seems probable after the changeover to the 1969 models is completed. Imports of cars from Europe and Japan continued to gain in July as the inventory buildup in these cars accelerated.

Copper imports in July were only about two-thirds of the pre-strike rate, as both refined and unrefined types fell sharply. Arrivals of refined copper in July were at the prestrike level, but imports of unrefined copper were considerably below a "normal" rate. Exceptionally heavy withdrawals of copper from customs warehouses in June to avoid payment of import duties which were reimposed on July 1, following their suspension since early 1966, may have temporarily reduced new import requirements. After working off of these inventories there may be an upturn in copper imports later in the year, unless of course, domestic demand declines. For the next month or two, however, production difficulties in Chile resulting from a drought and the consequent reduction in waterpower may limit imports from that country.

The Treasury Department has announced the imposition of countervailing duties on all shipments of dutiable imports from France, beginning September 14. The action is a result of an investigation conducted after issuance by the French Government of a decree providing for certain subsidy payments on French exports. The amount of the countervailing duty will be equal to 2.5 per cent of the f.o.b. price of the imported merchandise from September 15 through the end of October, and half that rate from November until January 31 when the French subsidies are scheduled to be removed. Since the countervailing duties at the full rate of 2.5 per cent are to be imposed only for slightly more than one month, little permanent effect on our imports from France is expected, although there may be some postponements.

<u>Financial markets in major industrial countries</u>. In general, financial markets have eased somewhat in most industrial countries during recent weeks, although, except in Canada and in the Euro-dollar market, the softening in interest rates from peaks reached earlier this year has not gone as far as it has in the United States. In most countries, interest rates are currently below their recent highs, with declines in long-term yields noticeably less pronounced than in those on short-term instruments. It is not yet clear to what extent, if any, this trend toward ease will be impeded by the current speculative movement into German marks.

The sharpest declines in interest rates have occurred in the Euro-dollar and Canadian markets, with the 3-month Euro-dollar rate dropping from 7-1/8 in late May to 6-1/8 per cent by the end of August; the Canadian 91-day Treasury bill rate fell by 1.45 percentage points during the same period. Because of the close link between these markets and the U.S. financial market, such changes can be attributed in large part to the significant drop in U.S. rates during roughly the same period. Relaxation of pressures in other foreign financial markets also can apparently be characterized in part as a reaction to changed financial conditions in the United States, and in some cases to a desire to back away from abnormally high rates established earlier. Improved balances of payments in a number of countries have contributed directly to the easing of monetary conditions by adding to bank reserves, and in Canada and Japan discrete policy actions have signaled the trend towards ease.

SHORT-TERM INTEREST RATES
(per cent per annum)

	1967		1968		Recent Rates					
	Low	High	Low	High	6/21	7/12	8/2	8/16	8/23	8/30
Euro-dollar										
Call	4.00 (9/1)	6.75 (12/22)	4.50 (1/26)	6.62 (6/28)	6.50	5.75	5.75	5.75	5.88	6.00
3-month	4.62 (4/28)	6.75 (11/24)	5.44 (2/16)	7.19 (5/31)	6.88	6.31	6.06	6.00	6.00	6.13
United Kingdom:										
Treasury bill	5.16 (5/19)	7.44 (11/24)	6.81 (8/23)	7.47 (2/2)	7.09	7.09	6.97	6.84	6.88	6.87
Local authority	5.50 (9/19)	7.75 (12/26)	7.50 (8/23)	8.50 (6/14)	8.38	8.19	7.88	7.88	7.50	7.50
Germany:										
Call money	0.75 (7/20)	5.88 (1/2)	1.50 (1/19)	3.56 (8/26)	2.44	1.88	2.63	3.25	3.56	2.50
3-month inter-bank	3.23 (7/23)	5.95 (1/6)	3.22 (1/23)	3.75 (6/30)	3.63	3.50	3.50	3.50	3.63	3.62
Switzerland:										
3-month bank deposit	2.75 (9/15)	4.50 (4/7)	2.75 (5/7)	3.75 (8/16)	3.75	3.75	3.75	3.75	n.a.	n.a.
France:										
Call money 1/	3.75 (9/8)	5.88 (1/4)	4.75 (2/21)	6.00 (8/29)	5.75	6.00	6.00	5.88	5.88	6.00
12-month Treasury bill 2/	4.61 (6/15)	5.19 (3/6)	5.02 (2/26)	6.02 (7/16)	5.75	6.02	6.02	5.96	5.92	6.09
Belgium:										
3-month Treasury bill	4.40 (12/31)	5.85 (Jan.)	3.75 (8/30)	4.40 (1/29)	3.75	3.75	3.75	3.75	3.75	3.75
Netherlands:										
3-month local authority	5.38 (4/17)	6.63 (1/3)	4.75 (2/8)	5.88 (6/21)	5.88	5.75	5.13	5.13	5.13	n.a.
Canada:										
91-day Treasury bill	3.86 (4/21)	5.84 (12/22)	5.57 (8/23)	6.79 (5/3)	6.46	6.17	5.82	5.67	5.57	5.31
Japan:										
Call, over-month end	6.57 (May)	8.03 (Dec.)	8.40 (Feb.)	9.13 (July)	9.13	9.13	9.13	8.76	8.76	n.a.

1/ Wednesday or Thursday rates.
2/ Recent auction dates are for June 25, July 16, July 31, August 12 and August 21. Rates for July 31 and August 21 auctions are for 10-month bills; rate of 8/30 is for 3-mo. bills. 12-mo. bills auctioned on 8/26 went at 5.89%.
Note: If high or low rate prevailed on more than one date in period, only latest date is shown.

LONG-TERM INTEREST RATES
(per cent per annum)

	1967		1968		Recent Rates					
	Low	High	Low	High	6/21	7/12	8/2	8/16	8/23	8/30
Euro-bonds:										
Foreign governments	6.12 (4/21)	7.44 (12/22)	7.38 (7/30)	7.81 (7/5)	7.79	7.76	7.62	7.60	7.60	7.60
United Kingdom:										
3-1/2% War Loan 1/	6.41 (4/21)	7.20 (12/15)	7.12 (1/12)	7.77 (7/5)	7.53	7.53	7.52	7.55	7.57	7.55
Germany:										
6% public authority	6.62 (12/29)	7.55 (1/2)	6.24 (8/30)	6.88 (3/21)	6.34	6.34	6.31	6.25	6.25	6.24
France:										
Public sector 2/	6.30 (8/11)	6.48 (12/29)	6.45 (5/10)	6.99 (6/21)	6.99	6.78	6.71	6.64	6.67	n.a.
Italy:										
Composite 3/	6.35 (Feb.)	6.51 (Dec.)	6.48 (Feb.)	6.55 (June)	6.55	n.a.	n.a.	n.a.	n.a.	n.a.
Belgium:										
Government 4/	6.54 (Dec.)	6.77 (July)	6.44 (June)	6.60 (Feb.)	6.44	6.52	6.45	6.45	6.45	6.45
Netherlands:										
Government	5.46 (5/5)	6.09 (12/29)	6.21 (1/5)	6.65 (7/12)	6.55	6.65	6.56	6.54	6.53	n.a.
Canada:										
Government--										
4-1/2% 1972 5/	4.98 (3/29)	6.75 (12/27)	6.34 (8/8)	7.28 (5/22)	6.61	6.77	6.46	6.38	6.38	6.24
4-1/2% 1983 5/	5.44 (3/17)	6.69 (10/18)	6.45 (8/7)	7.08 (5/22)	6.67	6.65	6.48	6.48	6.51	6.45
Japan:										
Banks loans & discounts 3/	7.28 (Aug.)	7.37 (Jan.)	7.39 (Jan.)	7.52 (June)	7.52 6/	n.a.	n.a.	n.a.	n.a.	n.a.
Bank Debentures 3/	7.30 (Jan.)	8.17 (Dec.)	8.51 (Jan.)	8.84 (June)	8.84 6/	n.a.	n.a.	n.a.	n.a.	n.a.
Telegraph & Telephone Bonds 3/	7.56 (Jan.)	8.58 (Dec.)	8.57 (Feb.)	8.83 (June)	8.83 6/	n.a.	n.a.	n.a.	n.a.	n.a.

1/ Thursday rates. 2/ Net of withholding tax, weekly average. 3/ Monthly averages. 4/ Beginning of month. 5/ Wednesday rates. 6/ June.

Note: If high or low rate prevailed on more than one date in period, only latest date is shown.

In the United Kingdom short-term rates have declined significantly while long-term rates, although slightly below their mid-July highs, remain above the end-of-May levels. The sharp decline in Euro-dollar rates from their peaks at the end of May has been a major factor permitting the decrease of U.K. short-term yields. The markedly lower discount on forward sterling probably both reflected and aided the strengthening trend in British financial markets. The expectation throughout July that the discount rate would be reduced also contributed to the decline in the Treasury bill rate. It was widely assumed that the authorities would react to the strengthening of sterling in early July by lowering Bank Rate, and the market had discounted the anticipated reduction. However, the setback dealt to sterling by the poor July trade figures and the impact of the East European crisis make a cut in Bank Rate in the coming weeks unlikely.

British long-term interest rates rose very sharply from May until early July in connection with increased concern over the future of the $2.40 parity. In the early part of July, however, bond prices advanced markedly, primarily in response to (a) assurances that international assistance would be provided to deal with withdrawals of officially held sterling balances and (b) the announcement that Britain's trade deficit had substantially narrowed in June. Bond prices weakened again in Mid-August on news that the July trade

deficit had again widened. The Czech crisis the following week reduced bond prices further. Gilt-edged yields, although above end-of-May levels, currently remain below their early July highs.

When the pound was devalued in November, the Bank of England instructed the banks to limit the total volume of lending to the private sector to levels then outstanding. Loans to finance exports were exempted, however, and, as a result, total lending continued to rise. By late May private sector loans were 4 per cent above the November level, indicating that "export" credits extended by the banks during this period were exceedingly large. The Bank of England was therefore prompted, on May 24, to impose a new ceiling directing that lending to private borrowers not exceed the May level. Loans for exports were included under the May ceiling, indicating that the Bank was tightening monetary policy further.

Through August, private borrowing at banks stayed within the prescribed limits, but there are indications that the demand for bank credit is strengthening. Since the Bank has made clear that breaches of the ceiling will not be allowed, lower interest rates would be inopportune--an additional reason not to expect a Bank Rate reduction in the near future.

Financial markets in Germany have remained liquid, although interest rates have moved downward only slightly further. An indication of financial strength is the fact that the bond market has been absorbing a growing volume of net new issues while bond yields have

continued to decline, albeit only slightly. In July and August nearly $485 million (equivalent) in DM issues were placed in Germany by foreign borrowers, $200 million of which was placed by the IBRD. The total was significantly larger than the $134 million sold in the first six months of the year. The share of foreign issues offered in Germany taken by German investors has also risen sharply this year--from 38 per cent in the first half of 1967 to 83 per cent.

During the remainder of the year, domestic recourse to the capital markets is expected to fall off from the advanced levels of the first eight months. The central government is not expected to float any more issues this year, and there are at present only two local government offerings on the calendar. Public sector capital expenditures, however, are expected to continue to rise during the last half of the year, although at a slower rate than earlier.

By mid-August interest rates in France had declined from their post-crisis peaks but remained above mid-May levels. The French authorities reacted to the crisis by increasing the cost of credit. At the same time they permitted an extremely rapid rise in the volume of bank credit outstanding to accommodate the financial requirements of those many firms, particularly smaller ones, left on the verge of bankruptcy by strike losses and greatly increased wage bills. "Medium and small firms" were cushioned from the cost effects of higher interest

rates, and their access to bank credit was facilitated by the creation of special borrowing facilities. Such enterprises, constituting 90 per cent of all French firms, may borrow from commerical banks their increased working capital requirements made necessary by the unrest for a period of up to 18 months at a fixed rate of 5 per cent. Loans made under this regulation are rediscountable at the Bank of France outside the discount ceilings and at 3-1/2 per cent, i.e., at the discount rate prevailing before the July 2 increase. Also, in July the medium-term paper reserve requirements for commercial banks were reduced from 16 per cent of deposit liabilities to 14 per cent. It is estimated that this had the effect of reducing total reserve requirements (cash plus medium-term paper) from about 20 per cent to about 18. Basic rediscount ceilings for individual banks were also increased by 20 per cent for a four-month period.

As a result of the above measures, Bank of France credit increased from Fr. 23,763 million on May 8 to Fr. 34,980 million on August 14, an increase of over 47 per cent. During the same period in 1967, central bank credit increased by only 7 per cent.

The much higher budget deficit resulting from the Spring unrest implies increased Treasury recourse to the money market. During the period from mid-May to August 8, the Treasury auctioned Fr. 3.7 billion of 12- and 10-month bills, compared with Fr. 2.0 billion a year earlier, an increase of 85 per cent. The cost of Treasury borrowing was up, though not as much as the discount rate; before the crisis,

the yield on such bills averaged about 5.3 per cent, about 60 basis points below recent rates. The French Treasury debt is becoming more concentrated in short-term maturities and the Treasury will likely continue to be an active participant in the short-term market. In the long-term sector of the market, however, new bond issue activity by the private sector has been at a virtual standstill.

In the Netherlands short-term rates increased from mid-May to the end of July by over 1 percentage point. During August, rates declined somewhat and are currently approaching end-May levels. Short-term rates in Belgium have remained steady throughout the period. The short-term rate in Switzerland increased by 50 basis points between the end of April and early June and has not since declined. In May and June bond yields in Italy continued their upward movement, while longer-term rates in Belgium and the Netherlands fluctuated within a relatively narrow range during the May-August period.

Effective August 29, the Danish discount rate was reduced from 6-1/2 to 6 per cent--the third reduction this year--in recognition of continued tendencies toward better overall balance in the Danish economy.

Monetary conditions in Canada have eased significantly during recent weeks. The Bank of Canada reduced the bank rate in two 1/2 percentage point steps during July, and effective September 3, the discount rate has been reduced another 1/2 percentage point to 6 per cent. The Canadian Treasury bill yield is currently almost 1-1/2

percentage points below the May peak, and long-term government bond yields have declined by about 65 basis points over the same period. Short-term rates are now at the levels which prevailed before Canada's foreign exchange crisis began in January.

The shift from the extreme tightness of early 1968, when interest rates reached record highs, has a number of explanations. The principal factor was the end of Canada's foreign exchange crisis and speculative capital outflows, and their replacement by an already large and potentially sizable inflow of reserves. Since Canada had a very strong trade account and also undertook heavy flotations of bonds abroad during the first half of 1968, the reversal of speculative capital outflows has caused a rapid increase in official foreign exchange reserves. The reserves are approaching the $2.544 billion limit which was agreed upon with the United States in exchange for the exemption of Canada from the IET on new issues, and the Bank of Canada is easing monetary policy partly, at least, in order to discourage a continuation of this potentially embarrassing capital inflow.

The second major factor contributing to the Bank of Canada's decision to ease credit conditions is provided by a combination of soft domestic demand pressures and the March imposition of an income tax surcharge. Since demand pressures had partially subsided by the time the tax increase was passed, monetary policy was eased to maintain domestic aggregate demand at desirable levels.

The decline in United States interest rates in recent months provides a third cause for the downward trend in Canadian yields. The

extensive integration of the financial markets of the two countries means that Canadian interest rates have an inherent tendency to follow the trend in United States yields, even in circumstances--unlike the present--when Canadian economic objectives would seem to call for an opposite trend.

Japan formally relaxed its tight money policy on August 7, when the Bank of Japan reduced its basic discount rate from 6.21 per cent to 5.84 per cent. This move restored the rate to the level prevailing prior to January 6, 1968. Other interest rates were also reduced in August. The over-month-end call loan rate was cut on August 7 to 8.76 per cent from 9.13 per cent. On August 9 the Bankers' Association reduced by 0.365 percentage points the maximum interest rate on new loans.

The average interest rate on bank loans and discounts had already leveled off in the second quarter at 7.52 per cent, having risen from a low of 7.28 per cent reached last August. It is likely that this rate will ease now, in line with the trend for other money rates.

Selected long-term rates generally rose during the first half of this year; unfortunately, more recent data are not available. The yield on bank debentures increased from 8.51 per cent in January to 8.84 per cent in June, and the yield on Japan's telegraph and telephone bonds also rose from 8.70 to 8.83 per cent over the same period.

Although some interest rates are declining, credit conditions are likely to remain somewhat tight through September. The Bank of Japan's current quarterly ceiling on the expansion of commerical bank credit, which is relatively stringent, will remain in force through September.

APPENDIX A: BANK LENDING PRACTICES SURVEY *

Four-fifths of the 125 banks reporting in the August 15 Bank Lending Practices Survey indicated that demand for business loans was essentially unchanged or moderately weaker during the preceding three months (Table 1). This is in marked contrast to the previous survey, in which 70 per cent of the banks expected that loan demand would be stronger in this period. About 80 per cent of the respondent banks now anticipate unchanged or moderately weaker loan demand over the next three months ending in November. However, with loan/deposit ratios still very high, most banks reported that lending policies in August remained unchanged from those in May.

Interest rates and compensating balance requirements.

Nearly 85 per cent of the banks indicated essentially unchanged interest rate policy on loans to business borrowers and 96 per cent reported unchanged interest rate policy in dealing with independent finance companies. Policies regarding compensating balances--which influence the effective interest rate borrowers must pay--were also unchanged at nearly all the banks on loans to both business borrowers and independent finance companies, although, as with interest rate policy, this percentage was somewhat higher with respect to finance companies.

Other nonprice terms and conditions.

Nonprice terms and conditions on loans to businesses also were unchanged at most of the reporting banks. However, a small percentage of the banks reported moderate easing of policies on loans to new and established customers, and to local service area customers.

Other types of loans.

For the most part, the willingness of banks to make other types of loans was also unchanged since the preceding survey. Although about one-fifth of the reporting banks were more willing to make single-family mortgage loans, a somewhat smaller number reported that they were less willing to make other types of mortgage loans. As in the last survey, however, an appreciable number of banks reported that they had become more willing to make consumer instalment loans.

Size of bank differences.

Demand for business loans as compared to three months ago, and that anticipated in the next three months is reported to be somewhat stronger at larger rather than smaller banks (Table 2). Generally, however, no significant differences exist with respect to bank size as to policy responses on interest rate, compensating balance, or nonprice terms and conditions. Smaller banks indicated a firmer policy with respect to establishing new or larger credit lines to independent finance companies than did larger banks. Large banks seemed less willing to make mortgage loans, broker loans, and participation loans with correspondent banks.

* - Prepared by Don Matthews, Research Assistant, Banking Section, Division of Research and Statistics.

Factors associated with policy changes.

While many banks commented that there had been no significant changes in the last ninety days, several stated that since July 31 they had begun to climb out of the tight money situation as a result of improved deposit inflows. One bank in qualifying its essentially unchanged policy indicated that it felt that conditions for the past year relating to deposit levels, loan demand, interest rates, etc. had been characterized by considerable uncertainty.

Some indicated that with improved deposit inflows and with demand for loans expected to be moderately weaker during the next three months, they are presently considering a move to more active loan policy. A Philadelphia bank said, "We are aggressively seeking any type of sound and profitable loan." However, many banks point to continued high loan/deposit ratios as the reason for their unchanged restrictive loan policies.

Several banks in New York indicated less willingness to make loans to brokers. One bank stated that it had all loans to brokers under surveillance due to the difficulties that these institutions were experiencing--paper jam, financial problems, etc.

QUARTERLY SURVEY OF CHANGES IN BANK LENDING PRACTICES
AT SELECTED LARGE BANKS IN THE U.S. 1/
(STATUS OF POLICY ON AUGUST 15, 1968 COMPARED TO THREE MONTHS EARLIER)
(NUMBER OF BANKS & PERCENT OF TOTAL BANKS REPORTING)

	TOTAL		MUCH STRONGER		MODERATELY STRONGER		ESSENTIALLY UNCHANGED		MODERATELY WEAKER		MUCH WEAKER	
	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT
STRENGTH OF DEMAND FOR COMMERCIAL AND INDUSTRIAL LOANS (AFTER ALLOWANCE FOR BANK'S USUAL SEASONAL VARIATION)												
COMPARED TO THREE MONTHS AGO	125	100.0	2	1.6	23	18.4	72	57.6	27	21.6	1	0.8
ANTICIPATED DEMAND IN NEXT 3 MONTHS	124	100.0	0	0.0	26	21.0	72	58.0	26	21.0	0	0.0

	ANSWERING QUESTION		MUCH FIRMER POLICY		MODERATELY FIRMER POLICY		ESSENTIALLY UNCHANGED POLICY		MODERATELY EASIER POLICY		MUCH EASIER POLICY	
	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT
LENDING TO NONFINANCIAL BUSINESSES												
TERMS AND CONDITIONS:												
INTEREST RATES CHARGED	125	100.0	1	0.8	9	7.2	106	84.8	9	7.2	0	0.0
COMPENSATING OR SUPPORTING BALANCES	125	100.0	1	0.8	9	7.2	111	88.8	4	3.2	0	0.0
STANDARDS OF CREDIT WORTHINESS	125	100.0	0	0.0	8	6.4	115	92.0	2	1.6	0	0.0
MATURITY OF TERM LOANS	125	100.0	0	0.0	7	5.6	113	90.4	5	4.0	0	0.0
REVIEWING CREDIT LINES OR LOAN APPLICATIONS												
ESTABLISHED CUSTOMERS	125	100.0	0	0.0	2	1.6	114	91.2	9	7.2	0	0.0
NEW CUSTOMERS	125	100.0	4	3.2	9	7.2	92	73.6	19	15.2	1	0.8
LOCAL SERVICE AREA CUSTOMERS	123	100.0	0	0.0	4	3.3	108	87.8	11	8.9	0	0.0
NONLOCAL SERVICE AREA CUSTOMERS	123	100.0	4	3.3	17	13.8	94	76.4	7	5.7	1	0.8

1/ SURVEY OF LENDING PRACTICES AT 125 LARGE BANKS REPORTING IN THE FEDERAL RESERVE QUARTERLY INTEREST RATE SURVEY AS OF AUGUST 15, 1968.

	ANSWERING QUESTION		MUCH FIRMER POLICY		MODERATELY FIRMER POLICY		ESSENTIALLY UNCHANGED POLICY		MODERATELY EASIER POLICY		MUCH EASIER POLICY	
	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT
FACTORS RELATING TO APPLICANT 2/												
VALUE AS DEPOSITOR OR SOURCE OF COLLATERAL BUSINESS	125	100.0	3	2.4	15	12.0	105	84.0	2	1.6	0	0.0
INTENDED USE OF THE LOAN	124	100.0	2	1.6	12	9.7	106	85.5	4	3.2	0	0.0
LENDING TO "NONCAPTIVE" FINANCE COMPANIES												
TERMS AND CONDITIONS:												
INTEREST RATES CHARGED	124	100.0	0	0.0	4	3.2	119	96.0	1	0.8	0	0.0
COMPENSATING OR SUPPORTING BALANCES	124	100.0	0	0.0	4	3.2	119	96.0	1	0.8	0	0.0
ENFORCEMENT OF BALANCE REQUIREMENTS	123	100.0	1	0.8	10	8.1	111	90.3	1	0.8	0	0.0
ESTABLISHING NEW OR LARGER CREDIT LINES	124	100.0	8	6.5	19	15.3	89	71.7	8	6.5	0	0.0

	ANSWERING QUESTION		CONSIDERABLY LESS WILLING		MODERATELY LESS WILLING		ESSENTIALLY UNCHANGED		MODERATELY MORE WILLING		CONSIDERABLY MORE WILLING	
	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT	BANKS	PCT
WILLINGNESS TO MAKE OTHER TYPES OF LOANS												
TERM LOANS TO BUSINESSES	125	100.0	2	1.6	12	9.6	103	82.4	8	6.4	0	0.0
CONSUMER INSTALMENT LOANS	124	100.0	0	0.0	3	2.4	104	83.9	15	12.1	2	1.6
SINGLE FAMILY MORTGAGE LOANS	121	100.0	1	0.8	8	6.6	86	71.1	22	18.2	4	3.3
MULTI-FAMILY MORTGAGE LOANS	121	100.0	3	2.5	13	10.7	99	81.8	4	3.3	2	1.7
ALL OTHER MORTGAGE LOANS	121	100.0	2	1.7	14	11.6	93	76.8	11	9.1	1	0.8
PARTICIPATION LOANS WITH CORRESPONDENT BANKS	125	100.0	1	0.8	9	7.2	107	85.6	8	6.4	0	0.0
LOANS TO BROKERS	124	100.0	1	0.8	13	10.5	104	83.9	6	4.8	0	0.0

2/ FOR THESE FACTORS, FIRMER MEANS THE FACTORS WERE CONSIDERED MORE IMPORTANT IN MAKING DECISIONS FOR APPROVING CREDIT REQUESTS, AND EASIER MEANS THEY WERE LESS IMPORTANT.

COMPARISON OF QUARTERLY CHANGES IN BANK LENDING PRACTICES AT BANKS GROUPED BY SIZE OF TOTAL DEPOSITS 1/
(STATUS OF POLICY ON AUGUST 15, 1968, COMPARED TO THREE MONTHS EARLIER)
(NUMBER OF BANKS IN EACH COLUMN AS PER CENT OF TOTAL BANKS ANSWERING QUESTION)

SIZE OF BANK -- TOTAL DEPOSITS IN BILLIONS

	TOTAL		MUCH STRONGER		MODERATELY STRONGER		ESSENTIALLY UNCHANGED		MODERATELY WEAKER		MUCH WEAKER	
	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1
STRENGTH OF DEMAND FOR COMMERCIAL AND INDUSTRIAL LOANS (AFTER ALLOWANCE FOR BANK'S USUAL SEASONAL VARIATION)												
COMPARED TO THREE MONTHS AGO	100	100	2	1	24	15	50	63	24	20	0	1
ANTICIPATED DEMAND IN NEXT 3 MONTHS	100	100	0	0	29	17	54	60	17	23	0	0

	TOTAL		MUCH FIRMER		MODERATELY FIRMER		ESSENTIALLY UNCHANGED		MODERATELY WEAKER		MUCH WEAKER	
	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1
LENDING TO NONFINANCIAL BUSINESSES												
TERMS AND CONDITIONS:												
INTEREST RATES CHARGED	100	100	2	0	5	8	86	85	7	7	0	0
COMPENSATING OR SUPPORTING BALANCES	100	100	2	0	7	7	84	92	7	1	0	0
STANDARDS OF CREDIT WORTHINESS	100	100	0	0	2	8	93	92	5	0	0	0
MATURITY OF TERM LOANS	100	100	0	0	5	6	90	90	5	4	0	0
REVIEWING CREDIT LINES OR LOAN APPLICATIONS												
ESTABLISHED CUSTOMERS	100	100	0	0	2	1	86	94	12	5	0	0
NEW CUSTOMERS	100	100	5	2	5	8	71	76	17	14	2	0
LOCAL SERVICE AREA CUSTOMERS	100	100	0	0	3	4	84	89	13	7	0	0
NONLOCAL SERVICE AREA CUSTOMERS	100	100	5	2	8	17	76	76	8	5	3	0

1/ SURVEY OF LENDING PRACTICES AT 41 LARGE BANKS (DEPOSITS OF $1 BILLION OR MORE) AND 84 SMALL BANKS (DEPOSITS OF LESS THAN $1 BILLION) REPORTING IN THE FEDERAL RESERVE QUARTERLY INTEREST RATE SURVEY AS OF AUGUST 15, 1968.

SIZE OF BANK -- TOTAL DEPOSITS IN BILLIONS

	NUMBER ANSWERING QUESTION		MUCH FIRMER POLICY		MODERATELY FIRMER POLICY		ESSENTIALLY UNCHANGED POLICY		MODERATELY EASIER POLICY		MUCH EASIER POLICY	
	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1
FACTORS RELATING TO APPLICANT 2/												
VALUE AS DEPOSITOR OR SOURCE OF COLLATERAL BUSINESS	100	100	0	4	10	13	85	83	5	0	0	0
INTENDED USE OF THE LOAN	100	100	0	2	10	10	85	86	5	2	0	0
LENDING TO "NONCAPTIVE" FINANCE COMPANIES												
TERMS AND CONDITIONS:												
INTEREST RATES CHARGED	100	100	0	0	3	4	97	95	0	1	0	0
COMPENSATING OR SUPPORTING BALANCES	100	100	0	0	3	4	94	96	3	0	0	0
ENFORCEMENT OF BALANCE REQUIREMENTS	100	100	0	1	3	11	94	88	3	0	0	0
ESTABLISHING NEW OR LARGER CREDIT LINES	100	100	3	8	10	18	82	67	5	7	0	0

	NUMBER ANSWERING QUESTION		CONSIDERABLY LESS WILLING		MODERATELY LESS WILLING		ESSENTIALLY UNCHANGED		MODERATELY MORE WILLING		CONSIDERABLY MORE WILLING	
	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1	$1 & OVER	UNDER $1
WILLINGNESS TO MAKE OTHER TYPES OF LOANS												
TERM LOANS TO BUSINESSES	100	100	2	1	7	11	86	81	5	7	0	0
CONSUMER INSTALMENT LOANS	100	100	0	0	3	2	86	83	8	14	3	1
SINGLE FAMILY MORTGAGE LOANS	100	100	0	1	5	7	66	74	21	17	8	1
MULTI-FAMILY MORTGAGE LOANS	100	100	3	2	18	7	68	89	8	1	3	1
ALL OTHER MORTGAGE LOANS	100	100	0	2	21	7	66	83	13	7	0	
PARTICIPATION LOANS WITH CORRESPONDENT BANKS	100	100	0	1	12	5	76	90	12	4	0	0
LOANS TO BROKERS	100	100	0	1	15	8	78	87	7	4	0	0

2/ FOR THESE FACTORS, FIRMER MEANS THE FACTORS WERE CONSIDERED MORE IMPORTANT IN MAKING DECISIONS FOR APPROVING CREDIT REQUESTS, AND EASIER MEANS THEY WERE LESS IMPORTANT.

TABLE 3

NET RESPONSES OF BANKS IN LENDING PRACTICES SURVEYS
(In per cent)

	Feb. 1967	May 1967	Aug. 1967	Nov. 1967	Feb. 1968	May 1968	Aug. 1968
Strength of loan demand 1/ (compared to 3 months ago)	-29.3	12.0	20.2	18.8	-8.0	64.8	-2.4
Anticipated demand in next 3 months	17.3	44.4	63.2	71.2	50.0	66.4	--
LENDING TO NONFINANCIAL BUSINESSES 2/							
Terms and Conditions							
Interest rates charged	-75.2	-69.8	21.6	30.4	34.4	93.6	0.8
Compensating or supporting balances	2.3	1.5	20.8	25.0	16.1	56.8	4.8
Standards of credit worthiness	9.1	9.5	12.0	8.9	7.3	32.8	4.8
Maturity of term loans	- 3.0	- 3.1	5.6	12.1	1.6	32.8	1.6
Reviewing Credit Lines							
Established customers	-14.3	-14.2	1.6	6.4	-0.8	28.0	-5.6
New Customers	-38.3	-23.1	16.8	21.6	10.5	64.8	-5.6
Local service area customers	-17.6	-12.1	0.8	6.5	2.5	30.0	-5.6
Non-local service area customers	-10.8	- 4.0	16.1	18.9	11.6	56.9	10.6
Factors Relating to Applicant (Net percentage indicating more important)							
Value of depositor as source of business	5.3	6.3	25.6	20.0	19.2	54.4	12.8
Intended use of loan	-12.9	-13.4	10.4	14.4	12.0	44.4	8.1
LENDING TO NONCAPTIVE FINANCE COMPANIES 2/							
Terms and Conditions							
Interest rates charged	-49.6	-14.2	6.4	10.4	22.4	60.5	2.4
Compensating or supporting balances	4.5	2.4	9.6	11.2	5.6	25.0	2.4
Enforcement of balance requirements	9.8	4.8	14.4	17.6	12.8	32.3	8.1
Establishing new or larger credit lines	- 0.8	- 5.6	13.7	14.4	7.2	53.2	15.3
WILLINGNESS TO MAKE OTHER LOANS 3/							
Term loans to businesses	-25.6	-21.5	6.4	11.2	- 4.0	49.6	4.8
Consumer instalment loans	-23.5	-31.2	-16.1	-16.1	-22.6	- 0.8	-11.3
Single-family mortgage loans	-42.0	-53.2	- 8.2	4.1	- 4.9	32.0	-14.1
Multi-family mortgage loans	- 4.6	-17.0	9.0	14.0	7.4	36.4	8.2
All other mortgage loans	-14.5	-28.3	9.8	14.0	--	43.4	3.4
Participation loans with correspondent banks	-22.1	-24.2	- 6.4	- 4.8	8.8	16.0	1.6
Loans to brokers	-17.4	-13.8	1.6	3.2	1.6	23.4	6.5

1/ Per cent of banks reporting stronger loan demand minus per cent of banks reporting weaker loan demand. Positive number indicates net stronger loan demand, negative number indicates net weaker loan demand.
2/ Per cent of banks reporting firmer lending policies minus per cent of banks reporting weaker lending policies. Positive number indicates net firmer lending policies, negative number indicates net easier lending policies.
3/ Per cent of banks reporting less willingness to make loans minus per cent of banks more willing to make loans. Positive number indicates less willingness, negative number indicates more willingness.
NOTE: 133 banks participated in the February 1967 Survey; 125 banks have participated in the surveys since that time.

APPENDIX B: CHANGES IN U.S. LIABILITIES TO FOREIGN OFFICIAL ACCOUNTS

The three tables appended deal successively with (1) the financing of the U.S. balance of payments deficit, (2) the composition of changes in U.S. liabilities to foreign official accounts, and (3) the place of changes in U.S. liabilities among the official reserve transactions of 7 continental European countries, and the relation of these changes to the over-all balance of payments surpluses of this group of countries.

The period covered is a 2-1/4-year interval starting from March 31, 1966. This is divided into 6-month periods and one 3-month period, chosen to avoid periods ending at midyear or December 31. The following list will serve as a reminder of the state of economic affairs in each period.

I.	April-September 1966	Culmination of tight money. Downturn in Germany and U.K.
II.	Oct. 1966-Mar. 1967	Recessions in Europe and U.S. Early-1967 revival of confidence in sterling.
III.	April-September, 1967	Beginnings of upturns.
IV.	Oct. 1967-Mar. 1968	Sharp rise in U.S. imports. Sterling devaluation. Gold rush.
V.	April-June, 1968	Further expansion. French crisis.

Over these 27 months there was only a negligible net increase (under $0.4 billion) in total U.S. liquid and near-liquid liabilities to foreign official accounts apart from the transfer of U.K. security portfolio proceeds to the U.K. reserves. (See last line of Table 1, with footnote 2.) In period III, however, there was a large increase ($1.5 billion); together with a large increase in liquid liabilities to foreign private accounts, including the foreign branches of U.S. banks, this covered a very large over-all deficit ($4.4 billion at an annual rate, on basis described in footnote 1 of Table 1) and also served to provide a substantial amount of assistance to the United Kingdom (represented approximately by the $0.9 billion increase in official U.S. holdings of convertible foreign currencies -- 4th line of Table 1). In period IV the U.S. deficit increased further and even larger assistance was given the United Kingdom than in period III, but the rise in U.S. liabilities to foreign official accounts was reduced to negligible proportions (apart from the liquefying

of the British security portfolio), because gold sales jumped to $2.4 billion. These gold sales -- the amount includes, of course, the U.S. share of gold pool sales -- were partly to central banks, partly to other foreign buyers, and partly to domestic buyers. To the extent that the other foreign buyers were moving out of currencies other than dollars, their purchases caused reserve losses for the countries whose currencies were involved; through the operation of the pool these reserve losses took the form partly of gold losses in those countries and partly of reduction in U.S. liabilities.

In the second quarter of 1968 -- period V -- U.S. liabilities to foreign accounts fell by $1.4 billion in three months, despite the continuing large U.S. balance of payments deficit. As may be seen in the last column of Table 1, this astonishing result was due mainly to the extremely large ($2.3 billion) increase in U.S. liquid liabilities to private foreign accounts, which in turn was made possible by flights of private foreign funds out of sterling and the French franc, mainly via the Euro-dollar market. Besides this, the period was a seasonally favorable one (to the extent of $0.3 billion). Other changes, mutually offsetting, were an increase in our IMF position resulting from the British and French IMF drawings, and a related reduction of our official holdings of foreign currencies as the U.K. paid off Federal Reserve swap drawings.

Table 2 shows that over the 2-1/4 years under review the net change in U.S. liabilities to foreign official accounts was made up as follows:

To other than leading industrial countries	+$1.4 billion
To Canada and Japan	- .3
To United Kingdom (adjusted for portfolio liquidation)	- .6
To 7 Continental European countries1/	- .1
Unallocated	+ .1
	+$ .4 billion

The rise in liabilities to countries outside the Group of Ten took the form mainly of an increase in time deposits of original maturity over one year. Japan also acquired long-term time deposits and Canada took nonmarketable U.S. Treasury bonds denominated in U.S. dollars: "liquid" dollar assets of these two countries were reduced by $1.5 billion. They took no foreign currency claims on the United States.

The seven continental European countries took virtually no long-term time deposits or nonmarketable U.S.-dollar securities, but they increased their official foreign currency claims on the United States by $0.5 billion.

1/ Including BIS.

The U.S.-dollar official claims of these countries on the United States were reduced by $0.4 billion over the 2-1/4-year period (next-to-last line of Table 3; excluding BIS). The last line of Table 3 indicates that through swap drawings initiated by the Federal Reserve, $0.8 billion of the $1.2 billion increase in such dollar liabilities during periods I to IV -- from March 31, 1966 to March 31, 1968 -- was given exchange value guaranties; in the second quarter of 1968, when the dollar liabilities fell to these countries by $1.6 billion, the swap drawings on them were cut only $0.5 billion.

Table 3, line 1, shows that the continental G-10 countries had a fairly steady over-all balance of payments surplus (as measured by changes in net external assets of commercial banks plus net official reserve assets) between March 31, 1966 and March 31, 1968, at annual rates between $1.5 and $2 billion, with seasonally more favorable results in the April-to-September semesters. In these 24 months, their net official reserve assets rose by $2.8 billion, with a similar seasonal variation. It should be observed, however, that in period IV -- October 1967 to March 1968 -- both the over-all surplus and the reserve gain would have been larger if it had not been for gold-rush buying by holders of their currencies.

In periods I and II, the increase in U.S. liabilities to official accounts in these seven countries was substantially smaller than their total net reserve asset gains, because they acquired some gold and added substantially to their IMF and GAB positions. In period III, however, the U.S. liabilities increased by $1.2 billion, a little more than the amount of net reserve gains.

The subsequent shrinkage in the rate of additions to U.S. reserve liabilities to these countries was not due to the shrinkage, seasonal or otherwise, in their over-all payments surplus, because this shrinkage was more than compensated for by their gold losses. What caused the slowing in rise of their claims on the United States was a sharp increase in their reserve claims on other countries, primarily on the United Kingdom.

In period V -- the three months April-June of this year -- U.S. official reserve liabilities to the seven continental G-10 countries fell by $1.5 billion. The decline occurred mainly in dollar holdings of Germany and Italy; both countries purchased substantial amounts of gold, and French and British drawings of their currencies through the IMF were converted into dollars.

Table 1

FINANCING THE U.S. PAYMENTS DEFICIT[1]
(in millions of dollars)

	Six-month periods ending: Sept. 1966	March 1967	Sept. 1967	March 1968	April-June 1968p.
Adjusted deficit[1]					
Seasonally adjusted					
Annual rate (b.)	2.0	3.4	4.4	5.9[2]	4.2
Actual amount, s.a.	1,110	1,704	2,177	2,971	1,062
Without seas. adj.	1,560	1,570	2,285	2,748	762
Incr. in U.S. official holdings of convertible fgn.currencies	589	-834	886	1,546	-267
Net financing through gold, IMF, and liability increases	2,149	736	3,171	4,294	495
Incr. in liquid liabilities:					
to commercial banks	1,460	80	1,447	1,217	2,219
to other private fgn. accts.	157	26	108	227	96
Gold sales	382	172	107	2,374	22
Decr. in IMF position (incr.,-) less gold deposit liab. to IMF	403	32	-10	-97	-437
Incr. in liabilities to foreign official accounts	-253	426	1,519	573[3]	-1,405

1/ This analysis deals with the balance financed by official reserve transactions and increases in liquid liabilities to commercial banks abroad and to other foreign private accounts. This is closely similar to the balance on the liquidity basis before special transactions, except that it counts "above the line " rather than as financing items, the following: all changes in liabilities, liquid or nonliquid, to international institutions other than the IMF; foreign prepayments of debts to the U.S. Government; and certain special transactions other than changes in foreign official holdings of nonmarketable U.S. Treasury debt and long-term time deposits. In particular U.K. official transactions in U.S. corporate and Agency securities are counted above the line.

2/ Would be $4.9 billion if adjusted for U.K. reserve addition from security liquidations.

3/ Includes proceeds of U.K. security liquidations added to U.K. reserves ($490 million).

September 5, 1968

Table 2

BREAKDOWN OF CHANGES IN
LIABILITIES TO FOREIGN OFFICIAL ACCOUNTS[1/]
(in millions of dollars)

	Six-month periods ending: Sept. 1966	March 1967	Sept. 1967	March 1968	April-June 1968p.
Total[1/]	-253	426	1,519	573	-1,405
To others than leading industrial countries:					
Long-term time deposits	196	469	341	243	106
Non-marketable US-$ bonds & notes	0	0	0	0	10
Short-term US-$ assets[2/] & marketable US-$ Govt. securities	19	- 8	218	-140	- 36
Foreign currency securities	-49	0	0	0	0
Total	(166)	(461)	(559)	(103)	(80)
To Canada and Japan:					
Long-term time deposits	113	240	86	72	58
Non-marketable US-bonds & notes	0	-155	200	70	500
Short-term US-$ asssts[2/] & marketable US-$ Govt. securities	-444	-135	-344	-222	-351
Total	(-331)	(-50)	(-58)	(-80)	207
To United Kingdom:					
Long-term time deposits	61	-32	-52	-36	0
Short-term US-$ assets[2/] & marketable US-$ Govt. securities	-671	263	-366	605	-104
Total	(-610)	(231)	(-418)	(569)	(-104)
To 7 Continental European countries:[3/]					
Long-term time deposits	0	2	- 1	- 1	0
Nonmarketable US-$ bonds & notes	-12	- 5	- 6	-10	- 8
Short-term US-$ assets & marketable U.S.-$ Govt. securities	707	-237	1,283	-521	-1,707
Foreign currency securities	-198	- 1	157	474	126
Total	(497)	(-241)	(1,433)	(-58)	(-1,589)
Unallocated [4/]	25	25	4	38	...

1/ See last line of Table 1. Does not include changes in foreign official holdings of U.S. corporate and Government Agency securities.
2/ Includes nonmarketable (short-term) certificates, in addition to marketable bills and certificates, deposits, and miscellaneous short-term private U.S. liabilities.
3/ Belgium, France, Germany, Italy, Netherlands, Sweden, Switzerland; also BIS.
4/ Miscellaneous nonmarketable U.S. Government liabilities other than U.S. Treasury securities.

Table 3

CHANGES IN RESERVE POSITIONS
OF 7 CONTINENTAL EUROPEAN COUNTRIES
(in millions of dollars)

	Six-month periods ending:				April-June 1968p.
	Sept. 1966	March 1967	Sept. 1967	March 1968	
Increase in net external assets of commercial banks & official agencies	1,166	749	1,203	346	n.a.
Commercial banks (short-term)	-194	572	284	-59	
Official	1,360	177	919	405	-750
Gold	290	53	121	-746	351
IMF and GAB positions	585	115	-385	130	29
Other net assets:					
Other than U.S. liabilities	-28	235	-5	961	325
U.S. liabilities	513	-226	1,188	60	-1,455
Payable in foreign currency	-198	0	96	476	126
Payable in U.S. dollars	711	-226	1,092	-416	-1,581
Memo: Increase in US-initiated swap drawings from these countries and BIS	225	-225	403	434	-513

Source: Confidential BIS compilations, except breakdown of changes in official "other net assets"; changes in U.S. liabilities correspond to data in Table 2, but exclude BIS. Change in "other net assets other than U.S. liabilities" is a residual, and may include errors arising from differences between U.S. liability accounts and foreign asset accounts.

U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

SEASONALLY ADJUSTED