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Confidential (FR) Class II FOMC

May 13, 1981

RECENT DEVELOPMENTS

Prepared for the Federal Open Market Committee
By the staff of the Board of Governors of the Federal Reserve System

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SELECTED DOMESTIC NONFINANCIAL DATA
(Seasonally adjusted)

	Latest data			Percent change from		
	Period	Release date	Data	Preceding period	Three periods earlier	Year earlier
				(At annual rate)		
Civilian labor force	Apr.	5-8-81	106.7	6.2	4.5	2.2
Unemployment rate (%) 1/	Apr.	5-8-81	7.3	7.3	7.4	6.9
Insured unemployment rate (%) 1/	Apr.	5-8-81	3.3	3.3	3.4	3.7
Nonfarm employment, payroll (mil.)	Apr.	5-8-81	91.5	-2.9	.1	.6
Manufacturing	Apr.	5-8-81	20.5	3.2	2.2	-.9
Nonmanufacturing	Apr.	5-8-81	71.0	-4.6	-.5	1.0
Private nonfarm:						
Average weekly hours (hr.) 1/	Apr.	5-8-81	35.3	35.3	35.5	35.3
Hourly earnings ($) 1/	Apr.	5-8-81	7.12	7.10	7.02	6.54
Manufacturing:						
Average weekly hours (hr.) 1/	Apr.	5-8-81	40.1	40.0	40.4	39.8
Unit labor cost (1967=100)	Mar.	4-29-81	205.1	.6	9.6	9.4
Industrial production (1967=100)	Mar.	4-15-81	151.7	4.8	1.9	-.3
Consumer goods	Mar.	4-15-81	147.7	6.5	.0	-.6
Business equipment	Mar.	4-15-81	179.5	10.1	3.8	1.9
Defense & space equipment	Mar.	4-15-81	101.0	3.6	1.2	4.0
Materials	Mar.	4-15-81	153.7	2.3	2.9	-1.0
Consumer prices all items (1967=100)	Mar.	4-23-81	265.5	7.3	9.2	10.5
All items, excluding food & energy	Mar.	4-23-81	248.3	4.9	5.7	9.9
Food	Mar.	4-23-81	271.6	4.4	2.1	10.0
Producer prices: (1967=100)						
Finished goods	Apr.	5-8-81	267.3	9.5	11.7	10.6
Intermediate materials, nonfood	Apr.	5-8-81	307.9	13.4	12.2	10.8
Crude foodstuffs & feedstuffs	Apr.	5-8-81	262.4	18.6	-15.4	11.9
Personal income ($ bil.) 2/	Mar.	4-17-81	2,334.9	9.1	10.2	11.1
				(Not at annual rates)		
Mfrs. new orders dur. goods ($ bil.)	Mar.	4-30-81	84.6	2.9	2.3	9.1
Capital goods industries	Mar.	4-30-81	28.9	10.1	5.1	6.3
Nondefense	Mar.	4-30-81	23.8	15.8	10.0	5.5
Defense	Mar.	4-30-81	5.1	-10.6	-13.2	10.1
Inventories to sales ratio: 1/						
Manufacturing and trade, total	Feb.	5-7-81	1.36	1.35	1.38	1.39
Manufacturing	Mar.	4-30-81	1.56	1.55	1.53	1.59
Trade	Feb.	5-7-81	1.18	1.17	1.23	1.26
Ratio: Mfrs.' durable goods inventories to unfilled orders 1/	Mar.	4-30-81	.587	.590	.579	.572
Retail sales, total ($ bil.)	Apr.	5-12-81	86.3	-1.0	1.0	13.0
GAF 3/	Apr.	5-12-81	18.4	1.2	2.2	12.1
Auto sales, total (mil. units.) 2/	Apr.	5-5-81	8.06	-21.7	-13.6	-1.7
Domestic models	Apr.	5-5-81	5.75	-25.2	-16.6	-4.1
Foreign models	Apr.	5-5-81	2.31	-11.5	-5.2	4.7
Housing starts, private (thous.) 2/	Mar.	4-16-81	1,284	5.8	-16.4	23.5
Leading indicators (1967=100)	Mar.	4-29-81	137.1	1.4	-.1	4.3

1/ Actual data used in lieu of percent changes for earlier periods.
2/ At annual rate.
3/ Excludes mail order houses.

Economic activity continued to grow in April, although at a slower pace than prevailed at the turn of the year. Industrial production apparently posted another gain but nonfarm payroll employment declined. On balance, consumer spending for goods fell in April, as an increase in outlays on nonauto items was more than offset by a sharp drop in auto sales following the termination of rebates. Housing starts remained at a low level in March, but business investment spending showed considerable strength in the first quarter. Inflation moderated in recent months with a weakening in prices of gasoline, food, and housing; but pressures from rising labor costs continued to be strong.

Industrial Production and Employment

Industrial production tentatively is estimated to have risen about 1/2 percent in April, following a similar gain in March. Auto assemblies led the April advance, rising almost 5 percent but only to an annual rate of 6.8 million units. Assemblies are scheduled to rise further in May, but these plans may be scaled back unless sales pick up soon. The walk-out of union miners that began March 27 cut coal production in half; this had the effect of damping the overall production index by about 0.3 percent. Raw steel production also declined slightly, while output of other industries including equipment increased further. Production gains raised capacity utilization for manufacturing somewhat in April.

A small rise in manufacturing employment accompanied the increase in industrial production in April. Total nonfarm payroll employment, however, was down about 45,000 from March after adjusting for workers on strike; since January hiring has tapered off steadily. Employment

CHANGES IN EMPLOYMENT[1]
(Thousands of employees; based on seasonally adjusted data)

	1979	1980	1980 Q3	1980 Q4	1981 Q1	1981 Mar.	1981 Apr.
	- - - - Average monthly changes - - -						
Nonfarm payroll employment[2]	176	37	112	247	196	62	-220
Strike adjusted	182	31	135	220	194	70	-43
Manufacturing	1	-56	10	89	29	26	55
Durable	4	-46	3	68	22	30	38
Nondurable	-3	-10	7	21	7	-4	17
Construction	20	-9	8	35	0	-10	-82
Trade	40	16	54	6	98	47	-124
Finance and services	74	74	84	86	63	43	77
Private nonfarm production workers	112	-5	133	179	157	83	-188
Manufacturing production workers	-11	-63	14	74	24	26	45
Total employment[3]	172	-42	133	34	377	485	564
Nonagricultural	174	-48	78	36	416	490	377

1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments. Strike-adjusted data noted.
3. Survey of households.

SELECTED UNEMPLOYMENT RATES
(Percent; based on seasonally adjusted data)

	1979	1980	1980 Q3	1980 Q4	1981 Q1	1981 Mar.	1981 Apr.
Total, 16 years and older	5.8	7.1	7.5	7.5	7.4	7.3	7.3
Teenagers	16.1	17.8	18.4	18.3	19.1	19.1	19.1
20-24 years old	9.1	11.4	12.1	12.1	11.8	11.7	12.1
Men, 25 years and older	3.3	4.8	5.4	5.0	4.8	4.7	4.6
Women, 25 years and older	4.8	5.5	5.6	5.9	5.8	5.9	5.6
White	5.1	6.3	6.7	6.6	6.6	6.5	6.5
Black and other	11.3	13.3	13.9	14.1	13.2	13.7	13.2
Fulltime workers	5.3	6.9	7.3	7.3	7.1	7.1	6.9
White collar	3.3	3.7	3.8	3.9	3.9	3.9	4.0
Blue collar	6.9	10.1	11.1	10.7	10.0	9.8	9.6

continued to rise in the service industries, but there was a sizable drop in employment at retail trade establishments, where seasonal hiring for Easter was less than usual. The number of construction jobs also fell again in April, bringing the cumulative job decline in this sector since January to nearly 200,000. The gains in manufacturing employment were concentrated in durable goods industries. The factory workweek also edged up--returning to the level prevailing at the end of 1980. Despite substantial rehiring over the past 9 months, employment in manufacturing is still well below the pre-recession peak in mid-1979.

As in March, the April survey of households showed large increases in both employment and the labor force, leaving the overall unemployment rate unchanged at 7.3 percent--about where it has been since December. The two employment measures often have shown disparate monthly movements, but they have tended to track together over the longer term. The recovery in household employment lagged behind that reported in the payroll survey during the second half of 1980; the recent large increases in household employment have narrowed the gap considerably.

Personal Income and Consumer Spending

Personal income growth tapered off in recent months and was barely sufficient to keep ahead of inflation. Income rose 9-1/4 percent (annual rate) from January to March versus 13-1/2 percent between last September and January. Much of the slowdown reflected smaller increases in wages and salaries in commodity-producing industries as employment gains dwindled. Meanwhile, farm proprietors' income fell through March as a result of declines in livestock and crop prices coupled with higher production costs. Real disposable personal income grew at about a 2-1/2

PERSONAL INCOME
(Based on seasonally adjusted data)

	1979	1980	1980 Q4	1981 Q1	1981 Feb.	1981 Mar.
	- - Percentage changes at annual rates[1] - -					
Total personal income	12.3	11.0	14.3	11.4	8.5	9.1
Wage and salary disbursements	10.8	9.0	17.8	13.4	7.3	8.6
Private	11.6	9.2	18.3	15.2	7.7	9.5
Disposable personal income						
Nominal	11.7	10.9	12.8	10.6	8.5	8.6
Real	2.0	.8	2.9	2.5	2.2	-.9
	- - Changes in billions of dollars[2] - -					
Total personal income	18.3	18.7	23.6	19.4	16.3	17.7
Wage and salary disbursements	10.3	9.8	18.1	13.6	8.7	10.4
Private	8.9	8.1	14.8	12.5	7.5	9.3
Manufacturing	2.0	2.3	5.8	2.9	1.3	1.7
Other income	8.9	9.6	6.4	9.4	7.9	7.7
Transfer payments	2.8	4.1	.4	1.9	.0	1.8
Less: Personal contributions for social insurance	.9	.8	.9	3.6	.3	.4
Memorandum:						
Personal saving rate[3]	5.2	5.6	5.1	4.7	4.7	n.a.

1. Changes over periods longer than one quarter are measured from final quarter of preceding period to final quarter of period indicated. Changes for quarterly periods are compounded rates of change; monthly changes are not compounded.
2. Average monthly changes are from the final month of the preceding period to the final month of period indicated; monthly figures are changes from the preceding month.
3. Monthly saving rate equals the centered three-month moving average of personal saving as a percentage of the centered three-month moving average of disposable personal income.

percent annual rate for the first quarter as a whole, but the level was still only fractionally above its previous peak in January 1980.

Growth in consumer spending on goods was strong in the first quarter. In April, however, total retail sales declined 1 percent. The weak overall sales figures reflected mainly a sharp drop in unit auto sales. Excluding automobiles and nonconsumption items, nominal sales advanced 1 percent in April, after posting a similar gain in March. In April, sales at the GAF grouping and at gasoline and food stores registered sizable gains. This sales performance was consistent with an improvement in consumer confidence according to both the Michigan and Conference Board surveys. After drifting downward since November, the composite sentiment measures from these surveys rose in April to values close to those reported last fall.

Auto sales were off sharply throughout April from their March levels. Total unit purchases dropped to an 8.1 million annual rate--the slowest sales pace since June 1980 when credit controls were still in effect; sales of domestic units were at a 5.8 million unit annual rate. A fall in sales of domestically-produced automobiles was expected following the end of rebates that boosted sales in February and March. The slump in sales during April along with higher production rates resulted in a rise in the stock of unsold cars. Domestic auto stocks at the end of April increased to 1.25 million units, a very low level historically, but equivalent to a substantial 65 days supply at the low April sales rate. Purchases of imported cars declined in April to a 2.3 million unit annual rate from 2.6 million in March.

RETAIL SALES
(Percent change from previous period;
based on seasonally adjusted data)

	1980	1981				
	Q4	Q1	Jan.	Feb.	Mar.	Apr.
Total sales	3.3	4.7	2.4	1.6	.4	-1.0
(Real)[1]	.8	2.8	1.8	.9	-.1	n.a.
Total, less auto and nonconsumption items	3.3	3.3	1.7	0.0	.9	1.0
GAF[2]	3.3	3.1	1.4	1.5	-.4	1.2
Durable goods	3.4	8.2	4.2	4.6	-.3	-5.1
Auto	1.6	9.7	3.8	9.0	-.8	-9.3
Furniture & appliances	3.1	4.4	5.2	-3.2	.1	2.0
Nondurable goods	3.2	3.1	1.6	.2	.8	1.0
Apparel	1.4	5.1	4.1	2.0	-1.9	1.6
Food	2.6	2.1	-.1	.2	2.1	1.3
General merchandise[3]	4.1	1.8	-1.0	3.1	0.0	.7
Gasoline	2.5	4.6	2.6	1.2	-.6	1.4

1. BCD series 59. Data are available approximately 3 weeks following the retail sales release.
2. General merchandise, apparel, and furniture and appliance stores.
3. General merchandise excludes mail-order nonstores; mail-order sales are also excluded in the GAF composite sales summary.

AUTO SALES
(Millions of units; seasonally adjusted annual rates)

	1980		1981			
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Total	8.8	9.0	10.0	10.3	10.3	8.1
Foreign-made	2.3	2.5	2.7	2.9	2.6	2.3
U.S.-made	6.5	6.6	7.3	7.3	7.7	5.8
Small	3.2	3.3	3.8	3.9	4.1	2.8
Intermediate & standard	3.3	3.3	3.4	3.4	3.5	2.9

Note: Components may not add to totals due to rounding.

Inventory Investment

Business continued to follow lean inventory policies throughout the first quarter and, relative to sales, stocks remained close to average historical levels. The book value of manufacturing and trade inventories rose rapidly early in the year, with increases averaging about $50 billion at an annual rate in January and February. In real terms, though, there was no buildup in stocks except for crude oil and petroleum products. Prompt adjustments in production schedules occurred in response to sluggish sales and prevented the development of major imbalances; by the end of March, inventory accumulation in book-value terms had slowed, and real stocks apparently declined further.

In the manufacturing sector, the book-value of stocks rose at a $25 billion annual rate in March, following increases of $47 billion and $34 billion in the preceding two months. Nearly four-fifths of the March accumulation occurred in the nondurable goods category, including an $11 billion buildup in stocks of petroleum products that partly reflected price increases. Physical stocks of both crude oil and petroleum products have been well above average since January. In the durable goods category, several of the industries that reported substantial accumulations in January and February showed only small or no book-value increases in March. Moreover, the book value of stocks at merchant wholesalers declined at a $10 billion rate in March and showed a liquidation for the first quarter as a whole.

Business Fixed Investment

Capital spending grew briskly in the first quarter. Real shipments of nondefense capital goods are estimated to have increased more than 4

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars at annual rates)

		1980			1981			
	1979	Q2	Q3	Q4	Q1	Jan.	Feb.(r)	Mar.(p)
Book Value Basis								
Total	47.4	33.8	27.5	13.7	n.a.	40.7	59.8	n.a.
Manufacturing	29.9	20.4	-.1	3.5	35.2	47.0	33.9	24.7
Wholesale	10.3	10.9	18.5	10.3	-1.3	-7.4	13.9	-10.2
Retail	7.2	2.4	9.1	-.1	n.a.	1.2	12.0	n.a.
Constant Dollar Basis								
Total	7.2	.5	-1.9	-5.1	n.a.	2.4	-3.3	n.a.
Manufacturing	6.8	-.5	-5.2	-3.6	n.a.	9.8	5.5	n.a.
Wholesale	.4	1.6	1.9	.3	n.a.	-5.4	-.7	n.a.
Retail	-.1	-.6	1.3	-1.9	n.a.	-2.0	-8.1	n.a.

Details may not add to total due to rounding.

INVENTORIES RELATIVE TO SALES

		1980			1981			
	1979	Q2	Q3	Q4	Q1	Jan.	Feb.(r)	Mar.(p)
Book Value Basis								
Total	1.41	1.50	1.45	1.38	n.a.	1.35	1.36	n.a.
Manufacturing	1.52	1.71	1.64	1.55	1.57	1.54	1.55	1.56
Wholesale	1.17	1.21	1.17	1.12	1.08	1.06	1.08	1.09
Retail	1.44	1.43	1.40	1.35	n.a.	1.31	1.30	n.a.
Constant Dollar Basis								
Total	1.63	1.76	1.72	1.66	n.a.	1.65	1.66	n.a.
Manufacturing	1.87	2.10	2.04	1.96	n.a.	1.97	1.98	n.a.
Wholesale	1.41	1.46	1.45	1.39	n.a.	1.37	1.41	n.a.
Retail	1.44	1.47	1.44	1.41	n.a.	1.38	1.35	n.a.

Annual ratios are averages of monthly ratios. Quarterly ratios are end-of-quarter inventories to average monthly sales in the quarter.

percent, and truck sales--while sluggish--rose somewhat from the depressed fourth-quarter rate. In the nonresidential structures area, real construction outlays surged in January and remained at a high level through March.

Commitments for capital spending suggest some further near-term advance. Constant-dollar orders for nondefense capital goods rose 12.4 percent in March and 4.3 percent for the first quarter as a whole. Despite this surge in new commitments, shipments growth may slow in the coming months because the backlog of unfilled orders for nondefense capital goods has been fairly low relative to deliveries. Contracts for nonresidential plant rose in February and March, following a sharp decline in January, and for the quarter as a whole these contracts were off about 25 percent.

As for longer term investment indicators, the spring McGraw-Hill survey reported that businesses are planning to increase nominal plant and equipment spending 12 percent in 1981. The planned rise in nominal outlays is about the same as indicated in the fall report, but the industry composition is considerably different. Basic durable goods manufacturing industries such as iron and steel and motor vehicles have boosted their plans while nondurable goods producers have scaled back their ambitious capital spending programs of last autumn. In comparison to the McGraw Hill 12 percent, the February Commerce Department survey reported a 10.2 percent rise and the Merrill Lynch survey a 10 percent increase. Given the high level of spending so far this year and the outlook for BFI prices, the survey results suggest little additional gains in real outlays through the end of the year.

BUSINESS CAPITAL SPENDING INDICATORS
(Percentage change from preceding comparable period;
based on seasonally adjusted data)

	1980		1981			
	Q3	Q4	Q1	Jan.	Feb.	Mar.
Nondefense capital goods shipments						
Current dollars	2.1	3.4	3.0	3.1	-2.3	5.0
Constant dollars[1]	2.0	-.9	4.2	4.3	-2.3	.9
Addenda: Sales of heavy-weight trucks (thousands)	290	230	250	280	230	230
Nonresidential construction						
Current dollars	-4.8	3.0	7.7	4.8	-.5	.0
Constant dollars	-7.0	2.1	6.3	4.6	-.9	-.8
Addenda: Oil and gas well drilling (millions of feet)	25.2	26.5	24.7	21.7	25.4	27.1

1. FRB staff estimate.

BUSINESS CAPITAL SPENDING COMMITMENTS
(Percentage change from preceding comparable period;
based on seasonally adjusted data)

	1980		1981			
	Q3	Q4	Q1	Jan.	Feb.	Mar.
Nondefense capital goods orders						
Current dollars	.2	3.7	7.5	13.1	-16.0	15.8
Constant dollars	.6	.8	4.3	10.5[1]	-15.1	12.4
Machinery						
Current dollars	8.9	6.0	6.5	9.2	-7.0	2.3
Constant dollars[1]	5.7	3.9	3.4	7.4	-7.8	2.0
Addenda: Ratio of current dollar unfilled orders to shipments						
Total	6.37	6.10	5.99	6.02	6.10	5.84
Machinery	4.21	4.16	3.99	3.99	4.04	3.92
Contracts for nonresidential plant						
Current dollars	55.0	26.7	-25.2	-41.6	9.4	34.9
Constant dollars	62.0	25.3	-26.0	-42.1	8.6	35.3

1. FRB staff estimate.

Residential Construction

Housing activity has weakened further in recent months in response to stringent financial conditions. In February and March, housing starts for both single- and multi-family units were well below their levels of 1980-Q4 when total starts averaged about 1.5 million units. In contrast to the reduced level of starts, the total value of residential construction put-in-place during the first quarter rose 5 percent from the preceding quarter, reflecting work on the relatively large number of units started in the second half of last year.

Weakness in the housing sector also showed up in home sales. Sales of new houses remained just above the 500,000 unit annual rate mark in March--almost 20 percent below last summer's peak. Builders have managed to keep inventory positions lean; the number of new houses unsold at the end of March was the lowest since the spring of 1976. Demand for existing homes also has fallen, with sales in the first quarter down 15 percent from the final quarter of last year.

Th slowing of activity in real estate markets has been accompanied by a general deceleration in the rise of house prices. The average price of existing homes sold in the first quarter was 10 percent higher than a year earlier, compared with 14 percent increase over the preceding year; part of the slowdown in this measure of house prices may be attributable to a downgrading in the type of units sold. The slowing has been widespread regionally, with the exception of the South where both sales volume and price increases have been relatively well maintained. Increases in new-house prices measured by the quality-adjusted Census Bureau index, while quite volatile in the last few quarters, also have

SURVEYS OF PLANT AND EQUIPMENT EXPENDITURES
(Percent change from prior year)

		Planned for 1981					
		Commerce Department[1]		McGraw-Hill		Merrill Lynch	
	1980	Dec. 1980	Feb. 1981	Fall 1980	Spring 1981	Fall 1980	Spring 1980
All Business	9.3	10.8	10.2	11.9[2]	12.0	7.0[2]	10
Manufacturing	17.4	14.1	12.1	14.6	15.0	10.6	12
Durables	15.4	13.3	12.8	4.7	10.3	4.3	10
Nondurables	19.5	14.9	11.4	23.8	19.8	16.2	14
Nonmanufacturing	4.7	8.7	8.9	9.4	10.1	4.0	9
Mining	18.7	18.8	17.5	13.0	5.6	2.6	14
Transportation	-2.1	8.2	6.5	5.4	8.7[5]	1.0	14
Utilities	4.4	8.7	8.0	8.6	13.1	3.1	7
Trade and Services	3.2	6.8	6.3	11.8[3]	10.7	5.1	5[6]
Communications and other	6.2	9.5	13.4	8.5[4]	n.a.	5.6	23[4]

1. Results are adjusted for systematic bias. Without this adjustment, the Commerce results would have been 8.6 percent in December and 8.6 percent in February.
2. Not strictly comparable to the other reports because of coverage differences.
3. Contains commercial businesses only.
4. Contains the communication industry only.
5. Includes the communication industry.
6. Consists of commercial business and other industries.

RECENT ERROR HISTORY OF THE SPRING PRIVATE SURVEYS
(Percent change from prior year)

Year	Anticipated Change, McGraw- Hill	Anticipated Change, Merrill Lynch	Actual Change
1974	19.5	19.2	12.7
1975	5.5	6.0	.3
1976	12.9	7.3	6.8
1977	17.5	16.4	12.7
1978	17.3	15.4	13.3
1979	15.7	15.0	15.1
1980	12.2	11.4	9.3[1]

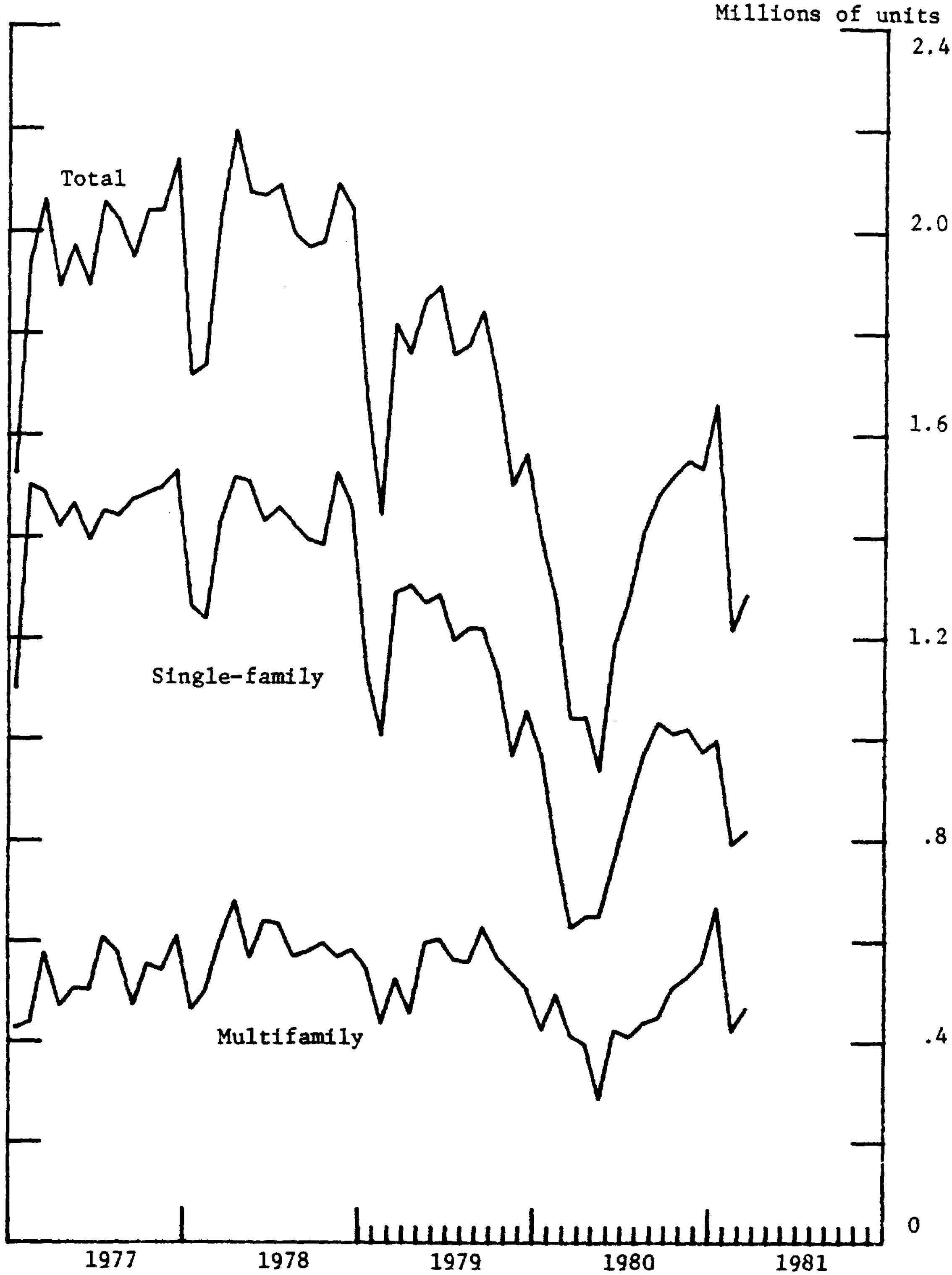
1. Based on the rebenchmarked Commerce Study and not strictly comparable to other data.

PRIVATE HOUSING ACTIVITY
(Seasonally adjusted annual rates, millions of units)

	1980			1981			
	Annual	Q3	Q4	Q1	Jan.	Feb.	Mar.[1]
All units							
Permits	1.17	1.39	1.31	1.17	1.23	1.17	1.13
Starts	1.29	1.39	1.54	1.39	1.66	1.21	1.28
Single-family units							
Permits	.70	.85	.79	.68	.72	.67	.65
Starts	.85	.96	1.00	.87	.99	.79	.82
Sales							
New homes	.53	.60	.54	.52	.53	.51	.51
Existing homes	2.88	3.06	3.00	2.55	2.58	2.56	2.52
Multifamily units							
Permits	.47	.54	.52	.50	.51	.50	.48
Starts	.44	.43	.53	.52	.67	.42	.47
Mobile home shipments	.22	.22	.25	n.a.	.23	.26	n.a.

1. Preliminary estimates.
n.a.--not available.

PRIVATE HOUSING STARTS
(Seasonally adjusted annual rate)



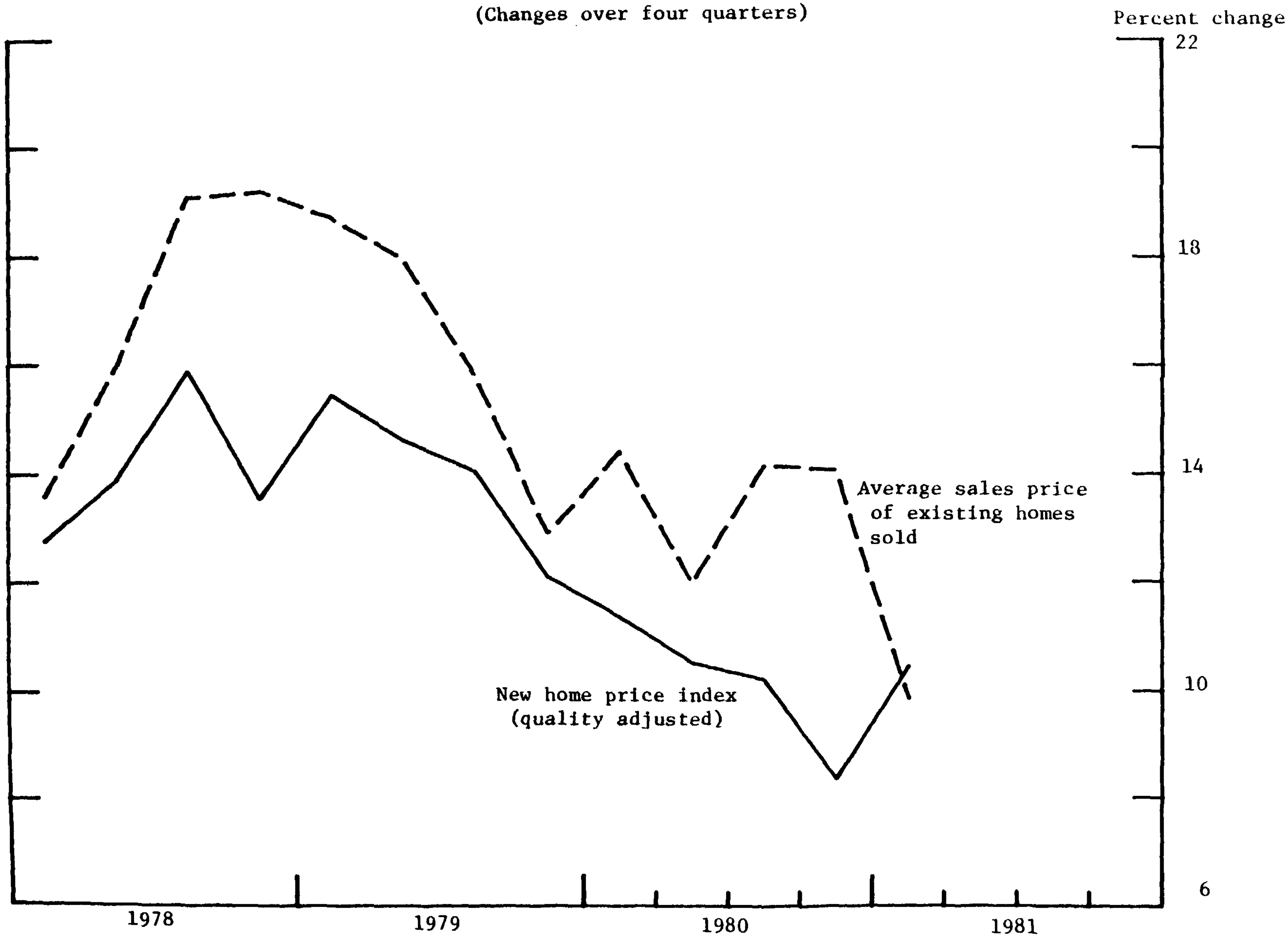
shown a trend toward deceleration on a year-over-year basis. Some of the recent variability in this measure of house prices may reflect the increased use of nontraditional financing techniques, which can affect contracted sales prices.

Government Sector

On a NIPA basis, federal purchases of goods and services rose $7.6 billion (in current dollars) in the first quarter, which represented a rise in real terms of 12.5 percent at an annual rate. The increase included an unusually large rise of $5 billion in CCC acquisitions. Normally, a seasonal reduction in CCC loans occurs in the first quarter, but this year farmers apparently delayed loan repayments until April. In contrast, increases in defense purchases at $3.3 billion in the first quarter slowed relative to the average $5.7 billion quarterly pace observed in 1980. The slower growth in defense purchases appears to be transitory. In March, for example, manufacturers' shipments of defense goods exceeded the November level after a two-month decline and unfilled orders continued to rise through March. Moreover, recent OMB projections call for further increases in defense purchases to a rate of $5.9 billion per quarter over the next 6 quarters, or about a 16 percent nominal increase at an annual rate.

The unified budget deficit edged down slightly in the first quarter to $32.1 billion (not seasonally adjusted) from $33.6 billion in the preceding quarter even though tax collections fell slightly behind expectations. In April, receipts of individual nonwithheld income taxes accelerated relative to a year earlier especially in the April 15-28 period. Total refund payments also accelerated in this period.

RECENT CHANGES IN HOME PRICES
(Changes over four quarters)



Indicators of state and local government spending have been mixed in recent months. The real value of new construction put-in-place rose substantially during the first quarter due to a spurt in spending on road projects. Nevertheless, construction outlays were down 2 percent in real terms from a year ago. Meanwhile, the sector's payroll employment has shown no growth this year. State and local governments apparently have been hiring at a rate just sufficient to replace losses in federally-funded jobs as the administration winds down the CETA public service employment program.

Prices and Labor Costs

Recent price developments have signaled a slowing of inflation in a number of markets. Gasoline prices reportedly have edged down in recent weeks; house price increases have weakened, and some measures even show a decline; and consumer food price advances have continued to be relatively moderate. However, American automakers have announced new price increases, and spot prices for crude foodstuffs turned up in April. Moreover, underlying labor cost pressures remain quite strong.

The upsurge in energy prices early in the year now has abated, although the indirect effects of those increases are still percolating through the economy. Consumer energy prices rose 2 percent in March, far less than in February when the main impact of oil decontrol hit. Most of the March increase probably occurred early in the month; industry sources report that gasoline prices have edged lower over the last six weeks. Crude oil prices also have been reduced by some oil-exporting countries in light of sluggish demands and high inventories. Nevertheless, the prices of energy-intensive products such as industrial

RECENT CHANGES IN PRODUCER PRICES
(Percentage change at annual rates; based on seasonally adjusted data)[1]

	Relative importance[2] Dec. 1980	1980	1980 Q3	1980 Q4	1981 Q1	1981 Mar.	1981 Apr.
Finished goods	100.0	11.8	13.5	8.3	12.0	15.1	9.5
Consumer foods	23.0	7.5	31.0	4.3	.3	9.1	0.0
Consumer nonfood	56.6	14.2	7.5	8.9	17.4	19.7	12.8
Energy	12.0	27.8	3.6	14.8	61.7	73.6	19.0
Exc. energy	44.7	10.4	8.7	7.3	7.2	4.5	10.6
Capital equipment	20.3	11.4	9.9	11.8	11.5	8.9	11.2
Intermediate materials[3]	93.6	12.4	7.8	12.9	13.2	15.2	13.4
Exc. food and energy	77.4	10.1	6.9	11.0	7.1	7.4	12.6
Crude food materials	58.2	8.6	73.9	-4.0	-23.1	-24.6	18.6
Crude nonfood	41.8	19.1	32.3	27.5	35.7	-5.3	16.5
Exc. energy	15.6	7.5	55.0	15.4	-37.3	-25.8	36.2

1. Changes are from final month of preceding period to final month of period indicated.
2. Relative importance weights are on a stage of processing basis.
3. Excludes materials for food manufacturing and animal feeds.

RECENT CHANGES IN CONSUMER PRICES[1]
(Percentage change at annual rates; based on seasonally adjusted data)[2]

	Relative importance Dec. 1980	1980	1980 Q3	1980 Q4	1981 Q1	1981 Feb.	1981 Mar.
All items	100.0	12.4	7.8	13.2	9.6	11.5	7.3
Food	17.3	10.2	19.7	13.1	2.1	3.6	4.4
Energy[3]	10.8	18.1	2.5	.3	49.1	61.0	24.5
All items less food and energy[3]	71.8	12.1	5.8	14.4	5.8	5.4	4.9
Homeownership	25.8	16.5	-3.5	23.1	3.1	..4	3.2
Used cars	3.0	18.3	39.0	62.3	6.5	6.5	-2.0
All items less food, energy, homeownership, and used cars[4]	46.6	9.4	9.6	6.6	8.8	9.2	9.2
Other commodities[4]	20.5	8.1	10.0	4.0	6.6	7.4	6.8
Other services[4]	26.1	10.3	9.4	8.5	10.1	9.6	9.1

1. Based on index for all urban consumers.
2. Changes are from final month of preceding period to final month of period indicated.
3. Energy items: gasoline and motor oil, fuel oil and coal, gas and electricity.
4. Reconstructed series; includes home maintenance and repair commodities and services (combined relative importance weight of 3.6), also included in homeownership costs. These series are seasonally adjusted separately.

chemicals, asphalt roofing, and synthetic fibers were still rising rapidly in the April PPI.

The decline in the CPI measure of house prices has been especially striking. These prices have declined for three consecutive months, following increases of 16 percent in 1979 and 11-1/2 percent in 1980. Because home purchase prices enter the CPI with a large weight, the fall in house prices so far this year has reduced the CPI for all items by about two percentage points at an annual rate.

The food sector is another area in which inflation rates have eased early this year, but the price outlook for the balance of the year looks less favorable. The moderation in food prices in the March CPI was more broadly based than in either January or February, as inflation slowed for a number of food items while meat prices declined for a third month in a row. In addition, there have been some developments in the agricultural sector favorable to the price outlook: sugar prices have plummeted since last October; U.S. feed grain inventories are slightly more plentiful than previously was thought; preliminary indications are that the wheat crop will be large this year; and, spring rains have replenished topsoil moisture in a number of agricultural regions. Nonetheless, livestock prices turned up in the April PPI following several months of declines, and underlying soil conditions still remain dry across large portions of the country.

Making lasting inroads against inflation will require an easing of price increases in markets other than those for food, energy, and homeownership. So far, there are relatively few signs of such weakness.

HOURLY EARNINGS INDEX[1]
(Percent change at annual rates;
based on seasonally adjusted data)[2]

	1979	1980	1981 Q1	1981 Mar.	1981 Apr.
Total private nonfarm	8.1	9.7	10.0	8.3	3.1
Manufacturing	8.7	11.0	9.2	9.1	11.1
Durable	8.7	11.7	9.3	8.7	11.0
Nondurable	8.7	9.8	9.0	9.8	11.2
Contract construction	6.8	7.4	9.0	8.0	1.9
Transportation and public utilities	9.0	9.5	9.2	6.5	6.6
Total trade	7.6	8.8	11.3	9.1	-.8
Services	7.6	9.5	10.1	8.2	-.5

1. Excludes the effect of interindustry shifts in employment and fluctuations in overtime pay in manufacturing.
2. Changes over periods longer than one quarter are measured from final quarter of preceding period to final quarter of period indicated. Quarterly changes are at compound rates; monthly changes are not compounded.

MAJOR COLLECTIVE BARGAINING SETTLEMENTS
(Percent change at annual rates)

	Average adjustment 1976	1977	1978	1979	1980	First Three Months 1981
Wage-rate settlements (1,000 or more workers)						
First year adjustments	8.4	7.8	7.6	7.4	9.5	9.0
Average over life of contracts[1]	6.4	5.8	6.4	6.0	7.1	7.7
Wage and benefit settlements (5,000 or more workers)						
First year adjustments	8.5	9.6	8.3	9.0	10.4	10.4
Average over life of contracts[1]	6.6	6.2	6.3	6.6	7.0	7.3
Effective wage-rate changes (1,000 or more workers)	8.1	8.0	8.2	9.1	9.3	1.3[2]
Current settlements	3.2	3.0	2.0	3.0	3.6	.2[2]
Prior settlements	3.2	3.2	3.7	3.0	3.1	.5[2]
Escalator provisions	1.6	1.7	2.4	3.1	2.6	.5[2]

1. Excluding cost-of-living adjustments.
2. Not at annual rates.

A reconstructed CPI series that excludes volatile items such as food, energy, homeownership, and used cars rose at about a 9-1/4 percent annual rate in both February and March--about the same as during 1980 as a whole. Consumer prices for new cars declined in March, but rebounded at the producer level in April with the ending of rebates and the announcement of further price hikes by U.S. manufacturers. In addition, producer prices for capital equipment rose rapidly through April, and prices for construction materials also increased substantially.

The continued rapid increase of prices other than food, energy, and homeownership stems in part from the persistence of labor cost pressures. Although wage rates, as measured by the often-volatile hourly earnings index for nonfarm production workers, rose at only a 3 percent annual rate in April, the 10 percent rate of increase in 1981-Q1 was slightly more than in 1980. Because of the sizable hike in social security taxes in January, the increase in hourly compensation in the first quarter--at an 11.3 percent annual rate--was even larger than the rise in wage rates in that period. Wage increases recently negotiated by major collective bargaining units (those covering 1,000 workers or more) also have shown no signs of moderation. Excluding potential wage gains under cost-of-living clauses, wage increases negotiated in settlements reached during the first quarter averaged 9.0 percent in the first year and 7.7 over the contract life, compared with 9.5 and 7.1 percent, respectively, in 1980. The recent slowing of increases in the CPI, however, eventually could trim the size of overall wage adjustments under major bargaining agreements that have escalator provisions.

LABOR PRODUCTIVITY AND COSTS
(Percent change at compound annual rates;
based on seasonally adjusted data)

	1973-Q4 to 1980-Q1[1]	1980-Q1 to 1981-Q1(p)	1980		1981
			Q3	Q4	Q1(p)
Output per hour					
Total private business	.8	.5	1.5	-1.2	3.9
Nonfarm business	.6	1.0	3.8	-.4	3.6
Manufacturing	1.7	1.4	-1.5	11.4	1.6
Compensation per hour					
Total private business	9.1	10.5	9.7	8.4	11.5
Nonfarm business	8.9	10.3	9.3	9.6	11.3
Manufacturing	9.5	12.2	12.7	10.2	10.6
Unit labor costs					
Total private business	8.2	9.9	8.1	9.7	7.4
Nonfarm business	8.3	9.3	5.3	10.1	7.5
Manufacturing	7.6	10.7	14.5	-1.1	8.8

1. 1973-Q4 and 1980-Q1 are the last two business cycle peaks.

A strong rebound in productivity tempered the increase in nonfarm unit labor costs to a 7-1/2 percent annual rate in the first quarter. Yet, since the cyclical peak in 1980-Q1, productivity growth has contributed little to slowing the trend rate of increase in unit labor costs. Nonfarm productivity has risen just 1 percent, or slightly above its post-1973 trend rate, and the cyclical recovery of productivity over the last three quarters has been relatively weak in comparison to past cycles. As a result, unit labor costs in the nonfarm business sector were 9-1/4 percent higher in 1981-Q1 than a year earlier.

SELECTED DOMESTIC FINANCIAL DATA

Indicator	Latest data: Period	Latest data: Level	Net Change from: Month ago	Net Change from: Three months ago	Net Change from: Year ago
		$ billions	Percent at annual rates		
Monetary and credit aggregates[1]					
Total reserves	Aprilp	39.9	-1.5	-1.5	6.4
Nonborrowed reserves	Aprilp	38.6	-12.0	-0.9	10.1
Money supply					
M-1A	Aprilp	365.1	0.3	-8.9	-0.4
M-1B	Aprilp	429.7	19.3	13.2	11.2
M-2	Aprilp	1728.6	10.4	11.2	11.4
M-3	Aprilp	2028.2	9.9	10.0	11.9
CB Gross Time and savings deposits	Aprilp	757.2	5.6	4.6	10.2
Total Thrift deposits (S&Ls + MSBs) + Credit Unions) Total	Aprilp	719.2	-1.8	0.1	7.0
Bank credit	Aprilp	1269.2	3.9	3.8	8.6

Indicator		Latest data: Period	Latest data: Percent or index	Net Change from: Month ago	Net Change from: Three months ago	Net Change from: Year ago
Market yields and stock prices						
Federal funds	wk. endg.	5/6/81	18.91	3.48	2.40	5.95
Treasury bill (90 day)	" "	5/6/81	15.73	2.36	.41	6.06
Commercial paper (90-119 day)	" "	5/6/81	16.84	2.91	.95	5.77
New utility issue Aaa	" "	5/8/81	15.97	--	--	4.59
Municipal bonds (Bond Buyer) 1 day	1 day	5/7/81	10.90	.69	1.00	2.94
FNMA auction yield (FHA/VA)		5/11/81	17.21	.74	1.62	4.05
Dividend price ratio (common stocks)	wk. endg.	5/6/81	5.02	.16	.02	-.80
NYSE index (12/31/65=50)	end of day	5/4/81	75.52	-1.77	1.21	15.02

Indicator	Period	Net Change or Gross Offerings: Latest data	Year ago	Year to date: 1981	Year to date: 1980
Credit demands					
Business loans at commercial banks[1]	April	0.6	-0.8	7.6	12.0
Consumer instalment credit outstanding[1]	March	3.1	0.7	6.0	5.8
Mortgage debt outstanding (major holders)[1 2]	February	5.5	7.1	11.0	14.5
Corporate bonds (public offerings)	April	4.3e	3.8	13.2e	9.7
Municipal long-term bonds (gross offerings)	April	4.5e	4.9	13.5	12.8
Federally sponsored agcy. (net borrowing)	April	2.8e	3.6	5.7e	12.2
U.S. Treasury (net cash borrowing)	April	-3.6e	4.6	32.2e	23.7

1/ Seasonally adjusted.
2/ Includes comm'l banks, S&Ls, MSBs, life ins. cos, FNMA and GNMA.
e - Estimated.
p - Preliminary.

The narrow monetary aggregates, adjusted to remove the effects of shifts into NOW accounts, surged in April. The April strength likely reflected some realignment of cash balances with trends in income and spending following a period of sluggish behavior; changes in patterns of tax payments and refunds appear to have had little net effect on money growth. Owing to the burst in M-1B growth, M-2 expansion remained quite rapid in April even though growth of its nontransaction component weakened considerably.

Open market operations did not accommodate the strong growth of money through the provision of nonborrowed reserves, and borrowing at the discount window increased substantially over the course of April. Pressures on the federal funds rate and other money market rates intensified in early May when the System increased both the basic discount rate and the surcharge. Most short-term market rates have risen 3 to 5 percentage points since the last FOMC meeting. Long-term bond rates generally have reached new highs and on balance have advanced about one percentage point over the intermeeting period. Rates on home mortgages in the primary market have continued rising at a more gradual pace.

Despite higher bond rates and some decline in equity prices in the latter part of the month, corporate bond and stock offerings remained strong in April, while short-term business borrowing weakened. With the federal budget shifting from a large deficit to a surplus, the Treasury's demands on credit markets moderated last month. State and local governments, however, continued to borrow heavily. Residential mortgage flows slackened in March--and may well have diminished further in April. In

SELECTED FINANCIAL MARKET QUOTATIONS[1]
(Percent)

	1980		1981		Change from:	
	Mid June* Low	Dec. High	FOMC Mar. 31	May 12	Dec. High	FOMC Feb. 3
Short-term rates						
Federal funds[2]	8.99	19.83	14.93	18.20p	-1.63	3.27
Treasury bills						
3-month	6.18	17.14	12.46	16.94	-.20	4.48
6-month	6.60	15.74	12.03	15.83	.09	3.80
1-year	7.00	14.06	11.73	14.85	.79	3.12
Commercial paper						
1-month	7.98	20.77	13.74	18.34	-2.43	4.60
3-month	7.78	19.88	13.21	18.07	-1.81	4.86
6-month	7.59	18.58	12.88	17.38	-1.20	4.50
Large negotiable CDs[3]						
1-month	7.96	21.29	13.72	18.64	-2.65	4.92
3-month	7.90	20.90	13.54	18.80	-2.10	5.26
6-month	7.66	19.19	13.52	18.25	-.94	4.73
Eurodollar deposit[2]						
1-month	8.88	22.54	14.56	19.93p	-2.61	5.37
3-month	8.99	21.36	14.78	19.57p	-1.79	4.79
Bank prime rate	12.00	21.50	17.50	19.50	-2.00	2.00
Intermediate- and long-term rates						
U.S. Treasury (constant maturity)						
3-year	8.56	14.41	13.27	15.48	1.07	2.21
10-year	9.47	13.57	13.13	14.46	.89	1.33
30-year	9.49	13.17	12.65	13.95	.78	1.30
Municipal (Bond Buyer)	7.44	10.56	10.09[4]	10.90[4]	.34	.81
Corporate Aaa						
New issue	10.53	14.51	15.07[5]	15.97p[5]	1.46	.90
Recently offered	10.79	15.03	14.71[6]	15.69p[6]	.66	.98
Primary conventional mortgages	12.35	14.95	15.40[6]	16.12[6]	1.17	.72

	1980	1981	1981		Percent change from:	
	Mid-Oct. High	Mar.-Apr. Low	FOMC Mar. 31	May.12	Mar.-Apr. Low	FOMC Mar.31
Stock Prices						
Dow-Jones Industrial	972.44	759.13	1,003.87	970.82	28	-3
NYSE Composite	77.24	55.30	78.27	75.60	37	-3
AMEX Composite	363.33	215.69	360.60	358.25	66	-1
NASDAQ (OTC)	199.43	124.09	210.18	213.12	72	1

1. One-day quotes except as noted.
2. Averages for statement week closest to date shown.
3. Secondary market.
4. One-day quotes for preceding Thursday.
5. One-day quotes for preceding Friday.
6. One-day quotes for preceding Friday.
* Most lows occurred on or around June 13.

contrast, consumer installment credit expanded in March at its strongest pace since September 1979, reflecting in part the rebate-related boost in car sales.

Monetary Aggregates and Bank Credit

Adjusted for shifts into NOW accounts, M-1B expanded at an estimated 14-1/4 percent annual rate in April, about double the pace of March.[1] All components of M-1B strengthened in April. "Other checkable deposits" rose $6-3/4 billion, after a $5-1/4 billion increase in March. Even so, the contraction in demand deposits moderated considerably in April, and growth of currency picked up to a 10-1/4 percent annual rate, well above the first-quarter pace. Changes in the payment and processing of federal income taxes appear to have had little effect on monetary expansion during April. The Treasury's efficiency in processing tax payments reportedly has improved, tending to speed debits to checking accounts and thus to lower M-1B. This effect, however, seems to have been offset by increases in tax refunds and in nonwithheld tax payments, which tended to raise M-1B.

Expansion in M-2 was restrained in April by a slowing in the growth of the nontransaction component of this aggregate--to a 9-1/2 percent annual rate, well below the March pace. Inflows to money market mutual funds (MMMFs) tapered off, total savings and small time deposits were flat, and overnight RPs declined.[2]

1. These figures are based on revised seasonal adjustment factors and a new procedure that seasonally adjusts the other checkable deposits component. Although the change in seasonal adjustment procedures raises M-1B growth in the first quarter about 1-1/4 percentage points--to 1 percent at an annual rate--first-quarter M-1B growth was still considerably lower than would have been expected on the basis of historical relationships among money, GNP, and interest rates.

2. The drop in overnight RPs resulted in part from a conversion of overnight RPs to term contracts around the Easter weekend, when many firms took either Friday or Monday as a holiday.

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

	1980 Q3	1980 Q4	1981 Q1	1981 Feb.	1981 Mar.	1981 Apr.[e]	Apr. '80 to Apr. '81[e]
	---- Percentage change at annual rates ----						
Money stock measures							
1. M-1A	11.5	8.0	-18.6	-21.5	-5.2	0.3	-0.4
2. (Adjusted)[2]	n.a.	n.a.	(0.3)	(0.9)	(7.2)	(14.5)	n.a.
3. M-1B	13.9	10.9	6.6	8.7	11.2	19.3	11.2
4. (Adjusted)[2]	n.a.	n.a.	(1.1)	(1.5)	(7.3)	(14.2)	n.a.
5. M-2	15.7	8.1	8.4	9.8	15.1	12.0	11.8
6. M-3	13.1	10.3	12.0	10.8	9.2	10.0	12.0
Selected components							
7. Currency	10.9	8.5	5.9	7.2	6.1	10.2	9.0
8. Demand deposits	11.8	8.0	-29.2	-34.6	-10.6	-4.4	-4.4
9. Other checkable deposits	58.0	57.6	380.2	272.0	123.4	140.2	224.6
10. M-2 minus M-1B (11+12+13+16)	16.4	7.2	9.0	10.1	16.5	9.6	12.0
11. Overnight RPs and Eurodollars, NSA[3]	135.6	15.4	0.0	-36.8	45.4	-43.8	43.4
12. Money market mutual fund shares, NSA	75.7	-15.5	84.5	174.0	171.4	130.7	93.9
13. Commercial banks	10.8	9.8	5.6	0.7	6.7	2.0	8.0
14. savings deposits	22.9	1.7	-31.2	-23.0	-9.7	-1.4	-2.9
15. small time deposits	2.9	15.4	30.0	14.2	16.0	4.2	15.3
16. Thrift institutions	9.7	7.8	3.2	-0.4	0.7	-1.4	5.9
17. savings deposits	22.8	-2.4	-30.9	-22.8	-9.8	-5.5	-5.2
18. small time deposits	3.6	12.8	19.1	9.1	5.0	0.2	11.1
19. Large time deposits	-9.5	21.8	36.2	22.8	-17.8	-3.7	12.0
20 at commercial banks, net[4]	-14.3	17.6	36.5	21.9	-20.9	-3.4	8.5
21. at thrift institutions	19.1	42.9	32.9	30.0	0.0	-5.3	28.7
22. Term RPs, NSA	47.8	41.5	14.4	-27.8	-66.5	13.4	24.4
	—Average monthly change in billions of dollars—						
MEMORANDA:							
23. Managed liabilities at commercial banks (24+25)	-0.3	7.7	2.9	2.9	-6.8	-1.7	2.1
24. Large time deposits, gross	0.3	5.6	4.4	4.5	-2.3	2.7	2.9
25. Nondeposit funds	-0.6	2.1	-0.2	-1.6	-4.5	-4.4	-0.8
26. Net due to related foreign institutions, NSA	-1.9	-0.2	-1.5	0.0	-4.6	-4.2	-2.3
27. Other[5]	1.3	2.4	1.3	-1.6	0.1	-0.1	1.4
28. U.S. government deposits at commercial banks[6]	0.8	-1.0	1.1	1.2	3.5	0.6	-0.3

1. Quarterly growth rates are computed on a quarterly average basis.
2. Figures in parentheses have been adjusted to remove the distorting effects since the beginning of 1981 of shifts of funds out of demand deposits and other accounts into NOW accounts. Based on a variety of evidence, it is estimated that 77-1/2 percent of inflows into other checkable deposits—in excess of "trend"—was from demand deposits in January, and 72-1/2 percent in February, March and April.
3. Overnight and continuing contract RPs issued to the nonbank public by commercial banks, net of amounts held by money market mutual funds, plus overnight Eurodollar deposits issued by Caribbean branches of U.S. member banks to U.S. nonbank customers.
4. Net of large-denomination time deposits held by money market mutual funds and thrift institutions.
5. Consists of borrowings from other than commercial banks in the form of federal funds purchased, securities sold under agreements to repurchase and other liabilities for borrowed money (including borrowings from the Federal Reserve), loans sold to affiliates, loan RPs, and other minor items. Changes since October 1980 are partially estimated.
6. Consists of Treasury demand deposits at commercial banks and Treasury note balances.
n.a.—not available. e—estimated.

The slowdown in growth of MMMF shares reflected a moderation in the second half of April in growth of assets at broker-dealer and general purpose funds, and a contraction in the assets of institution-only funds catering to large investors, many of whom have direct access to money markets and readily shift funds to and from MMMFs as relative returns change. Yields on the MMMFs have lagged the upward movement in market rates, despite the generally short average maturities of MMMF portfolios.

While outflows from savings deposits moderated in April, growth of small time deposits decelerated to the slowest pace since last August. Depository institutions, especially S&Ls, have experienced weak MMC flows during a period when a record volume of money market certificates was maturing and when the spread between rates on MMMF shares and those on MMCs favored MMMFs until very recently.

MMC DEPOSITS AT THRIFT INSTITUTIONS AND SELECTED INTEREST RATES

		Net change in MMCs (NSA)		Maturing MMCs		Effective Rate on	MMMF
		S&Ls	MSBs	S&Ls	MSBs	MMCs	yield
		($billions)				(percent)	
1981	Jan.	7.0	.4	31.0	8.5	14.81	17.08
	Feb.	5.0	1.7	21.8	4.3	15.20	16.36
	Mar.	- .1	.5	35.6	7.4	13.98	15.08
	Apr.	0.3	n.a.	43.0	12.0	14.33	14.19

Growth in M-3 edged up in April to a 10 percent annual rate, as the slowdown in M-2 was more than offset by sharply reduced runoffs of large time deposits at commercial banks and an uptick in term RPs. Large time deposits outstanding at S&Ls are estimated to have remained unchanged on

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

		1980			1981				Apr. 80 to
		Q2	Q3	Q4	Q1	Feb.	Mar.	Apr.[e]	Apr. 81[e]
					Commercial Bank Credit				
1.	Total loans and investments at banks[2]	-4.1	12.9	14.6	7.8	8.1	-0.6	3.9	8.6
2.	Investments	12.0	20.5	11.9	10.5	9.8	2.2	-1.8	14.5
3.	Treasury securities	13.1	39.1	11.1	15.2	18.0	-4.2	6.3	23.1
4.	Other securities	11.4	11.5	12.3	8.0	5.6	5.5	-6.0	10.3
5.	Total loans[2]	-9.4	10.2	15.6	6.7	7.4	-1.5	6.1	6.6
6.	Business loans[2]	-9.3	15.2	21.2	8.1	4.7	2.5	2.2	9.5
7.	Security loans	-17.1	-10.2	60.1	25.0	-32.1	33.0	64.2	22.4
8.	Real estate loans	1.9	4.5	11.0	9.4	12.4	9.1	7.6	7.0
9.	Consumer loans	-16.9	-7.6	-0.2	-1.4	-4.1	2.1	n.a.	n.a.
					Short- and Intermediate-Term Business Credit				
10.	Total short- and intermediate-term business credit (sum of lines 14, 15 and 16)	2.5	9.0	14.4	15.4	15.6	14.2	n.a.	n.a.
11.	Business loans net of bankers acceptances	-10.7	14.3	24.1	7.6	4.5	3.3	-0.7	9.2
12.	Commercial paper issued by nonfinancial firms[3]	62.6	-19.3	-3.0	30.7	23.8	29.2	-14.3	14.6
13.	Sum of lines 11 & 12	-2.9	10.1	21.0	10.5	7.3	6.2	-2.3	9.8
14.	Line 13 plus loans at foreign branches[4]	-0.6	9.6	19.4	13.7	11.4	10.3	-1.0	10.8
15.	Finance company loans to business[5]	-2.3	-4.6	14.6	8.5	6.6	-3.3	n.a.	n.a.
16.	Total bankers acceptances outstanding[5]	31.5	21.0	-15.7	35.6	56.2	62.3	n.a.	n.a.

1. Average of Wednesdays for domestic chartered banks and average of current and preceding ends of months for foreign-related institutions.
2. Loans include outstanding amounts of loans reported as sold outright to a bank's own foreign branches, unconsolidated nonbank affiliates of the bank, the bank's holding company (if not a bank), and unconsolidated nonbank subsidiaries of the holding company.
3. Average of Wednesdays.
4. Loans at foreign branches are loans made to U.S. firms by foreign branches of domestic-chartered banks.
5. Based on average of current and preceding ends of months.
n.a.--not available. e--estimate.

a month-average basis in April--as in March--with S&Ls apparently reluctant to issue such deposits in an environment of slack mortgage demand, rising interest rates, and investor concern about the financial strength of the institutions.

Total bank credit grew at a 4 percent annual rate in April after registering a slight decline in March. Investments were little changed as an increase in U.S. government securities was about offset by a decline in other investments. Business loans rose slightly, owing entirely to a large increase in holdings of bankers acceptances. Growth in real estate lending decelerated somewhat further in the month to a 7-1/2 percent annual rate. Consumer loans at large weekly reporting banks declined on a seasonally adjusted basis in April.

Banks acquired funds well in excess of their domestic needs in April. As shown in the table below, commercial banks advanced about $4 billion, net, to their foreign branches, partly in response to yield relationships that continued to favor overseas investment of funds raised in the United States.

COMMERCIAL BANK SOURCES AND USES OF FUNDS
April 1981
(Billions of dollars, seasonally adjusted)

Uses of Funds	
Net funds advanced to foreign branches	4.2
Loans and investments	4.1
Total uses	8.3
Sources of Funds	
Transaction deposits	7.1
Savings and small time deposits	.9
Large time deposits	2.7
Total deposits	10.7
Nondeposit sources (excluding borrowing from branches)	- .1
Other balance sheet items and discrepancy	- 2.3
Total sources	8.3

GROSS OFFERINGS OF CORPORATE SECURITIES
(Monthly totals or monthly averages; in millions of dollars)

	1980		1981		
	Year	Q4	Q1 p	Mar. p	Apr. p
	-------- Seasonally adjusted ----				
Corporate securities--total	6,074	4,946	5,858	5,700	7,000
Publicly offered bonds	3,462	2,209	3,388	3,300	3,500
Privately placed bonds	915	616	577	600	600
Stocks	1,697	2,121	1,893	1,800	2,900
	----- Not seasonally adjusted ----				
Publicly offered bonds--total	3,462	1,960	2,979	3,600	4,250
By quality[1]					
Aaa and Aa	1,666	702	904	1,390	1,240
Less than Aa[2]	1,796	1,258	2,075	2,210	3,010
By type of borrower					
Utility[3]	1,304	949	1,150	1,550	1,570
Industrial	1,323	456	1,285	1,100	1,740
Financial	835	555	544	950	940
Memo Items:					
Convertible bonds	390	433	434	425	305
Deep discount bonds[4]	--	--	167	500	1,750
Stocks--total	1,697	2,358	1,774	1,800	1,800
By type of issuer					
Utility	606	619	524	500	850
Industrial	833	1,281	1,036	1,100	850
Financial	258	458	214	200	100

p--Preliminary.
1. Bonds categorized according to Moody's bond ratings.
2. Includes issues not rated by Moody's.
3. Includes equipment trust certificates.
4. Amounts shown are par values. In March and April gross proceeds from deep discount bonds were approximately $250 million and $780 million, respectively.

Business Finance

Partial data suggest that total funds raised in domestic markets by nonfinancial firms declined in April after falling off over the first quarter. An apparent further diminution in short-term borrowing was only partially offset by increased long-term financing, which reflected both a seasonally adjusted pickup in already brisk equity sales and continued strong issuance of notes and bonds.

Changing interest rate relationships likely accounted for the marked shifts in the composition of short-term borrowing by businesses in April. Bank lending to businesses was concentrated at large weekly reporters, whose business loans--excluding holdings of bankers acceptances--grew at a 10 percent annual rate after declining substantially in February and March. A narrowing of the spread between the prime rate and commercial paper rates--and the day to day volatility of paper rates--encouraged firms to tap their bank lines. Outstanding nonfinancial paper declined about $500 million in April.

The gain in business loans at large banks may also have reflected in part a drop in loans at U.S. branches and agencies of foreign banks, whose loan terms reportedly are more responsive than those of domestic banks to market rates. In addition, a runup in Eurodollar rates relative to the prime probably contributed to the slowing in the shifting of business loans to foreign branches of U.S. banks. Monthly increases in offshore branch loans to U.S. nonbank residents--typically priced off LIBOR--moderated from $1.2 billion on average in February and March to $500 million in April.[1]

1. The appendix discusses the pricing and booking of business loans.

Although long-term yields climbed to record levels, the volume of publicly-offered corporate bonds in April, at $3.5 billion (seasonally adjusted), was a bit above the strong pace in the first quarter, and considerably above the volume in December, when yields reached their previous highs. Some firms with continuing heavy needs for long-term capital have decided to come to market at regular intervals in order to avoid concentrated borrowing at unfavorable rates in a volatile rate environment. However, the postponement of about $2-1/2 billion of offerings originally announced for April suggests that many issuers are deferring bond issuance in the hope that long-term rates will drop; indeed, new issue volume appears to have weakened early in May following the most recent jump in interest rates.

Efforts to hold down borrowing costs are evident in the offering terms of many new issues. For example, the volume of convertible debentures has expanded considerably over the past year, and the average maturity of straight-debt offerings by nonfinancial businesses has decreased substantially. More recently, investment-grade firms have marketed a number of deep discount bonds, whose coupon rates were significantly below market yields. In March and April ten deep discount bonds were sold; these issues had par values totaling $2.3 billion, but gross proceeds were only about half that amount. Given the tax advantage to the issuer and the premium that investors are willing to pay for these bonds, the deep discount bonds offered so far appear to have reduced borrowing costs by roughly 1-1/2 percentage points.

Stock prices have been mixed over the intermeeting period. In mid-April, many indexes established 8-year highs, from which they retreated sharply in response to the runup in interest rates. With prices generally high, the volume of new equity offerings was strong in April, rising to $2.9 billion (seasonally adjusted). So far in 1981, gross stock issuance has averaged more than $2 billion per month, exceeding last year's record pace; initial public offerings are up significantly along with offerings by seasoned issuers.

Government Finance

The Board staff projects a combined unified budget and off-budget agency surplus of about $11-1/2 billion this quarter; however, facing substantial cash needs later this year, the Treasury likely will reduce its marketable debt by only $3 billion. The bulk of an $18 billion bill redemption is expected to be offset by sales of new coupon securities.

As a part of this program, the Treasury ran off $9-1/2 billion in bills in April and raised $6 billion in coupon issues. In early May, the Treasury raised $2.1 billion in its mid-quarter refunding, which was a typical 3-part package including $3 billion of 2-year notes, $1-3/4 billion of 10-year notes, and $2 billion of 30-year bonds; these securities were auctioned at record yields that attracted a large volume of noncompetitive tenders.

The large run-off of bills in April was accompanied by significant moderation in demand for Treasury bills by foreign central banks and by sharp reductions in dealer holdings of bills from about $14 billion at the end of March to about $3 billion one month later. This huge reduction in dealer inventories, which extended to Treasury coupons and agency and private short-term issues, appears for several reasons to reflect a

FEDERAL GOVERNMENT AND SPONSORED AGENCY FINANCING[1]
(Billions of dollars)

	1980	1981				
	Q4	Q1	Q2[f]	March	April[e]	May[f]
Treasury financing						
Combined surplus/deficit(-)	-35.8	-38.5	11.4	-13.0	14.7	-14.9
Net marketable borrowings/ repayments(-)	29.0	37.9	-3.1	15.4	-3.3	0.4
bills	15.8	19.1	-17.1	6.3	-9.5	-1.7
coupons	13.2	18.8	14.0	9.1	6.2	2.1
Nonmarketable borrowings/ repayments(-)	-1.3	-2.1	-2.4	-0.3	-0.3	-1.5
Other means of finance[2]	-0.6	1.1	-1.6	-1.5	-0.6	1.5
Change in cash balance	-8.7	-1.6	4.3	0.6	10.5	-14.5
Federally sponsored credit agencies net cash borrowing[3]	8.9	3.5	7.5	2.1	[illegible]	2.8

f--forecast. e--estimated.
1. Numbers reported on a not seasonally adjusted, payments basis.
2. Includes checks issued less checks paid, accrued items and other transactions.
3. Includes debt of Federal Home Loan Banks, the Federal Home Loan Mortgage Corporation, Federal National Mortgage Association, and the Federal Farm Credit Bank System.

reassessment of expectations of declines in short-term interest rates. For one, it occurred even though dealer financing rates increased in April only moderately more than bill rates. Moreover, the reduction in dealer holdings outpaced sizable declines in short positions in futures contracts, thereby virtually eliminating the large net long positions that dealers had built up over the first quarter.

Borrowing by federally sponsored credit agencies is estimated at $2.7 billion in April, with the Federal Farm Credit Banks raising $1.7 billion. The Federal Home Loan Banks borrowed $1.5 billion, about triple the March volume, and used the proceeds, along with a reduction in System liquidity, to finance $2.2 billion of advances to thrifts. The Federal National Mortgage Association ran off an additional $500 million of debt in April, reflecting continued weakness in its net mortgage purchases.

Despite record high yields, state and local governments boosted their gross issuance of long-term debt in April to a seasonally adjusted $4-3/4 billion from the $3-1/4 billion monthly average of the first quarter. The April increase is partly attributable to the limited ability of municipal utilities to delay offerings, given the usual rigidity of their large annual funding requirements and construction payment schedules; utility bonds accounted for an above-normal proportion of total issues in April. Pressing cash needs also appear to have accounted for a portion of the large volume of nonutility issues, which included $500 million of previously postponed offerings.

Although municipal volume in April may also indicate that many issuers did not expect yields to decline soon, some issuers apparently awaited a decline. During April, 18 issuers postponed more than $750

NET CHANGE IN MORTGAGE DEBT OUTSTANDING
(Seasonally adjusted annual rates, in billions of dollars)

Mortgage debt	1980 Q1	Q2	Q3	Q4	1981 Q1[e]
By type of debt					
Total	152	74	123	153	123
Residential	102	42	99	115	87
Other[1]	50	32	24	38	36
By type of holder					
Commercial banks	32	5	12	29	20
Savings and loans	26	4	39	45	30
Mutual savings banks	2	5	- 1	1	1
Life insurance companies	16	13	11	10	10
FNMA and GNMA	12	8	*	9	4
GNMA mortgage pools	18	17	19	16	14
FHLMC and FHLMC pools	3	3	5	1	2
Other[2]	43	28	38	40	42

1. Includes commercial and other nonresidential as well as farm properties.
2. Includes mortgage companies, real estate investment trusts, state and local government credit agencies, state and local government retirement funds, noninsured pension funds, credit unions, Farmers Home Administration and Farmers Home pools, Federal Land Banks, Federal Housing Administration, Veterans Administration, and individuals.
e--Partially estimated.
*--Between $0.5 billion and $-0.5 billion.

million in bond sales--double the monthly average for the first quarter. Only four of the postponements in April were mandated by statutory interest rate ceilings. Early in May, postponements totalled $600 million.

STATE AND LOCAL GOVERNMENT SECURITY OFFERINGS
(Monthly averages, billions of dollars)

	1980	1981		
	Q4	Q1[e]	March[e]	April[e]
	------- Seasonally adjusted ------			
Total	6.05	5.45	5.00	5.50
Long-term	3.60	3.25	3.10	4.70
Short-term	2.45	2.20	1.90	.80
	----- Not seasonally adjusted ----			
Total	5.33	4.90	5.20	6.50
Long-term	3.57	3.00	3.60	4.50
Housing bonds	1.08	.20	.25	.45
Short-term	1.76	1.90	1.60	2.00

e--estimate.

Mortgage Markets

Preliminary estimates indicate a sharp first quarter drop in net mortgage lending, especially residential mortgages. This slowing was most evident at depository institutions. Field reports suggest that mortgage originations picked up less than seasonally in April. Signs of continued slack include a further cutback in issuance of GNMA-guaranteed securities and reports of additional closings of offices by mortgage companies.

In March, net mortgage acquisitions at S&Ls dropped to less than half their autumn high, and new commitments remained at their low February level. This curtailment of mortgage activity may in part reflect an

PRIMARY MARKET FOR CONVENTIONAL HOME MORTGAGES

Period	Fixed-rate level-payment loans at S&Ls: Average rate for 80 percent loans (percent)	Change from month or week earlier (basis points)	Spread over corporates[1] (basis points)	RRMs at major lenders[2]: Average rate for loans of 80 percent or less (percent)
1980--High	16.35	--	385	n.a.
Low	12.18	--	-20	n.a.
1981--High	16.12	--	142	15.38
Low	14.80	--	-46	14.63
Mar.	15.40	27	69	14.70
Apr.	15.58	18	18	14.97
Mar. 27	15.40	0	69	14.63
Apr. 3	15.40	0	51	14.71
10	15.50	10	31	14.97
17	15.65	15	29	15.08
24	15.77	12	-1	15.13
May 1	15.82	5	44	15.38
8	16.12	30	43p	15.51

1. Average mortgage rate on new commitments minus average yield on recently offered Aaa utility bonds.
2. New commitments for renegotiable rate mortgages made pursuant to FHLBB regulations issued prior to April 1981 (from FNMA field reports).

SECONDARY MARKET FOR HOME MORTGAGES

Period	FNMA auctions of forward purchase commitments[1]: Conventional: Amount ($ millions) Offered	Conventional: Amount ($ millions) Accepted	Conventional: Yield to FNMA (percent)	FHA/VA: Amount ($ millions) Offered	FHA/VA: Amount ($ millions) Accepted	FHA/VA: Yield to FNMA (percent)	Yield on GNMA securities for immediate delivery[2] (percent)
1980--High	426	133	17.51	644	324	15.93	14.41
Low	29	20	12.76	97	52	12.28	10.79
1981--High	115	72	16.42	147	100	17.21	15.46
Low	12	11	14.83	58	35	14.84	13.18
Mar. 30	45	35	15.42	46	35	15.74	1 .18
Apr. 6	--	--	--	--	--	--	14.69
13	50	38	15.57	75	61	16.47	14.64
20	--	--	--	--	--	--	14.61
27	77	54	15.75	64	53	16.61	14.81
May 4	--	--	--	--	--	--	15.46
11	115	72	16.42	110	100	17.21	15.37

1. Auction yields on fixed-rate level-payment loans are gross, before deduction of 38 basis points for mortgage servicing.
2. Average net yields to investors assuming prepayment in 12 years on pools of 30-year FHA/VA level-payment mortgages typically carrying the prevailing ceiling rate on such loans.

effort by S&Ls to shorten the average maturity of their assets as a hedge against increases in the cost of their short-term liabilities. With deposit costs rising much more than average portfolio returns at S&Ls and MSBs in the first quarter, these institutions suffered unprecedented losses. S&L mergers are running well above last year's rate, but the increase appears to derive largely from the desire of S&Ls to improve their long-run competitive position and from passage of a Pennsylvania state law requiring federal insurance of all institutions, rather than from current earnings or capital problems.

NET INCOME AT S&Ls AND MSBs
(Percent of average assets)

		FSLIC Insured S&Ls	All Operating MSBs
1978	H1	.81	.64
	H2	.83	.58
1979	H1	.69	.54
	H2	.64	.38
1980	H1	.17	-.04
	H2	.10	-.20
1981	Q1[e]	(-.35 to -.45)	(-.48 to -.58)

e--estimate.
Source: FHLBB and NAMSB.

In the primary market, mortgage rates advanced further during April and early May. At a sample of S&Ls, the average contract interest rate on new commitments for fixed-rate, level-payment conventional home loans has increased 72 basis points since the last FOMC meeting, reaching 16.12 percent--near the 16.35 percent record weekly high in 1980. Yields have also risen on renegotiable-rate loans, with most lenders continuing to offer initial concessions of up to about 75 basis points as an inducement to borrowers to assume the interest rate risk. Uncertainty still surrounds the pricing of the adjustable-rate mortgages just authorized by the FHLBB (effective April 30) and by the Comptroller of the Currency earlier this year.[1]

Surveys suggest a spreading use of financing techniques designed to minimize borrower dependence on traditional financing at prevailing market rates. Fifty-five percent of members responding to a survey by the National Association of Home Builders indicated that in March they were offering "buy downs" on new homes--typically featuring a reduction of 2 to 3 percentage points in the interest rate payable by the buyer during the first three years of the mortgage. In a survey of members conducted by the National Association of Realtors during the latter part of April, about half of all respondents indicated that during the preceding six months, at least half of their existing home transactions involved creative financing--particularly assumptions of first mortgages, often combined with seller takebacks of second mortgages.

With yields on corporate bonds surging to new highs in early May, secondary market yields on home mortgages remained under upward pressure, especially those on FHA/VA loans, which are often pooled to back GNMA issues. As deepening discounts on 14 percent FHA/VA mortgages discouraged

1. The FHLBB regulations give federal S&Ls wide latitude with respect to the index used to adjust mortgage rates, the frequency and size of rate adjustments, and the division of rate adjustments between monthly payments and additions to principal. One large federal S&L in California has announced that its new adjustable-rate loans will be priced at market rates, with semiannual rate adjustments based on the industry's cost of funds, and a limit of 7-1/2 percent per year on changes in the monthly payment schedule. The flexibility of FHLBB's regulations reportedly has been a consideration in the decision of several large West Coast S&Ls to apply for federal charters.

originations of such loans, the ceiling rate on fixed-rate level payment loans was adjusted up to a record 14-1/2 percent, effective April 13, and then to 15-1/2 percent, effective May 8.

Consumer Credit

Consumer installment credit outstanding grew at a 12 percent annual rate in March, the sharpest increase since September 1979. The speedup resulted largely from a boost in growth of auto credit, associated with the rebate-induced strength in new-car sales in late February and in the first three weeks of March.

After negligible additions to consumer installment debt last year and recent strong growth in personal income, the debt position of households had improved considerably by March. The ratio of consumer installment debt repayments to disposable personal income was down to 16.4 percent in the first quarter, compared with the record 17.7 percent reading in mid-1979. Personal bankruptcies fell in the first quarter after surging last year, when recession and reaction to an earlier liberalization of federal bankruptcy law stimulated a record number of filings. Auto loan delinquency rates at auto finance companies fell substantially in the first quarter.

CONSUMER INSTALLMENT CREDIT[1]

	1979	1980	1980 Q4	1981 Q1	1981 Feb.	1981 Mar.
Total						
Change in outstandings						
Billions of dollars	38.4	1.4	12.6	23.9	24.0	37.3
Percent	14.0	0.5	4.2	7.8	7.7	11.9
Extensions						
Billions of dollars	324.8	305.9	322.0	342.4	344.5	357.9
Bank share (percent)	47.6	43.7	43.3	40.6	40.6	42.5
Liquidations						
Billions of dollars	286.4	304.5	309.4	318.5	320.5	320.6
Ratio to disposable income (percent)	17.5	16.7	16.3	16.4	16.5	16.4
Automobile credit						
Change in outstandings						
Billions of dollars	14.7	0.0	3.0	10.4	11.8	20.2
Percent	14.5	0.0	2.6	8.9	10.1	17.1
Extensions						
Billions of dollars	93.9	83.0	87.6	97.1	100.0	104.4
Revolving credit						
Change in outstandings						
Billions of dollars	8.6	2.9	4.6	6.3	5.3	7.0
Percent	19.9	5.5	8.4	11.3	9.4	12.3
Extensions						
Billions of dollars	120.2	129.6	134.8	141.7	142.4	144.9

1. Quarterly and monthly dollar figures and related percent changes are at seasonally adjusted annual rates.

APPENDIX*

LIBOR-PRICED LOANS AND MEASURES OF BUSINESS CREDIT

Since the beginning of the year, loans to U.S. nonbank residents at foreign branches of domestically chartered banks have grown rapidly, reaching $7.5 billion in April. To aid in identifying the causes of recent growth in these loans, an informal telephone survey was conducted of five money center banks, four of which have been identified as being heavily engaged in booking loans to U.S. nonbank residents at their foreign branches (loans at foreign branches). This information has been supplemented by a number of press accounts dealing with growth in these loans.

According to the bankers contacted, the rapid spread of alternatives to prime-based pricing of business loans underlies recent increases in loans at foreign branches. Corporate customers--originally multi-nationals but now even mid-sized companies--increasingly insist upon the inclusion of alternatives to prime-based pricing in loan agreements, the typical alternative being an interest rate based on the London Interbank Offer Rate (LIBOR). Bankers stated that they are responding to competitive pressures in satisfying customer demands for a LIBOR option.

A LIBOR pricing alternative is most likely to be included in a commitment agreement for a term loan or a revolving credit facility with a maturity in the one- to seven-year range. In such an agreement the borrower is offered the option of an interest rate based on the bank's prime rate or one based on LIBOR quotations made by one of the bank's foreign branches. Under prime-based pricing, the loan rate floats with the prime rate while, under the LIBOR option, the loan agreement typically specifies a period over which the interest rate is fixed. This period, usually selected by the borrower, most often is 3 months--in which case the loan is priced off the 3-month LIBOR--but pricing periods vary from 1 to 9 months. Typically, the borrower is permitted to switch from prime-based pricing to LIBOR-based pricing at any time, but a switch from LIBOR- to prime-based pricing is permitted only at the completion of a pricing period.[1]

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1. Bankers were asked about the relationship between LIBOR pricing options and so-called below-prime lending by U.S. banks. They stressed that the two types of loans are very different in nature. Below-prime loans typically have very short maturities--frequently overnight but almost always less than 60 days--in contrast to the one- to seven-year maturity of loans with LIBOR pricing options. Further, below-prime loans have fixed interest rates while interest rates on LIBOR-priced loans are adjusted periodically and therefore "float." Finally, below-prime loans are priced off domestic money market rates such as the federal funds rate, rather than being linked to LIBOR.

Policies regarding the booking location of loans with pricing options are not uniform among banks. Loans to U.S. corporations in which the prime-based pricing option has been chosen virtually always are booked at the head office. When the LIBOR-based option is chosen, many banks book the loan at an offshore branch. For these banks, the booking location is switched every time the customer exercises his option to change the pricing of the loan. Other banks--including one contacted--apparently book all such loans domestically on the grounds that the loans, made to U.S. firms, are domestic in origin and should not be shifted offshore simply because a pricing option has been exercised.

Those banks that book LIBOR-priced loans offshore view the loans as being international in terms of pricing and funding, and properly booked offshore. They pointed out that if a LIBOR-priced loan is not funded in the Euromarket the bank is exposed to interest rate risks associated with fluctuations in the spread between Euromarket and domestic rates. Of course, booking and funding are separable decisions. For example, a LIBOR-priced loan could be booked domestically and effectively funded in the Euromarket by the head office's borrowing from its foreign branch funds raised in the Euromarket. Indeed, the banks even acknowledged that a LIBOR-priced loan may be funded domestically.

A more satisfying explanation for offshore booking is provided by tax considerations. Tax practices in New York State provide strong incentives to book loans at offshore branches. If a loan is booked offshore rather than at the head office, a considerable portion of the income on the loan is not subject to state taxation.[1] To a lesser extent, tax practices in California and Illinois also provide incentives for banks to book loans offshore.

The availability of a LIBOR-pricing option should reduce the average cost to the borrower of a loan. Nonetheless, the borrower is faced with a very complicated decision because the choice of LIBOR pricing "locks in" the cost of funds for a period of time, forcing the borrower to forecast the future course of both the prime rate and LIBOR. In practice, at least some borrowers' decisions tend to be linked with a small

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1. The reason banks virtually always book prime-priced loans to U.S. residents domestically is not clear. Perhaps they are concerned that booking such loans offshore would lead New York State tax authorities to reconsider the tax status of all activities at offshore branches. In fact, one New York bank even books its LIBOR-priced loans onshore because it fears an adverse reaction from the state tax authorities and bad publicity if the loans were booked offshore.

lag to the observed prime rate-LIBOR differential.[1] For example, as the chart shows, loans at foreign branches began to increase shortly after the prime rate rose above LIBOR in late 1980. On the other hand, borrowers seem to respond with a longer lag when the prime rate falls below LIBOR because they are "locked into" the LIBOR option for a predetermined period of time.

The table shows that, through 1980, inclusion of loans at foreign branches in business loans and business loans plus nonfinancial commercial paper has little effect on their annual growth rates. However, since the second quarter of 1980 the inclusion of such loans has significantly affected quarterly growth rates for those measures of business credit. Two caveats are in order, however, in the use of these data. First, because loans at foreign branches may include substantial amounts of loans to nonbank financial firms, loans at foreign branches strictly speaking ought not be added to C&I loans. Correct procedures would be either to add in only C&I loans at foreign branches or to add all loans at foreign branches to C&I loans plus loans to nonbank financial intermediaries. The measures actually used overstate to some extent the effect of including C&I loans at foreign branches, but available data do not permit further improvement. Second, loans at foreign branches have been seasonally adjusted by means of seasonal factors utilized for C&I loans at large banks. These probably are not the correct seasonal factors, but the presumption is that loans at foreign branches are very close substitutes for C&I loans at large banks. If so, the error introduced by use of these factors is small.

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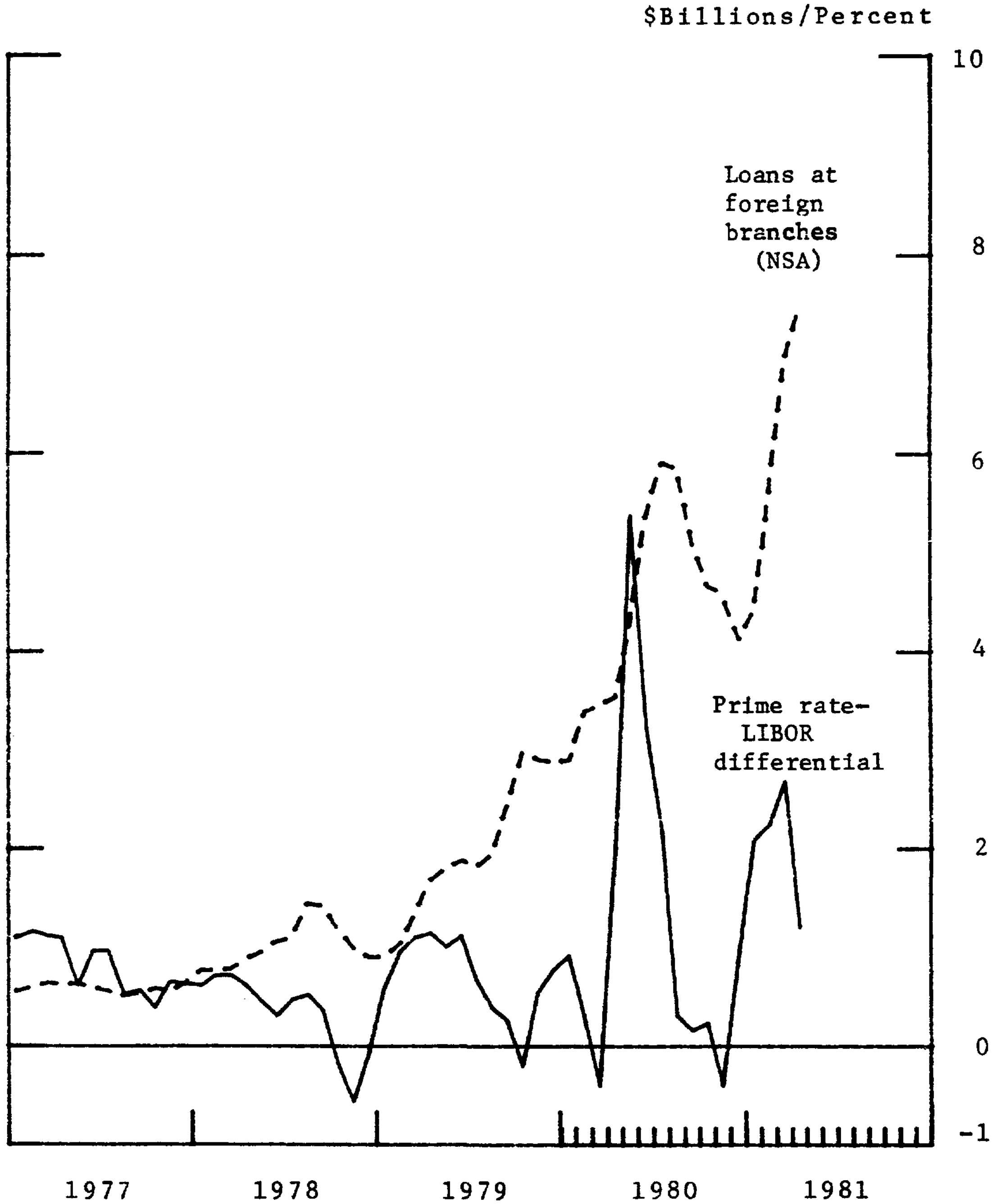
1. The interest rate differential displayed in the chart is a proxy for the prime-rate LIBOR differential. A three-month Eurodollar interbank bid rate has been used because a reliable series for LIBOR is not available. The interbank bid rate typically is 1/16 to 3/16 percentage point below LIBOR. The chart also cannot capture the various LIBOR maturity choices confronting customers.

LOANS AT FOREIGN BRANCHES AND THE PRIME RATE-LIBOR DIFFERENTIAL



EFFECTS OF INCLUDING LOANS AT FOREIGN BRANCHES
IN MEASURES OF BUSINESS CREDIT
(Percentage changes at annual rates,
based on seasonally adjusted data)

	1978	1979	1980	1980 Q2	1980 Q3	1980 Q4	1981 Q1	1981 Feb.	1981 Mar.	1981 Apr.
1. Business loans, net of bankers acceptances, plus loans at foreign branches	17.2	18.5	12.1	-8.2	13.8	22.5	11.5	9.5	8.4	0.7
a. contribution of loans at foreign branches	(0.1)	(0.6)	(0.3)	(2.5)	(-0.5)	(-1.7)	(3.9)	(5.0)	(5.1)	(1.4)
2. Line 1 plus commercial paper issued by nonfinancial firms	17.7	21.1	13.7	-0.6	9.6	19.6	13.7	11.4	10.3	-1.0
b. contribution of loans at foreign branches	(0.1)	(0.5)	(0.2)	(2.3)	(-0.5)	(-1.5)	(3.2)	(4.1)	(4.1)	(1.3)

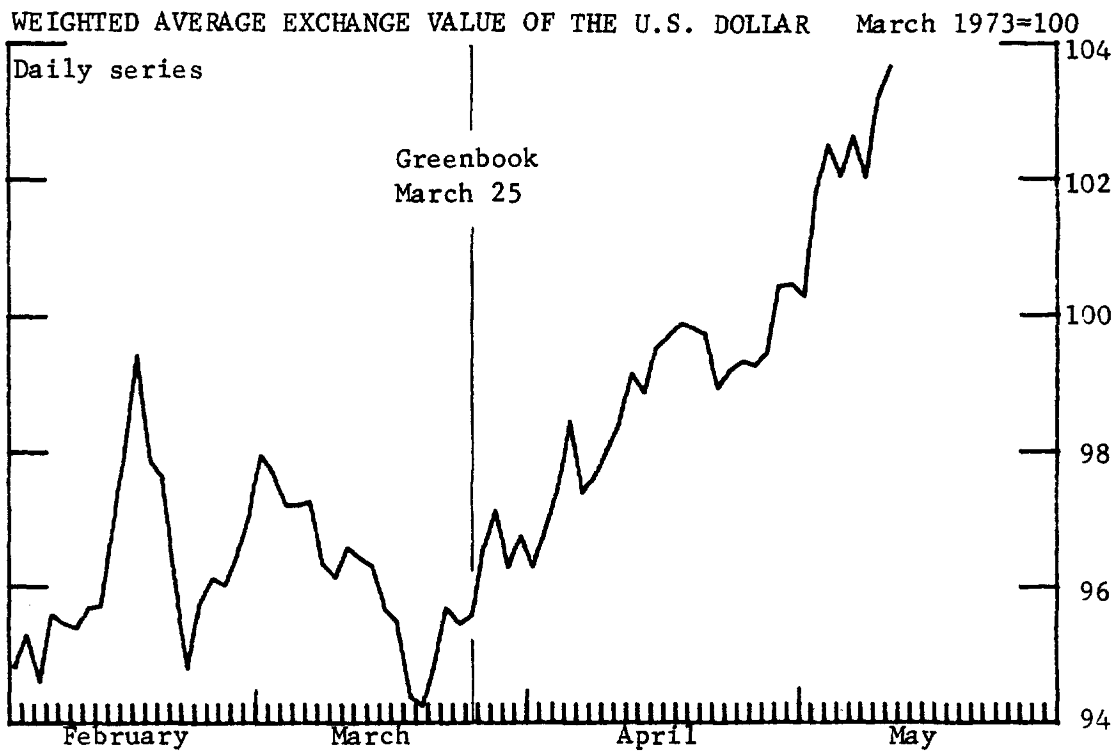
Note: Loans at foreign branches have been seasonally adjusted using seasonal factors for business loans at large banks.

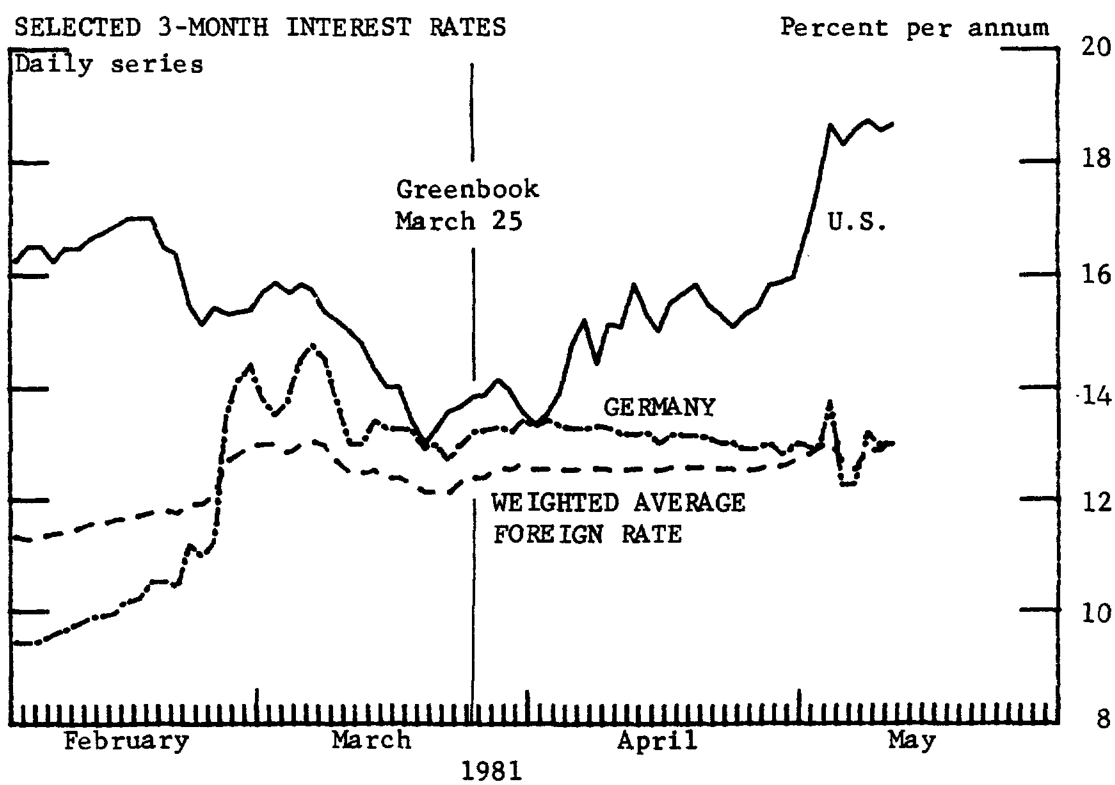
Foreign Exchange Markets

The dollar has appreciated by more than 8 percent on a weighted average basis since the March Greenbook, including a 1-1/2 percent rise since the French election on May 10. As illustrated by the chart on the next page, the dollar strengthened fairly steadily over this period. It appreciated by approximately 12 percent against the French franc, nearly 10 percent against the mark and the other Continental European currencies, 7-1/2 percent against the pound, 5 percent against the yen and 1-1/2 percent against the Canadian dollar.

The strengthening of the dollar since the March Greenbook has been mainly associated with the increase in dollar interest rates relative to foreign interest rates. The chart shows that 3-month dollar interest rates have risen by about 500 basis points over the period, whereas foreign 3-month interest rates have increased by less than 50 basis points on average. Notably, foreign interest rate changes have differed widely across countries. Interest rates have been relatively unchanged in Germany and have declined somewhat in Japan and the United Kingdom. By contrast, interest rates have risen by 300 basis points in Canada and by 200-300 basis points in France, Belgium, and Switzerland, where official discount or intervention rates have been raised.

A second factor that contributed to the dollar's rise since the March Greenbook was the announcement of March balance of trade figures for both the United States and Germany. The sharp reduction in the U.S. trade deficit during the first quarter (international


WEIGHTED AVERAGE EXCHANGE VALUE OF THE U.S. DOLLAR
March 1973=100
Daily series
Greenbook
March 25
104
102
100
98
96
94
February
March
April
May


SELECTED 3-MONTH INTEREST RATES
Percent per annum
Daily series
Greenbook
March 25
U.S.
GERMANY
WEIGHTED AVERAGE
FOREIGN RATE
20
18
16
14
12
10
8
February
March
April
May
1981

accounts basis), with a small surplus in March, contrasted with no decline in the German current account deficit during the first quarter and data for March showing a reversal of much of the February improvement.

. The Desk's only intervention during the period was a purchase of $74 million against marks on the day of the assassination attempt against President Reagan.

Within the European Monetary System, the Belgian franc was under strong pressure in late March and early April, while pressures on the French franc mounted following Mitterand's election victory on May 10. The intensification of pressures on the Belgian franc followed the rejection of economic measures proposed by then Prime Minister Martens, who resigned on March 31. Pressures on the franc eased considerably during the second week of April, after several policy actions were announced and a new government was formed, and the Belgian currency has been comfortably above its intervention floor for most of the subsequent period.

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Gold prices have been less than \$500 an ounce for most of the period since mid-April, compared with prices close to \$540 an ounce at the time of the March Greenbook.

OPEC surpluses and investment flows. For the second half of 1980 the OPEC current-account surplus is estimated at $48 billion, down moderately from $55 billion in the first half of the year. (See table.) Oil revenues of $137 billion in the second half of last year were $2 billion less than in the preceding half-year, as oil export prices rose about 9 percent while export volume decreased 10 percent. OPEC imports were held down by the hostilities between Iran and Iraq and increased only 7 percent ($4 billion) from the first half of the year to the second, an important factor in keeping the current-account surplus from declining more rapidly. Net payments for services and private transfers, and OPEC grant aid, together rose $3 billion.

On the basis of new Bank of England estimates, a much higher proportion than before of total OPEC investment flows can now be identified, at least in broad fashion. The new information relates to investments in industrial countries other than the United States and United Kingdom, to gold purchases, and to loans to developing countries.

Net new OPEC investments in the United States declined to about $5 billion in the second half of 1980, roughly half as large as in the first half. Holdings of Treasury bills, bank deposits, and other bank liabilities, which had been built up in the first half, were run down by $2.6 billion in the second, while accumulations of longer-term U.S. securities were stepped up somewhat in the second half to $6.7 billion. Other investments in the United States, largely consisting of changes in U.S. Government non-security liabilities, were again small but positive in the second half, in contrast to liquidations in 1979. For 1980 as a whole OPEC investments in the United States of $14-1/2 billion were a

ESTIMATES OF OPEC CURRENT ACCOUNT AND EXTERNAL INVESTMENTS
(Billions of dollars)

	1978	1979	1980	1979		1980	
	Year	Year	Year	1st H	2nd H	1st H	2nd H
Current account							
1. Exports	141	213	291	86	127	146	145
(Oil)	(130)	(201)	(276)	(81)	(120)	(139)	(137)
(Non-oil)	(11)	(12)	(15)	(5)	(7)	(7)	(8)
2. Imports	100	102	131	41	60	64	68
3. Trade balance (1-2)	41	111	160	45	67	82	77
4. Net services and private transfers	-38	-42	-50	-19	-23	-24	-26
5. Public transfers	-3	-5	-7	-2	-3	-3	-4
6. Current account balance (3 + 4 + 5)	0	64	103	24	41	55	48
External investments							
7. In United States	.3	7.1	14.4	-.9	8.0	9.5	4.9
a. Treas. bills & bank liabilities	-.2	8.3	.2	.9	7.3	2.8	-2.6
b. Other securities	.1	-.1	12.8	-1.6	1.6	6.1	6.7
c. Other	.4	-1.2	1.4[1]	-.2	-1.1	.6	.8[1]
8. In United Kingdom	.2	2.4	3.3	1.0	1.4	2.8	.5
9. In other industrial countries[2]	4.2	8.7	16.7	3.9	4.8	8.1	8.6
a. Germany[3]	.6	.9	9.2	.1	.8	4.0	5.2
b. Other	3.6	7.8	7.5	3.8	4.0	4.1	3.4
10. In Eurocurrency market[4]	3.0	33.5	41.0	4.4	29.1	22.5	18.5
11. Loans to developing countries	6.2	9.6	6.5	5.9	3.7	4.0	2.5
12. IMF and IBRD	-.7	-1.6	1.4	-1.0	-.6	.2	1.2
13. Gold purchases	.8	1.2	3.5	.7	.5	3.2	.3
Subtotal (7 thru 13)	14.0	60.9	86.8	14.0	46.7	50.3	36.5
14. Other investments plus net borrowings (6-13)	-12.0	4.1	16.2	10.0	-5.7	4.7	11.5

1. Partial estimate.
2. Excluding bank deposits.
3. Long-term only.
4. Including domestic-currency deposits outside the U.S. and U.K.

Note: Numbers may not add to totals due to rounding.

little more than double the 1979 amount, rising from 11 percent to 14 percent of the OPEC surplus.

Flows of OPEC funds into Eurocurrency deposits last year amounted to $41 billion. While still the single most important OPEC investment outlet, these new deposits diminished as a share of the total surplus from about 50 percent in 1979 to about 40 percent in 1980, a percentage much closer to the average for 1974-78. Placements in the Euromarket were somewhat smaller in the second half of the year than the first.

Elsewhere outside the United States, OPEC flows into U.K. investments (excluding Eurocurrency deposits) fell to a very small number in the second half of 1980. Investments (excluding bank deposits) in industrial countries other than the United States and United Kingdom declined moderately to $7.7 billion in the second half of the year from $8.1 billion in the first. The 1980 total of such investments was equivalent to 16 percent of the OPEC surplus, compared with 13 percent in 1979. Flows to individual countries are not separately identifiable except to Germany, where long-term OPEC investment last year came to $9.2 billion. Of that amount, $6.7 billion was loans to official borrowers, and most of the flow to the German private sector was also in the form of loans.

OPEC funds made available to the IMF and IBRD last year amounted to $1.4 billion, mostly a $1.2 billion rise in the OPEC countries' IMF reserve position. The Bank of England estimates OPEC gold purchases in 1980 at $3.5 billion, about three times as much, in dollar terms, as in 1979. The only identified OPEC investment outlet to show a decline in 1980 was loans to developing countries. These loans (including subscriptions to regional development institutions) decreased sharply from $9.6 billion in 1979

(15 percent of the total surplus) to \$6.5 billion in 1980 (6 percent of the surplus).

U.S. International Transactions

The merchandise trade deficit fell to $15 billion at an annual rate in the first quarter of 1981, from $24 billion in the fourth quarter of 1980. The value of exports increased substantially, while imports, particularly nonpetroleum imports, grew slowly.

The value of exports increased almost 10 percent in the first quarter over the average for the fourth quarter of 1980. About one-third of the increase was in agricultural commodities, particularly in

U.S. Merchandise Trade*

	1980			1981		
	Year	3Q	4Q	1Q	Feb.	March
Value (Bil. $, SAAR)						
Exports	221.8	223.1	226.7	247.7	240.3	258.5
Agricultural	42.0	43.0	44.0	50.5	47.9	53.6
Nonagricultural	179.8	180.0	182.7	197.2	192.3	204.9
Imports	249.1	236.6	250.8	262.5	261.2	254.8
Petroleum	78.9	69.5	77.3	83.0	88.7	72.0
Nonpetroleum	170.2	167.1	173.5	179.5	172.5	182.8
Trade Balance	-27.4	-13.6	-24.0	-14.8	-20.9	+3.7
Volume (Bil. 72$, SAAR)						
Exports - Agricultural	18.0	18.5	17.4	19.4	18.4	20.8
- Nonagric.	72.7	72.0	70.4	74.6	72.7	77.7
Imports - Petroleum	6.8	5.8	6.2	6.3	6.6	5.3
- Nonpetroleum	67.5	65.1	66.7	67.6	65.7	68.4

*/ International Transactions basis.
The merchandise trade data used in the International Transactions account is virtually the same as the trade data used in the GNP account. The only difference is that gold transactions are excluded from GNP data but are included in International Transactions data. In 1980 gold exports amounted to $4.0 billion, and gold imports excluded from GNP data amounted to $3.9 billion.

shipments of wheat and soybeans to Latin America and Africa. Non-agricultural exports rose 8 percent from fourth-quarter levels with most of the increase estimated to be in volume. By area, increases in such exports were particularly strong to Canada and to a lesser extent to Latin America. By commodity group, the increases were concentrated in machinery and in industrial supplies. Coal exports increased 16 percent, or by nearly $1 billion at an annual rate in the first quarter. Virtually all of the increase was in volume; part of the rise was attributable to strong foreign demand but some of the increase was in anticipation of the coal strike that began March 27. The strike should begin to affect export statistics towards the end of April.

The value of imports increased only 5 percent in the first quarter. About half the increase was in oil imports which grew by $6 billion at an annual rate. All of this growth was due to higher oil import prices resulting from the OPEC price increase of $3 per barrel made at the end of the year. Price increases in the next few months are expected to be minimal in the light of a continued decline in spot market prices. Oil import volume was little changed from the fourth quarter rate. Within the quarter, a sharp drop in the volume of oil imports in March offset higher imports in January and February. This sharp drop in the value of oil imports in March helps to account for the shift to a trade surplus in that month.

Oil Imports

	1980	4Q80	1Q80	Dec.80	Jan.81	Feb.81	Mar.81
Volume (MBD, SA)	7.09	6.57	6.58	6.81	7.27	6.98	5.65
Price ($/BBL)	30.46	32.25	34.59	32.88	33.51	35.14	35.31
Value (Bil. $, SAAR)	78.9	77.3	83.0	82.9	88.2	88.7	72.0

The value of nonpetroleum imports also increased somewhat in the first quarter. This increase was concentrated in industrial supplies with a smaller increase recorded for consumer goods. About half of the increase was estimated to be in volume. Foreign car imports were about the same in the first quarter as in the fourth quarter in both value and quantity; imports from Japan were above the quarterly rate implied by the recent auto understanding.

Turning to capital account, outflows of funds through U.S. banking offices were reported for both March and April. As shown in the accompanying table, banking offices in the United States shifted from a daily average of $7.4 billion in net borrowings from foreign offices in February to $1.4 billion in net advances to these offices in April. About 70 percent of this net $9 billion outflow was accounted for by member banks.

Available data suggest that regional member banks, during March and April, found it attractive to place funds borrowed in domestic money markets in the Eurodollar market through their foreign branches. One source of demand for these funds was large member banks that increased their LIBOR-priced loans to U.S. residents booked at their foreign branches; in March and April these loans increased by $1.6 billion. In late April these loans leveled off as the LIBOR-prime

Banking Position Vis-a-vis Own Foreign Branches
(Billions of dollars, daily averages, net due to foreign offices = (+))

	1980		1981			
	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.
All banks' net positions with own foreign offices	7.7	7.2	7.4	7.4	2.9	-1.4
(a) 10 largest member banks	-5.2	-5.2	-6.8	-4.8	-5.5	-7.6
(b) All other member banks	-8.1	-8.6	-8.5	-8.9	-10.2	-12.3
(c) Foreign based banks	21.8	21.8	23.5	22.1	19.8	19.9
(d) Nonmembers and Edge corporations	-.8	-.8	-.8	-.9	-1.3	-1.3

SOURCE: Required-reserve reports

differential disappeared. For a more detailed discussion of LIBOR-based loans see the appendix following Section III, "Domestic Financial Developments".

Also in the first quarter, money market mutual funds (MMFs) increased their holdings of Eurodollar money market investments by $4.5 billion, with about $2 billion of this increase reported for March. However, in April, Eurodollar holdings of MMFs changed little; at the end of the month, MMFs held slightly less than $12 billion of Eurodollar investments. These accounted for about 10 percent of the total assets of MMFs, a proportion which has shown little change over the past year.

Investor interest in the MMFs that specialize in Eurodollars has also grown at about the same rate as the total assets of all MMFs. Although over the past year the total assets of these seven MMFs have doubled to $20 billion, their one-fifth share of aggregate MMF assets was unchanged. Thus, it appears that investors consider MMFs specializing in Eurodollars as somewhat more risky than other MMFs since they have not increased the proportion of their MMF holdings devoted to such funds even in the face of the generally higher yields available from these funds.

Foreign official reserve holdings in the United States rose by about $7.5 billion in March, compared with a $2 billion cumulative reduction over the first 2 months of the year. OPEC countries accounted for $4.4 billion of the March increase and for $5.4 billion of the first-quarter increase in foreign official reserve assets. They also accounted for the $1.5 billion increase in foreign official holdings at the FRBNY in April. Increases in OPEC reserves have been invested in a variety of assets including the medium-term-debt of U.S. corporations; in March, $500 million of notes of three U.S. corporate borrowers were purchased through private placements.

U.S. reserve assets rose by $700 million in March. The entire increase reflected U.S. participation in the financing of IMF credit facilities. Overall, drawings on the IMF (primarily by non-oil LDCs) accelerated in the first quarter of 1981.

Net foreign private purchases of U.S. corporate stock totalled $1.7 billion in the first quarter of 1981, only $100 million less than the unusually high level of the fourth quarter. This is consistent with the usual behavior of foreign investors in the U.S. stock market, i.e., they tend to be net purchasers in a rising market.

MAY 11, 1981

U.S. INTERNATIONAL TRANSACTIONS
IN MILLIONS OF DOLLARS; RECEIPTS, OR INCREASE IN LIABILITIES,+

	1979 YEAR	1980 YEAR	1980 QII	1980 QIII	1980 QIV	1981 QI	1981 JAN.	1981 FEB.	1981 MAR.
1. CHANGE IN NET FOREIGN POSITIONS OF BANKING OFFICES IN U.S.(EXCL.LIAB.TO FOREIGN OFF.INST.)	14637	-29847	-22594	-11084	-4410	-9235	5722	-63	-14894
THROUGH INTERBANK TRANSACTIONS WITH									
A.OWN OFFICES IN FOREIGN COUNTRIES	20683	-12803	-18065	-2129	910	-10701	2536	-1959	-11278
B.UNAFFILIATED BANKING OFFICES IN FOR.COUNTRIES	3820	-6231	-2250	-4366	-2543	1975	2646	1378	-2049
THROUGH NONBANK TRANSACTIONS									
A.CLAIMS ON NONBANKS IN FOREIGN COUNTRIES (INC.,-)	-12130	-11826	-3206	-4260	-3708	-1005	417	114	-1536
B.LIABILITIES TO PRIVATE NONBANKS IN FOREIGN COUNTRIES (INC. CUSTODY LIAB.)	2324	1013	928	-329	931	495	123	404	-32
2. PRIVATE SECURITIES TRANSACTIONS, NET - EXCL. U.S. TREAS	-3349	2547	-665	-579	2120	1983	549	788	646
A.FOREIGN NET PURCHASES OF U.S. CORP. BONDS	256	1213	213	203	358	763	154	397	213
B.FOREIGN NET PURCHASES OF U.S. CORP. STOCKS	1037	4264	346	37	1883	1697	597	349	751
C.U.S. NET PURCHASES(-) OF FOREIGN SECURITIES	-4641	-2929	-1224	-818	-120	-477	-202	42	-317
3. FOREIGN NET PURCHASES OF U.S. TREASURY OBLIGATIONS 1/	4821	2680	-1261	-254	894	1405	-30	884	551
4. CHANGE IN FOREIGN OFFICIAL RESERVE ASSETS IN U.S. (INCREASE+)	-13,079	14,856	7,136	7,605	7,508	5,285	-1,624	-480	7,389
BY AREA									
A.G-10 COUNTRIES AND SWITZERLAND	21,121	2,539	1,272	1,351	5,525	1,965	1,490	-1,188	1,662
B.OPEC	6,540	12,093	4,230	3,850	737	5,425	-222	1,204	4,443
C.ALL OTHER COUNTRIES	1,500	5,303	1,633	2,405	1,245	-2,105	-2,893	-496	1,283
BY TYPE									
D.U.S. TREASURY SECURITIES 2/	-21,636	9,684	4,360	3,769	6,911	7,056	1,143	1,551	4,361
E.OTHER 3/	8,557	5,172	2,776	3,836	597	-1,771	-2,767	-2,031	3,028
5. CHANGE IN U.S. RESERVE ASSETS (INCREASE-) 4/	-306	-7,800	-452	-1,051	-3,762	-3,654	-1,560	-1,366	-728
6. TRADE BALANCE 5/	-29,386	-27,354	-7,253	-3,389	-6,008	-3,690	-2,251	-1,744	305
7. ALL OTHER TRANSACTIONS AND STATISTICAL DISCREPANCY	26,602	44,918	25,089	8,752	3,658	7,906	-806	1,981	6,731
MEMO:									
BIL. $ SEASONALLY ADJ. ANNUAL RATES									
MERCHANDISE TRADE BALANCE	-29.4	-27.4	-29.0	-13.6	-24.0	-14.8	-27.0	-20.9	3.7
CURRENT ACCOUNT BALANCE 6/	-0.7	0.1	-8.8	15.8	3.3	n.a.	n.a.	n.a.	n.a.

1/ INCLUDES U.S. TREASURY NOTES PUBLICLY ISSUED TO PRIVATE FOREIGN RESIDENT.
2/ INCLUDES NON-MARKETABLE AND MARKETABLE SECURITIES.
3/ INCLUDES DEPOSITS IN BANKS, COMMERCIAL PAPER, ACCEPTANCES, & BORROWING UNDER REPURCHASE AGREEMENTS.
4/ INCLUDES NEWLY ALLOCATED SDR'S OF $1,139 MILLION IN JANUARY 1979, $1,152 MILLION IN JANUARY 1980; AND $1,093 MILLION JANUARY 1981.
5/ INTERNATIONAL ACCOUNTS BASIS, SEASONALLY ADJUSTED.
6/ INCLUDES REVISED TRADE DATA.

Foreign Economic Developments. Economic activity in the major foreign economies remains weak. Recent data do not suggest an evident trend in real activity. Industrial production has not shown a consistent pattern in any of the major six over the past three months. In the past two months industrial production rose in three countries and fell in the other three and on average is below the year-ago magnitude.

Unemployment rates in the first quarter of 1981 were above those of the previous quarter in the major European countries and increased in the most recent months for the major countries which publish monthly figures (Italy does not). Unemployment rates have fallen in Canada and remained constant in Japan.

Consumer price inflation intensified in all the major foreign countries between the final quarter of 1980 and the initial quarter of this year with the exception of Italy. Among the same countries, only in Germany and Canada was the inflation rate worse in the first quarter of 1981 than over the same period a year earlier.

Major country current accounts (s.a., except Italy) improved between the third and fourth quarters of 1980 with the exception of Germany where the balance worsened. In Japan (s.a.) and Germany (n.s.a.) current accounts worsened in the first quarter of 1981. In the three countries where trade balances for the first quarter are available, Canada, France and Japan, trade balances (s.a.) improved.

The most important, if uncertain, policy development abroad was the election of Francois Mitterand in France. He ran on an expansionist

REAL GNP AND INDUSTRIAL PRODUCTION IN MAJOR INDUSTRIAL COUNTRIES
(Percentage change from previous period, seasonally adjusted)

				1979		1980				1981	1980	1981		
	1978	1979	1980	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Dec.	Jan.	Feb.	Mar.
Canada: GNP	3.4	2.6	0.1	1.1	0.5	-0.6	-1.1	0.4	2.0	n.a.	*	*	*	*
IP	5.3	2.1	-1.5	1.8	-0.5	-0.6	-2.5	-0.1	2.3	n.a.	0.2	-0.9	0.8	n.a.
France: GDP	4.0	3.7	1.4	2.1	0.4	0.4	-0.7	0.2	-0.3	n.a.	*	*	*	*
IP	1.9	4.7	-1.0	3.8	-2.2	0.5	-2.2	0.8	-2.7	n.a.	5.6	-6.8	-0.8	n.a.
Germany: GNP	3.6	4.5	1.8	0.7	0.8	2.1	-2.1	0.0	-0.5	n.a.	*	*	*	*
IP	2.0	5.3	0.0	1.5	0.3	0.9	-2.4	-1.2	-2.2	1.9	-2.8	1.9	5.7	-4.5
Italy: GDP	2.6	5.0	4.0	1.2	4.0	2.1	-0.9	-2.7	2.0	n.a.	*	*	*	*
IP	1.9	6.5	5.8	1.4	8.5	4.2	-2.6	-7.6	5.3	0.4	-6.0	-1.2	7.5	-1.4
Japan: GNP	6.0	5.9	5.5	1.7	1.1	1.8	0.8	1.5	0.6	n.a.	*	*	*	*
IP	6.2	8.3	7.1	2.0	2.6	4.1	0.2	-2.3	1.6	2.2	2.3	0.6	1.7	-1.5
United Kingdom: GDP	2.6	1.4	-2.0	-2.3	1.5	-0.7	-1.3	-1.9	-0.4	n.a.	*	*	*	*
IP	3.6	2.7	-6.8	-1.9	0.0	-2.4	-3.0	-3.4	-2.4	n.a.	-1.0	-1.4	0.8	n.a.
United States: GNP	4.8	3.2	-0.2	1.0	0.2	0.8	-2.6	0.6	0.9	1.6	*	*	*	*
IP	5.8	4.4	-3.6	0.2	-0.1	0.0	-5.2	-1.7	4.9	1.6	1.1	0.5	-0.4	0.4

* GNP data are not published on monthly basis.

CONSUMER AND WHOLESALE PRICES IN MAJOR INDUSTRIAL COUNTRIES
(Percentage change from preceding period)

	1979	1980				1981	1980	1981				MEMO: Latest 3 Months from Year Ago
	Q4	Q1	Q2	Q3	Q4	Q1	Dec.	Jan.	Feb.	Mar.	Apr.	
Canada: CPI	2.3	2.2	2.8	2.8	2.8	3.2	0.6	1.3	1.0	1.3	n.a.	12.2
WPI	3.6	4.9	1.4	2.5	3.1	n.a.	0.2	1.4	n.a.	n.a.	n.a.	11.5
France: CPI	2.8	3.8	3.1	3.2	2.8	3.0	0.9	1.2	0.9	1.0	n.a.	12.6
WPI	1.9	3.1	0.8	0.6	3.4	1.5	0.1	0.8	0.7	0.6	n.a.	6.4
Germany: CPI	0.9	1.9	1.8	0.7	0.8	2.2	0.6	0.8	0.7	0.7	0.7	5.6
WPI	1.1	3.9	1.7	-0.2	0.7	3.9	1.4	0.9	1.3	1.7	n.a.	6.2
Italy: CPI	5.6	6.5	3.9	4.3	5.3	5.2	1.2	1.9	1.8	1.4	n.a.	20.0
WPI	5.6	6.6	3.6	2.3	3.8	n.a.	1.4	1.6	1.6	n.a.	n.a.	15.8
Japan: CPI	1.9	2.0	3.0	1.1	1.2	1.3	-0.5	1.3	0.2	0.6	0.3	6.0
WPI	4.3	6.4	4.8	0.7	-0.7	-0.7	-0.2	-0.5	-0.2	0.0	n.a.	4.0
United Kingdom: CPI	2.8	4.7	5.8	2.2	1.9	2.4	0.5	0.6	0.9	1.5	n.a.	12.7
WPI	3.0	5.3	4.0	2.3	1.2	3.0	0.2	1.5	1.0	1.3	1.4	10.6
United States: CPI(SA)	3.4	3.9	3.1	1.9	3.1	2.6	1.0	0.7	1.0	0.6	n.a.	11.1
WPI(SA)	3.7	3.9	2.5	3.3	2.1	2.2	0.4	0.7	0.8	1.3	0.8	10.5

TRADE AND CURRENT-ACCOUNT BALANCES OF MAJOR INDUSTRIAL COUNTRIES[a]
(Billions of U.S. dollars; seasonally adjusted)

	1979	1980	1979 Q3	1979 Q4	1980 Q1	1980 Q2	1980 Q3	1980 Q4	1981 Q1	1981 Jan.	1981 Feb.	1981 Mar.
Canada: Trade	3.4	6.9	0.9	1.3	1.5	1.1	1.8	2.5	1.5	0.7	0.4	0.4
Current Account	-4.2	-1.3	-0.9	-0.8	-0.7	-0.9	-0.1	0.4	n.a.	*	*	*
France: Trade[b]	-2.4	-14.2	-1.4	-1.3	-3.5	-3.6	-4.0	-3.2	-2.7	-1.3	-0.7	-0.7
Current Account[b]	1.1	-7.4	0.6	-0.4	-2.4	-1.2	-1.9	-1.6	n.a.	*	*	*
Germany: Trade	12.2	5.1	2.3	1.6	1.7	1.3	1.2	0.9	n.a.	0.1	0.4	n.a.
Current Account (NSA)	-5.6	-15.6	-4.7	-0.8	-3.2	-3.7	-6.9	-1.9	-4.5	-2.5	-0.6	-1.3
Italy: Trade	-5.3	-22.8	-1.5	-3.3	-4.1	-4.2	-9.3	-5.2	n.a.	-1.8	-1.3	n.a.
Current Account (NSA)	5.1	-10.1	3.0	-1.5	-2.5	-1.9	-3.2	-2.5	n.a.	*	*	*
Japan: Trade[b]	1.8	2.1	-1.0	-1.6	-1.9	-0.9	1.6	2.8	3.4	1.3	1.0	1.0
Current Account	-8.8	-10.8	-3.9	-4.2	-5.1	-4.1	-1.6	0.4	-0.9	-0.1	-0.6	-0.3
United Kingdom: Trade	-7.4	2.9	-1.1	-1.7	-0.9	-0.7	1.5	3.0	n.a.	1.8	0.7	n.a.
Current Account[b]	-3.5	6.5	-0.4	-1.2	-0.2	-0.2	2.1	4.5	n.a.	2.5	1.4	n.a.
United States: Trade	-29.4	-27.2	-7.1	-9.2	10.8	-7.5	-2.9	-6.0	-3.7	-2.3	-1.7	0.3
Current Account	-0.7	0.1	1.1	-1.7	-2.6	-2.4	4.5	0.7	n.a.	*	*	*

a The current account includes goods, services, and private and official transfers.
b Quarterly data are subject to revision and are not consistent with annual data.
* Comparable monthly current account data are not published.

program. He will try to reverse the "Barre reforms" of the last several years, nationalize major companies and the remaining private banks, and increase minimum wages and reduce working time.

Central banks in Belgium, France, and Switzerland raised their lending rates since the last Greenbook to strengthen their respective currencies: the Belgian discount rate was raised to a record 16 percent on March 31 but had declined to 14 percent by April 30; the French raised their intervention rate to 12-1/2 percent on April 3 to 13-1/2 on May 5, and to 16 percent on May 12. Switzerland raised both the discount rate and the Lombard rate by one percent, to 5 percent and 6.5 percent, respectively, effective May 11.

In Italy, the government proposed a fiscal package that would reduce the fiscal deficit by about 5 trillion lire (about 1.5 percent of GNP); however, this should be viewed as an implementation of the budget rather than as a new tightening. In mid-April, Germany and France announced a coordinated international borrowing of $6 billion.

Individual Country Notes. In Japan domestic demand has not yet responded to the recent shift to a more expansionary demand-management policy. Industrial production (s.a.) fell sharply in March to a level less than two percent above the level of a year ago. The shift to growth led by domestic demand still appears to be moving at a very deliberate pace; private consumption remains weak and inventory adjustments are continuing. Labor market conditions deteriorated somewhat in March as well, as the ratio of job offers to job seekers fell by some five percent (s.a.). Inflation continues to moderate. The WPI was unchanged in March and was less than two percent above its March 1980 level, while the index of wholesale prices of manufactured goods fell in March for the seventh consecutive month. Consumer prices in mid-April moved upward only slightly, and the CPI was less than five percent above its year-ago level for the first time since October 1979. The March current account registered a small deficit bringing the total first-quarter deficit to slightly under $1 billion. The swing from the small fourth-quarter surplus in the current account was due to a marked deterioration in the services account, related in part to larger debt servicing payments. Long-term capital inflows into Japan have continued strong in recent months. Net foreign purchases of Japanese stocks and bonds were about $1.3 billion in March, bringing the total long-term inflow from this source in FY1980 (ending in March) to almost $13 billion. Another $600 million in net inflow was recorded in March.

The German industrial production index declined by 4.5 percent (seasonally adjusted monthly rate) in March after a jump of 5.7 percent in February. The first-quarter level of the index was 2 percent above the fourth quarter of last year. However, the usefulness of the index is dubious due to recent rebasing problems. The rate of unemployment has continued to rise and has reached 5.1 percent (s.a.) in April. Survey information continues to indicate weakness, and the volume of domestic orders has not improved significantly. Orders from abroad, however, have shown strong gains in recent months. Inflation, as measured by the consumer price index, has continued through April at an accelerated rate. The annual rate for the first four months of this year was about 8-1/2 percent. After unusually long negotiations, the metalworkers' union appears near agreement with management on wage increases of about 5 percent. This contract tends to set the pace for other industries in German wage negotiations. On May 11 the 2.6 million member Public Employees Union settled on a 4.3 percent wage increase.

The current account showed a $1.3 billion deficit in March, which brings the annualized (n.s.a.) deficit for the first quarter to $18 billion, compared to a deficit of $15.5 billion last year.

In the United Kingdom unemployment continues to rise. The unemployment rate in April 1981 was 10.1 percent (s.a.). However, the slowing in the rate of increase in unemployment as well as the increase in industrial production in February suggest that the U.K.'s recession may be coming to an end. The increase in the industrial production index in February was the first monthly increase since the 0.1 percent rise recorded in June 1980. Consumer and wholesale prices have accelerated in 1981. In the 6 months to March 1981, consumer prices rose 10-1/2 percent (a.r.), and for the 6-month period ending April 1981 wholesale prices increased by 12-1/2 percent (a.r.); at the end of 1980, comparable inflation rates were 7-1/2 percent and 5-3/4 percent, respectively. In part, the price increases in March were the result of increases in indirect taxes announced in the U.K.'s March 1981 budget. According to a U.K. government estimate, about two-thirds of the 1-1/2 percent March increase in consumer prices is attributable to measures announced in the budget. (The April price indexes also will be affected by budget measures.)

In France the recent victory of the Socialist Mitterand in the presidential election overshadows recent economic developments and casts a shadow over the future performance. President Mitterand ran on an expansionary platform, but one that may also demoralize if not paralyze private sector decision makers. A retreat from "liberalism" and a return toward "dirigism" is expected. Extensive nationalizations, increased minimum wages, reduced hours for the same pay, early retirement, a reduction in the foreign sector, reduced nuclear energy development, increased employment in the public sector (250,000), and tax reform are all expected.

The details of new government proposals and the strength of the left in Parliament will probably not be known until early July after a new National Assembly is elected.

Economic performance in the first quarter of this year was, by most indicators, inferior to an already poor performance in the final quarter of last year. Industrial production in January and February was 5 percent below the previous quarter. In the first quarter of this year unemployment reached a historical high (the series starts in 1974) of 7.1 percent, well above the 6.5 percent reported in each of the previous three quarters. Consumer price inflation in the first quarter was 12 percent (n.s.a.r.), marginally above the 11.2 percent rate of the previous quarter, but well below the rate for the first quarter of 1980. Since the election the Barre Government has raised the intervention rate to 16 percent and abolished the 5 percent reserve requirement on non-resident franc deposits in an attempt to support the franc. In addition reserve requirements on resident deposits were increased, presumably to offset the liquidity effect of reduced reserves on non-resident deposits. In mid-April the government announced a FF15 billion borrowing on international markets to be coordinated with a similar borrowing by Germany. The proceeds will be used for subsidized credits for activities economizing on energy and raw materials, activities to increase productivity, and activities using advanced technologies. The Socialists have suggested they may float a FF20 billion loan on the domestic market.

In Italy economic activity in the early part of this year was stronger than expected; industrial production in the first quarter of 1981 maintained the level reached in the fourth quarter of 1980. The March CPI data point to a slight cooling of inflation; the index rose 1.4 percent compared with an average monthly rise of 1.8 percent over the previous two months. Preliminary indications for April suggest a further slight deceleration. In February the trade deficit fell to $1.3 billion, and for the first two months of 1981 the deficit averaged $1.6 billion, continuing the improvement began in the fourth quarter of 1980. Exports have revived slightly, while imports have declined from the very high levels of last summer. As part of its economic stabilization program, the Italian cabinet has agreed on a fiscal package designed to reduce spending and raise revenues, having a net effect on the deficit of about 5 trillion lire. The package is intended to restrain the growth of the public sector deficit, which is currently threatening to exceed (by a wide margin) the level the Government previously proposed for 1981. The government's proposed measures still must obtain Parliamentary approval.

In Canada evidence suggests that real GNP growth in the first quarter of this year moderated from the 8 percent (s.a.a.r.) growth posted in the fourth quarter of 1980. The index of industrial production for the three-month period ending in February of this year was flat; in the previous three-month period the index rose by over 2-1/2 percent. Consumer price inflation accelerated during the first quarter of this year. For that quarter the index rose almost 13 percent (a.r.), compared with the over 11 percent rate posted in each of the preceding three quarters. The energy and food components of the index experienced the largest increases during the first quarter. In the first quarter of 1981, the trade account showed a surplus of $1.5 billion as compared with a surplus of $2.5 billion in the fourth quarter of 1980.

In Belgium industrial production (n.s.a.) has remained below year ago levels from October to the latest available data (January). The unemployment rate, which rose to 9.1 percent in December, has remained above 9 percent through February. While the consumer price index actually fell slightly in April as a result of the price freeze imposed for that month, the inflation rate as measured on a month-over-year-ago basis remains at approximately 7 percent. The Martens government responded to renewed pressure on the Belgian franc in March by proposing a tightening of fiscal policy and reform of the wage indexation system. Disagreement within the cabinet over the latter measure, in particular, caused the government to fall. On April 6 the former Minister of Finance, Mark Eyskens, became the new Prime Minister. The new government imposed a total price freeze for the month of April, thereby deferring temporarily the issue of reform of the wage indexation system, and proposed a generally restrictive package of government spending limits and tax and wage reductions for firms similar to that urged by the previous government. The general price freeze was allowed to expire on April 30, but a selective price freeze was implemented in its place. As part of the government's effort to defend the franc, the Belgian National Bank raised its discount rate to a post-war record 16 percent on March 31. In response, three-month interest rates rose from 13.2 percent in early March to 17.2 percent in early April. By mid-April pressure on the franc lessened and the Bank lowered its discount rate to 15 percent on April 16 and to 14 percent on April 30.

In Switzerland retail sales figures suggest that the pace of real economic activity remains strong. The unemployment rate in April remained at 0.2 percent, unchanged from the level reached in February and March and also in April 1980. While the consumer price index fell slightly in April, the inflation rate has risen sharply in the past six months. For the first four months of 1981 the consumer price index averaged 5.8 percent higher than in the same period in 1980. For 1980 the comparable average increase was 4.3 percent. On May 11, in response to weakness of the Swiss franc on the exchange markets, the rising inflation rate, and the strong domestic economy the Swiss National Bank raised its discount and Lombard rates by one percentage point to 5 percent and 6.5 percent, respectively.