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November 10, 1981

## **RECENT DEVELOPMENTS**

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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	Oct.	11-6-81	106.7	5.6	1.0	1.5
Unemployment rate (%) <u>1/</u>	Oct.	11-6-81	8.0	7.5	7.0	7.6
Insured unemployment rate (%) <u>1/</u>	Oct.	10-12-81	3.7	3.5	3.2	4.1
Nonfarm employment, payroll (mil.)	Oct.	11-6-81	91.7	-2.7	-6	1.2
Manufacturing	Oct.	11-6-81	20.2	-16.1	-6.0	.6
Nonmanufacturing	Oct.	11-6-81	71.5	1.2	1.0	1.4
Private nonfarm:						
Average weekly hours (hr.) <u>1/</u>	Oct.	11-6-81	34.9	34.9	35.3	35.3
Hourly earnings (\$) <u>1/</u>	Oct.	11-6-81	7.38	7.36	7.26	6.83
Manufacturing:						
Average weekly hours (hr.) <u>1/</u>	Oct.	11-6-81	39.4	39.3	40.0	39.7
Unit labor cost (1967=100) <u>1/</u>	Sept.	10-29-81	214.9	19.9	11.7	7.1
Industrial production (1967=100)	Sept.	10-16-81	152.1	-9.4	-2.1	5.3
Consumer goods	Sept.	10-16-81	148.5	-4.0	-4.8	2.8
Business equipment	Sept.	10-16-81	184.7	-3.9	2.4	8.2
Defense & space equipment	Sept.	10-16-81	103.4	3.5	6.7	5.4
Materials	Sept.	10-16-81	153.1	-13.2	-2.3	7.4
Consumer prices all items (1967=100)	Sept.	10-23-81	279.0	13.9	12.9	10.9
All items, excluding food & energy	Sept.	10-23-81	264.5	14.7	14.4	11.7
Food	Sept.	10-23-81	278.6	11.7	10.5	6.3
Producer prices: (1967=100)						
Finished goods	Oct.	11-10-81	273.8	6.6	4.1	7.3
Intermediate materials, nonfood	Oct.	11-10-81	314.3	.4	2.8	9.1
Crude foodstuffs & feedstuffs	Oct.	11-10-81	248.9	-30.5	-23.6	-12.0
Personal income (\$ bil.) <u>2/</u>	Sept.	10-20-81	2460.6	9.6	12.8	11.6
						(Not at annual rates)
Mfrs. new orders dur. goods (\$ bil.)	Sept.	11-2-81	85.8	-1.8	-2.9	4.4
Capital goods industries	Sept.	11-2-81	29.5	-3.1	4.8	4.8
Nondefense	Sept.	11-2-81	22.7	-8.0	-2.2	.9
Defense	Sept.	11-2-81	6.8	18.1	37.3	20.0
Inventories to sales ratio: <u>1/</u>						
Manufacturing and trade, total	Aug.	11-5-81	1.43	1.40	1.40	1.48
Manufacturing	Sept.	11-2-81	1.63	1.61	1.57	1.64
Trade	Aug.	11-5-81	1.25	1.23	1.22	1.27
Ratio: Mfrs.' durable goods inventories to unfilled orders <u>1/</u>	Sept.	11-2-81	.584	.574	.568	.560
Retail sales, total (\$ bil.)	Sept.	10-13-81	88.8	.4	1.7	10.2
GAF <u>3/</u>	Sept.	10-13-81	18.3	-1.2	-1.1	7.4
Auto sales, total (mil. units.) <u>2/</u>	Oct.	11-4-81	7.2	-19.1	-12.7	-20.9
Domestic models	Oct.	11-4-81	5.1	-25.5	-13.3	-24.0
Foreign models	Oct.	11-4-81	2.0	2.9	-11.1	-12.2
Housing starts, private (thous.) <u>2/</u>	Sept.	10-19-81	918.0	-1.7	-11.6	-38.1
Leading indicators (1967=100)	Sept.	10-29-81	130.1	-2.7	-2.9	-3.2

1/ Actual data used in lieu of percent changes for earlier periods.

2/ At annual rate.

3/ Excludes mail order houses.

## DOMESTIC NONFINANCIAL DEVELOPMENTS

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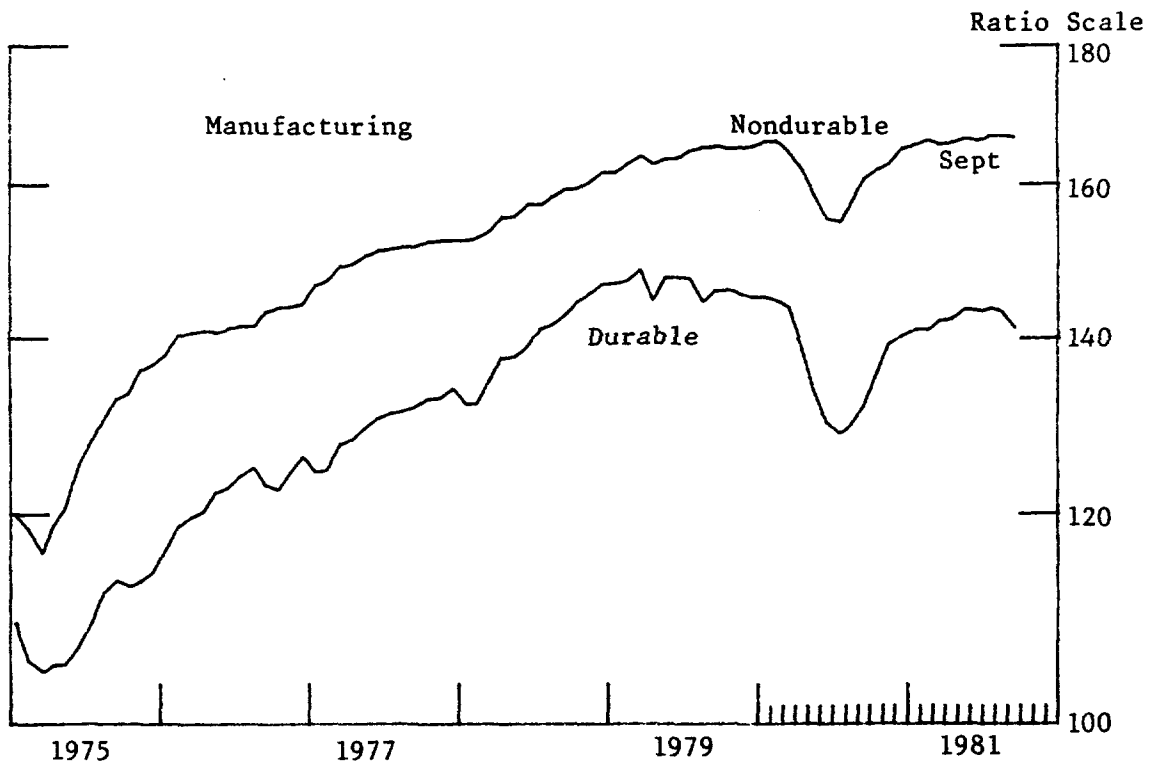
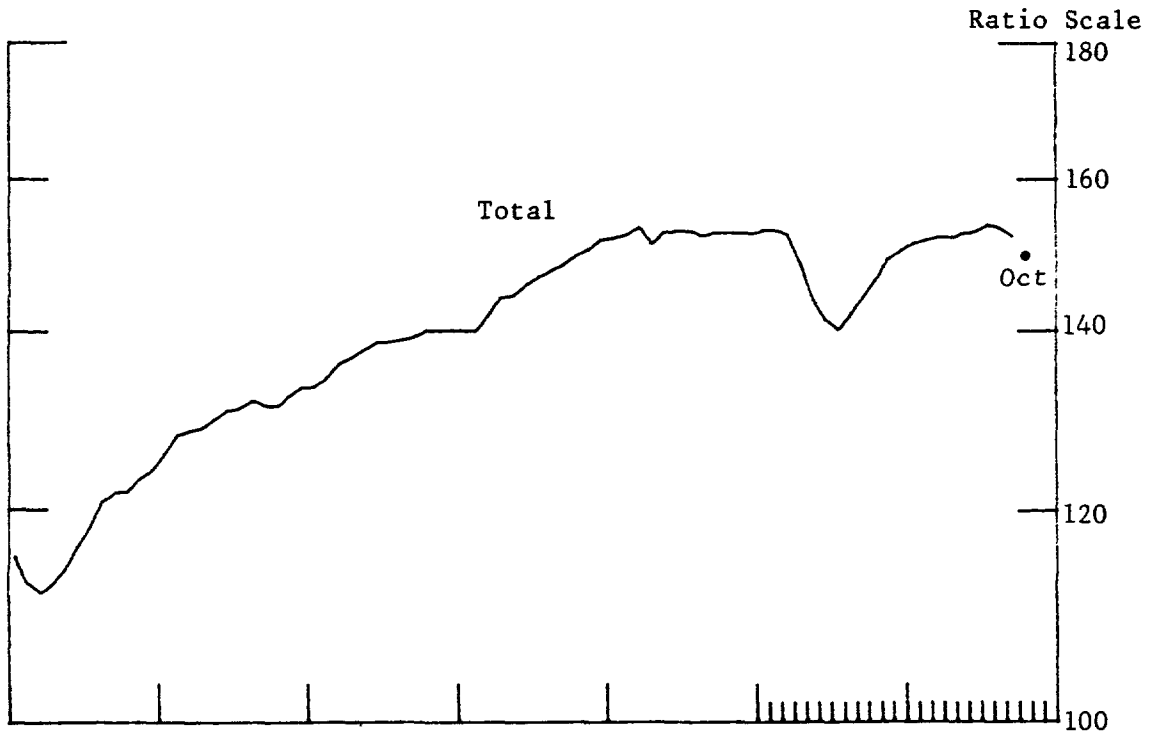
A widespread deterioration of economic activity appears to be underway in the current quarter. Industrial production is estimated to have declined in October for the third consecutive month, and manufacturing employment fell sharply, with declines occurring in a broad range of industries. Activity in sectors that had been weak, such as autos and housing, declined further. Business fixed investment has continued to slip lower, while inventory accumulation has increased. A burst of consumer price inflation occurred in the third quarter, although price increases have continued to ease for many consumer and producer commodities.

### Industrial Production and Capacity Utilization

Industrial production declined 0.3 percent in August and 0.8 percent in September, according to estimates of a month ago, and available data indicate that a larger cutback occurred in October. Auto assemblies in October were cut by roughly 11 percent, and the output of related parts and materials probably also declined considerably. Trade reports indicate that the industry currently plans a further reduction in assemblies in November to 5.4 million units at an annual rate.

Production of durable goods for the home fell in September and evidently again in October. Business equipment output declined in September for the first time since last winter and, given the reduced new orders for equipment and a diminished orders backlog, further weakness in this sector appears likely. Materials output, which had increased only slightly during the first half of 1981, turned down in

INDUSTRIAL PRODUCTION INDEXES  
(1967=100)



CAPACITY UTILIZATION: MANUFACTURING AND MATERIALS  
(Percent, seasonally adjusted)

	(1) 1972-1980 quarterly highs <sup>1</sup>	(2) 1967-1980 Mean	(3) August 1981	(4) September 1981 <sup>2</sup>
Manufacturing industries	87.8	82.6	79.3	78.5
Primary Processing	93.2	84.9	79.7	78.2
Textiles mill products	95.0	86.7	80.8	n.a.
Paper and products	95.7	89.4	87.7	88.5
Chemical and products	85.9	79.8	77.3	n.a.
Petroleum products	98.5	91.6	75.9	75.6
Rubber and Plastics products	99.3	89.4	86.2	84.9
Clay, glass and stone products	87.7	78.9	70.6	n.a.
Iron and Steel	102.5	83.9	79.2	n.a.
Nonferrous metals	98.2	84.9	83.8	82.3
Fabricated metal products	85.4	79.5	73.5	72.5
Advanced processing	85.7	81.3	79.1	78.6
Foods	87.1	84.5	83.1	n.a.
Nonelectrical machinery	87.9	80.8	80.3	79.4
Electrical machinery	89.8	79.9	84.2	83.0
Motor vehicles and parts	98.0	81.1	59.5	59.1
Aerospace and misc. trans. equip.	92.0	77.0	77.0	76.3
Instruments	89.3	83.2	80.5	79.7
Materials, total	92.3	84.4	81.4	80.4
Durable goods materials	91.3	81.0	79.0	77.4
Raw steel	105.4	86.8	80.6	77.2
Nondurable goods materials	93.8	87.6	83.5	83.4
Energy materials	94.7	89.2	85.0	83.9

1. Highs are specific to each series and are not necessarily coincident.

2. Preliminary estimates.



August and fell by more than 1 percent in September. Further declines apparently occurred among durable materials in October, as raw steel output dropped by more than 6 percent.

The capacity utilization rate in manufacturing, which had been edging lower since May, fell to 78-1/2 percent in September. Declines were both broader and deeper than in earlier months. The available evidence suggests that this slackening continued in October, with widespread declines occurring in durable manufacturing. The utilization rate for producers of raw steel dropped almost 3-1/2 percentage points in September and an even greater amount in October.

#### Employment

The employment situation weakened markedly in October. Payroll employment, as measured by the survey of establishments, declined 200,000 in October, with job losses heavily concentrated in the industrial sector and only partially offset by gains in the service sectors. Manufacturing employment, which had not fully recovered from the sharp contraction of 1980, dropped 275,000, as sizable losses were pervasive across both durable and nondurable goods industries. Employment in the transportation equipment industry is estimated to have fallen 85,000; because BLS does not attempt to seasonally adjust motor vehicle employment during the traditional model changeover period, the reported October drop reflects the cumulative job loss since June. The factory workweek--although up slightly from its holiday-reduced September figure--remained near its lowest level since the 1980 recession. In other sectors, weakness in construction employment persisted in October, but jobs continued to expand in the trade sector.

CHANGES IN EMPLOYMENT<sup>1</sup>  
(Thousands of employees; based on seasonally adjusted data)

	1979	1980	1981				
			Q2	Q3	Aug.	Sept.	Oct.
-Average monthly changes-							
<u>Nonfarm payroll employment</u> <sup>2</sup>	170	34	89	111	21	47	-205
Strike adjusted	176	28	117	94	-1	62	-220
Manufacturing	-5	-58	78	25	-30	-5	-275
Durable	1	-47	60	10	-1	-23	-183
Nondurable	-6	-12	18	15	-29	18	-92
Construction	15	-12	-44	-5	3	-7	-19
Trade	30	12	27	54	66	17	31
Finance and services	84	79	76	86	35	128	38
Government	27	13	55	-79	-75	-113	16
Private nonfarm production workers	103	-9	110	161	77	113	-212
Manufacturing production workers	-16	-67	57	16	-33	-1	-260
<u>Total employment</u> <sup>3</sup>	172	-42	-7	-41	-18	-674	-53
Nonagricultural	174	-48	-3	-56	-130	-615	-79

1. Average change from final month of preceding period to final month of period indicated. These figures are revised to reflect new seasonal factors and the 1980 benchmark to the establishment survey data.

2. Survey of establishments. Strike-adjusted data noted.

3. Survey of households.

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

	1979	1980	1981				
			Q2	Q3	Aug.	Sept.	Oct.
Total, 16 years and older	5.8	7.1	7.4	7.2	7.2	7.5	8.0
Teenagers	16.1	17.7	19.2	18.7	18.8	19.3	20.6
20-24 years old	9.0	11.5	12.3	11.7	11.8	12.1	12.8
Men, 25 years and older	3.3	4.7	4.8	4.8	4.8	5.0	5.5
Women, 25 years and older	4.8	5.5	5.7	5.7	5.5	5.9	6.1
White	5.1	6.3	6.5	6.2	6.1	6.5	6.9
Black and other	11.3	13.2	13.7	14.6	15.0	15.1	15.5
Fulltime workers	5.3	6.8	7.1	6.9	6.7	7.2	7.7
White collar	3.3	3.7	4.0	4.0	3.9	4.1	4.1
Blue collar	6.9	10.0	9.8	9.6	9.3	10.2	11.0

Total employment (household survey), which had fallen substantially in September, posted a further small decline last month. Unemployment increased by more than one-half million workers, and the unemployment rate moved upward for the third consecutive month and at 8.0 percent was the highest rate since 1975. The latest increase in joblessness occurred largely among adult male workers. As in September, layoffs accounted for a large share of the October increase in unemployment.

#### Personal Income and Consumer Spending

Total personal income growth slowed to a 9-1/2 percent annual rate in September, as employment cutbacks trimmed the rate of growth in private wages and salaries. The contraction of payroll employment and the small rise in average hourly earnings in October suggest that a further slowing of private wage and salary disbursements has occurred. In real terms, wages and salaries have been virtually unchanged since January.

Retail sales in constant dollars in September were a bit lower than early this year. Nominal sales gains in August and September--1.3 percent and 0.4 percent, respectively--were only large enough to offset rising prices. Sales at gasoline service stations rose sharply in September, while sales at food stores remained essentially unchanged after a sharp advance in August. In contrast, spending for general merchandise, apparel, and furniture and appliances (GAF) declined 1.2 percent in September; in the third quarter as a whole, nominal outlays for these discretionary items were up only fractionally.

PERSONAL INCOME  
(Based on seasonally adjusted data)

	1979	1980	1981				
			Q2	Q3	July	August	Sept.
- - - - Percentage changes at annual rates <sup>1</sup> - - - -							
Total personal income	12.3	11.0	8.7	12.6	17.1	11.3	9.6
Wage and salary disbursements	10.8	9.0	6.8	8.7	9.0	11.8	7.7
Private	11.6	9.2	7.2	9.3	9.9	13.7	5.8
Disposable personal income							
Nominal	11.7	10.9	8.0	11.4	17.0	9.5	8.7
Real	2.0	.8	1.4	2.2	4.7	3.0	-1.8
- - - - - Changes in billions of dollars <sup>2</sup> - - - - -							
Total personal income	18.3	18.7	14.6	25.4	34.0	22.8	19.6
Wage and salary disbursements	10.3	9.8	7.0	11.7	11.0	14.5	9.6
Private	8.9	8.1	5.9	9.9	9.9	13.8	5.9
Manufacturing	2.0	2.3	3.1	2.9	2.9	2.7	3.1
Other income	8.9	9.6	7.8	14.4	23.9	9.0	10.3
Transfer payments	2.8	4.1	1.5	5.9	15.3	.2	2.2
Less: Personal contributions for social insurance	.9	.8	.2	.7	1.0	.9	.2
Memorandum:							
Personal saving rate <sup>3</sup>	5.2	5.6	5.4	4.9	5.0	4.9	4.8

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.

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

	1981						
	Q1	Q2	Q3	June	July	Aug.	Sept.
Total sales	4.9	-.4	2.3	2.2	.0	1.3	.4
(Real) <sup>1</sup>	2.9	-1.7	.2	1.9	-1.0	.4	-.4
Total, less autos and nonconsumption items	3.5	1.0	.9	1.6	-.5	.7	.2
Total, exc. auto group, gasoline, and nonconsump- tion items	3.3	1.1	1.0	1.7	-.4	.9	.0
GAF <sup>2</sup>	3.1	1.1	.2	2.7	-2.2	2.3	-1.2
<u>Durable goods</u>	8.5	-4.1	5.7	3.8	.8	2.5	1.2
Automotive	10.0	-5.6	10.5	5.5	2.5	4.5	1.5
Furniture & appliances	4.4	-2.6	-.5	2.1	-4.0	3.8	-.2
<u>Nondurable goods</u>	3.3	1.3	.7	1.5	-.4	.7	.1
Apparel	5.1	-.5	1.2	2.0	.3	-.2	-.5
Food	2.1	2.3	2.7	1.8	.4	2.1	-.1
General merchandise <sup>3</sup>	1.8	3.2	.1	3.1	-2.5	2.8	-1.8
Gasoline	4.9	.1	-.1	1.4	-1.1	-.2	1.5

1. BCD series 59. Data are available approximately 3 weeks following the retail sales release.

2. General merchandise, apparel, and furniture and appliance stores.

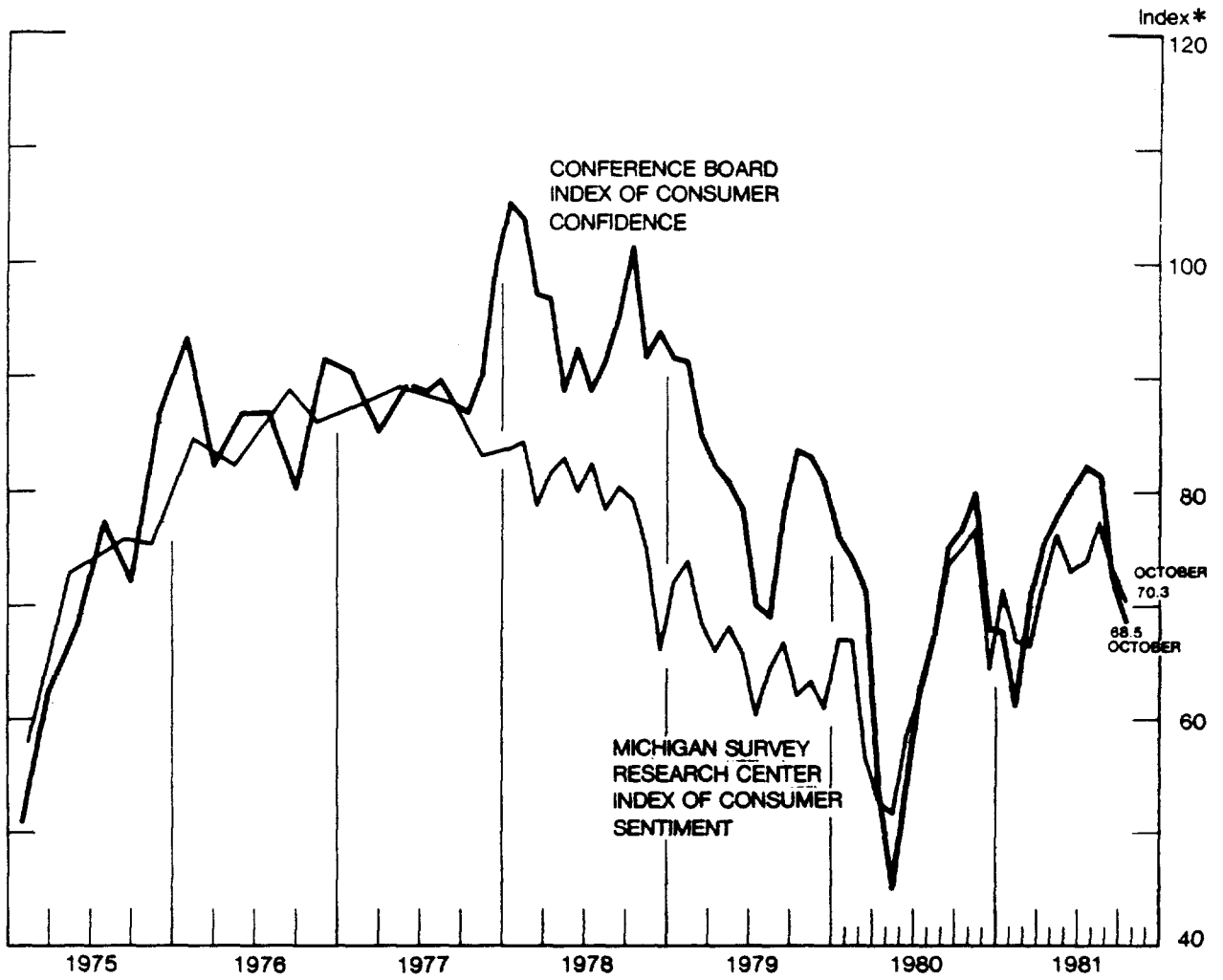
3. General merchandise excludes mail-order nonstores; mail-order sales are also excluded in the GAF composite sales summary.

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

	1981						
	Q1	Q2	Q3	July	Aug.	Sept.	Oct.
Total	10.0	7.9	9.0	8.2	10.1	8.8	7.2
Foreign-made	2.7	2.3	2.1	2.3	2.1	2.0	2.0
U.S.-made	7.3	5.6	6.9	5.9	7.9	6.9	5.1
Small	3.9	2.9	3.5	3.1	4.1	3.5	2.6
Intermediate & standard	3.4	2.8	3.4	2.8	3.9	3.5	2.5

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

**Consumer Attitudes**



\* Michigan Survey Research Center Index of Consumer Sentiment (1966 QI = 100) and Conference Board Index of Consumer Confidence (1969-1970 = 100). Bases of indexes are derived from responses (favorable minus pessimistic) to five equally weighted questions. Questions in the two indexes are different.

Note: CB index plotted middle of bi-monthly period to May-June 1977, and monthly beginning in June 1977; SRC index plotted middle of quarter to 1977 QIV, and monthly beginning in January 1978.

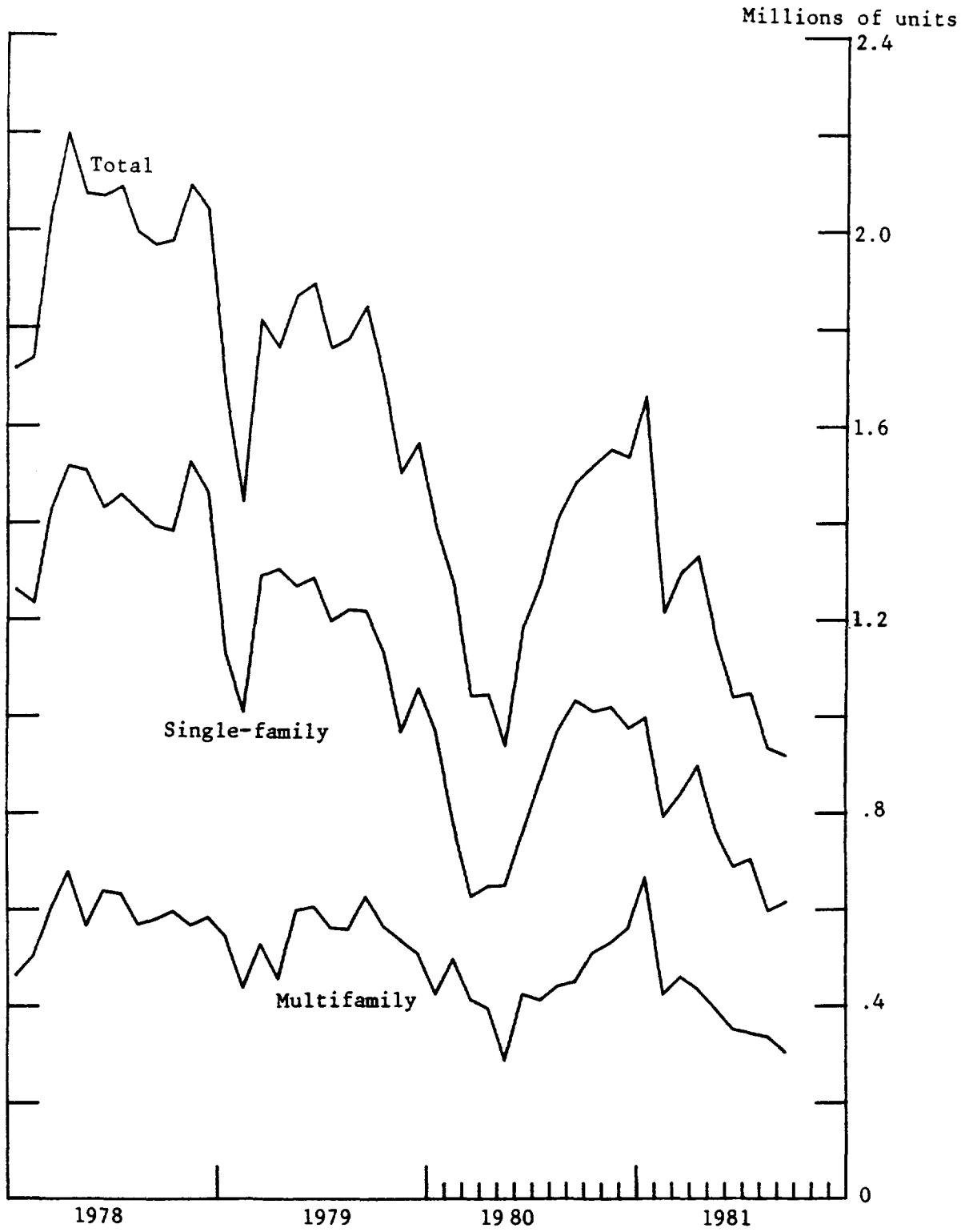
Sales of new domestic autos plunged from a seasonally adjusted annual rate of 6.9 million units in September to a rate of 5.1 million units rate in October. The decrease in sales occurred even though some of the fall rebate programs were extended through October and into November. Sales of new imported cars in October continued at the reduced 2.0 million unit rate of September, in large part reflecting the import quota on Japanese-made cars. Consistent with sluggish consumer demands in recent months, the Michigan and Conference Board surveys for October suggest that consumer confidence in favorable business conditions and employment and income prospects has declined significantly since last summer. While the Michigan survey found expectations of generally lower inflation and interest rates, the outlook for future economic conditions deteriorated.

In a special question added to the October Conference Board Survey, 30 percent of the respondents said that they had delayed a purchase because of high interest rates. Those interviewed said that on average they would have had to pay 17-1/4 percent interest on the postponed purchase. Cars were the most frequently mentioned postponed outlay.

#### Residential Construction

Conditions in the housing market in September deteriorated further, thus extending the general decline that began in 1978. Housing starts fell nearly 2 percent in September to a 920,000 unit seasonally adjusted annual rate, approaching the post-war low. Permits issued for new houses also declined further in September. Sales of new houses, at an annual rate of 312,000 units, were the lowest in the 18-year history of the series. Sales of existing houses have not declined quite so precipitously,

PRIVATE HOUSING STARTS  
(Seasonally adjusted annual rate)





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

	1980	1981					
	Annual	01	02	03	July	Aug.	Sept. <sup>1</sup>
All units							
Permits	1.19	1.18	1.11	.87	0.91	.87	.84
Starts	1.29	1.39	1.18	.97	1.05	.93	.92
Single-family units							
Permits	.71	.69	.64	.49	.53	.49	.45
Starts	.85	.87	.78	.64	.70	.60	.62
Sales							
New homes	.53	.51	.45	.36	.42	.36	.31
Existing homes	2.88	2.54	2.59	2.28	2.52	2.26	2.07
Multifamily units							
Permits	.48	.49	.47	.38	.39	.37	.40
Starts	.44	.52	.39	.33	.34	.34	.30
Mobile home shipments	.22	.25	.26	n.a.	.27	.23	n.a.

1. Preliminary estimates.

possibly reflecting the importance of loan assumptions and seller financing in supporting this type of activity.

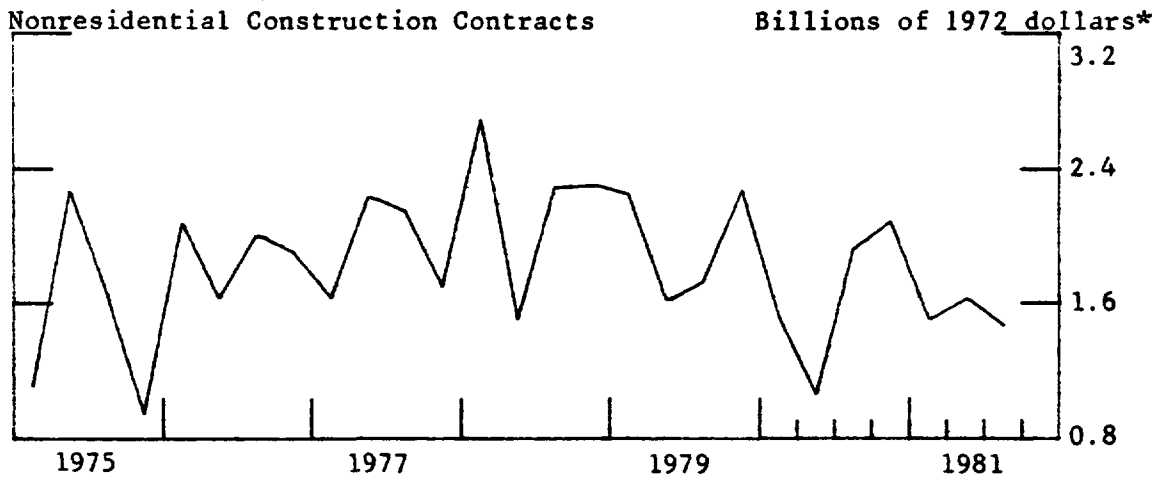
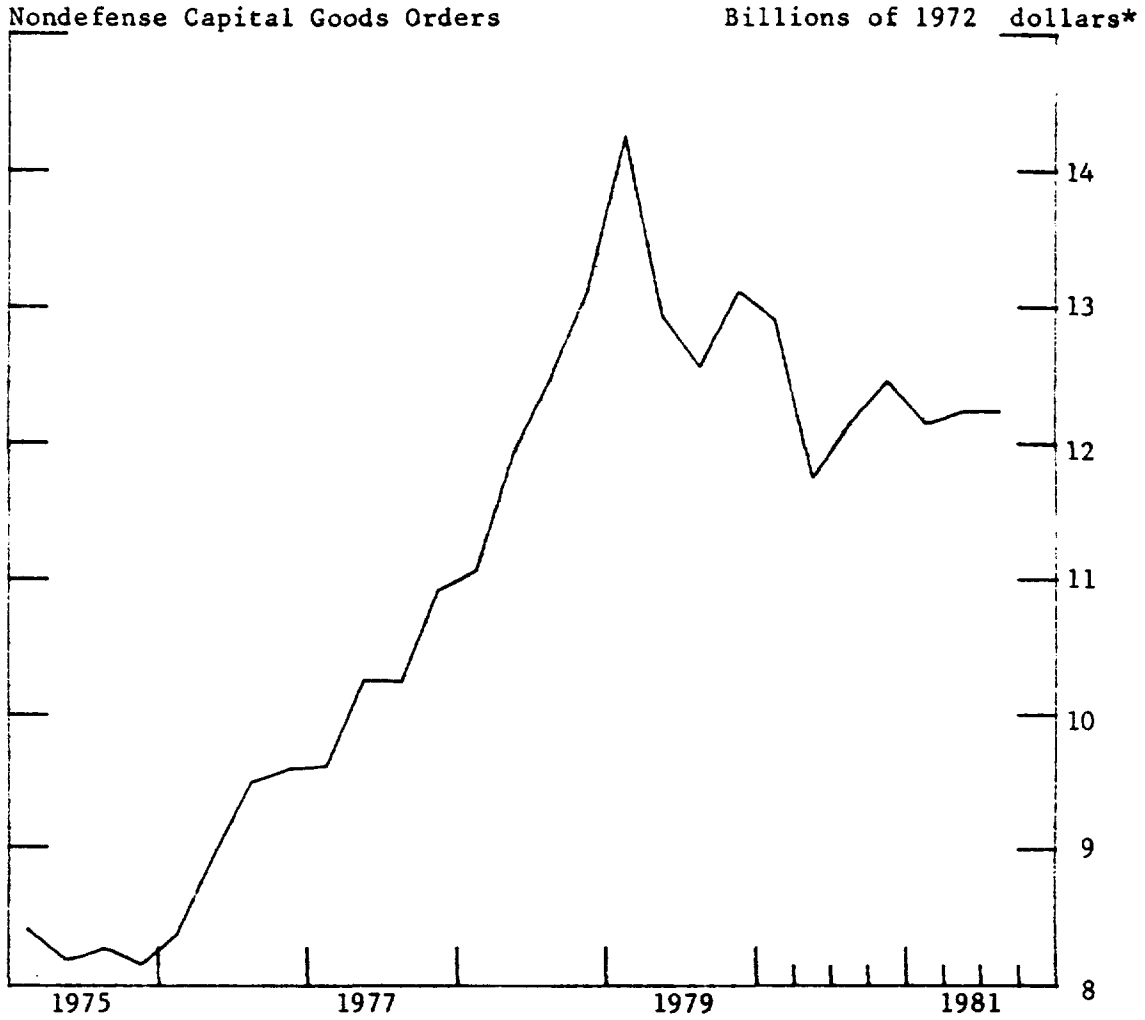
Measures of house prices have continued to increase this year, although less than prices in general. The average price of existing homes sold in September was \$79,000, only 5.6 percent above September 1980. The average price of new homes sold in September was \$82,800, up 3 percent from September 1980.

Largely in response to weak effective demand for housing, cost increases for construction inputs also have diminished in recent months. The producer price index for materials for all types of construction edged lower during the third quarter, following an advance of about 8-1/2 percent over the previous year. Producer prices for softwood lumber and plywood--key inputs in housing construction--have declined steadily since mid-summer.

#### Business Fixed Investment

Business fixed investment in real terms edged lower in the third quarter, following a small decline in the second quarter. Equipment spending has been especially weak in the past two quarters and is only moderately above its cyclical low of 1980-Q2. There was a substantial increase in purchases of motor vehicles in the third quarter, but as measured in the national income and product accounts this was more than offset by reduced outlays for electrical and nonelectrical machinery and selected transportation items. Business spending for structures continued to rise in the third quarter, though at a slower rate than in early 1981. Real outlays increased for all major types of structures except in the public utility sector where expenditures fell slightly.

COMMITMENTS FOR BUSINESS CAPITAL SPENDING  
(Seasonally Adjusted)



\* Quarterly average of monthly data.

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

	1981					
	Q1	Q2	Q3	July	Aug.	Sept.
Nondefense capital goods shipments						
Current dollars	1.4	3.2	1.1	-2.7	2.7	.6
Constant dollars <sup>1</sup>	.3	-.6	.3	-3.3	3.4	.2
Addendum: Sales of heavy-weight trucks (thousands)	247	226	232	205	235	256
Nonresidential construction						
Current dollars	8.0	1.7	3.4	2.3	.6	-.6
Constant dollars	5.7	1.2	2.9	1.7	.7	-1.0
Addendum: Oil and gas well drilling (millions of feet)	24.7	30.1	26.7	29.5	25.1	25.6

1. FRB staff estimate.

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

	1981					
	Q1	Q2	Q3	July	Aug.	Sept.
Nondefense capital goods orders						
Current dollars	1.2	1.9	-.2	4.3	2.0	-8.0
Constant dollars	-2.5	.8	.0	4.5	2.8	-8.5
Machinery						
Current dollars	1.1	3.1	-.4	-3.5	7.7	-4.3
Constant dollars <sup>1</sup>	-2.1	.6	-2.1	-4.0	7.4	-5.1
Addenda: Ratio of current dollar unfilled orders to shipments						
Total	6.32	6.10	5.97	6.17	6.01	5.89
Machinery	4.68	4.62	4.47	4.54	4.45	4.44
Nonresidential building contracts						
Current dollars	-25.2	10.2	-9.7	-28.9	-24.5	21.5
Constant dollars <sup>1</sup>	-28.5	9.4	-10.0	-30.2	-23.8	21.6

1. FRB staff estimate.

MCGRAW-HILL FALL SURVEY  
 PLANT AND EQUIPMENT EXPENDITURES ANTICIPATED FOR 1982  
 (Percent change from prior year)

All business	9.6
Manufacturing	11.5
Durables	10.1
Nondurables	12.9
Nonmanufacturing	8.3

RECENT ERROR HISTORY OF THE FALL MCGRAW-HILL SURVEY

Year	Anticipated Change	Actual Change	Error (Anticipated Less Actual Change)
	-----Percent-----		
1970	8.3	5.5	2.8
1971	2.4	1.9	.5
1972	6.9	8.9	-2.6
1973	10.6	12.8	-2.2
1974	13.6	12.7	.9
1975	11.8	.3	11.5
1976	8.8	6.8	2.0
1977	13.0	12.7	.3
1978	11.1	13.3	-2.2
1979	9.9	15.1	-5.2
1980	9.5	9.3	.2
1981	11.9	8.8 <sup>1</sup>	3.1

1. Anticipated by August Commerce Survey.

Capital spending commitments in real terms continue to indicate weakness in expenditures. Total contracts and orders for plant and equipment, an overall indicator of capital investment spending, fell 5.8 percent in September. In the equipment category, orders for non-defense capital goods dropped 8.5 percent. The ratio of unfilled orders for nondefense capital goods to their shipments continued to fall as it has for the most part during 1980 and 1981. Contracts as well as permits for nonresidential structures increased in September. However, these are volatile series and the September advances follow large declines in August.

In addition to this near-term weakness, the latest McGraw-Hill survey indicates that no increase is likely in 1982's real capital spending. According to the survey, businesses plan to increase current dollar capital outlays by 9.6 percent in 1982, but they anticipate that prices for capital goods will go up by the same amount. It should be noted that in past periods of sluggish economic activity, the McGraw-Hill survey has tended to overestimate actual expenditures.

#### Business Inventory Investment

Manufacturing and trade inventories were accumulated at an increased rate in July and August. This, plus the large increase in manufacturing inventories in September, suggests that the total inventory accumulation in 1981-Q3 will be substantial. Inventory-to-sales ratios generally have been rising.

Movements in manufacturers' inventory have been dominated for the past three to four months by the accumulation of durable stocks. In

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

	1979	1980	1981					
			Q1	Q2	Q3	July	Aug.(r)	Sept.(p)
<u>Book Value Basis</u>								
Total	49.0	31.0	41.1	35.0	n.a.	46.5	53.7	n.a.
Manufacturing	31.5	16.4	34.2	12.7	26.7	26.0	17.9	36.3
Durable	23.7	10.2	18.5	9.8	25.3	26.1	16.4	33.4
Nondurable	7.8	6.2	15.7	3.0	1.4	-.2	1.5	2.9
Wholesale	10.3	11.7	.0	6.7	5.6	-9.7	17.0	9.4
Retail	7.2	2.9	6.8	15.6	n.a.	30.2	18.8	n.a.
Automotive	1.4	-2.3	-3.5	12.2	n.a.	14.7	7.3	n.a.
Gen. Merchandise	1.1	1.4	3.1	2.6	n.a.	5.9	4.4	n.a.
<u>Constant Dollar Basis</u>								
Total	7.2	-2.5	-1.3	11.0	n.a.	16.1	6.4	n.a.
Manufacturing	6.8	-1.0	4.6	.9	n.a.	7.3	-2.2	n.a.
Wholesale	.4	.6	-1.6	3.2	n.a.	-6.4	7.2	n.a.
Retail	-.1	-2.2	-4.3	6.9	n.a.	15.2	1.3	n.a.
Automotive	-.3	-1.2	-5.9	5.7	n.a.	6.3	-2.8	n.a.

INVENTORIES RELATIVE TO SALES<sup>1</sup>

	1980		1981					
	Cyclical Peak <sup>2</sup>		Q1	Q2	Q3	July	Aug.(r)	Sept.(p)
<u>Book Value Basis</u>								
Total	1.53		1.39	1.41	n.a.	1.41	1.43	n.a.
Manufacturing	1.76		1.61	1.60	1.63	1.60	1.61	1.63
Durable	2.36		2.09	2.05	2.13	2.07	2.10	2.15
Nondurable	1.18		1.11	1.12	1.10	1.10	1.10	1.10
Wholesale	1.21		1.08	1.11	1.13	1.10	1.14	1.12
Retail	1.44		1.31	1.36	n.a.	1.37	1.37	n.a.
Automotive	2.01		1.47	1.77	n.a.	1.73	1.69	n.a.
Gen. Merchandise	2.28		2.22	2.21	n.a.	2.29	2.26	n.a.
<u>Constant Dollar Basis</u>								
Total	1.76		1.63	1.66	n.a.	1.68	1.70	n.a.
Manufacturing	2.11		1.97	1.95	n.a.	1.97	2.00	n.a.
Wholesale	1.45		1.33	1.40	n.a.	1.38	1.45	n.a.
Retail	1.48		1.36	1.42	n.a.	1.45	1.43	n.a.
Automotive	2.05		1.51	1.84	n.a.	1.88	1.70	n.a.

1. Ratio of end-of-period inventories to average monthly sales for the period.

2. Highs are specific to each series and are not necessarily coincident.

(r) Revised estimates.

(p) Preliminary estimates.

particular, the book value of inventories in the primary metals and machinery industries have been rising since May. At the same time shipments and orders in these industries have remained weak, an indication that part of this accumulation was probably unintended.

Stocks of retail stores excluding the automotive grouping showed sizable increases in August, rising at an annual rate of \$4.1 billion and constant dollar basis. A substantial part of this buildup occurred at general merchandise stores where sales have been relatively unchanged in recent months. Stocks of automotive stores declined at a \$2.8 billion annual rate in August, reflecting the initial success of rebates and other promotional sales efforts. Auto dealers' stocks of new cars were reduced further in September, but they rose in October with the sharp drop in sales.

#### Federal Government

Final figures for the budget for FY1981 show receipts of \$602.6 billion, outlays of \$660.5 billion, and a deficit of \$57.9 billion. The deficit was \$2.3 billion higher than estimated by the Administration in the July Mid-Session Review. To a large extent the underestimate reflects the effects of slower economic activity on receipts. (An attached table shows the evolution of budget estimates for FY1981.)

In the final quarter of the fiscal year, total expenditures on an NIA basis were \$3.1 billion higher, at an annual rate, than projected at the time of the Mid-Session Review. Purchases of nondefense goods were higher primarily because of acquisitions for the Strategic Petroleum Reserve. Transfer payments were lower than forecast in the Mid-Session



THE FISCAL YEAR 1981 BUDGET  
(Unified budget; billions of dollars)

	Time of Budget Estimate						Actual
	Jan. 1980	Mar. 1980	July 1980	Jan. 1981	Mar. 1981	July 1981	
<u>Outlays</u>							
Defense	146.2	150.5	157.5	161.1	162.1	160.4	159.7
Int. Affairs	9.6	10.1	10.3	11.3	11.3	11.8	11.1
Energy	8.1	6.9	7.2	8.7	9.3	9.5	10.6
Agriculture	2.8	2.0	2.2	1.1	1.2	4.0	5.6
Interest (net)	67.2	68.4	67.6	80.4	77.2	83.1	82.6
Comm. & Housing	0.7	0.4	0.7	3.5	3.2	4.2	4.0
Income Security <sup>1</sup>	336.1	334.0	346.5	352.1	349.4	348.7	348.4
Fiscal Ass't.	9.6	7.4	7.3	6.9	6.8	6.9	6.6
All Other <sup>2</sup>	35.5	31.8	34.5	37.6	34.7	32.6	31.8
Total	615.8	611.5	633.8	662.7	655.2	661.2	660.5

Receipts

Current Law	579.0	589.2	591.6	605.0	608.8	607.8	n.a.
Total	600.0	628.0	604.0	607.5	600.3	605.6	602.6

<u>Deficit</u>	-15.8	+16.5	-29.8	-55.2	-54.9	-55.6	-57.9
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(percentage)

Economic Assumptions,  
Calendar Year 1981

GNP growth (Q4/Q4)	11.7	11.4	12.6	12.3	11.0	11.8
Unemployment rate	7.4	7.3	8.5	7.7	7.7	7.5
CPI (Q4/Q4)	8.7	9.0	9.8	12.6	10.5	8.6
Bill rate (annual average)	9.0	9.5	9.0	13.5	11.1	13.6

1. Education, Training and Employment, Social Services, Health, Income Security and Veterans Benefits.

2. Science, Natural Resources, Transportation, Community Development, Justice, General Government, Offsetting Receipts and Allowances.

Review, but this was almost exactly offset by higher subsidies. Receipts were less than previously projected, reflecting the downward revision in the level of unified budget receipts and some technical factors.

Congressional action on the budget for FY1982 continues to lag, causing forecasts for this fiscal year's deficit to become increasingly uncertain. The House has completed action on 11 of the 13 appropriation bills. The Senate, however, has passed only five major bills, which generally exceed the targets set by the Administration in September.

#### State and Local Government

Purchases by state and local governments in real terms have fallen further in recent months, as outlays continue to be constrained by the ongoing reduction in federal grants-in-aid, sluggish growth of tax receipts, and high cost of financing construction projects. The decline in construction spending has been particularly sharp, and the value of new construction in real terms in the third quarter was 22 percent below its extremely high first-quarter level. For the first nine months of the year, real construction outlays were 5-1/2 percent below the average for 1980. Outlays for education buildings and for water and sewer projects were well below 1980 levels, while highway and street construction was higher due to a boost in road-building last winter.

Preliminary data indicate that state and local employment edged up about 20,000 in October. Overall, state and local employment has weakened over the last half year. In the past 6 month period, payrolls fell around 400,000 after six quarters of little change. The phase-out of federally financed public service jobs accounted for most of the

decrease over the last half-year; almost 300,000 CETA jobs have been eliminated since February.

### Prices

The slowdown in inflation so far this year has been most evident in markets for commodities rather than services. In recent months, retail food prices have risen more rapidly and increases continued to be sizable for both homeownership and consumer services.

Producer prices of finished goods advanced 0.6 percent in October, following a 0.2 percent rise in September. This swing is exaggerated by the treatment of car and truck prices in the PPI. The September index was lowered significantly as liquidation allowances for 1981 models were included in car and truck prices, and the October index was boosted by inclusion of 1982 models at higher prices. Nevertheless, over the past two months price increases for many other finished consumer goods and for a broad range of capital equipment items have been below those earlier in the year.

At the intermediate level, the index for materials other than food and energy rose just 0.1 percent in October. The weakness in commodity prices may be starting to reflect the recent declines in import prices, as well as slack demand.

At the consumer level in September, a sharp rise in home financing costs (3.2 percent) was partly responsible for the high September CPI rate. The total index, excluding house purchase and mortgage interest costs, advanced 0.8 percent, which is close to the average monthly advance in this measure during the past year. Mortgage costs in the September index were boosted by the increases of FHA/VA ceiling rates

## RECENT CHANGES IN PRODUCER PRICES

(Percentage change at annual rates; based on seasonally adjusted data)<sup>1</sup>

	Relative importance Dec. 1980	1980	1981				
			Q1	Q2	Q3	Sept.	Oct.
Finished goods	100.0	11.8	13.3	6.8	2.8	2.2	6.6
Consumer food	23.1	7.5	1.6	1.8	5.6	.5	-2.8
Consumer energy	12.0	27.8	66.8	4.5	-7.0	6.9	-4.4
Other consumer goods	44.6	10.4	7.8	8.8	3.1	2.7	12.4
Capital equipment	20.3	11.4	12.0	9.8	5.7	.4	10.8
Intermediate materials <sup>2</sup>	93.6	12.4	14.3	7.7	4.3	3.1	.4
Exc. energy	77.3	10.1	8.0	8.8	6.7	6.3	1.3
Crude Materials							
Food	57.7	8.6	-23.1	8.6	-12.1	-30.2	-30.5
Energy	26.8	26.9	110.0	4.3	1.6	14.2	-14.2
Other	15.5	7.5	-36.7	1.7	3.2	-10.1	2.7

1. Changes are from final month of preceding period to final month of period indicated.

2. Excludes materials for food manufacturing and animal feeds.

RECENT CHANGES IN CONSUMER PRICES<sup>1</sup>(Percentage change at annual rates; based on seasonally adjusted data)<sup>2</sup>

	Relative importance Dec. 1980	1980	1981			
			Q1	Q2	Q3	Sept.
All items	100.0	12.4	9.6	7.4	13.5	13.9
Food	17.3	10.2	2.1	-.1	10.9	11.7
Energy	10.8	18.1	49.1	4.7	3.0	2.9
Homeownership	25.8	16.5	3.1	16.9	21.3	19.6
All items less food, energy, and homeown- ership <sup>3</sup>	49.6	9.9	8.0	8.8	12.4	12.3
Used cars	3.0	18.3	6.5	4.9	44.2	48.3
Other commodities <sup>3</sup>	20.5	8.1	6.6	7.8	6.8	5.9
Other services <sup>3</sup>	26.1	10.3	10.1	10.0	13.3	11.3
Memorandum:						
Experimental CPI <sup>4</sup>	100.0	10.8	11.5	5.7	10.3	9.6

1. Based on index for all urban consumers (CPI-U).

2. Changes are from final month of preceding period to final month of period indicated.

3. Includes the home maintenance and repair component of homeownership costs.

4. BLS experimental index for "All items"--CPI-U-X1--which uses a rent substitution measure for homeownership costs.

from 15-1/2 to 17-1/2 percent. A subsequent reduction to 16-1/2 percent should have a moderating influence on the October index.

Food prices at the consumer level rose rapidly in September, as an earlier increase in livestock prices was passed on to the retail level. However, producer prices for finished foods were little changed in September and October, and a renewed price decline has been evident at the farm level since mid-summer. These developments suggest that inflation rates for consumer foods should moderate in the near-term. Although gasoline prices rose in September for the first time since March, the energy grouping continued to register only a small increase.

If food, energy, and homeownership are excluded, the September and third-quarter rates for the remaining half of the CPI exhibit marked increase over the pace of the first half of this year. Services, which do not slow in the first half, account for much of the recent acceleration. The third-quarter increase for services includes exceptional adjustments in mass transit fares and telephone rates as well as the large once-a-year hike in school tuition and related costs. Medical services also have risen faster in the third quarter than during the first half of the year.

#### Wages and Labor Costs

Wage rates, as measured by the hourly earnings index for production workers, rose at an 8.2 percent annual rate in the third quarter, and the preliminary data for October show another relatively small increase. This index has risen at an 8-3/4 percent annual rate over the first 3 quarters of 1981, a deceleration of almost 1 percentage point from last year's rapid advance. Increases in hourly compensation for all persons working

SELECTED MEASURES OF COMPENSATION, PRODUCTIVITY,  
AND COSTS (NONFARM BUSINESS)  
(Seasonally adjusted annual rates)

	1981						
	1980	Q1	Q2	Q3	Sept.	Oct.	1st three quarters
<u>Hourly Earnings Index - production workers<sup>1</sup></u>							
Total private nonfarm	9.6	9.6	8.3	8.2	5.6	2.4	8.7
Manufacturing	10.9	9.3	9.7	8.5	10.2	3.4	9.2
Durable	11.6	9.4	9.6	8.6	9.0	4.3	9.2
Nondurable	9.8	9.1	10.0	8.2	12.3	1.9	9.1
Contract construction	7.6	9.2	4.9	8.8	3.0	9.7	7.6
Transportation and public utilities	9.4	9.4	11.0	6.9	- .3	5.9	9.1
Total trade	8.8	9.6	7.1	7.7	8.2	-4.0	8.1
Service	9.5	9.8	8.5	8.6	2.2	2.5	9.0

<u>Labor Productivity and Costs - all persons<sup>1</sup></u>							
Compensation per hour	10.1	11.6	9.6	9.4	n.a.	n.a.	10.2
Output per hour	.1	4.3	1.4	-2.2	n.a.	n.a.	1.1
Unit labor costs	9.9	7.0	8.1	11.9	n.a.	n.a.	9.0

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Addendum:

<u>Employment Cost Index, wages and salaries - all persons<sup>2</sup></u>							
Total	9.0	10.5	8.4	n.a.	n.a.	n.a.	n.a.
By Occupation:							
White collar	8.7	11.7	8.4	n.a.	n.a.	n.a.	n.a.
Blue collar	9.6	8.3	9.1	n.a.	n.a.	n.a.	n.a.
Service Workers	8.1	12.2	5.5	n.a.	n.a.	n.a.	n.a.
By Bargaining Status:							
Union	10.9	8.0	10.3	n.a.	n.a.	n.a.	n.a.
Nonunion	8.0	11.4	7.5	n.a.	n.a.	n.a.	n.a.

1. 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.

2. Percent change from final month of previous period, compounded. Seasonal adjustment performed by FRB staff.

NEGOTIATED WAGE RATES CHANGES  
Under Major Collective Bargaining Settlements<sup>1</sup>

	1979	1980	1981 1st 3 Qs
<b>All Industries</b>			
First-year adjustments	7.4	9.5	11.5
Average over life of contract	6.0	7.1	9.3
Workers affected (in thousands)	3492	3787	1480
<b>Contracts with escalator provisions</b>			
First-year adjustments	6.2	8.0	7.9
Average over life of contract	4.6	5.0	6.4
Workers affected (in thousands)	2028	2268	306
<b>Contracts without escalator provisions</b>			
First-year adjustments	9.1	11.7	12.4
Average over life of contract	8.0	10.3	10.0
Workers affected (in thousands)	1464	1489	1174

1. Contracts covering 1,000 or more workers; estimates exclude potential gains under cost-of-living clauses.

in the private nonfarm sector of the economy--a more comprehensive measure of wage and supplement costs--have averaged about the same rate so far this year as in 1980. The wage component of compensation has slowed somewhat, but the increase in social security taxes has added about 0.9 percentage points (annual rate) to the rise over the first three quarters of this year.

Due to the relatively light bargaining calendar this year, new settlements have played a smaller than usual role in wage developments. On the other hand, contractual changes in previously negotiated agreements are of growing importance in numerous key industries. Recently, wage concessions have been granted by union and management employees at several major airlines and at financially-troubled firms in the motor vehicle parts, rubber, and steel industries. Negotiated changes in work rules that could bolster productivity are also becoming more frequent.

Labor productivity in the nonfarm business sector declined at a 2.2 percent annual rate in 1981-Q3, primarily reflecting the drop in output. Since the business cycle peak in 1980-Q1, output per hour has risen at a 0.6 percent annual rate. This poor productivity performance has offset little of the rise in hourly compensation. As a result, unit labor costs in the nonfarm sector rose at almost a 12 percent rate in 1981-Q3 and at a 9 percent annual rate in the first three quarters of 1981.



## APPENDIX II-A\*

### PLANNED CHANGES IN THE CPI HOMEOWNERSHIP MEASURE

The measurement of owner-occupied housing costs for the consumer price index will be changed from the present method, based on house prices and mortgage interest rates, to a rental equivalence index, according to an announcement on October 27 by the Bureau of Labor Statistics (BLS). This change will be introduced in two stages: first, in January 1983, in the index for all urban consumers (CPI-U); and second, in January 1985, in the index for wage earners and clerical workers (CPI-W).<sup>1</sup> As occurs in major CPI revisions, the revised procedure will not be extended back to earlier periods, and thus the switch to these new measures will not affect the past index levels but only those subsequent to the change. The old series will continue to be constructed for a six-month overlap period in each case.

The rental equivalence measure to be included in the CPI-U in 1983 represents an initial refinement of the current CPI rent index. This work, already underway, essentially involves reweighting of the rent sample to better represent owner-occupied housing and some changes in calculation procedures. Augmentation of the rent sample and other improvements derived from BLS research will require more time. Depending on the continued availability of funds, BLS will introduce these improvements in part by 1985 and more completely by the time of the next CPI revision, probably in 1986.

According to BLS, the experimental "rent substitution" measure (CPI-U-X1)--now reported in the monthly CPI release with four other experimental measures--will be emphasized more in the future. In this series, the current CPI rent index<sup>2</sup> is substituted for the homeownership measure. Almost as important, its weight, which is based on the estimated rental value of owner-occupied housing,<sup>3</sup> is well below that of the homeownership component of the CPI-U. As seen in the chart that follows, the rent substitution measure for "All items" rises substantially less than the current published index in periods such as 1979-80 and recent months when mortgage rates and/or house prices rise rapidly and boost the CPI-U homeownership measure. The opposite occurs when the CPI measure of mortgage rates or house prices declines (1980-Q3, 1981-Q1).

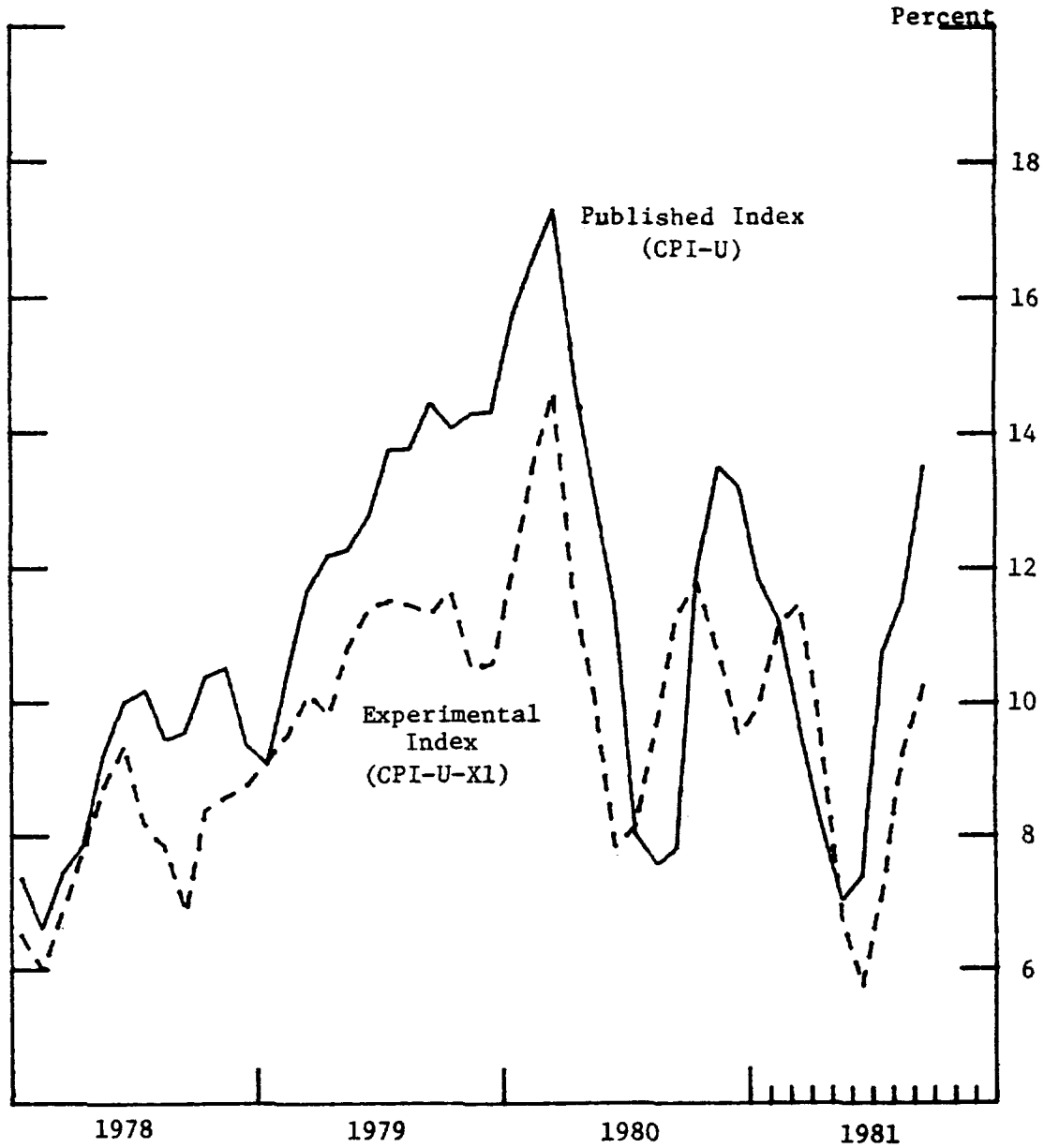
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1. The CPI-W refers to the traditional CPI population. In 1978, at the time of the last major CPI revision, the BLS began to publish the more comprehensive CPI-U, which covers the expenditures of the urban civilian population.
2. Which reflects housing typically occupied by renters.
3. Derived from information in the 1972-73 Consumer Expenditures Survey.

A change in the homeownership measure was first proposed before the last CPI revision, but was postponed to allow more time for research and discussion. According to BLS, the timing of the announcement and of the effective dates for introducing the changes now planned was influenced by several considerations, particularly by the need for substantial advance notice to the public. The early change in the CPI-U (January 1983) is a response to recent tax legislation that indexes tax brackets and personal exemptions to this measure. The new tax brackets must be announced in December 1984 and will be based on CPI-U data over the previous two years. Most private contracts, as well as government transfer payments, are linked to the CPI-W. In view of the number and duration of such contracts, a longer advance notice was considered advisable for this series. Factors in hastening the BLS decision include the increasing public concern about the validity of the present homeownership measure as well as the serious erosion of the data base for this measure associated with recent developments in the mortgage and housing markets.

CHANGES IN CONSUMER PRICES:  
 PUBLISHED AND EXPERIMENTAL INDEXES<sup>1</sup>  
 (3-month changes, at compound annual rates)



1. Experimental index measures owner-occupied housing costs on a rental equivalence basis, but using the current CPI rent index.

SELECTED FINANCIAL MARKET QUOTATIONS<sup>1</sup>  
(Percent)

	1981				Change from:	
	Julv High	FOMC Aug. 18	FOMC Oct. 6	Nov. 9	Julv High	FOMC Oct. 6
<u>Short-term rates</u>						
Federal funds <sup>2</sup>	19.93	18.19	15.46	13.90 <sub>p</sub>	-6.03	-1.56
Treasury bills						
3-month	15.72	15.72	13.90	11.19	-4.53	-2.71
6-month	15.42	15.62	14.12	11.63	-3.79	-2.49
1-year	14.52	14.74	13.83	11.48	-3.04	-2.35
Commercial paper						
1-month	18.23	18.02	14.84	12.77	-5.46	-2.07
3-month	17.68	17.63	15.07	12.59	-5.09	-2.48
6-month	16.86	17.09	14.97	12.25	-4.61	-2.72
Large negotiable CDs <sup>3</sup>						
1-month	18.55	18.14	15.14	13.03	-5.52	-2.11
3-month	18.38	18.08	15.57	12.97	-5.41	-2.60
6-month	18.16	18.20	15.81	12.90	-5.26	-2.91
Eurodollar deposits <sup>2</sup>						
1-month	19.49	18.66	16.00	14.14 <sub>p</sub>	-5.35	-1.86
3-month	18.91	18.73	17.03	14.33 <sub>p</sub>	-4.58	-2.70
Bank prime rate	20.50	20.50	19.00	17.00	-3.50	-2.00
<u>Intermediate- and long-term rates</u>						
U.S. Treasury (constant maturity)						
3-year	15.75	15.90	15.78	13.25	-2.50	-2.53
10-year	14.71	14.79	15.14	13.39	-1.32	-1.75
30-year	13.96	13.95	14.60	13.56	-.40	-1.04
Municipal (Bond Buyer)	11.44	11.94 <sup>4</sup>	12.93 <sup>4</sup>	12.44	1.00	-.49
Corporate Aaa						
New issue	16.73	--	--	17.17 <sub>p</sub> <sup>5</sup>	.44	--
Recently offered	16.55	16.63 <sup>6</sup>	17.72 <sup>6</sup>	16.45 <sub>e</sub>	-.10	-1.27
Primary conventional mortgages	17.11	17.27 <sup>6</sup>	18.28 <sup>6</sup>	18.37 <sup>6</sup>	1.26	.09
	1980	1981		Percent change from:		
	Dec. 31	High	FOMC Oct. 6	Nov. 9	1981 High	FOMC Oct. 6
<u>Stock Prices</u>						
Dow-Jones Industrial	963.99	1,024.05	856.26	855.21	-16.5	-.1
NYSE Composite	77.86	79.14	69.03	71.67	-9.4	3.8
AMEX Composite	348.99	380.36	308.69	325.29	-14.5	5.4
NASDAQ (OTC)	202.34	223.47	185.87	199.92	-10.5	7.6

1. One-day quotes except as noted.

2. Averages for statement week closest to date shown.

3. Secondary market.

p--Preliminary

4. One-day quotes for preceding Thursday.

5. Average for preceding week.

6. One-day quotes for preceding Friday.

e--Estimated.

## DOMESTIC FINANCIAL DEVELOPMENTS

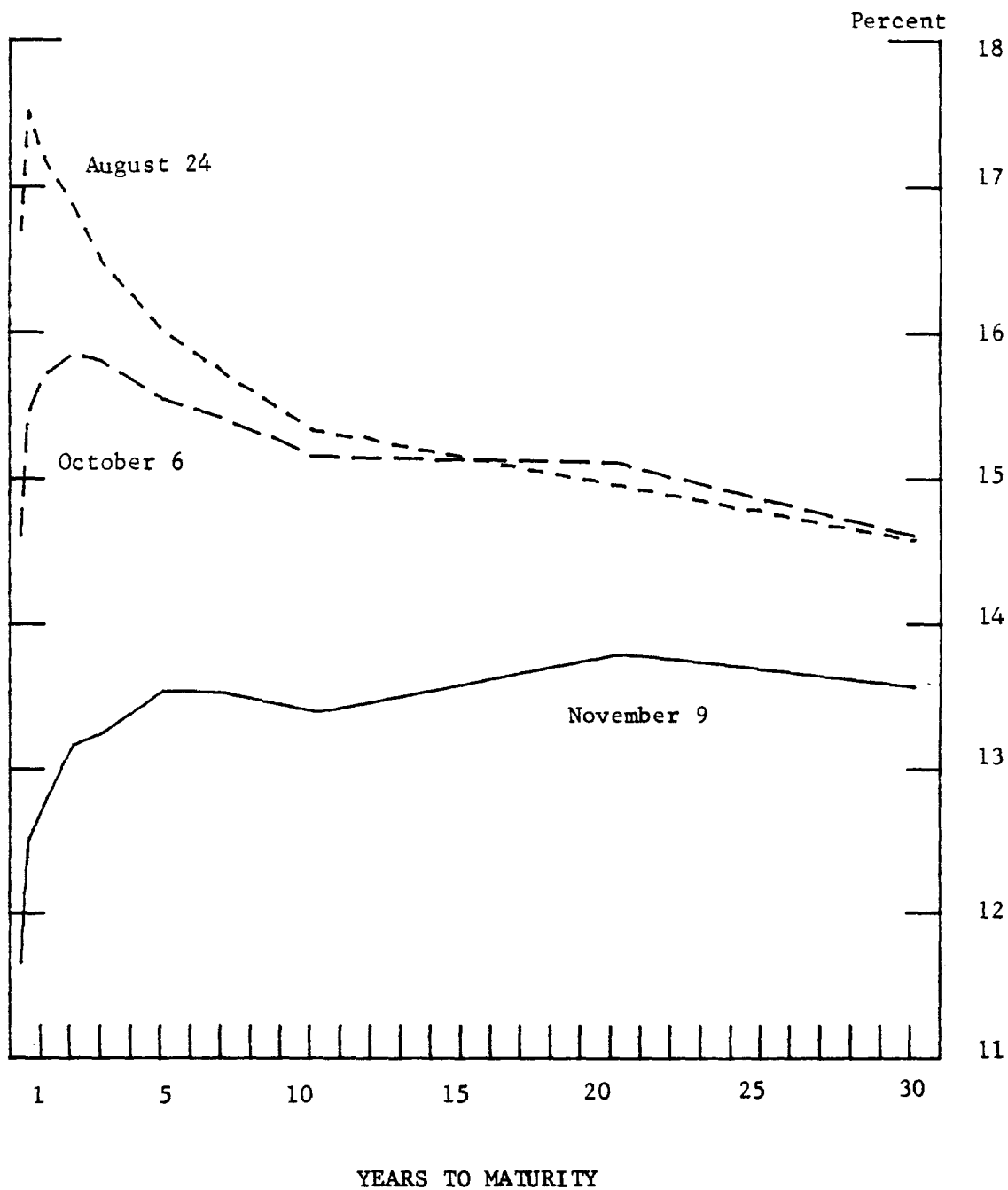
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M1-B posted a small increase in October, about offsetting its September contraction. M2 also strengthened, reflecting both the upturn in M1-B and bigger inflows to the nontransactions component following the introduction of the tax-exempt all savers certificate on October 1. The expansion of the monetary aggregates was, nonetheless, less rapid than provided for by the System's injection of nonborrowed reserves and money market conditions eased considerably over the intermeeting period.

Most short-term market rates of interest have fallen 2 to 2-3/4 percentage points, drifting lower in October and declining sharply further in early November. The basic discount rate was lowered to 13 percent, and banks cut their prime lending rate 2 percentage points to 17 percent. Long-term yields generally have fallen by around 1/2 to 1-3/4 percentage points, and home mortgage rates have eased a bit from record highs posted in mid-October. Although market sentiment has been improved by signs of near-term easing of money and credit demands, concerns remain about the long-range implications of federal budget policy. Such concerns are reflected in the upward sloping yield curve that has emerged recently.

The overall credit demands of nonfinancial businesses moderated in October. Firms borrowed less heavily from banks and in the commercial paper market, and their issuance of long-term securities remained limited. As the bond market rallied in early November, public offerings picked up, likely reflecting long-delayed debt restructuring. Available data suggest that household borrowing in the mortgage market has continued to shrink, and consumer installment credit, which had been buoyed for a time by stronger car sales, likely weakened substantially in October. Meanwhile,

TREASURY SECURITY YIELD CURVES



the government sector placed heavy demands on credit markets as the Treasury began financing a record quarterly unified plus off-budget deficit, and state and local governmental borrowing remained substantial.

#### Monetary Aggregates and Bank Credit

M1-B, adjusted for shifts to NOW accounts, grew at only a 3-1/2 percent annual rate in October. The persistent weakness in the growth of M1-B in the face of declining interest rates appears attributable both to a slowing of nominal GNP growth and to continued intensive efforts to economize on cash balances as interest rates still remain at historically high levels. As summarized in an appendix to this section, the findings of a recent Reserve Bank survey indicate a considerable spreading of sophisticated cash management techniques this year--with more in store for the future.

M2 advanced at a 9-1/4 percent annual rate in October, up from the comparatively slow pace of the previous month and the third quarter as a whole. The relatively small M1-B component accounted for a disproportionately large part of the acceleration in the broader aggregate as growth in the nontransactions component registered a rather modest pick-up despite the advent of the all savers certificate (ASC).

Sales of ASCs were sizable, but the bulk of these funds appears to have shifted from other small time deposits, particularly 6-month MMCs. Survey results indicate that ASCs had attracted \$27-3/4 billion during the first part of October.<sup>1</sup> Meanwhile, MMCs ran off by a record amount,

1. The data cover deposit flows over the first two weeks of October for commercial banks, MSBs and credit unions, and over the first twenty days of the month for S&Ls. By institution, the \$27-3/4 billion in ASCs was divided as follows: \$13-1/2 billion at S&Ls; \$10-1/4 billion at commercial banks; \$2-3/4 billion at MSBs; and \$1-1/4 billion at credit unions.

III-4  
MONETARY AGGREGATES  
(Based on seasonally adjusted data unless otherwise noted)<sup>1</sup>

	1981						Q4 '80 to Oct. '81 <sup>e</sup>
	Q1	Q2	Q3	Aug.	Sept.	Oct. <sup>e</sup>	
---- Percentage change at annual rates ----							
<u>Money stock measures</u>							
1. M1-A	-20.8	-5.3	-3.7	3.0	-7.6	3.0	-8.1
2. (Adjusted) <sup>2</sup>	(-1.7)	(5.1)	(-1.5)	(6.5)	(-5.2)	(2.8)	0.6
3. M1-B	4.9	8.7	0.2	7.3	-2.8	3.6	4.2
4. (Adjusted) <sup>2</sup>	(-0.8)	(5.3)	(-0.7)	(6.9)	(-4.0)	(3.4)	1.3
5. M2	8.3	10.6	7.1	11.6	6.4	9.2	8.9
6. M3	12.4	10.6	10.2	13.4	8.2	6.5	10.9
<u>Selected components</u>							
7. Currency	5.5	7.9	5.0	4.0	-1.0	3.0	5.5
8. Demand deposits	-32.9	-11.8	-8.0	1.5	-11.7	3.6	-14.1
9. Other checkable deposits	372.3	107.4	21.5	31.3	23.7	6.6	180.0
10. M2 minus M1-B (11+12+13+16)	9.4	11.3	9.4	13.0	9.4	11.0	10.5
11. Overnight RPs and Eurodollars, NSA <sup>3</sup>	0.0	58.9	12.8	27.6	-110.7	-108.8	1.7
12. Money market mutual fund shares, NSA	84.5	113.7	87.8	99.2	94.9	72.7	127.6
13. Commercial banks	6.0	4.2	6.8	10.8	6.3	10.4	6.4
14. savings deposits	-30.5	-11.9	-19.6	-29.9	-21.7	-19.8	-19.5
15. small time deposits	30.2	13.4	21.0	30.9	20.1	24.0	23.6
16. Thrift institutions	3.5	-0.3	-2.9	-3.9	0.2	4.0	0.3
17. savings deposits	-29.6	-12.6	-23.0	-28.0	-23.3	-22.4	-20.5
18. small time deposits	19.0	4.7	5.1	5.7	8.6	13.7	10.1
19. Large time deposits	39.6	10.3	24.6	26.0	7.7	-3.6	22.6
20. at commercial banks, net <sup>4</sup>	40.6	10.1	26.6	26.3	5.3	-8.2	22.7
21. at thrift institutions	34.7	11.2	15.1	22.3	21.9	19.1	21.8
22. Term RPs, NSA	18.1	12.2	41.6	5.5	82.4	-33.4	19.2
--Average monthly change in billions of dollars--							
<u>MEMORANDA:</u>							
23. Managed liabilities at commercial banks (24+25)	4.3	8.8	6.3	11.3	0.0	-5.4	5.8
24. Large time deposits, gross	5.1	7.5	7.0	9.5	2.8	-1.2	6.1
25. Nondeposit funds	-0.8	1.3	-0.7	1.8	-2.8	-4.2	-0.3
26. Net due to related foreign institutions, NSA	-1.6	0.5	0.9	4.2	-1.3	-4.6	-0.6
27. Other <sup>5</sup>	0.7	0.8	-1.7	-2.4	-1.6	0.4	0.3
28. U.S. government deposits at commercial banks <sup>6</sup>	1.1	-0.3	-0.7	-2.7	-0.3	3.5	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 subsequent months.
  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. Excludes retail RPs.
  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.
- e--estimated.



presumably reflecting large transfers into ASCs and into SSCs, which also showed strong gains.<sup>1</sup> A comparatively small portion of the flows to ASCs appears to have been diverted from savings accounts, which declined at a slightly slower pace than in September.

The amount moving into ASCs from retail RPs, which contracted by \$2-3/4 billion through mid-October to a level of about \$11-1/2 billion, also appears to have been small. The volume of retail RPs purchased with the intent to roll over into ASCs evidently was smaller than expected, and the bulk of these instruments represents high-yielding, low-denomination alternatives to regulated deposits. Finally, as expected, MMMFs seem to have been a minor source of funds for ASCs; expansion in MMMFs last month showed only a moderate slowing from the strong September pace.

The overnight RP component of M2 declined by \$2-1/4 billion (not seasonally adjusted) in October, following an even larger contraction in September. The weakness in RPs may reflect in part reduced needs by bank dealer departments, whose securities inventories declined in both September and October. Moreover, banks may have experienced collateral constraints as U.S. government demand and note balances rose substantially over the two-month period.

Growth of M3 decelerated to a 6-1/2 percent annual rate in October, the slowest rate of expansion in this measure in a year and a half. The slowdown reflected primarily a runoff in large time deposits at com-

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1. Flows into SSCs have surged since the August 1 removal of the cap on ceiling rates, even though survey results indicate that the proportion of banks and MSBs paying the maximum allowable rates has fallen to about 60 percent. Of those institutions, 85 percent paid returns on SSCs that were within 2 percentage points of the 16 percent nominal ceiling rates in September. About 80 percent of S&Ls were paying ceiling rates on SSCs in September.

III-6  
 COMMERCIAL BANK CREDIT AND SHORT- AND INTERMEDIATE-TERM BUSINESS CREDIT  
 (Percentage changes at annual rates, based on seasonally adjusted data)<sup>1</sup>

	1980		1981				Oct. 80	Oct. 81 <sup>e</sup>	
	Q3	Q4	Q1	Q2	Q3	Aug.	Sept.		Oct. <sup>e</sup>
----- Commercial Bank Credit -----									
1. Total loans and investments at banks <sup>2</sup>	12.9	14.5	7.8	8.2	9.0	10.1	10.6	8.1	9.8
2. Investments	20.7	11.8	10.5	6.5	3.9	4.9	0.7	8.4	7.9
3. Treasury securities	39.1	11.1	14.8	15.7	-5.7	-10.0	-18.1	-5.1	7.3
4. Other securities	11.5	12.3	8.0	1.7	9.1	13.1	10.8	15.5	8.1
5. Total loans <sup>2</sup>	10.2	15.5	6.8	8.9	10.8	12.0	14.0	7.9	10.5
6. Business loans <sup>2</sup>	15.5	21.0	6.5	11.9	20.2	22.1	18.3	13.0	15.0
7. Security loans	-10.2	60.1	27.3	53.2	-54.5	-132.7	47.5	19.6	18.4
8. Real estate loans	4.6	11.0	9.4	7.3	8.5	10.1	9.2	6.9	9.0
9. Consumer loans	-7.6	-0.2	-1.4	-1.4	0.0	-1.4	1.4	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)	9.0	14.2	13.7	15.8	26.6	29.6	26.9	n.a.	n.a.
11. Business loans net of bankers acceptances	14.5	24.2	5.6	10.5	22.2	26.0	20.6	12.7	15.4
12. Commercial paper issued by nonfinancial firms <sup>3</sup>	-19.7	-6.2	29.5	42.2	59.4	76.7	87.0	7.0	38.6
13. Sum of lines 11 & 12	10.3	20.7	8.2	14.1	26.6	32.0	28.7	11.9	17.9
14. Line 13 plus loans at foreign branches <sup>4</sup>	9.8	19.3	11.3	14.0	28.4	33.8	30.2	15.5	19.4
15. Finance company loans to business <sup>5</sup>	-4.6	14.6	8.5	19.3	14.7	15.4	1.5	n.a.	n.a.
16. Total bankers acceptances outstanding <sup>5</sup>	21.0	-15.7	35.6	23.1	28.9	22.6	33.3	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.
- . Based on average of current and preceding ends of months.
- n.a.--not available. e--estimated.

mercial banks. Issuance of large time deposits by S&Ls moderated only slightly.

At commercial banks, total managed liabilities contracted in October, as inflows to core deposits and U.S. government deposits strengthened somewhat and bank credit expansion slowed. Indeed, net advances to foreign branches were boosted by \$4-1/2 billion in October. Banks continued, however, to increase their purchases of federal funds from Federal Home Loan banks.<sup>1</sup>

Bank credit grew in October at an 8 percent annual rate, down somewhat from the pace of the previous two months. Runoffs of Treasury securities abated and bank acquisitions of other securities accelerated, but loan expansion slowed markedly. Business loan growth, though still robust, dropped to its slowest pace since May. Expansion in security loans moderated as dealers trimmed their inventories, and real estate lending slowed.

#### Business Finance

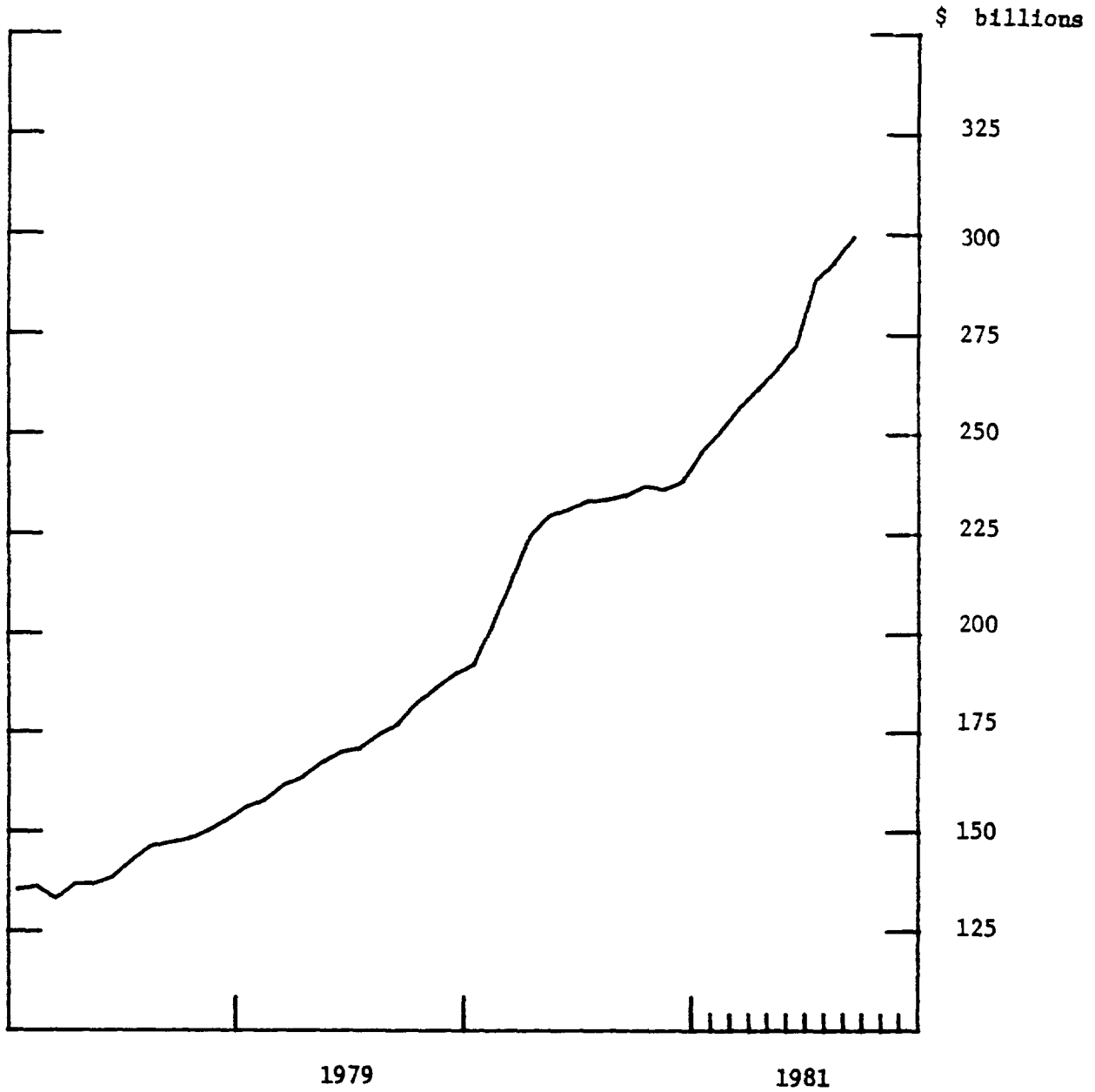
Overall borrowing by nonfinancial businesses appears to have moderated in October from the relatively strong third-quarter pace. In short-term markets, the decline in business loan growth at banks was accompanied by a sharp reduction in net issuance of nonfinancial commercial paper. The deceleration in bank lending to businesses reflected a net decline in such loans at foreign-related institutions, after several months of rapid expan-

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1. In the past two months, some improvement in deposit flows coupled with reduced mortgage lending has enabled S&Ls also to rely less on managed liabilities--FHLB advances in particular. The decline in advances was unanticipated, leading to a buildup in FHLB liquidity to historically high levels and an accompanying increase in federal funds sales by these institutions.

III-8  
UNUSED C&I LOAN COMMITMENTS AT SELECTED  
LARGE COMMERCIAL BANKS

(billions of dollars, seasonally adjusted)



sion, as well as slower growth at large banks.<sup>1</sup> Latest data available indicate that unused business loan commitments at large banks increased significantly again in September. The continued brisk expansion of commitments in part may have reflected attempts by firms to ensure access to credit in the event that conditions in long-term markets remain unfavorable or banks decide to become more selective in their lending in a weakening economy.

The volume of public corporate bond offerings continued low in October, particularly for industrial and financial corporate issues, owing to the high level of long-term rates. Offerings by utilities have held up quite well, but even in this sector several sizable issues were postponed in October when market conditions deteriorated temporarily. Private placement activity also is estimated to have remained sluggish in October, as life insurance companies apparently have continued to respond to the potential for liquidity pressures by directing a larger portion of their new investments into more liquid instruments.

Share prices have risen somewhat over the intermeeting period; nevertheless, the broad indexes are still well below their recent peak levels of mid-August. Because of the weak market conditions, new equity offerings in October totaled only \$700 million, seasonally adjusted, just half of the already reduced pace of the third quarter.

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1. The weakness at large banks may partly reflect the wide spread of the prime rate over the London Interbank Offered Rate (LIBOR). Many large banks now include LIBOR as a pricing option in loan agreements with large corporate customers, and some report that they often book or rebook loans abroad when customers elect the LIBOR option. Accordingly, with the prime-LIBOR spread remaining wide in October, lending to U.S. residents by foreign branches of domestically chartered banks picked up from the already rapid pace of recent months. In addition, the weakness in business lending at large banks also reflects Dupont's partial repayment of the loan it took down in August to finance its acquisition of Conoco. Repayment was reportedly made with the proceeds from new issues of commercial paper, which by November 6 totaled nearly \$2 billion.

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

	1981				
	Q1	Q2	Q3 <sup>p</sup>	Oct. <sup>p</sup>	Nov. <sup>f</sup>
----- Seasonally adjusted -----					
Corporate securities--total	5,942	6,886	3,615	3,400	4,700
Publicly offered bonds <sup>1</sup>	3,443	3,007	1,603	2,000	3,300
Privately placed bonds	523	843	609	700	700
Stocks	1,976	3,036	1,403	700	700
----- Not seasonally adjusted -----					
Publicly offered bonds--Total <sup>1</sup>	3,038	3,597	1,677	2,150	2,700
By Industry					
Utility	1,125	1,275	979	1,395	--
Industrial	1,289	1,383	465	275	--
Financial	624	939	333	480	--
By quality <sup>2</sup>					
Aaa and Aa	914	1,246	685	610	--
A and Baa	1,728	1,663	627	1,325	--
Less than Baa <sup>3</sup>	396	688	364	215	--
Memo items.					
Convertible bonds	439	491	150	155	--
Original discount bonds					
Par value	167	1,175	343	135	--
Gross proceeds	85	480	173	107	--
Stocks--total	1,889	2,850	1,403	900	800
By Industry					
Utility	499	1,012	486	386	--
Industrial	1,186	1,425	597	417	--
Financial	204	413	320	97	--

p--preliminary. f--forecast.

1. Total reflects gross proceeds rather than par value of original discount bonds.

2. Bonds categorized according to Moody's bond ratings.

3. Includes issues not rated by Moody's.

Government Finance

The combined unified and off-budget deficit of the federal government in the current quarter likely will be a record \$54 billion.<sup>1</sup> To finance this deficit, the Treasury's market borrowing requirements-- swollen by continuing redemptions of savings bonds and other nonmarketable securities--will amount to \$41 billion. The remainder will be covered by a reduction of the Treasury's cash balance and other means of finance.

It is expected that all of the increase in Treasury borrowing in the fourth quarter will be in the short-term area. The Treasury will likely tap the bill market for a record \$24-1/2 billion, while the volume of coupon financing probably will be about in line with other recent quarters. Thus far in the quarter, the Treasury has raised \$18 billion of net new money, including nearly \$4 billion in the recently completed mid-quarter financing.

Borrowing by federally sponsored credit agencies dropped off sharply in October to about half the pace of the third quarter. This decline reflected a net repayment of debt by the FHLBs in response to their high liquidity. FNMA raised \$1.8 billion in new money in October, about \$.3 billion of which was in Residential Financing Securities (one-year debentures that satisfy the requirements for depository institution investment of ASC proceeds). New yields on these instruments change daily. In October they averaged about the same as the investment yield on 1-year Trea-

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1. About \$12 billion of this figure is the result of an accelerated Social Security payment at the end of the quarter. January's payment will be issued on Thursday, December 31, since January 3 is a Sunday and the previous Friday is a holiday.

FEDERAL GOVERNMENT AND SPONSORED AGENCY FINANCING<sup>1</sup>  
 (Total for period; billions of dollars)

	FY81	Q3	<sup>f</sup> 04	Oct.	<sup>f</sup> Nov.
<u>Treasury financing</u>					
Combined surplus/deficit(-)	-78.9	-15.4	-53.9	-16.3 <sup>e</sup>	-13.6
Net marketable borrowings/ repayments(-)	88.9	22.5	41.0	10.6	11.5
Bills	23.0	4.6	24.6	5.7	5.5
Coupons	65.9	17.9	16.4	4.9	6.0
Nonmarketable borrowings/ repayments(-)	-9.5	-4.0	-2.5	-.4	-1.0
Other means of finance <sup>2</sup>	-2.7	-.7	7.8	3.7 <sup>e</sup>	-2.3
Change in cash balance	-2.3	+2.3	-7.6	-2.4	-5.4
<u>Federally sponsored credit agencies net cash borrowing<sup>3</sup></u>	37.5	15.4	6.4	2.8 <sup>e</sup>	1.4

1. Numbers reported on a not seasonally adjusted, payment 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.

e--estimated. f--forecast.

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

	1980	1981				
	Year	HI	<sup>e</sup> 03	Sept.	<sup>e</sup> Oct.	<sup>f</sup> Nov.
----- Seasonally adjusted -----						
Total	6.22	6.51	6.30	8.40	8.80	6.00
Long-term	4.03	3.71	3.60	4.60	3.30	3.30
Short-term	2.19	2.80	2.70	3.80	5.50	2.70
----- Not seasonally adjusted -----						
Total	6.22	6.41	5.95	7.60	7.30	6.00
Long-term	4.03	3.79	3.25	3.50	3.50	3.50
Short-term	2.19	2.62	2.70	4.10	3.80	2.50

e--estimate. f--forecast.



sury bills, giving institutions a sizable positive net return on ASC proceeds--as well as saving FNMA some money. The rate spread between other FNMA obligations and Treasury securities with similar maturities has narrowed from more than 125 basis points in late summer to around 100 basis points currently.

The gross issuance of municipal securities remained high in October. Volume in the long-term market totaled \$3-1/4 billion (seasonally adjusted)--only slightly less than the third-quarter average. A significant portion of the proceeds of long-term debt continued to be used for corporate-type purposes, such as pollution control. In the short-term sector, gross issuance swelled to \$5-1/2 billion with financings by HUD and the state of Washington accounting for more than three-quarters of this total. More generally, tax-exempt issuers appear to have stepped up their use of short-term financing in recent months, partly in response to the high level of bond yields. The outstanding volume of tax-exempt commercial paper (not included in the short-term totals in the table) has increased from about \$500 million in June to \$900 million in October.

Perhaps reflecting the heavy volume of short-term financing, short-term tax-exempt yields have fallen over the intermeeting period by less than half the decline in yields on Treasury issues of comparable maturity. The introduction of ASCs may also have been a factor in the relative stickiness of short-term municipal yields, but the effect was clearly less severe than some predictions had suggested.

III-14  
NET CHANGE IN MORTGAGE DEBT OUTSTANDING  
(Seasonally adjusted annual rates, in billions of dollars)

Mortgage debt	1980				1981		
	01	02	03	04	01	02	03 <sup>e</sup>
<u>By type of debt</u>							
Total	151	87	122	143	114	113	97
Residential	104	54	95	105	82	76	63
Other <sup>1</sup>	47	33	27	38	33	37	34
<u>By type of holder</u>							
Commercial banks	26	9	14	25	21	27	25
Savings and loans	26	1	39	46	30	23	9
Mutual savings banks	2	-1	-1	1	1	-1	*
Life insurance companies	17	14	11	9	10	9	9
FNMA and GNMA	11	7	3	8	*	1	8
GNMA mortgage pools	18	19	18	15	14	19	10
FHLMC and FHLMC pools	3	3	4	2	2	3	1
Other <sup>2</sup>	48	35	34	37	36	32	35

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.

SECONDARY MARKET FOR HOME MORTGAGES

Period	FNMA auctions of forward purchase commitments <sup>1</sup>						Yield on GNMA securities for immediate delivery <sup>2</sup> (percent)
	Conventional			FHA/VA			
	Amount (\$ millions)	Yield to FNMA (percent)	Yield to FNMA (percent)	Amount (\$ millions)	Yield to FNMA (percent)	Yield to FNMA (percent)	
	Offered	Accepted		Offered	Accepted		
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	316	168	19.22	257	182	19.23	17.46
Low	12	11	14.83	26	16	14.84	13.18
Sept. 21	--	--	--	--	--	--	16.33
28	35	21	19.22	43	30	19.23	17.46
Oct. 5	--	--	--	--	--	--	16.72
13	15	11	18.61	26	16	17.74	16.24
19	--	--	--	--	--	--	16.24
26	28	16	18.61	40	21	18.51	16.95
Nov. 2	--	--	--	--	--	--	15.93

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.

Mortgage Markets

Mortgage debt formation weakened further in the third quarter, dropping to the slowest pace since the second quarter of 1980. The deceleration was most pronounced in the residential sector, especially at S&Ls where net mortgage lending ground to a halt in September.

The near-term outlook for mortgage lending at thrift institutions worsened in September against a backdrop of record-high mortgage rates and weakened deposit flows. New commitments at S&Ls fell to \$2.9 billion (seasonally adjusted), the lowest monthly pace since the series originated in 1976, and loan commitments outstanding at these institutions declined further.

High mortgage rates are, of course, deterring loan originations more generally. The slow activity at mortgage bankers is reflected in part by weak demand in auctions of FNMA purchase commitments. The volume of conventional and FHA/VA mortgage commitments offered in the bi-weekly FNMA auctions in October was only about an eighth of the already depressed average volume per auction in 1980. In addition, there has been no commitment activity since mid-September in FNMA's auction for graduated-payment FHA mortgages.<sup>1</sup>

In addition, mortgage activity currently is being limited by the rapidly changing nature of mortgage instruments. Many mortgage lenders continue to be reluctant to make long-term fixed-rate mortgage loans, while consumers reportedly remain reluctant to accept the risks associ-

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1. Commitments under FNMA's new mandatory delivery program also have fallen sharply. The level of these commitments averaged only \$50 to \$60 million in September and October, down from an average of \$220 million in the previous three months.

III-16  
 CONSUMER INSTALLMENT CREDIT  
 (seasonally adjusted annual rates)

	1979	1980	1981			
			02	03	Aug.	Sept.
- - - - - Percent rate of growth - - - - -						
Change in outstandings -- total	14.0	0.5	7.1	9.6	10.7	10.5
By type:						
Automobile credit	14.5	0.0	1.0	18.8	21.1	22.5
Revolving credit	19.9	5.5	15.3	8.5	9.8	5.8
All other	12.1	-2.9	13.8	2.2	2.2	2.1
- - - - - Billions of dollars - - - - -						
Change in outstandings -- total	38.4	1.4	22.4	30.5	34.3	33.8
By type:						
Automobile credit	14.7	0.0	1.2	22.4	25.4	27.4
Revolving credit	8.6	2.9	8.8	5.0	5.9	3.5
All other	15.1	-1.5	12.4	3.1	3.0	2.9
By major holder:						
Commercial banks	18.2	-8.4	1.0	3.0	2.2	1.5
Finance companies	14.0	8.4	8.9	24.1	28.6	32.2
All other	6.2	1.4	12.5	4.1	3.5	0.2
Extensions -- total	324.8	305.9	344.1	348.3	346.8	353.1
By type:						
Automobile credit	93.9	83.0	87.9	103.7	102.9	110.1
Revolving credit	120.2	129.6	147.7	146.0	143.6	148.0
All other	110.7	93.3	108.5	98.6	100.3	95.0
Liquidations -- total	286.4	304.5	321.7	317.8	312.5	319.3
Memo: Ratio of liquidations to disposable income (percent)	17.5	16.7	16.2	15.6	15.3	15.5

ated with adjustable-rate mortgages, even with their typical 75 to 100 basis point markdown below fixed-rate loans. Nonetheless, recent FHLBB survey data indicate that almost 30 percent of all conventional first mortgage loans closed in early September were adjustable-rate instruments of some kind.

#### Consumer Credit

Consumer installment credit growth in September remained at about the August pace, up somewhat from the previous few months. The increase in credit growth--nearly all of which was at finance companies--resulted solely from a surge in automobile sales that was spurred by sales incentives programs. Judging from the plunge in new car sales in October and sluggish consumer spending generally, the expansion in consumer credit was likely quite weak last month. Weakness in consumer lending was evident at large weekly reporting banks in October.

Owing in part to the sluggish combined growth in installment and mortgage debt since early 1980, households in the aggregate have reduced their debt burdens. In particular, the ratio of debt repayments to disposable personal income declined in the third quarter to near its lowest level in 10 years.

APPENDIX III-A\*

FINANCIAL INNOVATION AND THE MONETARY AGGREGATES--  
SUMMARY OF BANK CONTACT GROUP RESPONSES

Owing to the persistent weakness of M1-B this year, Reserve Bank staff were asked to gather information regarding recent and prospective developments in the use of cash management techniques. The findings suggest that monetary growth in 1981 likely has not been substantially reduced by a spreading of deposit sweeping arrangements, in which transaction balances are kept from rising above predetermined levels by periodic transfers of funds to higher yielding assets; rather, the recent weakness in money demand appears to have reflected a more intensive use of cash management capabilities already in place as the year began--in particular, the ability of large corporations to sweep their own accounts, augmented by growing use of related cash management techniques such as cash concentration accounts, lock boxes, and deposit information systems. However, there were fairly widespread indications in most Federal Reserve districts that demands by smaller and medium sized firms for deposit-sweeping and other cash management services are growing rapidly. In response, a large number of regional banks apparently have begun to develop programs that will become available within the next year or two, some as soon as early next year. On the consumer side, growth in M1-B may also be affected in the near term by the growing popularity and aggressive promotion of consumer-oriented cash management services, and the continuing development by depository institutions of retail accounts offering high liquidity coupled with market-related rates of return.

Although the availability of cash management services and attractive substitutes for traditional transaction balances appear likely to expand considerably in coming months and years, it was beyond the scope of the survey to quantify the impact on M1-B. On the one hand, the relatively few very large corporations that already have assimilated fully available cash management techniques likely account for a considerable part of business transaction activities. On the other hand, many of the firms that have not yet adopted more sophisticated cash management techniques may do so rapidly.

Under the deposit-sweeping arrangements currently available to businesses--usually at large banks--balances typically are swept daily, apparently about mid-morning. Sweeps may also be made upon the instruction of the customer, and there are a few reports that deposits may be put into interest bearing alternatives up until noon or later. Swept funds typically are placed in RPs or very short-term--overnight to 5-day--commercial paper. Lesser amounts are said to be placed in CDs and Euro-dollar deposits, with the latter apparently available generally from large banks in the New York and Philadelphia areas, but obtainable elsewhere mainly to accommodate specific requests of customers. Although bank cash management services for smaller firms remain largely in the

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\* Prepared by Thomas F. Brady, Economist, Banking Section.

developmental state in most areas,<sup>1</sup> some banks already have begun to publicize and offer such services.

Arrangements to pay for deposit-sweeping services vary by customer and may involve fees, compensating balances (with required levels sometimes linked to market interest rates), spreads between what the swept funds earn and what the customer receives, or some combination of such procedures. It is thought that as deposit-sweeping services grow in popularity and usage, more standardized pricing may develop.

Banks discourage overdrafts at the wholesale level, and overdraft privileges do not appear to play a role in corporate cash management techniques. There has been, however, increasing demand for cash concentration accounts, lock boxes, and especially deposit information and projection services. The use of these techniques is reported to have increased considerably in the past year in several districts.

Consumers also may make use of cash management services or they may acquire various forms of highly liquid assets featuring market-related rates of returns. Currently, cash management accounts are offered by brokerage firms. They involve linking a demand deposit, a MMMF, and an account at the brokerage firm; account minimums are on the order of \$20,000. Excess cash from the brokerage account is swept weekly into the MMMF while checks written on the demand deposit account are funded by running down first excess cash in the brokerage account and then the MMMF. Credit is automatically extended to cover checks in excess of funds in the MMMF by making margin loans against the securities in the brokerage account. Most districts report that cash management accounts are being heavily promoted--including seminars to explain their use--and that they have elicited considerable interest.

A similar service has been developed very recently in which a NOW account and a MMMF are linked, with weekly deposit sweeping designed to maintain a \$2,500 average balance in the NOW account. Although this low minimum balance type of service currently is offered only by a few institutions, major credit card companies are reportedly in the process of providing client banks with similar capabilities. Such services reportedly will become operational early in 1982.

At least one bank is offering retail RPs connected to NOW accounts, with funds transferred between the NOW account and the RP at the customer's

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1. For example, a New York City bank has recently begun to offer a service to smaller firms which sweeps excess deposits into a MMMF daily. For a fee of \$100 per month, average balances are kept at \$6,500; a second plan, which maintains an average balance of \$20,000, has no fee attached. Another bank is reported prepared to sweep small firms' funds into RPs in lots of \$25,000.

instructions, in \$100 lots. As well, there are several reports suggesting that banks continue to seek competitive products that offer high liquidity and market-related yields. For example, a West Coast bank is reported to be offering \$100,000 14-day CDs for \$20,000 with the difference lent at a rate equal to the yield on the CD. However, there was general agreement among respondents that banks' attempts to compete with MMMFs by using loophole MMCs have not been very successful.<sup>1</sup> Overdraft privileges on retail accounts are quite common and are reported to have grown significantly in recent years. It is not clear to what extent individuals use this feature as a cash management technique.

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1. Loophole MMCs--an arrangement whereby the issuing depository institutions makes MMCs available for less than the \$10,000 legal minimum denomination by lending the depositor a portion of this amount, often up to \$7,000--appear to be generally available in the New York district but less common elsewhere. The loan rate is typically a fixed spread, usually a percentage point, over the MMC rate, but sometimes floats with the Treasury bill rate. In some cases, the MMC is linked with a transaction account and is checkable up to the maximum line of credit.



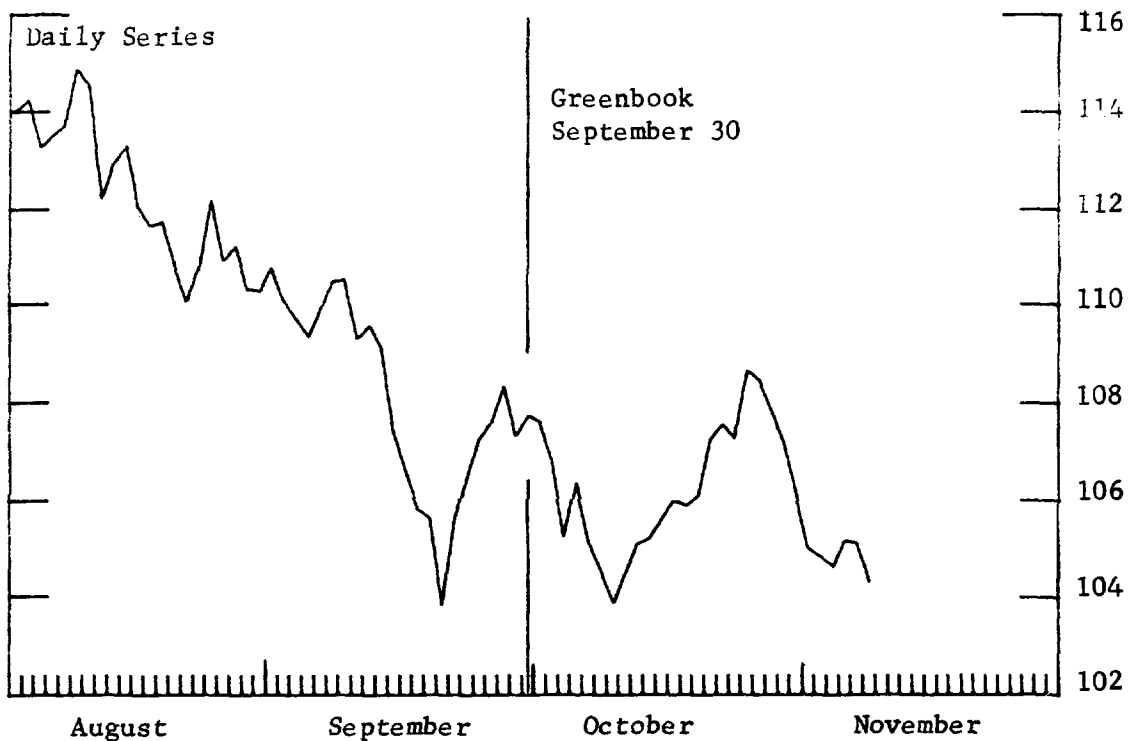
Foreign Exchange Markets

As shown by the chart on the next page, the weighted average value of the dollar has moved sharply down, up, and back down since the September Greenbook, depreciating by about 3 percent on balance. The net depreciation was associated with a decline of more than 3 percentage points in short-term dollar interest rates, compared with an average decline of about 1 percentage point in short-term foreign interest rates. The temporary strengthening of the dollar during the middle of October was associated with renewed sentiment that dollar interest rates might move back up, with increased tensions in the Middle East following the assassination of Egyptian President Sadat, and with political confrontations in Poland.

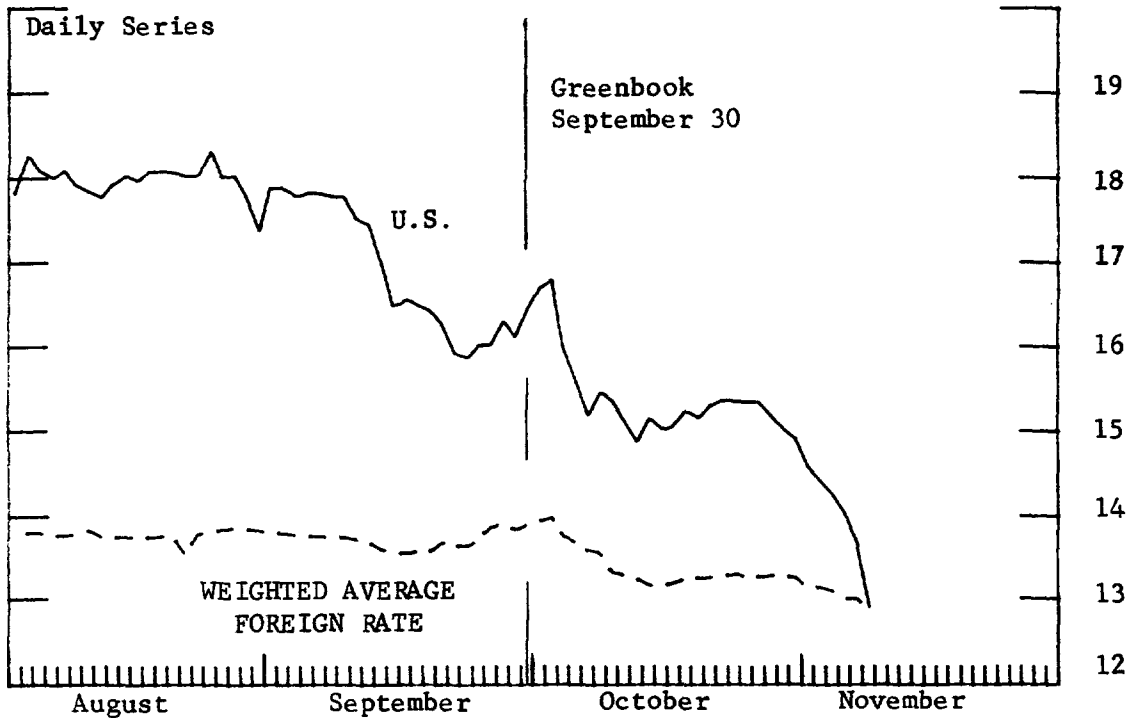
On October 4 the EMS currency band was realigned, with the central rates for the Deutschemark and Dutch guilder revalued by 5-1/2 percent vis-a-vis the Belgian franc, Danish Krone and Irish pound, while the central rates for the French franc and Italian lira were devalued by 3 percent. As a result of the realignment the market value of the French franc depreciated by about 4 percent against the mark, which moved the franc to the top of the new currency band while the mark and guilder moved to the bottom. The market value of the Belgian franc depreciated by about 2 percent against the mark.

The EMS realignment provided scope for a reduction of French interest rates, which have declined by around 3 percentage points since the last Greenbook. German interest rates have declined by about 1 percentage point over the same period. Continuing tight monetary

WEIGHTED AVERAGE EXCHANGE VALUE OF THE U.S. DOLLAR March 1973=100



SELECTED 3-MONTH INTEREST RATES Percent per annum



conditions in Switzerland have contributed to a further 5 percent appreciation of the Swiss franc against the mark since the end of September.

U.S. International Transactions

U.S. merchandise trade. In September the U.S. merchandise trade deficit was reduced substantially from the extraordinarily large August figure as exports rose and as imports declined. Exports of both agricultural and nonagricultural goods rose in September from low August levels. The drop in imports in September was largely in nonoil trade, was spread among most commodity categories (including steel and foreign cars), and largely reversed the sharp run-up in values in August. Oil imports in September amounted to 6.0 million barrels per day (seasonally adjusted), about 7 percent less than recorded in August; the average import price was essentially unchanged from August levels.

U.S. Merchandise Trade*						
	1980 Year	1981				
		1Q	2Q	3Q	Aug.	Sept.
<u>Value (Bil. \$, SAAR)</u>						
<u>Exports</u>	<u>224.0</u>	<u>244.4</u>	<u>241.9</u>	<u>232.0</u>	<u>228.9</u>	<u>234.0</u>
Agricultural	42.0	50.9	44.3	39.6	38.7	41.7
Nonagricultural	181.7	193.5	197.6	192.5	190.2	192.3
<u>Imports</u>	<u>249.3</u>	<u>263.1</u>	<u>269.6</u>	<u>260.9</u>	<u>284.4</u>	<u>253.7</u>
Petroleum	78.9	83.3	84.8	71.9	78.2	72.3
Nonpetroleum	170.4	179.8	184.8	189.0	206.3	181.5
<u>Trade Balance</u>	<u>-25.3</u>	<u>-18.7</u>	<u>-27.7</u>	<u>-28.9</u>	<u>-55.5</u>	<u>-19.7</u>
<u>Volume (Bil. 72\$, SAAR)</u>						
Exports - Agricultural	18.1	19.5	17.5	16.6	16.2	17.9
- Nonagric.	73.4	73.2	73.3	69.8	69.3	69.5
Imports - Petroleum	6.8	6.3	6.2	5.6	6.2	5.7
- Nonpetrol.	67.6	67.8	70.7	73.7	80.5	71.6

\*/ International Transactions and GNP basis.

For the third quarter as a whole, the trade deficit was little changed from that of the second quarter with the value of both exports and imports declining. About half of the decline in exports was in agricultural shipments during the summer months. Falling prices accounted for about half the decline in agricultural exports and a drop in volume the other half. By September, agricultural exports, particularly shipments of wheat and soybeans, began to pick up with the beginning of the new crop year, even though prices continued to ease.

The decline in the value of nonagricultural exports in the third quarter was concentrated in metals (reflecting particularly a drop in the volume of aluminum and a decline in the price of gold) and in civilian aircraft. The drop in aircraft exports was from a particularly large number of deliveries of big jets in the previous quarter. These and smaller declines in other commodity categories more than offset the sharp pick-up in the volume of coal exports in the third quarter that followed the settlement of the miners' strike. On average, the volume of nonagricultural exports dropped about 5 percent as demand from major trading partners continued to be weak, while prices of these exports rose by about 2 percent on average.

The third quarter decline in imports about equalled that of exports. However, the decrease was more than accounted for by a sharp drop in oil imports that far exceeded an increase in nonoil imports.

Oil imports in the third quarter declined in both volume and in price. The volume of oil imported averaged 9 percent less than in the second quarter while the price dropped \$2.35 per barrel. Despite some sharp month-to-month fluctuations, the trend in oil imports this year has been

downward as a result of a drawdown of U.S. oil stocks and continued weakness in consumption.

1981 U.S. Oil Imports						
	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>July</u>	<u>Aug.</u>	<u>Sept.</u>
Volume (mbd, SA)	6.59	6.52	5.92	5.38	6.54	6.04
Price (\$/BBL)	34.63	35.62	33.27	33.69	33.09	33.11
Value (Bil. \$, SAAR)	83.3	84.8	71.9	65.4	78.2	72.3

As a result of the October OPEC meeting, Saudi Arabia agreed to raise the price of its crude oil by \$2 per barrel to \$34 per barrel and to cut production to sustain this price through 1982. Several other oil exporters (Nigeria, United Kingdom, Norway, Mexico) had been aligned to the Saudi price prior to the meeting and are expected to raise their price proportionally. Even though some producers agreed to cut their prices to the new unified \$34 per barrel marker price (adjusted for quality differentials), the market share of these producers had already fallen precipitously during 1981 so that the net effect of the unified pricing agreement will be to increase the weighted average official OPEC price. If the Saudis cut production sufficiently to prevent discounts by other producers from the agreed unified price, the average U.S. import price should reach about \$35 per barrel early next year and remain at that level through 1982.

The increase in nonoil imports in the third quarter was largely in machinery and in consumer goods, with smaller increases in steel and automotive imports from Canada being offset by decreases in both food imports and in foreign car imports. The number of cars imported from

Japan and Europe in the third quarter was 6 percent less than in the second quarter, and was 20 percent less than the peak import rate in the third quarter of last year. Since then (3Q80), the number of foreign cars imported has declined each quarter. During this period dealer inventories of foreign cars have been drawn down to near record lows as sales declined only gradually.

U.S. International Capital Transactions. U.S.-based banks advanced, on a daily average basis, \$5 billion to their own foreign branches in September-October. During the same interval, loans to U.S. nonbank residents by those foreign branches increased, on a daily average basis, by about \$2 billion. The increase in branch loans most likely resulted from more extensive use by borrowers of LIBOR-pricing options included in loan commitments. The prime rate exceeded LIBOR by an average of 215

International Banking Data  
(billions of dollars)

	1980			1981			*/
	Dec.	March	June	Aug.	Sept.	Oct.	
1. Banking Positions Vis-a'-vis Own Foreign Offices <u>1/</u>							
(a) All banks	7.2	3.0	5.0	8.9	7.5	2.9	
(b) U.S.-based banks	-14.6	-16.9	-14.1	-10.0	-12.1	-15.2	
(c) Foreign-based banks	21.8	19.9	19.2	18.9	19.6	18.1	
2. Credit Extended to U.S. Non- bank Residents by Foreign Branches of U.S. banks <u>2/</u>	4.2	7.0	7.1	8.6	9.2	10.6	
3. Eurodollar Holdings of U.S. Nonbank Residents <u>3/</u>	60.8	66.3	76.8	85.5 <sup>P</sup>	n.a.	n.a.	

\*/ Daily average through October 28.

1/ Daily averages, net due to own foreign offices = (+).

2/ Daily averages.

3/ End of month.

basis points in September and 195 basis points in October, somewhat more than the 170 basis point average differential for the first eight months of the year.

As shown in the table above, Eurodollar holdings of U.S. nonbank residents increased by about \$25 billion in the first 8 months of the year. About \$9 billion of the increase was accounted for by holdings of Eurodollar CDs by money-market mutual funds. The great bulk of these Eurodollar CD holdings are with London branches of U.S. banks. Throughout this period U.S. banks significantly increased their reliance on the London CD market as a source of funds. As a percentage of outstanding CDs at domestic offices of weekly-reporting banks, CDs issued by London branches increased from 25 to 31 percent. During the 8 months the reserve-adjusted costs to U.S. banks of Eurodollar and domestic CDs were about equal.

The development of the Eurodollar CD market is likely to continue. In mid-October three U.S. banks successfully petitioned the dealer community to be treated as top-tier banks in the secondary market for Eurodollar CDs, i.e., to be traded homogeneously at the lowest rate in that market. This should improve the liquidity of the three banks' issues, as well as the liquidity of the issues of the four banks already included in the top tier. The addition of names to the top tier will make that market deeper and perhaps allow an even narrower bid-asked spread than the 10 basis points now quoted by dealers.

Beginning at the end of August new data have been collected on overnight Eurodollar deposits of U.S. nonbank residents at foreign branches of U.S. banks. These data show that U.S. nonbank residents



November 10, 1981

U.S. International Transactions  
(in billions of dollars; receipts, or increase in liabilities = (+))

	1979 Year	1980 Year	1981					
			Q1	Q2	Q3	July	Aug.	Sept.
1. CHANGE IN NET FOREIGN POSITIONS OF BANKING OFFICES IN THE UNITED STATES <u>1/</u>	14.7	-29.8	-10.2	-7.4	n.a.	6.1	-.9	n.a.
2. PRIVATE SECURITIES TRANSACTIONS, NET <u>2/</u>	-3.3	2.5	2.0	1.7	n.a.	.1	.4	n.a.
A. FOREIGN NET PURCHASES OF U.S. CORP. BONDS	.3	1.2	.8	.6		.3	.2	
B. FOREIGN NET PURCHASES OF U.S. CORP. STOCKS	1.0	4.3	1.7	2.6		.1	--	
C. U.S. NET PURCHASES (-) OF FOREIGN SECURITIES	-4.6	-3.0	-.5	-1.4		-.3	.2	
3. FOREIGN NET PURCHASES (+) OF U.S. TREAS. OBLIGATIONS <u>3/</u>	4.8	2.7	1.4	.7	n.a.	-.5	.5	n.a.
4. CHANGE IN FOREIGN OFFICIAL RESERVE ASSETS IN U.S., INCREASE (+)	-13.1	14.9	5.6	-3.1	n.a.	-.2	-4.8	n.a.
BY AREA								
A. G-10 COUNTRIES AND SWITZERLAND	-21.1	-2.5	1.9	-8.0		-1.4	-2.9	
B. OPEC	6.5	12.1	5.7	2.5		2.4	-1.6	
C. ALL OTHER COUNTRIES	1.5	5.3	-2.0	2.3		-1.1	-.3	
BY TYPE								
D. U.S. TREASURY SECURITIES <u>4/</u>	-21.6	9.7	7.2	-2.1		-1.7	-1.7	
E. OTHER <u>5/</u>	8.6	5.2	-1.6	-1.1		1.8	-3.1	
5. CHANGE IN U.S. RESERVE ASSETS INCREASE (-) <u>6/</u>	-.3	-7.8	-3.7	.8	n.a.	.7	-.4	n.a.
6. TRADE BALANCE, n.s.a.	-27.3	-25.3	-5.3	-5.6	-9.2	-2.2	-4.9	-2.1
7. ALL OTHER TRANSACTIONS AND STATISTICAL DISCREPANCY	24.6	43.0	10.2	12.9	n.a.	-4.0	10.1	n.a.
MEMO:								
BIL. \$ SEASONALLY ADJ. ANNUAL RATES								
MERCHANDISE TRADE BALANCE	-27.3	-25.3	-18.7	-27.7	-28.9	-11.5	-55.5	-19.7
CURRENT ACCOUNT BALANCE	1.4	3.7	13.0	4.3	n.a.	n.a.	n.a.	n.a.

1/ EXCLUDES LIABILITIES TO FOREIGN OFFICIAL INSTITUTIONS.

2/ EXCLUDES U.S. TREASURY OBLIGATIONS.

3/ INCLUDES U.S. TREASURY NOTES PUBLICLY ISSUED TO PRIVATE FOREIGN RESIDENTS.

4/ INCLUDES NON-MARKETABLE SECURITIES.

5/ INCLUDES DEPOSITS IN BANKS, COMMERCIAL PAPER, ACCEPTANCES, & BORROWING UNDER REPURCHASE AGREEMENTS.

6/ INCLUDES NEWLY ALLOCATED SDR'S OF \$1,139 MILLION IN JANUARY 1979; \$1,152 MILLION IN JANUARY 1980; and \$1,093 MILLION JANUARY 1981.

currently hold about \$2 billion more in overnight Eurodollar deposits than the slightly more than \$6 billion in such deposits now included as a component of M2.

Half of the \$2 billion in newly-reported overnight deposits are at the Caribbean branches of about two dozen regional banks. In October, on a daily average basis, the amounts of such deposits reported by the individual regional banks ranged from less than \$5 million to more than \$120 million. Overall, the new data strongly suggest that the practice of offering overnight Eurodollar investments to corporate customers has now spread from the current M2 reporters (a total of 27 major money center and larger regional banks) to a second tier of smaller regional banks.

The remainder of the \$2 billion of newly-reported overnight Eurodollar deposits of U.S. nonbanks at foreign branches of U.S. banks are outside the Caribbean, primarily in London. The London deposits appear to be held mostly by money market mutual funds that are willing to accept a somewhat lower yield in London to avoid Caribbean exposures. To the extent that these London deposits are held by money market mutual funds they are already reflected in M2.

Foreign official reserve assets in the United States fell about \$4.8 billion in August. Partial data, based on holdings at the FRBNY, indicate additional decreases totalling about \$1.0 billion in September and October. Holdings of the G-10 countries fell about \$2.9 billion in August and \$2.3 billion in September-October,

. OPEC holdings fell about \$1.6 billion in August, but increased by a like amount in September-October.

Foreign Economic Developments. Economic activity in most of the major foreign industrial economies has continued to be weak. Only in Japan, where in the third quarter expanding exports served to support a 1.2 percent (s.a.) rise in the level of industrial production above its level of the previous quarter, has economic activity shown some strength. In recent months, the unemployment rate in the major foreign industrial countries remained virtually flat or rose from already high levels and there has been little significant change in the rate of increase of consumer prices.

The Japanese and the German current-account balances showed continued improvement in the third quarter. Japan recorded a current-account surplus of \$2.4 billion in the third quarter, as compared with a \$2 billion surplus in the second quarter and a deficit of \$1 billion in the first quarter. The third quarter German current-account deficit is expected to be lower than the \$2.3 billion deficit (s.a.) posted in the second quarter.

In most of the major industrial countries both monetary and discretionary fiscal policy remain restrictive; the principal exception is Japan where the Bank of Japan has projected an increase in the growth rate of M2 in the fourth quarter. The generally weak economic activity and high unemployment and interest rates have tended to increase government deficits.

Individual Country Notes. In Japan, a continued widening of the current-account surplus has given rise to a renewal of international criticism of Japanese trade policies. The current-account surplus for September of almost \$1.4 billion (s.a.) was the largest in two years and

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

		1978	1979	1980	1980				1981			1981			
					Q1	Q2	Q3	Q4	Q1	Q2	Q3	June	July	Aug.	Sept.
Canada:	GNP	3.7	3.0	0.0	-0.9	-1.0	0.2	2.3	1.0	1.3	n.a.	*	*	*	*
	IP	3.4	4.7	-1.6	-0.7	-2.5	-0.3	2.3	1.9	2.6	n.a.	0.5	-2.2	-1.3	n.a.
France:	GDP	4.0	3.7	1.5	0.2	-0.6	0.2	-0.1	-1.1	1.2	n.a.	*	*	*	*
	IP	1.9	4.7	-1.2	0.5	-2.2	0.0	-2.0	-4.1	-0.8	n.a.	2.5	[ 1.6 ]		n.a.
Germany:	GNP	3.6	4.5	1.7	1.9	-2.0	0.0	-0.4	0.4	-0.7	n.a.	*	*	*	*
	IP	2.0	5.3	-0.1	0.9	-2.4	-1.5	-1.8	2.2	-0.3	-1.2	-3.6	1.9	-0.9	-0.9
Italy:	GDP	2.6	5.0	4.0	2.1	-0.9	-2.7	2.0	0.6	-0.8	n.a.	*	*	*	*
	IP	1.9	6.6	5.6	4.4	-2.7	-7.6	5.3	0.7	-2.5	-5.1	0.2	0.6	-13.6	18.2
Japan:	GNP	6.0	5.9	5.5	1.8	0.8	1.5	0.5	1.1	1.2	n.a.	*	*	*	*
	IP	6.2	8.3	7.1	4.1	0.2	-2.3	1.6	1.7	-0.3	1.2	2.6	1.0	-2.6	2.4
United Kingdom:	GDP	3.6	1.7	-2.1	-0.9	-1.5	-1.3	-0.4	-1.0	-0.6	n.a.	*	*	*	*
	IP	3.6	2.7	-6.6	-2.3	-3.0	-3.0	-2.7	-1.2	-0.8	n.a.	1.5	-0.0	-0.1	n.a.
United States:	GNP	4.8	3.2	-0.2	0.8	-2.6	0.6	0.9	2.1	-0.4	-0.1	*	*	*	*
	IP	5.8	4.4	-3.6	0.1	-5.3	-1.5	4.5	2.0	0.5	0.2	0.1	0.6	-0.3	-0.8

\* GNP data are not published on monthly basis.

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

											MEMO:
	1980			1981			1981				Latest 3 Months from Year Ago
	Q2	Q3	Q4	Q1	Q2	Q3	July	Aug.	Sept.	Oct.	
Canada: CPI	2.8	2.8	2.8	3.2	3.1	3.0	0.9	0.7	0.7	n.a.	12.7
WPI	1.1	2.8	3.2	2.5	2.1	n.a.	0.4	-1.6	3.1	n.a.	9.5
France: CPI	3.1	3.2	2.8	3.0	3.3	3.9	1.7	1.2	1.1	n.a.	13.6
WPI	0.8	0.6	3.4	1.5	4.5	4.0	1.5	1.1	0.3	n.a.	14.1
Germany: CPI	1.8	0.7	0.8	2.2	1.8	1.2	0.4	0.3	0.5	0.3	6.4
WPI	1.7	-0.2	0.7	3.9	2.3	2.1	0.7	1.3	0.9	n.a.	9.3
Italy: CPI	3.9	4.2	5.3	5.2	4.3	2.8	0.9	0.7	1.4	2.0	18.6
WPI	3.6	2.2	3.8	5.0	5.1	n.a.	0.9	1.2	1.3	n.a.	18.5
Japan: CPI	3.0	1.1	1.2	1.3	1.3	-0.1	-0.3	-1.0	2.0	0.4	3.6
WPI	4.8	0.7	-0.7	-0.7	1.1	1.4	0.4	0.5	0.0	n.a.	1.4
United Kingdom: CPI	5.8	2.2	1.9	2.4	4.9	1.7	0.4	0.7	0.6	n.a.	11.3
WPI	4.0	2.3	1.2	3.0	3.4	2.1	0.5	0.9	0.8	0.9	10.5
United States: CPI(SA)	3.1	1.9	3.1	2.6	1.8	2.9	1.2	0.8	1.2	n.a.	10.8
WPI(SA)	2.5	3.3	2.1	2.6	2.2	1.0	0.4	0.3	0.2	n.a.	8.1

TRADE AND CURRENT-ACCOUNT BALANCES OF MAJOR INDUSTRIAL COUNTRIES<sup>a</sup>  
(Billions of U.S. dollars; seasonally adjusted)

	1979	1980	1980				1981					
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	July	Aug.	Sept.
Canada: Trade	3.4	6.7	1.4	0.9	2.0	2.4	1.4	0.8	0.6	0.4	0.3	0.1
Current Account	-4.2	-1.6	-0.8	-1.0	-0.2	0.3	-1.1	-2.0.	n.a.	*	*	*
France: Trade <sup>b</sup>	-2.4	-14.2	-3.4	-3.5	-4.0	-3.2	-2.7	-2.1	-2.4	-1.1	0.0	-1.4
Current Account <sup>b</sup>	1.1	-7.9	-2.6	-1.2	-2.1	-2.0	-2.4	-0.4	n.a.	*	*	*
Germany: Trade	12.3	4.9	1.7	1.2	1.1	0.9	0.2	3.1	n.a.	1.7	0.4	n.a.
Current Account (NSA)	-5.3	-17.4	-2.9	-4.0	-7.1	-3.3	-4.4	-2.3	-5.0	-1.5	-2.6	-0.9
Italy: Trade	-5.2	-22.6	-4.1	-4.4	-8.6	-5.5	-4.5	-4.8	-4.4	-1.3	-1.4	-1.7
Current Account (NSA)	5.5	-9.8	-4.4	-1.5	-1.0	-2.9	-5.8	n.a.	n.a.	*	*	*
Japan: Trade <sup>b</sup>	1.8	2.1	-1.8	-0.9	1.4	2.9	3.3	5.5	6.3	1.6	2.2	2.5
Current Account <sup>b</sup>	-8.8	-10.7	-5.0	-4.1	-1.8	-0.2	-1.0	2.0	2.4	0.1	0.9	1.4
United Kingdom: Trade	-7.4	2.9	-0.9	-0.7	1.5	3.0	n.a.	n.a.	n.a.	n.a.	n.a.	0.0
Current Account <sup>b</sup>	-3.0	6.6	0.2	-0.2	2.1	4.5	n.a.	n.a.	n.a.	n.a.	n.a.	0.3
United States: Trade	-27.3	-25.3	-10.1	-6.7	-2.9	-5.6	-4.7	-6.9	-7.2	-1.0	-4.6	-1.6
Current Account	1.4	3.7	-2.1	-0.5	5.0	1.4	3.3	1.1	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.

brought the total surplus for the quarter to \$2.4 billion, which is somewhat above the second quarter surplus. Trade relations with the United States and the EC in particular have begun to show signs of strain as Japan's cumulative bilateral surpluses with them for the last six months have reached \$7.4 and \$5.4 billion (n.s.a.), respectively. The strength of the Japanese trade position has arisen both from ongoing growth in real exports, which expanded at a 14 percent annual rate in the third quarter, and a decline in real imports (at a 3-1/2 percent annual rate).

Although the latest monthly assessments of the domestic economy by the Bank of Japan and the Economic Planning Agency are upbeat about the prospects for near-term expansion of consumer spending, the pace of the recovery of domestic demand still appears to be moderate at best, as medium and small-scale firms still hold large unplanned inventories. Although industrial production (s.a.) rose sharply in September from its low August level, the unemployment rate moved upward again after 3 months of decline. The ratio of job offers to acceptances, a reliable indicator of labor-market conditions in Japan, fell in September, also indicating weakness.

Wholesale prices in September were unchanged from their level in August. Although there was a sharp upward movement in the CPI, in September and October it was still less than 4 percent above its year-previous level, reflecting the moderate trend of consumer prices in recent quarters. The Bank of Japan has projected an increase in the growth rate of M2 in the fourth quarter to a year-over-year rate of 10-11 percent, about a point higher than the comparable figure for the previous quarter.

Industrial production in Germany in the third quarter declined somewhat further from its low level of the second quarter. This weakness was fairly evenly spread across all industries with above average weakness in steel and strength in automobiles. The rate of unemployment at 6.2 percent (s.a.) reached a post-war record in October. Job openings, at the same time, were at their lowest level in the post-war years. Apart from exports, for which recent data indicate a slowing of growth, no domestic demand sector shows enough strength to indicate an early end to the stagnation in output.

The rate of inflation continues to be relatively high. Wholesale prices rose in excess of 8 percent (a.r.) in the third quarter, while the CPI rose by 5.2 percent. The CPI in October was 6.7 percent above its year-earlier level. While the high rate of inflation in wholesale prices point to no early let up in consumer price inflation, the recent strengthening of D-mark exchange rates should have a moderating effect on import prices and hence on the general price level.

The adjustment of the current-account deficit, which began in the second quarter, appears to be continuing. Seasonally adjusted, the second-quarter deficit was about half of the first-quarter deficit. Preliminary data through September indicate that the adjusted third quarter current-account deficit has been reduced further. The bulk of the adjustment has occurred in the trade account, where large gains in export volumes have improved the trade balance.

Only one month after the government presented its budget for 1982, which projected a significant decline in the deficit below this year's DM 35 billion, it has become apparent that a weaker economy than



previously expected will generate less tax revenues and require more unemployment benefits. So far, the additional fiscal shortfall is estimated officially at about DM 7 billion. The government intends to cover this shortfall by new taxes and a larger transfer of Bundesbank profits than originally expected.

In France, real GDP grew by 4.8 percent (s.a.a.r.) in the second quarter of this year. The level of GDP in the first half of this year, however, remained below its level for the same period in 1980. An increase in real consumption expenditures of nearly 5 percent and a rise of more than 34 percent in real exports, which were supported mainly by a sharp increase in services exports, were the most important factors leading to the strong real growth in the second quarter. In the third quarter, consumer price inflation accelerated to more than 15-3/4 percent from more than 13 percent in the second quarter.

The current-account deficit (s.a.) fell from nearly \$2-1/2 billion in the first quarter to under \$1/2 billion in the second quarter. After three consecutive quarters of improvement, the trade balance (s.a.) in the third quarter deteriorated somewhat. The trade deficit in the first three quarters this year was about \$3-3/4 billion dollars smaller than that recorded in the corresponding period in 1980.

French interest rates have fallen since the realignment within the EMS, when the franc-mark central rate was changed by 8-1/2 percent. At the end of September, 3-month money, for example, was earning 18-5/8 percent; in early November, the rate was 15-1/2 percent.

Industrial production in the United Kingdom, is starting to show some signs of recovery. Although total industrial production was flat

in July and declined slightly in August, the index for manufacturing industry alone increased by 8 percent in the three-month period ending in August. Output is still depressed, however, with total industrial production at the same level that it was in the first quarter of this year and manufacturing output only slightly above the first-quarter level. In addition, a preliminary estimate for the third quarter indicates a 2 percent (s.a.a.r.) decline in personal consumption for the second consecutive quarter. Third-quarter consumption is estimated to have been at the level prevailing in the same quarter last year. Real personal disposable income has fallen sharply this year; a decline in the personal saving rate -- from 16.5 percent (s.a.) in the final quarter of 1980 to 12.5 percent in the second quarter -- has moderated the impact of the drop in real disposable income on consumption.

Since April, when increases in various indirect taxes and public charges substantially raised the price level. U.K. inflation has been fairly moderate. In the five-month period ending in September, consumer prices rose about 7 percent (a.r.). Wholesale prices during this period increased 8-1/2 percent. Partly in order to prevent exchange-rate depreciation from adding to the inflation rate, the Bank of England has exerted upward pressure on market interest rates. In mid-September, the London clearing banks raised their base rates 2 percentage points to 14 percent. At the beginning of October the base rates were again increased by 2 percentage points, but subsequently have been reduced by 1 percentage point to 15 percent.

Trade and current-account data for September have been published, but data for the March-August period are not yet available. (The civil service labor dispute has delayed publication of these data.) The

September data indicate that the U.K.'s trade and current accounts are still in surplus -- \$24 million and \$267 million, respectively -- but that there has been a sharp reduction from surpluses averaging \$1-1/4 billion in the trade account and \$2 billion in the current account in January and February of this year.

Industrial production data confirm the weakness of the Italian economy; in the third quarter, industrial production was 2 percent below its year-earlier level. Leading indicators, however, suggest that the weakening in economic activity may have begun to moderate somewhat in the last four months of this year.

After moderate increases in the summer, the consumer price index rose sharply in September and October to a level over 18-1/2 percent above that of the year-earlier level. In the third quarter, the trade deficit (s.a.) was \$4-1/2 billion; in the first 9 months of 1981, the deficit was almost \$14 billion, compared with a deficit of about \$17 billion in the corresponding period of last year.

On September 30, the Spadolini government presented its 1982 budget proposals to Parliament. Expenditures relative to GDP are slated to remain steady, with investment expenditures rising and social welfare expenditures falling. Personal income taxes are scheduled to rise sharply. The final form of the budget is unclear, however, because labor unions are resisting the tax increase.

There is strong evidence that a slowdown in economic activity began in Canada in the third quarter of this year. Industrial production (s.a.) fell 1.3 percent in August after falling 2.2 percent in July. The unemployment rate increased slightly in October over September to 8.3

percent; this represents a more than 1 percentage point increase over the August rate of 7.2 percent. There was little change in the Canadian inflation rate in the third quarter.

The Canadian trade surplus fell from about \$850 million in the second quarter to less than \$640 million in the third quarter. The more than \$2.9 billion surplus recorded in the first three quarters of this year is almost \$1.4 billion below the surplus for the comparable period a year earlier.

The Swedish government has proposed a major reform of its personal income tax system to be effected over the 1983-85 period. According to the proposals, marginal income tax rates will be reduced significantly, with the largest reductions accruing to those who earn between \$20,000 and \$30,000. Additionally, income levels to which the marginal tax rates apply are scheduled to rise on average by 5-1/2 percent per year over the period. The consequent loss of revenue will be partially offset by a limit on the deductibility of mortgage interest. If the bill is passed in its current form, it is likely that the government will propose an increase in payroll taxes to finance the remaining net revenue loss.

Real activity as yet shows no signs of recovery in the Benelux countries. In August, Belgian industrial production was below its year-earlier level, and the unemployment rate was again unchanged from the July level of 14.4 percent (n.s.a.). Inflation remains high; the consumer price index in the three months ending October averaged 8 percent above its year-earlier level. In the Netherlands, industrial production in the second quarter averaged 1 percent (s.a.) below its average for

the first quarter, and unemployment rose further in August and September to 9.5 percent (s.a.), more than 2 percentage points higher than its level during the first month of the year. The consumer price index in October was 7.1 percent above its year earlier level.

Disagreements about the future course of fiscal policy led recently to the resignation of the Belgian and Dutch governments. No new elections have been scheduled in the Netherlands, and negotiations for a new coalition cabinet are underway. The Belgian election held on November 8 resulted in gains for the right-wing Liberal party and substantial losses for the Flemish Social Christian party of outgoing Prime Minister M. Eyskens. No party won enough votes to form a government by itself, and a new coalition will have to be formed.