## **Prefatory Note**

The attached document represents the most complete and accurate version available based on original copies culled from the files of the FOMC Secretariat at the Board of Governors of the Federal Reserve System. This electronic document was created through a comprehensive digitization process which included identifying the best-preserved paper copies, scanning those copies,[1] and then making the scanned versions text-searchable.[2] Though a stringent quality assurance process was employed, some imperfections may remain.

Please note that this document may contain occasional gaps in the text. These gaps are the result of a redaction process that removed information obtained on a confidential basis. All redacted passages are exempt from disclosure under applicable provisions of the Freedom of Information Act.

---

[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

[2] A two-step process was used. An advanced optimal character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

Confidential (FR) Class III FOMC

December 16, 1992

# RECENT DEVELOPMENTS

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

CONTENTS

## II DOMESTIC NONFINANCIAL DEVELOPMENTS



## III DOMESTIC FINANCIAL DEVELOPMENTS

Tables



Charts



IV INTERNATIONAL DEVELOPMENTS



Tables



Charts

# DOMESTIC NONFINANCIAL DEVELOPMENTS

Economic activity appears to be maintaining a relatively brisk rate of expansion in the current quarter. Private payroll employment has been rising since September, albeit slowly, and industrial production posted healthy increases in October and November. On the demand side, consumer spending evidently is growing at a rapid clip, buttressed by an apparent upturn in wage income and sharply improved confidence. Further gains also have been posted in single-family home sales and starts. Indicators of business investment have been mixed of late, with the possibility that spending on equipment is being temporarily damped by tax uncertainties and anticipations of new product introductions. The recent news on prices and wages has been a bit less favorable, on balance, than the reports of a few months ago, but, given the slack remaining in the economy, it seems unlikely that the underlying disinflationary trend has run its course.

Gross Domestic Product

According to BEA's preliminary estimate, real GDP increased at an annual rate of 3.9 percent in the third quarter, an upward revision of 1.2 percentage points from the advance estimate. About one-third of the upward revision was in nonfarm inventories, and the remainder was spread fairly evenly through the various categories of final sales. During the first three quarters of this year, real GDP rose at a 2-3/4 percent annual rate.[1]

1. It is noteworthy that a decomposition of nominal GDP from the income side of the accounts shows a widening of the statistical discrepancy, from $16.4 billion in the fourth quarter of 1991 to $41.7 billion in the third quarter of this year. Some analysts have suggested that this shortfall in income growth relative to GDP growth measured from the spending side of the national accounts points to a potential downward revision in the latter. But, at this point, one cannot rule out the possibility that the gap will be closed by upward revisions to estimated income flows.

## REAL GROSS DOMESTIC PRODUCT AND RELATED ITEMS

(Percent change from previous period at compound annual rates; based on seasonally adjusted data, measured in 1987 dollars)

| | 1990–Q4 to 1991–Q4 | 1992–Q2 Final | 1992–Q3 Advance | 1992–Q3 Preliminary |
|---|---|---|---|---|
| 1. Gross domestic product | .1 | 1.5 | 2.7 | 3.9 |
| 2. Final sales | –.6 | –.1 | 2.1 | 2.9 |
| 3. Consumer spending | .0 | –.1 | 3.4 | 3.7 |
| 4. Business fixed investment | –7.0 | 16.1 | .3 | 1.9 |
| 5. Producers' durable equipment | –3.5 | 24.1 | 8.5 | 9.2 |
| 6. Nonresidential structures | –14.3 | –.8 | –17.7 | –14.4 |
| 7. Residential investment | –.1 | 12.6 | .4 | .8 |
| 8. Government purchases | –.6 | –1.2 | 2.0 | 3.3 |
| 9. Exports of goods and services | 7.4 | –1.4 | 1.9 | 9.4 |
| 10. Imports of goods and services | 4.8 | 14.7 | 6.9 | 12.8 |
| *ADDENDA:* | | | | |
| 11. Nonfarm inventory investment [1] | –9.6 [2] | 6.0 | 9.8 | 14.8 |
| 12. Retail autos [1] | –1.3 [2] | 5.5 | 2.4 | 1.6 |
| 13. Excluding retail autos [1] | –8.3 [2] | .5 | 7.4 | 13.2 |
| 14. Farm inventory investment [1] | .3 [2] | 1.8 | 5.0 | 5.3 |
| 15. Net exports of goods and services [1] | –21.8 [2] | –43.9 | –51.5 | –49.8 |
| 16. Nominal GDP | 3.5 | 4.3 | 4.5 | 5.6 |
| 17. GDP fixed–weight price index | 3.5 | 2.9 | 2.1 | 2.2 |
| 18. GDP implicit price deflator | 3.4 | 2.8 | 1.8 | 1.7 |
| 19. Corporate profits [3] | 346.3 [2] | 388.4 | n.a. | 370.4 |
| 20. Profit share (percent) [4] | 6.1 [2] | 6.6 | n.a. | 6.2 |
| 21. Personal saving rate (percent) | 4.7 [2] | 5.3 | 4.5 | 4.5 |

1. Level, billions of 1987 dollars.
2. Annual average.
3. With inventory valuation and capital consumption adjustments; level, billions of dollars.
4. Economic profit as a share of nominal GNP.

Labor Markets

Recent data indicate some strengthening of labor demand. In November, private payrolls expanded slightly for the third consecutive month; however, the average workweek also increased further in November, and hours for private production and nonsupervisory workers rose 3/4 percent, matching the October gain. On average, aggregate hours in October and November were about 2-3/4 percent at an annual rate above the third-quarter level. Meanwhile, the civilian unemployment rate fell for a fifth consecutive month in November to 7.2 percent, 0.6 percentage point less than its most recent peak of last June. In addition, since the time of the November labor market surveys, initial claims for unemployment insurance benefits have declined further.[2]

Total nonfarm payroll employment expanded 105,000 in November. Government employment was up 60,000 last month, but about three-fourths of this increase reflected temporary hiring to staff polling places during the general election. Manufacturing employment rose 35,000 in November after three months of sizable declines. In the service-producing sector, 64,000 jobs were added, with gains in health, business, and a range of other services. Construction employment fell back a bit last month; it has changed little, on net, for the year to date, after dropping by a total of about 600,000 workers in 1990 and 1991. In the retail sector, employment was off 46,000 last month, because of less-than-usual seasonal hiring at general merchandise stores.[3]

2. Much of the especially sharp decline in initial claims for the week ended November 28 likely was due to seasonal adjustment problems associated with the Thanksgiving holiday.

3. On a not seasonally adjusted basis, retail employment was up 240,000 last month, but the seasonal factors were looking for an increase of 286,000; as a result, seasonally adjusted employment showed a decline. The seasonal factors expect a 280,000 increase in the number of retail jobs in December.

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

| | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Sep. | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|
| | Average monthly changes | | | | | | |
| Nonfarm payroll employment[2] | -79 | 15 | 74 | 25 | 12 | 34 | 105 |
| Private | -91 | -4 | 64 | -13 | 44 | 66 | 45 |
| Manufacturing | -36 | -17 | -14 | -45 | -43 | -65 | 35 |
| Durable | -33 | -16 | -15 | -33 | -27 | -45 | 20 |
| Defense-related[3] | -8 | -9 | -12 | -13 | -10 | -18 | -8 |
| Nondurable | -3 | -1 | 1 | -11 | -16 | -20 | 15 |
| Construction | -26 | 4 | -1 | -9 | -17 | 24 | -11 |
| Retail trade | -35 | -7 | 21 | -11 | 16 | 16 | -46 |
| Finance, insurance, real estate | -3 | 2 | -1 | -1 | 8 | 11 | -4 |
| Services | 30 | 28 | 70 | 70 | 84 | 77 | 64 |
| Health services | 29 | 16 | 20 | 20 | 18 | 29 | 22 |
| Business services | 3 | 11 | 39 | 10 | 3 | 77 | 21 |
| Total government | 12 | 19 | 10 | 37 | -32 | -32 | 60 |
| Private nonfarm production workers | -76 | 18 | 89 | -16 | 44 | 106 | 10 |
| Manufacturing production workers | -23 | 1 | -9 | -36 | -37 | -43 | 40 |
| Total employment[4] | -62 | 207 | 75 | 42 | -36 | -76 | 420 |
| Nonagricultural | -54 | 203 | 56 | 46 | -60 | 6 | 369 |
| Memo: | | | | | | | |
| Aggregate hours of private production workers (percent change) | -.1 | .1 | .0 | -.1 | -1.0 | .7 | .7 |
| Average workweek (hours) | 34.3 | 34.5 | 34.4 | 34.4 | 34.3 | 34.5 | 34.7 |
| Manufacturing (hours) | 40.7 | 41.0 | 41.1 | 41.0 | 40.9 | 41.1 | 41.3 |

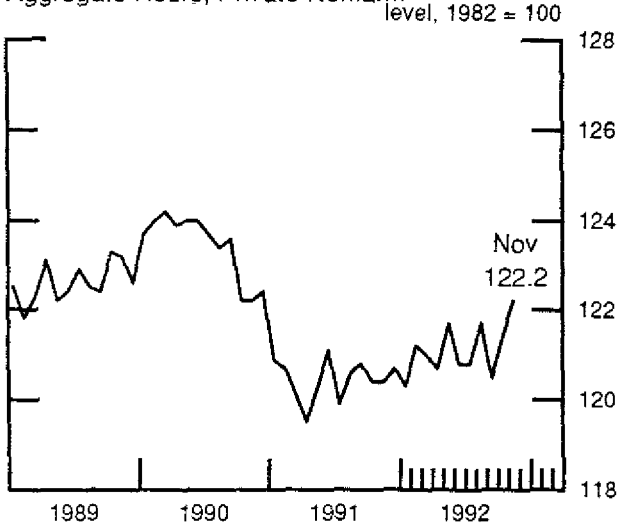
1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments.
3. Industries which are dependent on defense expenditures for at least 50 percent of their output.
4. Survey of households.

UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES
(Percent; seasonally adjusted)

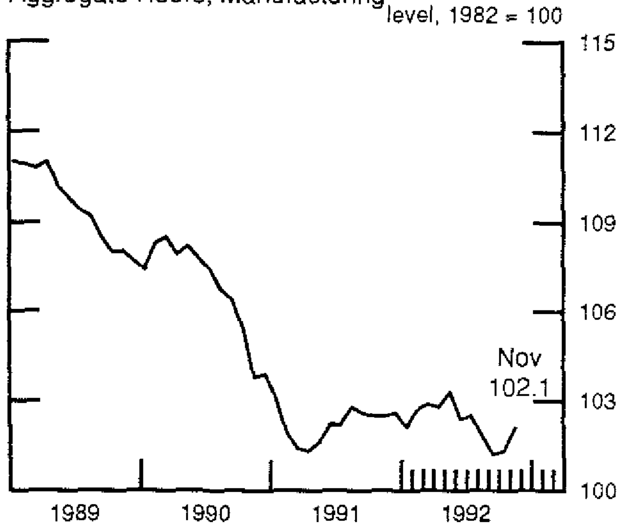
| | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Sep. | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|---|
| Civilian unemployment rate (16 years and older) | 5.5 | 6.7 | 7.2 | 7.5 | 7.6 | 7.5 | 7.4 | 7.2 |
| Teenagers | 15.5 | 18.7 | 19.6 | 21.0 | 20.4 | 20.4 | 18.3 | 20.2 |
| 20-24 years old | 8.8 | 10.8 | 11.1 | 11.3 | 11.6 | 11.6 | 10.9 | 11.1 |
| Men, 25 years and older | 4.4 | 5.7 | 6.3 | 6.5 | 6.6 | 6.6 | 6.6 | 6.1 |
| Women, 25 years and older | 4.3 | 5.1 | 5.6 | 5.8 | 5.8 | 5.7 | 5.6 | 5.7 |
| Labor force participation rate | 66.4 | 66.0 | 66.2 | 66.5 | 66.4 | 66.3 | 66.1 | 66.2 |

# LABOR MARKET INDICATORS

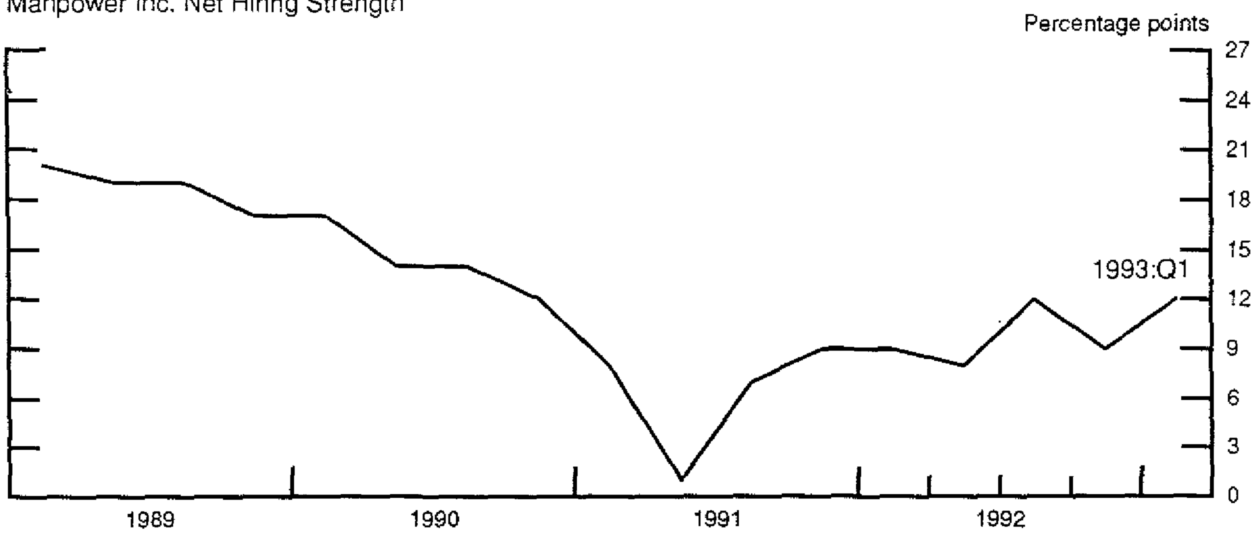
Aggregate Hours, Private Nonfarm



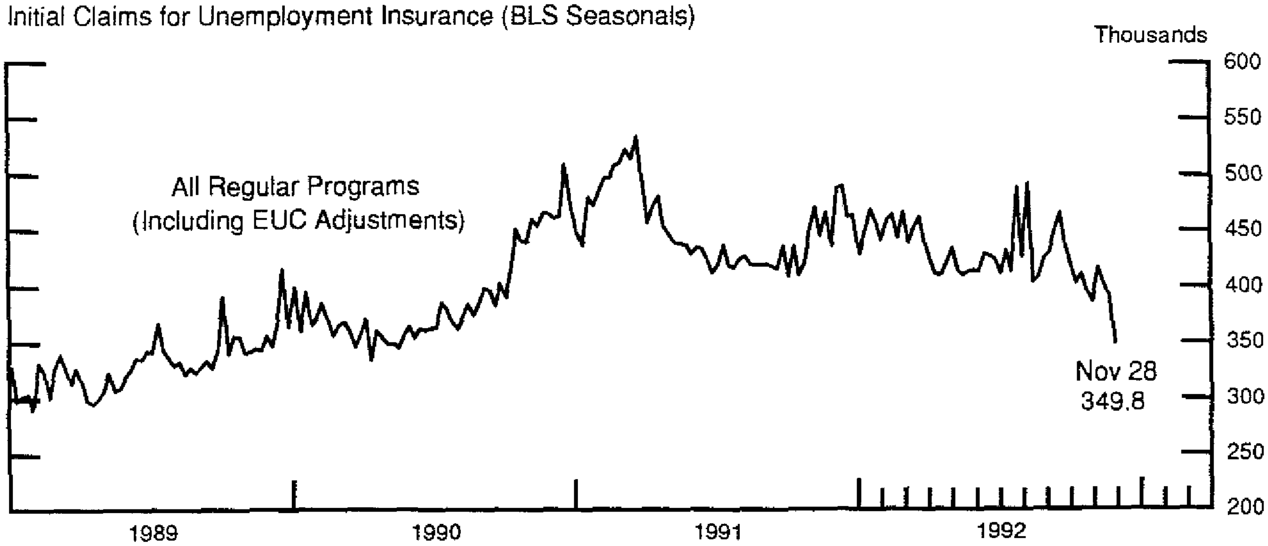

Aggregate Hours, Manufacturing




Manpower Inc. Net Hiring Strength[1]

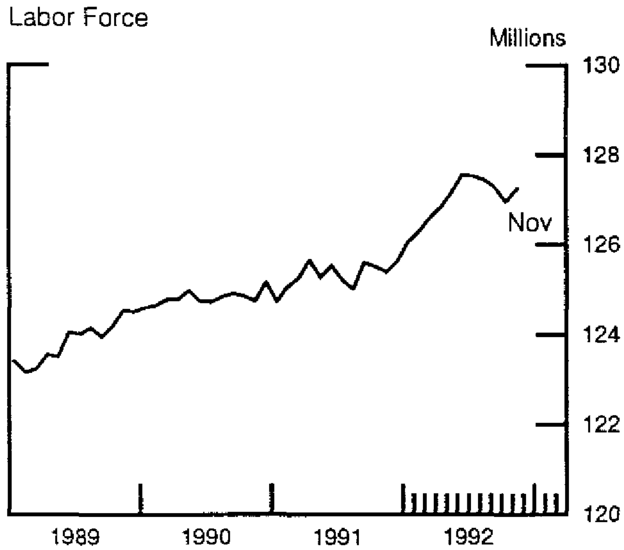



Initial Claims for Unemployment Insurance (BLS Seasonals)

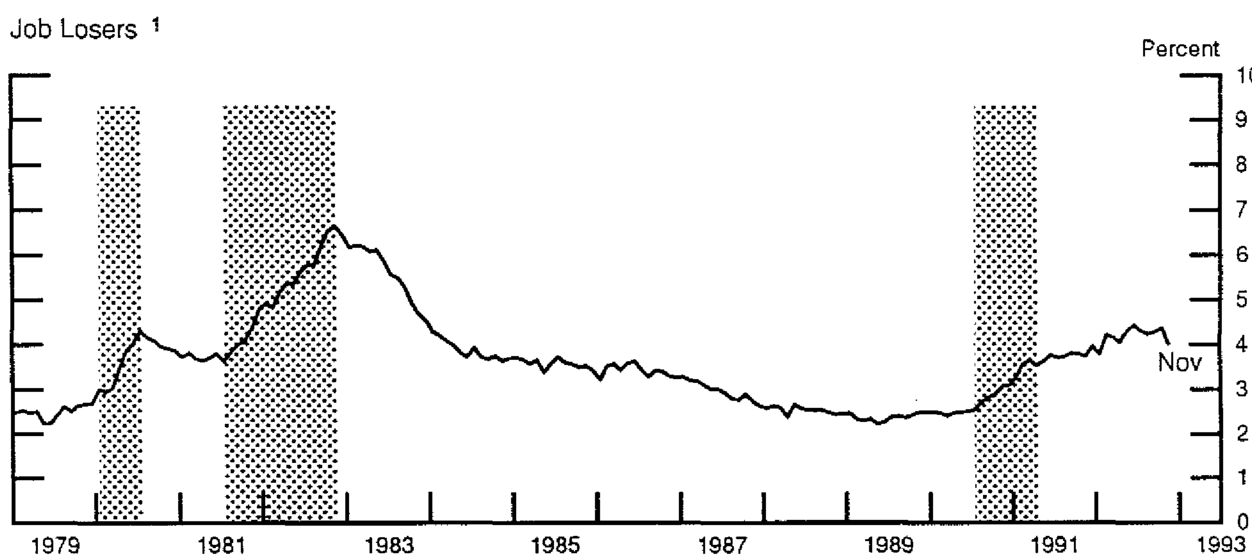


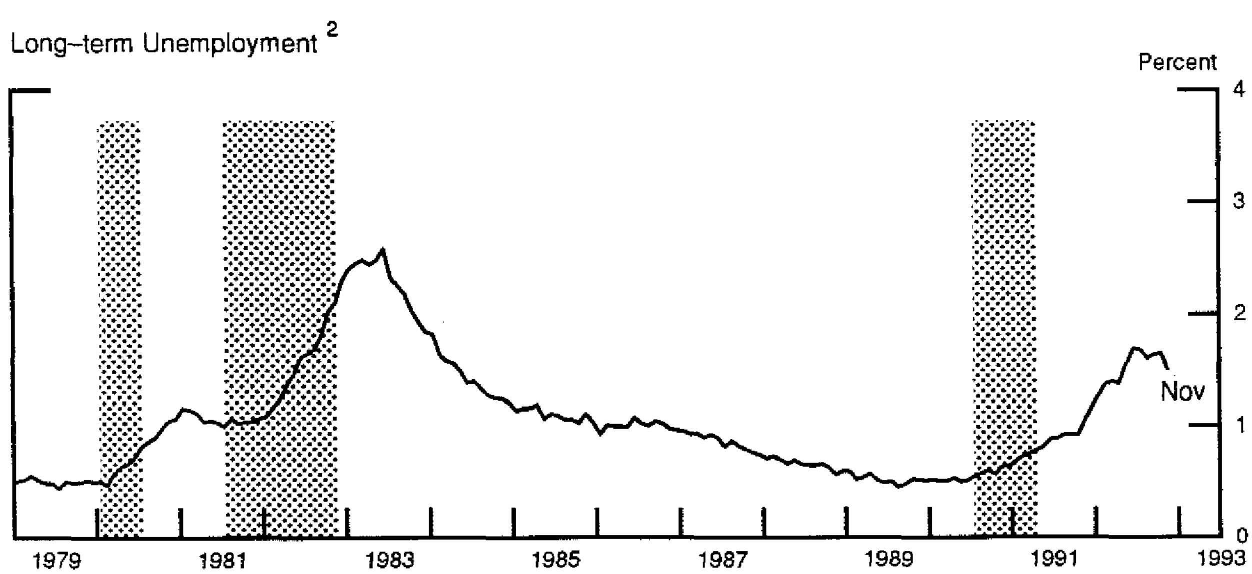

1. Percent of firms planning to increase employment minus those planning decreases, seasonally adjusted.

# INDICATORS FROM THE SURVEY OF HOUSEHOLDS








1. As a share of civilian labor force.

2. Unemployed 27 weeks or more as a share of the civilian labor force.

In November, the average workweek in the private nonfarm sector posted its second consecutive monthly gain of 0.2 hour; at 34.7 hours, its level is the highest since late 1989. In manufacturing, the workweek climbed to a 26-year high of 41.3 hours; under the circumstances, it seems likely that future increases in manufacturing production worker hours will be achieved largely by an expansion in payrolls.

Data from the household survey for November also suggest an improvement in labor demand. The declines in the unemployment rate from July through September resulted from jobless workers exiting the labor force rather than strength in hiring. However, last month this pattern changed noticeably: Both employment and the labor force expanded, but household employment was up much more than the labor force; as a result, the unemployment rate declined 1/4 percentage point. Other encouraging data from the November household survey included a decline in the number of job losers (particularly those on permanent layoff) and a small drop in long-term unemployment (those unemployed twenty-seven weeks or longer).

Looking ahead, the latest Manpower Inc. survey of hiring plans for the first quarter of 1993 was mildly favorable. The survey, which was conducted in late October and early November, showed that firms plan modest employment growth in services, trade, and finance, insurance, and real estate early next year. In addition, the survey indicates that first-quarter job gains are likely in construction and in manufacturing. Through October, however, the Conference Board survey of help-wanted advertising showed only slight improvement, remaining near its cyclical low.

Turning to recent data on wages, average hourly earnings of private production or nonsupervisory workers rose 0.6 percent in November, after a 0.2 percent increase in October. The largest gain

AVERAGE HOURLY EARNINGS
(Percentage change; based on seasonally adjusted data)[1]

| | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Sep. | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|---|
| | | | -Annual rate- | | | -Monthly rate- | | |
| Total private nonfarm | 3.5 | 3.1 | 3.5 | 1.1 | 1.9 | -.3 | .2 | .6 |
| Manufacturing | 3.6 | 3.0 | 1.8 | 2.5 | 2.5 | .0 | -.1 | .3 |
| Durable | 3.6 | 3.2 | .7 | 3.7 | .3 | -.5 | .2 | .2 |
| Nondurable | 3.8 | 2.8 | 1.9 | 3.0 | 4.6 | .6 | -.4 | .3 |
| Contract construction | .2 | 1.3 | 1.1 | 4.0 | -3.6 | -1.0 | .6 | .1 |
| Transportation and public utilities | 3.1 | 1.7 | 2.1 | 1.8 | 2.7 | .2 | -.1 | .9 |
| Finance, insurance and real estate | 5.1 | 4.3 | 6.2 | -.7 | 3.0 | -1.1 | .6 | 1.5 |
| Total trade | 3.0 | 3.3 | 2.9 | .0 | 2.4 | -.2 | .2 | .5 |
| Services | 4.4 | 3.8 | 4.3 | 1.1 | 2.3 | -.2 | .3 | .6 |

1. Annual changes are measured from final quarter of preceding year to final quarter of year indicated.

Average Hourly Earnings


1. Twelve-month percent change.

was in finance, insurance, and real estate, where wages jumped 1-1/2 percent, but several other sectors reported sizable increases. Nevertheless, over the twelve months ended in November, hourly earnings were up only 2.7 percent, slightly less than the increase during the previous twelve-month period.

Industrial Production and Capacity Utilization

Industrial production advanced 0.4 percent in November, after an upward-revised gain of 0.5 percent in October. Increases were widespread in November within the manufacturing and mining industries, while output at utilities dropped.

Motor vehicle assemblies were about unchanged in November, but an increase appears to be in train this month; weekly data suggest that the step-up in auto assemblies planned by manufacturers is under way, while truck assemblies appear to be holding at about the November level, a little short of the scheduled rate. Current schedules for the opening months of 1993 point to a sizable increase, but there has been a clear tendency over the past several years for initial announcements for the first quarter to be pared back considerably.

Outside of motor vehicles, output of consumer goods showed small increases in October and November. The gains were concentrated in nondurables, although, among durables, furniture production increased sharply. The output of business equipment rose another 1/2 percent last month; within that category, production of information processing equipment increased nearly 1 percent, as output of computers continued to climb. Industrial equipment also posted a healthy gain in November; elsewhere, output of equipment

GROWTH IN SELECTED COMPONENTS OF INDUSTRIAL PRODUCTION
(Percent change from preceding comparable period)

| | Proportion in total IP 1991:Q4 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Sep. | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|
| | | -----Annual Rate------ | | | -----Monthly Rate----- | | |
| Total index | 100.0 | -2.9 | 5.2 | 2.1 | -.3 | .5 | .4 |
| Previous | | -2.9 | 5.2 | 1.9 | -.2 | .3 | |
| Motor vehicles and parts | 4.2 | -20.0 | 44.4 | -9.3 | -2.3 | 4.3 | .7 |
| EXCLUDING MOTOR VEHICLES AND PARTS: | | | | | | | |
| Total index | 95.8 | -2.1 | 3.8 | 2.7 | -.2 | .3 | .4 |
| Products, total | 57.1 | -1.4 | 2.0 | 2.0 | -.3 | .4 | .3 |
| Final products | 42.9 | -2.1 | 2.6 | 2.3 | -.3 | .4 | .3 |
| Consumer goods | 25.0 | -1.2 | 2.5 | 2.4 | -.3 | .3 | .2 |
| Durables | 3.7 | 3.1 | 9.1 | .8 | -2.2 | -.5 | .0 |
| Nondurables | 20.9 | -2.1 | 1.4 | 2.7 | .1 | .4 | .3 |
| Excluding energy | 18.2 | -.7 | 1.4 | 3.3 | .1 | .3 | .3 |
| Business equipment | 14.6 | -1.7 | 7.6 | 5.7 | -.3 | .7 | .5 |
| Information processing | 6.9 | 5.8 | 13.3 | 11.3 | -.1 | 1.7 | .9 |
| Industrial | 3.9 | -12.1 | 6.3 | .0 | -.7 | .3 | .7 |
| Other | 3.8 | -3.5 | -.8 | 1.5 | -.2 | -.8 | -.7 |
| Defense and space equip. | 4.4 | -10.9 | -9.1 | -10.6 | -.9 | -.7 | -.9 |
| Intermediate products | 14.2 | .8 | .4 | 1.1 | -.4 | .5 | .2 |
| Construction supplies | 5.3 | 2.7 | 4.7 | 3.3 | -1.8 | 1.1 | .6 |
| Materials | 38.7 | -3.2 | 6.4 | 3.7 | -.1 | .1 | .5 |
| Durables | 18.2 | -1.7 | 6.5 | 3.8 | -.8 | .8 | .4 |
| Nondurables | 9.0 | -1.4 | 8.0 | 3.7 | .2 | -.3 | 1.6 |
| Energy | 10.2 | -6.0 | 2.8 | 3.8 | 1.3 | -.8 | -.2 |
| Memo: | | | | | | | |
| Manufacturing excluding motor vehicles and parts | 80.8 | -1.1 | 3.9 | 2.6 | -.3 | .4 | .4 |
| Mining | 7.3 | -7.1 | 4.3 | 2.0 | .0 | .1 | .6 |
| Utilities | 7.7 | -8.5 | 1.5 | 6.3 | .3 | -.5 | -.6 |

1. From the final quarter of the previous period to the final quarter of the period indicated.

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

| | 1967-91 Avg. | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Sep. | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|
| Total industry | 82.1 | 78.2 | 78.8 | 78.8 | 78.5 | 78.7 | 78.9 |
| Manufacturing | 81.4 | 77.3 | 77.9 | 77.8 | 77.4 | 77.7 | 77.9 |
| Primary processing | 82.3 | 80.5 | 81.3 | 81.9 | 81.3 | 81.6 | 82.4 |
| Advanced processing | 81.0 | 76.0 | 76.5 | 76.2 | 75.9 | 76.2 | 76.2 |

was held down by a further decline in commercial aircraft production.[4]

Output of construction supplies grew noticeably in October and November, retracing part of the losses that occurred in late summer. These increases partly reflected gains in output of lumber and are broadly consistent with the recent firming in homebuilding activity. Production of industrial materials also grew in November, as output of paper, textiles, and chemicals posted notable gains.

PRODUCTION OF DOMESTIC AUTOS AND TRUCKS
(Millions of units at an annual rate; FRB seasonal basis)

| | 1992 | | | 1993 | 1992 | | |
|---|---|---|---|---|---|---|---|
| | Q2 | Q3 | Q4 | Q1[1] | Oct. | Nov. | Dec.[1] |
| Domestic production | 10.0 | 9.5 | 10.2 | 11.1 | 9.9 | 10.1 | 10.7 |
| Autos | 6.1 | 5.6 | 5.7 | 6.3 | 5.5 | 5.6 | 6.0 |
| Trucks | 3.9 | 3.9 | 4.5 | 4.8 | 4.4 | 4.5 | 4.7 |

1. Figures beyond November are based on current manufacturers' schedules.

## Personal Consumption and Income

Incoming data on retail sales point to a further strong advance in consumer spending in the current quarter, and consumer confidence, which was stuck in the doldrums last summer and early fall, has risen impressively of late.

Total retail sales posted a modest increase in November after a substantial upward revision to growth in October. November spending in the retail control category, which excludes auto sales and sales at building material and supply stores, advanced 0.4 percent last month, and the October gain was revised up 0.8 percentage point, to

4. Production cutbacks at Boeing are expected to continue throughout 1993 in response to weak new orders, cancellations, and customer requests for delayed deliveries.

**RETAIL SALES**
(Seasonally adjusted percentage change)

| | 1992 | | | 1992 | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Sep. | Oct. | Nov. |
| Total sales | 2.7 | .2 | 1.6 | .7 | 1.9 | .4 |
| Previous estimate | | | 1.5 | .5 | .9 | |
| Retail control[1] | 2.2 | .3 | 1.7 | .3 | 1.2 | .4 |
| Previous estimate | | | 1.7 | .2 | .4 | |
| Total excl. automotive group | 2.5 | .3 | 1.5 | .5 | 1.1 | .3 |
| Previous estimate | | | 1.5 | .4 | .4 | |
| GAF[2] | 5.4 | -.6 | 3.4 | .6 | 1.1 | .4 |
| Previous estimate | | | 3.4 | .6 | 1.3 | |
| Durable goods stores | 3.9 | .5 | 1.9 | 1.7 | 2.8 | .5 |
| Previous estimate | | | 1.7 | 1.1 | 1.7 | |
| Bldg. material and supply | 7.4 | .3 | -.7 | 3.4 | .0 | -1.7 |
| Automotive dealers | 3.5 | .0 | 1.7 | 1.7 | 4.8 | .6 |
| Furniture and appliances | 4.0 | -.5 | 3.2 | .5 | 1.3 | 1.7 |
| Other durable goods | 2.1 | 3.8 | 4.6 | 1.3 | -.9 | 1.3 |
| Nondurable goods stores | 2.1 | .1 | 1.4 | .2 | 1.3 | .3 |
| Previous estimate | | | 1.4 | .2 | .4 | |
| Apparel | 3.7 | 2.0 | 3.7 | 1.1 | 1.2 | .3 |
| Food | .2 | .5 | .8 | -1.3 | .9 | .7 |
| General merchandise[3] | 6.6 | -1.8 | 3.4 | .4 | 1.0 | -.0 |
| Gasoline stations | -.3 | 2.2 | .4 | -.2 | .1 | .1 |
| Other nondurables[4] | 1.6 | -.3 | .4 | 1.4 | 2.3 | .2 |

1. Total retail sales less building material and supply stores and automotive dealers, except auto and home supply stores.
2. General merchandise, apparel, furniture, and appliance stores.
3. General merchandise excludes mail order nonstores; mail order sales are also excluded in the GAF grouping.
4. Includes sales at eating and drinking places, drug and proprietary stores.

1.2 percent.[5] The average level of nominal sales in the control category in October and November was up substantially (1-3/4 percent) from the third-quarter average. Sales of light vehicles also rose considerably in October and November, compared with their average selling pace during the third quarter, and a further gain was reported in the first ten days of December. Increases in the sales of light trucks accounted for the gains of October and November, but the very recent data show stronger numbers for cars as well. All told, the data in hand indicate that consumer outlays for goods, which registered a sizable gain last quarter, have remained on a solid upward trajectory.

According to both the Michigan and the Conference Board surveys, consumer sentiment (chart) has rebounded since October. Comparison of the preliminary and final releases of the Michigan survey for November indicates that sentiment was higher in the latter half of the month than in the first half, and the preliminary reading for December showed a further increase. This pattern invites the interpretation that the initial surge in optimism around the election may have been reinforced by the predominantly upbeat tone of the economic news since the beginning of November.

The higher level of consumer sentiment is not surprising from the standpoint of econometric models of sentiment. Indeed, what is surprising is that spirits remained so low earlier. Econometric models have consistently overpredicted both the Michigan and the Conference Board indexes for most of the past two years; however, with the December increase in the preliminary reading from the

5. Press reports about holiday sales have featured supposedly impressive year-over-year increases. However, this perspective may provide an exaggerated view about the near-term performance of sales. For example, even if (seasonally adjusted) spending at general merchandise stores did not grow at all in December, year-over-year comparisons would show an increase in sales of close to 12 percent because sales were strong from January through October.

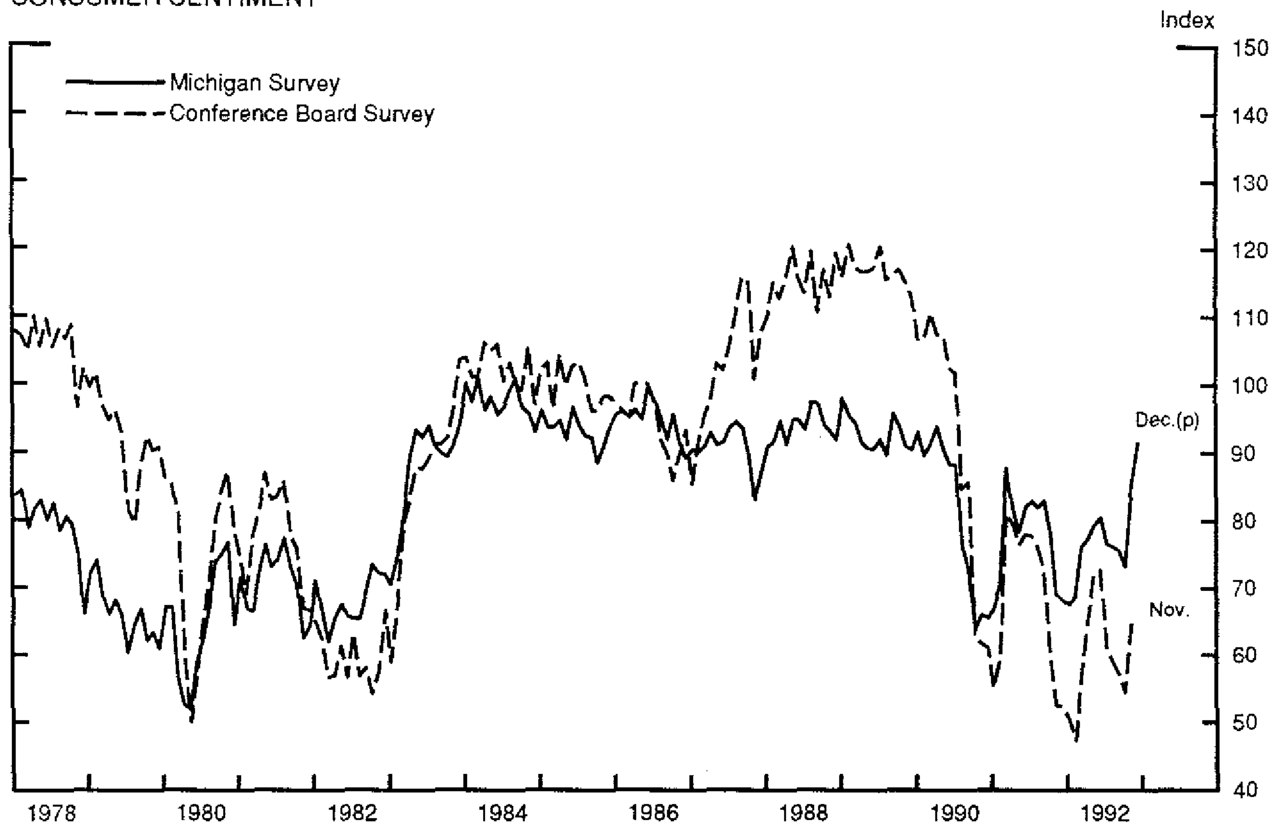
SALES OF AUTOMOBILES AND LIGHT TRUCKS[1]
(Millions of units at a seasonally adjusted annual rate)

| | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Oct. | 1992 Nov. | 1992 Dec.[2] 1-10 |
|---|---|---|---|---|---|---|---|---|
| Total | 13.86 | 12.30 | 12.37 | 12.99 | 12.59 | 13.49 | 12.99 | 14.10 |
| Autos | 9.50 | 8.39 | 8.31 | 8.50 | 8.21 | 8.30 | 8.17 | 9.06 |
| Light trucks | 4.36 | 3.91 | 4.06 | 4.49 | 4.38 | 5.19 | 4.82 | 5.04 |
| North American[3] | 10.84 | 9.73 | 9.86 | 10.57 | 10.41 | 11.26 | 10.78 | 11.86 |
| Autos | 6.90 | 6.14 | 6.07 | 6.32 | 6.24 | 6.28 | 6.20 | 7.04 |
| Big Three | 5.82 | 4.99 | 5.02 | 5.17 | 4.94 | 5.17 | 5.06 | 5.66 |
| Transplants | 1.08 | 1.14 | 1.05 | 1.15 | 1.30 | 1.11 | 1.14 | 1.39 |
| Light trucks | 3.95 | 3.59 | 3.79 | 4.25 | 4.17 | 4.98 | 4.58 | 4.82 |
| Foreign produced | 3.01 | 2.57 | 2.50 | 2.43 | 2.18 | 2.23 | 2.21 | 2.24 |
| Autos | 2.60 | 2.25 | 2.24 | 2.18 | 1.97 | 2.02 | 1.98 | 2.02 |
| Light trucks | .41 | .32 | .27 | .24 | .20 | .21 | .24 | .22 |

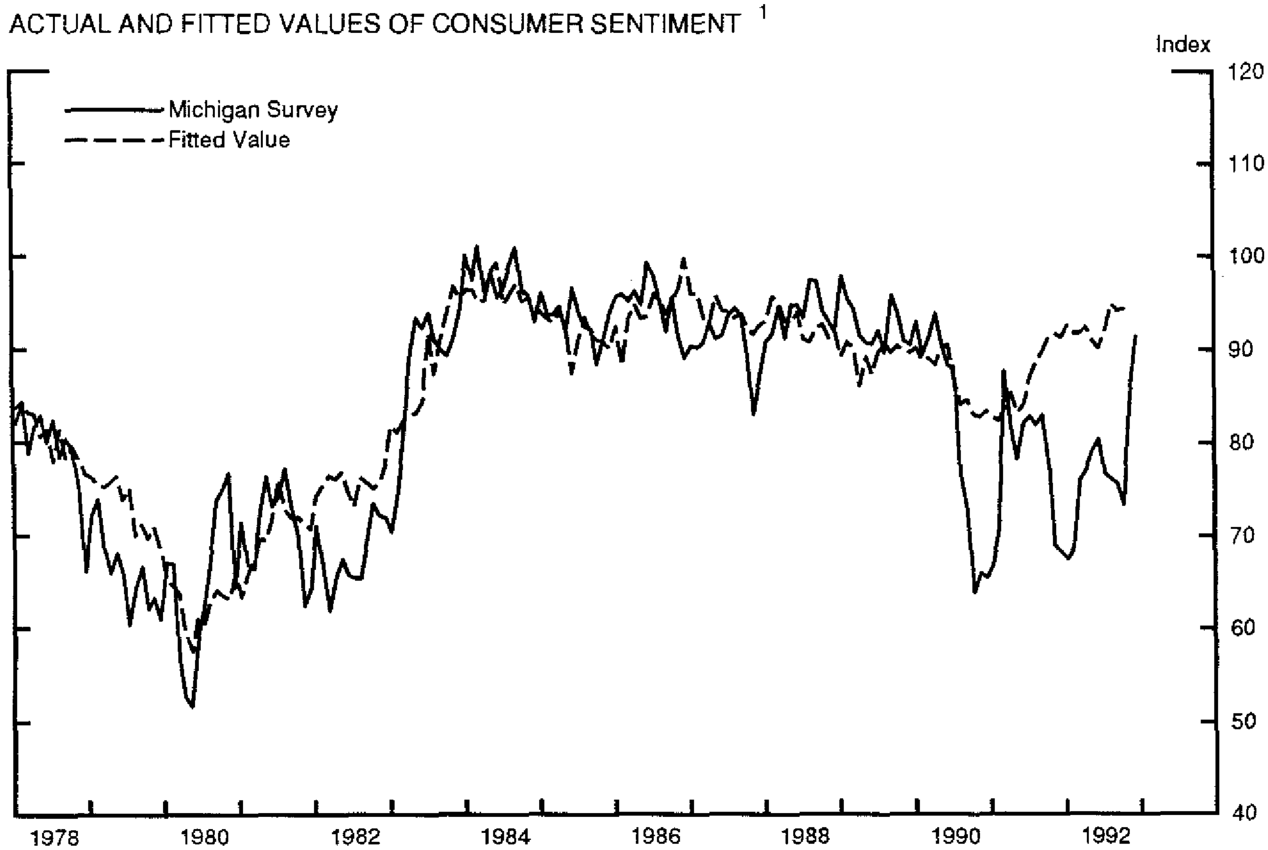
Note: Data on sales of trucks and imported autos for the current month are preliminary and subject to revision.

1. Components may not add to totals because of rounding.
2. Sales of North American produced vehicles are data: sales of imported vehicles are staff estimates.
3. Excludes some vehicles produced in Canada and Mexico that are classified as imports by the industry.

CONSUMER SENTIMENT




ACTUAL AND FITTED VALUES OF CONSUMER SENTIMENT [1]




1. The equation for estimating consumer sentiment is described in the text.
p = preliminary

PERSONAL INCOME
(Average monthly change at an annual rate; billions of dollars)

| | | 1992 | | | 1992 | |
|---|---|---|---|---|---|---|
| | 1991 | Q1 | Q2 | Q3 | Sep. | Oct. |
| Total personal income | 12.8 | 21.6 | 9.6 | 13.5 | 24.4 | 51.1 |
| Wages and salaries | 5.2 | 11.3 | 3.6 | 5.6 | -4.1 | 18.3 |
| Private | 3.8 | 8.6 | .9 | 5.6 | -3.8 | 15.0 |
| Other labor income | 1.5 | 1.4 | 1.4 | 1.4 | 1.4 | 1.5 |
| Proprietors' income | .1 | 7.1 | -4.2 | 5.4 | 20.2 | 21.2 |
| Farm | -.3 | 1.7 | -5.9 | 2.6 | 14.2 | 16.9 |
| Rent | .6 | -.1 | 3.7 | -1.2 | 2.2 | 5.4 |
| Dividend | -.8 | .1 | 1.2 | 1.5 | 1.0 | 1.5 |
| Interest | -.6 | -8.6 | -.8 | -3.8 | -3.7 | -3.0 |
| Transfer payments | 7.8 | 12.2 | 5.3 | 5.2 | 7.2 | 7.5 |
| Less: Personal contributions for social insurance | 1.1 | 1.9 | .6 | .5 | -.2 | 1.1 |
| Less: Personal tax and nontax payments | -.1 | -5.0 | 3.3 | 4.6 | 2.0 | 5.3 |
| Equals: Disposable personal income | 12.9 | 26.6 | 6.3 | 8.9 | 22.4 | 45.8 |
| Memo: Real disposable income | 1.2 | 9.8 | -1.9 | 1.6 | -3.2 | 22.0 |

REAL PERSONAL CONSUMPTION EXPENDITURES[1]

| | | 1992 | | | 1992 | |
|---|---|---|---|---|---|---|
| | 1991 | Q1 | Q2 | Q3 | Sep. | Oct. |
| | | ------Annual rate----- | | | Monthly rate | |
| Personal consumption expenditures | .0 | 5.1 | -.1 | 3.7 | .3 | .3 |
| Durable goods | -2.5 | 16.5 | -2.1 | 9.5 | .4 | 1.8 |
| Excluding motor vehicles | -1.0 | 15.2 | -1.6 | 18.6 | .6 | .3 |
| Nondurable goods | -1.5 | 5.5 | -1.5 | 2.5 | .1 | .1 |
| Excluding gasoline | -1.6 | 5.6 | -1.7 | 2.8 | -.2 | .3 |
| Services | 1.6 | 2.2 | 1.2 | 3.0 | .3 | .0 |
| Excluding energy | 1.5 | 3.0 | .9 | 3.2 | .2 | .1 |
| Memo: | | | | | | |
| Personal saving rate (percent) | 4.7 | 4.9 | 5.3 | 4.5 | 4.4 | 4.7 |

1. The revised data on retail sales for September and October have not yet been incorporated into the PCE data.

Michigan survey, confidence is much closer to the level predicted by various regression equations (chart).[6]

Real disposable personal income rose only 0.4 percent (annual rate) in the third quarter (table), and adjusting income for the negative effects of Hurricanes Andrew and Iniki would raise the third-quarter growth rate only about 1/4 percentage point. Nominal personal income jumped 1 percent in October, but most of the gain was due to special factors such as a rebound from the depressing effects of the hurricanes, one-time transfers to Japanese-Americans interned during World War II, and retirement incentives for Postal Service employees. Excluding these factors, nominal income was up a more modest 0.4 percent in October. However, average weekly earnings posted a sizable gain in November, suggesting that wage and salary income will show a substantial improvement in that month.

Business Fixed Investment

Real outlays for producers' durable equipment, which rose at an average annual rate of more than 10 percent over the first three quarters of 1992, appear to be on track for another advance in the current quarter. Equipment investment probably has been supported by the pick-up in economic growth in recent quarters as well as a substantial increase in cash flow since late last year. Meanwhile, the outlays for nonresidential construction appear to have firmed a little in early autumn, after a steep drop during the summer.

In the near term, one potentially important influence on equipment spending is the possible enactment of investment

6. The fitted values of sentiment in the chart are derived from a model that relates the level of sentiment in month *t* to several right-hand variables: the unemployment rate in month *t*, the change in the unemployment rate in month *t*, the change in the unemployment rate over the last year, the change in real disposable income in month *t*, the change in income over the last year, the change in prices in month *t*, the change in prices over the last year, and a trend. The model was estimated over the period from January 1960 to June 1990 and simulated for the period since June 1990. Similar results were obtained with a variety of other specifications.

BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period;
based on seasonally adjusted data, in current dollars)

| | 1992 | | | 1992 | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Aug. | Sep. | Oct. |
| Producers' durable equipment | | | | | | |
| Shipments of nondefense capital goods | .5 | 1.4 | .8 | -2.1 | 2.8 | -.6 |
| Excluding aircraft and parts | .2 | 2.6 | 3.0 | -2.4 | 3.4 | -1.2 |
| Office and computing | 5.0 | 3.8 | .2 | -3.2 | -3.0 | -1.6 |
| All other categories | -1.2 | 2.3 | 3.9 | -2.2 | 5.4 | -1.1 |
| Shipments of complete aircraft[1] | 64.6 | -12.7 | -18.1 | -10.2 | 7.6 | -16.1 |
| Sales of heavy weight trucks | 7.1 | 5.9 | 2.0 | 1.2 | 4.6 | 6.8 |
| Orders of nondefense capital goods | 2.5 | -.4 | -3.6 | -3.9 | 8.6 | 3.7 |
| Excluding aircraft and parts | 4.0 | .5 | 2.5 | -3.1 | 6.5 | -1.3 |
| Office and computing | 9.2 | 4.4 | 2.0 | 4.3 | -4.4 | -1.5 |
| All other categories | 2.6 | -.6 | 2.6 | -5.2 | 10.0 | -1.2 |
| Nonresidential structures | | | | | | |
| Construction put-in-place | .6 | .6 | -3.2 | -4.8 | 3.3 | -.3 |
| Office | -4.9 | -6.7 | -11.2 | -3.9 | .2 | .6 |
| Other commercial | 1.5 | 3.8 | -2.2 | -9.1 | 10.1 | -.1 |
| Industrial | 2.4 | -6.0 | -8.5 | -13.0 | 6.2 | -3.6 |
| Public utilities | 5.2 | 2.5 | .1 | -.3 | .8 | -.5 |
| All other | -2.7 | 6.2 | .9 | -1.7 | 1.2 | 1.3 |
| Rotary drilling rigs in use | -4.7 | -1.4 | .8 | -.2 | -.6 | 9.4 |
| Footage drilled[2] | -17.3 | -4.5 | 3.1 | -2.9 | -4.9 | 33.7 |
| Memo: | | | | | | |
| Business fixed investment[3] | 3.0 | 16.1 | 1.9 | n.a. | n.a. | n.a. |

1. From the Current Industrial Report "Civil Aircraft and Aircraft Engines." Monthly data are seasonally adjusted using FRB seasonal factors constrained to BEA quarterly seasonal factors. Quarterly data are seasonally adjusted using BEA seasonal factors.
2. From Department of Energy. Not seasonally adjusted.
3. Based on constant-dollar data; percent change, annual rate.
n.a. Not available.

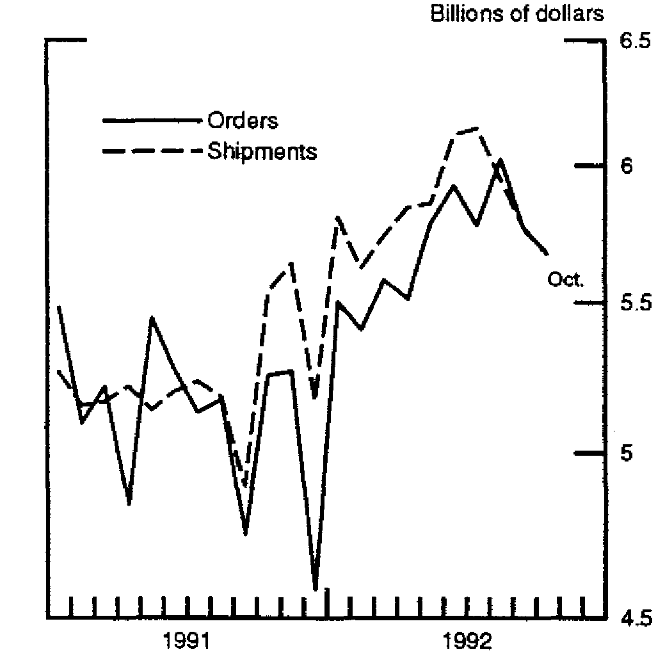
incentives in 1993. Although no explicit policy has been proposed, President-elect Clinton has supported targeted investment incentives, and a marginal investment tax credit has been widely discussed. In similar episodes in the past, anticipation of the future enactment of such incentives led businesses to shift their capital spending plans to reduce their tax liabilities. However, several aspects of the current experience suggest that these transitory forces will not significantly alter the near-term path of investment in producers durable equipment. First, delivery lags are such that most current shipments are the result of orders placed before the election. Second, congressional leaders have indicated that any tax change should be made retroactive to the beginning of December.[7]

The available data on shipments of nondefense capital goods, which extend only through October, indicate that some significant shifts in the composition of spending are occurring. Outlays for computing equipment trended up at an annual rate of close to 40 percent from early 1991 through the third quarter of this year, accounting for almost all of the advance in total equipment outlays over the period. However, nominal shipments of computers declined nearly 8 percent from August to October, and nominal orders have fallen in each of the past two months. The recent softening in the sector may have been driven, in part, by the expectation of continued large price declines, and by the anticipation of new

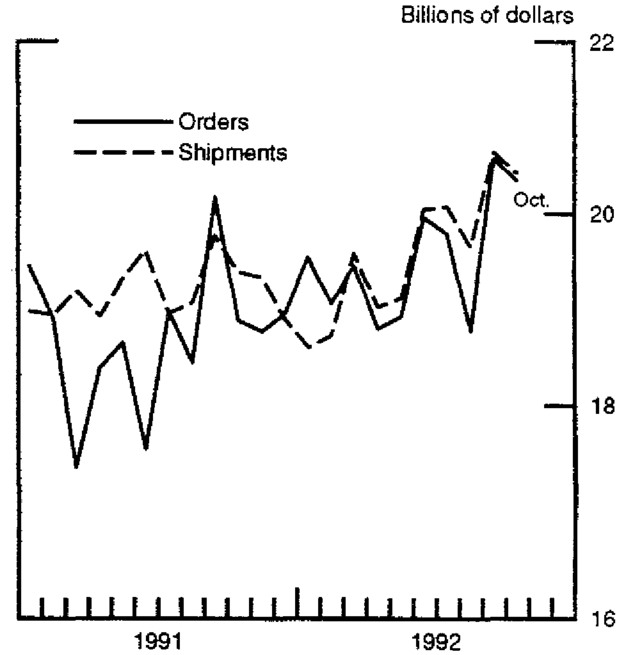
7. The anticipation of an investment tax credit probably will have a relatively small effect on production of capital goods, given that a substantial proportion of the domestic production of these goods is exported (and the prospect of an ITC has no bearing on foreign demand); moreover, if manufacturers think that any weakness in orders late this year is transitory, in that it stems from the possible enactment of a tax credit, they may decide to maintain production, temporarily holding more inventories.

# RECENT DATA ON ORDERS AND SHIPMENTS

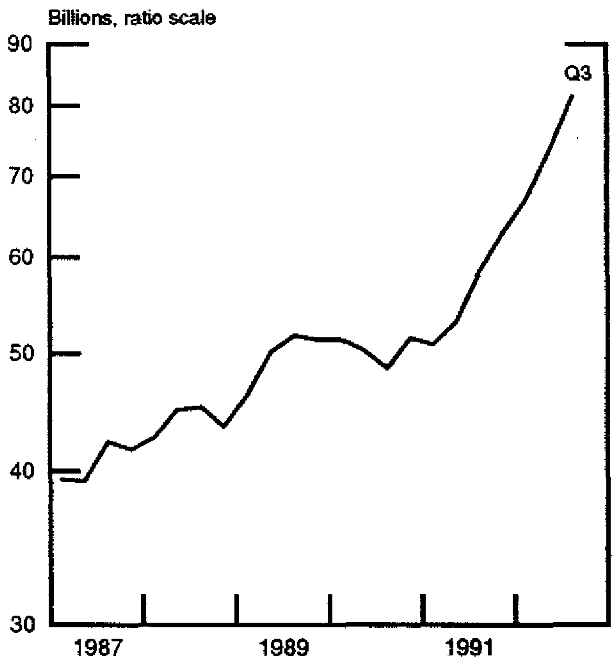
Office and Computing Equipment



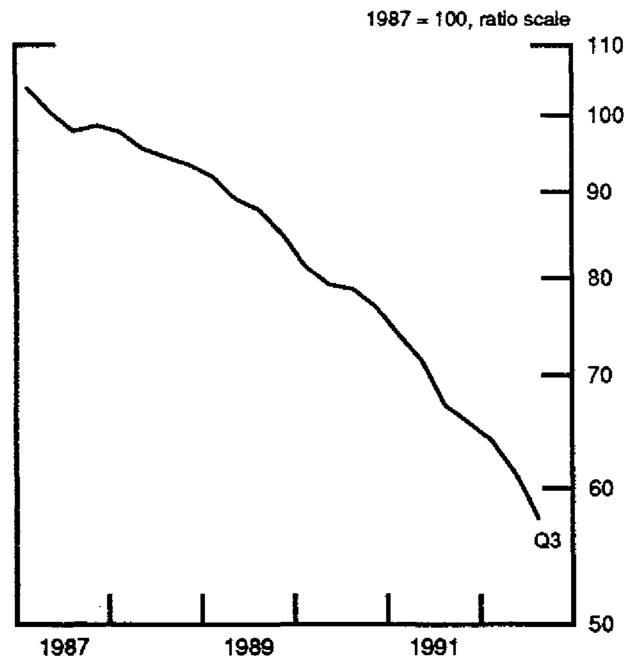

Other Equipment (ex. aircraft and computers)




OUTLAYS FOR COMPUTERS
(1987 dollars, seasonally adjusted)




DEFLATOR FOR COMPUTERS
(Seasonally adjusted)



products set to be introduced early next year, such as Intel's powerful Pentium processor.[8]

The segment of the computer market in which the recent softness has been concentrated is still a matter of conjecture. According to recent press reports, the leading PC producers are seeing continued strong demand, and have accumulated relatively large backlogs in recent months; this suggests that the declines in overall orders and shipments of computing equipment stems from weakness for higher-value products, such as mainframes and workstations. Whatever the case, the continuing rapid downtrend in the overall price index for computers (chart) likely will offset the weakness in nominal shipments, thus giving rise to a firmer picture in terms of constant-dollar outlays.

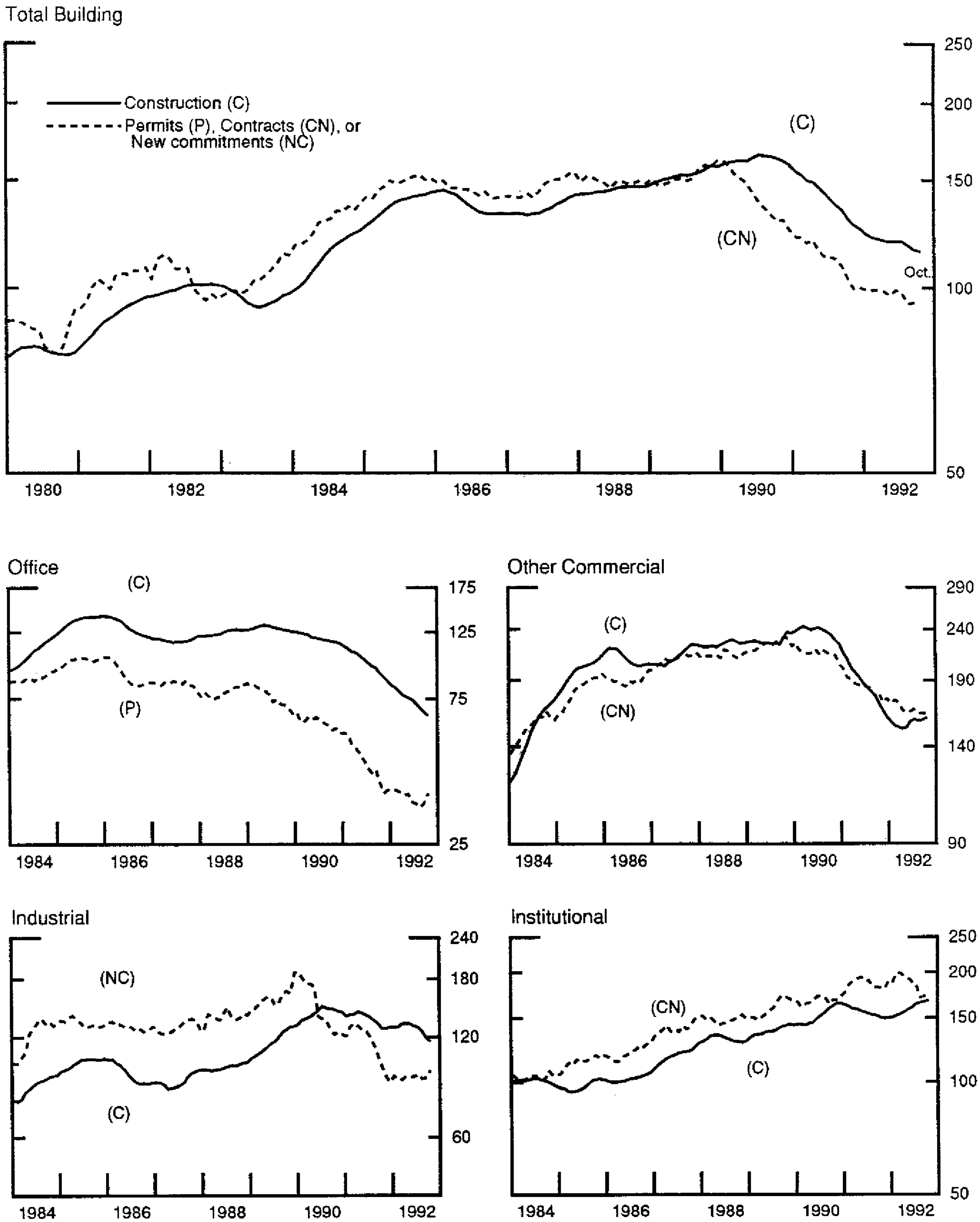
Recent data on other equipment investment have been more positive. Sales of heavy trucks have risen notably in recent months, and the increase in light vehicle sales so far this quarter probably reflects greater demand from both businesses and households.[9] In addition, domestic aircraft purchases should not be the big negative that they were in the previous quarter; these purchases had soared to an unsustainably high level last spring, and their third-quarter drop brought them to a more normal level. Nonetheless, outlays in this sector probably will be trending down during the next couple of years, reflecting the problems that currently beset the domestic airlines.

8. Industry sources have informed us that this processor may be at least three times faster than the top-of-the-line PC chips that are currently available. The speed gains offered by Pentium-based systems are such that PCs incorporating this chip will be competitive with the low end of the workstation market. The prospective list prices for the machines unveiled so far have ranged from $5,000 to $15,000. Industry sources have suggested that these machines will most likely sell at even lower prices by next spring.

9. Navistar, which marketed its products aggressively as its fiscal year came to an end in October, accounted for two-thirds of the increase in heavy truck sales in that month.

## NONRESIDENTIAL CONSTRUCTION AND SELECTED INDICATORS*

(Index, Dec. 1982 = 100, ratio scale)




*Six-month moving average for all series shown. For contracts, total only includes private, while individual sectors include private and public. New commitments are the sum of permits and contracts.

Outlays for items other than transportation and computing equipment increased at an annual rate of 11 percent in the third quarter, and, on net, recent data on orders and shipments point to a further solid gain this quarter (chart). One particularly strong area in recent months has been communications equipment such as cellular phones and equipment for communications networks.

Turning to the recent detail on nonresidential construction, the expenditures for office buildings, which had plunged during the summer, flattened out in September and October. However, the long-run trend in this sector probably still is pointing downward. Construction in the "other commercial" sector dropped sharply in August but jumped back in September and held steady in October; its trend this year has been essentially sideways. Elsewhere, the uptrend in institutional construction that was evident earlier in the year appears to have moderated in recent months, and outlays for industrial structures continued weak in the early autumn.

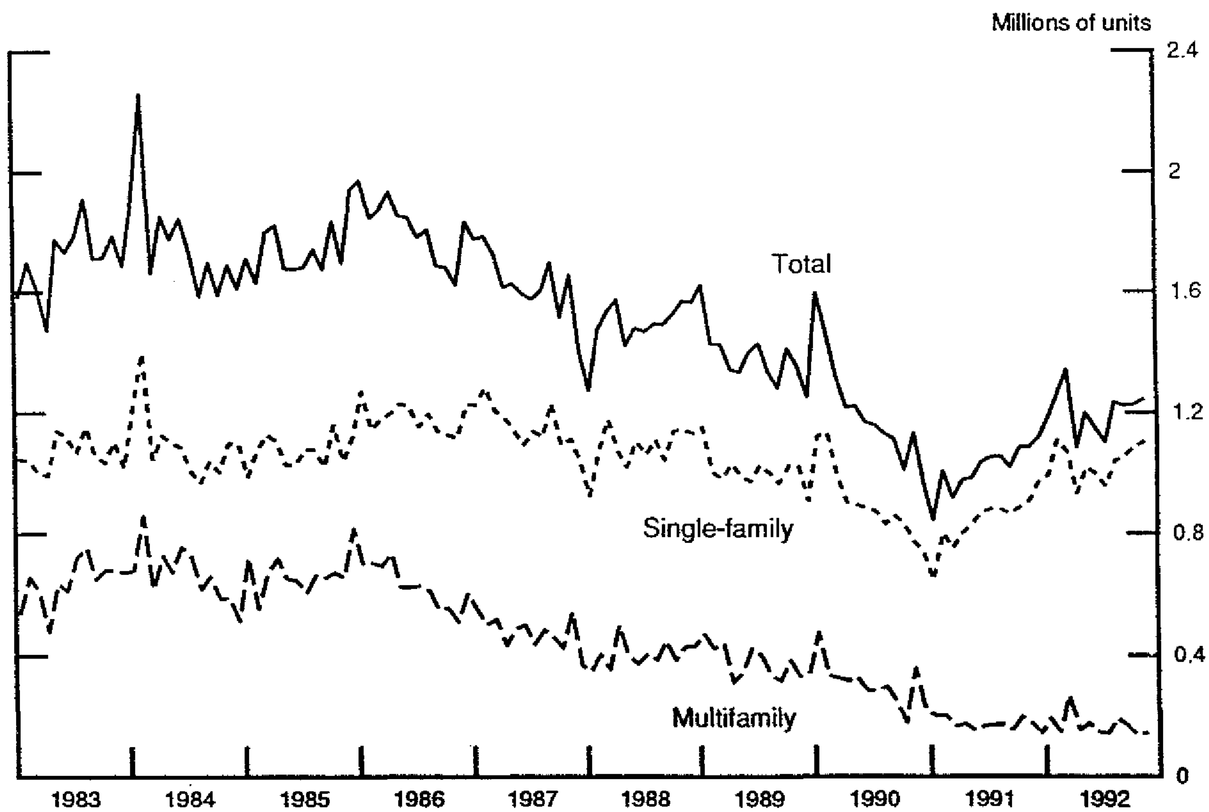
Price declines for office buildings and other commercial properties continued in the third quarter. According to the Russell-NCREIF index (chart), the national average of nominal appraised values for office properties fell 3-1/2 percent in that period. The values of retail properties and warehouses also declined. Other evidence of continued softening in prices comes from the FDIC's October Survey of Real Estate. Nearly one-third of the banking examiners and liquidators who responded to that survey reported continued declines in real estate prices, and only 5 percent reported price increases. The persistence of high office vacancy rates, especially in downtown locations, continues to be an important factor depressing prices.

PRIVATE HOUSING ACTIVITY
(Millions of units; seasonally adjusted annual rates)

| | 1991 | 1992 | | | 1992 | | |
|---|---|---|---|---|---|---|---|
| | Annual | Q1 | Q2 | Q3[r] | Sep.[r] | Oct.[r] | Nov.[p] |
| All units | | | | | | | |
| Permits | .95 | 1.12 | 1.05 | 1.09 | 1.13 | 1.14 | 1.12 |
| Starts | 1.01 | 1.26 | 1.14 | 1.19 | 1.22 | 1.22 | 1.24 |
| Single-family units | | | | | | | |
| Permits | .75 | .92 | .88 | .89 | .91 | .96 | .95 |
| Starts | .84 | 1.06 | .98 | 1.02 | 1.05 | 1.09 | 1.10 |
| Sales | | | | | | | |
| New homes | .51 | .62 | .56 | .64 | .67 | .60 | n.a. |
| Existing homes | 3.22 | 3.41 | 3.43 | 3.35 | 3.30 | 3.60 | n.a. |
| Multifamily units | | | | | | | |
| Permits | .20 | .19 | .17 | .20 | .21 | .18 | .17 |
| Starts | .17 | .20 | .16 | .17 | .17 | .14 | .14 |

p Preliminary. r Revised estimates. n.a. Not available.

PRIVATE HOUSING STARTS
(Seasonally adjusted annual rate)



PRICES OF COMMERCIAL BUILDINGS
(Percent change, national average)

| | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 |
|---|---|---|---|---|---|
| Russell-NCREIF index | | | | | |
| Office buildings | -8.5 | -17.5 | -1.7 | -4.0 | -3.5 |
| Retail stores | -.3 | -8.3 | -1.9 | -1.9 | -1.5 |
| Warehouses | -4.6 | -8.7 | -1.8 | -2.1 | -3.0 |

One recent bright spot in the nonresidential structures sector is drilling activity; the count of rigs in use jumped 9-1/2 percent in October and advanced 5 percent further last month. These gains are reportedly attributable to the increase in natural gas prices since last spring and to the expiration, at the end of the year, of a roughly $6 per barrel tax subsidy.[10] Presumably, the part of the recent increase in drilling activity that is related to the expiration of the tax subsidy is being borrowed from the future. Moreover, oil drilling in coming months likely will be adversely influenced by the recent slump in crude oil prices.

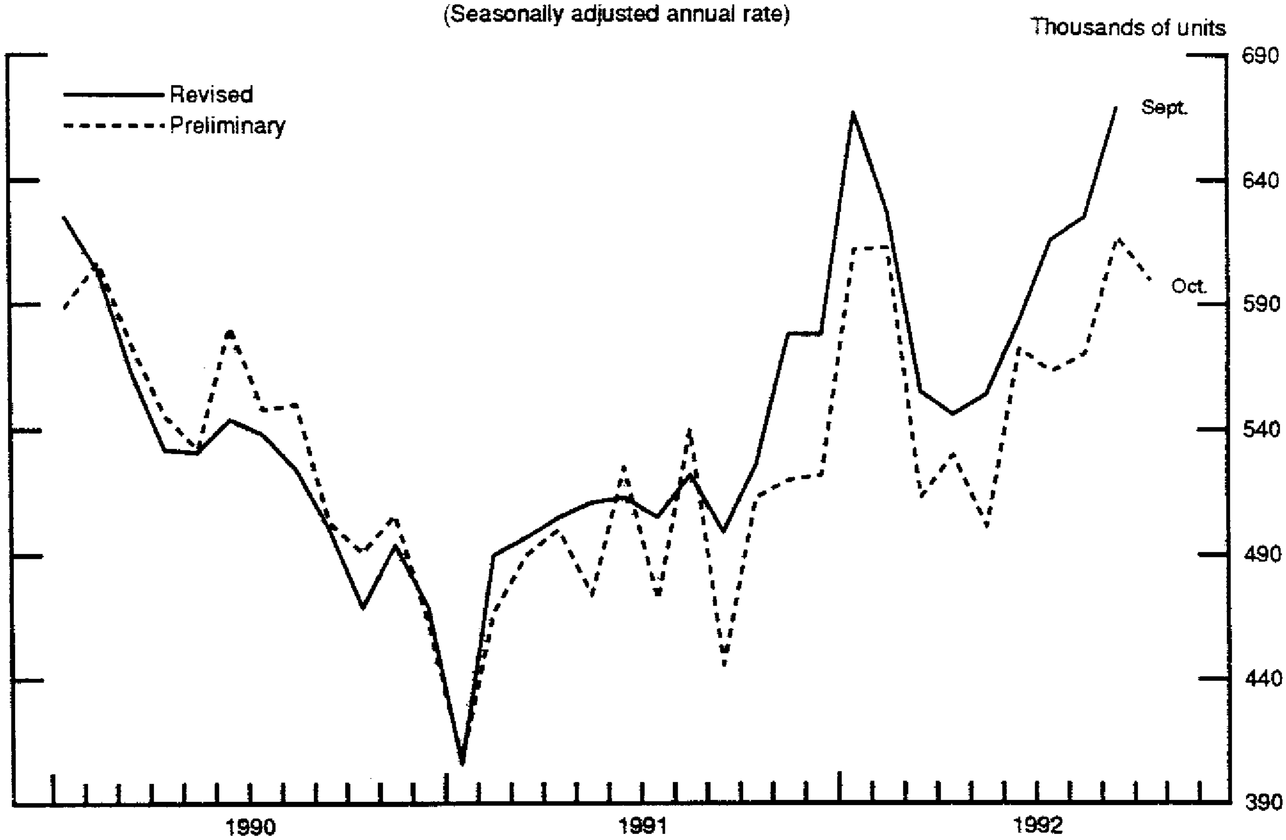
Housing Markets

Housing demand and production appear to be continuing on gradual recovery paths. Total housing starts in November were little changed from a month earlier, but single-family starts were revised upward for October and posted a further gain in November, to the highest level since February. By contrast, apartment building continues to be depressed. Since the housing trough early last year, single-family homebuilding has accounted for nearly 90 percent

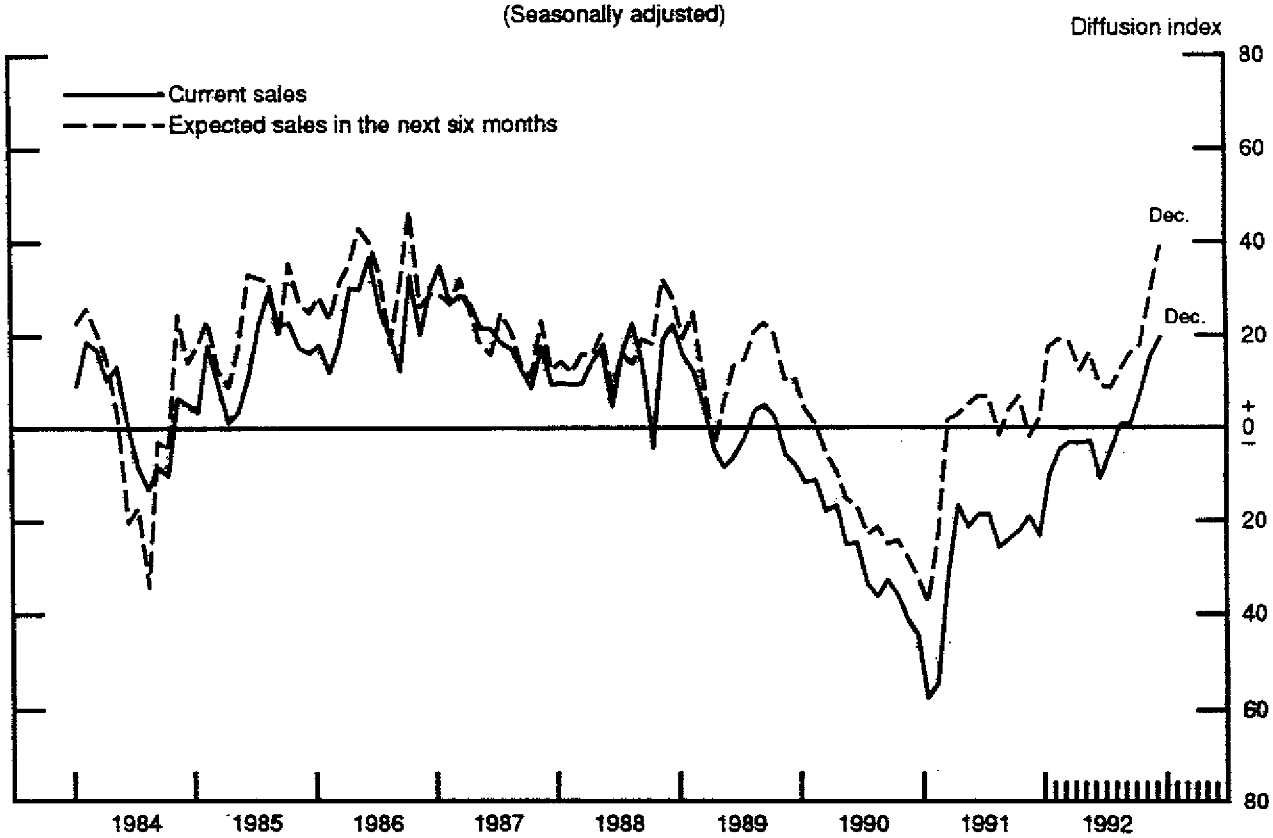
10. An economist at the American Gas Association estimates that about one-third of the recent uptick in drilling activity is attributable to the expiration of this subsidy; he argued that the rest of the increase reflects the usual response of drilling activity to higher prices.

# The Market for New Homes

Preliminary and Revised New Home Sales
(Seasonally adjusted annual rate)




Home Builders' Evaluations
(Seasonally adjusted)



of the increase in residential investment expenditures, a much higher share than in previous recoveries.

Home sales also have been firming. The estimate of new home sales in September was revised up to the highest monthly pace since late 1989. Because of continuing difficulties with the Census Bureau's new home survey, the preliminary estimate of a sharp decline in sales in October appears to be unreliable; the October figure likely will be revised upward, as has been the case with each preliminary monthly estimate this year (chart).[11] Additional evidence of stepped-up demand for new homes comes from builders surveyed by the National Association of Home Builders, whose evaluations of current and prospective home sales are the most positive since the mid-1980s. In the market for existing homes, sales jumped 9 percent in October to the highest monthly pace since 1988. A near-record 79 percent of consumers think "now is a good time to buy," according to the Michigan survey.

Recent evidence on the direction of house prices has been mixed. For the country as a whole, sales prices of new and existing homes in October were up 2 to 5 percent from a year earlier, a bit above other recent monthly readings. However, constant-quality price indexes, which are available only on a quarterly basis, have remained flat.

The cost of constructing new homes may be receiving some upward pressure from materials costs: Spot prices for plywood have jumped 24 percent since late October, and spot prices for lumber have risen 11 percent. The previous spike in these prices occurred in late summer, in the wake of Hurricane Andrew. In contrast, the recent increases in lumber and plywood prices appear to stem from the

---

11. The Census Bureau plans to introduce, perhaps as early as next month, new estimation procedures that should eliminate the bias in the preliminary estimate of monthly sales.

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars at annual rates;
based on seasonally adjusted data)

| | 1992 | | | 1992 | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Aug. | Sep. | Oct. |
| Current-cost basis | | | | | | |
| Total | -7.9 | 22.7 | 14.3 | 19.2 | -18.2 | -31.1 |
| Excluding auto dealers | -13.7 | 16.1 | 16.7 | 20.5 | -12.2 | -19.9 |
| Manufacturing | -11.2 | -1.5 | 6.1 | 25.3 | -14.5 | -6.8 |
| Excluding aircraft | -7.1 | 6.3 | 12.1 | 26.7 | -6.1 | -8.3 |
| Wholesale | -1.2 | 6.1 | -1.1 | 6.9 | -13.8 | -15.4 |
| Retail | 4.5 | 18.1 | 9.3 | -13.0 | 10.1 | -8.9 |
| Automotive | 5.8 | 6.6 | -2.3 | -1.3 | -6.0 | -11.2 |
| Excluding auto dealers | -1.3 | 11.5 | 11.7 | -11.6 | 16.1 | 2.2 |
| Constant-dollar basis | | | | | | |
| Total | -13.2 | 7.4 | 15.4 | 19.1 | -7.1 | n.a. |
| Excluding auto dealers | -18.0 | 1.9 | 13.8 | 13.0 | -3.8 | n.a. |
| Manufacturing | -8.7 | -6.5 | 4.5 | 20.4 | -14.5 | n.a. |
| Wholesale | -4.9 | 2.1 | .2 | 4.1 | -3.8 | n.a. |
| Retail | .5 | 11.8 | 10.8 | -5.4 | 11.2 | n.a. |
| Automotive | 4.8 | 5.5 | 1.6 | 6.1 | -3.3 | n.a. |
| Excluding auto dealers | -4.4 | 6.3 | 9.2 | -11.5 | 14.6 | n.a. |

INVENTORIES RELATIVE TO SALES[1]
(Months supply; based on seasonally adjusted data)

| | 1992 | | | 1992 | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Aug. | Sep. | Oct. |
| Current-cost basis | | | | | | |
| Total | 1.52 | 1.51 | 1.50 | 1.51 | 1.50 | 1.49 |
| Excluding auto dealers | 1.50 | 1.49 | 1.48 | 1.49 | 1.47 | 1.47 |
| Manufacturing | 1.62 | 1.57 | 1.57 | 1.60 | 1.56 | 1.57 |
| Excluding aircraft | 1.45 | 1.41 | 1.41 | 1.44 | 1.41 | 1.41 |
| Wholesale | 1.36 | 1.36 | 1.32 | 1.34 | 1.33 | 1.33 |
| Retail | 1.54 | 1.57 | 1.56 | 1.55 | 1.55 | 1.52 |
| Automotive | 1.85 | 1.90 | 1.86 | 1.89 | 1.84 | 1.73 |
| Excluding auto dealers | 1.46 | 1.48 | 1.48 | 1.47 | 1.47 | 1.46 |

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

improvement in the housing sector for the nation as a whole. Industry analysts speculate that the increasing evidence of a housing recovery and the likelihood of future increases in demand for wood products has caused some hoarding, which may be responsible for part of the recent increases in lumber and plywood prices.[12]

Business Inventories

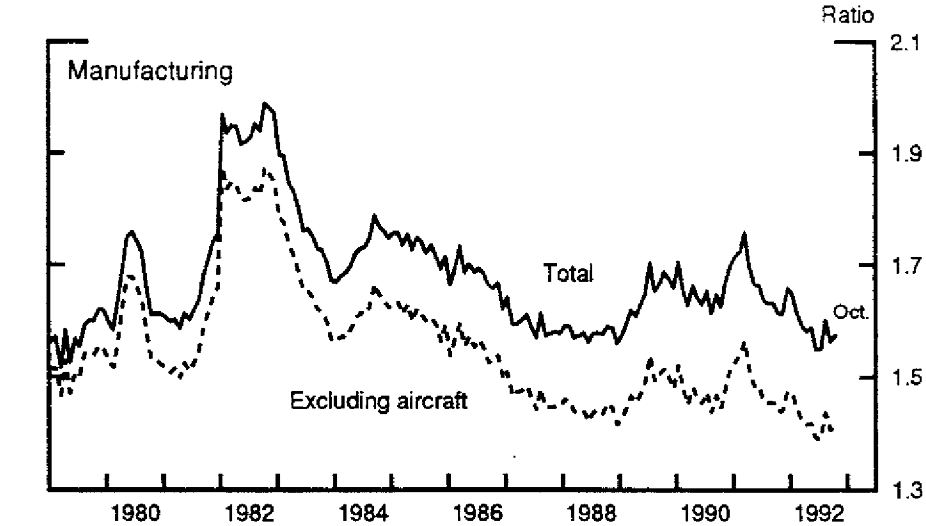
The business inventory situation has changed little over the last few months. Stocks in major sectors have remained broadly in line with sales (chart), and there have been no signs of serious overhangs either in the incoming data or in anecdotal reports. By the same token, there still is little hard evidence of firms moving more aggressively toward intended accumulation of stocks.

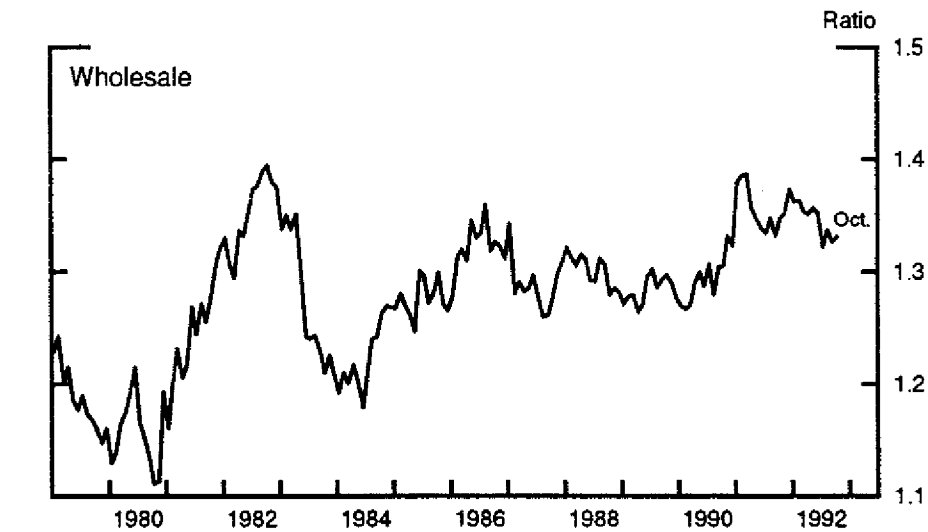
In the early part of the fourth quarter, manufacturers continued to show restraint in their inventory behavior. Factory stocks were reduced further in October, even as output expanded and new orders rose for the second month in a row. Nonetheless, the pace of inventory trimming was slower than in September. By stage of processing, the October drawdown was largely in inventories of materials and supplies, especially in the transportation equipment industry. Work-in-process inventories rose in October (again, a substantial part of it in transportation equipment), while stocks of finished goods were about unchanged.

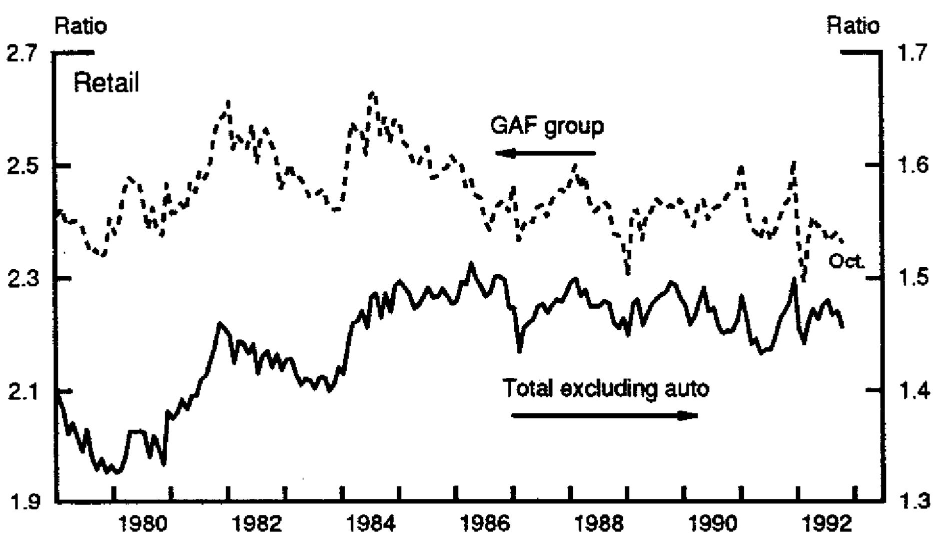
In the trade sector, retail inventories declined about $9 billion in October, with a sharp drop in the stocks held by auto dealers more than accounting for the decline. Excluding the auto sector, retail stocks increased only slightly in October, and, as a result of a strong increase in sales, the inventory-sales ratio for these stores edged down. For stores in the GAF grouping (that is,

12. Direct use of lumber in home building accounts for about 40 percent of total domestic lumber consumption.

# RATIO OF INVENTORIES TO SALES
(Current–cost data)



general merchandise, apparel, and furniture stores) the inventory-sales ratio fell to a relatively low level (chart, lower panel).

In the wholesale sector, inventories were drawn down $15-1/2 billion at an annual rate in October, after a downward-revised liquidation of nearly $14 billion in September. Wholesale inventory data at the industry level showed widespread declines in both September and October; two exceptions were the apparel and motor vehicles industries. The inventory-sales ratio for the merchant wholesale sector in October was near the low end of the range observed over the past two years (chart, middle panel).

Federal Sector

With the Congress in recess and the incoming administration forging its fiscal plans, the news on the federal sector is relatively light.

The unified federal budget showed a deficit of $49 billion in October, an increase of $12 billion from the deficit recorded in the same month of 1991. Nearly all of the increase was on the outlays side. A shift in the timing of disbursements for military pay, veterans' benefits, and social security payments accounted for about $5 billion of the rise in outlays; these payments were moved forward into October because November 1, the normal date of disbursement, came on a weekend. Most of the remaining increase in outlays resulted from increased spending on Medicaid, Medicare, income security, and social security.

Defense outlays resumed their downward trend in October, after a temporary bulge in the third quarter.[13] After adjustment for

13. The degree to which the third-quarter bulge in real defense expenditures translated into increased production of goods and services is not altogether clear. In particular, about half of the third-quarter bulge in defense outlays was accounted for by increased spending for durable goods, but defense inventories held by manufacturers fell by roughly the same amount. Taken at face value, these data would seem to suggest that the rise in outlays for
(Footnote continues on next page)

FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis; billions of dollars, except where noted)

| | Fiscal year to date | | | |
|---|---|---|---|---|
| | Oct. 1991 | Oct. 1992 | Dollar change | Percent change |
| Outlays | 114.7 | 125.7 | 11.0 | 9.6 |
| Deposit insurance (DI) | -.8 | -2.6 | -1.8 | 240.1 |
| Defense Cooperation account (DCA) | -1.2 | .0 | 1.2 | -97.6 |
| Outlays excluding DI and DCA | 116.7 | 128.3 | 11.6 | 10.0 |
| National defense | 25.1 | 27.4 | 2.4 | 9.5 |
| Net interest | 16.8 | 16.5 | -.3 | -1.8 |
| Social security | 22.7 | 24.3 | 1.7 | 7.3 |
| Medicare and health | 17.2 | 19.0 | 1.8 | 10.7 |
| Income security | 14.3 | 18.3 | 4.0 | 28.1 |
| Other | 20.7 | 22.8 | 2.1 | 10.0 |
| Receipts | 78.1 | 76.8 | -1.2 | -1.6 |
| Personal income taxes | 40.1 | 37.3 | -2.8 | -7.0 |
| Social insurance taxes | 28.4 | 29.6 | 1.2 | 4.1 |
| Corporate income taxes | .4 | 2.1 | 1.7 | 391.1 |
| Other | 9.1 | 7.9 | -1.3 | -13.9 |
| Deficit(+) | 36.6 | 48.9 | 12.3 | 33.5 |
| excluding DI and DCA | 38.6 | 51.5 | 12.9 | 33.4 |

Note: Components may not sum to totals because of rounding.

the shift in paydates, defense spending amounted to $24.6 billion in October, compared with an average of $25.8 billion over the first nine months of calendar 1992. In real terms, the October level of these outlays was down about 6 percent from that of a year earlier.

Federal employment shrank in October and November, reflecting implementation by the Postal Service of a reorganization plan which was to eliminate 30,000 management and support jobs via an early retirement program. A larger-than-expected number of workers (about 47,000) accepted early retirement, and the Postal Service plans to replace some of those retirees; long-term hiring plans call for an additional 12,000 employees.

State and Local Government Sector

After a jump early in the year, the real purchases of state and local governments have risen only slightly, on net, over the past couple of quarters, and the indicators for the current quarter are mixed. Employment jumped in November after edging down the month before, but most of the November advance reflected the temporary hiring of election workers. Meanwhile, real outlays for state and local construction projects edged down in October to a level 1.0 percent below the third-quarter average. The largest declines were in outlays for highways and hospitals.

For the year to date, state and local construction outlays have been running at a level well above that of 1991. Construction of educational facilities has risen a bit further this year, after strong gains over the previous few years, and spending for other

(Footnote continued from previous page)

durable goods did not generate any new production in the third quarter; however, the data are sufficiently unreliable as to make one wary of such a strong conclusion. The remaining portion of the third-quarter spending bulge reflected a rise in the outlays for defense services (other than compensation); that gain was more clearly an increment to current production in the third quarter.

types of buildings is up considerably. Outlays for roads and highways also have increased appreciably this year: over the first ten months of 1992, the average level of these expenditures, in real terms, was more than 13 percent above the annual average for 1991. Federally funded spending accounts for roughly half of total state and local outlays on all highways and related structures and appears to have been one important factor supporting the recent rise in that category of expenditure. The Intermodal Surface Transportation Efficiency Act of 1991 authorized the Department of Transportation to spend up to $20.4 billion on highways in each of the five fiscal years starting in 1993; although appropriations have fallen well short of this level, they have moved up considerably since FY1991, and actual outlays also have increased.

Many states and localities continue to experience severe budgetary pressures. More than three-fifths of the states say that revenues in fiscal 1992 (July to June for most states) fell short of levels projected when the budgets were passed. As for FY93, many states reportedly are planning reductions, in real terms, in their general fund spending; in some cases lawmakers are said to be making new efforts to impose greater restraint on entitlements. Hiring, especially at the state level, also appears likely to be restrained. Indeed, many states are planning to reduce employment in 1993, with the largest decreases slated to be in New Jersey, Michigan, and Massachusetts. In addition, about one-third of the states are planning no rise in compensation for state employees during fiscal 1993. Localities, on the whole, may be faring a little better, as employment at that level has increased about 3 percent since the end of 1990, compared with only a 1 percent rise at the state level.

Prices

After a string of good reports on inflation, the data for the last couple of months have been somewhat less favorable. In October and November, the consumer price index for items other than food and energy rose 0.5 and 0.3 percent, respectively, after five consecutive increases of only 0.2 percent. Nonetheless, there seems to be little reason to think that the underlying inflation trends have worsened: A considerable degree of slack remains in the domestic economy; the dollar has appreciated, on balance, in recent months; and crude oil prices have been falling of late.

Prices of consumer commodities other than food and energy were boosted in October by sharply higher prices for apparel, tobacco, and used cars. In November, however, the prices of apparel and tobacco stabilized, and increases were small, on net, for the remaining commodities. In the services category, airfares surged in October and November, as companies sought to restore profit margins that had been squeezed by the promotions of last summer; recently, however, renewed fare discounting has been reported. The cost of shelter also jumped in October, but a smaller increase was posted in that category in November. Despite the recent bumpiness, the trend in core inflation still appears to be headed downward; for the twelve months ended in November, the CPI excluding food and energy rose 3.4 percent, compared with 4.5 percent over the preceding twelve-month period.

Inflation expectations, as measured by the Michigan consumer survey's mean expected price change over the next twelve months, jumped a full percentage point in November to 4.6 percent; however, this rise was fully reversed in December, according to the preliminary reading for that month. Such monthly volatility in the mean estimate of inflation expectations usually can be traced to

RECENT CHANGES IN PRODUCER PRICES
(Percent change; based on seasonally adjusted data)[1]

| | Relative importance Dec. 1991 | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|---|
| | | | | -----Annual rate------ | | | -Monthly rate- | |
| Finished goods | 100.0 | 5.7 | -.1 | 1.0 | 3.3 | 1.6 | .1 | -.2 |
| Consumer foods | 21.9 | 2.6 | -1.5 | .3 | -1.0 | 3.6 | .1 | -.5 |
| Consumer energy | 13.8 | 30.7 | -9.6 | -7.0 | 17.9 | -.5 | 1.4 | -1.5 |
| Other finished goods | 64.2 | 3.5 | 3.1 | 3.7 | 1.8 | 1.2 | -.1 | .1 |
| Consumer goods | 39.5 | 3.7 | 3.4 | 3.6 | 2.4 | 1.2 | -.1 | .2 |
| Capital equipment | 24.7 | 3.4 | 2.5 | 3.5 | .9 | .9 | -.2 | .1 |
| Intermediate materials[2] | 95.3 | 4.6 | -2.7 | .0 | 5.4 | .3 | .0 | -.2 |
| Excluding food and energy | 81.7 | 1.9 | -.8 | 1.7 | 1.7 | 1.0 | -.2 | .0 |
| Crude food materials | 41.2 | -4.2 | -5.8 | 11.8 | 1.9 | -6.2 | .6 | -.6 |
| Crude energy | 40.0 | 19.1 | -16.6 | -26.6 | 51.5 | 16.4 | -.5 | .6 |
| Other crude materials | 18.7 | .6 | -7.6 | 15.0 | 4.8 | 2.5 | -1.3 | -.9 |

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
(Percent change; based on seasonally adjusted data)[1]

| | Relative importance Dec. 1991 | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|---|
| | | | | -----Annual rate------ | | | -Monthly rate- | |
| All items[2] | 100.0 | 6.1 | 3.1 | 3.5 | 2.6 | 2.6 | .4 | .2 |
| Food | 16.0 | 5.3 | 1.9 | 1.5 | -1.2 | 4.7 | .0 | .0 |
| Energy | 7.4 | 18.1 | -7.4 | -6.9 | 12.5 | .4 | .5 | .8 |
| All items less food and energy | 76.6 | 5.2 | 4.4 | 4.8 | 2.8 | 2.5 | .5 | .3 |
| Commodities | 24.8 | 3.4 | 4.0 | 5.3 | 2.1 | 2.1 | .3 | .1 |
| Services | 51.9 | 6.0 | 4.6 | 4.8 | 2.9 | 2.6 | .6 | .3 |
| Memorandum: | | | | | | | | |
| CPI-W[3] | 100.0 | 6.1 | 2.8 | 3.0 | 2.7 | 2.9 | .4 | .2 |

1. Changes are from final month of preceding period to final month of period indicated.
2. Official index for all urban consumers.
3. Index for urban wage earners and clerical workers.

changes in the number of survey respondents who expect very large increases in prices over the next twelve months (table). By contrast, the median of the distribution, which is less sensitive to such outliers, exhibits smaller monthly fluctuations; it has remained in the neighborhood of 3 percent since late last year.[14]

The CPI for food has flattened in the past two months after a spurt in August and September. Fruit and vegetable prices have been responsible for much of the volatility in food prices for some time now; they fell sharply in the spring, rebounded in late summer, and recently have turned down once again. Apart from fruit and vegetable prices, increases in food prices have been quite subdued in the past year, and recent reports on crop and livestock production suggest no shortfalls that might pose a serious threat to the continuation of this trend.

After rising 0.5 percent in October, consumer energy prices moved up an additional 0.8 percent in November. Gasoline prices rose sharply in November as a drop in crude oil costs was more than offset by the effect of new federal requirements for winter-season additives that are designed to reduce the formation of smog. Industry analysts say that the new regulations, which went into effect in thirty-nine major metropolitan areas at the start of November, will raise costs by three to five cents per gallon. The regulations will be in effect in at least some cities until the end of February. Meanwhile, further declines in crude oil prices in recent weeks suggest that softer gasoline and heating oil prices may be in the offing in coming months; indeed, at the producer level,

---

14. The median is less volatile than the mean and therefore gives a more reliable signal of changes in expectations. However, the median gives a forecast of inflation that is biased downward. By contrast, the mean forecast is unbiased. After adjustment for the historical bias in the median forecast, both measures indicate that consumers expect inflation to run at about 4 percent next year, well above this year's apparent outcome.

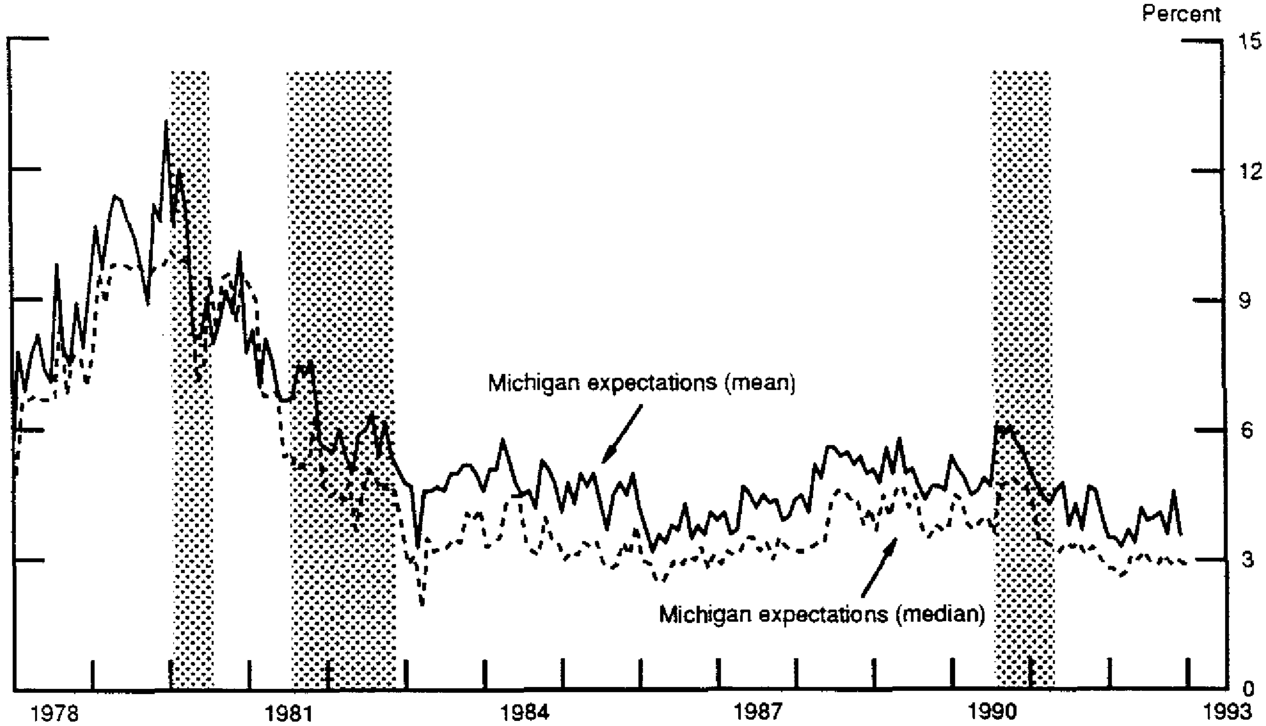
INFLATION RATES EXCLUDING FOOD AND ENERGY

| | Percent change from twelve months earlier | | |
|---|---|---|---|
| | Nov. 1990 | Nov. 1991 | Nov. 1992 |
| CPI | 5.3 | 4.5 | 3.4 |
| Goods | 3.1 | 4.4 | 2.5 |
| Alcoholic beverages | 4.3 | 10.0 | 2.9 |
| New vehicles | 1.8 | 3.7 | 2.6 |
| Apparel | 4.2 | 4.4 | .9 |
| Housefurnishings | .6 | .9 | 1.4 |
| Housekeeping supplies | 3.3 | 2.5 | .5 |
| Entertainment | 3.2 | 3.7 | 1.8 |
| Services | 6.2 | 4.5 | 3.9 |
| Owners' equivalent rent | 5.0 | 3.7 | 3.0 |
| Tenants' rent | 4.1 | 3.1 | 2.5 |
| Other renters' costs | 13.1 | 7.8 | 5.9 |
| Airline fares | 18.6 | -5.2 | 9.0 |
| Medical care | 9.8 | 7.9 | 7.3 |
| Entertainment | 5.6 | 5.1 | 2.8 |
| PPI Finished goods | 3.6 | 3.1 | 2.0 |
| Consumer goods | 3.9 | 3.4 | 2.1 |
| Capital equipment, excluding computers | 3.2 | 2.6 | 2.3 |
| Computers | n.a. | n.a. | -15.8 |
| PPI intermediate materials | 1.8 | -1.0 | 1.0 |
| PPI crude materials | .2 | -8.3 | 2.8 |
| Factors Affecting Price Inflation | | | |
| ECI hourly compensation[1] | 4.9 | 4.5 | 3.4 |
| Goods-producing | 5.0 | 4.5 | 3.9 |
| Service-producing | 4.8 | 4.5 | 3.1 |
| Civilian unemployment rate[2] | 6.0 | 6.9 | 7.2 |
| Capacity utilization[2] (manufacturing) | 80.7 | 78.2 | 77.9 |
| Non-oil import prices[3] | 2.4 | .4 | 2.8 |
| Consumer goods, excluding autos, food, and beverages | 3.6 | .5 | 3.7 |
| Autos | 1.0 | 4.2 | 2.3 |

1. Private industry workers, periods ended in September.
2. End-of-period value.
3. BLS import price index (not seasonally adjusted), periods ended in September.
n.a. - not available

# INFLATION EXPECTATIONS

(Michigan Survey)




EXPECTED CHANGE IN PRICES DURING THE NEXT 12 MONTHS

| | 1991 | 1992 | | | 1992 | | | |
|---|---|---|---|---|---|---|---|---|
| | Q4 | Q1 | Q2 | Q3 | Sep. | Oct. | Nov. | Dec.(p) |
| Mean increase | 4.4 | 3.4 | 3.8 | 4.0 | 4.1 | 3.6 | 4.6 | 3.6 |
| Standard deviation | 7.6 | 5.6 | 5.4 | 5.9 | 5.7 | 5.7 | 7.3 | 5.3 |
| Median increase | 3.1 | 2.7 | 3.1 | 3.0 | 3.1 | 2.9 | 3.0 | 2.9 |
| | -------------percent of respondents------------ | | | | | | | |
| Same or down | 26 | 34 | 25 | 25 | 24 | 29 | 2.3 | n.a. |
| Will go up by: | | | | | | | | |
| 1-2 % | 14 | 13 | 15 | 17 | 14 | 15 | 18 | n.a. |
| 3-5 % | 37 | 33 | 38 | 35 | 41 | 37 | 37 | n.a. |
| 6-9 % | 6 | 5 | 5 | 5 | 5 | 5 | 4 | n.a. |
| 10-14 | 6 | 7 | 7 | 7 | 7 | 5 | 8 | n.a. |
| 15% or higher | 5 | 3 | 3 | 5 | 4 | 3 | 5 | n.a. |
| NA, don't know | 5 | 4 | 6 | 4 | 4 | 5 | 1 | n.a. |

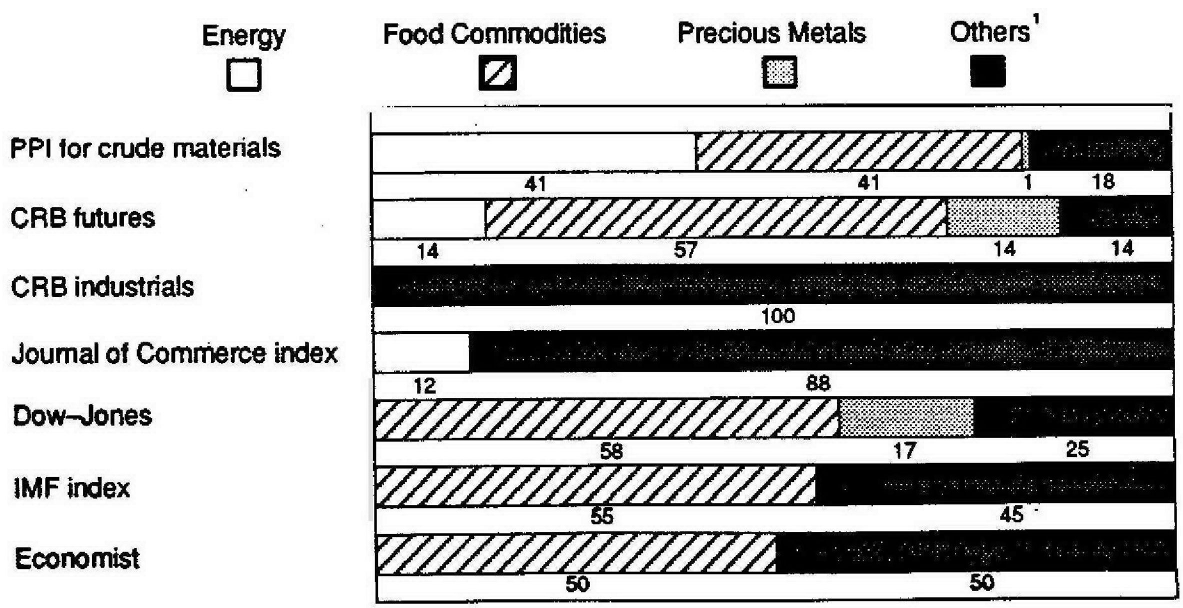
PRICE INDEXES FOR COMMODITIES AND MATERIALS[1]

| | Last observation | Percent change[2] 1990 | 1991 | 1992 To Nov. 10[3] | 1992 Nov. 10[3] to date | Memo Year earlier to date |
|---|---|---|---|---|---|---|
| 1. PPI for crude materials[4] | Nov. | 6.0 | -11.6 | 3.9 | n.a. | 1.8 |
| 1a. Foods and feeds | Nov. | -4.2 | -5.8 | 1.2 | n.a. | 1.3 |
| 1a. Energy | Nov. | 19.1 | -16.6 | 6.8 | n.a | 2.6 |
| 1b. Excluding food and energy | Nov. | .6 | -7.6 | 3.3 | n.a. | 2.8 |
| 1c. Excluding food and energy, seasonally adjusted | Nov. | .7 | -7.6 | 3.1 | n.a. | 2.8 |
| 2. Commodity Research Bureau | | | | | | |
| 2a. Futures prices | Dec. 15 | -2.7 | -6.5 | -4.1 | 1.4 | -3.8 |
| 2b. Industrial spot prices | Dec. 15 | .6 | -11.3 | -.6 | .6 | -.4 |
| 3. *Journal of Commerce* industrials | Dec. 15 | -2.4 | -7.2 | 2.9 | -.2 | 2.9 |
| 3a. Metals | Dec. 15 | -3.9 | -7.1 | -.3 | .9 | .7 |
| 4. Dow-Jones Spot | Dec. 15 | -1.7 | -12.1 | 4.0 | 7.0 | 7.9 |
| 5. IMF commodity index[4] | Oct. | -5.2 | .7 | -3.4 | n.a. | -3.7 |
| 5a. Metals | Oct. | -1.1 | -8.9 | -.4 | n.a. | -1.8 |
| 5b. Nonfood agriculture | Oct. | -3.5 | 1.3 | 3.5 | n.a. | 3.4 |
| 6. *Economist* (U.S. dollar index) | Dec. 8 | -4.4 | -9.1 | -3.1 | 2.9 | .2 |
| 6a. Industrials | Dec. 8 | -3.2 | -14.9 | -1.6 | 3.2 | 2.1 |

1. Not seasonally adjusted.
2. Change is measured to end of period, from last observation of previous period
3. Week of the November Greenbook.
4. Monthly observations. IMF index includes items not shown separately.

n.a. Not available

## Index Weights



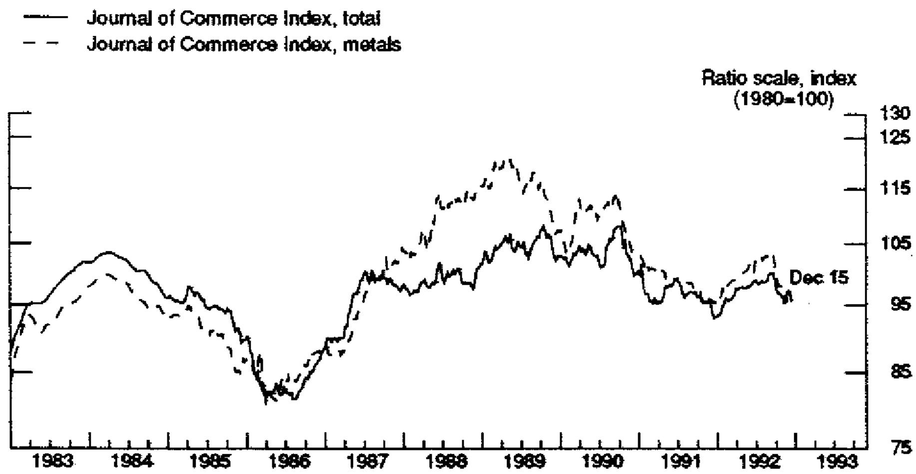

1. Forest products, industrial metals, and other industrial materials.

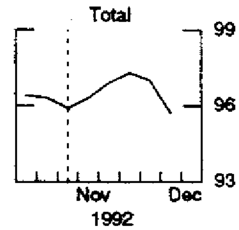
the prices of these products already were down by a considerable amount in November. Natural gas prices in the CPI moved up sharply in November, as the spike in spot-market price increases associated with Hurricane Andrew was passed on to the consumer level. Much of this increase should be reversed in coming months, as spot prices for natural gas have returned most of the way to their pre-hurricane level.

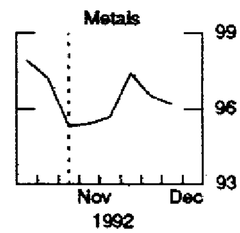
Producer prices at the finished level declined 1/4 percent in November, pulled down by the large declines in gasoline and fuel oil prices and a 1/2 percent decline in food prices. Excluding food and energy, the PPI increased 0.1 percent last month, a bit less than the average pace over the previous twelve months. Automobile prices were up 1 percent in November, but this followed a decline of more than 2 percent in October. Auto manufacturers apparently introduced price discounts earlier than usual, leading to swings in the seasonally adjusted numbers. At earlier stages of processing, prices of intermediate materials other than food and energy have been about flat in recent months. Over the past twelve months, intermediate materials prices have risen about 1 percent, after falling by a similar amount over the preceding twelve months.

Prices of industrial commodities have changed relatively little since the last Greenbook (table and chart). However, prices of forest products (plywood and lumber) are up sharply; as noted earlier, recent price increases in this sector may reflect, in part, expectations in the industry of stronger demand for new housing. Prices of farm crops (corn, wheat, and soybeans) also have moved up in recent weeks from earlier lows; stronger-than-expected exports of wheat, weather-related lags in the corn harvest, and normal seasonal influences appear to be the chief causes of these increases. Finally, in the oil market, the spot price of West Texas

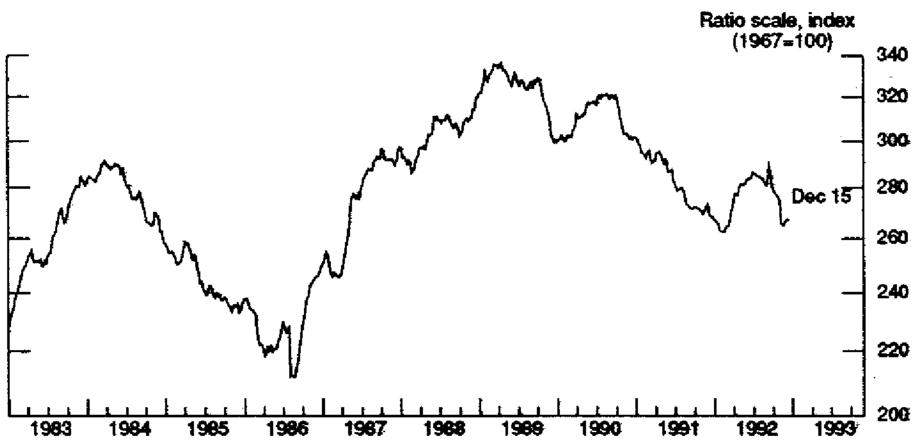
# COMMODITY PRICE MEASURES *

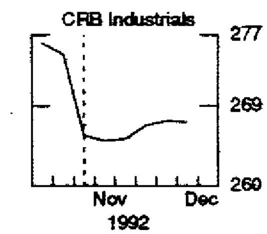


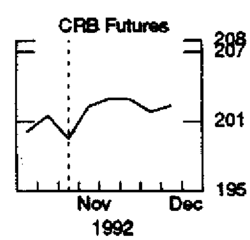




CRB Spot Industrials




CRB Futures

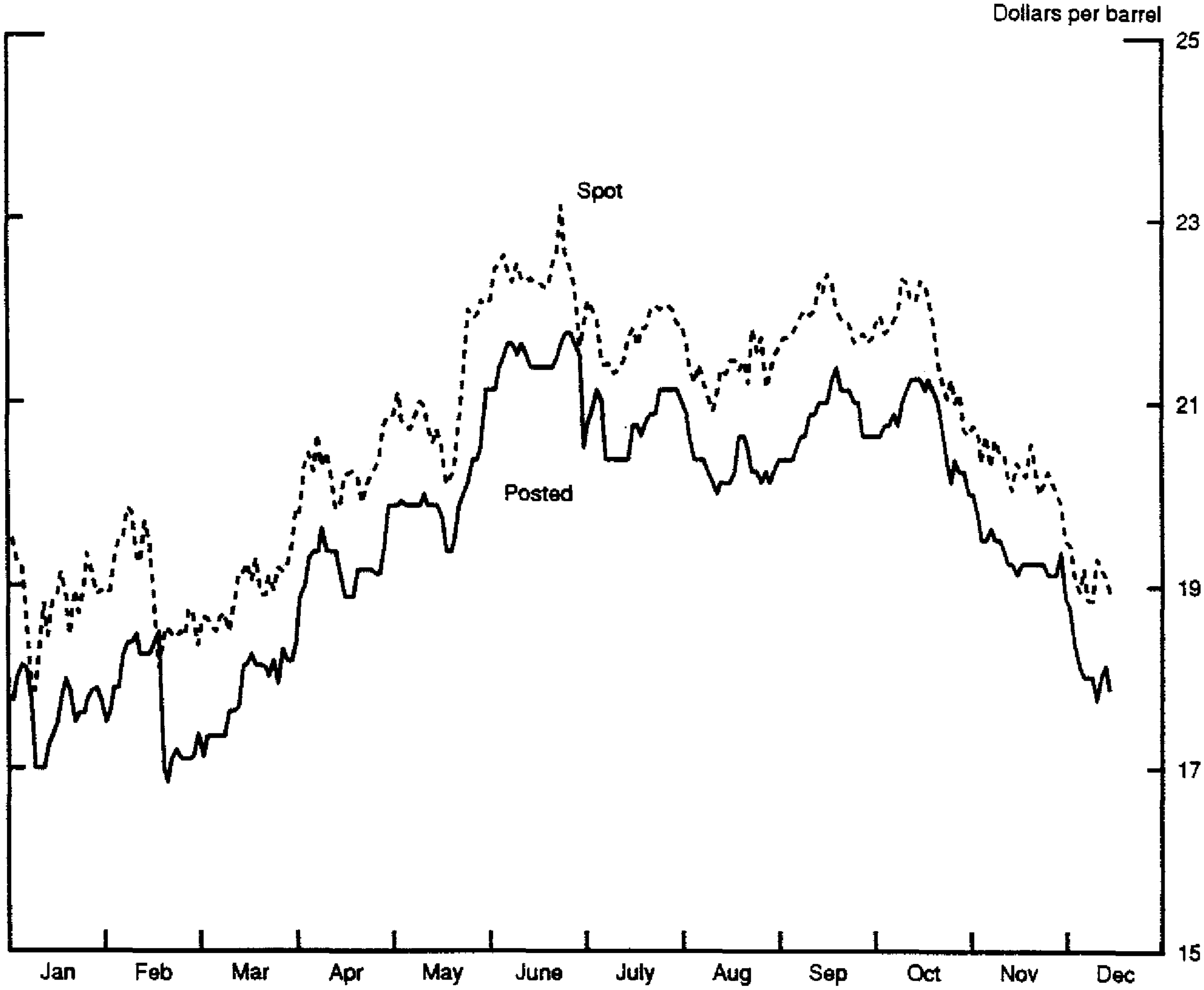




* Weekly data, Tuesdays; Journal of Commerce data monthly before 1985

Dotted lines indicate week of last Greenbook.

Intermediate has come down about $1.50 per barrel since the last Greenbook, as the recent OPEC agreement to curtail production apparently has failed to impress the markets.

## Daily Spot and Posted Prices of West Texas Intermediate [1]




1. Posted prices are evaluated as the mean of the range listed in the Wall Street Journal.

### MONTHLY AVERAGE PRICES—WEST TEXAS INTERMEDIATE

| Year and Month | Posted | Spot |
|---|---|---|
| 1992 | | |
| January | 17.63 | 18.82 |
| February | 17.72 | 19.00 |
| March | 17.81 | 18.92 |
| April | 19.20 | 20.24 |
| May | 19.90 | 20.94 |
| June | 21.46 | 22.38 |
| July | 20.77 | 21.76 |
| August | 20.32 | 21.35 |
| September | 20.83 | 21.90 |
| October | 20.77 | 21.68 |
| November | 19.38 | 20.34 |
| December [1] | 18.17 | 19.13 |

1. Price through December 15.

# DOMESTIC FINANCIAL DEVELOPMENTS

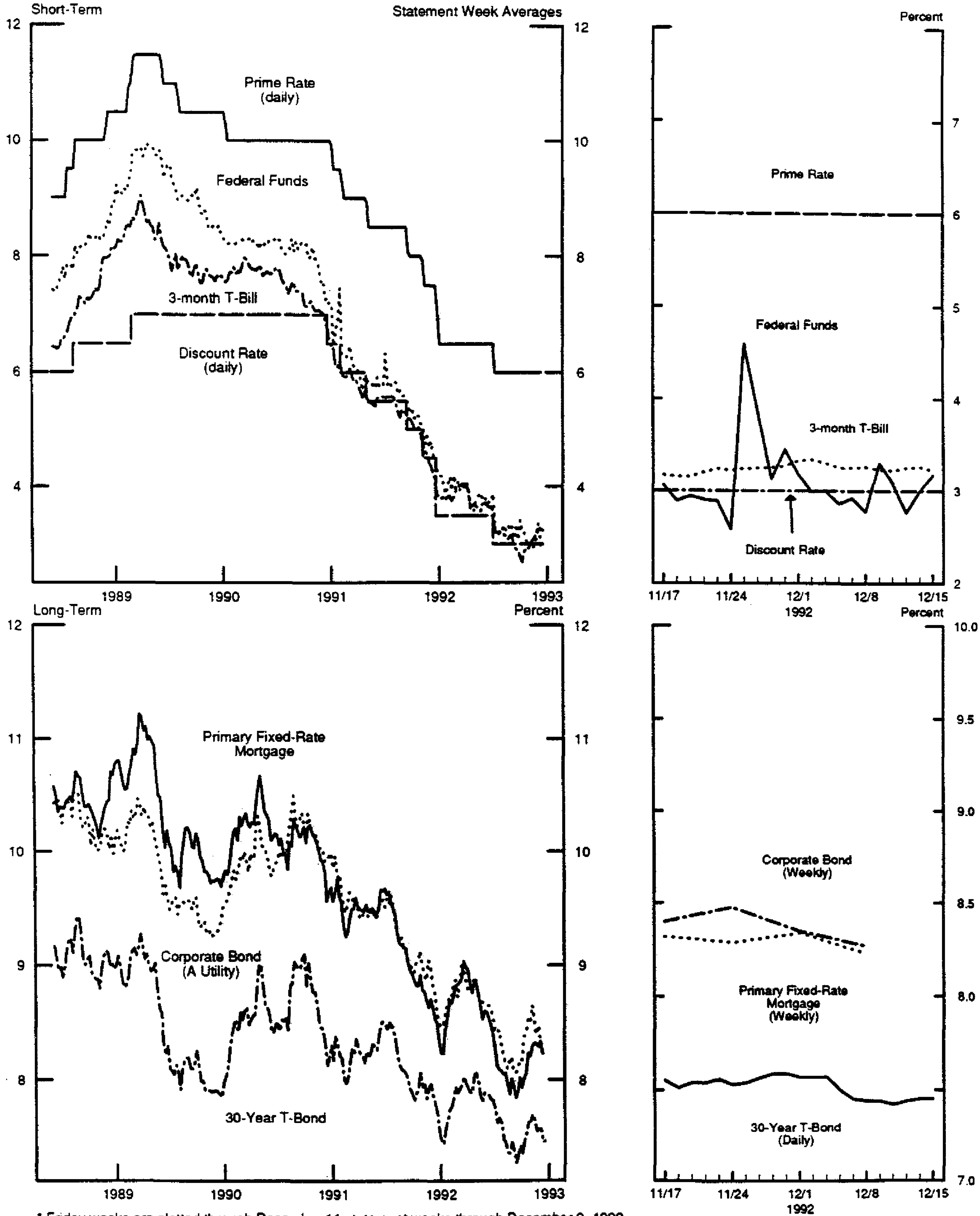
# SELECTED FINANCIAL MARKET QUOTATIONS[1]
(percent)

| | 1992 Sept 4 | 1992 FOMC Nov 17 | 1992 Dec 15 | Change from: Sept 4 | Change from: FOMC Nov 17 |
|---|---|---|---|---|---|
| **Short-term rates** | | | | | |
| Federal funds[2] | 3.19 | 3.04 | 2.92 | -.27 | -.12 |
| Treasury bills[3] | | | | | |
| 3-month | 2.92 | 3.17 | 3.22 | .30 | .05 |
| 6-month | 2.96 | 3.38 | 3.40 | .44 | .02 |
| 1-year | 3.06 | 3.54 | 3.63 | .57 | .09 |
| Commercial paper | | | | | |
| 1-month | 3.22 | 3.29 | 3.80 | .58 | .51 |
| 3-month | 3.22 | 3.83 | 3.71 | .49 | -.12 |
| Large negotiable CDs[3] | | | | | |
| 1-month | 3.06 | 3.18 | 3.58 | .52 | .40 |
| 3-month | 3.06 | 3.77 | 3.49 | .43 | -.28 |
| 6-month | 3.11 | 3.77 | 3.57 | .46 | -.20 |
| Eurodollar deposits[4] | | | | | |
| 1-month | 3.31 | 3.13 | 3.56 | .25 | .43 |
| 3-month | 3.31 | 3.88 | 3.50 | .19 | -.38 |
| Bank prime rate | 6.00 | 6.00 | 6.00 | .00 | .00 |
| **Intermediate- and long-term rates** | | | | | |
| U.S. Treasury (constant maturity) | | | | | |
| 3-year | 4.38 | 5.21 | 5.29 | .91 | .08 |
| 10-year | 6.40 | 6.86 | 6.83 | .43 | -.03 |
| 30-year | 7.29 | 7.55 | 7.45 | .16 | -.10 |
| Municipal revenue[5] (Bond Buyer) | 6.31 | 6.57 | 6.46 | .15 | -.11 |
| Corporate--A utility recently offered | 8.06 | 8.45 | 8.27 | .21 | -.18 |
| Home mortgage rates[6] | | | | | |
| FHLMC 30-yr. FRM | 7.84 | 8.32 | 8.23 | .39 | -.09 |
| FHLMC 1-yr. ARM | 5.15 | 5.20 | 5.47 | .32 | .27 |

| | Record highs | Date | 1989 Lows Jan 3 | 1992 FOMC Nov 17 | 1992 Dec 15 | Percent change from: Record highs | 1989 lows | FOMC Nov 17 |
|---|---|---|---|---|---|---|---|---|
| **Stock prices** | | | | | | | | |
| Dow-Jones Industrial | 3413.21 | 6/1/92 | 2144.64 | 3193.32 | 3284.36 | -3.78 | 53.14 | 2.85 |
| NYSE Composite | 240.24 | 12/8/92 | 154.00 | 231.09 | 238.02 | -.92 | 54.56 | 3.00 |
| AMEX Composite | 418.99 | 2/12/92 | 305.24 | 384.29 | 390.66 | -6.76 | 27.98 | 1.66 |
| NASDAQ (OTC) | 667.12 | 12/8/92 | 378.56 | 627.07 | 650.75 | -2.45 | 71.90 | 3.78 |
| Wilshire | 4278.27 | 12/8/92 | 2718.59 | 4101.16 | 4232.63 | -1.07 | 55.69 | 3.21 |

1/ One-day quotes except as noted.
2/ Average for two-week reserve maintenance period closest to date shown. Last observation is average to date for maintenance period ending December 23, 1992.
3/ Secondary market.
4/ Bid rates for Eurodollar deposits at 11 a.m. London time.
5/ Based on one-day Thursday quotes and futures market index changes.
6/ Quotes for week ending Friday previous to date shown.

## Selected Interest Rates*




* Friday weeks are plotted through December 11 statement weeks through December 9, 1992.

## DOMESTIC FINANCIAL DEVELOPMENTS

The federal funds rate has remained around 3 percent over the intermeeting period, and other short-term rates have registered mixed changes. Likely responding in part to increased supply, yields on Treasury bills have risen slightly. One-month private rates rose sharply around December 1st, as maturity dates crossed year-end, but have declined somewhat since then. Most 3- to 6-month private rates have fallen, probably reflecting lessened year-end pressures and perceptions of reduced credit risk as the economy strengthened. Bond rates rose in the first part of the intermeeting period on evidence of a more robust economy, but they have declined about 10 basis points on balance, partly because concerns have diminished about the odds of a deficit-expanding fiscal package next year. Stock prices have risen between 2 and 4 percent in the intermeeting period; most of the major indexes--with the notable exception of the Dow-Jones Industrials--set record highs in early December.

Private borrowing appears to have picked up in the fourth quarter. In the household sector, consumer installment credit registered a further slight increase in October. In addition, it seems likely that home mortgage debt will accelerate because of increased home sales and some liquification of home equity in refinancing transactions. Short-term borrowing by nonfinancial businesses was strong in November, as outstanding commercial paper grew rapidly and business loans at banks also advanced; part of the pickup in short-term borrowing, however, reflected a shift from bond markets. Overall, borrowing by nonfinancial firms thus probably has been limited, but this is a substantial change from the slight declines recorded in the second and third quarters. Equity issuance in the fourth quarter continues near its reduced third-quarter pace.

MONETARY AGGREGATES
(based on seasonally adjusted data unless otherwise noted)

| | 1991[1] | 1992 Q2 | 1992 Q3 | 1992 Sep | 1992 Oct | 1992 Nov p | Growth Q4 91- Nov 92p |
|---|---|---|---|---|---|---|---|
| | ------------Percent change at annual rates------------ | | | | | | |
| 1. M1 | 8.0 | 9.8 | 10.3 | 19.1 | 22.7 | 14.2 | 14.5 |
| 2. M2 | 2.8 | 0.4 | 0.1 | 3.5 | 5.1 | 3.4 | 2.2 |
| 3. M3 | 1.2 | -1.3 | -0.2 | 1.7 | 0.6 | 2.0 | 0.6 |
| | ------------Percent change at annual rates------------ | | | | | | Levels bil. $ Nov 92p |
| Selected components | | | | | | | |
| 4. M1-A | 5.6 | 9.1 | 11.2 | 22.8 | 20.8 | 8.7 | 637.9 |
| 5. Currency | 8.4 | 5.8 | 11.2 | 17.4 | 8.4 | 6.7 | 290.0 |
| 6. Demand deposits | 3.4 | 12.5 | 11.4 | 26.9 | 30.8 | 11.1 | 339.3 |
| 7. Other checkable deposits | 12.4 | 11.0 | 8.8 | 12.9 | 25.9 | 23.1 | 381.2 |
| 8. M2 minus M1[2] | 1.1 | -3.0 | -3.7 | -2.6 | -1.8 | -1.0 | 2485.9 |
| 9. Overnight RPs and Eurodollars, NSA | -7.0 | -27.7 | 15.7 | -25.3 | 12.9 | -3.2 | 74.8 |
| 10. General purpose and broker/dealer money market mutual fund shares | 3.9 | -3.9 | -8.2 | -17.2 | 10.1 | 3.8 | 348.7 |
| 11. Commercial banks | 7.1 | 0.5 | -1.8 | 2.5 | 1.1 | -1.5 | 1261.3 |
| 12. Savings deposits (including MMDAs) | 13.3 | 12.0 | 10.0 | 16.7 | 14.7 | 10.3 | 749.8 |
| 13. Small time deposits | 1.1 | -13.3 | -16.7 | -16.8 | -18.0 | -18.0 | 511.6 |
| 14. Thrift institutions | -6.9 | -6.7 | -5.1 | -2.8 | -8.7 | -4.9 | 802.3 |
| 15. Savings deposits (including MMDAs) | 9.3 | 18.9 | 8.3 | 10.8 | 8.8 | 10.1 | 431.8 |
| 16. Small time deposits | -16.8 | -29.4 | -18.7 | -17.4 | -27.6 | -21.9 | 370.6 |
| 17. M3 minus M2[3] | -5.7 | -9.3 | -1.8 | -7.5 | -21.8 | -5.1 | 684.9 |
| 18. Large time deposits | -11.7 | -18.9 | -16.2 | -14.4 | -21.2 | -11.9 | 369.6 |
| 19. At commercial banks, net[4] | -5.1 | -14.8 | -16.0 | -16.7 | -25.0 | -9.4 | 303.1 |
| 20. At thrift institutions | -31.7 | -37.0 | -16.8 | -3.5 | -1.8 | -24.7 | 66.5 |
| 21. Institution-only money market mutual fund shares | 33.4 | 20.1 | 39.9 | 0.0 | -64.1 | -12.3 | 203.5 |
| 22. Term RPs, NSA | -22.0 | 7.8 | 2.2 | 29.5 | 35.2 | 32.6 | 79.4 |
| 23. Term Eurodollars, NSA | -11.0 | -22.7 | -25.6 | -64.0 | -12.5 | 10.1 | 47.8 |
| | -----Average monthly change in billions of dollars---- | | | | | | |
| MEMORANDA:[5] | | | | | | | |
| 24. Managed liabilities at commercial banks (25+26) | -0.6 | -3.1 | 0.4 | 3.5 | -8.7 | -3.3 | 673.8 |
| 25. Large time deposits, gross | -0.2 | -4.8 | -3.7 | -3.4 | -7.9 | -3.3 | 370.0 |
| 26. Nondeposit funds | -0.4 | 1.7 | 4.1 | 6.9 | -0.8 | 0.0 | 303.8 |
| 27. Net due to related foreign institutions | 0.4 | 5.0 | 0.5 | 3.0 | 3.5 | -0.9 | 64.4 |
| 28. Other[6] | -0.8 | -3.3 | 3.6 | 3.9 | -4.3 | 0.9 | 239.4 |
| 29. U.S. government deposits at commercial banks[7] | 0.2 | 1.3 | -0.1 | -7.2 | -3.0 | -3.2 | 19.2 |

1. Amounts shown are from fourth quarter to fourth quarter.
2. Nontransactions M2 is seasonally adjusted as a whole.
3. The non-M2 component of M3 is seasonally adjusted as a whole.
4. Net of large denomination time deposits held by money market mutual funds and thrift institutions.
5. Dollar amounts shown under memoranda are calculated on an end-month-of-quarter basis.
6. Consists of borrowing 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 borrowing from the Federal Reserve and unaffiliated foreign banks, loan RPs and other minor items). Data are partially estimat
7. Consists of Treasury demand deposits and note balances at commercial banks.
p - preliminary

Gross issuance of bonds by state and local governments cooled off in November, after three strong months. In contrast, federal borrowing has risen more than seasonally to finance a large fourth-quarter deficit.

M2 growth fell back a bit in November while M3 growth increased somewhat. M2 and M3 in November were both somewhat below their annual growth cones.[1] Data for early December point to a weak month for both aggregates.

Monetary Aggregates and Bank Credit

The slowing of M2 growth in November, to a 3-1/2 percent annual rate, mainly reflected a sharp deceleration in demand deposits, which owed partly to a backup in money market rates and to a slowing in the rate of increase in mortgage refinancing activity. Other checkable deposit (OCD) growth remained robust, with about half of its increase stemming from reclassification of large time deposits as OCDs. M2 growth for the fourth quarter appears to be below that of nominal income, which would produce the seventh successive quarterly increase in M2 velocity. Despite the slowing in M2, growth in M3 picked up a bit in November, as the contraction of institution-only money funds abated and runoffs of large time deposits at banks slowed.

In November, bank credit, boosted again by loan growth, expanded at a 4-3/4 percent pace. As loan growth has picked up, banks' security acquisitions have run well below the torrid pace set earlier this year. Business loans expanded at a 5-1/4 percent rate in November, the third consecutive advance after a series of runoffs dating back to late 1991. Last month's business loan growth likely was boosted by the slowdown in junk bond and equity issuance and by efforts to lock in year-end financing; however, perhaps half of it

1. Growth in the monetary and debt aggregates in 1992 is discussed in the appendix.

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

| Category | 1990 Dec. to 1991 Dec. | 1992 Q 2 | 1992 Q 3 | 1992 Sep. | 1992 Oct. | 1992 Nov. | Level, bil.$ 1992 Nov. |
|---|---|---|---|---|---|---|---|
| | Commercial bank credit | | | | | | |
| 1. Total loans and securities at banks | 3.9 | 3.0 | 4.1 | 6.7 | 4.8 | 4.7 | 2,936.3 |
| 2. Securities | 17.7 | 16.5 | 15.1 | 7.4 | 11.7 | 9.3 | 831.5 |
| 3. U.S. government | 23.8 | 21.9 | 17.8 | 9.3 | 13.3 | 13.7 | 653.6 |
| 4. Other | 1.6 | -2.0 | 5.9 | 0.0 | 6.7 | -6.7 | 177.9 |
| 5. Loans | -0.2 | -1.8 | 0.0 | 6.5 | 2.0 | 2.9 | 2,104.8 |
| 6. Business | -2.8 | -4.2 | -0.9 | 4.8 | 0.4 | 5.2 | 606.0 |
| 7. Real estate | 2.9 | 0.2 | 0.5 | 5.3 | 5.6 | 3.1 | 889.2 |
| 8. Consumer | -3.9 | -3.0 | -2.5 | -1.7 | -4.0 | -1.4 | 354.6 |
| 9. Security | 21.3 | 22.4 | 12.5 | 71.0 | -9.1 | -23.7 | 64.4 |
| 10. Other | -2.8 | -9.0 | 1.7 | 12.3 | 4.5 | 13.4 | 190.7 |
| | Short- and intermediate-term business credit | | | | | | |
| 11. Business loans net of bankers acceptances | -2.4 | -3.7 | -1.2 | 5.0 | -1.6 | 4.4 | 598.8 |
| 12. Loans at foreign branches[2] | -1.6 | 26.3 | 1.6 | 4.9 | 14.8 | 34.0 | 25.4 |
| 13. Sum of lines 11 and 12 | -2.4 | -2.6 | -1.1 | 4.8 | -1.0 | 5.6 | 624.2 |
| 14. Commercial paper issued by nonfinancial firms | -10.4 | -3.9 | 7.1 | 1.7 | 20.2 | 49.6 | 151.3 |
| 15. Sum of lines 13 and 14 | -3.9 | -2.9 | 0.5 | 4.4 | 2.8 | 13.8 | 775.4 |
| 16. Bankers acceptances, U.S. trade-related[3,4] | -16.2 | -27.3 | -19.5 | -25.1 | 5.1 | n.a. | 23.5[5] |
| 17. Finance company loans to business[4] | 1.4 | -1.6 | 8.6 | 4.3 | -2.4 | n.a. | 304.5[5] |
| 18. Total (sum of lines 15, 16, and 17) | -2.9 | -3.1 | 2.2 | 3.7 | 1.5 | n.a. | 1,094.6[5] |

1. Average of Wednesdays. Data are adjusted for breaks caused by reclassifications.
2. Loans at foreign branches are loans made to U.S. firms by foreign branches of domestically chartered banks.
3. Consists of acceptances that finance U.S. imports, U.S. exports, and domestic shipment and storage of goods.
4. Based on average of data for current and preceding ends of month.
5. October 1992.
n.a.--Not available.

resulted from drawdowns on a line of credit by a single nonfinancial firm experiencing difficulty in the commercial paper market. Real estate loans continued their moderate rate of expansion in November, with all of the growth occurring at domestic banks. Foreign-related institutions, whose real estate lending is mainly to the commercial sector, ran down their portfolios slightly.

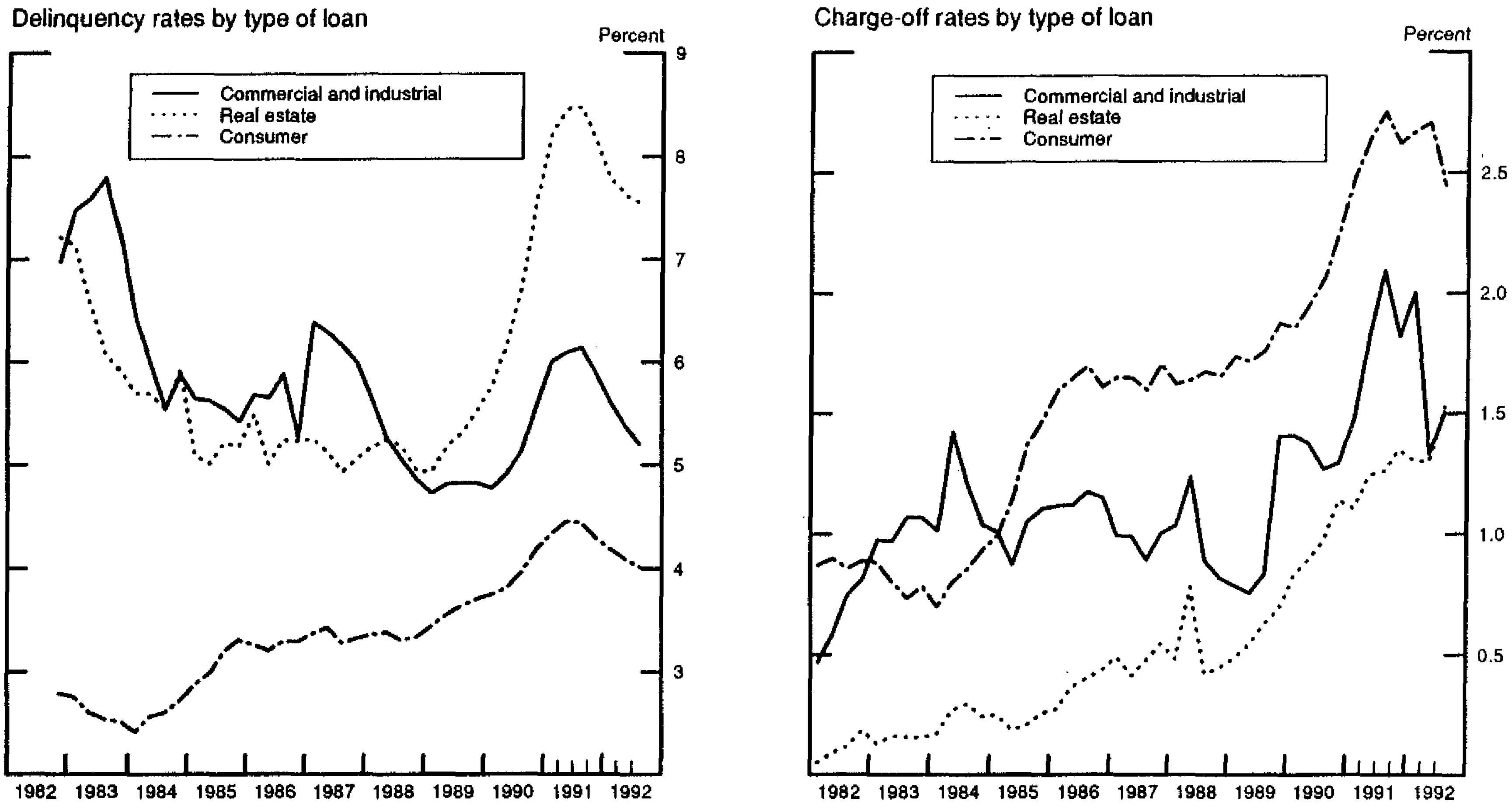
The quality of bank loan portfolios continued to improve in the third quarter. Call report data showed delinquency rates for the major categories of loans declining further, although they remained high (chart). Delinquency rates for real estate loans peaked in 1991 in most regions of the country, but they continued to rise in the West. ABA data on the percentage of delinquent closed-end consumer loans confirmed the downward trend of the call report data, but delinquency rates for credit card debt moved up. Call report data on net charge-off rates for business and consumer loans in the third quarter were below recent peaks. Net charge-off rates for real estate loans, however, continued to rise, largely because of heavier write-offs of commercial mortgages.

As banks have improved their capital positions in 1992, through higher retained earnings and market sales of debt and equity, the proportion of total loans held at adequately and well-capitalized banks has risen substantially (table). Since December 1991, the share of loans at institutions classified as well capitalized under FDICIA has nearly doubled, the share at adequately capitalized banks has been halved, and the share at under capitalized banks has drifted toward insignificance.[2]

Improvements in capital positions have affected deposit and loan growth at banks this year. About half of the large commercial

2. The table, which is based solely on capital ratios, overstates somewhat the share of loans held by banks that are officially classified in the adequately and well-capitalized groups because examiners can downgrade a bank with a poor CAMEL rating.

## Delinquency and Charge-Off Rates at Large Banks, SA




Note: Data are from FFIEC's quarterly Reports of Condition and Income for banks with at least $300 million in assets, and for all banks with foreign offices. Delinquent loans include those past due 30 days or more and still accruing interest, as well as those on nonaccrual status. Delinquency rates are averages of the beginning and end of each quarter. Charge-off rates are annualized, net of recoveries, divided by average outstanding loans. Delinquency rate series began 1982 Q4, charge-off rate series began 1982 Q1.

DISTRIBUTION OF BANK LOANS BY CAPITAL STATUS OF THE BANK
(percent)

| Capital Status | Share on call date: Dec 91 | Mar 92 | Jun 92 | Sep 92 |
|---|---|---|---|---|
| Well capitalized | 39.9 | 49.9 | 61.5 | 75.2 |
| Adequately capitalized | 50.2 | 43.7 | 36.3 | 23.4 |
| Under capitalized | 10.0 | 6.4 | 2.2 | 1.4 |

MEDIAN CHANGE IN GROWTH RATES AT LARGE COMMERCIAL BANKS
(growth in 1992 Q3 relative to growth in 1992 H1)
(annual rate, percentage points)

| | Capital position in June 1992 | |
|---|---|---|
| Capital position in December 1991 | Did not improve | Improved |
| M2 deposit growth | | |
| • Under | 1.2 | 3.5 |
| • Adequate | 3.4 | 7.5 |
| Securities growth | | |
| • Under | 30.0 | -1.3 |
| • Adequate | -0.1 | 0.0 |
| Loan growth | | |
| • Under | -0.9 | 4.4 |
| • Adequate | 1.8 | 3.5 |

banks that were undercapitalized in December 1991 improved their capital positions by June 1992, with most becoming adequately capitalized. Growth of M2 deposits at these banks stepped up in the third quarter by 3-1/2 percentage points, relative to the growth rate in the first half of the year. Banks that improved from adequately capitalized to well capitalized posted an even larger acceleration, 7-1/2 percentage points. Similarly, banks that improved their capital zones relied on securities acquisitions less and on loan growth more than banks that did not improve. Only banks that had been undercapitalized in December 1991 and remained so in June 1992 had a higher pace of acquisitions of securities and a slower rate of loan growth in the third quarter than in the first half of the year.

Corporate Securities Markets

Pressures related to the year-end began to emerge in money market rates in the first week of November, about a month earlier than in 1990 and 1991. Market participants cited several factors for this earlier onset: the length of the year-end period, less willingness by investors to hold paper backed by Japanese banks, concern about GMAC and other large direct issuers, and potential restraints on bank lending resulting from the more stringent capital tests imposed by FDICIA. As many borrowers reportedly have accomplished their funding objectives, the implied turn-of-the year forward rates have eased noticeably recently--but they remain well above the 3 percent federal funds rate.

While the desire to lock in funding over year-end probably contributed to the nearly 50 percent annual rate of growth of commercial paper outstanding in November, another important influence was the departure of borrowers from long-term debt markets amid a backup in long-term rates that began in October and continued

GROSS OFFERINGS OF SECURITIES BY U.S. CORPORATIONS
(Monthly rates, not seasonally adjusted, billions of dollars)

| | 1990 | 1991 | 1992 Q2 | 1992 Q3[p] | 1992 SEP[p] | 1992 OCT[p] | 1992 NOV[p] |
|---|---|---|---|---|---|---|---|
| Corporate securities - total[1] | 19.82 | 32.15 | 41.42 | 42.21 | 43.25 | 40.82 | 33.90 |
| Public offerings in U.S. | 17.68 | 29.36 | 38.17 | 39.82 | 41.61 | 38.47 | 31.61 |
| Stocks--total[2] | 1.95 | 5.44 | 7.08 | 5.69 | 5.31 | 6.97 | 4.61 |
| Nonfinancial | 1.03 | 3.72 | 4.99 | 2.86 | 2.62 | 3.23 | 2.13 |
| Utility | 0.35 | 0.42 | 1.24 | 1.11 | 1.82 | 0.51 | 0.48 |
| Industrial | 0.68 | 3.30 | 3.75 | 1.75 | 0.79 | 2.71 | 1.65 |
| Financial | 0.92 | 1.72 | 2.09 | 2.83 | 2.70 | 3.74 | 2.49 |
| Bonds | 15.73 | 23.92 | 31.09 | 34.13 | 36.30 | 31.50 | 27.00 |
| Nonfinancial | 5.62 | 9.52 | 12.33 | 14.91 | 14.95 | 15.50 | 8.00 |
| Utility | 1.97 | 2.99 | 5.41 | 7.49 | 7.06 | 4.50 | 2.20 |
| Industrial | 3.64 | 6.54 | 6.92 | 7.43 | 7.90 | 11.00 | 5.80 |
| Financial | 10.11 | 14.40 | 18.76 | 19.22 | 21.35 | 16.00 | 19.00 |
| By quality[3] | | | | | | | |
| Aaa and Aa | 3.42 | 3.72 | 2.84 | 4.75 | 4.98 | 5.76 | 1.97 |
| A and Baa | 6.44 | 12.09 | 15.02 | 15.01 | 15.97 | 11.71 | 12.24 |
| Less than Baa | 0.15 | 1.03 | 3.31 | 3.12 | 2.59 | 4.18 | 1.68 |
| No rating (or unknown) | 0.04 | 0.02 | 0.02 | 0.04 | 0.02 | 0.63 | 0.03 |
| Memo items: | | | | | | | |
| Equity-based bonds[4] | 0.40 | 0.63 | 0.52 | 0.28 | 0.33 | 0.43 | 0.30 |
| Mortgage-backed bonds | 2.43 | 2.99 | 6.63 | 6.76 | 6.13 | 6.00 | 4.91 |
| Other asset-backed | 3.27 | 4.08 | 3.26 | 4.45 | 6.61 | 3.23 | 6.18 |
| Variable-rate notes | 0.80 | 0.84 | 2.18 | 2.00 | 3.12 | 1.56 | 1.15 |
| Bonds sold abroad - total | 1.92 | 2.33 | 2.46 | 2.18 | 1.35 | 2.00 | 2.15 |
| Nonfinancial | 0.46 | 1.00 | 1.06 | 0.71 | 0.38 | 1.00 | 0.70 |
| Financial | 1.46 | 1.33 | 1.40 | 1.46 | 0.96 | 1.00 | 1.45 |
| Stocks sold abroad - total | 0.22 | 0.46 | 0.79 | 0.22 | 0.29 | 0.36 | 0.14 |
| Nonfinancial | 0.10 | 0.38 | 0.67 | 0.17 | 0.29 | 0.21 | 0.09 |
| Financial | 0.12 | 0.08 | 0.12 | 0.04 | 0.00 | 0.14 | 0.04 |

1. Securities issued in the private placement market are not included. Total reflects gross proceeds rather than par value of original discount bonds.
2. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings. Such swaps totaled $15 billion in 1991.
3. Bonds categorized according to Moody's bond ratings, or to Standard and Poor's if unrated by Moody's. Excludes mortgage-backed and asset-backed bonds.
4. Includes bonds convertible into equity and bonds with warrants that entitle the holder to purchase equity in the future.

p--preliminary.

through mid-November. Public offerings of bonds by nonfinancial investment-grade firms were only about $6.5 billion in November compared with $11.5 billion in October. The decline in long rates beginning in late November has sparked a rebound in issuance this month.

Despite record stock prices and extremely high average P-E ratios, equity issuance by nonfinancial firms slowed in November, but appeared to be picking up some in the early weeks of December. In particular, IPOs, which had been slow since June, showed signs in December of returning to the faster pace recorded in the spring of this year.

Two major finance companies experienced difficulties in the intermeeting period. GMAC faced higher borrowing costs in light of questions about GM's financial health. A week before Thanksgiving, GMAC announced that it would no longer finance vehicles not produced by GM, and market participants took this announcement as indicating that the company was having difficulties raising funds in capital markets. Shortly thereafter, Moody's downgraded GMAC's senior long-term debt rating from A2 to Baa1 and its commercial paper rating from P-1 to P-2. Westinghouse Electric, already under fire from investors for losses at Westinghouse Credit, announced that it would liquidate its credit subsidiary and take an additional $2.3 billion pre-tax charge against its loan portfolio. With this announcement Westinghouse's share price rose 25 percent, because investors believed that the firm was leaving its major problem behind. Investor concern and downgrades had already forced Westinghouse to replace most of its commercial paper by drawing on bank lines.

November's heavy issuance of asset-backed securities has carried over into December. Thus far, $5.8 billion have been sold after offerings of $6.2 billion in November. The market continued to be receptive to innovative transactions and to offerings sold by infrequent issuers. For example, Chrysler Financial successfully sold an auto-loan-backed issue with a tranche that carried a final maturity of one year and thus was eligible for purchase by money market mutual funds under SEC Rule 2a-7. Demand also was strong for auto-loan-backed debt issued for Honda Motor Credit, which was in the market for the first time. On the other hand, the market has demanded a premium for new GMAC issues, as the company has already issued $11 billion of auto-loan-backed securities this year.

The set of assets securitizable in the public market is expected to grow in 1993 because of the SEC's adoption of a new rule exempting structured financings from the Investment Company Act of 1940. As a result securities backed by instruments such as small business loans, Medicare receivables, and high-yield bonds, available to date only in the private placement market or abroad, are expected to be introduced to the public markets in the near future.

Treasury and Sponsored Agency Financing

The staff projects that the federal government's $128 billion fourth-quarter deficit will be financed largely by $75 billion of marketable borrowing and by a $42 billion drawdown in the cash balance. To date in the fourth quarter, the Treasury has increased the gross sizes of the weekly bill auctions from $20.4 billion to $24.8 billion and gross sizes of coupon auctions by as much as $500 million. Further increases in both bill and coupon auction sizes are likely.

An announcement by Argentina that it would purchase directly from the Treasury the zero-coupon securities required to defease the principal of its restructured debt was widely anticipated and had little effect on Treasury bond yields. Spreads over Treasuries of

TREASURY AND AGENCY FINANCING[1]
(Total for period; billions of dollars)

| | 1992 | | | | |
|---|---|---|---|---|---|
| | Q3 | Q4[p] | Oct. | Nov.[p] | Dec.[p] |
| Treasury financing | | | | | |
| Total surplus/deficit (-) | -62.4 | -128.1 | -48.9 | -37.2 | -42.0 |
| Means of financing deficit: | | | | | |
| Net cash borrowing from the public | 77.0 | 79.7 | -1.6 | 62.1 | 19.2 |
| Marketable borrowings/ repayments (-) | 72.6 | 75.2 | -2.5 | 59.7 | 18.0 |
| Bills | 16.1 | 22.6 | -6.5 | 17.2 | 11.9 |
| Coupons | 56.4 | 52.7 | 4.0 | 42.5 | 6.1 |
| Nonmarketable | 4.4 | 4.5 | .9 | 2.3 | 1.2 |
| Decrease in the cash balance | -11.7 | 42.3 | 39.4 | -7.3 | 10.2 |
| Memo: Cash balance at end of period | 58.8 | 16.5 | 19.4 | 26.7 | 16.5 |
| Other[2] | -2.8 | 6.1 | 11.0 | -17.5 | 12.6 |
| Federally sponsored credit agencies, net cash borrowing[3] | 17.0 | -- | 3.3 | -- | -- |
| FHLBs | 4.8 | -- | 1.6 | -- | -- |
| FHLMC | 4.3 | -- | -2.6 | -- | -- |
| FNMA | 6.2 | -- | 4.5 | -- | -- |
| Farm Credit Banks | 0.9 | -- | -.2 | -- | -- |
| SLMA | .7 | -- | -- | -- | -- |
| FAMC[4] | .0 | -- | -.0 | -- | -- |

1. Data reported on a not seasonally adjusted, payment basis.
2. Includes checks issued less checks paid, accrued items and other transactions.
3. Excludes mortgage pass-through securities issued by FNMA and FHLMC.
4. Federal Agricultural mortgage Corporation.
p--projected.
Note: Details may not add to totals due to rounding.

intermediate-maturity debt instruments of GSEs widened 8 to 10 basis points over the intermeeting period, in part because Federal Home Loan banks stopped paying down their outstanding debt, as advances to members began growing after a long period of runoffs.

As of early December the Treasury had about $120 billion of leeway for net new debt issuance under the $4.15 trillion debt ceiling. The debt ceiling likely will be reached late during the first quarter of 1993.

Municipal Securities

Municipal bond yields were pushed lower in recent weeks by a drop in gross issuance from its recent torrid pace. The prospect of $9 billion in bond redemptions in January 1993, representing more than 1 percent of the outstanding stock, also nudged yields downward. In addition, market reports suggested increased interest in tax-exempt securities by high-income individuals, in anticipation of higher personal income tax rates under the Clinton administration. Both new capital and refunding issuance fell in November, reaching the lowest levels since early in the year. Nonetheless, about $90 billion of refunding debt has been sold thus far in 1992, a rate of issuance that is more than 30 percent faster than the previous record, set in 1986, and which may have nearly exhausted the pool of issues that can be refunded profitably at current yields.[3]

Some issuers have sold municipal bonds with transferable call options, a device that allows an issuer to reap the benefits of a refunding without actually calling the old bond and incurring the cost of issuing a new bond. If interest rates were to fall so that a refunding became attractive, the issuer could sell the call

3. Recent revisions by IDD, the source for municipal volume data, have boosted reported refunding issuance for 1992. The rapid pace of refundings in 1986 owed to falling interest rates and anticipated limits on the number of pre-refundings.

GROSS OFFERINGS OF MUNICIPAL SECURITIES
(Monthly rates, not seasonally adjusted, billions of dollars)

| | 1990 | 1991 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Sep. | 1992 Oct.[p] | 1992 Nov.[p] |
|---|---|---|---|---|---|---|---|---|
| Total offerings[1] | 13.49 | 16.60 | 17.80 | 24.35 | 25.09 | 23.33 | 23.67 | 15.05 |
| Total tax-exempt | 13.24 | 16.18 | 17.26 | 23.61 | 24.65 | 29.06 | 23.06 | 14.61 |
| Long-term | 10.26 | 12.84 | 15.53 | 19.31 | 18.62 | 18.70 | 21.09 | 14.13 |
| Refundings[2] | 1.68 | 3.11 | 6.18 | 8.52 | 8.60 | 8.20 | 7.33 | 6.10 |
| New capital | 8.58 | 9.73 | 9.35 | 10.79 | 10.02 | 10.50 | 13.76 | 8.03 |
| Short-term | 2.96 | 3.39 | 1.73 | 4.29 | 6.03 | 10.36 | 1.97 | .48 |
| Total taxable | .25 | .42 | .55 | .75 | .44 | .39 | .61 | .44 |

p--preliminary.
1. Includes issues for public and private purposes.
2. Includes all refunding bonds, not just advance refundings.

option, either to the current holders of the bonds or to other investors desiring to hedge a portfolio of callable bonds. The issuer of the option would receive cash about equal to the present value of the interest savings that could have been achieved by refunding the bond. This feature was very attractive to issuers (such as those constrained to one refunding per issue by the Tax Reform Act of 1986) that could not refund through traditional means. Nearly $2 billion of debt with these call options has been sold since Paine-Webber pioneered their use in April 1992. Recently the first sale of the options themselves took place when Georgia Utility sold call options on a general obligation issue; most of the calls reportedly were purchased by mutual funds.

Prices of municipal bonds backed by the guaranteed investment contracts (GICs) of Executive Life Insurance Company, which failed in April 1991, jumped after a ruling by the California state court of appeals. The court ruled that holders of the nearly $2 billion in GICs shared with regular Executive Life policyholders the right to pursue claims on company assets. The municipal GICs were viewed as annuities that could be classified as insurance products under California law.

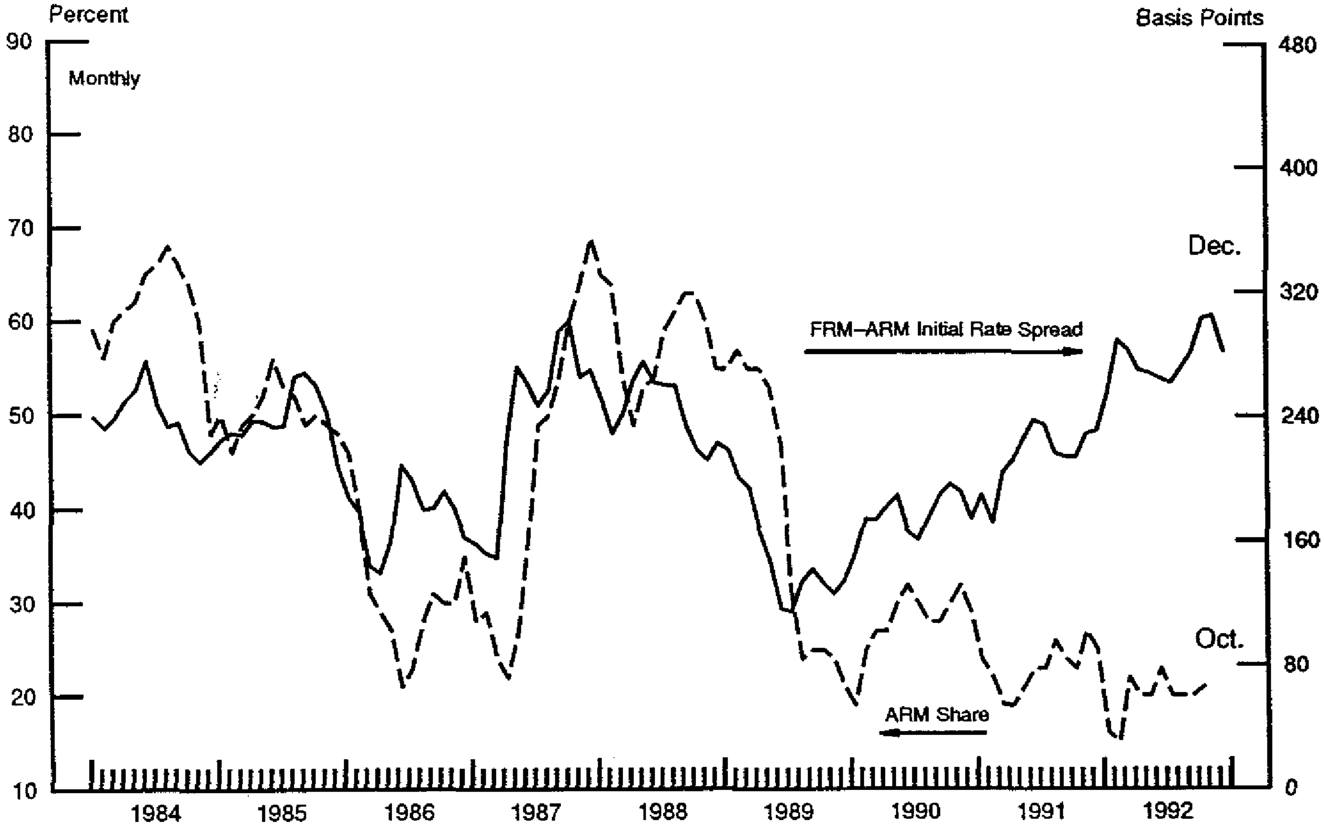
Mortgage Markets

Commitment rates on thirty-year, fixed-rate mortgages were down about 10 basis points over the intermeeting period, while those on adjustable-rate mortgages rose about 25 basis points. ARM rates stood at their highest level since mid-July, but their initial rate advantage over FRMs was still 270 basis points. In the past, when spreads were this wide, ARMs accounted for over two-thirds of conventional loan closings, but for much of this year they have accounted for less than one-quarter of conventional originations (chart).

Through the first three quarters of 1992, relatively low ARM volume did not prevent ARM-backed securities from picking up substantially, versus the same period a year ago. Private conduits accounted for 40 percent of new ARM-backed securities issued through September 1992 (table), reflecting securitizations by the RTC (classified as private because they lack a government guarantee), a few California-based thrifts, and other channels. The agencies accounted for the remaining 60 percent. Gross issuance of FRM-backed pass-throughs by the agencies rose to a record $42 billion in October, reflecting heavy issuance by Fannie Mae and Freddie Mac. Intermediate-term mortgages continued to account for around 40 percent of agency pass-through issuance.

Borrowers have seen substantial benefits from the reduction in mortgage interest rates. Staff estimates, based on the change over the past two years in the average interest rate for the stock of residential mortgage debt outstanding in December 1990, suggest as much as $35 billion in annual interest savings on fixed- and adjustable-rate mortgages combined. This estimate is essentially the change in the average cost of carry for mortgage debt existing at the end of 1990. Some of the savings may, of course, be offset

## ARM Share vs. FRM–ARM Initial Rate Spread




MORTGAGE-BACKED SECURITY ISSUANCE
(Monthly averages, billions of dollars, NSA unless noted)

| | Pass-through securities | | | | | Multiclass securities | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Federal Agency | | Private | | | | | | |
| | Total (SA) | Fixed-Rate | ARM-backed | Fixed-Rate | ARM-backed | Total | Private issues[1] | FNMA REMICs | FHLMC REMICs | Agency strips |
| 1988 | 13.7 | 10.2 | 2.3 | .3 | 1.0 | 6.8 | 5.0 | .9 | .9 | n.a. |
| 1989 | 17.7 | 14.1 | 2.7 | .7 | .5 | 8.4 | 1.6 | 3.1 | 3.2 | .3 |
| 1990 | 21.7 | 17.2 | 2.4 | 1.4 | .6 | 11.5 | 2.4 | 5.1 | 3.4 | .6 |
| 1991 | 26.2 | 20.4 | 2.0 | 2.5 | 1.6 | 18.4 | 3.0 | 8.5 | 6.0 | .9 |
| 1992-Q1 | 34.2 | 29.1 | 2.0 | 4.9 | 2.0 | 23.5 | 4.8 | 11.1 | 7.0 | .6 |
| Q2 | 49.2 | 36.8 | 3.6 | 5.4 | 1.6 | 33.9 | 6.6 | 13.9 | 12.4 | .9 |
| Q3 | 40.2 | 30.0 | 3.2 | 6.1 | 2.3 | 36.1 | 6.8 | 16.7 | 11.5 | 1.1 |
| 1992-Aug. r | 37.1 | 29.8 | 3.0 | 4.1 | 2.5 | 36.7 | 8.0 | 15.0 | 12.9 | .8 |
| Sep. r | 44.2 | 31.6 | 3.5 | 7.5 | 2.7 | 32.4 | 6.1 | 15.4 | 9.9 | 1.1 |
| Oct. p | 51.7 | 41.9 | 3.5 | 4.4 | 2.4 | 41.5 | 6.0 | 19.0 | 13.5 | 3.0 |

1. Excludes pass-through securities with senior/subordinated structures.
p--preliminary r--revised n.a.--not available

initially by the transactions costs (points, taxes, and fees) involved in refinancing, which can be significant.

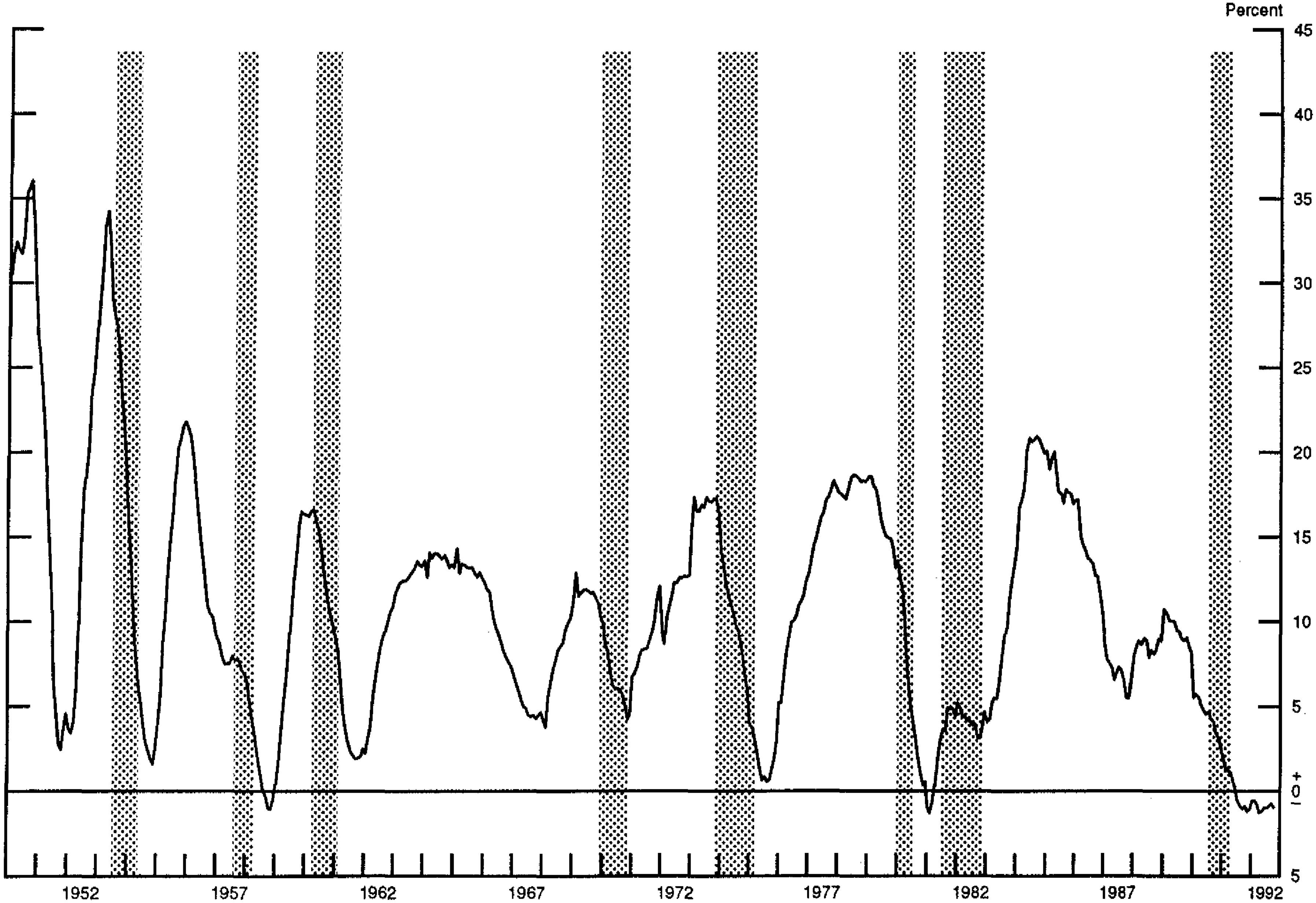
Evidence on the quality of real estate loan portfolios was mixed. As mentioned above, delinquency rates at commercial banks declined in the third quarter. However, data from the Mortgage Bankers Association (MBA) on the number of delinquent loans indicated that the overall delinquency rate on home mortgages rose slightly in the third quarter. These data, from a survey of 330 mortgage servicers, showed that the deterioration primarily was in loans 90 or more days overdue, as the 30-day and 60-day delinquency rates fell slightly. Despite the small increase, the overall delinquency rate remained below its 1991 average. Delinquency rates on commercial mortgages, reported by the American Council of Life Insurance, fell in the third quarter for the first time in two years, but remained at a fairly high level.

Fragmentary data suggest that fourth-quarter growth of mortgage credit will outstrip the estimated 2 percent pace for the third quarter. In that quarter, multifamily and commercial mortgage debt contracted at annual rates of 3-1/2 and 7-1/2 percent, respectively, but single-family mortgage and farm mortgage debt grew at annual rates of 5 and 1-1/4 percent, respectively.

Consumer Credit

Consumer installment credit outstanding inched up at a 1/2 percent annual rate in October, down from a 2-1/2 percent rate in September. The October increase was dominated by a strong advance in revolving credit, which more than offset continued weakness in the auto and other categories. While weak, auto loans did not decline in September and October; after contractions in the outstanding stock of auto loans over the past two years, even small amounts of new auto lending now tend to exceed the volume of

TOTAL CONSUMER INSTALLMENT CREDIT OUTSTANDING
(YEAR TO YEAR PERCENT CHANGES)



repayments flowing from the reduced stock. Total consumer credit (installment plus noninstallment) declined at a 3 percent annual rate in October.

CONSUMER CREDIT
(Seasonally adjusted)

| | Percent change (at annual rate) | | | | | | | Memo: Outstandings ($billion) |
|---|---|---|---|---|---|---|---|---|
| | | | | 1992 | | 1992 | | 1992 |
| | 1989[1] | 1990 | 1991 | H1 | Q3[r] | Sept.[r] | Oct.[p] | Oct.[p] |
| Installment | 5.8 | 2.6 | -1.0 | -1.3 | -.5 | 2.4 | .4 | 722.3 |
| Auto | 1.4 | -2.4 | -7.6 | -4.3 | .1 | 2.1 | .1 | 257.4 |
| Revolving | 15.2 | 11.9 | 8.9 | 3.8 | 4.2 | 9.5 | 7.9 | 251.7 |
| Other | 4.2 | .8 | -2.3 | -3.5 | -6.3 | -5.4 | -8.1 | 213.3 |
| Non-installment | 3.9 | -3.5 | -10.0 | 13.0 | 8.2 | 3.4 | -46.1 | 55.2 |
| Total | 5.6 | 2.1 | -1.7 | -.4 | .2 | 2.5 | -3.1 | 777.5 |

1. Growth rates are adjusted for discontinuity in data between December 1988 and January 1989.
r--revised. p--preliminary.
Note: Details may not add to totals due to rounding.

Despite its recent increases, outstanding consumer installment credit in October remained below its year-earlier level (chart). The extended weakness in this cycle is unprecedented in the past 42 years. Indeed, there have been only two prior periods of negative year-over-year changes (1958 and 1980-81), both of which were considerably shorter in duration. The first followed the short, but severe, 1957-58 recession, while the second followed the imposition of credit controls in the first half of 1980. The current episode of contraction contrasts with historical experience this far into a recovery and undoubtedly reflects in part the paydown of relatively expensive debt with low-yielding liquid assets.

Interest rates on consumer loans continued to decline in the most recent months but remained at relatively wide spreads compared with three-year Treasuries. The average "most common" rate on 48-month new car loans at commercial banks fell 55 basis points between August and November to 8.60 percent, the lowest rate in the 20-year history of this series. The rate on credit cards reached a 12-year low and a similar pattern was observed for rates on personal loans. Rates at finance companies on loans for used cars fell in October to the lowest level in the 20-year history of that series, but rates on loans for new cars rose, reflecting the removal of incentives at GM.

CONSUMER INTEREST RATES
(Annual percentage rate)

| | | | | 1992 | | | | |
|---|---|---|---|---|---|---|---|---|
| | 1990 | 1991 | 1992 | May | Aug. | Sept. | Oct. | Nov. |
| Commercial banks[1] | | | | | | | | |
| New cars (48 mo.) | 11.78 | 11.14 | 9.29 | 9.52 | 9.15 | ... | ... | 8.60 |
| Personal (24 mo.) | 15.46 | 15.18 | 14.04 | 14.28 | 13.94 | ... | ... | 13.55 |
| Credit cards | 18.17 | 18.23 | 17.78 | 17.97 | 17.66 | ... | ... | 17.38 |
| Auto finance companies[2] | | | | | | | | |
| New cars | 12.54 | 12.41 | ... | 10.67 | 8 .88 | 8.65 | 9.51 | ... |
| Used cars | 15.99 | 15.60 | ... | 14.01 | 13.49 | 12.06 | 12.01 | ... |

1. Average of "most common" rate charged for specified type and maturity during the first week of the mid-month of each quarter.
2. Average rate for all loans of each type made during the month regardless of maturity.

## Appendix

## Growth of Money and Credit in 1992

Growth of the broader monetary aggregates slowed in 1992 from the previous year's pace, despite a pickup in nominal GDP growth. From the fourth quarter of 1991 through November, M2 increased 2-1/4 percent, placing it somewhat below the lower end of its 2-1/2 to 6-1/2 percent annual range. M3 remained below its 1 to 5 percent range, expanding only 1/2 percent in 1992. The velocities of the broader aggregates surged, even though market interest rates declined. Some investors shifted out of M2 as the steep yield curve made capital market instruments more attractive. In addition, high consumer loan rates led some households to repay debt in lieu of holding deposits. Tendencies in both these directions were reinforced by the behavior of depositories, which remained unaggressive in seeking deposits and making loans, likely owing in part to higher intermediation costs and continued pressures to strengthen capital positions. With demand for bank loans also weak through much of the year, bank credit expanded at only a 4 percent rate through November. The balance sheets of thrift institutions contracted about 4 percent, less than last year, partly because of a reduction in Resolution Trust Corporation (RTC) resolutions. Within the broad aggregates, growth was concentrated in M1, as steep declines in market and time deposit interest rates induced large inflows into transaction accounts.

Total domestic nonfinancial debt expanded only 4-1/2 percent from the fourth quarter of last year through October, placing the level of nonfinancial debt at the bottom of its 4-1/2 to 8-1/2 percent monitoring range. The federal sector continued to borrow heavily, its debt increasing at a double-digit pace. Nonfederal debt growth remained sluggish, as nonfinancial businesses, households, and state and local governments restrained spending and refinanced existing debt.

### M1

M1 accelerated in 1992, increasing more than 14 percent. By November, demand deposits were almost 20 percent above their level of the fourth quarter of 1991, owing mostly to the effects of lower interest rates across the maturity spectrum. At the long end of the yield curve, declines in mortgage interest rates spurred two episodes of heavy refinancing, and because a large portion of the prepayments are held in demand deposits until mortgage servicers remit these funds, this boosted the level of demand deposits. The volume of refinancing activity accelerated early in the year, slowed at midyear, and quickened again throughout the summer and fall. However, the growth of demand deposits slowed precipitously in November, and such deposits appear to be declining in December, perhaps as mortgage refinancings fall back from the exceptionally high October pace. At the short end of the yield curve, the drop in money market interest rates over the year raised compensating balances to pay for bank services and reduced incentives to economize on cash balances.

Inflows into OCDs have been heavy, especially following the System's easing actions. However, depositories appear to have cut offering rates on these deposits more quickly than in the past. As opportunity costs returned to levels near those prior to the rate cuts, inflows into OCDs quickly subsided, lessening the impact of lower money market interest rates. Some of the OCD growth in the fourth quarter reflected the closing of a Regulation D loophole that forced to reclassify large time deposits as other checkable deposits.

Currency growth was moderate at the beginning of the year, but it picked up over the summer before slowing in the fall. Large shipments to Latin America, Eastern Europe, and the former Soviet republics account for much of the increase. Partly as a result of rapid currency growth, the monetary base grew at a 10-1/2 percent pace in 1992. Rapid growth of the base also reflected the 20 percent increase in total reserves that resulted from the brisk growth of required reserves against transaction deposits, adjusted for changes in reserve requirements.[1]

M2

After posting a modest increase in the first quarter, M2 declined through early summer. On a quarterly average basis, M2 growth rates during the second and third quarters were the lowest since the current series began in 1959. Slowing growth in liquid retail deposits and demand deposits accompanied strong outflows from small time deposits and money market mutual funds. Responding to further declines in market interest rates in April and July, transaction and savings deposits began to show more strength after midyear. During the second half of the year, M2 growth averaged 3 percent, about twice its first-half rate.

Inflows into savings deposits ranged from moderate to heavy, but outflows from small time deposits and money market mutual funds more than offset these gains. The nontransaction portion of M2 contracted in every month of the year except February. The decline in small time deposits partly reflected the runoff of brokered time deposits, as regulatory restrictions and ample inflows of savings and transaction deposits caused banks to reduce substantially the volume of brokered deposits. In addition, slow nontransaction deposit growth reflects the rate disadvantage of all M2 components relative to the historical returns advertised by bond mutual funds, which received record inflows during the year. Since midyear, the contraction of nontransaction accounts has slowed. Short-term deposits and money market mutual funds have benefitted from the modest flattening of the yield curve since October, which has diminished the allure of capital market instruments and been associated with the smallest monthly increase in bond mutual funds in almost two years. The pickup in nominal income growth and bank credit later in the second half of the year also has lessened some of the contractionary pressure on M2 that existed earlier.

M3

After a brief surge in early 1992, M3 contracted through the end of June. Weak loan demand and increased costs of depository intermediation continued to restrain the growth of bank and thrift balance sheets just as they had in 1991. Though the weakness in M2 accounted for much of the decline, a faster runoff of large time deposits also played a part. During the third quarter, stronger M2 growth and larger flows into institutional money funds offset

1. As a result of the Board's action to reduce the required reserve ratio on transaction deposits from 12 to 10 percent beginning in April, total reserves not adjusted for changes in reserve requirements increased only 3 percent since the fourth quarter of 1991 and the base increased 8-1/2 percent.

outflows from large time deposits, leaving the aggregate about flat. The aggregate strengthened a little during the fourth quarter. Throughout the year, weak loan demand and increased costs of depository intermediation continued to restrain the growth of bank and thrift balance sheets just as they had in 1991.

Institution-only money funds sustained strong inflows during the first three quarters. Some investors in these funds are very sensitive to the spread between the rate paid on these funds and money market rates. Since the assets of these funds are not marked to market, yields on these accounts tend to exceed market rates in periods of declining rates. The general downward trend of short-term rates during the year supported strong inflows until the fourth quarter, when higher short-term interest rates led to a reversal of these flows.

Domestic Nonfinancial Debt

The debt of domestic nonfinancial sectors is estimated to have expanded 4-1/2 percent in 1992, about the same as in 1991, while nominal income growth apparently increased around two percentage points. The federal deficit declined as a lack of funding for RTC resolutions held down spending associated with deposit insurance programs; still, federal sector debt continued to rise at a double digit pace. Private sector debt growth remained weak.

In the household sector, home mortgage interest rates fell to their lowest levels in almost 20 years during the first and third quarters, spurring considerable refinancing activity. However, the level of housing construction remained lackluster, and net expansion of home mortgage debt growth was only marginally above last year's lethargic pace. Consumer credit continued to contract until the fall.

Net borrowing by nonfinancial businesses has been negligible over all this year. For nonfinancial corporations, internally generated funds were adequate to cover outlays for inventories and fixed capital during the year. High stock prices encouraged equity issuance, which outstripped share retirements by a wide margin. Lower long-term interest rates provided firms with an opportunity to fund out short-term debt in the bond markets.

In the state and local government sector, gross bond issuance has been vary heavy this year, but net debt expansion was limited. About one-third of the funds raised were used to retire outstanding debt, much of which was issued in the early and mid-1980s.

THE GROWTH AND FLOW OF MONETARY AND CREDIT AGGREGATES
(Q4 to Q4 averages, seasonally adjusted unless otherwise noted)

| Growth rates or flows | 1988 | 1989 | 1990 | 1991 | 1992[1] | Memo: Recent 1992 levels (billions of dollars)[1] |
|---|---|---|---|---|---|---|
| Growth rates (percent) | | | | | | |
| M1 | 4.3 | 0.6 | 4.2 | 8.0 | 14.5 | 1019.2 |
| M2 | 5.2 | 4.8 | 4.0 | 2.8 | 2.2 | 3505.1 |
| M3 | 6.4 | 3.6 | 1.7 | 1.2 | 0.6 | 4190.0 |
| Domestic nonfinancial debt | 9.2 | 8.1 | 6.9 | 4.3 | 4.4 | 11622.4 |
| Bank credit | 7.9 | 7.3 | 5.5 | 3.6 | 4.0 | 2936.3 |
| Thrift credit | 7.6 | -2.5 | -9.8 | -10.7 | -3.6 | 1378.9 |
| Flows ($ billions) | | | | | | |
| M1 | | | | | | |
| Currency | 15.3 | 10.3 | 24.2 | 20.5 | 22.7 | 290.0 |
| Demand deposits | -3.0 | -7.5 | -1.9 | 12.4 | 49.8 | 339.3 |
| Other checkable deposits | 21.3 | 4.5 | 8.8 | 39.3 | 48.0 | 381.2 |
| M2 | | | | | | |
| Nontransactions M2 | 123.4 | 149.0 | 79.7 | 28.8 | -55.8 | 2485.9 |
| Savings & MMDAs | -10.9 | -35.0 | 29.5 | 121.9 | 138.9 | 1181.5 |
| Small time deposits | 115.4 | 115.6 | 20.2 | -105.7 | -180.8 | 882.2 |
| General purpose and broker/dealer money market mutual fund assets | 20.2 | 74.4 | 32.6 | 11.6 | -11.8 | 348.7 |
| Overnight RPs, net (NSA) | 3.1 | -6.8 | -8.1 | -1.4 | 0.4 | 54.0 |
| Overnight Eurodollars, net (NSA) | -4.0 | 1.2 | 5.2 | 2.9 | -1.9 | 20.7 |
| M3 | | | | | | |
| Non-M2 component | 81.7 | -19.5 | -56.9 | -44.4 | -46.3 | 684.9 |
| Institution-only money market mutual fund assets | -1.1 | 16.2 | 26.5 | 45.4 | 24.4 | 203.5 |
| Large time deposits | 52.2 | 18.1 | -64.4 | -57.8 | -67.5 | 369.6 |
| Term RPs, net (NSA) | 15.7 | -22.6 | -9.5 | -19.1 | 8.9 | 79.4 |
| Term Eurodollars net (NSA) | 14.7 | -26.2 | -10.8 | -11.5 | -9.4 | 47.8 |

1. For monetary aggregates and bank credit, through November; for domestic nonfinancial debt, through October; for thrift credit, through August.

# INTERNATIONAL DEVELOPMENTS

Merchandise Trade

The U.S. merchandise trade deficit narrowed slightly in September to $8.3 billion (seasonally adjusted, Census basis), compared with $8.9 billion (revised) in August. A 7 percent increase in exports outweighed a 4 percent rise in imports. The increase in exports was largely in capital goods (particularly computers and semiconductors, and to a lesser extent other machinery). Nearly half of the rise in imports was in consumer goods; the rest of the increase was spread among the other major trade categories. Data for October will be released December 17 and will be included in the Greenbook supplement.

U.S. MERCHANDISE TRADE: MONTHLY DATA
(Billions of dollars, seasonally adjusted, Census basis)

| | Exports | | | Imports | | | |
|---|---|---|---|---|---|---|---|
| | Total | Ag. | NonAg. | Total | Oil | NonOil | Balance |
| 1992-Jan | 35.5 | 3.6 | 31.9 | 41.3 | 3.6 | 37.6 | -5.8 |
| Feb | 37.7 | 3.7 | 33.9 | 40.9 | 3.3 | 37.6 | -3.3 |
| Mar | 37.1 | 3.5 | 33.6 | 42.7 | 3.4 | 39.2 | -5.6 |
| Apr | 36.4 | 3.8 | 32.7 | 43.5 | 4.0 | 39.5 | -7.1 |
| May | 35.7 | 3.3 | 32.4 | 42.9 | 4.2 | 38.7 | -7.1 |
| Jun | 38.2 | 3.5 | 34.7 | 44.9 | 4.8 | 40.1 | -6.7 |
| Jul | 37.8 | 3.9 | 33.9 | 45.1 | 4.8 | 40.3 | -7.3 |
| Aug | 35.8 | 3.6 | 32.2 | 44.7 | 4.6 | 40.2 | -8.9 |
| Sep | 38.2 | 4.0 | 34.2 | 46.5 | 4.8 | 41.7 | -8.3 |

Source: U.S. Department of Commerce, Bureau of the Census.

In the third quarter, the trade deficit widened to $106 billion at an annual rate (BOP basis) from $98 billion annual rate in the second quarter. Exports increased 3 percent while imports rose 4 percent.

The growth in exports in the third quarter was the first increase recorded since the fourth quarter of last year. The

MAJOR TRADE CATEGORIES
(Billions of dollars, BOP basis, SAAR)

| | Year | 1991 | | 1992 | | | $ Change | |
|---|---|---|---|---|---|---|---|---|
| | 1991 | Q3 | Q4 | Q1 | Q2 | Q3 | Q3-Q3 | Q3-Q2 |
| Trade Balance | -73.4 | -80.7 | -74.2 | -68.9 | -98.2 | -106.2 | -25.5 | -7.9 |
| Total U.S. Exports | 416.0 | 416.6 | 431.4 | 431.8 | 429.9 | 443.2 | 26.6 | 13.4 |
| Agric. Exports | 40.1 | 40.7 | 43.2 | 43.3 | 41.9 | 46.4 | 5.7 | 4.5 |
| Nonagric. Exports | 375.8 | 375.9 | 388.2 | 388.5 | 388.0 | 396.8 | 20.9 | 8.9 |
| Industrial Suppl. | 101.8 | 100.5 | 100.0 | 99.7 | 100.3 | 103.2 | 2.7 | 2.9 |
| Gold | 3.6 | 3.4 | 3.6 | 3.8 | 3.5 | 3.7 | 0.2 | 0.2 |
| Fuels | 14.3 | 12.7 | 14.7 | 13.9 | 13.5 | 13.4 | 0.7 | -0.0 |
| Other Ind. Suppl. | 83.9 | 84.3 | 81.8 | 82.1 | 83.3 | 86.1 | 1.8 | 2.8 |
| Capital Goods | 167.0 | 166.7 | 176.3 | 176.4 | 173.9 | 174.6 | 7.8 | 0.7 |
| Aircraft & Parts | 36.4 | 35.4 | 40.8 | 42.6 | 37.7 | 33.3 | -2.1 | -4.4 |
| Computers & Parts | 27.3 | 26.8 | 27.9 | 27.4 | 28.6 | 29.0 | 2.2 | 0.4 |
| Other Machinery | 103.3 | 104.5 | 107.5 | 106.4 | 107.6 | 112.2 | 7.8 | 4.6 |
| Automotive Goods | 40.0 | 43.7 | 41.7 | 42.9 | 46.2 | 49.0 | 5.3 | 2.8 |
| To Canada | 22.8 | 25.0 | 23.1 | 20.8 | 23.7 | 24.5 | -0.5 | 0.8 |
| To Other | 17.5 | 18.7 | 18.6 | 22.1 | 22.5 | 24.5 | 5.8 | 2.0 |
| Consumer Goods | 45.9 | 44.9 | 48.2 | 47.9 | 48.5 | 51.4 | 6.5 | 2.9 |
| Other Nonagric. | 21.0 | 20.1 | 22.1 | 21.5 | 19.1 | 18.6 | -1.5 | -0.4 |
| Total U.S. Imports | 489.4 | 497.3 | 505.6 | 500.7 | 528.1 | 549.4 | 52.1 | 21.3 |
| Oil Imports | 51.2 | 52.5 | 48.8 | 41.5 | 51.7 | 56.9 | 4.4 | 5.1 |
| Non-Oil Imports | 438.2 | 444.8 | 456.8 | 459.2 | 476.4 | 492.5 | 47.7 | 16.2 |
| Industrial Suppl. | 83.9 | 80.0 | 83.3 | 84.3 | 88.3 | 88.0 | 8.0 | -0.3 |
| Gold | 2.9 | 2.3 | 3.1 | 2.3 | 3.6 | 2.8 | 0.5 | -0.8 |
| Other Fuels | 3.9 | 3.8 | 4.8 | 4.4 | 4.6 | 4.4 | 0.6 | -0.2 |
| Other Ind. Suppl. | 77.1 | 73.9 | 75.4 | 77.7 | 80.1 | 80.8 | 6.9 | 0.7 |
| Capital Goods | 120.7 | 121.3 | 122.1 | 125.1 | 131.4 | 138.0 | 16.7 | 6.6 |
| Aircraft & Parts | 11.7 | 12.5 | 11.5 | 12.1 | 13.5 | 12.3 | -0.3 | -1.2 |
| Computers & Parts | 26.1 | 27.1 | 26.8 | 27.7 | 30.7 | 33.8 | 6.8 | 3.1 |
| Other Machinery | 82.9 | 81.7 | 83.8 | 85.4 | 87.2 | 91.9 | 10.2 | 4.7 |
| Automotive Goods | 84.9 | 90.8 | 88.6 | 87.8 | 89.5 | 91.3 | 0.5 | 1.8 |
| From Canada | 28.8 | 33.1 | 30.1 | 30.9 | 31.7 | 33.0 | -0.1 | 1.3 |
| From Other | 56.2 | 57.7 | 58.5 | 56.9 | 57.8 | 58.3 | 0.6 | 0.5 |
| Consumer Goods | 108.0 | 109.9 | 118.7 | 116.2 | 119.2 | 128.5 | 18.5 | 9.2 |
| Foods | 26.5 | 26.3 | 26.4 | 26.8 | 29.1 | 28.3 | 2.0 | -0.8 |
| All Other | 14.1 | 16.5 | 17.7 | 19.0 | 18.9 | 18.5 | 1.9 | -0.4 |

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

increase was spread among all major trade categories and primarily went to developing countries in Latin America and Asia. A sharp rise in exports to Japan in the third quarter reversed a drop in the second quarter; exports to Japan in the third quarter were only slightly higher than in the first quarter. Exports to Western Europe declined for the second quarter in a row and were at their lowest level since the third quarter of last year; the largest declines were to the United Kingdom and France.

Most of the growth in exports in the third quarter was in quantity, with the largest increases recorded for agricultural products, computers, and other machinery; there were also strong increases in exported automotive products and consumer goods. Aircraft exports declined for the second consecutive quarter from peak levels reached in the first quarter of this year.

Non-oil imports grew 3-1/2 percent in the third quarter, all in quantity. Forty percent of the increase was in consumer goods; the increase was in a wide range of items -- from apparel to toys and entertainment equipment -- and came primarily from China and various other developing countries in Asia. The increase in imported consumer goods in the third quarter was followed by a strong pickup in U.S. consumer spending in October and November. The remaining increase in non-oil imports in the third quarter was in capital goods (especially computers). U.S. domestic sales of computers have been very strong, fueled by price wars and by a push by U.S. businesses to upgrade PCs and workstations to take advantage of improved software. Most of the increased sales were in the low end of the computer spectrum, items that are often imported. Imports of machinery other than computers also rose solidly in the third quarter; the steady increase in these imports throughout 1992 represents the first turnup in these items since 1988 and is consistent with some firming in domestic spending for this equipment.

Oil Imports

The quantity of oil imports rose sharply in September as stocks were built up. The volume of oil imports for the third quarter was almost 0.3 mb/d above the second-quarter rate, the result of increased consumption and a drop in domestic production that was in part the result of Hurricane Andrew.

OIL IMPORTS
(BOP basis, seasonally adjusted annual rates)

| | 1992 | | | Months | | | |
|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Jun | Jul | Aug | Sep |
| Value (Bil. $) | 41.47 | 51.73 | 56.85 | 57.24 | 57.56 | 54.90 | 58.10 |
| Price ($/BBL) | 15.27 | 17.47 | 18.55 | 18.81 | 18.67 | 18.49 | 18.47 |
| Quantity (mb/d) | 7.44 | 8.11 | 8.39 | 8.33 | 8.44 | 8.13 | 8.61 |

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Prices of oil imports moved in a narrow range from June through September, mirroring the stability over a similar period in spot oil prices. Since the middle of October, spot prices have fallen roughly $3.00 per barrel on strong production by Saudi Arabia and Iran, lackluster product demand, and disappointment with the November OPEC agreement. Spot West Texas Intermediate currently stands just above $19.00 per barrel. These movements in spot prices (after accounting for shipping and contract lags) suggest that import prices should fall to roughly $16.50 per barrel in December.

Prices of Non-oil Imports and Exports

In October, prices of non-oil imports rose 0.3 percent, the fifth consecutive month of increase. The largest rise was in the price of imported consumer goods. (Price data for November will be

IMPORT AND EXPORT PRICE MEASURES
(percent change from previous period, annual rate)

| | Year 1992-Q3 / 1991-Q3 | Quarters 1992 Q1 | Q2 | Q3 | Months 1992 Sep | Oct |
|---|---|---|---|---|---|---|
| | | (Quarterly Average, AR) | | | (Monthly Rates) | |
| | ---BLS Prices--- | | | | | |
| Imports, Total | 2.8 | -1.2 | 0.8 | 6.6 | 0.2 | 0.6 |
| Foods, Feeds, Bev. | -1.1 | 10.0 | -15.0 | -1.5 | 0.4 | 0.3 |
| Industrial Supplies | 1.8 | -15.1 | 12.1 | 9.7 | 0.2 | 1.1 |
| Ind Supp Ex Oil* | 0.4 | 4.7 | -0.5 | 2.1 | 0.2 | 0.2 |
| Capital Goods | 4.0 | 4.7 | -3.4 | 8.4 | 0.7 | 0.0 |
| Automotive Products | 2.5 | 0.9 | -2.6 | 4.6 | 0.1 | 0.4 |
| Consumer Goods | 4.2 | 6.2 | 0.3 | 5.3 | -0.1 | 0.6 |
| Memo: | | | | | | |
| Oil | 4.5 | -45.0 | 44.4 | 25.5 | 0.1 | 2.6 |
| Non-oil | 2.6 | 4.4 | -2.7 | 4.8 | 0.2 | 0.3 |
| Exports, Total | 1.0 | -1.2 | 2.0 | 0.7 | 0.2 | -0.4 |
| Foods, Feeds, Bev. | -0.4 | -1.3 | -2.0 | -13.6 | 3.0 | -2.6 |
| Industrial Supplies | 0.2 | -6.5 | 5.5 | 5.5 | -0.3 | -0.5 |
| Capital Goods | 1.4 | 1.2 | 0.9 | 1.2 | -0.2 | -0.2 |
| Automotive Products | 1.8 | 1.6 | 1.2 | 1.3 | 0.2 | 0.6 |
| Consumer Goods | 2.6 | 5.9 | 1.6 | 0.3 | 0.0 | 0.2 |
| Memo: | | | | | | |
| Agricultural | -0.5 | -3.3 | -1.0 | -7.6 | 1.9 | -2.0 |
| Nonagricultural | 1.2 | -1.0 | 2.7 | 2.0 | -0.1 | -0.2 |
| | ---Prices in the NIPA Accounts--- | | | | | |
| Fixed-Weight | | | | | | |
| Imports, Total | 2.5 | -4.2 | 4.8 | 5.9 | -- | -- |
| Oil | 8.0 | -48.9 | 72.1 | 28.6 | -- | -- |
| Non-oil | 2.1 | 1.8 | 0.0 | 4.3 | -- | -- |
| Exports, Total | 0.8 | -0.7 | 1.5 | 0.4 | -- | -- |
| Ag | -1.0 | -4.1 | -1.1 | -8.2 | -- | -- |
| Nonag | 1.1 | -0.4 | 1.8 | 1.8 | -- | -- |
| Deflators | | | | | | |
| Imports, Total | -0.1 | -6.9 | 2.3 | 2.3 | -- | -- |
| Oil | 7.6 | -48.6 | 70.7 | 26.7 | -- | -- |
| Non-oil | -0.9 | -1.5 | -2.3 | -0.1 | -- | -- |
| Exports, Total | -0.9 | -1.1 | -1.8 | -1.6 | -- | -- |
| Ag | -1.9 | -5.2 | -1.6 | -5.2 | -- | -- |
| Nonag | -0.8 | -0.7 | -1.8 | -1.4 | -- | -- |

*/ Months not for publication.

released December 24.) For the third quarter, prices of non-oil imports rose at about a 4-1/2 percent annual rate. Strong price increases for imports of capital goods were attributable in part to the depreciation of the dollar over the summer. Prices of imported consumer goods and automotive products also rose noticeably in the third quarter.

Prices of exports have changed little on average in recent months. Prices of nonagricultural exports decreased slightly in October (with most of the decrease in industrial supplies and capital goods) and rose slightly in the third quarter (with increases in all major categories). Prices of agricultural exports declined in October as they did in the first three quarters.

U.S. Current Account

The U.S. current account deficit in the third quarter was $57 billion (seasonally adjusted, annual rate), $14 billion smaller than in the second quarter.

U.S. Current Account
(billions of dollars, seasonally adjusted annual rates)

| | Merchandise Trade, net | Services net | Investment Income, net | Transfers net | Current Acct Balance: Pub. | Current Acct Balance: Ex Special Grants 1/ |
|---|---|---|---|---|---|---|
| Years | | | | | | |
| 1989 | -115.7 | 25.8 | 14.3 | -25.6 | -101.1 | -101.1 |
| 1990 | -108.9 | 32.1 | 19.2 | -32.9 | -90.4 | -87.5 |
| 1991 | -73.4 | 45.3 | 16.4 | 8.0 | -3.7 | -41.0 |
| Quarters | | | | | | |
| 1991-1 | -73.3 | 37.4 | 27.9 | 56.8 | 48.8 | -37.1 |
| 2 | -65.6 | 43.1 | 15.7 | 16.5 | 9.7 | -36.2 |
| 3 | -80.7 | 48.1 | 12.3 | -24.0 | -44.3 | -47.1 |
| 4 | -74.2 | 52.5 | 9.8 | -17.1 | -28.9 | -43.5 |
| 1992-1 | -68.9 | 55.4 | 17.9 | -28.0 | -23.6 | -25.4 |
| 2-r | -98.2 | 50.6 | 7.7 | -31.2 | -71.2 | -74.2 |
| 3 | -106.2 | 62.5 | 14.2 | -27.5 | -57.0 | -57.0 |

1/ Excludes foreign cash grants to the United States to cover costs of the war in the Persian Gulf. These grants amounted to $4.3 billion in 1990, $42.6 billion in 1991, and $1.3 billion in 1992; they are shown in the accounts as positive unilateral transfers. Also excludes special U.S. grants to foreign countries amounting to $7.2 billion in 1990 and $5.2 billion in 1991.

The narrowing of the deficit in the third quarter occurred primarily as increases in net receipts from services and investment income more than offset a weakening in the merchandise trade balance. The sharp increase in net service receipts was largely a result of losses recovered from foreign reinsurers for damage caused by Hurricanes Andrew and Iniki in late August and mid-September. Net income from both direct and portfolio investments increased somewhat in the third quarter. There was a slight easing of income payments on foreign direct investments in the United States, and U.S. income receipts on direct investments abroad increased marginally. Sharply lower interest rates led to a larger drop in portfolio income payments than in portfolio income receipts (recorded liabilities exceed recorded assets). In addition, U.S. net unilateral transfers abroad dropped back somewhat in the third quarter from levels recorded in the second quarter.

U.S. International Financial Transactions

Foreign official reserve assets in the United States rose sharply in October, almost entirely reversing September's decline. (See line 4 of the Summary of U.S. International Transactions Table.) The changes in both months were largely accounted for by the Bank for International Settlements (BIS). Partial data for November from the FRBNY indicate that a moderate decline in G-10 reserve holdings was almost matched by a further increase in BIS holdings.

Banks reported substantial net capital outflows between the last day of September and the last day of October (line 1), partially reversing the large September inflow. However, monthly average data on the net claims of U.S. banking offices on their own foreign offices and IBFs, shown on line 1 of the International

SUMMARY OF U.S. INTERNATIONAL TRANSACTIONS
(Billions of dollars)

| | 1990 Year | 1991 Year | 1991 Q4 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Aug. | 1992 Sept. | 1992 Oct. |
|---|---|---|---|---|---|---|---|---|---|
| Private Capital | | | | | | | | | |
| Banks | | | | | | | | | |
| 1. Change in net foreign positions of banking offices[1] in the U.S. (+ = inflow) | 36.6 | -18.4 | -2.1 | 4.4 | -2.5 | 32.8 | 11.4 | 26.3 | -20.1 |
| Securities | | | | | | | | | |
| 2. Private securities transactions, net[2] | -29.1 | -10.9 | -6.0 | -4.3 | 1.7 | -12.3 | -1.3 | -4.7 | -3.9 |
| a) foreign net purchases (+) of U.S. corporate bonds[3] | 16.2 | 25.7 | 6.6 | 7.7 | 11.8 | 6.8 | 2.7 | 2.3 | 3.2 |
| b) foreign net purchases (+) of U.S. corporate stocks | -13.7 | 10.1 | -1.5 | -2.8 | -1.2 | -3.8 | -1.4 | -2.4 | 0.4 |
| c) U.S. net purchases (-) of foreign securities | -31.6 | -46.8 | -11.1 | -9.1 | -8.8 | -15.3 | -2.6 | -4.6 | -7.5 |
| 3. Foreign net purchases (+) of U.S. Treasury obligations | -1.0 | 19.3 | 1.9 | 0.8 | 10.4 | 5.0 | 7.4 | -2.7 | 3.1 |
| Official Capital | | | | | | | | | |
| 4. Changes in foreign official reserves assets in U.S. (+ = increase) | 32.1 | 16.0 | 13.3 | 21.0 | 20.3 | -8.2 | 2.5 | -12.9 | 11.6 |
| a) By area | | | | | | | | | |
| G-10 countries | 10.0 | -17.6 | 0.5 | 2.4 | 3.3 | 3.8 | 1.0 | 0.5 | -3.0 |
| OPEC | 1.2 | -5.8 | 1.2 | 2.7 | -2.5 | 2.9 | -0.1 | 1.8 | 0.9 |
| All other countries | 20.8 | 39.3 | 11.6 | 15.9 | 19.5 | -14.9 | 1.7 | -15.2 | 13.7 |
| b) By type | | | | | | | | | |
| U.S. Treasury securities | 29.6 | 14.8 | 12.6 | 14.9 | 11.1 | -0.3 | -0.9 | -4.1 | -6. |
| Other[4] | 2.5 | 1.2 | 0.7 | 6.0 | 9.2 | -7.8 | 3.4 | -8.8 | 18.0 |
| 5. Changes in U.S. official reserve assets (+ = decrease) | -2.2 | 5.8 | 1.2 | -1.1 | 1.5 | 2.0 | 1.5 | * | 0.5 |
| Other transactions (Quarterly data)[5] | | | | | | | | | |
| 6. U.S. direct investment (-) abroad | -32.7 | -27.1 | -11.7 | -15.1 | -7.0 | -7.2 | n.a. | n.a. | n.a. |
| 7. Foreign direct investment (+) in U.S. | 45.1 | 11.5 | 5.7 | -3.8 | 5.3 | -3.4 | n.a. | n.a. | n.a. |
| 8. Other capital flows (+ = inflow)[6] | -5.8 | 8.6 | 2.5 | 12.4 | 17.8 | -11.6 | n.a. | n.a. | n.a. |
| 9. U.S. current account balance | -90.4 | -3.7 | -7.2 | -5.9 | -17.8 | -14.2 | n.a. | n.a. | n.a. |
| 10. Statistical discrepancy | 47.4 | -1.1 | 2.4 | -8.4 | -29.7 | 17.1 | n.a. | n.a. | n.a. |
| MEMO: | | | | | | | | | |
| U.S. merchandise trade balance -- part of line 9 (Balance of payments basis, seasonally adjusted) | -108.9 | -73.4 | -18.5 | -17.2 | -24.6 | -26.5 | n.a. | n.a. | n.a. |

1. Includes changes in positions of all depository institutions, bank-holding companies, and certain transactions between brokers/dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements.)
2. These data have not been adjusted to exclude commissions on securities transactions and, therefore, do not match exactly the data on U.S. international transactions as published by the Department of Commerce.
3. Includes all U.S. bonds other than Treasury obligations.
4. Includes deposits in banks, commercial paper, acceptances, borrowing under repurchase agreements, and other securities.
5. Seasonally adjusted.
6. Includes U.S. government assets other than official reserves, transactions by nonbanking concerns, and other banking and official transactions not shown elsewhere. In addition, it includes amounts resulting from adjustments to the data ma the Department of Commerce and revisions to the data in lines 1 through 5 since publication of the quarterly data in t. Survey of Current Business.
*--Less than $50 million.
NOTE: Details may not add to total because of rounding.

Banking Data Table, show far less volatility. On a monthly average basis, net Eurodollar borrowing by foreign-chartered banks (line 1b) has been increasing since August, a net inflow. These increases have been concentrated at branches and agencies of non-Japanese banks and have coincided with asset growth at these banks.

U.S. net purchases of foreign stocks and bonds were very high in October (line 2c of the Summary of U.S. International Transactions Table), bringing the total for the first 10 months of 1992 close to the record 1991 pace. Net purchases of equities of about $4.1 billion in October were concentrated in the United Kingdom, Switzerland, and Australia. Net bond purchases ($3.4 billion) were concentrated in the United Kingdom and France.

Private foreign net purchases of U.S. bonds were also substantial in October: $3.1 billion in U.S. Treasury securities (line 3), $2.6 billion in U.S. government agency bonds, and $0.6 billion in corporate bonds (both included in line 2a). In addition, foreigners bought U.S. stocks net in October (line 2b), after four consecutive months of net sales.

Data recently released by BEA for the third quarter are shown in lines 6 through 10. U.S. direct investment abroad (line 6) continued strong at more than $7 billion, although the outflow for the second quarter was revised down from $11 billion to $7 billion. Foreign direct investment in the United States (line 7) was a net outflow of $3 billion, largely reflecting outflows on intercompany accounts and negative reinvested earnings.

The statistical discrepancy in the U.S. international accounts (line 10) rose to $17 billion in the third quarter, partially reversing the large negative discrepancy in the accounts in the first half of the year. A small part of this shift can be explained

INTERNATIONAL BANKING DATA
(Billions of dollars)

| | 1990 | 1991 | | | | 1992 | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Dec. | Mar. | June | Sept. | Dec. | June | July | Aug. | Sept. | Oct. | Nov. |
| 1. Net Claims of U.S. Banking Offices (excluding IBFS) on Own Foreign Offices and IBFS | -31.3 | -23.8 | -13.7 | -14.1 | -35.8 | -56.8 | -56.0 | -54.1 | -58.0 | -61.4 | -66.6 |
| (a) U.S.-chartered banks | 5.5 | 7.6 | 5.4 | 11.0 | 12.4 | 8.3 | 9.0 | 11.2 | 12.7 | 14.6 | 13.5 |
| (b) Foreign-chartered banks | -36.9 | -31.3 | -19.2 | -25.2 | -48.3 | -65.1 | -65.0 | -65.3 | -70.9 | -76.1 | -80.1 |
| 2. Credit Extended to U.S. Nonbank Residents by Foreign Branches of U.S. Banks | 24.7 | 26.0 | 23.9 | 23.7 | 23.9 | 24.5 | 25.1 | 24.8 | 24.8 | 25.1 | 25.1 |
| 3. Eurodollar Holdings of U.S. Nonbank Residents 1/ | 116.1 | 114.6 | 105.8 | 100.8 | 102.9 | 91.2 | 88.2 | 85.4 | 84.6 | 86.7 | 89.0 |

1. Includes term and overnight Eurodollars held by money market mutual funds. Note: These data differ in coverage and timing from the overall banking data incorporated in the international transactions accounts. Line 1 is an average of daily data reported to the Federal Reserve by U.S. banking offices. Line 2 is an average of daily data. Line 3 is an average of daily data for the overnight component and an average of Wednesday data for the term component.

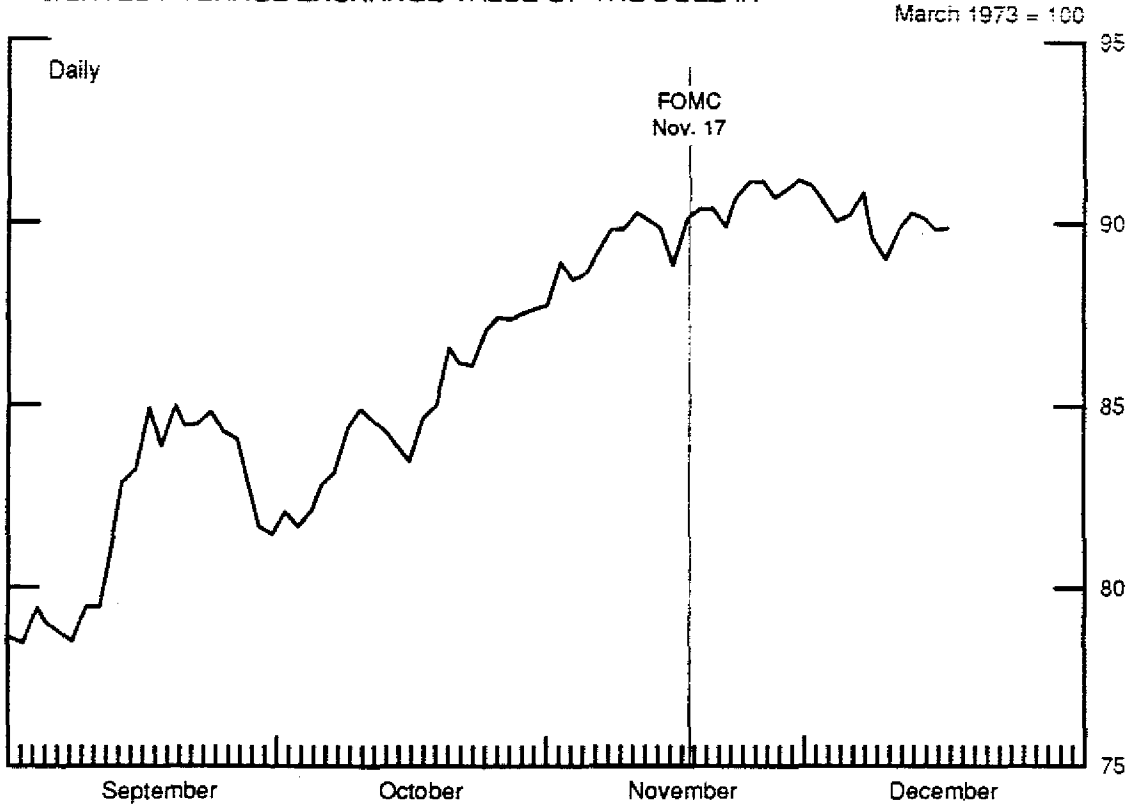
by an acceleration of shipments of U.S. currency abroad in the third quarter: no data on increases in foreign holdings of U.S. currency are included by BEA in the international transactions accounts. According to confidential data collected by the FRBNY, net currency shipments amounted to $6.7 billion in the third quarter, compared with $2.3 billion in the second quarter and $1.7 billion in the first. In October, net shipments fell to $0.6 billion.

Foreign Exchange Markets

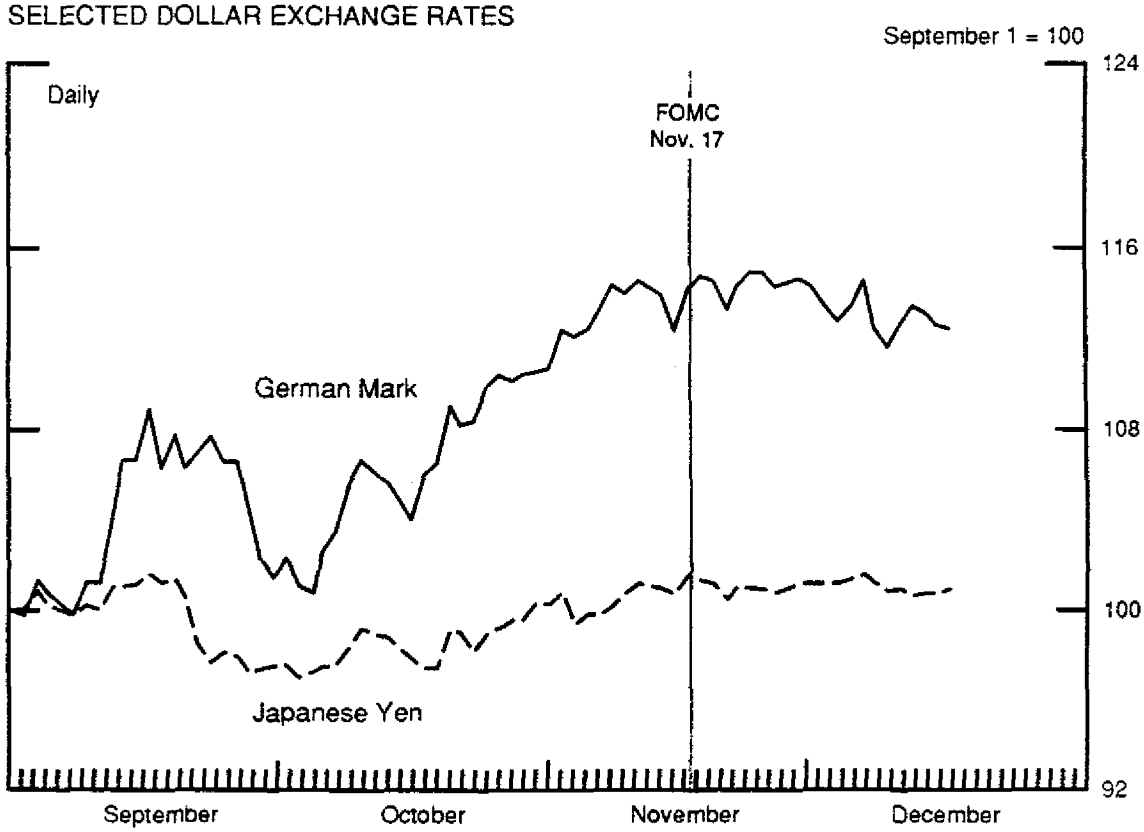
The weighted average foreign exchange value of the dollar in terms of the other G-10 currencies has declined slightly on balance since the last meeting and posted a net decline of about 1-1/4 percent. The dollar has declined nearly 3 percent against the mark, and about 1-1/4 percent against the yen. The dollar had a slight upward drift for the first half of the period in response to data showing that the outlook for U.S. economic growth is improving, while the outlook for economic growth in Japan and Germany is deteriorating. Towards the end of the period, in thin end-of-year markets, the dollar gave up its gains. Strong anti-inflation rhetoric by Bundesbank officials in the latter half of the period reduced expectations of Bundesbank near-term easing and contributed to the dollar's decline.

The dominant development in foreign exchange markets during the period has been an apparent rekindling of exchange rate pressures on some of those currencies that had unilaterally (Sweden and Norway) or multilaterally (the Exchange Rate Mechanism countries) tied their currencies to the other European currencies. On November 19, following very large sales of foreign currency over the previous 1-1/2 weeks, the Bank of Sweden allowed its currency to float.

WEIGHTED AVERAGE EXCHANGE VALUE OF THE DOLLAR




SELECTED DOLLAR EXCHANGE RATES



The floating of Sweden's currency placed pressures on the currencies of Norway and Denmark. Pressures also emerged for the currencies of Spain, Portugal, and Ireland. These three currencies were considered prime candidates for devaluation at the beginning of the period because the floating of the lira and sterling in September had reduced the competitiveness of their exports, and because during the previous exchange rate pressures in September these countries had defended their currencies with capital controls that, in the case of Spain and Ireland, were expected to be removed by year-end.

During the intermeeting period, but following Sweden's floating, three other currencies were either floated or realigned. The peseta and escudo were devalued 6 percent shortly following the Swedish action. This devaluation of the peseta is in addition to its 7 percent devaluation in September. Spain and Portugal also removed their capital controls during the period. Toward the end of the period, Norway, , allowed its currency to float.

The French franc was also under pressure during the period. Harsh rhetoric by Bundesbank President Schlesinger in which he indicated that it would be improper to ease German interest rates to help other countries, and in which he termed ERM intervention at the limit as destabilizing, contributed to pressures on the franc. Later, statements by the finance ministers of both countries as well as statements by Bundesbank officials indicated support for the franc at its current parities.

Although the currencies of Ireland and Denmark were not devalued during the period, both currencies experienced intermittent periods of intense pressure. The last such period was just prior to the Edinburgh summit, on the possibility that the currencies of both countries would be devalued during the summit. Following the summit, pressures on these currencies eased.

The Swiss franc appears to have gained on safe-haven concerns over the turmoil in Europe. During the period, a referendum to join the European Economic Area was rejected by Swiss voters. Following the rejection, the Swiss franc advanced against the mark. On balance, the Swiss franc has appreciated 1-1/4 percent against the mark during the intermeeting period.

Three-month interest rates in Japan rose 5 basis points during the intermeeting period while long rates were unchanged. Three-month rates rose 10 basis points in Germany during the period, perhaps in part due to the strong anti-inflation rhetoric coming from Bundesbank officials. Long rates in Germany have stayed firm. Three-month rates in France have risen just over 150 basis points in response to the renewed exchange pressures on the French franc. Sweden's three-month rate has declined 250 basis points to 10-1/4 percent because Sweden no longer needs to maintain high interest rates to support its currency.

In world equity markets, the Hang Seng index of the Hong Kong stock market declined 12 percent during the intermeeting period as a result of a dispute between the United Kingdom and China over democratic reforms for Hong Kong. This dispute has called into question the commitment of the Chinese government not to exert control over Hong Kong's markets. The Swedish stock market rose 21 percent during the intermeeting period. This rally is likely to be attributable to several factors, including lower interest rates in Sweden and an increase in the competitiveness of Sweden's exports following the krona's floating. Also, expectations that the Swedish currency would soon devalue or float may have deterred investment in Swedish equities before the devaluation.

Developments in Foreign Industrial Countries

Most recent indicators point to continued weakness in the major foreign industrial countries. In the third quarter, real GDP (s.a.a.r.) declined 1.5 percent in Japan and 1.9 percent in Germany. In both countries early fourth-quarter data also suggest weak activity. In France and Canada, real GDP increased in the third quarter, but only at annual rates of about 1-1/2 percent. In the United Kingdom, provisional data suggest that real GDP was either flat or down slightly in the third quarter. With activity weak, inflation rates generally have continued to trend lower.

Several countries recently announced monetary targets for next year. The German target for M3, which appears likely to be exceeded significantly this year, was raised slightly. The French target also was edged upward, while the Swiss and Italian targets remained unchanged.

Individual country notes. In Japan, real GDP declined 1.5 percent (s.a.a.r.) in the third quarter, following a downward revised decline of 0.9 percent in the second quarter. While consumption rose in the third quarter (up 2.7 percent), plant and equipment investment showed a further sharp decline (down 8.4 percent). Housing investment was about flat. Government investment declined 12.3 percent, but this only partially reversed the very rapid increase of the previous quarter, and on a year-over-year basis government investment was up 12.8 percent. A reduced pace of inventory investment made a negative contribution to growth of 0.7 percentage point. Net exports made a 0.3 percent percentage point

REAL GNP AND INDUSTRIAL PRODUCTION IN MAJOR INDUSTRIAL COUNTRIES
(Percentage change from previous period, seasonally adjusted) 1

| | Q4/Q4 1990 | Q4/Q4 1991 | 1991 Q4 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 July | 1992 Aug. | 1992 Sept. | 1992 Oct. | 1992 Nov. | Latest 3 months from year ago 2 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Canada** | | | | | | | | | | | | |
| GDP | -2.0 | -.0 | .0 | .2 | .1 | .4 | * | * | * | * | * | .7 |
| IP | -6.3 | -1.4 | -1.1 | -.2 | .4 | n.a. | -.4 | 1.9 | n.a. | n.a. | n.a. | -.4 |
| **France** | | | | | | | | | | | | |
| GDP | 1.5 | 1.7 | .1 | 1.0 | .2 | .4 | * | * | * | * | * | 1.7 |
| IP | -.3 | 1.9 | -.2 | .1 | -.1 | n.a. | .0 | .0 | n.a. | n.a. | n.a. | -.7 |
| **WEST GERMANY** | | | | | | | | | | | | |
| GDP | 5.8 | 2.0 | -.3 | 2.0 | -.3 | -.5 | * | * | * | * | * | .9 |
| IP | 5.4 | .3 | -1.2 | 2.8 | -2.0 | -1.3 | -.4 | .2 | .0 | -2.2 | n.a. | -1.9 |
| **Italy** | | | | | | | | | | | | |
| GDP | 1.6 | 1.7 | .4 | .6 | .2 | n.a. | * | * | * | * | * | 1.5 |
| IP | -3.8 | -.5 | 1.1 | 2.5 | -2.8 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | .5 |
| **JAPAN** | | | | | | | | | | | | |
| GDP | 4.7 | 3.0 | .5 | 1.0 | -.2 | -.4 | * | * | * | * | * | .9 |
| IP | 6.9 | -1.6 | -1.2 | -3.1 | -2.3 | .3 | .4 | -4.2 | 5.2 | -2.9 | n.a. | -6.2 |
| **United Kingdom** | | | | | | | | | | | | |
| GDP | -1.0 | -1.6 | -.3 | -.4 | -.2 | .0 | * | * | * | * | * | -.8 |
| IP | -3.1 | -.7 | -.1 | -.8 | -.3 | .7 | 1.1 | -.3 | .5 | 1.0 | n.a. | .1 |
| **UNITED STATES** | | | | | | | | | | | | |
| GDP | -.5 | .1 | .1 | .7 | .4 | 1.0 | * | * | * | * | * | 2.2 |
| IP | .3 | -.5 | -.2 | -.7 | 1.3 | .5 | .8 | -.2 | -.3 | .5 | .4 | .9 |

1. Asterisk indicates that monthly data are not available.
2. For quarterly data, latest quarter from year ago.

CONSUMER AND WHOLESALE PRICES IN MAJOR INDUSTRIAL COUNTRIES
(Percentage change from previous period) 1

| | Q4/Q4 1990 | Q4/Q4 1991 | 1991 Q2 | 1991 Q3 | 1991 Q4 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Aug. | 1992 Sept. | 1992 Oct. | 1992 Nov. | Latest 3 months from year ago |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Canada** | | | | | | | | | | | | | |
| CPI | 4.9 | 4.1 | .7 | .6 | -.1 | .4 | .5 | .4 | .0 | -.1 | .2 | n.a. | 1.3 |
| WPI | 1.9 | -3.2 | -1.6 | -.9 | -.4 | .5 | .6 | .8 | .1 | .6 | .5 | n.a. | 2.2 |
| **France** | | | | | | | | | | | | | |
| CPI | 3.6 | 2.9 | .7 | .8 | .8 | .7 | .7 | .5 | .1 | .1 | .1 | .0 | 2.3 |
| WPI | .7 | -3.6 | -1.5 | -.7 | -1.0 | .2 | .4 | n.a. | * | * | * | * | -1.1 |
| **West Germany** | | | | | | | | | | | | | |
| CPI | 3.0 | 3.9 | .9 | 1.5 | .7 | 1.2 | 1.1 | .5 | .2 | .3 | .3 | .5 | 3.7 |
| WPI | .9 | 1.6 | .3 | .7 | .2 | .4 | .5 | -2.0 | -.7 | -.4 | -.1 | n.a. | -1.2 |
| **Italy** | | | | | | | | | | | | | |
| CPI | 6.3 | 6.1 | 1.4 | 1.0 | 1.7 | 1.4 | 1.2 | .7 | .1 | .3 | .6 | .6 | 4.9 |
| WPI | 9.9 | 1.1 | -1.0 | .5 | 1.4 | .0 | .8 | -.5 | -.3 | .2 | n.a. | n.a. | 1.7 |
| **Japan** | | | | | | | | | | | | | |
| CPI | 3.2 | 3.2 | .8 | .4 | 1.1 | -.3 | 1.3 | -.1 | .1 | .5 | -.1 | -.3 | 1.3 |
| WPI | 1.9 | -1.3 | -.4 | -.4 | -.7 | -.4 | .0 | -.1 | .1 | -.3 | -.7 | .0 | -1.3 |
| **United Kingdom** | | | | | | | | | | | | | |
| CPI | 10.0 | 4.2 | 2.1 | .4 | 1.0 | .5 | 2.2 | -.1 | .1 | .4 | .4 | -.1 | 3.4 |
| WPI | 5.9 | 4.9 | 1.9 | .6 | .5 | 1.4 | 1.1 | .4 | .1 | .1 | .1 | .3 | 3.3 |
| **United States** | | | | | | | | | | | | | |
| CPI (SA) | 6.3 | 3.0 | .6 | .7 | .9 | .7 | .8 | .6 | .3 | .2 | .4 | .2 | 3.1 |
| WPI (SA) | 6.4 | -.1 | -.2 | .0 | .5 | .0 | .8 | .4 | .1 | .3 | .1 | -.2 | 1.5 |

1. Asterisk indicates that monthly data are not available.

TRADE AND CURRENT ACCOUNT BALANCES OF MAJOR INDUSTRIAL COUNTRIES 1
(Billions of U.S. dollars, seasonally adjusted except where otherwise noted)

| | 1990 | 1991 | 1991 Q2 | 1991 Q3 | 1991 Q4 | 1992 Q1 | 1992 Q2 | 1992 Q3 | 1992 Aug. | 1992 Sept. | 1992 Oct. | 1992 Nov. |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Canada** | | | | | | | | | | | | |
| Trade | 9.4 | 5.0 | 1.7 | .9 | 1.0 | 1.6 | 1.6 | 1.5 | .6 | .4 | n.a. | n.a. |
| Current account | -21.5 | -25.5 | -6.0 | -6.6 | -7.3 | -6.2 | -6.2 | -6.4 | * | * | * | * |
| **France** | | | | | | | | | | | | |
| Trade | -9.3 | -5.3 | -1.5 | -1.5 | .4 | 1.1 | 1.9 | 1.3 | -.6 | .7 | .2 | n.a. |
| Current account | -9.5 | -4.7 | -1.6 | -.2 | 1.1 | n.a. | n.a. | n.a. | * | * | * | * |
| **Germany 2** | | | | | | | | | | | | |
| Trade (NSA) | 65.2 | 12.9 | -1.1 | 2.8 | 6.7 | 4.4 | 3.4 | 8.5 | 3.9 | 3.8 | n.a. | n.a. |
| Current Account (NSA) | 46.4 | -19.5 | -5.9 | -5.9 | -2.2 | -5.6 | -6.1 | -9.0 | -1.3 | -2.5 | -.8 | n.a. |
| **Italy** | | | | | | | | | | | | |
| Trade | -12.2 | -13.0 | -3.5 | -4.9 | -3.3 | -1.9 | -4.0 | n.a. | n.a. | n.a. | n.a. | n.a. |
| Current account (NSA) | -14.4 | -21.5 | -4.6 | -3.7 | -5.0 | n.a. | n.a. | n.a. | * | * | * | * |
| **Japan** | | | | | | | | | | | | |
| Trade | 51.7 | 78.5 | 19.7 | 21.0 | 21.2 | 28.0 | 24.5 | 26.2 | 8.3 | 9.4 | 10.4 | 8.8 |
| Current account | 35.9 | 73.1 | 18.8 | 19.5 | 22.9 | 28.6 | 28.8 | 28.1 | 8.5 | 9.9 | 10.4 | n.a. |
| **United Kingdom** | | | | | | | | | | | | |
| Trade | -33.0 | -18.3 | -3.8 | -4.0 | -4.7 | -5.4 | -5.7 | -6.2 | -2.2 | -1.8 | -1.9 | n.a. |
| Current account | -26.8 | -9.9 | -.4 | -2.1 | -3.0 | -5.1 | -5.1 | -5.7 | -2.1 | -1.6 | -1.8 | n.a. |
| **United States** | | | | | | | | | | | | |
| Trade | -108.9 | -73.4 | -16.4 | -20.2 | -18.5 | -17.2 | -24.6 | -26.5 | -9.4 | -9.0 | n.a. | n.a. |
| Current account | -90.4 | -3.7 | 2.4 | -11.1 | -7.2 | -5.9 | -17.8 | n.a. | * | * | * | * |

1. The current account includes goods, services, and private and official transfers. Asterisk indicates that monthly data are not available.
2. Before July 1990, West Germany only.

positive contribution to growth as exports increased 3.5 percent while imports rose 3.3 percent.

Indicators of activity early in the fourth quarter have also been generally weak. Industrial production (s.a.) fell 2.9 percent in October, and its 12-month decline widened to 6.4 percent. Retail sales in October were 2.6 percent below their year-earlier level. New passenger car registrations (s.a.) fell a further 9.3 percent in October and were down 16.1 percent on a 12-month basis. New machinery orders (s.a.) fell 30.7 percent in October, more than reversing their sharp increase of the previous month, and were 23.9 percent below their year-earlier level. The unemployment rate (s.a.) remained unchanged for the fourth consecutive month at 2.2 percent in October, but the job offers to applicants ratio (s.a.) dropped a further 5 percent to a level 34.7 percent below its peak of March 1991.

The Bank of Japan's quarterly economic survey (Tankan) taken in November reported a further deterioration in business sentiment. The index measuring the business sentiment of major manufacturing firms (the percent having a favorable view of business conditions minus the percent with an unfavorable outlook) fell to minus 44 from minus 37 in the last survey taken in August, its lowest level since 1975. On average, firms predicted a 4.7 percent decline in investment in the current fiscal year, down from the 2.8 percent

JAPANESE ECONOMIC INDICATORS
(percent change from previous period except where noted, s.a.)

| | 1992 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Aug. | Sep. | Oct. |
| Machinery Orders | 2.4 | -14.3 | 11.4 | -- | 4.4 | 20.7 | -30.7 |
| New Car Registrations | 1.5 | -6.7 | -2.6 | -- | -6.1 | 6.5 | -9.3 |
| Job Offers Ratio | -5.3 | -9.6 | -9.7 | -- | -2.0 | -1.0 | -5.0 |
| Business Sentiment* (%) | -5 | -24 | -37 | -44 | -- | -- | -- |

* Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.

reduction forecast in the previous Tankan. The index showing the degree to which firms felt inventories were excessive edged down to 37 from 38 in the previous survey.

Consumer prices in the Tokyo area (n.s.a.) declined 0.3 percent in November, and their 12-month increase fell to 0.6 percent. However, nearly all of this reduction was due to a sharp fall in perishable food prices that had been elevated last year by the effects of typhoons. Excluding these items, the 12-month consumer price inflation rate was 2.1 percent, little changed from that of recent months. Wholesale prices (n.s.a.) were unchanged in November and showed a 12-month decline of 1.3 percent.

The trade surplus (s.a.) decreased slightly in November, but for the first eleven months of the year the surplus was $107 billion (a.r.), 39 percent above the surplus in the corresponding period last year.

Real GDP in western Germany continued to decline in the third quarter, registering a drop of 1.9 percent (s.a.a.r.) that reflected significant weakness in domestic demand. Both consumption and investment spending fell sharply, while net exports provided a partial offset. Net exports, which include trade with eastern Germany, have continued to contribute to growth in real GDP despite weak growth in Germany's major trading partners.

Industrial production (s.a.) in western Germany has been on a downtrend since early this year. Data for October suggest that the fourth quarter is off to a poor start, with industrial production more than 2 percent below its September level. The volume of new orders for west German manufactured goods (s.a.) has fallen steadily since early in the year, and declined more than 5 percent in October relative to the third-quarter average. After remaining steady throughout 1991 at roughly 6.3 percent, the unemployment rate (s.a.)

in western Germany has edged up since February and stood at 6.7 percent in November.

WESTERN GERMAN ECONOMIC INDICATORS
(percent change from previous period except where noted, s.a.)

| | 1991 | 1992 | | | | | |
|---|---|---|---|---|---|---|---|
| | Q4 | Q1 | Q2 | Q3 | Sep. | Oct. | Nov. |
| Manufacturing Orders | -1.5 | 2.2 | -4.0 | -2.1 | 0.2 | -5.1 | -- |
| Capacity Utilization | -0.9 | -0.6 | -1.4 | -2.2 | -- | -- | -- |
| Unemployment Rate (%) | 6.3 | 6.2 | 6.5 | 6.6 | 6.5 | 6.6 | 6.7 |
| Production Plans* (%) | -1.7 | -3.7 | -6.0 | -12.0 | -21.0 | -35.0 | -- |

* Percent of mining and manufacturing firms that expect to increase production minus those who expect to decrease it.

On a year-over-year basis, consumer prices increased almost 3.5 percent in the third quarter and were up 3.7 percent in November. Wholesale prices (n.s.a.) in western Germany dropped 1.7 percent in October on a year-over-year basis, and increases in producer prices have moderated significantly. Import prices (n.s.a.) in western Germany began to edge down in June, and declined in September to reach a level almost 5 percent below their level in September 1991.

After improving in the fourth quarter of last year, the pan-German current account (n.s.a.) deteriorated in the first three quarters of this year. The widening of the current account deficit, which reached a cumulative $21.5 billion (n.s.a.) through October, primarily reflects a drop off in the value of exports.

Through October, M3 in western and eastern Germany combined increased 10.2 percent (s.a.a.r.) in 1992, relative to the fourth quarter of 1991. In both September and October, growth in M3 was boosted by the sizable DM intervention in exchange markets that occurred in mid-September. Monetary expansion remains well above the Bundesbank's M3 target range of 3-1/2 percent to 5-1/2 percent growth for 1992. The Bundesbank announced recently that its monetary target for next year is M3 growth in the range of 4-1/2 percent to 6-1/2 percent.

On November 27, the German parliament approved a draft budget for 1993 that holds the growth of nominal Federal expenditures to 2.5 percent. However, there remains a significant risk that the economic assumptions upon which the 1993 budget is based are too optimistic and that the actual deficit will exceed the projected DM 43 billion. In addition, Finance Minister Waigel announced that he intends to introduce next spring additional programs for eastern Germany in a supplemental budget of DM 2-3 billion. The government has indicated that the new programs will be financed through the reduction of other expenditures.

The round of yearly wage negotiations just beginning is off to a promising start, and it appears likely that the Kohl government will achieve its rumored goal of limiting nominal wage increases to 4 percent or less. So far, workers in the insurance and steel industries have agreed to wage increases of 4.2 percent and 3.4 percent, respectively, with the steel contract extending over an 18-month period. The union representing 2.3 million public sector employees, which is likely to be the trendsetter, has tabled a bid for a 5 percent increase.

In France, real marketable GDP, a reliable preliminary indicator of total GDP, rose 1.6 percent (s.a.a.r.) in the third quarter. The increase was entirely due to strong consumption, which registered growth of 3.6 percent, after declining 0.8 percent in the second quarter. Net exports and investment both made negative contributions. Recent monthly indicators have been mixed but, on balance, suggest that the modest second-quarter strength will not be sustained into the fourth quarter. Both the Bank of France's measure of industrial output (s.a.) and survey measures of production and investment intentions (s.a.) fell in October. The unemployment rate (s.a.) also rose slightly in October to 10.4 percent. In contrast, consumption of manufactured products (s.a.), equal to one-third of total consumption, increased 1.6 percent in October, suggesting that some of the third-quarter strength in consumption continued into the fourth quarter.

Finance Minister Sapin announced that the 1993 target range for M3 would be 4 percent to 6-1/2 percent, up slightly from the 1992 range of 4 percent to 6 percent. He also predicted that the final figure for actual M3 growth this year would be roughly 6 percent. The target range was announced on the same day as the German target range with the same upper limit of 6-1/2 percent in part to signal that monetary cooperation between France and Germany would continue to be close. Monetary targets are less important to the conduct of monetary policy in France than in Germany because France's participation in the ERM leads it to target the FF/DM exchange rate.

Inflation has continued to decline. In November, the consumer price index was 2.1 percent above its year-earlier level, down from 2.4 percent in the previous month.

The cumulative trade surplus (s.a.) over the first 10 months of this year was $4.3 billion; over the same period a year earlier France registered a deficit of $4.9 billion.

In Italy, economic growth continues to slow. Adjusting for the number of working days, industrial production in September fell 5.5 percent below its year-earlier level. In August, new orders fell 10.8 percent below their August 1991 level, while retail sales rose only 2.8 percent on this basis. This weakening trend in consumption is likely to continue because of plummeting consumer confidence. In October, the consumer confidence index fell 8.5 percent below September's level, which in turn was 10.5 percent below July's figure. (The survey is not conducted in August.) The only bright spot appears to be the foreign sector where, in October, exports grew 7.4 percent over last year while imports fell 0.5 percent.

The weakness of economic growth has slowed the rate of inflation. The year-on-year consumer price inflation rate fell to 4.9 percent in November, the sixth consecutive monthly reduction. The producer price index in September rose 1.8 percent on a year-on-year basis while the wholesale price index increased 1 percent.

Approximately 80 percent of the 93 trillion lire (roughly $71 billion equivalent) deficit-reduction package for 1993 has been approved by both houses of Parliament. The lower house has approved the remaining 20 percent of the package and has sent the bill to the upper house. Final passage is expected by Christmas.

The Bank of Italy recently announced that the monetary target for next year would remain unchanged, calling for 5 percent to 7 percent growth of M2.

The U.K. economy has exhibited a few signs of recovery. Industrial production (s.a.) rose 1 percent in October following a 0.4 percent gain in September. Manufacturing production (s.a.) rose 0.3 percent after it contracted 0.2 percent the previous month. Provisional data indicate that, after falling 0.7 percent (s.a.a.r.) in the second quarter, real GDP stalled in the third quarter, the ninth consecutive quarter of either flat or falling GDP. Unemployment (s.a.) continued to rise in October, and the rate remained at 10.1 percent, a five-year high. Consumer spending has been sluggish in recent months; the volume of retail sales (s.a.) fell 0.1 percent in November after rising 0.1 percent in October to stand only 0.7 percent above a year ago. Consumer confidence remains depressed at a level not far from its recession trough.

Consumer price inflation continues to moderate, despite the recent depreciation of the pound. Consumer prices (n.s.a.) fell 0.1 percent in November after rising 0.4 percent in October, making the 12-month rate of inflation 3 percent, the lowest level since 1986. Excluding mortgage interest rates, consumer prices were 3.6 percent above their level of November 1991, within the government's inflation target of 1-4 percent. Producers' output prices (s.a.) rose 0.3 percent in November after they rose 0.1 percent in October and were 3.3 percent above their year-earlier level. The prices of producers' materials and fuels (n.s.a.) rose 3 percent in November after rising 2.7 percent in October, largely reflecting price increases of imported materials associated with sterling's devaluation.

Despite continued weakness in domestic demand, the trade deficit (s.a.) widened considerably in recent months. The cumulative current account deficit for the first ten months of the year was $21.3 billion (s.a.a.r.), compared with a deficit of $9.5 billion in the same period of 1991.

The Canadian economy continued to inch forward in the third quarter. GDP increased 1.4 percent (s.a.a.r.) but still stood 1.6 percent below its cyclical peak in the first quarter of 1990. Final domestic demand rose 5.3 percent, and private investment in machinery and equipment surged to an all-time high, as Canadian businesses took advantage of low U.S. computer prices. However, the external sector made a negative net contribution as imports grew 11.4 percent. In addition, inventory destocking accelerated.

Activity indicators for the fourth quarter suggest continued sluggishness. In October, motor vehicle sales (s.a.) fell 4 percent below their third-quarter average. Housing starts (s.a.) in October and November combined were down 3.5 percent from the third quarter.

A sharp upturn in the labor force participation rate caused the unemployment rate (s.a.) to soar from 11.3 percent in October to 11.8 percent in November, its highest level in nine years. However, total employment (s.a.) rose 0.1 percent, the fourth consecutive monthly advance.

Recent price data show that inflation has remained moderate. The targeted 12-month change in the CPI, excluding food and energy, increased from 1.6 percent to 1.7 percent in October. The all-items CPI was up 1.6 percent over this period, and wholesale prices rose 2.8 percent. Average wage settlements (a.r.) for the first three quarters increased 2.3 percent, compared with a 3.6 percent average for all of 1991 and 5.6 percent for 1990.

On December 2, Finance Minister Don Mazankowski announced that he now expects the federal budget deficit for fiscal year 1992, which ends March 31, 1993, to reach C$34.4 billion (5 percent of GDP), about 25 percent above its target level. Accordingly, the government announced C$0.7 billion in spending cuts over the next four months (the end of fiscal year 1992), and further cuts for fiscal years 1993 and 1994.

In Switzerland, third-quarter national income account data showed continued weakness. GDP declined 0.1 percent (s.a.a.r.), after declining 0.4 percent in the second quarter. Strong positive contributions from net exports and the government sector limited this decline. The other components fell sharply, with consumption declining 1.1 percent in the third quarter after declining 3 percent in the second quarter, and investment dropping 4.5 percent after falling 10.4 percent in the second quarter. Inflation declined again in November to 3.3 percent on a year-over-year basis from 3.5 percent in the previous month, and was well below its 5-1/2 percent rate of a year ago.

The Swiss National Bank (SNB) announced that it will retain its target for Central Bank Money (CBM) growth of 1 percent per year in 1993. This target, first set at 1 percent in 1990, is a medium-term target to which the SNB adheres over a three- to five-year horizon. It reserves the right to deviate temporarily from it in response to circumstances. The SNB said that CBM will probably contract 1 percent in 1992, and that the target has been undershot by an average of 1.7 percentage point since it was first set; consequently, there would be room for it to grow above its target rate in 1993.

On December 6, Switzerland voted in a referendum not to join the European Economic Area (EEA). Approval of the treaty required both a popular majority nationwide and majorities in more than half of Switzerland's 26 Cantons. While the popular vote was close, with only 50.3 percent voting against the EEA treaty, the rejection was more decisive at the Canton level with all the German speaking Cantons except Basel rejecting the treaty. The rejection came despite strong support from the government, labor unions and business, and apparently was due mainly to voter concern that approval would lead to an influx of immigrants and that sovereignty would be lost to EC institutions in Brussels. The Swiss rejection will delay implementation of the EEA treaty, which was to take effect on January 1, 1993.

Poland and the IMF reached agreement on a memorandum of understanding for a new 14-month stand-by arrangement totalling about $700 million. The IMF Executive Board is expected to approve the program in January. Last April Poland received a three-year Extended Fund Facility arrangement, but fell out of compliance with the program within six months as the budget deficit exceeded program targets. Subsequently, a new Polish government has assumed office and has addressed several economic issues, including proposal of a tight 1993 budget. With agreement on a new IMF program, Poland is expected to approach commercial bank creditors again for reduction of its $12 billion in commercial debt. In 1991 Paris Club creditors agreed to reduce by 50 percent the net present value of Poland's official debt, which is estimated to be about $35 billion. In late November seven countries, including the United States, agreed to redirect resources from the Polish currency stabilization fund to a proposal for Polish bank recapitalization and privatization. Of the $500 million pledged thus far, the U.S. contribution is $200 million.

The Russian Congress of People's Deputies closed its most recent session on December 14 after confirming Viktor Chernomyrdin as Prime Minister. Chernomyrdin, formerly Deputy Prime Minister for energy, was nominated for the post by President Yeltsin. The Congress also agreed to hold a referendum on April 11 on constitutional changes aimed at clarifying the distribution of powers among the different branches of the Russian government. Yeltsin's decision to nominate Chernomyrdin was somewhat of a surprise because under an agreement reached earlier with the Congress Yeltsin could have retained Acting Prime Minister Gaidar in his post at least until the referendum in April. Chernomyrdin has said that he will maintain Gaidar's reforms, but it is unclear how the change in the Russian government will affect the course of reform.

Economic Situation in Other Countries

In Mexico, real GDP in the third quarter was 2.8 percent above a year earlier. The trade deficit is continuing to widen, and the authorities have introduced some trade barriers to slow this trend. The North American Free Trade Area agreement will be signed December 17. Growth in Taiwan and Korea has slowed. In Taiwan, sluggish world demand has weakened activity and narrowed the trade surplus. In Korea, slower growth reflects tight economic policies. As a result, Korea's trade deficit has narrowed considerably. In Brazil, economic activity continues to be depressed and inflation high as a result of the Franco government's inability to enact controversial fiscal and other economic reforms. On December 10, the economic subcommittee of the Brazilian Senate ratified the Brady Plan restructuring of Brazil's $44 billion commercial bank debt. The agreement is not expected to be implemented until Brazil takes more serious steps towards economic reform. In Venezuela, the economic and political climate remains unsettled in the wake of the coup attempt on November 27. In Argentina, industrial output in the third quarter was 13.4 percent above a year earlier. The trade surplus has narrowed considerably, mainly because of real exchange rate appreciation. On December 6, a signing ceremony was held for the Brady Plan commercial bank debt restructuring agreement.

Individual country notes. In Mexico, real GDP was 2.8 percent higher in the third quarter than a year earlier, the same rate of growth as in the first half (year-over-year). The government has forecast 1993 growth at 2.5 to 3 percent. The CPI rose by 0.8 percent in November, leaving the index 12.9 percent higher than a year earlier. Fiscal and monetary policies remain tight, with the aim of lowering twelve-month consumer price inflation to single digits in early 1993. A public sector fiscal surplus of 0.4 percent of GDP, excluding privatization proceeds, is expected in 1992. Another small surplus is budgeted for 1993.

Despite these restrictive policies, the cumulative trade deficit through September 1992 was $11.1 billion, up from $4.3 billion a year earlier, in part because of the continuing real appreciation of the peso. Imports were 28 percent higher, due in part to a 38 percent increase in consumer goods imports. Manufactured exports were only 9.4 percent higher, petroleum exports were unchanged, and other exports were lower.

In an apparent effort to slow the widening of the trade and current account deficits, some trade restrictions have been introduced in recent months, including labeling and certification rules, a sharply reduced duty-free allowance on goods imported into Mexico by land, and a 33 percent duty on any amount above the exemption. These actions disrupted U.S. exports to Mexico and may weaken U.S. industry and Congressional support for the North American Free Trade Area agreement. The agreement will be signed December 17.

The twenty-eight-day Treasury bill auction rate was 17 percent on December 16, down from its October 14 peak of 19.7 percent. The decline in part reflects the reduced expectation of an imminent devaluation after the October decision to increase the pace at which the exchange rate band is being widened and the consequent reduction in the risk premium demanded by bidders for these instruments. Secondary market interest rates have fallen by less. Private sector demand for credit remains strong, but commercial banks are increasingly cautious because of the growth of non-performing loans and the need to meet higher capitalization requirements that take effect January 1. Some banks may have difficulty meeting the new requirements. Non-performing loans were nearly 6 percent of total loans outstanding last August compared with less than 1 percent in 1989.

The spot rate for the dollar has fluctuated narrowly in the past five weeks and stood at 3,120 pesos on December 15, which is near the mid-point of the exchange rate band. On December 15, the

Mexico City stock market index was nearly 37 percent above its late September low and nearly 20 percent higher than the end of 1991.

In Taiwan, real GNP was 5.2 percent higher in the third quarter than a year earlier, the slowest growth in two years. Net export growth continued to slow, mainly in response to weak world demand. In the first 11 months of 1992, exports were about 7.5 percent higher than during the same period in 1991, well below the average export growth rate of 14.4 percent per year in 1987-91. Imports were about 14.9 percent higher. The trade surplus for the 11-month period fell to $9.1 billion from $12.4 billion in January-November 1991, despite a growing trade surplus with China, mainly through Hong Kong. Investment has picked up at the start of an ambitious six-year infrastructure program, with total investment projected to rise roughly 13 percent by year-end. Although public investment is lower than the target previously set for 1992, overall investment growth is above last year's rate of 9.5 percent. Consumer price inflation in Taiwan has increased recently, largely because of the extraordinary effects of a typhoon. Consumer prices were 5.1 percent higher in October than a year earlier.

The Korean government's controls on construction and tight credit policy have led to a slowdown in domestic demand, a reduction in inflationary pressures, and a narrowing of the trade deficit this year. Growth in the first three quarters of 1992 was 5.7 percent above the same period last year, well below potential estimated at 7 percent and growth of 8.8 percent recorded in the same period last year. Investment, the main source of the expansion last year, was little changed in the first three quarters. Consumer prices were 5.4 percent higher in October than a year earlier, down from an increase of 9 percent in the year ending October 1991. In the first eleven months of this year, Korea's trade deficit (on a customs clearance basis) fell to $5.2 billion from $11 billion in the same period last year. Exports grew 8.6 percent in the first eleven months of 1992, down slightly from last year. Imports were unchanged, compared with growth of 18 percent in the same period last year.

In Brazil, real GDP in the second quarter was 2 percent below a year earlier. Inflation in November is estimated to have been 23 percent and would have been higher had Acting President Franco not delayed increases in public sector tariffs. Depressed internal demand and improved competitiveness following a 17 percent real effective exchange rate depreciation in late 1991 combined to widen the cumulative trade surplus through October to $13 billion from $9.3 billion in the same period of 1991. Exports were 10 percent higher, while imports were 5 percent lower.

As of early December, international reserves were an estimated $20 billion, down from a record level of $23 billion in September. The decline probably reflects capital outflows resulting from the loss of investor confidence in the government. Acting President Franco advocates government controls on interest rates and prices to alleviate social and economic inequities. The rest of the government is mired in gridlock, unable to reach the consensus needed to cut budgetary deficits and enact other controversial reforms. This lack of consensus was underscored by the government decision on December 15 to postpone the privatization of a large steel mill that had been scheduled for December 22.

On December 10, the economic subcommittee of the Brazilian Senate ratified the Brady Plan restructuring of Brazil's $44 billion commercial bank debt. The accord is not expected to be implemented until Brazil takes more serious steps towards economic reform.

In Venezuela, the political and economic climate remains unsettled in the wake of the unsuccessful military coup attempt on November 27, the second one this year. The coup attempt highlighted serious shortcomings in policymakers' ability to spread the benefits of Venezuela's rapid economic growth during 1991-92 to the lower and middle classes. However, the public is not enthusiastic about the prospect of military rule.

The bolivar has remained relatively stable vis-a-vis the dollar from mid-November through December 15,

. The price of Venezuela's "Brady bonds" declined from 56.75 percent of face value on November 26, before the coup attempt, to 54.5 percent of face value on December 15. The Caracas stock exchange index fell from 20,353 on November 26 to 19,125 on November 30, the first business day after the coup, but rallied to 20,400 as of December 15.

In Argentina, economic activity slowed in the third quarter, while inflation has fallen to its lowest level in more than a decade. Industrial production in the third quarter was 13.4 percent above a year earlier, down from a 20.5 percent increase in the second quarter (year-over-year). Consumer prices rose by only 0.5 percent during November, compared with monthly averages of 1.1 percent during the previous six months and 5.2 percent during 1991. The cumulative trade surplus through August 1992 was $630 million, down from nearly $4 billion a year earlier. The slowdown in growth and the smaller trade surplus are largely attributable to high real interest rates and an estimated 40 percent real appreciation against the dollar since March 1991.

Real exchange rate appreciation fueled fears of devaluation, leading to the first run on the peso since the "Convertibility Law" committed the central bank to exchange pesos for dollars at par in

March 1991. During the second week of November, the central bank successfully defended the exchange rate by purchasing 300 million in pesos for the equivalent in dollars. The public, for the moment at least, appears to be more confident that the central bank will continue to honor its commitment to maintain the one-to-one parity.

Argentina reached final agreement with foreign commercial banks on a Brady Plan restructuring package on its $28 billion commercial bank debt. The signing ceremony took place on December 6. Nearly two-thirds of the debt will be swapped for fixed-rate par bonds paying a maximum 6 percent interest rate. The remainder will be exchanged for bonds to be issued at a 35 percent discount and paying 13/16 percent above LIBOR. Argentina will purchase $3.2 billion in 30-year zero-coupon U.S. Treasury bonds as collateral for the par and discount bonds using about $200 million of its international reserves and about $3 billion in earmarked loans from the IMF, World Bank, IDB, and the Japan Export-Import Bank. The exchange of debt is expected to take place in April 1993.